FINANCIAL REPORT

FY18

OF THE UNITED STATES GOVERNMENT

DEPARTMENT OF THE TREASURY
WASHINGTON D.C.
SECRETARY OF THE TREASURY

A Message from the Secretary

I am pleased to present the 2018 *Financial Report of the United States Government.* This Report provides a comprehensive view of the federal government's current financial position and future fiscal projections.

Driven by the *Tax Cuts and Jobs Act* and regulatory relief, United States GDP grew by 3.1 percent in calendar year 2018, the highest Q4 over Q4 growth that we have realized in thirteen years. Unemployment declined to a 49-year low, and American workers continued to take home more in their paychecks. Consumer and business confidence remain at or near all-time highs, and we continue to project robust business investment and growth in the year to come. Ongoing efforts by the Administration to open markets for American businesses abroad will further strengthen our economy and create more opportunities for hardworking families. We remain focused on promoting sustained economic growth that will result in more prosperity for the American people, and will lead to higher revenues and a stronger fiscal outlook for the federal government.

This Report highlights trends in Government revenues and costs, as well as the Government's long-term fiscal challenge of funding the Social Security, Medicare and Medicaid programs.

When making policy decisions, it is essential that we have transparency with respect to our federal government's finances. This Report reflects that commitment and is presented to facilitate open and productive dialogue so that all Americans can work together towards a more secure and prosperous future.

Steven T. Mnuchin

Steven T. Mnuchin

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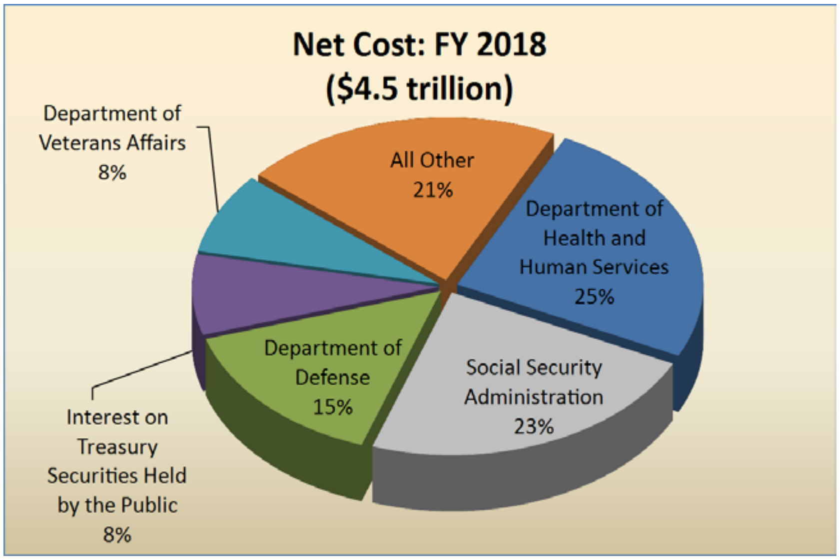
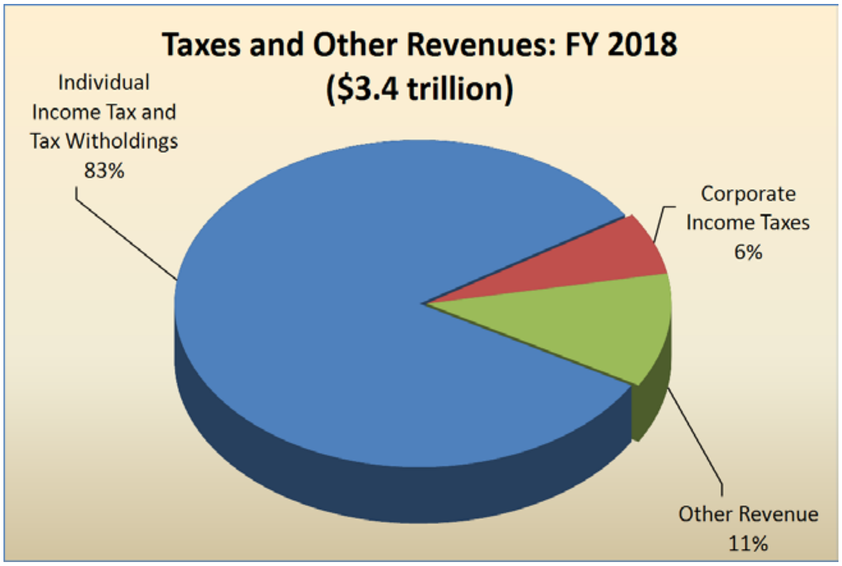




The government's net cost before taxes and other revenues for fiscal year 2018 was $4.5 trillion - an increase of $10.1 billion (0.2 percent) from fiscal year 2017.

Net cost equals gross costs of $4.8 trillion, less earned program revenues (e.g., Medicare premiums, national park entry fees), and then adjusted for gains or losses from assumption changes used to estimate future federal employee and veterans benefits payments.

The increase in net cost is the combined effect of many offsetting increases and decreases across the government.

Total government tax and other revenues grew by $9.7 billion (0.3 percent) to about $3.4 trillion for fiscal year 2018.

The government deducts $3.4 trillion in tax and other revenues from its $4.5 trillion net cost (with some adjustments) to derive its fiscal year 2018 "bottom line" net operating cost of $1.2 trillion, which is largely unchanged compared to fiscal year 2017.

By comparison, the government's budget deficit for fiscal year 2018 was $779.0 billion – an increase of $113.3 billion (about 17.0 percent) over fiscal year 2017. The $380.0 billion difference between the budget deficit and net operating cost is primarily due to accrued costs (incurred but not necessarily paid) that are included in net operating cost, but not the budget deficit. These include but are not limited to estimated future costs of federal employee and veterans benefits.

An Unsustainable Fiscal Path

The long-term fiscal projections indicate that the government's debt-to-GDP ratio will rise from 78 percent in 2018 to 530 percent over the 75-year projection period, and will continue to rise thereafter, if current policy is kept in place. The projections in this *Financial Report* show that current policy is not sustainable. These projections assume that current policy will continue indefinitely, and are, therefore, neither forecasts nor predictions. Nevertheless, policy changes must be enacted so that financial outcomes will be different than those projected.

The primary deficit is the difference between non-interest spending and receipts. As a ratio relative to gross domestic product (GDP), (the primary deficit-to-GDP ratio), it is useful for gauging long-term fiscal sustainability. This ratio spiked from 2009 through 2012 due to the financial crisis of 2008-09, the ensuing severe recession, and increased spending and temporary tax reductions enacted to stimulate the economy and support recovery. As the economic recovery took hold, the primary deficit-to-GDP ratio fell, averaging 1.9 percent from 2013-2018. The ratio is projected to rise to 2.9 percent in 2019 and then shrink slightly through 2024 as the economy grows. After 2024, increased spending for Social Security and health programs is projected to result in increasing primary deficits that peak in 2039 at 4.1 percent. This is due to the continued retirement of the baby boom generation and increases in health care costs. After 2039, the ratio gradually decreases to 2.5 percent in 2093 as the aging of the population slows. The primary deficit projections, along with those for interest rates and GDP, determine the debt-to-GDP ratio projections.

These projections assume the individual income and estate and gift tax provisions of the TCJA are permanently extended and discretionary spending grows at the same rate as nominal GDP beyond 2019. Congressional action is required to make these changes. GDP, interest, and other economic and demographic assumptions are the same as those that underlie the most recent Social Security and Medicare trustees' report projections, adjusted for historical revisions that occur annually. See Note 23 for more information.

If changes in policy are not so abrupt as to slow economic growth, then the sooner policy changes are adopted, the smaller the changes to revenue and/or spending will be required to return the government to a sustainable fiscal path.

NATION BY THE NUMBERS

A Snapshot of The Government's Financial Position & Condition

	2018	2017*
Financial Measures (Dollars in Billions):		
Gross Costs	**$ (4,808.5)**	**$ (4,606.2)**
Less: Earned Revenue	$ 392.8	$ 431.9
Gain/(Loss) from Changes in Assumptions	$ (125.2)	$ (356.5)
Net Cost	**$ (4,540.9)**	**$ (4,530.8)**
Less: Total Tax and Other Revenues	$ 3,384.3	$ 3,374.6
Unmatched Transactions and Balances	$ (2.4)	$ 2.6
Net Operating Cost	**$ (1,159.0)**	**$ (1,153.6)**
Budget Deficit	**$ (779.0)**	**$ (665.7)**
Assets, comprised of:		
Loans Receivable, Net	$ 1,419.1	$ 1,350.2
Property, Plant, and Equipment, Net	$ 1,090.5	$ 1,087.0
Other	$ 1,327.1	$ 1,097.7
Total Assets	**$ 3,836.7**	**$ 3,534.9**
Less: Liabilities, comprised of:		
Debt Held By the Public & Accrued Interest	$ (15,812.7)	$ (14,724.1)
Federal Employee & Veteran Benefits	$ (7,982.3)	$ (7,700.1)
Other	$ (1,562.5)	$ (1,472.6)
Total Liabilities	**$ (25,357.5)**	**$ (23,896.8)**
Net Position (Assets Less Liabilities)	**$ (21,520.8)**	**$ (20,361.9)**
Sustainability Measures (Dollars in Trillions):		
Social Insurance Net Expenditures	$ (53.8)	$ (49.0)
Total Federal Non-Interest Net Expenditures	$ (46.2)	$ (16.2)
Sustainability Measures as Percent of Gross Domestic Product (GDP):		
Social Insurance Net Expenditures	(4.0%)	(4.0%)
Total Federal Non-Interest Net Expenditures	(3.3%)	(1.2%)
Fiscal Gap[1]	(4.1%)	(2.0%)

*Restated - see Financial Statement Note 1.U

[1] To prevent the debt-to-GDP ratio from rising over the next 75 years, a combination of non-interest spending reductions and receipts increases that amounts to 4.1 percent of GDP on average is needed (2.0 percent of GDP on average in 2017). See Financial Statement Note 23.

Executive Summary to the Fiscal Year 2018 Financial Report of the United States Government

The Fiscal Year 2018 *Financial Report of the United States Government* (*Financial Report*) presents the U.S. government's current financial position and condition, and discusses key financial topics and trends. The *Financial Report* is produced by the U.S. Department of the Treasury (Treasury) in coordination with the Office of Management and Budget (OMB) of the Executive Office of the President. The table on the preceding page presents several key indicators of the government's financial position and condition, which are discussed in this Summary and, in greater detail, in the *Financial Report*. The Secretary of the Treasury, Director of OMB, and the Comptroller General of the United States at the Government Accountability Office (GAO) believe that the information discussed in this *Financial Report* is important to all Americans.

This *Financial Report* addresses the government's financial activity and results as of and for the fiscal years ended September 30, 2018 and 2017. Note 26, Subsequent Events discusses events that occurred after the end of the fiscal year which may affect the government's financial position and condition.

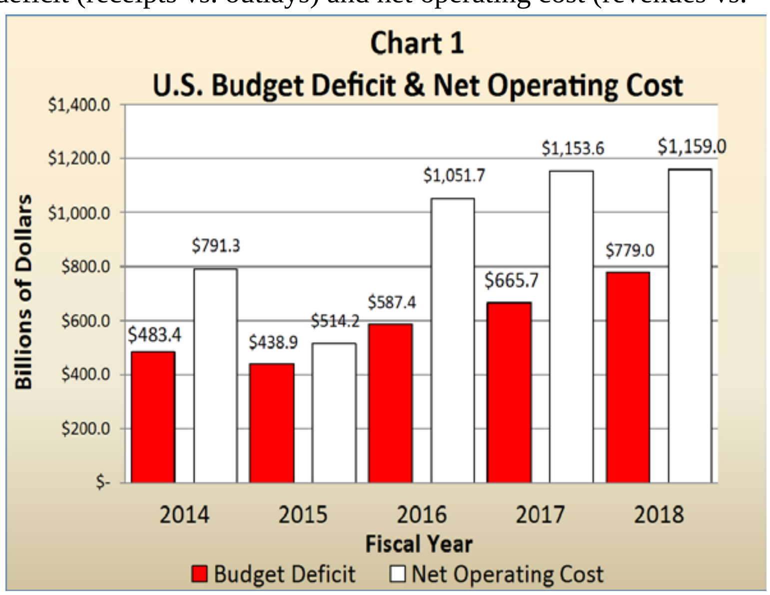
Where We Are Now

Comparing the Budget and the Financial Report

The *Budget of the United States Government (Budget)* and the *Financial Report* present complementary perspectives on the government's financial position and condition.

- The *Budget* is the government's primary financial planning and control tool. It accounts for past government receipts and spending, and includes the President's proposed receipts and spending plan. Receipts are cash received by the U.S. government and spending is measured as outlays, or payments made by the government to the public. Receipts greater than outlays creates a budget surplus; and outlays greater than receipts creates a budget deficit.
- The *Financial Report* includes the government's costs and revenues, assets and liabilities, and other important financial information. It compares the government's revenues (amounts earned, but not necessarily collected), with costs (amounts incurred, but not necessarily paid) to derive net operating cost.

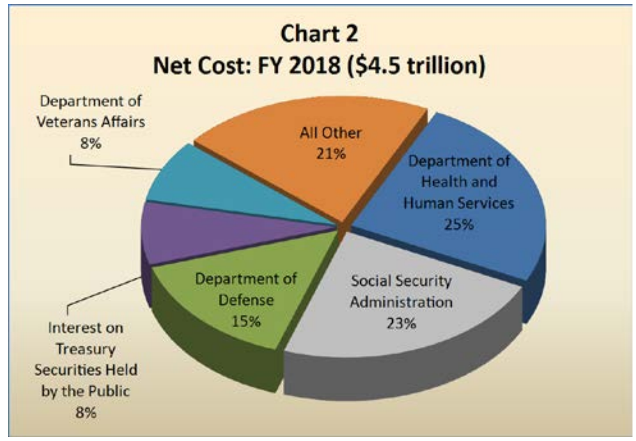
Chart 1 compares the government's budget deficit (receipts vs. outlays) and net operating cost (revenues vs. costs) for fiscal years 2014 - 2018. During fiscal year 2018:



- A $127.1 billion increase in outlays was offset in part by a $13.8 billion increase in receipts to increase the budget deficit by $113.3 billion (about 17.0 percent) to $779.0 billion.
- Net operating cost remained largely unchanged during fiscal year 2018 at $1.2 trillion, increasing by $5.4 billion or 0.5 percent. This is due mostly to a $10.1 billion or 0.2 percent increase in net cost which slightly more than offset a $9.7 billion or 0.3 percent increase in tax and other revenues.
- The $380.0 billion difference between the budget deficit and net operating cost is primarily due to accrued costs (incurred but not necessarily paid) related to increases in estimated federal employee and veteran benefits liabilities and certain other liabilities that are included in net operating cost, but not the budget deficit.

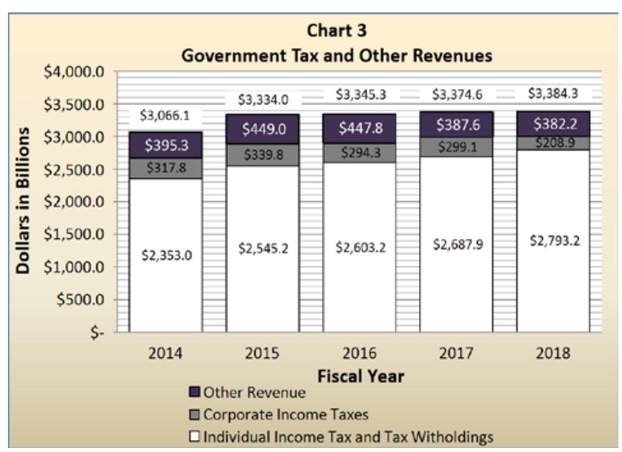
Costs and Revenues

The government's "bottom line" net operating cost remained largely unchanged at $1.2 trillion during fiscal year 2018, increasing by $5.4 billion (0.5 percent). It is calculated as follows:



- Starting with total gross costs of $4.8 trillion, the government subtracts earned program revenues (e.g., Medicare premiums, national park entry fees, and postal service fees) and adjusts the balance for gains or losses from changes in actuarial assumptions used to estimate future federal employee and veterans benefits payments to derive its net cost before taxes and other revenues of $4.5 trillion (see Chart 2), an increase of $10.1 billion (0.2 percent) from fiscal year 2017. This net increase is the combined effect of many offsetting increases and decreases across the government. For example:
  - o Entities administering federal employee and veterans benefits programs, including the Office of Personnel Management (OPM), Department of Veterans Affairs (VA), and Department of Defense (DOD) employ a complex series of assumptions, including but not limited to interest rates, beneficiary eligibility, life expectancy, and medical cost levels, to make actuarial projections of their long-term benefits liabilities. Changes in these assumptions can result in either losses (net cost increases) or gains (net cost decreases). Across the government, these net losses from changes in assumptions amounted to $125.2 billion in fiscal year 2018, a loss decrease (and a corresponding net cost decrease) of $231.3 billion compared to fiscal year 2017.
  - o The Department of Energy's (DOE) net cost increased by $99.6 billion, predominantly due changes in estimated environmental remediation costs.
  - o Department of Health and Human Services (HHS) and Social Security Administration (SSA) net costs increased $56.4 billion and $39.5 billion, respectively, largely due to increases in benefit expenses from the social insurance programs administered by those entities (e.g., Medicare, Social Security).
  - o At DOD, a $33.0 billion net cost increase includes a $39.2 billion decrease in earned revenues across the Department, as well as increases in the costs of procurement, personnel, and research and development. These increases were partially offset by a decrease in losses from changes in assumptions referenced above and a decrease in costs of military operations, readiness, and support.
  - o Interest costs related to the federal debt held by the public increased by $61.0 billion due largely to an increase in the debt and average interest rates, as well as inflation adjustments on certain Treasury securities. Interest costs increased by 20.6 percent in 2018 from 2017 and by 37.4 percent over the past five years.

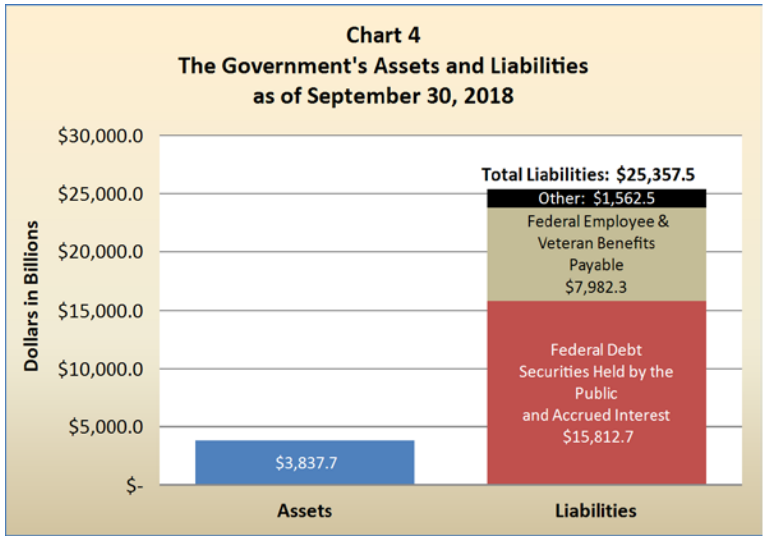
- The government deducts tax and other revenues from net cost (with some adjustments) to derive its fiscal year 2018 "bottom line" net operating cost of $1.2 trillion.



  - o From Chart 3, total government tax and other revenues grew by $9.7 billion (0.3 percent) to about $3.4 trillion for fiscal year 2018.
  - o Together, individual income tax and tax withholdings, and corporate taxes accounted for about 88.7 percent of total tax and other revenues in fiscal year 2018. Other revenues include Federal Reserve earnings, excise taxes, and customs duties.

Assets and Liabilities

Chart 4 summarizes the assets and liabilities that the government reports on its Balance Sheet. As of September 30, 2018:



- Total assets ($3.8 trillion) consist mostly of $1.4 trillion in net loans receivable (primarily student loans) and $1.1 trillion in net property, plant, and equipment).
    - Other significant government resources not reported on the Balance Sheet include stewardship assets, natural resources, and the government's power to tax and set monetary policy.
- Total liabilities ($25.4 trillion) consist mostly of: (1) $15.8 trillion in federal debt securities held by the public and accrued interest and (2) $8.0 trillion in federal employee and veteran benefits payable.
    - The "public" consists of individuals, corporations, state and local governments, Federal Reserve Banks, foreign governments, and other entities outside the federal government.
- The government also reports about $5.8 trillion of intragovernmental debt outstanding, which arises when one part of the government borrows from another.
    - For example, government funds (e.g., Social Security and Medicare trust funds) typically must invest excess annual receipts, including interest earnings, in Treasury-issued federal debt securities. Although not reflected in Chart 4, these securities are included in the calculation of federal debt subject to the debt limit.
- Debt held by the public plus intragovernmental debt equals gross federal debt, which, with some adjustments, is subject to a statutory debt ceiling ("debt limit").
    - At the end of fiscal year 2018, debt subject to the statutory limit was $21.5 trillion. Increasing or suspending the debt limit does not increase spending or authorize new spending; rather, it permits the government to continue to honor pre-existing commitments.
    - Legislation most recently suspended the debt limit from February 9, 2018 through March 1, 2019. Effective March 2, 2019, the statutory debt limit was set at $22.0 trillion, and on March 4, 2019, the Secretary of the Treasury notified the Congress that the statutory debt limit would be reached on or after that day. When delays in raising the debt limit occur, Treasury implements "extraordinary measures" on a temporary basis, to enable the government to protect the full faith and credit of the United States by continuing to pay its bills. Treasury began taking these extraordinary measures on March 4, 2019.

Key Economic Trends

An examination of key macroeconomic indicators is essential to the discussion of the government's financial performance. During fiscal year 2018, economic growth and the pace of job creation each accelerated, and the unemployment rate declined to a 49-year low. These and other economic and financial developments are discussed in greater detail in the *Financial Report*.

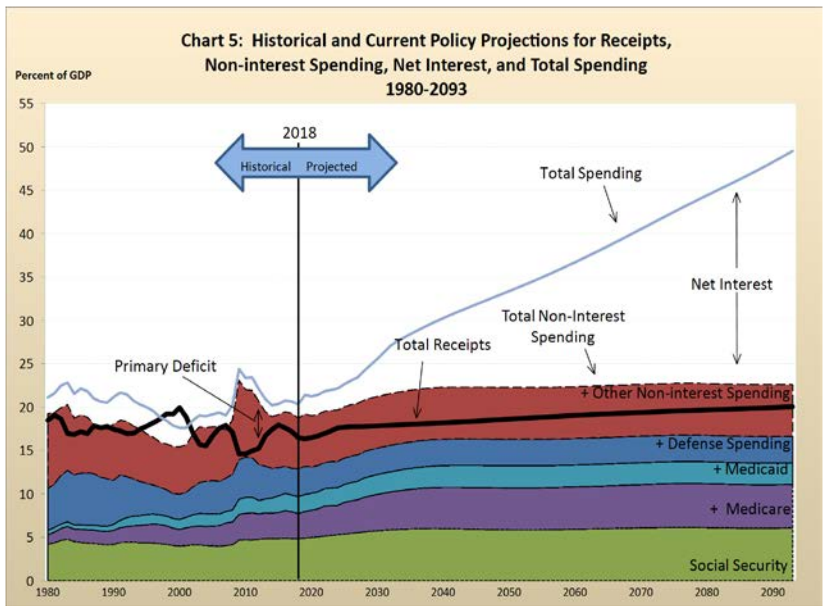
An Unsustainable Fiscal Path

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

The current fiscal path is unsustainable. To determine if current fiscal policy is sustainable, the projections discussed in the *Financial Report* assume current policy will continue indefinitely.[1] The projections are therefore neither forecasts nor predictions. Nevertheless, policy changes must be enacted so that actual financial outcomes will be different than those projected.

Receipts, Spending, and the Debt

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



- The primary deficit is the difference between non-interest spending and receipts. The primary deficit expressed as a ratio relative to GDP (the primary deficit-to-GDP ratio) is useful for gauging long-term fiscal sustainability.
- The primary deficit-to-GDP ratio spiked during 2009 through 2012 due to the financial crisis of 2008-09 and the ensuing severe recession, as well as increased spending and temporary tax reductions enacted to stimulate the economy and support recovery. As an economic recovery took hold, the primary deficit-to-GDP ratio fell, averaging 1.9 percent from 2013-2018. The ratio is projected to rise to 2.9 percent in 2019 and then shrink slightly through 2024 as the economy grows. After 2024, however, increased spending for Social Security and health programs[2] due to the continued retirement of the baby boom generation and increases in health care costs is projected to result in increasing primary deficits that peak in 2039, when the primary deficit-to-GDP ratio reaches 4.1 percent. After 2039, the ratio gradually decreases as the aging of the population continues at a slower pace, and reaches 2.5 percent in 2093.
- These projections assume the individual income and estate and gift tax provisions of the TCJA are permanently extended and discretionary spending grows at the same rate as nominal GDP beyond 2019. Congressional action is required to make these changes. GDP, interest, and other economic and demographic assumptions are the same as those that underlie the most recent Social Security and Medicare trustees' report projections, adjusted for historical revisions that occur annually. See Note 23 for more information.

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[1] Current policy in the projections is based on current law, but includes extension of certain policies that expire under current law but are routinely extended or otherwise expected to continue.
[2] See the 2018 Trustees Report for Medicare (pp 4-5) and Social Security (pp 4-23) and the 2017 Medicaid Actuarial Report

- The persistent long-term gap between projected receipts and total spending shown in Chart 5 occurs despite the projected effects of the *Affordable Care Act* (ACA)[3] on long-term deficits.
    - o Enactment of the ACA in 2010 and the *Medicare Access and CHIP Reauthorization Act* (MACRA) in 2015 established cost controls for Medicare hospital and physician payments whose long-term effectiveness is still to be demonstrated.
    - o There is uncertainty about the extent to which these projections can be achieved and whether the ACA's provisions that reduce Medicare cost growth will be overridden by new legislation.

Table 1 summarizes the status and projected trends of the government's Social Security and Medicare Trust Funds.

Table 1: Trust Fund Status

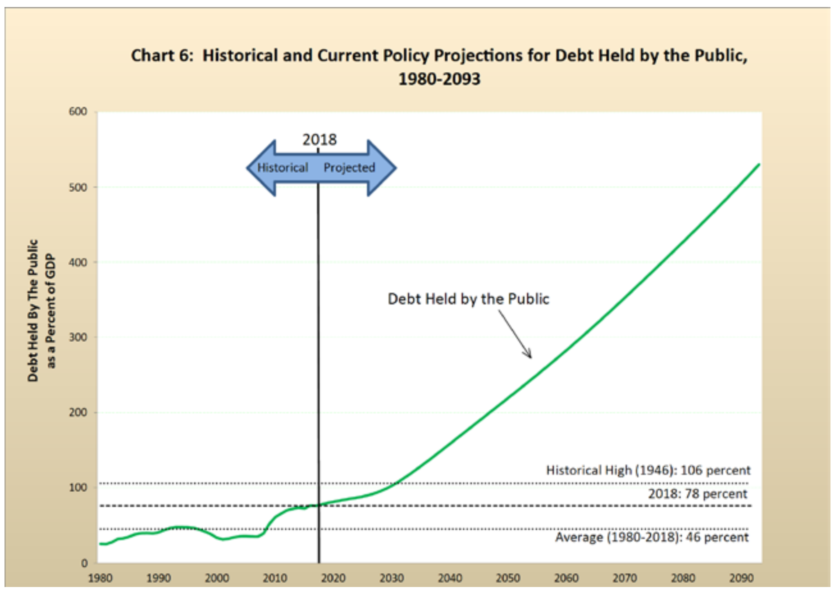
Fund	Projected Depletion	Projected Post-Depletion Trend
Medicare Hospital Insurance (HI)*	2026 (2029 in FY 2017 Report)	In 2026, trust fund income is projected to cover 91 percent of benefits, decreasing to 78 percent in 2042, then increasing to 85 percent by 2092.
Combined Old-Age Survivors and Disability Insurance (OASDI)**	2034 (unchanged from FY 2017 Report)	In 2034, trust fund income is projected to cover 79 percent of scheduled benefits, decreasing to about 74 percent by 2092.

* Source: 2018 Medicare Trustees Report ** Source: 2018 OASDI Trustees Report

Projections assume full Social Security and Medicare benefits are paid after fund depletion contrary to current law.

The primary deficit projections in Chart 5, along with those for interest rates and GDP, determine the debt-to-GDP ratio projections in Chart 6.

- The debt-to-GDP ratio was 78 percent at the end of fiscal year 2018, and under current policy is projected to exceed 100 percent by 2030, and reach 530 percent in 2093.
- The debt-to-GDP ratio rises continuously mainly because higher levels of debt lead to higher net interest expenditures, which lead to higher deficits and debt. The continuous rise of the debt-to-GDP ratio indicates that current fiscal policy is unsustainable.
- These debt-to-GDP projections are higher than the corresponding projections in both the fiscal year 2017 and fiscal year 2016 *Financial Reports*.



[3] The ACA refers to P.L. 111-148, as amended by P.L. 111-152. The ACA expands health insurance coverage, provides health insurance subsidies for low-income individuals and families, includes many measures designed to reduce health care cost growth, and significantly reduces Medicare payment rates relative to the rates that would have occurred in the absence of the ACA. (See Note 22 and the Required Supplementary Information section of the *Financial Report*, and the 2018 Medicare Trustees Report for more information).

The Fiscal Gap and the Cost of Delaying Fiscal Policy Reform

- The 75-year fiscal gap is a measure of how much primary deficits must be reduced over the next 75 years in order to make fiscal policy sustainable. That estimated fiscal gap for 2018 is 4.1 percent of GDP (compared to 2.0 percent for 2017).
- This estimate implies that making fiscal policy sustainable over the next 75 years would require some combination of spending reductions and receipt increases that equals 4.1 percent of GDP on average over the next 75 years. The fiscal gap represents 21.9 percent of 75-year present value receipts and 18.6 percent of 75-year present value non-interest spending.
- The timing of policy changes to make fiscal policy sustainable has important implications for the well-being of future generations as is shown in Table 2.

Table 2	
Costs of Delaying Fiscal Reform	
Period of Delay	**Change in Average Primary Surplus**
Reform in 2019 (No Delay)	4.1 percent of GDP between 2019 and 2093
Reform in 2029 (Ten-Year Delay)	4.9 percent of GDP between 2029 and 2093
Reform in 2039 (Twenty-Year Delay) ..	6.0 percent of GDP between 2039 and 2093
Note: Reforms taking place in 2018, 2028, and 2038 from the 2017 Financial Report were 2.0, 2.4, and 3.0 percent of GDP, respectively.	

  - Table 2 shows that, if action is delayed by 10 years, the estimated magnitude of primary surplus increases necessary to close the 75-year fiscal gap increases by nearly 20 percent from 4.1 percent of GDP on average over 75 years to 4.9 percent on average over 65 years); if action is delayed by 20 years, the magnitude of reforms necessary increases by about 46 percent.
  - Future generations are harmed by a policy delay because the higher the primary surpluses are during their lifetimes, the greater is the difference between the taxes they pay and the programmatic spending from which they benefit.

Conclusion

- Projections in the *Financial Report* indicate that the government's debt-to-GDP ratio is projected to rise over the 75-year projection period and beyond if current policy is kept in place. The projections in this *Financial Report* show that current policy is not sustainable.
- If changes in fiscal policy are not so abrupt as to slow economic growth and the sooner those policy changes are adopted, the smaller the changes to revenue and/or spending will be required to return the government to a sustainable fiscal path.

Find Out More

The *2018 Financial Report* and other information about the nation's finances are available at:

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

The Government Accountability Office's (GAO) audit report on the U.S. government's consolidated financial statements can be found beginning on page 226 of the full *Financial Report*. GAO was unable to express an opinion (disclaimed) on these consolidated financial statements for the reasons discussed in the audit report.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Introduction

The Fiscal Year *2018 Financial Report of the United States Government (Financial Report)* provides the President, Congress, and the American people with a comprehensive view of the federal government's financial position and condition, and discusses important financial issues and significant conditions that may affect future operations, including the need to achieve fiscal sustainability over the medium and long term.

Pursuant to 31 United States Code (U.S.C.) § 331(e)(1), the Department of the Treasury (Treasury), in cooperation with the Office of Management and Budget (OMB), must submit an audited (by the Government Accountability Office or GAO) financial statement for the preceding fiscal year, covering all accounts and associated activities of the executive branch of the United States (U.S.) government[1] to the President and Congress no later than six months after the September 30 fiscal year-end.

The *Financial Report* is prepared from the financial information provided by 158 federal consolidation entities (see organizational chart on the next page and Appendix A). As it has for the past 21 years, GAO issued a disclaimer of opinion on the accrual-based, consolidated financial statements for the fiscal years ended September 30, 2018 and 2017. GAO also issued a disclaimer of opinion on the sustainability financial statements, which consist of the 2018 and 2017 Statements of Long-Term Fiscal Projections (SLTFP); the 2018, 2017, 2016, 2015, and 2014 Statements of Social Insurance (SOSI); and the 2018 and 2017 Statements of Changes in Social Insurance Amounts (SCSIA). A disclaimer of opinion indicates that sufficient information was not available for the auditors to determine whether the reported financial statements were fairly presented in accordance with U.S. Generally Accepted Accounting Principles (GAAP). In fiscal year 2018, 35[2] of the 40 most significant entities earned unmodified ("clean") opinions on their financial statements.

The fiscal year 2018 *Financial Report* consists of:

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

This *Financial Report* addresses the government's financial activity and results as of and for the fiscal years ended September 30, 2018 and 2017. Note 26, *Subsequent Events* discusses events that occurred after the end of the fiscal year which may affect the government's financial position and condition.

In addition, the Results in Brief and Executive Summary to this *Financial Report* provides a quick reference to the key issues in the *Financial Report* and an overview of the government's financial position and condition.

Mission & Organization

The government's fundamental mission is derived from the Constitution: *"…to form a more perfect union, establish justice, insure domestic tranquility, provide for the common defense, promote the general welfare and secure the blessings of liberty to ourselves and our posterity."* The government's functions have evolved over time to include health care, income security, veterans benefits and services, housing and transportation, security, and education. Exhibit 1 provides an overview of how the U.S. government is organized.

[1] The *Government Management Reform Act* of 1994 has required such reporting, covering the executive branch of the Government, beginning with financial statements prepared for fiscal year 1997. The consolidated financial statements include the legislative and judicial branches.

[2] The 35 entities include the Department of Health and Human Services, which received disclaimers of opinion on its 2018, 2017, 2016, 2015, and 2014 SOSI and on its 2018 and 2017 SCSIA.

Exhibit 1

THE UNITED STATES GOVERNMENT

THE CONSTITUTION

LEGISLATIVE BRANCH

THE CONGRESS
SENATE HOUSE

Architect of the Capitol
U.S. Botanic Garden
Government Accountability Office
Government Publishing Office
Library of Congress
Congressional Budget Office
U.S. Capitol Police

EXECUTIVE BRANCH

THE PRESIDENT
THE VICE PRESIDENT
EXECUTIVE OFFICE OF THE PRESIDENT

White House Office
Office of the Vice President
Council of Economic Advisers
Council on Environmental Quality
National Security Council
Office of Administration
Office of Management and Budget
Office of National Drug Control Policy
Office of Policy Development
Office of Science and Technology Policy
Office of the U.S. Trade Representative

JUDICIAL BRANCH

THE SUPREME COURT OF THE U.S.

U.S. Courts of Appeals
U.S. District Courts
Territorial Courts
U.S. Court of International Trade
U.S. Court of Federal Claims
Administrative Office of the U.S. Courts
Federal Judicial Center
U.S. Sentencing Commission

SIGNIFICANT CONSOLIDATION ENTITIES

DEPARTMENT OF AGRICULTURE
DEPARTMENT OF COMMERCE
DEPARTMENT OF DEFENSE
DEPARTMENT OF EDUCATION
DEPARTMENT OF ENERGY
DEPARTMENT OF HEALTH AND HUMAN SERVICES
DEPARTMENT OF HOMELAND SECURITY
DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
DEPARTMENT OF THE INTERIOR
DEPARTMENT OF JUSTICE
DEPARTMENT OF LABOR
DEPARTMENT OF STATE
DEPARTMENT OF TRANSPORTATION
DEPARTMENT OF THE TREASURY
DEPARTMENT OF VETERANS AFFAIRS

OTHER SIGNIFICANT CONSOLIDATION ENTITIES

ENVIRONMENTAL PROTECTION AGENCY
GENERAL SERVICES ADMINISTRATION
NATIONAL AERONAUTICS AND SPACE ADMINISTRATION
NATIONAL SCIENCE FOUNDATION
OFFICE OF PERSONNEL MANAGEMENT
SMALL BUSINESS ADMINISTRATION
SOCIAL SECURITY ADMINISTRATION
U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT
U.S. NUCLEAR REGULATORY COMMISSION
SECURITY ASSISTANCE ACCOUNTS
EXPORT-IMPORT BANK OF THE U.S.
FARM CREDIT SYSTEM INSURANCE CORPORATION

FEDERAL COMMUNICATIONS COMMISSION
FEDERAL DEPOSIT INSURANCE CORPORATION
GENERAL FUND OF THE U.S. GOVERNMENT
MILLENNIUM CHALLENGE CORPORATION
NATIONAL CREDIT UNION ADMINISTRATION
NATIONAL RAILROAD RETIREMENT INVESTMENT TRUST
OVERSEAS PRIVATE INVESTMENT CORPORATION
PENSION BENEFIT GUARANTY CORPORATION
RAILROAD RETIREMENT BOARD
SECURITIES AND EXCHANGE COMMISSION
SMITHSONIAN INSTITUTION
TENNESSEE VALLEY AUTHORITY
U.S. POSTAL SERVICE

OTHER CONSOLIDATION ENTITIES ARE LISTED IN APPENDIX A OF THIS FINANCIAL REPORT

The Government's Financial Position and Condition

This *Financial Report* presents the government's financial position at the end of the fiscal year, explains how and why the financial position changed during the year, and discusses the government's financial condition and how it may change in the future.

Table 1
The Federal Government's Financial Position and Condition

	2018	2017*	Increase / (Decrease) $	%
FINANCIAL MEASURES (Dollars in Billions)				
Gross Cost	**$ (4,808.5)**	**$ (4,606.2)**	**$ 202.3**	**4.4%**
Less: Earned Revenue	$ 392.8	$ 431.9	$ (39.1)	(9.1%)
Gain/(Loss) from Changes in Assumptions	$ (125.2)	$ (356.5)	$ (231.3)	(64.9%)
Net Cost	**$ (4,540.9)**	**$ (4,530.8)**	**$ 10.1**	**0.2%**
Less: Tax and Other Revenues	$ 3,384.3	$ 3,374.6	$ 9.7	0.3%
Unmatched Transactions & Balances	$ (2.4)	$ 2.6	$ (5.0)	(192.3%)
Net Operating Cost	**$ (1,159.0)**	**$ (1,153.6)**	**$ 5.4**	**0.5%**
Budget Deficit	**$ (779.0)**	**$ (665.7)**	**$ 113.3**	**17.0%**
Assets:				
Cash & Other Monetary Assets	$ 507.5	$ 271.2	$ 236.3	87.1%
Loans Receivable, Net	$ 1,419.1	$ 1,350.2	$ 68.9	5.1%
Inventories & Related Property, Net	$ 337.5	$ 326.7	$ 10.8	3.3%
Property, Plant & Equipment, Net	$ 1,090.5	$ 1,087.0	$ 3.5	0.3%
Other	$ 482.1	$ 499.8	$ (17.7)	(3.5%)
Total Assets	**$ 3,836.7**	**$ 3,534.9**	**$ 301.8**	**8.5%**
Liabilities:				
Federal Debt Held by the Public & Accrued Interest	$ (15,812.7)	$ (14,724.1)	$ 1,088.6	7.4%
Federal Employee & Veteran Benefits	$ (7,982.3)	$ (7,700.1)	$ 282.2	3.7%
Other	$ (1,562.5)	$ (1,472.6)	$ 89.9	6.1%
Total Liabilities	**$ (25,357.5)**	**$ (23,896.8)**	**$ 1,460.7**	**6.1%**
Net Position (Assets minus Liabilities)	**$ (21,520.8)**	**$ (20,361.9)**	**$ 1,158.9**	**5.7%**
SUSTAINABILITY MEASURES (Dollars in Trillions)				
Social Insurance Net Expenditures:				
Social Security (OASDI)	$ (16.1)	$ (15.4)	$ 0.7	4.5%
Medicare (Parts A, B, & D)	$ (37.6)	$ (33.5)	$ 4.1	12.2%
Other	$ (0.1)	$ (0.1)	$ -	0.0%
Total Social Insurance Net Expenditures	**$ (53.8)**	**$ (49.0)**	**$ 4.8**	**9.8%**
Total Federal Non-Interest Net Expenditures	**$ (46.2)**	**$ (16.2)**	**$ 30.0**	**185.2%**
75-Year Fiscal Gap (Percent of Gross Domestic Product)[1]	**(4.1%)**	**(2.0%)**	**2.1%**	**105.0%**

*Restated (see Financial Statement Note 1.U)

[1]To prevent the debt-to-GDP ratio from rising over the next 75 years, a combination of non-interest spending reductions and receipts increases that amounts to 4.1 percent of GDP on average is needed (2.0 percent of GDP on average in 2017). See Financial Statement Note 23.

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

- During fiscal year 2018, the budget deficit increased by 17.0 percent and gross cost increased by 4.4 percent, while net cost, tax and other revenues, and net operating cost each increased by less than one percent.
- The government's gross costs of $4.8 trillion, less $392.8 billion in revenues earned for goods and services provided to the public (e.g., Medicare premiums, national park entry fees, and postal service fees), plus $125.2 billion in net losses from changes in assumptions (e.g., interest rates, inflation, disability claims rates) yields the government's net cost of $4.5 trillion, a slight increase of $10.1 billion or 0.2 percent over fiscal year 2017.
- Deducting $3.4 trillion in tax and other revenues, with some adjustment for unmatched transactions and balances, results in a "bottom line" net operating cost of $1.2 trillion for fiscal year 2018, an increase of $5.4 billion or 0.5 percent over fiscal year 2017.
- Comparing total 2018 government assets of $3.8 trillion to total liabilities of $25.4 trillion (comprised mostly of $15.8 trillion in federal debt held by the public and accrued interest payable[3], and $8.0 trillion of federal employee and veterans benefits payable) yields a negative net position of $21.5 trillion.
- The budget deficit is primarily financed through borrowing from the public. As of September 30, 2018, debt held by the public, excluding accrued interest, was $15.8 trillion. This amount, plus intragovernmental debt ($5.8 trillion) equals gross federal debt, which, with some adjustments, is subject to the statutory debt limit. As of September 30, 2018, the government's total debt subject to the debt limit was $21.5 trillion. The statutory debt limit was most recently suspended through March 1, 2019.

This *Financial Report* also contains information about projected impacts on the government's future financial condition. Under federal accounting rules, social insurance amounts as reported in both the SLTFP and in the SOSI are not considered liabilities of the government. From Table 1:

- The SLTFP shows that the present value (PV)[4] of total non-interest spending, including Social Security, Medicare, Medicaid, defense, and education, etc.), over the next 75 years, under current policy, is projected to exceed the PV of total receipts by $46.2 trillion (total federal non-interest net expenditures from Table 1).
- The SOSI shows that the PV of the government's expenditures for Social Security and Medicare Parts A, B and D, and other social insurance programs over 75 years is projected to exceed social insurance revenues[5] by about $53.8 trillion, a $4.8 trillion increase over 2017 social insurance projections.
- The two sustainability measures in Table 1 differ primarily because total non-interest net expenditures from the SLTFP include the effects of general revenues and non-social insurance spending, neither of which is included in the SOSI.

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

- The budget deficit (i.e., including the consolidated receipts and outlays from federal funds and the Social Security Trust Fund) increased from $665.7 billion in fiscal year 2017 to $779.0 billion in fiscal year 2018. The deficit-to-GDP ratio in 2018 was 3.9 percent, an increase from 3.5 percent in fiscal year 2017 and above the 3.2 percent average over the past 40 years.[6]
- The budget deficit is primarily financed through borrowing from the public. As of September 30, 2018, the $15.8 trillion in debt held by the public, excluding accrued interest, equates to approximately 78 percent of GDP.
- The 2018 SOSI projection of $53.8 trillion net PV excess of expenditures over receipts over 75 years represents about 4.0 percent of the PV of GDP over 75 years. The excess of total projected non-interest spending over receipts of $46.2 trillion from the SLTFP represents 3.3 percent of GDP over 75 years. As discussed in this *Financial Report*, changes in these projections can, in turn, have a significant impact on projected debt as a percent of GDP.
- To prevent the debt-to-GDP ratio from rising over the next 75 years, a combination of non-interest spending reductions and receipts increases that amounts to 4.1 percent of GDP on average is needed (2.0 percent of GDP on average in the 2017 projections). The fiscal gap represents 21.9 percent of 75-year present value receipts and 18.6 percent of 75-year present value non-interest spending.

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

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

[5] Social Security is funded by the payroll taxes and revenue from taxation of benefits. Medicare Part A is funded by the payroll taxes, revenue from taxation of benefits, and premiums that support those programs. Medicare Parts B and D are primarily financed by general revenues and premiums. By accounting convention, these general revenues are eliminated in consolidation at the governmentwide level and, as such, are not included in the SOSI. For the fiscal year 2018 and 2017 SOSI, the amounts eliminated totaled $32.9 trillion and $30.0 trillion, respectively.

[6] Final Monthly Treasury Statement (as of September 30, 2018 and 2017), Joint Statement of Treasury Secretary Steven T. Mnuchin and OMB Director Mick Mulvaney on Budget Results for Fiscal Year 2018

Fiscal Year 2018 Financial Statement Audit Results

For fiscal year 2018, GAO issued a disclaimer of audit opinion on the accrual-based, governmentwide financial statements, as it has for the past 21 years, due to certain material weaknesses in internal control over financial reporting and other limitations on the scope of its work. In addition, GAO issued a disclaimer of opinion on the sustainability financial statements due to significant uncertainties primarily related to the achievement of projected reductions in Medicare cost growth and certain other limitations. GAO's audit report on page 226 of this *Financial Report*, discusses GAO's findings.

22 of the 24 entities required to issue audited financial statements under the *Chief Financial Officers* (CFO) *Act* received unmodified audit opinions, as did 13 of 16 additional significant reporting entities (see Table 10 and Appendix A).[7]

The Governmentwide Reporting Entity

This *Financial Report* includes the financial status and activities of the executive, legislative, and judicial branches of the federal government. Statement of Federal Financial Accounting Standards (SFFAS) No. 47, *Reporting Entity*, provides criteria for identifying organizations that are consolidation entities, disclosure entities, and related parties. Such criteria are summarized in Note 1A and in Appendix A, which lists the entities included in this *Financial Report* by these categories. The assets, liabilities, results of operations, and related activity for consolidation entities are consolidated in the financial statements.

The Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac) meet the criteria for disclosure entities and, consequently, are not consolidated into the government's financial statements. However, the values of the investments in such entities, changes in value, and related activity with these entities are included in the consolidated financial statements. The Federal Reserve System (FR System) is a disclosure entity and is not consolidated into the government's financial statements. See Note 1A—Significant Accounting Policies, Reporting Entity and Note 25—Disclosure Entities and Related Parties for additional information. In addition, per SFFAS No. 31, *Accounting for Fiduciary Activities*, fiduciary funds are not consolidated in the government financial statements.[8]

Most significant reporting entities prepare financial reports that include financial and performance related information, as well as Annual Performance Reports. More information may be obtained from entities' websites indicated in Appendix A and at www.performance.gov.

The following pages contain a more detailed discussion of the government's financial results for fiscal year 2018, the budget, the economy, the debt, and a long-term perspective about fiscal sustainability, including the government's ability to meet its social insurance benefits obligations. The information in this *Financial Report*, when combined with the *Budget of the U.S. Government (Budget)*, collectively presents information on the government's financial position and condition.

Accounting Differences Between the Budget and the Financial Report

Each year, the Administration issues two reports that detail the government's financial results: the *Budget* and this *Financial Report*. The exhibit on the following page provides the key characteristics and differences between the two documents.

Treasury generally prepares the financial statements in this *Financial Report* on an accrual basis of accounting as prescribed by GAAP for federal entities.[9] These principles are tailored to the government's unique characteristics and circumstances. For example, entities prepare a uniquely structured "Statement of Net Cost," which is intended to present net government resources used in its operations. Also, unique to government is the preparation of separate statements to reconcile differences and articulate the relationship between the budget and financial accounting results.

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[7] The 22 entities include the Department of Health and Human Services, which received disclaimers of opinions on its 2018, 2017, 2016, 2015, and 2014, SOSI and its 2018 and 2017 SCSIA. The 13 entities include the Federal Deposit Insurance Corporation (FDIC), the National Credit Union Administration (NCUA), and the Farm Credit System Insurance Corporation (FCSIC), which operate on a calendar year basis (December 31 year-end). Statistic reflects 2017 audit results for these organizations if 2018 results are not available.

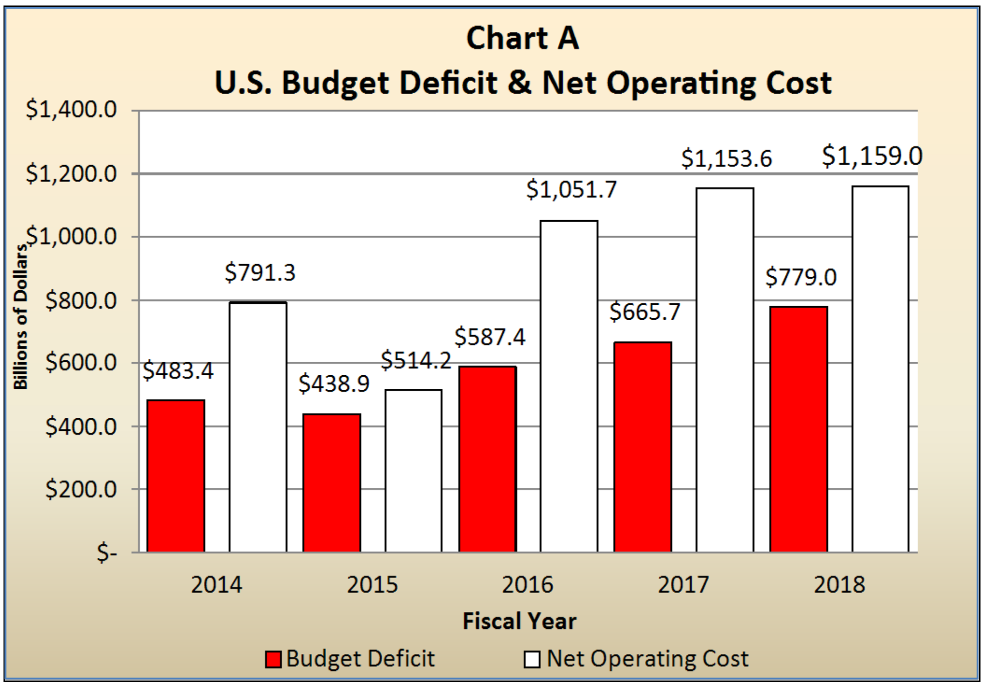
[8] See Note 21—Fiduciary Activities

[9] Under GAAP, most U.S. government revenues are recognized on a 'modified cash' basis, (see Financial Statement Note 1.B). The Statement of Social Insurance presents the present value of the estimated future revenues and expenditures for scheduled benefits over the next 75 years for the Social Security, Medicare, Railroad Retirement programs; and 25 years for the Black Lung program. The Statement of Long-Term Fiscal Projections presents the present value of the projected future receipts and non-interest spending for the federal government.

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

Budget Deficit vs. Net Operating Cost

The budget deficit is measured as the excess of outlays, or payments made by the government, over receipts, or cash received by the government. Net operating cost, on an accrual basis, is the excess of costs (what the government has incurred, but has not necessarily paid) over revenues (what the government has collected and expects to collect, but has not necessarily received). As shown in Chart A, net operating cost typically exceeds the budget deficit due largely to the inclusion of cost accruals associated with increases in estimated liabilities for the government's postemployment benefit programs for its military and civilian employees and veterans as well as environmental liabilities.



The government's primarily cash-based[10] budget deficit increased by $113.3 billion (about 17.0 percent) from approximately $665.7 billion in fiscal year 2017 to about $779.0 billion in fiscal year 2018 due to lower growth in receipts compared to the increase in outlays in fiscal year 2018. The $13.8 billion (0.4 percent) increase in receipts can be attributed primarily to higher net individual income tax receipts, excise taxes, social insurance and retirement receipts, and customs duties. Outlays increased $127.1 billion (3.2 percent). Contributing to the increase over fiscal year 2017 were higher outlays for Defense, Medicaid, Social Security, disaster relief and flood insurance, Refundable Premium Tax Credits and cost sharing reductions, interest on the Treasury debt held by the public (public debt), and lower government-sponsored enterprises' (GSE) receipts (i.e., dividends from Fannie Mae and Freddie Mac), which are an offset to outlays.[11]

The Treasury Department's September 2018 Monthly Treasury Statement (MTS) is the source of receipts, spending, and deficit information for this Report. The MTS presents primarily cash-based spending, or outlays, for the fiscal year in a number of ways, including by month, by entity, and by budget function classification. The federal budget is divided into approximately 20 categories – or budget functions - as a means of organizing federal spending by primary purpose (e.g., National Defense, Transportation, Health). Multiple entities may contribute to one or more budget functions, and a single

[10] Interest outlays on Treasury debt held by the public are recorded in the budget when interest accrues, not when the interest payment is made. For federal credit programs, outlays are recorded when loans are disbursed, in an amount representing the present value cost to the government, commonly referred to as credit subsidy cost. Credit subsidy cost excludes administrative costs.

[11] 10/15/18 press release -- Joint Statement of Treasury Secretary Steven T. Mnuchin and OMB Director Mick Mulvaney on Budget Results for Fiscal Year 2018.

budget function may be associated with only one entity. For example, the Department of Defense (DOD), Department of Homeland Security (DHS), the Department of Energy (DOE), and multiple other entities administer programs that are critical to the broader functional classification of National Defense. DOD, the Office of Personnel Management (OPM), and many other entities also administer Income Security programs (e.g., retirement benefits, housing, financial assistance). By comparison, the Medicare program is a budget function category unto itself and is administered exclusively at the federal level by the Department of Health and Human Services (HHS). Federal spending information by budget function and other categorizations may be found in the September 2018 MTS.[12]

The government's largely accrual-based net operating cost remained largely unchanged at $1.2 trillion increasing by $5.4 billion (0.5 percent) during fiscal year 2018. As explained below, net operating costs are affected by both changes in revenues and costs.

Table 2 provides a summary of the items reported in the *Reconciliation of Net Operating Cost and Budget Deficit*, which articulates the relationship between the government's accrual-based net operating cost and the primarily cash-based budget deficit. From Table 2, the $380.0 billion net difference between the government's budget deficit and net operating cost for fiscal year 2018, is mostly attributable to: (1) a $282.2 billion net increase in liabilities for federal employee and veteran benefits payable, (2) a $112.8 billion increase in environmental and disposal liabilities; and (3) several offsetting items, including, but not limited to a $32.3 billion decrease in insurance and guarantee program liabilities and a $15.9 billion increase in Accounts Payable. These affect net operating cost, but not the budget deficit.

Table 2: Net Operating Cost vs. Budget Deficit

Dollars in Billions		2018		2017*
Net Operating Cost	**$**	**(1,159.0)**	**$**	**(1,153.6)**
Change in:				
Federal Employee and Veteran Benefits Payable	$	282.2	$	490.7
Environmental and Disposal Liabilities	$	112.8	$	17.9
Insurance and guarantee program liabilities	$	(32.3)	$	15.5
Accounts payable	$	15.9	$	8.4
Other, Net	$	1.4	$	(44.6)
Subtotal - Net Difference:	$	380.0	$	487.9
Budget Deficit	**$**	**(779.0)**	**$**	**(665.7)**

*Restated (see Financial Statement Note 1.U)

[12] Final Monthly Treasury Statement for Fiscal Year 2018 through September 30, 2018 and Other Periods.

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

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

Costs and Revenues

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

Table 3: Gross Cost, Revenues, Net Cost, and Net Operating Cost

Dollars in Billions		2018		2017*		Increase / (Decrease) $	%
Gross Cost	**$**	**(4,808.5)**	**$**	**(4,606.2)**	**$**	**202.3**	**4.4%**
Less: Earned Revenue	$	392.8	$	431.9	$	(39.1)	(9.1%)
Gain/(Loss) from Changes in Assumptions	$	(125.2)	$	(356.5)	$	(231.3)	(64.9%)
Net Cost	**$**	**(4,540.9)**	**$**	**(4,530.8)**	**$**	**10.1**	**0.2%**
Less: Tax and Other Revenues	$	3,384.3	$	3,374.6	$	9.7	0.3%
Unmatched Transactions and Balances	$	(2.4)	$	2.6	$	(5.0)	(192.3%)
Net Operating Cost	**$**	**(1,159.0)**	**$**	**(1,153.6)**	**$**	**5.4**	**0.5%**

*Restated (see Financial Statement Note 1.U)

Table 3 shows that the government's "bottom line" net operating cost remained largely unchanged during 2018 at $1.2 trillion increasing only $5.4 billion (0.5 percent), during the fiscal year. This slight increase is due mostly to a $10.1 billion (0.2 percent) increase in entity net costs, which slightly more than offset a $9.7 billion (0.3 percent) increase in tax and other revenues over the past fiscal year as discussed in the following.

Gross Cost and Net Cost

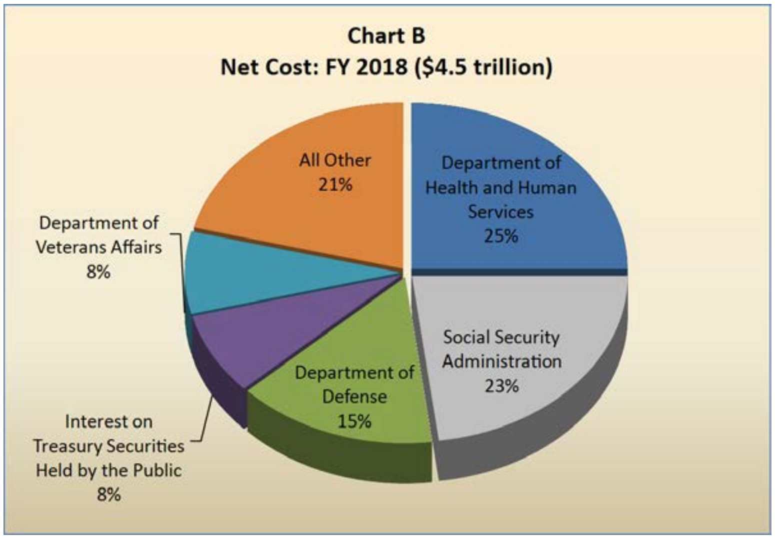
The Statement of Net Cost starts with the government's total gross costs of $4.8 trillion, subtracts revenues earned for goods and services provided (e.g., Medicare premiums, national park entry fees, and postal service fees), and adjusts the balance for gains or losses from changes in actuarial assumptions used to estimate certain liabilities, including federal employee and veterans benefits to derive its net cost of $4.5 trillion (See Chart C), a $10.1 billion (0.2 percent) increase over fiscal year 2017.

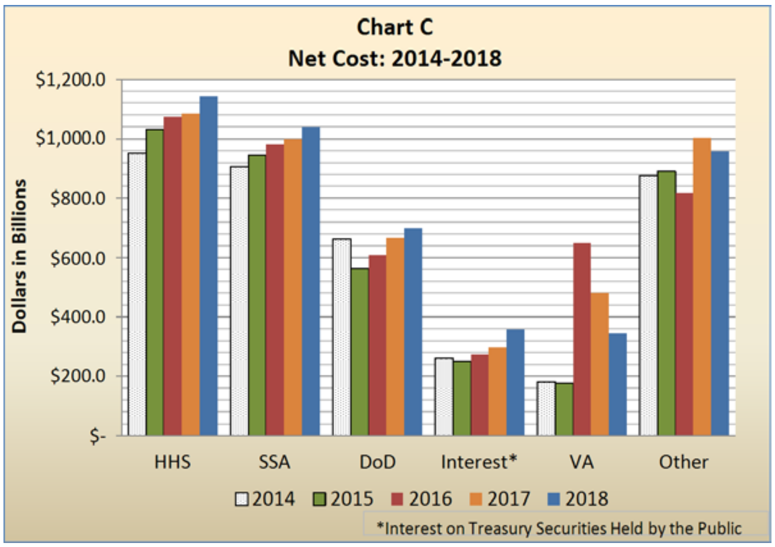
Typically, the annual change in the government's net cost is impacted by a variety of offsetting increases and decreases across entities. For example, offsetting changes in net cost during fiscal year 2018 included:

- Entities administering federal employee and veterans benefits programs employ a complex series of assumptions, including but not limited to interest rates, beneficiary eligibility, life expectancy, and medical cost levels, to make actuarial projections of their long-term benefits liabilities. Changes in these assumptions can result in either losses (net cost increases) or gains (net cost decreases). Across the government, these net losses from changes in assumptions amounted to $125.2 billion in fiscal year 2018, a loss decrease (and a corresponding net cost decrease) of $231.3 billion compared to fiscal year 2017. The primary entities that administer programs impacted by these assumptions – typically federal employee pension and benefit programs – are the OPM, Department of Veterans Affairs (VA), and DOD. These entities recorded losses from changes in assumptions in the amounts of $26.2 billion, $79.2 billion, and $16.8 billion, respectively – all decreased amounts compared to 2017.

[13] As shown in Table 3, net operating cost includes an adjustment for unmatched transactions and balances, which represent unreconciled differences in intragovernmental activity and balances between federal entities. These amounts are described in greater detail in the Other Information section of this *Financial Report*.

- o These actuarial estimates and the resulting gains or losses from changes in assumptions can sometimes cause significant swings in total entity costs from year to year. For example, for fiscal year 2018, changes in net cost at VA ($132.8 billion decrease), OPM ($66.2 billion decrease), and DOD ($33.0 billion increase), were impacted by the corresponding changes in gains or losses from assumption changes at these entities.



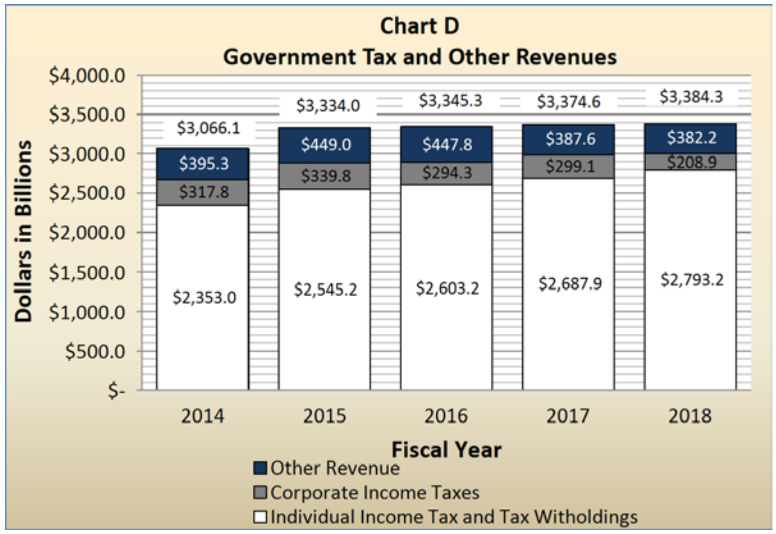


- At DOD, the $33.0 billion net cost increase includes the net effect of a $39.2 billion decrease in earned revenues across the department, as well as increases in the net costs of procurement, military personnel and research and development (R&D). These increases were partially offset by a decrease in losses from changes in assumptions referenced above (net cost decrease), and a decrease in costs of military operations, readiness, and support;
- $56.4 billion and $39.5 billion net cost increases at HHS and the Social Security Administration (SSA), respectively, were primarily due to cost increases of the benefits programs that these entities administer (HHS – Medicare and Medicaid programs, SSA – Old-Age, Survivors, and Disability Insurance (OASDI) programs);
- A $99.6 billion net cost increase at DOE largely due to refined environmental liability estimates, including those for Waste Treatment and Immobilization Plant construction, operating costs, tank farm retrieval, and closure costs at DOE's Hanford site;
- A $20.2 billion net cost decrease at the Pension Benefit Guaranty Corporation (PBGC) stems mostly from higher interest rate factors used to measure liabilities for the single- and multi-employer programs; and
- A $61.0 billion cost increase in interest on debt held by the public due largely to an increase in the debt and average interest rates, as well as inflation adjustments on certain Treasury securities. Interest costs have increased by 20.6 percent in 2018 from 2017 and by 37.4 percent over the past five years.

Chart B shows the composition of the government's net cost. In fiscal year 2018, nearly three fourths of total net cost came from HHS, SSA, DOD, and VA. Interest on Treasury securities (i.e., debt) held by the public contributed an additional 8 percent, and the other entities included in the government's fiscal year 2018 Statement of Net Cost accounted for a combined 21 percent of the government's total net cost for fiscal year 2018. Chart C shows the five-year trend in these costs. These entities have consistently incurred the largest entity shares of the government's total net cost in recent years. As indicated above, HHS and SSA net costs for fiscal year 2018 ($1.1 trillion and $1.0 trillion, respectively) are attributable to major social insurance programs administered by these entities. DOD net costs of $698.4 billion relate primarily to operations, readiness, and support; personnel; research; procurement; and retirement and health benefits. VA costs of $346.9 billion support health, education and other benefits programs for our nation's veterans. The $132.8 billion decrease in VA net cost during fiscal year 2018 is primarily due to the decrease in losses from changes in actuarial assumptions as referenced earlier. From Chart C, over the past five years, HHS, SSA, and Interest costs have increased 20.1 percent, 14.6 percent, and 37.4 percent, respectively.

Tax and Other Revenues

As noted earlier, tax and other revenues from the Statement of Operations and Changes in Net Position are deducted from total net cost to derive the government's "bottom line" net operating cost. Chart D shows that total tax and other revenue increased slightly by $9.7 billion or 0.3 percent to $3.4 trillion for fiscal year 2018. This increase is attributable mainly to an overall growth in individual income tax collections, partially offset by reduced estate and corporate income tax collections and deposit of earnings from the FR System.[14] Earned revenues from Table 3 are not considered "taxes and other revenue" and, thus, are not shown in Chart D. Individual income tax and tax withholdings and corporate income taxes accounted for about 82.5 percent and 6.2 percent of total revenue, respectively in fiscal year 2018; other revenues from Chart D include Federal Reserve earnings, excise taxes, unemployment taxes, and customs duties.



As previously shown in Table 3, the increases in net cost and tax and revenues almost entirely offset each other, resulting in the government's bottom line net operating cost remaining largely unchanged at $1.2 trillion for fiscal year 2018.

Tax Expenditures

Tax and other revenues reported reflect the effects of tax expenditures, which are special exclusions, exemptions, deductions, tax credits, preferential tax rates, and tax deferrals that allow individuals and businesses to reduce taxes they may otherwise owe. Tax expenditures may be viewed as alternatives to other policy instruments, such as spending or regulatory programs. For example, the government supports college attendance through both spending programs and tax expenditures. The government uses Pell Grants to help low- and moderate-income students afford college and allows certain funds used to meet college expenses to grow tax free in special college savings accounts. Tax expenditures may include deductions and exclusions which reduce the amount of income subject to tax (e.g., deductions for personal residence mortgage interest). Tax credits, which reduce tax liability dollar for dollar for the amount of credit (e.g., child tax credit), are also considered tax expenditures. Tax expenditures may also allow taxpayers to defer tax liability.

Receipts in the calculation of surplus or deficit, and tax revenues in the calculation of net position, reflect the effect of tax expenditures. As discussed in more detail in the Other Information section of this *Financial Report*, tax expenditures will generally lower federal government receipts although tax expenditure estimates do not necessarily equal the increase in Federal revenues (or the change in the budget balance) that would result from repealing these special provisions.

Tax expenditures are reported annually in the Analytical Perspectives of the *Budget*. In addition, current and past tax expenditure estimates and descriptions can be found at the following location from the U.S. Treasury's Office of Tax Policy: https://home.treasury.gov/policy-issues/tax-policy/tax-expenditures.

[14] Fiscal year 2018 Department of the Treasury Agency Financial Report, p. 37

Assets and Liabilities

The government's net position at the end of the year is derived by netting the government's assets against its liabilities, as presented in the Balance Sheet (summarized in Table 4). The Balance Sheet does not include the financial value of the government's sovereign powers to tax, regulate commerce, or set monetary policy or value of nonoperational resources of the government, such as national and natural resources, for which the government is a steward. In addition, as is the case with the Statement of Operations and Changes in Net Position, the Balance Sheet includes a separate presentation of the portion of net position related to funds from dedicated collections. Moreover, the government's exposures are broader than the liabilities presented on the Balance Sheet. The government's future social insurance exposures (e.g., Medicare and Social Security) as well as other fiscal projections, commitments and contingencies, are reported in separate statements and disclosures. This information is discussed later in this MD&A section, the financial statements, and RSI sections of this *Financial Report*.

Table 4: Assets and Liabilities

Dollars in Billions	2018	2017*	Increase / (Decrease) $	%
Assets				
Cash & Other Monetary Assets	$ 507.5	$ 271.2	$ 236.3	87.1%
Loans Receivable, Net	$ 1,419.1	$ 1,350.2	$ 68.9	5.1%
Inventories & Related Property, Net	$ 337.5	$ 326.7	$ 10.8	3.3%
Property, Plant & Equipment, Net	$ 1,090.5	$ 1,087.0	$ 3.5	0.3%
Other	$ 482.1	$ 499.8	$ (17.7)	(3.5%)
Total Assets	**$ 3,836.7**	**$ 3,534.9**	**$ 301.8**	**8.5%**
Less: Liabilities, comprised of:				
Federal Debt Held by the Public & Accrued Interest	$ (15,812.7)	$ (14,724.1)	$ 1,088.6	7.4%
Federal Employee & Veteran Benefits	$ (7,982.3)	$ (7,700.1)	$ 282.2	3.7%
Other	$ (1,562.5)	$ (1,472.6)	$ 89.9	6.1%
Total Liabilities	**$ (25,357.5)**	**$ (23,896.8)**	**$ 1,460.7**	**6.1%**
Net Position (Assets Minus Liabilities)	**$ (21,520.8)**	**$ (20,361.9)**	**$ 1,158.9**	**5.7%**

*Restated (see Financial Statement Note 1.U)

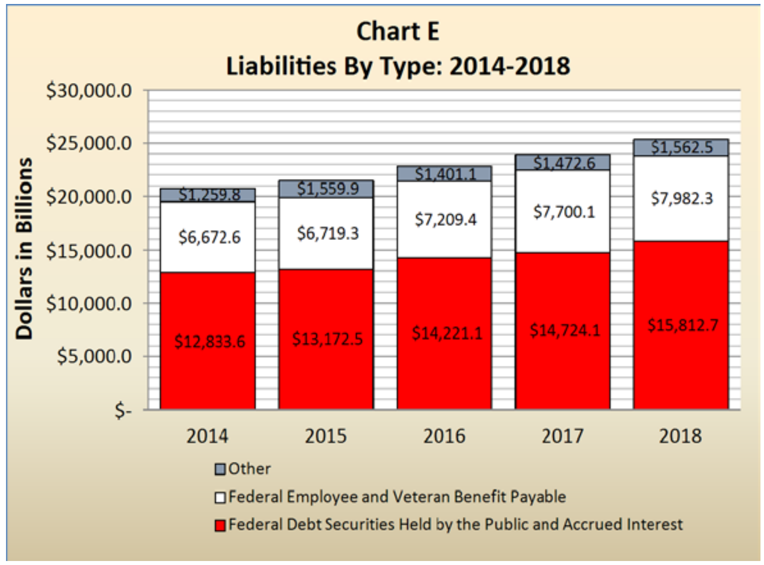
Assets

As of September 30, 2018, the government's $3.8 trillion in assets are comprised mostly of net loans receivable ($1.4 trillion) and net property, plant, and equipment (PP&E) ($1.1 trillion).[15] From Financial Statement Note 4, The Department of Education's (Education's) Federal Direct Student Loan Program accounted for $1.1 trillion (78.6 percent) of total net loans receivable. Education's direct student loan program receivables balances have grown by more than 190 percent since fiscal year 2011 largely due to increased direct loan disbursements, attributable to the continued effect of 2010 legislation requiring a transition for new loans from guaranteed student loans to full direct lending by Education.[16]

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

[16] With the enactment of the SAFRA Act, which was included as part of the *Health Care and Education Reconciliation Act of 2010* (HCERA) (P. L. 111-152), no new loans were originated under the Federal Family Education Loan (FFEL) Program (guaranteed loan program) since July 1, 2010. See Department of Education fiscal year 2018 Agency Financial Report p. 50.

Liabilities



As indicated in Table 4 and Chart E, of the government's $25.4 trillion in total liabilities, the largest liability is federal debt securities held by the public and accrued interest, the balance of which increased by $1.1 trillion (7.4 percent) to $15.8 trillion as of September 30, 2018.

The other major component of the government's liabilities is federal employee and veteran benefits payable (i.e., the government's pension and other benefit plans for its military and civilian employees), which increased $282.2 billion (3.7 percent) during fiscal year 2018, to about $8.0 trillion. This total amount is comprised of $2.5 trillion in benefits payable for the current and retired civilian workforce, and $5.4 trillion for the military and veterans. OPM administers the largest civilian pension plan, covering nearly 2.7 million current employees and 2.6 million annuitants and survivors. The military pension plan covers about 2.1 million current military personnel (including active service, reserve, and National Guard) and approximately 2.3 million retirees and survivors.

Federal Debt

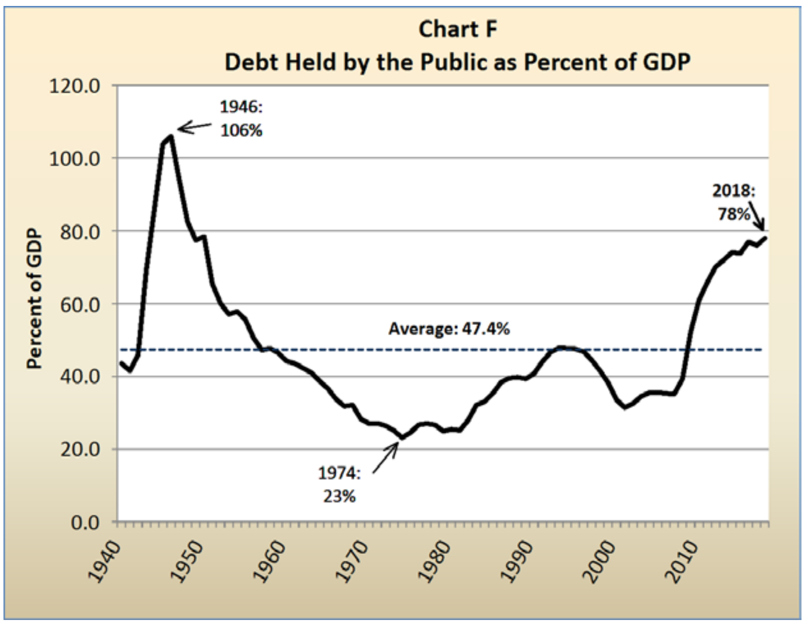
The budget surplus or deficit is the difference between total federal spending and receipts (e.g., taxes) in a given year. The government borrows from the public (increases federal debt levels) to finance deficits. During a budget surplus (i.e., when receipts exceed spending), the government typically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

The government's publicly-held debt, or federal debt held by the public, and accrued interest (Balance Sheet liability) totaled $15.8 trillion as of September 30, 2018. It is comprised of Treasury securities, such as bills, notes, and bonds, net of unamortized discounts and premiums; and accrued interest payable. The "public" consists of individuals, corporations, state and local governments, Federal Reserve Banks (FRBs), foreign governments, and other entities outside the federal government. As indicated above, budget surpluses have typically resulted in borrowing reductions, and budget deficits have conversely yielded borrowing increases. However, the government's debt operations are generally much more complex. Each year, trillions of dollars of debt mature and new debt is issued to take its place. In fiscal year 2018, new borrowings were $10.1 trillion, and repayments of maturing debt held by the public were $9.0 trillion, both increases from fiscal year 2017.

In addition to debt held by the public, the government has about $5.8 trillion in intragovernmental debt outstanding, which arises when one part of the government borrows from another. It represents debt issued by the Treasury and held by government accounts, including the Social Security ($2.9 trillion) and Medicare ($301.0 billion) trust funds. Intragovernmental debt is primarily held in government trust funds in the form of special nonmarketable securities by various parts of the government. Laws establishing government trust funds generally require excess trust fund receipts (including interest earnings) over disbursements to be invested in these special securities. Because these amounts are both liabilities of the Treasury and assets of the government trust funds, they are eliminated as part of the consolidation process for the governmentwide financial statements (see Note 11). When those securities are redeemed, e.g., to pay Social Security benefits, the government will need to obtain the resources necessary to reimburse the trust funds. The sum of debt held by the public and intragovernmental debt equals gross federal debt, which (with some adjustments), is subject to a statutory ceiling (i.e., the debt limit). At the end of fiscal year 2018, debt subject to the statutory limit (DSL) was $21.5 trillion[17] (see sidebar).

Prior to 1917, Congress approved each debt issuance. In 1917, to facilitate planning in World War I, Congress and the President established a dollar ceiling for federal borrowing. With the Public Debt Act of 1941 (Public Law [P.L.] 77-7), Congress and the President set an overall limit of $65 billion on Treasury debt obligations that could be outstanding at any one time. Since then, Congress and the President have enacted a number of measures affecting the debt limit, including several in recent years. Congress and the President most recently suspended the debt limit from February 9, 2018 through March 1, 2019. It is important to note that increasing or suspending the debt limit does not increase spending or authorize new spending; rather, it permits the United States to continue to honor pre-existing commitments to its citizens, businesses, and investors domestically and around the world.

The federal debt held by the public measured as a percent of GDP (debt-to-GDP ratio) (Chart F) compares the country's debt to the size of its economy, making this measure sensitive to changes in both. Over time, the debt-to-GDP ratio has varied widely:



- For most of the nation's history, through the first half of the 20th century, the debt-to-GDP ratio has tended to increase during wartime and decline during peacetime.
- Chart F shows that wartime spending and borrowing pushed the debt-to-GDP ratio to an all-time high of 106 percent in 1946, soon after the end of World War II, but it decreased rapidly in the post-war years,
- The ratio grew rapidly from the mid-1970s until the early 1990s. Strong economic growth and fundamental fiscal decisions, including measures to reduce the federal deficit and implementation of binding "Pay As You Go" (PAYGO) rules (which require that new tax or spending laws not add to the deficit), generated a significant decline in the debt-to-GDP ratio, from a peak of 48 percent in 1993-1995, to 31 percent in 2001.
- During the first decade of the 21st century, PAYGO rules were allowed to lapse, significant tax cuts were implemented, entitlements were expanded, and spending related to defense and homeland security increased. By September 2008, the debt-to-GDP ratio was 39 percent of GDP.
- PAYGO rules were reinstated in 2010, but the extraordinary demands of the last economic and fiscal crisis and the consequent actions taken by the federal government, combined with slower economic growth in the wake of the crisis, pushed the debt-to-GDP ratio up to 74 percent by the end of fiscal year 2014.
- The debt was 78.0 percent of GDP at the end of fiscal year 2018 (compared to 76 percent at the end of fiscal year 2017).[18] From Chart F, since 1940, the average debt-to-GDP ratio is 47.4 percent.

[17]Effective March 2, 2019, the statutory debt limit was set at $22.0 trillion, and on March 4, 2019, the Secretary of the Treasury notified the Congress that the statutory debt limit would be reached on or after that day. When delays in raising the debt limit occur, Treasury must often deviate from its normal debt management operations and take a number of extraordinary measures to meet the government's obligations as they come due without exceeding the debt limit. Treasury began taking these extraordinary actions on March 4, 2019.
[18]10/15/2018 press release: Joint Statement of OMB Director, Mick Mulvaney and Treasury Secretary, Steven T. Mnuchin.

The Economy in Fiscal Year 2018

Table 5: National Economic Indicators*

	FY 2018	FY 2017
Real GDP Growth	3.0%	2.3%
Business Fixed Investment Growth	6.8%	5.0%
Residential Investment Growth	0.5%	3.0%
Average monthly payroll job change (thousands)	219	168
Unemployment rate (percent, end of period)	3.7%	4.2%
Consumer Price Index (CPI)	2.3%	2.2%
CPI, excluding food and energy	2.2%	1.7%
Personal Consumption Expenditure (PCE) Price Index	2.0%	1.8%
Personal Consumption Expenditure (PCE) Price Index	1.9%	1.5%

* Some FY2017 data may differ from the FY2017 Financial Report due to updates and revisions.

The U.S. economy's performance provides a useful backdrop against which to evaluate the government's financial results. U.S. economic growth accelerated during fiscal year 2018 due to the Tax Cuts and Jobs Act and deregulation. Net jobs increased from an average of 168,000 jobs per month in fiscal year 2017 to 219,000 jobs per month in fiscal year 2018, and by the end of the fiscal year, the unemployment rate had declined to a 49-year low of 3.7 percent. Headline inflation (as measured by the Consumer Price Index, or CPI) was relatively stable, while core inflation, which excludes food and energy, accelerated. In fiscal year 2018, growth in after-tax personal income as well as productivity held steady at the solid paces seen in the previous fiscal year.

Buoyed by the first major tax reform in three decades, as well as other pro-growth policies, real (i.e., inflation-adjusted) GDP growth accelerated to 3.0 percent in fiscal year 2018, after growing in the previous fiscal year by 2.3 percent. A marked acceleration in consumption, as well as faster growth in business fixed investment and a significant contribution from net exports, drove growth. Growth of consumer spending strengthened to 2.9 percent in fiscal year 2018, up from 2.4 percent during the previous fiscal year, while business fixed investment accelerated for the second consecutive year, growing by 6.8 percent in the latest fiscal year after increasing at a 5.0 percent pace during fiscal year 2017.

During fiscal year 2018, for the first time in the history of the Job Openings and Labor Turnover Survey (JOLTS), the number of available job openings exceeded the number of unemployed persons. After the economy created 2.0 million payroll jobs during fiscal year 2017, an additional 2.6 million jobs were added during fiscal year 2018, and the average monthly pace of job creation also stepped up from 168,000 during fiscal year 2017 to 219,000 per month in the latest fiscal year. By the end of fiscal year 2018, the number of unemployed persons in the economy had declined by 805,000 to 6.0 million as of September 2018. The unemployment rate declined 0.5 percentage points, from 4.2 percent in September 2017 to 3.7 percent in September 2018, its lowest level since December 1969. During fiscal year 2018, other notable labor market developments included the decline in the unemployment rate for adult women to 3.3 percent, for African Americans to 6.0 percent, and for Hispanics to 4.5 percent, rates that are historically low. Declining unemployment rates are associated with faster economic growth rates and rising incomes.

During fiscal year 2018, headline inflation edged up, while core inflation accelerated more noticeably. The CPI rose 2.3 percent during fiscal year 2018, slightly faster than the 2.2 percent during fiscal year 2017, while core inflation accelerated to 2.2 percent, higher than the 1.7 percent reading during fiscal year 2017. The increase in the Federal Reserve's preferred measure of inflation, the Personal Consumption Expenditure (PCE) price index, was also relatively stable at the headline level, ticking up to 2.0 percent in fiscal year 2018 from 1.8 percent in fiscal year 2017. Over the course of the fiscal year, however, inflation by this measure decelerated later in the year. The PCE price index rose by 1.85 percent headline and 1.7 percent core in the last six months of fiscal year 2018 at a compound annual rate, and, in the final three months, rose by 1.5 headline and 1.4 percent core at a compound annual rate.

Growth of nominal disposable personal income (DPI) held steady during fiscal year 2018, which helped to stabilize purchasing power in real terms. Real DPI grew 2.8 percent in fiscal year 2018, matching the 2.8 percent rate during fiscal year 2017. Towards the end of fiscal year 2018, growth of nominal average hourly earnings also accelerated, helping to boost wages in real terms. Real average hourly earnings increased 0.5 percent during fiscal year 2018, after rising only 0.2 percent the previous fiscal year.

The housing market showed signs of slowing during fiscal year 2018, partly reflecting the marked rise in mortgage rates over the fiscal year. Residential investment grew by 0.5 percent, after a 3.0 percent advance during the previous fiscal year. Home price growth began to slow towards the end of the fiscal year. Existing home sales declined throughout fiscal year 2018, while new home sales tailed off at the very end of the fiscal year. However, the monthly average level of new residential construction spending was a bit higher during 2018 compared to 2017. Other indicators that drive housing demand are strong, such as labor force participation and household formation.

Growth of labor productivity held relatively steady during fiscal year 2018. Productivity growth rose 1.3 percent during fiscal year 2018, after increasing by 1.4 percent during fiscal year 2017. Growth in these two fiscal years contrasted sharply with the 0.1 percent decline in productivity growth during fiscal year 2016.

An Unsustainable Fiscal Path

An important purpose of the *Financial Report* is to help citizens understand current fiscal policy and the importance and magnitude of policy reforms necessary to make it sustainable. This *Financial Report* includes the SLTFP and a related Note Disclosure (Note 23). The Statements display the present value of 75-year projections of the federal government's receipts and non-interest spending[19] for fiscal year 2018 and fiscal year 2017.

Fiscal Sustainability

A sustainable fiscal policy is one where the debt-to-GDP ratio is stable or declining over the long term. The projections in this *Financial Report* indicate that current policy is not sustainable. As discussed below, if current policy is left unchanged, the debt-to-GDP ratio is projected to rise from its current level of 78 percent in 2018 to 84 percent by 2022, to over 100 percent by 2030, and to 530 percent in 2093 and to even higher levels, thereafter. Preventing the debt-to-GDP ratio from rising over the next 75 years is estimated to require some combination of spending reductions and revenue increases that amount to 4.1 percent of GDP over the period. While this estimate of the "75-year fiscal gap" is highly uncertain, it is nevertheless nearly certain that current fiscal policies cannot be sustained indefinitely.

Delaying action to reduce the fiscal gap increases the magnitude of spending and/or revenue changes necessary to stabilize the debt-to-GDP ratio. For example, the magnitude of spending cuts and/or revenue increases necessary to close the gap rises about 20 percent if reforms are delayed ten years, and about 46 percent if reform is delayed 20 years.

The estimates of the cost of policy delay assume policy does not affect GDP or other economic variables. Delaying fiscal adjustments for too long raises the risk that growing federal debt would increase interest rates, which would, in turn, reduce investment and ultimately economic growth.

The projections discussed here assume current policy[20] remains unchanged, and hence, are neither forecasts nor predictions. Nevertheless, policy changes must be enacted so that actual financial outcomes will be different than those projected.

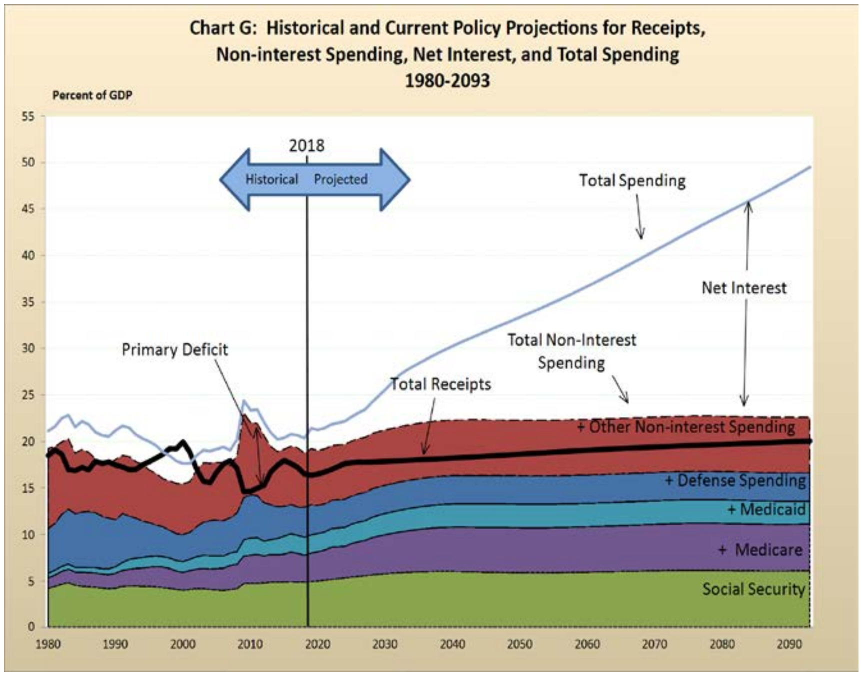
The Primary Deficit, Interest, and Debt

The primary deficit – the difference between non-interest spending and receipts – is the determinant of the debt-to-GDP ratio over which the government has the greatest control (the other determinants include interest rates and growth in GDP). Chart H shows receipts, non-interest spending, and the difference – the primary deficit – expressed as a share of GDP. The primary deficit-to-GDP ratio spiked during 2009 through 2012 due to the 2008-09 financial crisis and the ensuing severe recession, as well as the increased spending and temporary tax reductions enacted to stimulate the economy and support recovery. These elevated primary deficits resulted in a sharp increase in the ratio of debt to GDP, which rose from 39 percent at the end of 2008 to 70 percent at the end of 2012. As an economic recovery took hold, the primary deficit ratio fell, averaging 1.9 percent of GDP over 2013 through 2018. This primary deficit ratio was still high enough that the debt-to-GDP ratio increased further, ending 2018 at 78 percent. The primary deficit ratio is projected to rise to 2.9 percent in 2019 and then shrink slightly through 2024 as the economy grows. After 2024, however, increased spending for Social Security and health programs due to the ongoing retirement of the baby boom generation and increases in the price of health care services is projected to result in increasing primary deficit ratios that reach 3.0 percent of GDP in 2028. The primary deficit ratio peaks at 4.1 percent in 2039, gradually decreases beyond that point as aging of the population continues at a slower pace, and reaches 2.5 percent of GDP in 2093.

Primary deficit trends are heavily influenced by tax receipts. Receipts as a share of GDP were markedly depressed in 2009 through 2012 because of the recession and tax reductions enacted as part of the *American Recovery and Reinvestment Act of 2009* (ARRA) and the *Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010*. The share subsequently increased to 18 percent of GDP by 2015, then decreased to 16.5 percent in 2018, following enactment of the *Tax Cuts and Jobs Act of* 2018 (TCJA), below its 30-year average of 17.3 percent.

[19] For the purposes of the Statement of Long-Term Fiscal Projections and this analysis, spending is defined in terms of outlays. In the context of federal budgeting, spending can either refer to: (1) budget authority – the authority to commit the government to make a payment; (2) obligations – binding agreements that will result in either immediate or future payment; or (3) outlays, or actual payments made.

[20] Current policy in the projections is based on current law, but includes certain adjustments, such as extension of certain policies that expire under current law but are routinely extended or otherwise expected to continue (e.g., reauthorization of the Supplemental Nutrition Assistance Program).



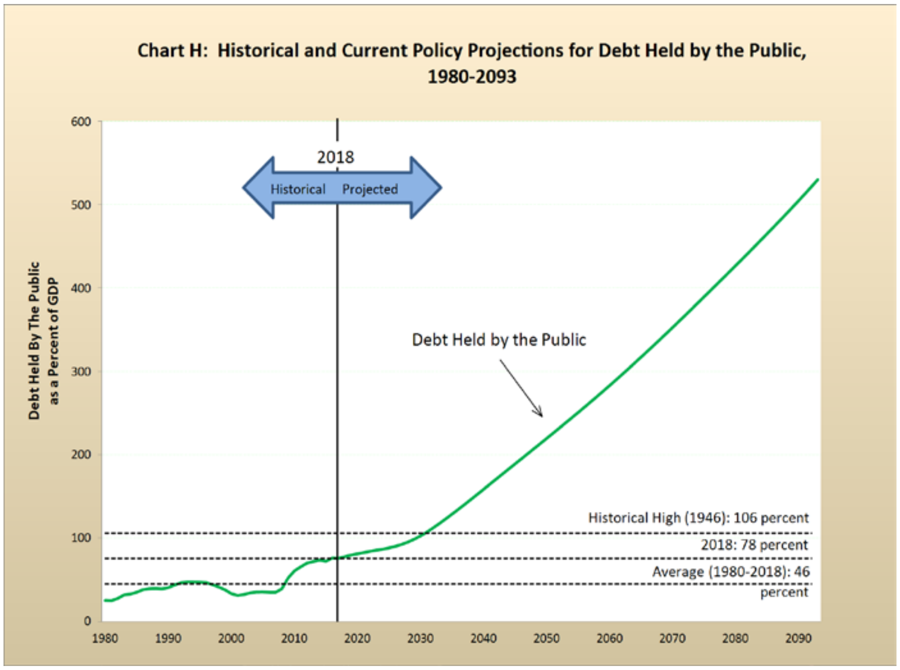
Receipts are projected to grow slightly more rapidly than GDP over the projection period as increases in real incomes cause more taxpayers and a larger share of income to fall into the higher individual income tax brackets.

Non-interest spending as a share of GDP is projected to rise gradually from 18.7 percent in 2018 to 21.0 percent in 2029, and ends at 22.6 percent in 2093. Beginning in 2020, these increases are principally due to faster growth in Medicare, Medicaid, and Social Security spending (see Chart G). Over the next 25 years, the aging of the baby boom generation is projected to increase the Social Security, Medicare, and Medicaid spending shares of GDP by about 1.0 percentage points, 1.7 percentage points, and 0.6 percentage points, respectively. After 2035, the Social Security spending share of GDP remains relatively stable, while the combined Medicare and Medicaid spending share of GDP continues to increase, albeit at a slower rate, due to projected increases in health care costs.

One of the most important assumptions underlying the projections is the future growth of health care costs. As discussed in Note 22, these future growth rates – both for health care costs in the economy generally and for Federal health care programs such as Medicare, Medicaid, and *Affordable Care Act* (ACA) exchange subsidies – are highly uncertain. In particular, enactment of the ACA in 2010 and the *Medicare Access and CHIP Reauthorization Act (MACRA)* in 2015 established cost controls for Medicare hospital and physician payments whose long-term effectiveness is still to be demonstrated. The Medicare spending projections in the long-term fiscal projections are based on the projections in the 2018 Medicare trustees' report, which assume the ACA and MACRA cost control measures will be effective in producing a substantial slowdown in Medicare cost growth. As discussed in Note 22, the Medicare projections are subject to much uncertainty about the ultimate effects of these provisions to reduce health care cost growth. For the long-term fiscal projections, that uncertainty also affects the projections for Medicaid and exchange subsidies, because the cost per beneficiary in these programs is assumed to grow at the same reduced rate as Medicare cost growth per beneficiary.

As discussed in Note 23, the primary deficit projections reported in the Fiscal Year 2018 Financial Report increased compared to those reported in the Fiscal Year 2017 Financial Report. These increases are attributable to a number of factors, but in great part to: (1) use of fiscal year 2018 actual budget results that differed from projections made in prior years, including lower corporate and individual income tax receipts, and higher non-defense discretionary spending as a result of the increased discretionary spending caps in the Bipartisan Budget Act of 2018 (BBA 2018); and (2) revised assumptions, including those related to corporate income taxes to reflect enactment of the TCJA, and to growth in discretionary spending. For the Fiscal Year 2018 Financial Report, corporate income tax receipts are assumed to be the same share of GDP as projected in the 2018 Midsession Review, which incorporates the expected effects of the TCJA. In addition, the projections assume that individual income and estate and gift tax provisions of the TCJA are permanently extended; Congressional action is required to make this change. With regard to discretionary spending, previous statements assumed that it followed the caps established by the Budget Control Act of 2011 (BCA) and then grew with nominal GDP in the years after caps expired. However, discretionary spending has not been limited to the caps established in the BCA. Instead, budget deals in 2013, 2015, and 2018 raised the caps in each of the years 2014 through 2019. Therefore, as a reasonable representation of current policy, the 2018 projections assume that discretionary spending grows at the same rate as nominal GDP beyond 2019, rather than being limited to the statutory caps, subject to Joint Committee on Deficit Reduction spending controls. Congressional action is required to make this change. GDP, interest, and other economic and demographic assumptions are the same as those that underlie the most recent Social Security and Medicare trustees' report projections, adjusted for historical revisions that occur annually. See Note 23—Long-Term Fiscal Projections for more information about the assumptions used in this analysis.

The primary deficit-to-GDP projections in Chart G, projections for interest rates, and projections for GDP together determine the debt-to-GDP ratio projections shown in Chart H. That ratio was 78 percent at the end of fiscal year 2018 and under current policy is projected to be 84 percent by 2022, over 100 percent by 2030, and 530 percent in 2093. The change in debt held by the public from one year to the next is approximately equal to the budget deficit, the difference between total spending and total receipts. The debt-to-GDP ratio rises continually in great part because higher levels of debt lead to higher net interest expenditures, and higher net interest expenditures lead to higher debt.[21] The continuous rise of the debt-to-GDP ratio indicates that current policy is unsustainable.



These debt-to-GDP projections are higher than the corresponding projections in both the fiscal year 2017 and fiscal year 2016 *Financial Reports*. For example, the last year of the 75-year projection period used in the fiscal year 2016 *Financial Report* is 2091. In the fiscal year 2018 *Financial Report*, the debt-to-GDP ratio for 2091 is projected to be 513 percent, which compares with 293 and 252 percent projected for that same year in the fiscal year 2017 *Financial Report* and the fiscal year 2016 *Financial Report,* respectively.[22]

The Fiscal Gap and the Cost of Delaying Policy Reform

The 75-year fiscal gap is one measure of the degree to which current policy is unsustainable. It is the amount by which primary surpluses over the next 75 years must, on average, rise above current-policy levels in order for the debt-to-GDP ratio in 2093 to remain at its level in 2018 (78 percent). The projections show that projected primary deficits average 3.2 percent of GDP over the next 75 years under current policy. If policies were adopted to eliminate the fiscal gap, the average primary surplus over the next 75 years would be 0.8 percent of GDP, 4.1 percentage points higher than the projected present value of receipts less non-interest spending shown in the basic financial statement. Hence, the 75-year fiscal gap is estimated to equal 4.1 percent of GDP. This gap represents 21.9 percent of 75-year present value receipts and 18.6 percent of 75-year present value non-interest spending. The fiscal gap was estimated at 2.0 percent in the 2017 *Financial Report*, 2.1 percentage points lower than estimated in this Report.

In these projections, closing the fiscal gap requires running substantially positive primary surpluses, rather than simply eliminating the primary deficit. The primary reason is that the projections assume future interest rates will exceed the growth rate of GDP. Achieving primary balance (that is, running a primary surplus of zero) implies that the debt grows each year by the amount of interest spending, which under these assumptions would result in debt growing faster than GDP.

Table 6 shows the cost of delaying policy reform to close the fiscal gap by comparing policy reforms that begin in three different years. Immediate reform would require increasing primary surpluses by 4.1 percent of GDP on average between 2019

Table 6

Costs of Delaying Fiscal Reform

Period of Delay	Change in Average Primary Surplus
Reform in 2019 (No Delay)	4.1 percent of GDP between 2019 and 2093
Reform in 2029 (Ten-Year Delay)	4.9 percent of GDP between 2029 and 2093
Reform in 2039 (Twenty-Year Delay)	6.0 percent of GDP between 2039 and 2093

Note: Reforms taking place in 2018, 2028, and 2038 from the 2017 Financial Report were 2.0, 2.4, and 3.0 percent of GDP, respectively.

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

[22] See the Note 23 of the *Fiscal Year 2017 Financial Report of the U.S. Government* for more information about changes in the long term fiscal projections between fiscal years 2016 and 2017.

and 2093 (i.e., some combination of reducing spending and increasing revenue by a combined 4.1 percent of GDP on average over the 75-year projection period). Table 6 shows that delaying policy reform forces larger and more abrupt policy reforms over shorter periods. For example, if policy reform is delayed by 10 years, closing the fiscal gap requires increasing the primary surpluses by 4.9 percent of GDP on average between 2029 and 2093. Similarly, delaying reform by 20 years requires primary surplus increases of 6.0 percent of GDP on average between 2039 and 2093. The differences between the required primary surplus increases that start in 2029 and 2039 (4.9 and 6.0 percent of GDP, respectively) and that which starts in 2019 (4.1 percent of GDP) is a measure of the additional burden that delay would impose on future generations. Future generations are harmed by policy reform delay, because the higher the primary surplus is during their lifetimes the greater the difference is between the taxes they pay and the programmatic spending from which they benefit.

Conclusion

The past 11 years saw the national debt nearly double as a share of GDP, bringing it to a level not seen since shortly after World War II. The debt-to-GDP ratio is projected to rise over the 75-year projection period and beyond if current policy is unchanged, which implies that current policy is not sustainable and must ultimately change. If policy changes are not so abrupt as to hinder economic growth, then the sooner policies are adopted to avert these trends, the smaller the changes to revenue and/or spending that would be required to achieve sustainability over the long term. While the estimated magnitude of the fiscal gap is subject to a substantial amount of uncertainty, there is little doubt that current policy is not sustainable.

These long-term fiscal projections and the topic of fiscal sustainability are discussed in further detail in Note 23 and the RSI section of this *Financial Report.*

Social Insurance

The long-term fiscal projections reflect government receipts and spending as a whole. The SOSI focuses on the government's "social insurance" programs: Social Security, Medicare, Railroad Retirement, and Black Lung. [23] For these programs, the SOSI reports: (1) the actuarial present value of all future program revenue (mainly taxes and premiums) - excluding interest - to be received from or on behalf of current and future participants; (2) the estimated future scheduled expenditures to be paid to or on behalf of current and future participants; and (3) the difference between (1) and (2). Amounts reported in the SOSI and in the RSI section in this *Financial Report* are based on each program's official actuarial calculations.

Table 7 summarizes amounts reported in the SOSI, showing that net social insurance expenditures are projected to be $53.8 trillion over 75 years as of January 1, 2018 for the "Open Group," an increase of $4.8 trillion over net expenditures of $49.0 trillion projected in the 2017 *Financial Report.*[24] The current-law 2018 amounts reported for Medicare reflect the physician payment levels expected under the MACRA payment rules and the ACA-mandated reductions in other Medicare payment rates, but not the payment reductions and/or delays that would result from trust fund depletion.[25] Similarly, current-law projections for Social Security do not reflect benefit payment reductions and/or delays that would result from fund depletion. By accounting convention, the transfers of general revenues are eliminated in the consolidation of the SOSI at the governmentwide level and as such, the general revenues that are used to finance Medicare Parts B and D are not included in these calculations. For the fiscal year 2018 and 2017 SOSI, the amounts eliminated totaled $32.9 trillion and $30.0 trillion, respectively. SOSI programs and amounts are included in the broader fiscal sustainability analysis in the previous section, although on a slightly different basis (as described in Note 23).

The amounts reported in the SOSI provide perspective on the government's long-term estimated exposures for social insurance programs. These amounts are not considered liabilities in an accounting context. Future benefit payments will be recognized as expenses and liabilities as they are incurred based on the continuation of the social insurance programs' provisions contained in current law. The social insurance trust funds account for all related program income and expenses. Medicare and Social Security taxes, premiums, and other income are credited to the funds; fund disbursements may only be made for benefit payments and program administrative costs. Any excess revenues are invested in special non-marketable U.S. government securities at a market rate of interest. The trust funds represent the accumulated value, including interest, of all prior program surpluses, and provide automatic funding authority to pay cover future benefits.

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

[24] 'Closed' Group and 'Open' Group differ by the population included in each calculation. From the SOSI, the 'Closed' Group includes: (1) participants who have attained eligibility and (2) participants who have not attained eligibility. The 'Open' Group adds future participants to the 'Closed' Group. See 'Social Insurance' in the Required Supplementary Information section in this *Financial Report* for more information.

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

Table 7: Social Insurance Future Expenditures in Excess of Future Revenues

Dollars in Trillions	2018	2017	Increase / (Decrease) $	%
Open Group (Net):				
Social Security (OASDI)	$ (16.1)	$ (15.4)	$ 0.7	4.5%
Medicare (Parts A, B, & D)	$ (37.6)	$ (33.5)	$ 4.1	12.2%
Other	$ (0.1)	$ (0.1)	$ -	0.0%
Total Social Insurance Expenditures, Net (Open Group)	**$ (53.8)**	**$ (49.0)**	$ 4.8	9.8%
Total Social Insurance Expenditures, Net (Closed Group)	**$ (73.5)**	**$ (68.2)**	$ 5.3	7.8%
Social Insurance Net Expenditures as a % of Gross Domestic Product (GDP)*				
Open Group				
Social Security (OASDI)	(1.2%)	(1.2%)		
Medicare (Parts A, B, & D)	(2.9%)	(2.8%)		
Total (Open Group)	**(4.0%)**	**(4.0%)**		
Total (Closed Group)	**(5.5%)**	**(5.5%)**		

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

* GDP values used are from the 2018 & 2017 Social Security and Medicare Trustees Reports and represent the present value of GDP over the 75-year projection period. As the GDP used for Social Security and Medicare differ slightly in the Trustees Reports, the two values are averaged to estimate the 'Other' and Total Net Social Insurance Expenditures as percent of GDP. As a result, totals may not equal the sum of components due to rounding.

Table 8 identifies the principal reasons for the changes in projected social insurance amounts during 2018 and 2017. The following briefly summarizes the significant changes for the current valuation (as of January 1, 2018) as disclosed in Note 22, Social Insurance. Note 22 is compiled from disclosures included in the financial reports of those entities administering these programs, including SSA and HHS. See Note 22 for additional information.

Table 8: Changes in Social Insurance Projections

Dollars in Trillions	2018	2017
Net Present Value (NPV) - Open Group (Beginning of the Year)	**$ (49.0)**	**$ (46.7)**
Changes In:		
Valuation Period	$ (1.9)	$ (2.0)
Demographic data and assumptions	$ 0.7	$ (0.2)
Economic data and assumptions[1]	$ (0.5)	$ (0.6)
Law or policy	$ (1.0)	$ -
Methodology and programmatic data[1]	$ 0.2	$ -
Economic and other healthcare assumptions[2]	$ (1.5)	$ (0.3)
Change in projection base[2]	$ (0.9)	$ 0.7
Net Change in Open Group measure	$ (4.8)	$ (2.3)
NPV - Open Group (End of the Year)	**$ (53.8)**	**$ (49.0)**

1 Relates to SSA.

2 Relates to HHS.

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

- Change in valuation period (affects both Social Security and Medicare): This change replaces a small negative net cash flow for 2017 with a much larger negative net cash flow for 2092. As a result, the present value of the estimated future net cash flows decreased (became more negative) by $1.9 trillion.
- Changes in demographic data, assumptions, and methods (affects both Social Security and Medicare): For the current valuation, the only change to the ultimate demographic assumptions was a small decrease of 10,000 Lawful Permanent Resident (LPR) immigrants per annum in the future. However, the starting demographic values and the way these values transition to the ultimate assumptions were changed. These changes included, but were not limited to lower birth rates than originally assumed, the observed persistent drop in the total fertility rate in recent years is now assumed to be a loss of potential births rather than just a deferral to this period, and higher death rates than projected in prior valuations for Medicare experience ages 65 and older. Overall, changes to these assumptions caused the present value of the estimated future net cash flows to increase (become less negative) by $700 billion.
- Changes in economic data and assumptions (affects Social Security only): The ultimate economic assumptions for the current valuation period are the same as those for the prior year valuation. However, the starting economic values and the way these values transition to the ultimate assumptions were changed. These changes included: the estimated level of

potential GDP was reduced by about 1 percent in 2017 and throughout the projection period, meaning that cumulative growth in actual GDP is 1 percent less over the remainder of the projected recovery than assumed in the prior valuation; near-term interest rates were decreased, and lower than expected ratios of and assumed extended recoveries for labor compensation to GDP and taxable payroll to GDP. Overall, changes to these assumptions caused the present value of the estimated future net cash flows to decrease (become more negative) by $500 billion.

- Changes in Law or Policy: Between the prior and current valuation periods, no new laws, regulations, or policies were enacted that are expected to have significant effects on the OASDI or Medicare programs. However, the current valuations for each program do incorporate some notable changes with negligible effects on the present value of estimated cash flows:
  - For Social Security, the 2012 Deferred Action for Childhood Arrivals (DACA) program is assumed to be phased out over the next two years (the prior valuation assumed that the 2012 DACA program would continue indefinitely); and the TCJA includes the elimination of the individual mandate penalty of the *Patient Protection and Affordable Care Act*, which is expected to cause some individuals to drop employer-sponsored health insurance, increase OASDI-covered wages, and taxable payroll slightly.
  - For Medicare, legislation that affected the present value of estimated cash flows includes but is not limited to: The *Disaster Tax Relief and Airport and Airway Extension Act of 2017* and the *Bipartisan Budget Act of 2018 (BBA)*.

  Overall, these changes to these assumptions caused the present value of the estimated future net cash flows to decrease (become more negative) by $1.0 trillion.
- Changes in economic and other healthcare assumptions (affects Medicare only): The economic assumptions used in the Medicare projections are the same as those used for the OASDI (described above) and are prepared by the Office of the Chief Actuary at SSA. In addition to the economic assumptions changes described above, the healthcare assumptions are specific to the Medicare projections. Changes to these assumptions in the current valuation include: utilization rate assumptions for inpatient hospital use and utilization rate and case mix assumptions for skilled nursing facilities were decreased; payment rates to private health plans are higher than projected in last year's report; higher projected manufacturer rebates. The net impact of these changes caused the present value of the estimated future net cash flows to decrease (become more negative) by $1.5 trillion.
- Change in Projection Base (affects Medicare only): Actual income and expenditures in 2017 were different than what was anticipated when the 2017 Medicare Trustees Report projections were prepared. Part A payroll tax income was lower and expenditures were higher than anticipated, based on actual experience. Part B total income and expenditures were higher than estimated based on actual experience. For Part D, actual income and expenditures were both lower than prior estimates. The net impact of the Part A, B, and D projection base changes is a decrease (become less negative) in the estimated future net cash flow by $900 billion.

Projected net expenditures for Medicare Parts A and B declined significantly between fiscal year 2009 and fiscal year 2010 reflecting provisions of the ACA. As reported in Note 22, uncertainty remains about whether the projected cost savings and productivity improvements will be sustained in a manner consistent with the projected cost growth over time. Note 22 includes an alternative projection to illustrate the uncertainty of projected Medicare costs. As indicated earlier, GAO disclaimed opinions on the 2018, 2017, 2016, 2015 and 2014 SOSI because of these significant uncertainties.

Costs as a percent of GDP of both Medicare and Social Security, which are analyzed annually in the Medicare and Social Security Trustees' Reports, are projected to increase substantially through the mid-2030s because: (1) the number of beneficiaries rises rapidly as the baby-boom generation retires and (2) the lower birth rates that have persisted since the baby boom cause slower growth in the labor force and GDP.[26] According to the Medicare Trustees' Report, spending on Medicare is projected to rise from its current level of 3.7 percent of GDP to 5.9 percent in 2042 and to 6.2 percent in 2092.[27] As for Social Security, combined spending is projected to generally increase from its current level of 4.9 percent of GDP to about 6.1 percent by 2038, declining to 5.9 percent by 2052 and then generally increase to 6.1 percent by 2092. The government collects and maintains funds supporting the Social Security and Medicare programs in Trust Funds. A scenario where projected funds expended exceed projected funds received, as reported in the SOSI, will cause the balances in those Trust Funds to deplete over time. Table 9 summarizes additional current status and projected trend information, including years of projected depletion, for the Medicare and Social Security Trust Funds.

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[26] A Summary of the 2018 Annual Social Security and Medicare Trust Fund Reports, p. 1-2 and the 2017 Medicaid Actuarial Report
[27] Percent of GDP amounts are expressed in gross terms (including amounts financed by premiums and state transfers).

Table 9: Trust Fund Status		
Fund	**Projected Depletion**	**Projected Post-Depletion Trend**
Medicare Hospital Insurance (HI)*	2026 (2029 in FY 2017 Report)	In 2026, trust fund income is projected to cover 91 percent of benefits, decreasing to 78 percent in 2042, then increasing to 85 percent by 2092.
Combined Old-Age Survivors and Disability Insurance (OASDI)**	2034 (unchanged from FY 2017 Report)	In 2034, trust fund income is projected to cover 79 percent of scheduled benefits, decreasing to about 74 percent by 2092.

* Source: 2018 Medicare Trustees Report ** Source: 2018 OASDI Trustees Report

Projections assume full Social Security and Medicare benefits are paid after fund depletion contrary to current law.

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

Financial Management

Results-Oriented Accountability for Grants

Approximately $700 billion is spent annually on grants and cooperative agreements. Grants managers, both internal and external to the government, report that approximately 40 percent of their time is spent using antiquated processes to monitor compliance rather than using data analytics to monitor results. The President's Management Agenda (PMA) Cross Agency Priority (CAP) Goal #8, Results-Oriented Accountability for Grants, provides a comprehensive roadmap for improving grants management and reducing recipient reporting burden. Increased efficiencies in the grant-making process will provide recipients more time to perform work associated with the grant, thereby helping agencies[28] more effectively achieve their missions.

The CAP Goal strategy focuses on standardizing grants data, modernizing digital tools, and using data to promote decision making that is based on risk and performance. In support of the CAP goal, OMB issued "Strategies to Reduce Grant Recipient Reporting Burden," M-18-24, which requires agencies to increase grant program efficiency, promote evaluation of grant programs, and reduce reporting burden.

M-18-24 requires agencies to use the System for Award Management (SAM) information to comply with award requirements, reducing the recipient burden and government cost of having multiple agencies request the same information (except under limited circumstances) from the grant recipient. M-18-24 also requires agencies to evaluate all systems and other methods used to collect information from recipients to determine if the same data is being collected by the agency multiple times and to develop a strategy to eliminate any duplicative requests.

OMB is leading an agency-wide Grants Management Data Standards Work Group, and in September 2018, the Group completed an initial set of draft grants management data standards. In November 2018, a Draft Grants Management Data Standards Feedback website was set up to gather public input on the data standards. Input from the public will be used in finalizing the data standards that will allow inter-agency grants data to be created, reduce the number of grants management systems, and promote a risk-based, data-driven approach to managing federal grants.

Getting Payments Right

Preventing improper payments within the federal government is a priority for the Administration and OMB. In March 2018, OMB released the PMA CAP Goal #9, Getting Payments Right. In addition to the historical focus on identifying and addressing improper payment issues after they occur, the CAP goal has a renewed focus on systemic enhancements to preventing improper payments from occurring at all. This CAP Goal has resulted in exceptional collaboration across the CFO community to identify the causes of improper payments through two main strategies: (1) reducing monetary loss and (2) clarifying and streamlining reporting requirements. For agencies with programs reporting more than $100 million in monetary loss in fiscal year 2018, a scorecard must be completed quarterly and posted on paymentaccuracy.gov. These scorecards provide information on the actions taken and progress made on preventing improper payments that would result in monetary loss to the government.

Just as it did in fiscal year 2018, in fiscal year 2019, OMB will continue to work with agencies to improve the identification of the root causes of improper payments that result in monetary loss and to promote data analytic methods that take a comprehensive view of an agency's payment lifecycle. In addition, OMB will continue to work with Treasury on outreach related to the Do Not Pay Business Center and the services they provide to agencies to ensure payment integrity. In June 2018, OMB released Circular A-123, Appendix C (M-18-20), Requirements for Payments Integrity Improvement to create a unified, comprehensive, and less burdensome set of requirements.

In fiscal year 2018, program performance was mixed, with some programs experiencing significant increases in improper payment estimates and others showing signs of improvement. As in the past, agencies recovered approximately $20 billion in overpayments through payment recapture audits and other methods. The estimated amount of improper payments increased in general across programs in fiscal year 2018, roughly in line with increases in program outlays. More details on fiscal year 2018 improper payment data can be found at PaymentAccuracy.gov.

In fiscal year 2019, OMB will continue to work with agencies, the Chief Financial Officers Council (CFOC), and other stakeholders as part of the Getting Payments Right CAP Goal. In addition, OMB will continue to rely on agency inspector general (IG) recommendations for additional program-specific improvements. OMB will also continue to improve communications with the public about improper payment rates and amounts.

[28]The term "agency" is used in the Financial Management section of the Management's Discussion and Analysis rather than the term "entity," which is used throughout the rest of the Financial Report. SFFAS No. 47, Reporting Entity, defines the term "entity" for federal financial reporting purposes and addresses both component and governmentwide financial reporting. The term entity is generally broader than "agency" because it refers to agencies, components of agencies, and the federal government as a whole. The term "agency" is used in this section because the laws, policies, and plans discussed in this section apply to "agencies" as defined in particular laws or policy guidance documents and because the laws, policies, and plans discussed in this section do not generally define the term "entity."

Leveraging Data as a Strategic Asset

The *Digital Accountability and Transparency Act of 2014* (DATA Act), signed on May 9, 2014, established a vision for the future of federal spending transparency. The Act amended the *Federal Funding Accountability and Transparency Act of 2006* by requiring that all federal spending be displayed on a website in searchable, downloadable, and machine-readable formats and by requiring publication of agency financial data.

The improved and expanded USAspending.gov website was launched on April 2, 2018. The new website allows taxpayers to examine nearly $4 trillion in federal spending and observe how this money flows from Congressional appropriations to local communities and businesses. The data from over 100 federal agencies is compiled by Treasury and will continue to be published on a quarterly basis. The new site allows users to explore information and download reports that are catered to their specific interests. The new site also includes a new feature, the Data Lab, which provides additional use cases, data visualizations, and analysis with insights into federal spending and trends.

In November 2017, GAO and many agency Offices of Inspector General published audits of the quality of the data as required under the DATA Act. As a result of these audits, in June 2018, OMB issued guidance to improve data quality, M-18-16, Management of Reporting Data Integrity Risk, Appendix A to OMB Circular A-123. The guidance requires agencies to develop and implement a Data Quality Plan for fiscal years 2019 through 2021 at a minimum. Agencies are required to integrate Enterprise Risk Management (ERM) processes and internal controls and agencies are also required to consider in their assurance statements all internal controls (including financial and non-financial controls, and controls over DATA Act, financial, and all other reporting). The CFOC and key stakeholders from the procurement and financial assistance communities developed a DATA Act Data Quality Playbook as a resource tool for management and the audit communities.

As the quality of this data improves, OMB will work with Treasury and agencies to find additional data sources that could be linked to the DATA Act to better inform the public about the purpose and results of spending.

Sharing Quality Financial Management Services

The federal financial management infrastructure exists in a complex environment of legacy information technology, customized tools built to unique requirements, and business processes that do not fully leverage modern technology. The sharing of financial technology and services has been successful for smaller agencies, but has not met expectations for larger agencies. A cross-agency subgroup of the CFOC developed the core business framework for financial management that was used in the fall of 2017 to explore industry capabilities for smarter use of technology in federal financial management. This information is being used to develop and implement recommendations to improve financial management across the government. Results of ongoing efforts to support PMA CAP Goal #5, Sharing Quality Services, will be provided in fiscal year 2019. Please visit https://www.performance.gov/CAP/CAP_goal_5.html for additional information regarding CAP Goal #5.

Audit

Since the passage of the *CFO Act of 1990*, the federal financial community has made significant progress in financial accounting and reporting. As shown in Table 10, for fiscal year 2018, 22 of the 24 CFO Act agencies obtained an opinion from the independent auditors on their financial statements.[29] In addition, 40 auditor-identified material weaknesses were reported at the end of both fiscal years 2017 and 2018. For 2018, half of these are associated with DOD, which just completed its first full-scope financial statement audit. The other half are associated with non-DOD agencies, which experienced a 25 percent reduction in material weaknesses, overall, from 27 at the end of fiscal year 2017 to 20 at the end of 2018. These results demonstrate that an increasing number of federal agencies have adopted and maintained disciplined financial reporting operations, implemented effective internal controls over financial reporting, and integrated transaction processing with accounting records. However, weaknesses in financial management practices continue to prevent two of the CFO Act agencies and the government as a whole from achieving an audit opinion.

Table 10: Agency Audit Results: FY 2018

Agency	Audit Opinion	Auditor-Reported Material Weaknesses: Beginning	New	Resolved	Consolidated	Ending
Department of Agriculture (USDA)	Unmodified	2	0	0	0	2
Department of Commerce (DOC)	Unmodified	1	1	0	0	2
Department of Defense (DOD)	Disclaimer	13	8	0	1	20
Department of Education (Education)	Unmodified	0	1	0	0	1
Department of Energy (DOE)	Unmodified	0	0	0	0	0
Department of Health and Human Services (HHS)*	Unmodified	1	0	1	0	0
Department of Homeland Security (DHS)	Unmodified	2	0	0	0	2
Department of Housing & Urban Development (HUD)	Disclaimer	9	0	2	2	5
Department of the Interior (DOI)	Unmodified	0	0	0	0	0
Department of Justice (DOJ)	Unmodified	0	0	0	0	0
Department of Labor (DOL)	Unmodified	1	0	1	0	0
Department of State (State)	Unmodified	0	0	0	0	0
Department of Transportation (DOT)	Unmodified	0	0	0	0	0
Department of the Treasury (Treasury)	Unmodified	1	0	1	0	0
Department of Veterans Affairs (VA)	Unmodified	6	0	1	0	5
Agency for International Development (USAID)	Unmodified	1	0	0	0	1
Environmental Protection Agency (EPA)	Unmodified	2	0	1	0	1
General Services Administration (GSA)	Unmodified	0	0	0	0	0
National Aeronautics & Space Administration (NASA)	Unmodified	0	0	0	0	0
National Science Foundation (NSF)	Unmodified	0	0	0	0	0
Nuclear Regulatory Commission (NRC)	Unmodified	0	0	0	0	0
Office of Personnel Management (OPM)	Unmodified	1	0	0	0	1
Small Business Administration (SBA)	Unmodified	0	0	0	0	0
Social Security Administration (SSA)	Unmodified	0	0	0	0	0
Totals		**40**	**10**	**7**	**3**	**40**

* Unmodified opinion on all statements except SOSI and SCSIA, which received a disclaimer.

[29] The 22 entities include HHS, which received an unmodified ("clean") opinion on all statements except the SOSI and the SCSIA.

Agency Financial Management Systems

Federal agencies improved, but continue to face challenges, in implementing financial management systems that meet federal requirements. The number of CFO Act agencies reporting lack of substantial compliance with one or more of the three Section 803(a) requirements of the *Federal Financial Management Improvement Act* (FFMIA) fell to seven in fiscal year 2018 from eight in fiscal year 2017, and the number of auditors reporting lack of substantial compliance with one or more of the three Section 803(a) FFMIA requirements fell to nine in fiscal year 2018 from ten in fiscal year 2017.

As suggested in the "Sharing Quality Financial Management Services" section above, because of the federal government's size and diversity, its financial management infrastructure consists of both legacy and modernized systems and standardized and customized systems. As the government's fiscal agent, Treasury has systems for collecting and disbursing the government's cash and financing disbursements when necessary, recording and reporting on those collections and disbursements, and reporting on all government revenues, expenses, assets, and liabilities.

The first four sections above[30] summarize what OMB and agencies have been doing and plan to do to improve financial management, including financial management systems. In addition, Treasury has financial management improvements plans that will have governmentwide implications, which are described in its fiscal year 2018 agency financial report (https://home.treasury.gov/about/budget-financial-reporting-planning-and-performance/agency-financial-report) and its fiscal year 2020 budget request and performance plan (https://home.treasury.gov/about/budget-financial-reporting-planning-and-performance/budget-requestannual-performance-plan-and). Also, other agencies have plans to improve their financial management and financial reporting systems described in their financial reports, budget requests, and performance plans. Most significantly, DOD has plans to address its material weaknesses in financial reporting, and is bringing its financial systems into compliance with federal financial management systems requirements, including the FFMIA; all of these plans can be found in the agency financial report (https://comptroller.defense.gov/odcfo/afr2018.aspx). In addition to focusing on financial systems, DOD's audit remediation efforts include issues related to real property, inventory, operating materials and supplies (OM&S), government property in the possession of contractors, information technology, and reconciling the Department's fund balance with Treasury.

Agency Internal Controls

Federal managers are responsible for developing and maintaining effective internal controls. Internal controls help to ensure effective and efficient operations, reliable financial reporting, and compliance with applicable laws and regulations. Safeguarding assets is a goal of each of these three objectives.

In response to major management challenges to achieving their mission and goals, agencies continue to recognize the utility of ERM as a tool to identify, assess, mitigate, manage and prepare for risk. ERM contributes to risk-informed decision-making, encouraging a proactive rather than reactive approach to risk, and fostering a risk-aware culture. It also allows agencies to make better decisions in a resource-constrained environment and focus more on performance than compliances in various areas, including grants management. Under ERM, internal controls are not limited to compliance and financial reporting. Rather, internal controls are a means to address management challenges that cut across multiple agency functions and reduce the risk to an acceptable level. OMB has promoted ERM as a management tool, and the 2016 update to OMB Circular A-123, *Management's Responsibility for Enterprise Risk Management and Internal Control*, explains ERM and the importance of integrating ERM with internal control processes.

OMB Circular No. A-123 implements the requirements of 31 U.S.C. 3512 (c) and (d) (commonly known as the *Federal Managers' Financial Integrity Act)* by providing agencies a framework for assessing and managing risks strategically and tactically. The Circular reflects changes incorporated in GAO's updated *Standards for Internal Control in the Federal Government* and contains multiple appendices that address one or more of the objectives of effective internal control.

- Appendix A provides for agencies to use a risk-based approach to assess, document, test, and report on internal controls over reporting and data integrity;
- Appendix B requires agencies to maintain internal controls that reduce the risk of fraud, waste, and error in government charge card programs;
- Appendix C implements the requirements for effective estimation and remediation of improper payments; and
- Appendix D defines new requirements for determining compliance with the FFMIA that are intended to reduce the cost, risk, and complexity of financial system modernizations.

As noted above, the total number of reported material weaknesses for the CFO Act agencies as of the issuance of this *Financial Report* was 40 for fiscal years 2018 and 2017. Effective internal controls are a challenge at the agency level and at the governmentwide level, with GAO reporting that at the governmentwide level, material weaknesses resulted in ineffective internal control over financial reporting. While progress is being made at many agencies and across the government in identifying and resolving internal control deficiencies, continued work is needed.

[30] These sections are "Results-Oriented Accountability for Grants," "Getting Payments Right," "Leveraging Data as a Strategic Asset," and "Sharing Quality Financial Management Services."

Agency Legal Compliance

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

Efficient Use of Real Property Assets

The federal government owns a significant amount of real property assets worldwide, with a majority of its holdings located in the U.S. These real property holdings include assets that are classified by property type in the Federal Real Property Profile (FRPP) as: land, buildings, and structures. The FRPP defines land as acreage and a building as a constructed asset that is enclosed with walls and a roof that provides space for agencies to perform activities, store materials, or provide space for people to live or work. A structure is defined as any constructed asset that does not meet the building definition above (i.e., fence, tower, parking structure). Further information can be found in the FRPP Data Dictionary available at https://www.gsa.gov/.

Land

The federal government owns roughly 640 million acres, about 28 percent, of the 2.27 billion acres of land in the United States. Four major federal land management agencies administer 610.1 million acres, or 95 percent, of this land. They are the Bureau of Land Management, Fish and Wildlife Service, and National Park Service in the Department of Interior (DOI); and the Forest Service in the U.S. Department of Agriculture (USDA). These lands are managed for many purposes, primarily related to conservation, preservation, recreation, and the extraction of natural resources such as timber, minerals, oil, and gas. Much of the land managed by DOI and USDA is public domain land and is generally intended to be retained by the government for use by future generations. This and other land that qualifies as stewardship land is not valued on the governmentwide Balance Sheet, but is discussed in Note 24 and in agency financial reports. In addition, DOD (excluding the Army Corps of Engineers) administers 11.4 million acres of land in the United States (as of September 30, 2014), consisting of military bases, training ranges, and more. Numerous other agencies administer the remaining federal acreage.

Structures

The government owns structures that are affixed to the land and in many instances cannot easily be physically separated from the land; these include parking structures, power plants, power generating stations, dams, and space exploration structures. These structures are managed by agencies such as DOE, the Army Corps of Engineers, and NASA. The federal government charges fees for the use of some of these structures, which defray some of the costs of the assets. The receipt of such user fees (e.g., sales of electrical power) is recorded as revenue. Structures are generally reflected on the Balance Sheet at cost, net of depreciation, and any environmental or other liabilities associated with structures are reflected on the Balance Sheet in accordance with generally accepted accounting principles.

Buildings

A large portion of the government's real property inventory includes federal owned buildings, with the majority in the custodial care of DOD. In general, agencies hold and manage buildings for administrative use to achieve their mission. The government does not hold buildings or any real property assets for investment or land banking purposes. Buildings owned by the government (and the land associated with the buildings) are generally reflected on the Balance Sheet at cost, net of depreciation. As noted above with structures, any environmental or other liabilities associated with buildings (and the land underneath the buildings) are also reflected on the Balance Sheet in accordance with generally accepted accounting principles. Any buildings (or structures, including the land underneath the buildings or structures) that are not in service are included on the Balance Sheet at net realizable value. After the government identifies buildings or other real property for disposal, it carries out public or negotiated sales, demolitions, public benefit conveyances, and, on occasion, property exchanges.

The federal domestic building inventory is diverse and, as of 2016, contains 252,000 buildings reflecting 2.6 billion square feet of space. The domestic portfolio requires approximately $18.8 billion in annual operation and maintenance expenditures, including approximately $7.3 billion in annual lease costs. The replacement value for the government's 232,000 owned buildings is approximately $1 trillion, and the repair costs are $115 billion. It should be noted, however, that replacement value is not synonymous with fair market value. Within both the owned and leased inventories, there are opportunities to use space more effectively and efficiently. Several initiatives are discussed below.

Transformation Efforts to Optimize the Use of Federal Real Property

On July 12, 2018, OMB issued Memorandum M-18-21 to require all federal entities to designate senior real property officers with the authority to coordinate all aspects of their real property programs and to serve on the Federal Real Property Council (FRPC). The reconstituted FRPC seeks to provide comprehensive governmentwide strategic direction that optimizes the federal real property portfolio to achieve statutory missions while managing costs over the short, mid, and long-term. The FRPC will address current challenges such as the lack of a comprehensive strategic approach to asset management, funding challenges, poor data quality, and the burden of legislative requirements by creating a governance structure to include an Executive Steering Committee (ESC) and working groups. Led by direction from the ESC, the working groups will map their outputs to the FRPC strategic direction to revise the national strategy's policy framework, standardize the business processes and data, and diagnose and address root causes.

The new strategic direction will build on the results of the Reduce the Footprint (RTF) policy, which was issued in 2015 and requires the CFO Act agencies to reduce the size of their federal real property portfolios by improving the use of government-owned buildings and by reducing the amount of leased space and the number of excess and underutilized properties. In addition, under the RTF policy, the CFO Act agencies developed and annually update five-year Real Property Efficiency Plans to identify reductions to their portfolios over a five-year time-period. In fiscal years 2016 and 2017, the CFO Act agencies reduced their fiscal year 2015 RTF baselines (which is the amount of space the CFO Act agencies held/occupied in 2015) by 12.4 million square feet, resulting in an annual estimated cost avoidance of $125 million. Under the RTF policy, the CFO Act agencies will continue to validate square footage and operations and maintenance costs in their Performance and Accountability Reports (PARs) or AFRs to show that they are continuing to reduce their real property footprint over time.

Additionally, governmentwide real property management will be improved by implementation of the *Federal Assets Sale and Transfer Act of 2016* (FASTA) and the *Federal Property Management Reform Act of 2016* (FPMRA). To date, OMB has met, by the required deadlines, all of its responsibilities under FASTA (with a yearly data call to all federal agencies for recommendations to the to-be-established Real Property Reform Board) and under FPMRA (with the establishment of the FRPC and the issuance of a yearly report).

Finally, to support increased reduction targets, the General Services Administration (GSA) and OMB developed a new management tool within the FRPP database that enables the CFO Act agencies to fully analyze the efficiency of their portfolios and to collocate with other agencies. In addition, GSA issued technical guidance in fiscal year 2017 to establish mandatory FRPP data validation and verification requirements that will enhance agencies' abilities to implement data driven decision making when developing their annual RTF reduction targets.

Together with the newly constituted FRPC, OMB will continue to work to optimize its use of federal real property.

Conclusion

The federal government has seen significant progress in financial management since the passage of the CFO Act more than 25 years ago; yet significant challenges remain. The issues that the federal government faces today require financial managers to move beyond the status quo and improve both the efficiency and effectiveness of financial management activities. The steps outlined above build on tools and capabilities that are in place today, and refocus energies on critical and emerging priorities – cutting wasteful spending, improving the efficiency of operations and information technology, and laying a foundation for improved data quality and collaboration.

Additional Information

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

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

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GAO U.S. GOVERNMENT ACCOUNTABILITY OFFICE
441 G St. N.W.
Washington, DC 20548

Comptroller General
of the United States

March 28, 2019

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

To operate as effectively and efficiently as possible, Congress, the administration, and federal managers must have ready access to reliable and complete financial and performance information—both for individual federal entities and for the federal government as a whole. Our report on the U.S. government's consolidated financial statements for fiscal years 2018 and 2017 underscores that much work remains to improve federal financial management and that the federal government continues to face an unsustainable long-term fiscal path.

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

- Certain material weaknesses[1] in internal control over financial reporting and other limitations resulted in conditions that prevented us from expressing an opinion on the accrual-based consolidated financial statements as of and for the fiscal years ended September 30, 2018, and 2017.[2] About 31 percent of the federal government's reported total assets as of September 30, 2018, and approximately 17 percent of the federal government's reported net cost for fiscal year 2018 relate to significant federal entities that received disclaimers of opinion[3] on their fiscal year 2018 financial statements or whose fiscal year 2018 financial information was unaudited.[4]

- Significant uncertainties (discussed in Note 22 to the consolidated financial statements), primarily related to the achievement of projected reductions in Medicare cost growth, prevented us from

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

[2]The accrual-based consolidated financial statements as of and for the fiscal years ended September 30, 2018, and 2017, consist of the (1) Statements of Net Cost, (2) Statements of Operations and Changes in Net Position, (3) Reconciliations of Net Operating Cost and Budget Deficit, (4) Statements of Changes in Cash Balance from Budget and Other Activities, and (5) Balance Sheets, including the related notes to these financial statements. Most revenues are recorded on a modified cash basis.

[3]A disclaimer of opinion arises when the auditor is unable to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion and accordingly does not express an opinion on the financial statements.

[4]The Department of Defense, the Department of Housing and Urban Development, and the Railroad Retirement Board each received a disclaimer of opinion on their respective fiscal year 2018 financial statements. Also, for fiscal year 2018, the financial information for Security Assistance Accounts was unaudited.

expressing an opinion on the sustainability financial statements,[5] which consist of the 2018 and 2017 Statements of Long-Term Fiscal Projections;[6] the 2018, 2017, 2016, 2015, and 2014 Statements of Social Insurance;[7] and the 2018 and 2017 Statements of Changes in Social Insurance Amounts. About $37.7 trillion, or 70 percent, of the reported total present value of future expenditures in excess of future revenue presented in the 2018 Statement of Social Insurance relates to Medicare programs reported in the Department of Health and Human Services' 2018 Statement of Social Insurance, which received a disclaimer of opinion. A material weakness in internal control also prevented us from expressing an opinion on the 2018 and 2017 Statements of Long-Term Fiscal Projections.

- Material weaknesses resulted in ineffective internal control over financial reporting for fiscal year 2018.

- Material weaknesses and other scope limitations, discussed above, limited tests of compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements for fiscal year 2018.

Overall, significant progress has been made in improving federal financial management since key federal financial management reforms were enacted in the 1990s. Twenty-two of the 24 Chief Financial Officers Act of 1990 (CFO Act) agencies received unmodified ("clean") opinions on their respective entities' fiscal year 2018 financial statements, up from six CFO Act agencies that received clean audit opinions for fiscal year 1996.[8] In addition, accounting and financial reporting standards have continued to evolve to provide greater transparency and accountability over the federal government's operations, financial condition, and fiscal outlook.

While the U.S. government's consolidated financial statements provide a high-level summary of the financial position, financial condition, and operating results for the federal government as a whole, the annual preparation and audit of individual federal entity financial statements continue to be critical, among other things, to

- provide individual federal entity accountability to Congress and citizens, including (1) independent assurance, shortly after the end of the fiscal year, of the reliability of reported financial information and (2) association of program costs with related program performance and results;

[5]The sustainability financial statements are based on projections of future receipts and spending, while the accrual-based consolidated financial statements are based on historical information, including the federal government's assets, liabilities, revenue, and net cost.

[6]The 2018 and 2017 Statements of Long-Term Fiscal Projections present, for all the activities of the federal government, the present value of projected receipts and non-interest spending under current policy without change, the relationship of these amounts to projected gross domestic product (GDP), and changes in the present value of projected receipts and non-interest spending from the prior year. These statements also present the fiscal gap, which is the combination of non-interest spending reductions and receipts increases necessary to hold debt held by the public as a share of GDP at the end of the projection period to its value at the beginning of the period. The valuation date for the Statements of Long-Term Fiscal Projections is September 30.

[7]Statements of Social Insurance are presented for the current year and each of the 4 preceding years as required by U.S. generally accepted accounting principles. For the Statements of Social Insurance, the valuation date is January 1 for the Social Security and Medicare programs, October 1 for the Railroad Retirement program (January 1 for 2014 and 2015), and September 30 for the Black Lung program.

[8]The 22 agencies include the Department of Health and Human Services, which received an unmodified ("clean") opinion on all statements except the Statements of Social Insurance and the Statements of Changes in Social Insurance Amounts.

- facilitate reliable, useful, and timely financial management information at the individual federal entity and program levels for effective management decision-making;

- assess the reliability and effectiveness of systems and related internal controls, including identifying control deficiencies that could lead to fraud, waste, and abuse; and

- deliver early warnings of emerging financial management issues.

Further, annual audits along with congressional and executive oversight provide significant incentives for individual federal entities to maintain reliable financial management information and effective systems and controls.

The preparation and audit of individual federal entities' financial statements have also identified numerous deficiencies, leading to corrective actions to strengthen federal entities' internal controls, processes, and systems. For instance, the U.S. Department of Agriculture took corrective actions to address deficiencies identified during its audits that enabled it to obtain an unmodified audit opinion on its full set of financial statements after 2 years of only receiving an opinion on its balance sheet. Also, management of the Department of Housing and Urban Development (HUD) has developed plans to address the multiple material weaknesses identified by HUD's Office of Inspector General.

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

DOD's financial management continues to face long-standing issues. Following years of unsuccessful financial improvement efforts at DOD and consistently being unable to receive an audit opinion on its financial statements, in 2005, the DOD Comptroller established the Financial Improvement and Audit Readiness Directorate to develop, manage, and implement a strategic approach for addressing internal control weaknesses and for achieving auditability, and to integrate those efforts with other improvement activities, such as the department's business systems modernization efforts.

DOD's strategy for achieving a clean opinion on its financial statements and improving overall financial management has shifted from preparing for audit readiness to undergoing financial statement audits and remediating audit findings. In a positive development, DOD underwent an audit of its entity-wide fiscal year 2018 financial statements, which resulted in a disclaimer of opinion issued by the DOD Office of Inspector General (OIG). The disclaimer of opinion was partially based on the disclaimers of opinion for multiple DOD components, including the Army, Navy, Air Force, U.S. Marine Corps, Defense Health Program, Defense Logistics Agency, U.S. Transportation Command, and U.S. Special Operations Command. The DOD OIG also reported 20 material weaknesses in internal control over financial reporting, contributing to its disclaimer of opinion.

DOD has stated that undergoing financial statement audits is valuable for a number of reasons, such as audit remediation efforts, improvements in its operations and readiness, and in the reliability of financial management information used in decision-making. For example, the Army created an application for storing and analyzing its financial data for audit, which also provided Army management with information used to determine funding priorities. Also, the Navy enhanced internal controls over its obligation management process, which resulted in identifying funds available for important activities, such as over $4 million for ship repair costs. In several instances, auditors found inaccurate inventory records that could affect readiness. For example, auditors found that certain Blackhawk helicopter parts included in inventory records were in fact unavailable or unusable.

DOD has acknowledged that achieving a clean audit opinion will take time. However, it stated that over the next several years, the resolution of audit findings will serve as an objective measure of progress toward that goal. DOD will need to develop and effectively monitor corrective action plans to appropriately address audit findings in a timely manner. DOD recently developed a centralized database to track the audit findings, recommendations, and related corrective action plans.

Various efforts are also under way to address the other two major impediments to an audit of the consolidated financial statements. For example, during fiscal year 2018, the Department of the Treasury (Treasury) continued to actively work with significant federal entities[9] to resolve differences in intragovernmental activity and balances between federal entities through its quarterly scorecard process.[10] This process highlights differences needing the entities' attention, identifies differences that need to be resolved through a formal dispute resolution process,[11] and reinforces the entities' responsibilities to resolve intragovernmental differences. Treasury also made significant progress in developing and implementing procedures to improve the accounting for and reporting of General Fund of the U.S. Government (General Fund) transactions and balances,[12] and working to resolve significant differences between the General Fund and federal entity trading partners.

In recent years, Treasury's corrective actions have included improving systems used for compiling the consolidated financial statements, enhancing guidance for collecting data from component entities, and implementing procedures to address certain internal control deficiencies detailed in our previously issued management report.[13] Treasury also continued to develop its process for preparing the Reconciliation Statements[14] by documenting its rationale for the reconciling items currently presented on the Reconciliation Statements. In addition to continued leadership by Treasury and the Office of Management and Budget (OMB), federal entities' strong and sustained commitment is critical to fully address these issues.

[9]The Office of Management and Budget and Treasury have identified 40 federal entities that are significant to the U.S. government's fiscal year 2018 consolidated financial statements, including the 24 CFO Act agencies. See app. A of the *Fiscal Year 2018 Financial Report of the United States Government* for a list of the 40 entities.

[10]For each quarter, Treasury produces a scorecard for each significant entity, as well as any other component entity reporting significant intragovernmental balances or differences, that reports various aspects of the entity's intragovernmental differences with its trading partners, including the composition of the differences by trading partner and category. Pursuant to Treasury guidance, entities are expected to resolve, with their respective trading partners, the differences identified in their scorecards.

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

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

[13]GAO, *Management Report: Continued Improvements Needed in Controls over the Processes Used to Prepare the U.S. Consolidated Financial Statements*, GAO-18-540 (Washington, D.C.: July 16, 2018).

[14]The Reconciliations of Net Operating Cost and Budget Deficit and Statements of Changes in Cash Balance from Budget and Other Activities (Reconciliation Statements) reconcile (1) the accrual-based net operating cost to the primarily cash-based budget deficit and (2) the budget deficit to changes in cash balances.

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

In addition to the material weaknesses referred to above, we identified three other material weaknesses. These are the federal government's inability to (1) determine the full extent to which improper payments occur and reasonably assure that appropriate actions are taken to reduce them, (2) identify and resolve information security control deficiencies and manage information security risks on an ongoing basis, and (3) effectively implement internal controls over estimating the cost of credit programs and determining the value of loans receivable and loan guarantee liabilities. Our audit report presents additional details concerning these material weaknesses and their effect on the accrual-based consolidated financial statements and managing federal government operations. Until the problems outlined in our audit report are adequately addressed, they will continue to have adverse implications for the federal government and the American people.

Resolving the problems outlined in our audit report is of utmost importance given the federal government's reported fiscal path. The 2018 Statement of Long-Term Fiscal Projections and related information in Note 23 and in the unaudited Required Supplementary Information section of the *Fiscal Year 2018 Financial Report of the United States Government* (*2018 Financial Report*) show that absent policy changes, the federal government continues to face an unsustainable long-term fiscal path. GAO and the Congressional Budget Office (CBO) also prepare long-term federal fiscal simulations, using different sets of assumptions, which continue to show federal debt held by the public rising as a share of gross domestic product (GDP) in the long term.[16] This situation—in which debt grows faster than GDP—means the current federal fiscal path is unsustainable.

GAO, CBO, and the *2018 Financial Report* all project that debt held by the public as a share of GDP will surpass its historical high (106 percent in 1946) within the next 13 to 20 years. Health care spending is a key driver of spending in the long-term projections. Eventually, however, spending on net interest (primarily interest on debt held by the public) is projected to grow such that over the long term it surpasses Social Security and becomes the largest category of spending in both the *2018 Financial Report* and GAO's simulations.[17] Reliable and complete financial information for federal entities will be needed for making policy changes that effectively address the unsustainable long-term fiscal path.

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[15]See GAO-18-540. In addition, see GAO, *DOD Financial Management*, accessed March 20, 2019, https://www.gao.gov/highrisk/dod_financial_management/why_did_study. Further, other auditors have made recommendations to DOD for improving its financial management.

[16]For more information on GAO's simulations, see GAO, *America's Fiscal Future: Fiscal Forecast*, accessed on March 20, 2019, https://www.gao.gov/americas_fiscal_future?t=fiscal_forecast. For more information on CBO's simulations, see Congressional Budget Office, *The 2018 Long-Term Budget Outlook* (Washington, D.C.: June 26, 2018).

[17]CBO's projections in its 2018 long-term budget outlook report also show net interest growing as a percentage of total spending. However, since CBO's 2018 extended baseline projections only go out to 2048, the cost of net interest does not quite overtake other categories in the projection period.

GAO plans to issue its annual report on the fiscal health of the federal government in the coming weeks.[18]

In taking action to change the federal government's long-term fiscal path, it will be important for Congress to consider alternative approaches for managing the level of debt. As currently structured, the debt limit—a legal limit on the total amount of federal debt that can be outstanding at one time[19]—does not restrict Congress's ability to enact spending and revenue legislation that affects the level of federal debt, nor does it otherwise constrain fiscal policy. Rather, the debt limit is an after-the-fact measure; the spending and tax laws that result in debt have already been enacted. The debt limit restricts Treasury's authority to borrow to finance the decisions already enacted by Congress and the President.

One cannot overstate the importance of preserving the confidence that investors have that debt backed by the full faith and credit of the United States will be honored. Failure to increase (or suspend) the debt limit in a timely manner could have serious negative consequences for the Treasury market and increase borrowing costs. The Bipartisan Budget Act of 2018 temporarily suspended the debt limit from February 9, 2018, through March 1, 2019.[20] On Monday, March 4, 2019, Treasury began to take extraordinary actions to continue funding government activities. It will continue taking these actions until the debt limit is raised or suspended.[21] With these extraordinary actions in place, CBO estimates that Treasury will have sufficient cash to make its usual payments until late into fiscal year 2019.

As we have previously reported, delays in raising the debt limit can create uncertainty in the Treasury market.[22] To avoid such uncertainty and the disruption to the Treasury market that it creates, as well as to help inform the fiscal policy debate in a timely way, we have suggested that Congress should consider ways to better link decisions about the debt limit with decisions about spending and revenue at the time those decisions are made.[23] We identified three potential approaches for Congress to consider regarding delegating borrowing authority:

- Option 1: Link action on the debt limit to the budget resolution.
- Option 2: Provide the administration with the authority to propose a change in the debt limit that would take effect absent enactment of a joint resolution of disapproval within a specified time frame.
- Option 3: Delegate broad authority to the administration to borrow as necessary to fund enacted laws.

[18]GAO, *The Nation's Fiscal Health: Action Is Needed to Address the Federal Government's Fiscal Future*, GAO-18-299SP (Washington, D.C.: June 21, 2018).

[19]The debt limit is codified at 31 U.S.C. § 3101(b), as amended, and applies to federal debt issued pursuant to the authority of 31 U.S.C. chapter 31. A very small amount of total federal debt is not subject to the debt limit. This amount primarily comprises unamortized discounts on Treasury bills and Zero Coupon Treasury bonds; debt securities issued by agencies other than Treasury, such as the Tennessee Valley Authority; and debt securities issued by the Federal Financing Bank.

[20]Section 30301 of Division C of the Bipartisan Budget Act of 2018, Pub. L. No. 115-123, div. C, tit. III, § 30301, 132 Stat. 64, 132 (Feb. 9, 2018), temporarily suspended the debt limit.

[21]Extraordinary actions are actions that Treasury takes as it nears the debt limit to avoid exceeding that limit. These actions are not part of Treasury's normal cash and debt management operations.

[22]GAO, *Debt Limit: Analysis of 2011-2012 Actions Taken and Effect of Delayed Increase on Borrowing Costs*, GAO-12-701 (Washington, D.C.: July 23, 2012), and *Debt Limit: Delays Create Debt Management Challenges and Increase Uncertainty in the Treasury Market*, GAO-11-203 (Washington, D.C.: Feb. 22, 2011).

[23]GAO, *Debt Limit: Market Response to Recent Impasses Underscores Need to Consider Alternative Approaches*, GAO-15-476 (Washington, D.C.: July 9, 2015).

All of these options maintain congressional control and oversight over federal borrowing.

Further, there are financial and other risks that could affect the federal government's financial position and condition and its financial management in the future. Financial risk factors that could affect the federal government's financial condition in the future include the following:

- The Pension Benefit Guaranty Corporation's (PBGC) financial future is uncertain because of long-term challenges related to its funding and governance structure. PBGC's liabilities exceeded its assets by about $51 billion as of the end of fiscal year 2018—an increase of about $16 billion from the end of fiscal year 2013. PBGC estimated that its exposure to potential further losses for underfunded plans in both the single and multiemployer programs was nearly $185 billion.[24]

- Federal support of the housing finance market remains significant even though the market has largely recovered since the 2007 to 2009 financial crisis. In 2008, the federal government placed the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac) under conservatorship and entered into preferred stock purchase agreements with these government-sponsored enterprises (GSE) to help ensure their financial stability. These agreements could affect the federal government's financial condition. At the end of fiscal year 2018, the federal government reported about $113 billion of investments in the GSEs, which is net of about $91 billion in valuation losses. The GSEs paid Treasury cash dividends of $9.9 billion and $25.3 billion during fiscal years 2018 and 2017, respectively. The reported maximum remaining contractual commitment to the GSEs, if needed, is $254.1 billion. The ultimate role of the GSEs could affect the federal government's financial position and the financial condition of federal entities, including the Federal Housing Administration (FHA), which in the past expanded its lending role in distressed housing and mortgage markets. Specifically, as of the end of fiscal year 2018, FHA's insured portfolio exceeded $1.2 trillion. The Government National Mortgage Association (Ginnie Mae) guarantees the performance of almost $2 trillion in securities backed by federally insured mortgages—of which $1.2 trillion were insured by FHA and $0.8 trillion by other federal entities, such as the Department of Veterans Affairs.

  We have reported on the need for Congress to consider legislation making changes to the future federal role in housing finance that addresses the structure of the GSEs; establishes clear, specific, and prioritized goals; and considers all relevant federal entities, such as FHA and Ginnie Mae.[25]

- The U.S. Postal Service (USPS) continues to be in poor financial condition. USPS cannot fund its current level of services and meet its financial obligations from its existing revenues. The fiscal year 2018 net loss of $3.9 billion marked its 11th consecutive year of net losses—totaling $69 billion. In addition, USPS has missed $48.2 billion in required payments for postal retiree health and pension benefits through fiscal year 2018, including $42.6 billion in missed payments for retiree health benefits since fiscal year 2010 and $5.6 billion in missed payments for pension benefits since fiscal year 2014. USPS has stated that it missed these payments to minimize the risk of running out of

[24]The Bipartisan Budget Act of 2018 established the Joint Select Committee on Solvency of Multiemployer Pension Plans, which was tasked with voting on a report that was to include any findings, conclusions, and recommendations (as well as proposed legislative language to carry out such recommendations) to significantly improve the solvency of multiemployer pension plans and PBGC by November 30, 2018. Pub. L. No. 115-123, div. C, tit. IV, subtit. A, § 30422, 132 Stat. 64, 133-37 (Feb. 9, 2018). However, even though the joint committee did not vote on a report and was statutorily set to terminate no later than December 31, 2018, its co-chairmen released a statement committing to working to solve the multiemployer pension crisis past the November 30 deadline.

[25]GAO, *Housing Finance: Prolonged Conservatorships of Fannie Mae and Freddie Mac Prompt Need for Reform*, GAO-19-239 (Washington, D.C.: Jan. 18, 2019).

cash, citing its precarious financial condition and the need to cover current and anticipated costs and any contingencies.[26]

- Some government insurance programs have not collected sufficient premiums or do not have sufficient dedicated resources to cover expected costs without borrowing from Treasury.[27] For example, as of September 2018, the Federal Emergency Management Agency (FEMA), which administers the National Flood Insurance Program, owed $20.5 billion to Treasury for money borrowed to pay claims and other expenses. We have reported that FEMA was unlikely to collect enough in premiums in the future to repay this debt.[28] The amount owed is net of $16 billion of debt that was canceled in October 2017 by the Additional Supplemental Appropriations for Disaster Relief Requirements Act, 2017.[29]

- Also, large events, such as natural disasters, pandemics, cyberattacks, military engagements, or economic crises, are not considered in the Statements of Long-Term Fiscal Projections. To the extent that such large events occur, the actual future spending may be greater than spending in these projections.

Every 2 years, GAO provides Congress with an update on its High-Risk Series, which highlights federal entities and program areas that are at high risk because of their vulnerabilities to fraud, waste, abuse, and mismanagement or are most in need of broad reform. We issued our most recently updated High-Risk Series on March 6, 2019.[30] GAO's High-Risk Series includes most of the above-noted issues, such as DOD financial management, ensuring the cybersecurity of the nation, the PBGC insurance programs, resolving the federal role in housing finance, USPS financial viability, and the National Flood Insurance Program.

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

Our audit report begins on page 226. Our guide, *Understanding the Financial Report of the United States Government*, is intended to help those who seek to obtain a better understanding of the financial report and is available on GAO's website at http://www.gao.gov.[31]

[26]GAO, *High-Risk Series: Substantial Efforts Needed to Achieve Greater Progress on High-Risk Areas*, GAO-19-157SP (Washington, D.C.: Mar. 6, 2019).

[27]We have suggested an alternative way to record insurance commitments in the budget such that the federal government's commitment would be more fully recognized. See GAO, *Fiscal Exposures: Improving Cost Recognition in the Federal Budget*, GAO-14-28 (Washington, D.C.: Oct. 29, 2013).

[28]GAO, *Flood Insurance: Comprehensive Reform Could Improve Solvency and Enhance Resilience*, GAO-17-425 (Washington, D.C.: Apr. 27, 2017).

[29]Additional Supplemental Appropriations for Disaster Relief Requirements Act, 2017, Pub. L. No. 115-72, § 308, 131 Stat. 1224, 1228-29 (Oct. 26, 2017).

[30]GAO-19-157SP.

[31]GAO, *Understanding the Financial Report of the United States Government*, GAO-18-239SP (Washington, D.C.: February 2018).

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

Gene L. Dodaro
Comptroller General
of the United States

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

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Financial Statements of the United States Government for the Fiscal Years Ended September 30, 2018, and 2017

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

ACCRUAL-BASED FINANCIAL STATEMENTS

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

Statements of Net Cost

These statements present the net cost of the government operations for fiscal years 2018 and 2017, including the operations related to funds from dedicated collections. Costs and earned revenues are categorized on the Statement of Net Cost by significant entity, providing greater accountability by showing the relationship of the entities' net cost to the governmentwide net cost. Costs and earned revenues are presented in this *Financial Report* on an accrual basis, while the budget presents outlays and receipts, generally on a cash basis. The focus of the budget of the U.S. is by entity. Budgets are prepared, defended, and monitored by entity. In reporting by entity, we are assisting the external users in assessing the budget integrity, operating performance, stewardship, and systems and controls of the government.

The Statements of Net Cost contain the following four components:

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

Individual entity net cost amounts will differ from the entity's financial statements primarily because of reallocations completed at the governmentwide level which are listed below.

- Employee benefit costs.
- Intragovernmental eliminations, as adjusted for buy/sell costs and related revenues.
- Imputed costs.

Because of its specific function, most of the employee benefit costs originally associated with the OPM have been reallocated to the user entities for governmentwide reporting purposes. The remaining costs for OPM on the Statements of Net Cost are the administrative operating costs, the expenses from prior costs from health and pension plan amendments, and the actuarial gains and losses, if applicable.

GSA is the primary provider of goods and services to federal entities. GSA's net cost is adjusted for its intragovernmental buy/sell costs and related revenues. The remaining costs for GSA on the Statements of Net Cost are administrative operating costs. With regard to intragovernmental buy/sell costs and related revenues, the amounts recognized by each entity are added to, and subtracted from, respectively, the individual entity non-federal net cost amounts.

In addition, the intragovernmental imputed costs recognized for the receipt of goods and services, financed in whole or part by the providing entities, are added to the individual entity non-federal net cost amounts. The most significant types of imputed costs that are recorded relate to post-retirement and health benefits, FECA, and the Treasury Judgment Fund. The consolidated Statements of Net Cost is intended to show the full cost for each entity, therefore, the amount of these imputed costs are added back to the reporting entities' gross cost line item and subtracted from the applicable administering entities' gross cost line item. These imputed costs have a net effect of zero on the Statements of Net Cost in the *Financial Report*.

The interest on securities issued by the Treasury and held by the public is reported on Treasury's financial statements, but, because of its importance and the dollar amounts involved, it is reported separately in these statements.

Statements of Operations and Changes in Net Position

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

Revenue

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

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

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

Other taxes and receipts include FRBs earnings, tax related fines, penalties and interest, and railroad retirement taxes.

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

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

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

Net Cost of Government Operations

The net cost of government operations—gross cost (including gains/losses from changes in assumptions) less earned revenue—flows through from the Statements of Net Cost. The net cost and intragovernmental net cost associated with funds from dedicated collections activities are separately reported.

Intragovernmental Transfers

Intragovernmental transfers reflect budgetary and other financing sources for funds from dedicated collections, excluding financing sources related to non-exchange revenues, intragovernmental interest, and miscellaneous revenues. These intragovernmental transfers include appropriations, transfers, and other financing sources. These amounts are labeled as “other changes in fund balance” in Note 20—Funds from Dedicated Collections. Some transfers reflect amounts required by statute to be transferred from the General Fund of the U.S. Government (General Fund) to funds from dedicated collections. For Supplementary Medical Insurance (SMI), transfers from the General Fund financed 72 percent and 70 percent of 2018 program costs to Part B and D, respectively.

Unmatched Transactions and Balances

Unmatched transactions and balances are adjustments needed to bring the change in net position into balance due primarily to unreconciled intragovernmental differences. See Note 1.R—Unmatched Transactions and Balances for detailed information.

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

Net Operating Cost

The net operating cost equals revenue less net cost of government operations (that flows from the Statement of Net Cost) adjusted by unmatched transactions and balances. See Note 1.R—Unmatched Transactions and Balances for detailed information.

Net Position, Beginning of Period

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

Adjustments to beginning net position may include corrections of material errors or changes in accounting principles. See Note 1.S—Adjustments to Beginning Net Position for detailed information.

Net Position, End of Period

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

Reconciliations of Net Operating Cost and Budget Deficit

These statements reconcile the results of operations (net operating cost) on the Statements of Operations and Changes in Net Position to the budget deficit (result of outlays exceeding receipts during a particular fiscal year). The premise of the reconciliation is that the accrual and budgetary accounting basis share transaction data.

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

Some presentations of the budget deficit make the distinction between on-budget and off-budget totals. On-budget totals reflect the transactions of all government entities, except those excluded from the budget by law. Off-budget totals reflect the transactions of government entities that are excluded from the on-budget totals by law. Under current law, the off-budget totals include the Social Security trust funds and the United States Postal Service (USPS). The budget deficit, as presented in the *Financial Report*, combines the on-budget and off-budget totals to derive consolidated totals for federal activity.

In fiscal year 2018, additional lines were included in the presentation of these statements to provide a further breakdown of certain categories of transactions.

Components of Net Operating Cost Not Part of the Budget Deficit

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

Components of the Budget Deficit Not Part of Net Operating Cost

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

Statements of Changes in Cash Balance from Budget and Other Activities

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

These statements reconcile the budget deficit to the change in cash and other monetary assets during the fiscal year. They also serve to explain how the budget deficits were financed. These statements show the adjustments for non-cash outlays included in the budget, and items affecting the cash balance not included in the budget, to explain the change in cash and other monetary assets.

The budget deficit is primarily financed through borrowings from the public. When receipts exceed outlays, the difference is a surplus. The budget treats borrowing and debt repayment as a means of financing, not as receipts and outlays. The budget records outlays for the interest on the public issues of Treasury debt securities as the interest accrues, not when the cash is paid.

Non-cash flow amounts in the budget related to loan financing account activity also reflect intragovernmental transactions such as interest expense paid or interest revenue received from Treasury, agency year-end credit reform subsidy reestimates, and the receipt of subsidy expense from program accounts. Cash flow from non-budget activities related to loan financing account activity includes all cash flows to and from the public, including direct loan disbursements/default payments to lenders, fees collected, principal and interest repayments, collections on defaulted guarantee loans, and sale proceeds of foreclosed property. The budget totals exclude the transactions of the financing accounts because they are not a cost to the government. However, since loan financing accounts record all credit cash flows to and from the public, they affect the means of financing a budget deficit.

In fiscal year 2018, additional lines were included in the presentation of these statements to provide a further breakdown of certain categories of transactions.

Balance Sheets

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

Assets

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

Liabilities and Net Position

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

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

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

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

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

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

SUSTAINABILITY FINANCIAL STATEMENTS

The sustainability financial statements are comprised of the Statements of Long-Term Fiscal Projections, covering all federal government programs, and the Statements of Social Insurance and the Statement of Changes in Social Insurance Amounts, covering social insurance programs (Social Security, Medicare, Railroad Retirement, and Black Lung programs). The sustainability financial statements are designed to illustrate the relationship between projected receipts and expenditures if current policy is continued over a 75 year time horizon.[1] In preparing the sustainability financial statements, management selects assumptions and data that it believes provide a reasonable basis to illustrate whether current policy is sustainable. Current policy is based on current law, but includes several adjustments. In the Statement of Long-Term Fiscal Projections, notable adjustments to current law are: (1) projected spending, receipts, and borrowing levels assume raising or suspending the current statutory limit on Federal debt, (2) continued discretionary appropriations are assumed throughout the projections period, (3) scheduled Social Security and Medicare Part A benefit payments are assumed to occur beyond the projected point of trust fund depletion, (4) discretionary spending after 2019 is assumed to not be limited by caps established by the BCA, (5) many mandatory programs with expiration dates prior to the end of the 75-year projection period are assumed to be reauthorized, and (6) tax changes under the TCJA of 2017 are assumed to continue beyond 2025. In the Statement of Social Insurance, the one adjustment to current law is that scheduled Social Security and Medicare part A benefit payments are assumed to occur beyond the projected point of trust fund depletions. Assumptions underlying such sustainability information do not consider changes in policy or all potential future events that could affect future income, future expenditures, and, hence, sustainability. The projections do not reflect any adverse economic consequences resulting from continuously rising debt levels. A large number of factors affect the sustainability financial statements and future events and circumstances cannot be estimated with certainty. Therefore, even if current policy is continued, there will be differences between the estimates in the sustainability financial statements and actual results, and those differences may be material. The unaudited Required Supplementary Information section of this report includes present value projections using different assumptions to illustrate the sensitivity of the sustainability financial statements to changes in certain assumptions. The sustainability financial statements are intended to help citizens understand current policy and the importance and magnitude of policy reforms necessary to make it sustainable.

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

Statements of Long-Term Fiscal Projections

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

The Statements of Long-Term Fiscal Projections display the present value of 75-year projections by major category of the federal government's receipts and non-interest spending. These projections show the extent to which future receipts of the government exceed or fall short of the government's non-interest spending. The projections are presented both in terms of present value dollars and in terms of present value dollars as a percent of present value GDP. The projections are on the basis of policies currently in place and are neither forecasts nor predictions. These projections are consistent with the projections for Social Security and Medicare presented in the Statements of Social Insurance and are based on the same economic and demographic assumptions as underlie the Statements of Social Insurance. These statements also display the fiscal gap, which is a summary measure of the change in receipts or non-interest spending necessary to hold the ratio of debt held by the public to GDP at the end of the projection period to its value at the beginning of the period. Note 23—Long-Term Fiscal Projections, further explains the methods used to prepare these projections and provides additional information. Unaudited

[1] With the exception of the Black Lung program, which has a rolling 25-year projection period that begins on the September 30 valuation date each year.

required supplementary information further assesses the sustainability of current fiscal policy and provides results based on alternative assumptions to those used in the basic statement.

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

Statements of Social Insurance and Changes in Social Insurance Amounts

The Statements of Social Insurance provide estimates of the status of the most significant social insurance programs: Social Security, Medicare, Railroad Retirement, and Black Lung[2]. They are administered by SSA, HHS, the Railroad Retirement Board (RRB), and DOL, respectively. The SSA and HHS projections are based on the economic and demographic assumptions representing the Trustees' reasonable estimates of likely future economic and demographic conditions, as set forth in the applicable Social Security and Medicare Trustees' reports as well as in the agency financial reports of HHS and SSA. RRB's projections are based on assumptions from the *27th Valuation on the Assets and Liabilities Under the Railroad Retirement Acts of December 31, 2016* with Technical Supplement, which was published in September 2018, as well as in RRB's performance and accountability report. DOL's (Black Lung) projections are based on assumptions included in its agency financial report. The SOSI projections, with one exception related to Medicare Part A and OASDI, are based on current law; that is, they assume that scheduled social insurance benefit payments would continue after related trust funds are projected to be depleted, contrary to current law. By law, once assets are depleted, expenditures cannot be made except to the extent covered by ongoing tax receipts and other trust fund income.

Note 22—Social Insurance describes the social insurance programs, reports long-range estimates that can be used to assess the financial condition of the programs, and explains some of the factors that impact the various programs. The Statements of Changes in Social Insurance Amounts show two reconciliations: (1) change from the period beginning on January 1, 2017 to the period beginning on January 1, 2018; and (2) change from the period beginning on January 1, 2016 to the period beginning on January 1, 2017.

[2] In relation to the amounts presented in the Statements of Social Insurance and Changes in Social Insurance Amounts, the combined Railroad Retirement and Black Lung programs account for less than a quarter of one percent of the statement totals, and therefore, are not material from the consolidated perspective.

United States Government
Statement of Net Cost
for the Year Ended September 30, 2018

(In billions of dollars)	Gross Cost	Earned Revenue	Subtotal	(Gain)/Loss from Changes in Assumptions	Net Cost
Department of Health and Human Services	1,252.6	110.5	1,142.1	0.4	1,142.5
Social Security Administration	1,038.5	0.2	1,038.3	-	1,038.3
Department of Defense	719.8	38.2	681.6	16.8	698.4
Interest on Treasury Securities Held by the Public	357.3	-	357.3	-	357.3
Department of Veterans Affairs	272.5	4.8	267.7	79.2	346.9
Department of Energy	147.0	6.1	140.9	-	140.9
Department of Agriculture	137.0	6.6	130.4	-	130.4
Department of the Treasury	150.5	21.9	128.6	-	128.6
Office of Personnel Management	101.3	23.4	77.9	26.2	104.1
Department of Transportation	79.0	1.1	77.9	-	77.9
Department of Homeland Security	78.3	14.8	63.5	1.1	64.6
Department of Education	79.2	31.4	47.8	-	47.8
Department of Housing and Urban Development	43.3	1.8	41.5	-	41.5
Department of Labor	41.1	-	41.1	-	41.1
Security Assistance Accounts	37.9	-	37.9	-	37.9
Department of Justice	35.4	1.9	33.5	-	33.5
Department of State	32.3	4.8	27.5	1.5	29.0
National Aeronautics and Space Administration	20.3	0.2	20.1	-	20.1
Department of the Interior	20.4	2.9	17.5	-	17.5
U.S. Agency for International Development	13.1	-	13.1	-	13.1
Railroad Retirement Board	13.1	-	13.1	-	13.1
Federal Communications Commission	10.8	0.4	10.4	-	10.4
Department of Commerce	11.8	3.6	8.2	-	8.2
Environmental Protection Agency	8.3	0.4	7.9	-	7.9
National Science Foundation	7.3	-	7.3	-	7.3
U.S. Postal Service	71.4	69.7	1.7	-	1.7
Smithsonian Institution	1.5	0.5	1.0	-	1.0
Millennium Challenge Corporation	0.8	-	0.8	-	0.8
Small Business Administration	0.7	0.3	0.4	-	0.4
National Credit Union Administration	0.9	0.6	0.3	-	0.3
U.S. Nuclear Regulatory Commission	0.9	0.7	0.2	-	0.2
Farm Credit System Insurance Corporation	0.2	0.2	-	-	-
Overseas Private Investment Corporation	-	0.1	(0.1)	-	(0.1)
Export-Import Bank of the U.S.	-	0.5	(0.5)	-	(0.5)
Securities and Exchange Commission	1.8	2.3	(0.5)	-	(0.5)
General Services Administration	-	0.8	(0.8)	-	(0.8)
Tennessee Valley Authority	9.9	11.2	(1.3)	-	(1.3)
National Railroad Retirement Investment Trust	0.1	1.9	(1.8)	-	(1.8)
Federal Deposit Insurance Corporation	1.3	10.8	(9.5)	-	(9.5)
Pension Benefit Guaranty Corporation	(7.8)	16.7	(24.5)	-	(24.5)
All other entities	18.7	1.5	17.2	-	17.2
Total	4,808.5	392.8	4,415.7	125.2	4,540.9

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

United States Government
Statement of Net Cost
for the Year Ended September 30, 2017 (Restated)

(In billions of dollars)	Gross Cost	Earned Revenue	Subtotal	(Gain)/Loss from Changes in Assumptions	Net Cost
Department of Health and Human Services	1,186.8	101.1	1,085.7	0.4	1,086.1
Social Security Administration	999.1	0.3	998.8	-	998.8
Department of Defense	718.7	77.4	641.3	24.1	665.4
Interest on Treasury Securities Held by the Public	296.3	-	296.3	-	296.3
Department of Veterans Affairs	254.8	4.8	250.0	229.7	479.7
Department of Energy	46.9	5.6	41.3	-	41.3
Department of Agriculture	142.9	8.1	134.8	-	134.8
Department of the Treasury	179.5	37.9	141.6	-	141.6
Office of Personnel Management	90.1	22.3	67.8	102.5	170.3
Department of Transportation	79.6	0.9	78.7	-	78.7
Department of Homeland Security	77.3	12.3	65.0	(0.5)	64.5
Department of Education	84.4	30.6	53.8	-	53.8
Department of Housing and Urban Development	69.1	1.7	67.4	-	67.4
Department of Labor	43.5	-	43.5	-	43.5
Security Assistance Accounts	36.7	-	36.7	-	36.7
Department of Justice	34.2	1.6	32.6	-	32.6
Department of State	31.3	4.8	26.5	0.3	26.8
National Aeronautics and Space Administration	19.6	0.2	19.4	-	19.4
Department of the Interior	20.2	2.7	17.5	-	17.5
U.S. Agency for International Development	13.2	-	13.2	-	13.2
* Railroad Retirement Board	13.0	3.8	9.2	-	9.2
Federal Communications Commission	20.7	0.4	20.3	-	20.3
Department of Commerce	12.9	3.3	9.6	-	9.6
Environmental Protection Agency	8.8	0.4	8.4	-	8.4
National Science Foundation	7.1	-	7.1	-	7.1
U.S. Postal Service	71.9	68.7	3.2	-	3.2
Smithsonian Institution	0.9	-	0.9	-	0.9
Millennium Challenge Corporation	0.7	-	0.7	-	0.7
Small Business Administration	0.1	0.3	(0.2)	-	(0.2)
National Credit Union Administration	(0.1)	0.7	(0.8)	-	(0.8)
U.S. Nuclear Regulatory Commission	0.9	0.8	0.1	-	0.1
Farm Credit System Insurance Corporation	-	0.4	(0.4)	-	(0.4)
Overseas Private Investment Corporation	-	0.1	(0.1)	-	(0.1)
Export-Import Bank of the U.S.	0.4	1.2	(0.8)	-	(0.8)
Securities and Exchange Commission	1.9	2.1	(0.2)	-	(0.2)
General Services Administration	0.2	0.6	(0.4)	-	(0.4)
Tennessee Valley Authority	9.9	10.7	(0.8)	-	(0.8)
Federal Deposit Insurance Corporation	1.5	10.6	(9.1)	-	(9.1)
Pension Benefit Guaranty Corporation	9.8	14.1	(4.3)	-	(4.3)
All other entities	21.4	1.4	20.0	-	20.0
Total	4,606.2	431.9	4,174.3	356.5	4,530.8

* Includes amounts from National Railroad Retirement Investment Trust (NRRIT) in 2017. In 2018, NRRIT amounts are reported separately.

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

United States Government
Statement of Operations and Changes in Net Position
for the Year Ended September 30, 2018

(In billions of dollars)	Funds other than those from Dedicated Collections (Combined)	Funds from Dedicated Collections (Note 20) (Combined)	Eliminations	Consolidated
		2018		
Revenue (Note 17):				
Individual income tax and tax withholdings	1,655.5	1,137.7	-	2,793.2
Corporate income taxes	208.9	-	-	208.9
Excise taxes	31.9	64.9	-	96.8
Unemployment taxes	-	43.2	-	43.2
Customs duties	41.5	-	-	41.5
Estate and gift taxes	23.0	-	-	23.0
Other taxes and receipts	133.4	30.7	-	164.1
Miscellaneous earned revenues	9.2	4.4	-	13.6
Intragovernmental interest	-	98.5	(98.5)	-
Total Revenue	2,103.4	1,379.4	(98.5)	3,384.3
Net Cost of Government Operations:				
Net cost	2,838.4	1,702.5	-	4,540.9
Intragovernmental net cost	(9.8)	9.8	-	-
Intragovernmental interest	98.5	-	(98.5)	-
Total net cost	2,927.1	1,712.3	(98.5)	4,540.9
Intragovernmental transfers	(372.8)	372.8	-	-
Unmatched transactions and balances (Note 1.R)	(2.4)	-	-	(2.4)
Net operating (cost)/revenue	(1,198.9)	39.9	-	(1,159.0)
Net position, beginning of period	(23,781.4)	3,419.5	-	(20,361.9)
Adjustments to beginning net position (Note 1.S)	(2.5)	2.6	-	0.1
Net operating (cost)/revenue	(1,198.9)	39.9	-	(1,159.0)
Net position, end of period	(24,982.8)	3,462.0	-	(21,520.8)

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

United States Government
Statement of Operations and Changes in Net Position
for the Year Ended September 30, 2017 (Restated)

(In billions of dollars)	Funds other than those from Dedicated Collections (Combined)	Funds from Dedicated Collections (Note 20) (Combined)	Eliminations	Consolidated
		2017		
Revenue (Note 17):				
Individual income tax and tax withholdings	1,560.1	1,127.8	-	2,687.9
Corporate income taxes	299.1	-	-	299.1
Excise taxes	24.7	62.6	-	87.3
Unemployment taxes	-	44.1	-	44.1
Customs duties	33.2	-	-	33.2
Estate and gift taxes	22.8	-	-	22.8
Other taxes and receipts	135.9	36.2	-	172.1
Miscellaneous earned revenues	24.0	4.1	-	28.1
Intragovernmental interest	-	99.6	(99.6)	-
Total Revenue	2,099.8	1,374.4	(99.6)	3,374.6
Net Cost of Government Operations:				
Net cost	2,882.7	1,648.1	-	4,530.8
Intragovernmental net cost	(8.5)	8.5	-	-
Intragovernmental interest	99.6	-	(99.6)	-
Total net cost	2,973.8	1,656.6	(99.6)	4,530.8
Intragovernmental transfers	(327.2)	327.2	-	-
Unmatched transactions and balances (Note 1.R)	2.6	-	-	2.6
Net operating (cost)/revenue	(1,198.6)	45.0	-	(1,153.6)
Net position, beginning of period	(22,619.9)	3,374.3	-	(19,245.6)
Adjustments to beginning net position (Note 1.S)	37.1	0.2	-	37.3
Net operating (cost)/revenue	(1,198.6)	45.0	-	(1,153.6)
Net position, end of period	(23,781.4)	3,419.5	-	(20,361.9)

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

United States Government
Reconciliations of Net Operating Cost and Budget Deficit
for the Years Ended September 30, 2018, and 2017

(In billions of dollars)	2018	Restated 2017
Net operating cost	(1,159.0)	(1,153.6)
Components of net operating cost not part of the budget deficit		
Excess of accrual-basis expenses over budget outlays		
* Federal employee and veteran benefits payable		
Pension and accrued benefits	88.4	180.5
Veterans compensation and burial benefits	146.3	313.7
Post-retirement health and accrued benefits	33.0	5.3
Other benefits	14.5	(8.8)
Subtotal - federal employee and veteran benefits payable	282.2	490.7
* Insurance and guarantee program liabilities	(32.3)	15.5
* Environmental and disposal liabilities	112.8	17.9
* Accounts payable	15.9	8.4
* Benefits due and payable	(7.7)	0.6
* Other liabilities	5.9	4.4
Subtotal - excess of accrual-basis expenses over budget outlays	376.8	537.5
Amortized expenses not included in budget outlays		
Property, plant, and equipment depreciation expense	72.7	33.6
Other expenses that are not reported as budget outlays		
Property, plant, and equipment disposals and revaluations	(4.0)	(10.0)
Excess of accrual-basis revenue over budget receipts		
Accounts receivable, net	6.2	(7.3)
Taxes receivable, net	(7.8)	(2.8)
Other losses/(gains) and cost/(revenue) that are not budget receipts		
* Investments in government-sponsored enterprises	(20.6)	16.0
Subtotal - components of net operating cost not part of budget deficit	423.3	567.0
Components of the budget deficit that are not part of net operating cost		
Budget receipts not included in net operating cost		
Credit reform and other loan activities	5.0	(9.5)
Budget outlays not included in net operating cost		
Acquisition of capital assets	(72.2)	(79.9)
* Debt and equity securities	5.9	(8.0)
* Inventories and related property	(10.8)	(12.4)
* Other assets	34.0	(2.2)
Subtotal - components of the budget deficit that are not part of net operating cost	(38.1)	(112.0)
Adjustments to beginning net position	0.1	37.3
Other		
All other reconciling items	(5.3)	(4.4)
Budget deficit	(779.0)	(665.7)

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

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

United States Government
Statements of Changes in Cash Balance from Budget and Other Activities for the Years Ended September 30, 2018, and 2017

(In billions of dollars)	2018	Reclassed 2017
Cash flow from budget activities		
Total budget receipts	3,328.7	3,314.9
Total budget outlays	(4,107.7)	(3,980.6)
Budget deficit	(779.0)	(665.7)
Adjustments for non-cash outlays included in the budget		
Non-cash flow amounts in the budget related to federal debt securities		
Accrued interest	268.5	248.4
Net amortization	41.9	19.0
Other	1.1	22.1
Subtotal - adjustments for non-cash flow amounts in the budget related to federal debt securities	311.5	289.5
Non-cash flow amounts in the budget related to loan financing account activity		
Interest revenue on uninvested funds	7.9	8.4
Interest expense on entity borrowings	(42.1)	(41.6)
Entities' downward reestimates/negative subsidy payments	(37.3)	(34.6)
Entities' subsidy expense/upward reestimates	35.8	84.9
Subtotal - adjustments for non-cash flow amounts in the budget related to loan financing account activity	(35.7)	17.1
Total of adjustments for non-cash outlays included in the budget	275.8	306.6
Cash flow from activities not included in the budget		
Cash flow from non-budget activities related to federal debt securities		
Interest paid	(260.4)	(240.0)
Subtotal - cash flow from non-budget activities related to federal debt securities	(260.4)	(240.0)
Cash flow from non-budget activities related to loan financing account activity		
Loan disbursements/default payments	(194.9)	(213.2)
Fees	25.0	26.3
Principal & interest repayments	117.7	121.0
Other collections on defaulted loans receivable and sale of foreclosed property	5.7	8.1
Other loan financing account activities	0.6	-
Subtotal - cash flow from non-budget activities related to loan financing account activity	(45.9)	(57.8)
Cash flow from financing federal debt securities		
Borrowings	10,080.1	8,700.8
Repayments	(8,993.5)	(8,222.9)
Discount/premium	(54.7)	(24.0)
Subtotal - cash flow from financing federal debt securities	1,031.9	453.9
Total cash flow from activities not included in the budget	725.6	156.1
Other		
Total other	13.9	6.3
Change in cash and other monetary assets balance	236.3	(196.7)
Beginning cash and other monetary assets balance	271.2	467.9
Ending cash and other monetary assets balance	507.5	271.2

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

United States Government
Balance Sheets
as of September 30, 2018, and 2017

(In billions of dollars)	2018	Restated 2017
Assets:		
Cash and other monetary assets (Note 2)	507.5	271.2
Accounts and taxes receivable, net (Note 3)	144.9	143.3
Loans receivable, net (Note 4)	1,419.1	1,350.2
Inventories and related property, net (Note 5)	337.5	326.7
Property, plant and equipment, net (Note 6)	1,090.5	1,087.0
Debt and equity securities (Note 7)	110.3	116.2
Investments in government-sponsored enterprises (Note 8)	113.2	92.6
Other assets (Note 9)	113.7	147.7
Total assets	3,836.7	3,534.9
Stewardship land and heritage assets (Note 24)		
Liabilities:		
Accounts payable (Note 10)	86.7	70.8
Federal debt securities held by the public and accrued interest (Note 11)	15,812.7	14,724.1
Federal employee and veteran benefits payable (Note 12)	7,982.3	7,700.1
Environmental and disposal liabilities (Note 13)	577.3	464.5
Benefits due and payable (Note 14)	211.1	218.8
Insurance and guarantee program liabilities (Note 15)	170.2	202.5
Loan guarantee liabilities (Note 4)	38.2	42.9
Other liabilities (Note 16)	479.0	473.1
Total liabilities	25,357.5	23,896.8
Contingencies (Note 18) and Commitments (Note 19)		
Net Position:		
Funds from Dedicated Collections (Note 20)	3,462.0	3,419.5
Funds other than those from Dedicated Collections	(24,982.8)	(23,781.4)
Total net position	(21,520.8)	(20,361.9)
Total liabilities and net position	3,836.7	3,534.9

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

United States Government
Statements of Long-Term Fiscal Projections (Note 23)
Present Value of 75-Year Projections as of September 30, 2018 and 2017[1]

	In trillions of dollars			Percent of GDP[2]		
	2018	2017	Change	2018	2017	Change
Receipts:						
Social Security payroll taxes	60.6	58.0	2.6	4.3	4.3	-
Medicare payroll taxes	20.3	19.4	0.9	1.4	1.4	-
Individual income taxes	143.8	141.9	1.9	10.2	10.5	(0.3)
Corporate income taxes	18.8	- [3]	- [3]	1.3	- [3]	- [3]
Other receipts[3]	18.5	49.0	(11.7)	1.3	3.6	(1.0)
Total receipts	262.0	268.4	(6.4)	18.6	19.9	(1.3)
Non-interest spending:						
Social Security	82.5	78.7	3.9	5.9	5.8	-
Medicare Part A[4]	29.1	26.6	2.5	2.1	2.0	0.1
Medicare Parts B & D[5]	35.7	32.3	3.4	2.5	2.4	0.1
Medicaid	34.1	32.1	2.0	2.4	2.4	-
Other mandatory	41.0	40.5	0.4	2.9	3.0	(0.1)
Defense discretionary	42.9	39.1	3.8	3.0	2.9	0.1
Non-defense discretionary	42.9	35.3	7.6	3.1	2.6	0.4
Total non-interest spending	308.2	284.6	23.6	21.9	21.1	0.8
Receipts less non-interest spending	(46.2)	(16.2)	(30.0)	(3.3)	(1.2)	(2.1)
Fiscal gap[6]				(4.1)	(2.0)	(2.1)

[1]75-year present value projections for 2018 are as of 9/30/2018 for fiscal years 2019-2093; projections for 2017 are as of 9/30/2017 for fiscal years 2018-2092.
[2]The 75-year present value of nominal Gross Domestic Product (GDP), which drives the calculations above is $1,406.3 trillion starting in fiscal year 2019, and was $1,347.0 trillion starting in fiscal year 2018.
[3]In fiscal year 2017, Corporate Income Taxes were included as part of Other Receipts. To incorporate the effects of the *Tax Cuts and Jobs Act of 2017,* Corporate Income Taxes are modeled separately in fiscal year 2018. Directly comparable data are not available for fiscal year 2017. The $11.7 trillion decrease in Other Receipts is the total of 2018 Corporate Income Taxes ($18.8 trillion) and Other Receipts ($18.5 trillion) less the 2017 Other Receipts ($49.0 trillion).
[4]Represents portions of Medicare supported by payroll taxes.
[5]Represents portions of Medicare supported by general revenues. Consistent with the President's Budget, outlays for Parts B & D are presented net of premiums.
[6]To prevent the debt-to-GDP ratio from rising over the next 75 years, a combination of non-interest spending reductions and receipts increases that amounts to 4.1 percent of GDP on average is needed (2.0 percent of GDP on average in 2017). See Note 23—Long-Term Fiscal Projections.

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

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

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

(In trillions of dollars)	2018	2017	2016	2015	2014
Federal Old-Age, Survivors and Disability Insurance (Social Security):[11]					
Revenue (Contributions and Dedicated Taxes) from:					
Participants who have attained eligibility age (age 62 and over)	1.5	1.4	1.3	1.2	1.0
Participants who have not attained eligibility age	31.8	30.3	29.3	27.8	25.4
Future participants	31.8	30.5	29.7	26.6	24.6
All current and future participants	65.1	62.1	60.3	55.5	51.0
Expenditures for Scheduled Future Benefits for:					
Participants who have attained eligibility age (age 62 and over)	(15.9)	(14.7)	(13.6)	(12.8)	(11.9)
Participants who have not attained eligibility age	(52.2)	(50.2)	(48.4)	(45.3)	(42.4)
Future participants	(13.0)	(12.6)	(12.4)	(10.9)	(10.0)
All current and future participants	(81.1)	(77.5)	(74.4)	(69.0)	(64.3)
Present value of future expenditures in excess of future revenue	(16.1)[1]	(15.4)[2]	(14.1)[3]	(13.4)[4]	(13.3)[5]
Federal Hospital Insurance (Medicare Part A):[11]					
Revenue (Contributions and Dedicated Taxes) from:					
Participants who have attained eligibility age (age 65 and over)	0.5	0.5	0.5	0.4	0.3
Participants who have not attained eligibility age	11.3	10.7	10.3	9.1	8.4
Future participants	11.0	10.6	10.0	8.4	7.8
All current and future participants	22.8	21.7	20.7	17.9	16.5
Expenditures for Scheduled Future Benefits for:					
Participants who have attained eligibility age (age 65 and over)	(5.0)	(4.5)	(4.3)	(3.8)	(3.5)
Participants who have not attained eligibility age	(18.6)	(17.2)	(16.8)	(14.5)	(14.1)
Future participants	(3.9)	(3.5)	(3.4)	(2.8)	(2.8)
All current and future participants	(27.5)	(25.3)	(24.5)	(21.1)	(20.4)
Present value of future expenditures in excess of future revenue	(4.7)[1]	(3.5)[2]	(3.8)[3]	(3.2)[4]	(3.8)[5]
Federal Supplementary Medical Insurance (Medicare Part B):[11]					
Revenue (Premiums) from:					
Participants who have attained eligibility age (age 65 and over)	1.3	1.1	1.0	0.9	0.8
Participants who have not attained eligibility age	6.6	5.9	5.3	4.6	4.5
Future participants	1.5	1.4	1.2	1.0	1.1
All current and future participants	9.4	8.4	7.5	6.5	6.5
Expenditures for Scheduled Future Benefits for:					
Participants who have attained eligibility age (age 65 and over)	(5.2)	(4.5)	(4.0)	(3.6)	(3.2)
Participants who have not attained eligibility age	(23.8)	(21.4)	(19.2)	(16.8)	(17.0)
Future participants	(5.4)	(4.9)	(4.3)	(3.5)	(4.1)
All current and future participants	(34.4)	(30.8)	(27.5)	(24.0)	(24.3)
Present value of future expenditures in excess of future revenue [6]	(25.0)[1]	(22.4)[2]	(20.0)[3]	(17.5)[4]	(17.9)[5]

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

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

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

(In trillions of dollars)	2018	2017	2016	2015	2014
Federal Supplementary Medical Insurance (Medicare Part D):[11]					
Revenue (Premiums and State Transfers) from:					
Participants who have attained eligibility age (age 65 and over)	0.3	0.3	0.3	0.3	0.2
Participants who have not attained eligibility age	2.1	2.0	2.2	1.8	1.6
Future participants	0.8	0.8	1.0	0.8	0.7
All current and future participants	3.2	3.1	3.5	2.9	2.5
Expenditures for Scheduled Future Benefits for:					
Participants who have attained eligibility age (age 65 and over)	(1.0)	(1.0)	(1.0)	(0.9)	(0.8)
Participants who have not attained eligibility age	(7.2)	(6.9)	(7.7)	(6.4)	(5.9)
Future participants	(2.9)	(2.9)	(3.6)	(2.8)	(2.6)
All current and future participants	(11.1)	(10.8)	(12.2)	(10.2)	(9.3)
Present value of future expenditures in excess of future revenue [6]	(7.9)[1]	(7.6)[2]	(8.7)[3]	(7.3)[4]	(6.8)[5]
Other:[7]					
Present value of future expenditures in excess of future revenues [8, 9, 10]	(0.1)	(0.1)	(0.1)	(0.1)	(0.1)
Total present value of future expenditures in excess of future revenue	(53.8)	(49.0)	(46.7)	(41.5)	(41.9)

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

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

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

(In trillions of dollars)	2018	2017	2016	2015	2014
Social Insurance Summary[11]					
Participants who have attained eligibility age:					
Revenue (e.g., contributions and dedicated taxes)	3.6	3.3	3.1	2.8	2.3
Expenditures for scheduled future benefits	(27.1)	(24.7)	(22.9)	(21.3)	(19.4)
Present value of future expenditures in excess of future revenue	(23.5)	(21.4)	(19.8)	(18.5)	(17.1)
Participants who have not attained eligibility age:					
Revenue (e.g., contributions and dedicated taxes)	51.8	48.9	47.1	43.4	40.0
Expenditures for scheduled future benefits	(101.8)	(95.7)	(92.2)	(83.1)	(79.6)
Present value of future expenditures in excess of future revenue	(50.0)	(46.8)	(45.1)	(39.7)	(39.6)
Closed-group - Total present value of future expenditures in excess of future revenue	(73.5)	(68.2)	(64.9)	(58.2)	(56.7)
Future participants:					
Revenue (e.g., contributions and dedicated taxes)	45.1	43.3	41.9	36.8	34.3
Expenditures for scheduled future benefits	(25.2)	(24.0)	(23.7)	(20.1)	(19.6)
Present value of future revenue in excess of future expenditure	19.9	19.3	18.2	16.8	14.8
Open-group - Total present value of future expenditures in excess of future revenue	(53.8)	(49.0)	(46.7)	(41.5)	(41.9)

1 The projection period for Social Security and Medicare is 1/1/2018-12/31/2092 and the valuation date is 1/1/2018.
2 The projection period for Social Security and Medicare is 1/1/2017-12/31/2091 and the valuation date is 1/1/2017.
3 The projection period for Social Security and Medicare is 1/1/2016-12/31/2090 and the valuation date is 1/1/2016.
4 The projection period for Social Security and Medicare is 1/1/2015-12/31/2089 and the valuation date is 1/1/2015.
5 The projection period for Social Security and Medicare is 1/1/2014-12/31/2088 and the valuation date is 1/1/2014.
6 These amounts represent the present value of the future transfers from the General Fund to the SMI Trust Fund. These future intragovernmental transfers are included as income in both HHS' and the Centers for Medicare and Medicaid Services' Financial Reports but, by accounting convention, are not income from the governmentwide perspective of this report.
7 Includes Railroad Retirement and Black Lung.
8 These amounts do not include the present value of the financial interchange between the railroad retirement and social security systems, which is included as income in the Railroad Retirement Financial Report, but is not included from the governmentwide perspective of this report. (See discussion of Railroad Retirement Program in the unaudited required supplementary information section of this report).
9 Does not include interest expense accruing on the outstanding debt of the Black Lung Disability Trust Fund.
10 For information on the projection periods and valuation dates for the Railroad Retirement and Black Lung programs, refer to the financial statements of RRB and DOL, respectively.
11 Current participants for the Social Security and Medicare programs are assumed to be the "closed-group" of individuals who are at least 15 years of age at the start of the projection period, and are participating as either taxpayers, beneficiaries, or both.

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

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

United States Government
Statement of Changes in Social Insurance Amounts
for the Year Ended September 30, 2018 (Note 22)

(In trillions of dollars)	Social Security[1]	Medicare HI[1]	Medicare SMI[1]	Other[2]	Total
Net present value (NPV) of future revenue less future expenditures for current and future participants (the "open group") over the next 75 years, beginning of the year	(15.4)	(3.5)	(30.0)	(0.1)	(49.0)
Reasons for changes in the NPV during the year:					
Changes in valuation period	(0.6)	(0.2)	(1.1)	-	(1.9)
Changes in demographic data, assumptions, and methods	0.1	0.4	0.2	-	0.7
Changes in economic data, assumptions, and methods	(0.5)	-	-	-	(0.5)
Changes in law or policy	-	(0.5)	(0.5)	-	(1.0)
Changes in methodology and programmatic data	0.2	-	-	-	0.2
Changes in economic and other health care assumptions	-	-	(1.5)	-	(1.5)
Change in projection base	-	(0.9)	-	-	(0.9)
Net change in open group measure	(0.8)	(1.2)	(2.9)	-	(4.8)
Open group measure, end of year	(16.1)	(4.7)	(32.9)	(0.1)	(53.8)

[1] Amounts represent changes between valuation dates 1/1/2017 and 1/1/2018.

[2] Includes Railroad Retirement changes between valuation dates 10/1/2016 and 10/1/2017 and Black Lung changes between 9/30/2017 and 9/30/2018.

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

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

United States Government
Statement of Changes in Social Insurance Amounts
for the Year Ended September 30, 2017 (Note 22)

(In trillions of dollars)	Social Security[1]	Medicare HI[1]	Medicare SMI[1]	Other[2]	Total
Net present value (NPV) of future revenue less future expenditures for current and future participants (the "open group") over the next 75 years, beginning of the year	(14.1)	(3.8)	(28.7)	(0.1)	(46.7)
Reasons for changes in the NPV during the year:					
Changes in valuation period	(0.6)	(0.2)	(1.2)	-	(2.0)
Changes in demographic data, assumptions, and methods	(0.1)	(0.1)	-	-	(0.2)
Changes in economic data, assumptions, and methods	(0.6)	-	-	-	(0.6)
Changes in law or policy	-	-	-	-	-
Changes in economic and other health care assumptions	-	0.2	(0.5)	-	(0.3)
Change in projection base	-	0.3	0.4	-	0.7
Net change in open group measure	(1.2)	0.3	(1.4)	-	(2.3)
Open group measure, end of year	(15.4)	(3.5)	(30.0)	(0.1)	(49.0)

[1] Amounts represent changes between valuation dates 1/1/2016 and 1/1/2017.

[2] Includes Railroad Retirement changes between valuation dates 10/1/2015 and 10/1/2016 and Black Lung changes between 9/30/2016 and 9/30/2017.

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

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

United States Government Notes to the Financial Statements for the Fiscal Years Ended September 30, 2018, and 2017

Note 1. Summary of Significant Accounting Policies

A. Reporting Entity

The government includes the executive branch, the legislative branch, and the judicial branch. This *Financial Report* includes the financial status and activities related to the operations of the government. SFFAS No. 47, *Reporting Entity*, effective for fiscal year 2018, provides criteria for identifying organizations that are included in the *Financial Report* as "consolidation entities" and "disclosure entities." Consolidation entities are consolidated into the government's financial statements. For disclosure entities, information is disclosed in the notes to the financial statements concerning (a) the nature of the federal government's relationship with the disclosure entities, (b) the nature and magnitude of relevant activity with the disclosure entities during the period and balances at the end of the period, and (c) a description of financial and non-financial risks, potential benefits and, if possible, the amount of the federal government's exposure to gains and losses from the past or future operations of the disclosure entity or entities.

Disclosure entities have a greater degree of autonomy than consolidation entities. Disclosure entities may maintain a separate legal identity, have a governance structure that vests most decision-making authorities in a governing body to insulate the organization from political influence, and/or have relative financial independence. These entities may include, but are not limited to, quasi-governmental and/or financially independent entities and organizations owned and/or controlled by the federal government as a result of (a) regulatory actions (such as organizations in receivership or conservatorship) or (b) other federal government intervention actions if the relationship with such entities is not expected to be permanent.

SFFAS No. 47 also provides guidance for identifying related parties and in determining what information to provide about related party relationships of such significance that it would be misleading to exclude such information. (See Appendix A—Reporting Entity, for a more detailed discussion.)

Based on the criteria in GAAP for federal entities, the assets, liabilities, and results of operations of Fannie Mae and Freddie Mac are not consolidated into the government's consolidated financial statements. However, the values of the investments in such entities, changes in value, and related activity with these entities are included in the government's consolidated financial statements. Although federal investments in Fannie Mae and Freddie Mac are significant, these entities do not meet the GAAP criteria for consolidation entities.

For fiscal year 2018, under SFFAS No. 47 criteria, Fannie Mae and Freddie Mac were owned or controlled by the federal government as a result of (a) regulatory actions (such as organizations in receivership or conservatorship) or (b) other federal government intervention actions. Under the regulatory or other intervention actions, the relationship with the federal government is not expected to be permanent. These entities are classified as disclosure entities based on their characteristics as a whole. For fiscal year 2017, these entities met the criteria of paragraph 50 of Statement of Federal Financial Accounting Concepts (SFFAC) No. 2, *Entity and Display* and do not appear in the federal budget section "Federal Programs by Agency and Account." SFFAS No. 47 replaced reporting entity criteria in SFFAC No. 2 (see Note 25—Disclosure Entities and Related Parties for additional information on these disclosure entities).

Also, under GAAP criteria, the FR System is not consolidated into the government's consolidated financial statements (see Note 25—Disclosure Entities and Related Parties for further information concerning the Federal Reserve System).

Implementation of SFFAS No. 47, as of October 1, 2017, did not have a significant impact on the composition of the entities consolidated in the *Financial Report* as compared to entities consolidated under SFFAC No. 2, for fiscal year 2017 (see Note 1.S—Adjustments to Beginning Net Position for information on the changes in accounting principles). For further information regarding Reporting Entity, see Appendix A—Reporting Entity.

B. Basis of Accounting and Revenue Recognition

Consolidated Financial Statements

The consolidated financial statements of the government were prepared using GAAP, primarily based on Federal Accounting Standards Advisory Board's (FASAB's) SFFAS. Intragovernmental transactions are eliminated in consolidation, except as described in the Other Information– Unmatched Transactions and Balances. See Note 1.R—Unmatched Transactions and Balances for detailed information. The consolidated financial statements include accrual-based financial statements and sustainability financial statements, which are discussed in more detail below, and the related notes to the consolidated financial statements. Collectively, the accrual-based financial statements, the sustainability financial statements, and the notes represent basic information that is deemed essential for the financial statements and notes to be presented in conformity with GAAP.

Accounting standards allow certain presentations and disclosures to be modified, if needed, to prevent the disclosure of classified information. Accordingly, modifications may have been made to certain presentations and disclosures.

Accrual-Based Financial Statements

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

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

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

Sustainability Financial Statements

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

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

New Standards Issued in Prior and Current Years and Implemented in Current Year

Beginning in fiscal year 2018, the government implemented, or began to implement, the requirements of new standards for: Reporting Entity, Tax Expenditures, Budget and Accrual Reconciliation, Assigning Assets to Component Reporting Entities, Amending Inter-Entity Cost Provisions, and Classified Activities. The new standards implemented are:

- SFFAS No. 47, *Reporting Entity*. SFFAS No. 47 established principles to identify organizations for which elected officials are accountable. The standard also guides preparers of general purpose federal financial reports (GPFFRs) in determining what organizations to report upon, whether such organizations are considered "consolidation entities" or "disclosure entities," and what information should be presented about those organizations. The standard also requires information to be provided about related party relationships of such significance that it would be misleading

[1] With the exception of the Black Lung program, which has a rolling 25-year projection period that begins on the September 30 valuation date each year.

to exclude information. Note 25— Disclosure Entities and Related Parties has been added to the *Financial Report* to capture additional information required under SFFAS No. 47. Refer to Note 25—Disclosure Entities and Related Parties and Appendix A for detailed information. SFFAS No. 47 became effective in fiscal year 2018.

- SFFAS No. 52, *Tax Expenditures*. SFFAS No. 52 requires certain information on tax expenditures to be included in the *Financial Report* to assist users in understanding the existence, purpose, and impact of tax expenditures. Disclosures within the notes to the financial statements should include a "plain language" definition, examples of types, and a description of how tax expenditures affect non-exchange revenue, tax collections and refunds, as well as whether tax expenditure amounts are presented in the basic financial statements. The MD&A should include a "plain language" definition, the general purpose, and examples of types of tax expenditures. The MD&A should also include information about other factors that may affect tax collections in order to place tax expenditure information in an appropriate context, a description of how tax expenditures are treated for budgetary and financial reporting purposes, and a statement regarding the availability of published information on tax expenditures, such as the Treasury Office of Tax Policy's unaudited annual report on tax expenditures, and how that information can be obtained. SFFAS No. 52 also encourages presentation of tax expenditures as unaudited other information (OI) in the *Financial Report*. SFFAS No. 52 became effective in fiscal year 2018.
- In October 2017, FASAB issued SFFAS No. 53, *Budget and Accrual Reconciliation; Amending SFFAS No. 7, and 24 and Rescinding SFFAS No. 22*. SFFAS No. 53 amends component entity requirements for a reconciliation between budgetary and financial accounting information established by SFFAS No. 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*. To increase informational value and usefulness, and to support the governmentwide financial statement reconciling net operating cost to the budget deficit, this Statement provides for the budget and accrual reconciliation (BAR) to replace the statement of financing. The BAR explains the relationship between the entity's net outlays on a budgetary basis and the net cost of operations during the reporting period. The BAR starts with net cost of operations and is adjusted by components of net cost that are not part of net outlays, components of net outlays that are not part of net cost, and other temporary timing differences, which reflect some special adjustments. SFFAS No. 53 is effective in 2019 and early implementation is permitted. During fiscal year 2018, USDA, VA, HHS, HUD, and Millennium Challenge Corporation (MCC) adopted this standard.
- Technical Bulletin (TB) 2017-2, *Assigning Assets to Component Reporting Entities*. TB 2017-2 provides guidance to address areas not directly covered in existing Statements and clarifies existing standards. The TB provides that assets may be assigned by a reporting entity to its component reporting entities on a rational and consistent basis. The TB provides that assets may only be assigned by a component reporting entity to its own sub-component reporting entities (such as bureaus, components, or responsibility segments within the same larger reporting entity or department). This TB facilitates reporting for large and complex organizations so that reporting is better aligned with their operations and results in less costly financial reporting by permitting the reporting entity to align reporting with established funding and governance structures. Component reporting entities should describe the policies used to assign significant assets. This TB also reduces barriers to and cost of adopting GAAP. TB 2017-2 became effective in fiscal year 2018.
- In May 2018, FASAB issued SFFAS No. 55, *Amending Inter-Entity Cost Provisions*. SFFAS No. 55 revises SFFAS No. 4, *Managerial Cost Accounting Standards and Concepts* (including Interpretation 6, *Accounting for Imputed Intra-departmental Costs: An Interpretation of SFFAS No. 4*). SFFAS No. 4 required component reporting entities to recognize the full costs of services received from other federal reporting entities even if there was no requirement to reimburse the providing entity for the full cost of such services. This Statement revises SFFAS No. 4 to provide for the continued recognition of significant inter-entity costs by business-type activities and rescinds the following: a) SFFAS No. 30, *Inter-Entity Cost Implementation: Amending SFFAS No. 4, Managerial Cost Accounting Standards and Concepts* and b) Interpretation 6, *Accounting for Imputed Intra-departmental Costs: An Interpretation of SFFAS No. 4*. Recognition of inter-entity costs by activities that are not business-type activities is not required with the exception of inter-entity costs for personnel benefits and the Treasury Judgment Fund settlements unless otherwise directed by the OMB. Notwithstanding the absence of a requirement, non-business-type activities may elect to recognize imputed cost and corresponding imputed financing for other types of inter-entity costs. Component reporting entities should disclose that only certain inter-entity costs are recognized for goods and services that are received from other federal entities at no cost or at a cost less than the full costs. SFFAS No. 55 is effective in 2019 and early implementation is permitted. During fiscal year 2018, DOD adopted this standard.
- SFFAS No. 56, *Classified Activities*. SFFAS No. 56 permits financial statement modifications that do not affect net results of operations or net position to prevent the disclosure of classified national security information or activities. In addition, this Statement allows a component reporting entity to be excluded from one reporting entity and consolidated into another reporting entity, and the effect of the modification may change the net results of operations

and/or net position. Further, interpretations of this Statement, which may themselves contain classified information, will address the requirements of this and other standards and permit other modifications when needed to prevent the disclosure of classified information. Modifications permitted by this Statement and future interpretations may affect the net results of operations and/or net position of those entities applying the interpretations. This standard may be implemented for fiscal year 2018.

In fiscal year 2016, the government began implementing the requirements of new standards related to the reporting for: Inventories and Related Property and Property, Plant, and Equipment. The standards being implemented are:

- FASAB issued SFFAS No. 48, *Opening Balances for Inventory, Operating Materials and Supplies, and Stockpile Materials.* SFFAS No. 48 permits a reporting entity to apply an alternative valuation method in establishing opening balances and applies when a reporting entity is presenting financial statements or one or more line items addressed by this statement. This standard can be applied for the first time or after a period during which existing systems could not provide the information necessary for producing GAAP-based financial statements without use of the alternative valuation methods. This is intended to provide an alternative method to adoption of GAAP when historical records and systems do not provide a basis for valuation of opening balances in accordance with SFFAS No. 3, *Accounting for Inventory and Related Property.* This application is available to each reporting entity only once per line item addressed in this statement. Reporting entities that meet either condition and elect to apply this statement should follow the guidance in SFFAS No. 21, *Reporting Corrections of Errors and Changes in Accounting Principles.* SFFAS No. 48 was effective beginning in fiscal year 2017. Early implementation was permitted. DOD did partially implement in 2016 and select component entities have continued to implement in 2017 and 2018. DOD has not declared full implementation yet.
- FASAB issued SFFAS No. 50, *Establishing Opening Balances for General Property, Plant and Equipment.* SFFAS No. 50 permits a reporting entity to apply an alternative valuation method in establishing opening balances and applies when a reporting entity is presenting financial statements or one or more line items addressed by this statement. This standard can be applied for the first time or after a period during which existing systems could not provide the information necessary for producing GAAP-based financial statements without use of the alternative valuation methods. This is intended to provide an alternative method to adoption of GAAP when historical records and systems do not provide a basis for valuation of opening balance in accordance with SFFAS No. 6, *Accounting for Property, Plant, and Equipment*. This application is available to each reporting entity only once per line item addressed in this statement. Reporting entities meeting the conditions and electing to apply this statement should follow the guidance in SFFAS No. 21, *Reporting Corrections of Errors and Changes in Accounting Principles.* SFFAS No. 50 was effective beginning in fiscal year 2017. Early implementation was permitted. DOD did partially implement in 2016 and select component entities have continued to implement in 2017 and 2018. DOD has not declared full implementation yet.

New Standards Issued and Not Yet Implemented

FASAB issued the following new standards that are applicable to the *Financial Report*, but are not yet implemented at the governmentwide level for fiscal year 2018:

- In April 2016, FASAB issued SFFAS No. 49, *Public-Private Partnerships Disclosure Requirements.* SFFAS No. 49 establishes principles to ensure disclosure about Public-Private Partnerships (P3s) are presented in the reporting entity's GPFFRs. P3s are defined as "risk sharing" arrangements or transactions lasting more than five years between public and private sector entities. Disclosure requirements comprise quantitative and qualitative information to assist users in understanding the nature of P3s. P3 disclosures help achieve the operating performance and budgetary integrity objectives outlined in SFFAC No. 1. P3s are a form of investments. They should be adequately disclosed in order to assist report users in determining: (a) the important assets of the U.S. government and how effectively they are being managed and (b) the identification of risks. SFFAS No. 49 is effective for periods beginning after September 30, 2018 and early implementation is permitted; however, it is not being early implemented in fiscal year 2018.
- In January 2017, FASAB issued SFFAS No. 51, *Insurance Programs*. SFFAS No. 51 establishes accounting and financial reporting standards to ensure that insurance programs are adequately defined and report consistent information about the liabilities for losses incurred and claimed as well as expected losses during remaining coverage. These will replace the insurance guarantee program standards provided in paragraphs 97-121 of SFFAS No. 5, *Accounting for Liabilities of the Federal Government*. To support consistency, it identifies three categories: 1) exchange transaction insurance programs other than life insurance, 2) non-exchange transaction insurance programs and 3) life insurance programs. Insurance programs are categorized based upon the type of revenue received as defined by SFFAS No. 7, *Accounting for Revenue and Other Financing and Concepts for Reconciling Budgetary and Financial Accounting,* as amended. SFFAS No. 51 provides guidance as to how and when insurance

programs should recognize revenue, expenses and liabilities according to the aforementioned categories. The recognition measurement, and disclosure guidance provides for concise, meaningful and transparent information regarding the operating performance of insurance programs. SFFAS No. 51 is effective for periods beginning after September 30, 2018 and early implementation is not permitted.

- In April 2018, FASAB issued SFFAS No. 54, *Leases: An Amendment of SFFAS No. 5, Accounting for Liabilities of the Federal Government, and SFFAS No. 6, Accounting for Property, Plant, and Equipment*. SFFAS No. 54 revises the financial reporting standards for federal lease accounting. It provides a comprehensive set of lease accounting standards to recognize federal lease activities in the reporting entity's GPFFRs and includes appropriate disclosures. This Statement requires that federal lessees recognize a lease liability and a leased asset at the commencement of the lease term, unless it meets any of the scope exclusions or the definition/criteria of short-term leases, or contracts or agreements that transfer ownership, or intragovernmental leases. A federal lessor would recognize a lease receivable and deferred revenue, unless it meets any of the scope exclusions or the definition/criteria or short-term leases, contracts or agreements that transfer ownership, or intragovernmental leases. SFFAS No. 54 is effective in 2021 and early adoption is not permitted.

C. Accounts and Taxes Receivable

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

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

D. Loans Receivable and Loan Guarantee Liabilities

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

The subsidy expense for direct or guaranteed loans disbursed during a fiscal year is the present value of estimated net cash flows for those loans or guarantees. For the fiscal year during which new direct or guaranteed loans are disbursed, the components of the subsidy expense of those new direct loans and loan guarantees are recognized separately among interest subsidy costs, default costs, fees and other collections, and other subsidy costs. Credit programs reestimate the subsidy cost allowance for outstanding direct loans and the liability for outstanding loan guarantees, by taking into account all factors that may have affected the estimated cash flows. Any adjustment resulting from the reestimates is recognized as a subsidy expense (or a reduction in subsidy expense).

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

E. Inventories and Related Property

Inventory is tangible personal property that is (1) held for sale, principally to federal entities, (2) in the process of production for sale, or (3) to be consumed in the production of goods for sale or in the provision of services for a fee. SFFAS No. 3, *Accounting for Inventory and Related Property*, requires inventories held for sale and held in reserve for future sale within the government to be valued using either historical cost or a method that reasonably approximates historical cost. Historical cost methods include first-in-first-out, weighted average, and moving average. Any other valuation method may be used if the results reasonably approximate one of the historical cost methods. FASAB issued additional guidance SFFAS No. 48, which permits a reporting entity to apply an alternative valuation method in establishing opening balances for inventory, OM&S, and stockpile materials and is intended to provide an alternative valuation method when historical records and systems do not provide a basis for valuation of opening balances in accordance with SFFAS No. 3.

As the largest contributor of inventories and related property, DOD values approximately 99 percent of its resale inventory using the moving average cost method as of September 30, 2018. DOD reports the remaining 1 percent of resale inventories at an approximation of historical cost using latest acquisition cost adjusted for holding gains and losses. OM&S are valued using various methods including moving average cost, standard price, historical cost, replacement price, and direct method. DOD uses both the consumption method (expensed when issued to an end user for consumption in normal operations) and the purchase method (expensed when purchased) of accounting for OM&S. Stockpile Materials are accounted for using actual cost or the lower of cost or market method. DOD continues to implement SFFAS No. 48, permitting alternative methods in establishing opening balances.

F. Property, Plant, and Equipment

Property, Plant, and Equipment (PP&E) consists of tangible assets that have an estimated useful life of two or more years, are not intended for sale in the ordinary course of business, and are intended to be used or available for use by the entity. These tangible assets may include land, land rights, assets acquired through capital leases, buildings and structures, furniture and fixtures, equipment, and vehicles.

SFFAS No. 6, *Accounting for Property, Plant, and Equipment* requires general PP&E to be recorded at cost. Cost shall include all costs incurred to bring the PP&E to a form and location suitable for its intended use. PP&E used in government operations are carried at acquisition cost, with the exception of some DOD equipment. FASAB issued additional guidance, SFFAS No. 50, *Establishing Opening Balances for General Property, Plant, and Equipment* which states that a reporting entity may choose alternative methods for establishing an opening balance for land and land rights. The entity may exclude land and land rights from the opening balance of general PP&E. In so doing, future land and land right acquisitions should be expensed. An entity electing to exclude land and land rights from its general PP&E opening balances must disclose, with a reference on the balance sheet to the related disclosure, the number of acres held at the beginning of each reporting period, the number of acres added during the period, the number of acres disposed of during the period, and the number of acres held at the end of each reporting period. DOD generally records PP&E at the estimated historical cost. However, when applicable DOD will continue to adopt SFFAS No. 50.

Costs to acquire PP&E, extend the useful life of existing PP&E, or enlarge or improve its capacity, that exceed federal entities' capitalization thresholds should be capitalized and depreciated or amortized. Depreciation and amortization expense should be recognized on all capitalized PP&E, except land and land rights of unlimited duration. In the case of constructed PP&E, the PP&E shall be recorded as construction work in process until it is placed in service, at which time the balance is transferred to PP&E.

For financial reporting purposes, heritage assets (excluding multi-use heritage assets) and stewardship land are not recorded as part of PP&E. Since heritage assets are intended to be preserved as national treasures, it is anticipated that they will be maintained in reasonable repair and that there will be no diminution in their usefulness over time. Many assets are clearly heritage assets. For example, the National Park Service manages the Washington Monument, the Lincoln Memorial and the Mall. Heritage assets that are predominantly used in general government operations are considered multi-use heritage assets and are included in PP&E. Stewardship land is also consistent with the treatment of heritage assets in that much of the government's land is held for the general welfare of the nation and is intended to be preserved and protected. Stewardship land is land owned by the government but not acquired for or in connection with general PP&E. Because most federal land is not directly related to general PP&E, it is deemed to be stewardship land and accordingly, it is not reported on the Balance Sheet. Examples of stewardship land include national parks and forests. For more details on stewardship assets, see Note 24—Stewardship Land and Heritage Assets.

G. Debt and Equity Securities

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

H. Investments in Government-Sponsored Enterprises

The senior preferred stock and associated warrants for the purchase of common stock in the GSEs (Fannie Mae and Freddie Mac) are presented at their fair value. Senior Preferred Stock Purchase Agreements (SPSPAs), which Treasury entered into with each GSE when they were placed under conservatorship, can result in payments to the GSEs when, at the end of any quarter, the Federal Housing Finance Agency (FHFA), acting as the conservator, determines that the liabilities of either GSE exceed its respective assets. Such payments result in an increase to the investment in the GSEs' senior preferred stock, with a corresponding decrease to cash held by Treasury.

The valuation to estimate the investment's fair value incorporates forecasts, projections, and cash flow analyses. Changes in valuation, including impairments, are deemed usual and recurring and thus are recorded as exchange transactions on the Statement of Net Cost and investments in GSEs on the Balance Sheet. The government also records dividends related to these investments as exchange transactions and accrues when declared.

The potential liabilities to the GSEs, if any, are assessed annually and recorded at the gross estimated amount. For more detailed information on investments in GSEs, refer to Note 8—Investments in Government-Sponsored Enterprises.

I. Federal Debt

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

J. Federal Employee and Veteran Benefits Payable

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

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

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

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

K. Environmental and Disposal Liabilities

Environmental and disposal liabilities are recorded at the estimated current cost of the cleanup plan, including the level of restoration to be performed, the current legal or regulatory requirements, and the current technology. Cleanup costs are the costs of removing, containing or disposing of hazardous waste. Hazardous waste is a solid, liquid, or gaseous waste that, because of its quantity or concentration, presents a potential hazard to human health or the environment. Cleanup costs include, but are not limited to, decontamination, decommissioning, site restoration, site monitoring, closure, and post-closure costs. Where technology does not exist to clean up radioactive or hazardous waste, only the estimable portion of the liability (typically monitoring and safe containment) is recorded.

L. Insurance and Guarantee Program Liabilities

Insurance and guarantee programs (such as Federal Crop Insurance Program and Benefit Pension Plans Program) are authorized by law to financially compensate a designated population of beneficiaries by accepting all or part of the risk for losses incurred as a result of an insured event. Programs excluded from this category include social insurance, loan guarantee, and federal employee and veteran benefit programs. Insurance and guarantee program funds are commonly held in revolving funds in the government and losses sustained by participants are paid from these funds. Many of these programs receive appropriations to pay excess claims or have authority to borrow from the Treasury. The values of insurance and guarantee program liabilities are particularly sensitive to changes in underlying estimates and assumptions. Insurance and guarantee programs with recognized liabilities in future periods (i.e., liabilities that extend beyond one year) are reported at their net present value.

M. Deferred Maintenance and Repairs

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

N. Contingencies

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

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

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

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

O. Commitments

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

P. Social Insurance

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

Q. Funds from Dedicated Collections

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

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

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

R. Unmatched Transactions and Balances

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

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

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

As intragovernmental transactions and balances reduce to immaterial amounts, the corresponding individual lines in the Unmatched Transactions and Balances table are adjusted to remove the differences for the fiscal year. Please refer to the table of Unmatched Transactions and Balances in Other Information (Unaudited) for examples of the individual lines. Materiality for these adjustments is considered in the absolute value, when at or below $0.1 billion.

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

S. Adjustments to Beginning Net Position

During fiscal years 2017 and 2018, DOD reported adjustments to beginning net position impacting the financial statements. DOD reported a decrease of $2.5 billion and an increase of over $37 billion in fiscal years 2018 and 2017, respectively, to beginning net position due to continuing implementation of SFFAS No. 48, *Opening Balances for Inventory, Operating Materials and Supplies, and Stockpile Materials* and SFFAS No. 50, *Establishing Opening Balances for General Property, Plant, and Equipment*.

SFFAS No. 47, *Reporting Entity*, was implemented in fiscal year 2018. The standard requires that consolidation entities be consolidated in their entirety. Prior to fiscal year 2018, only the federal portion of Smithsonian Institution was consolidated. For fiscal year 2018, all activities (federal and non-federal portions) of Smithsonian Institution were consolidated, resulting in a $2.6 billion adjustment to the fiscal year 2018 beginning net position.

In fiscal year 2017, Note 20—Funds from Dedicated Collections included $0.2 billion in adjustments to beginning net position for Gulf Coast Ecosystem Restoration Council and HUD. In fiscal year 2018, the adjustments to beginning net position for Smithsonian Institution of $2.6 billion related to dedicated collection funds.

T. Reclassifications

Certain fiscal year 2017 amounts were reclassified to conform to the fiscal year 2018 presentation. For example, reclassifications were made to certain line items presented on the Reconciliation of Net Operating Cost and Budget Deficit and the Statement of Changes in Cash Balance from Budget and Other Activities to provide a further breakdown of certain categories of transactions. Also, a review was done to enhance the format and readability of the *Financial Report* leading to consolidation of immaterial lines within tables, removal of information not required by FASAB, and be more in line with entity reporting requirements. In fiscal year 2018, the presentation of Note 4—Loans Receivable and Loan Guarantee Liabilities, Net for fiscal year 2017 was reclassified to mirror entity financial reporting reducing the need for manual calculations. The presentations of Note 5—Inventories and Related Property, Net, Note 6—Property, Plant, and Equipment, Net, and Note 13—Environmental and Disposal Liabilities removed the breakout of DoD for fiscal years 2017 and 2018.

U. Restatements

In fiscal year 2018, HUD recognized material misstatements that were due to (1) a discounting error in the Federal Housing Administration (FHA) cash flow model used to calculate the recovery rate applied to the annual financial statement re-estimate and (2) FHA not accounting for a contingency paid by the Treasury Judgment Fund. The corrections resulted in the restatement of certain prior year amounts reported on the Balance Sheet, Statement of Net Cost, Statement of Operations and Changes in Net Position, Reconciliations of Net Operating Cost and Budget Deficit, Note 4—Loans Receivable and Loans Guarantee Liabilities, Net (understated by $1.7 billion), and Note 16—Other Liabilities (overstated by $0.1 billion).

In fiscal year 2018, HUD made re-estimate presentation changes to subsidy expense (income) ($3.5 billion decrease), principal amount of loans under guarantee ($3.2 billion increase), and principal amount guaranteed by the United States ($2.6 billion increase) presented in Note 4—Loans Receivable and Loans Guarantee Liabilities fiscal year 2017 tables. HUD also changed the presentation of Note 20—Funds from Dedicated Collections from consolidation (includes eliminations) to combined (excludes eliminations) adjusting the ending net position by $0.1 billion in fiscal year 2017.

Also, in fiscal year 2018 errors were noted in the presentation of Note 19—Commitments for undelivered orders and other commitments that required correction of balances reported in fiscal year 2017. The corrections resulted in the restatement of prior year amounts for DOJ's undelivered orders ($13.9 billion increase) and Treasury's all other commitments ($10.8 billion increase).

Fiscal year 2017 beginning net position was restated by $51.2 billion due to compilation errors in the presentation of the Balance Sheet and Note 6—Property, Plant, and Equipment, Net. In addition, the related activity caused a restatement on the Statement of Net Cost in the amount of $1.3 billion.

V. Fiduciary Activities

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

W. Use of Estimates

The government has made certain estimates and assumptions relating to the reporting of assets, liabilities, revenues, expenses, and the disclosure of contingent liabilities to prepare these financial statements. There are a large number of factors that affect these assumptions and estimates, which are inherently subject to substantial uncertainty arising from the likelihood of future changes in general economic, regulatory, and market conditions. As such, actual results will differ from these estimates and such differences may be material.

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

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

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

The annual valuation performed as of September 30 on the senior preferred stock and warrants comprising the Investments in GSEs line item on the Balance Sheets incorporates various forecasts, projections, and cash flow analyses to develop an estimate of the asset's fair value. The value of the senior preferred stock is estimated by first estimating the fair value of the total equity of each GSE (which, in addition to the senior preferred stock, is comprised of other equity instruments including common stock, common stock warrants, and junior preferred stock). The fair value of the total equity is based on a discounted cash flow valuation methodology, whereby the primary input is the present value of the projected quarterly dividend payments. The fair value of the GSEs' other equity instruments are then deducted from its total equity, with the remainder representing the fair value of the senior preferred stock. The primary input into the warrants valuation is the market value of the shares of common stock of the GSEs which, along with the junior preferred stock, are traded on the over-the-counter (OTC) Bulletin Board. Treasury evaluates the need for adjusting the OTC market-based valuation of the warrants for the effects, if any, of significant events occurring after the close of the market but before the end of the measurement date. Treasury records any changes in valuation, including impairment, on the Statement of Net Cost and the Balance Sheet. Since the valuation is an annual process, Treasury deems changes in valuation of the senior preferred stock and warrants as usual and recurring.

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

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

X. Credit Risk

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

The government also takes on credit risk related to committed, but undisbursed direct loans, funding commitments to GSEs, and other activities. These activities generally focus on the underlying problems in the credit markets. These programs were developed to provide credit where borrowers are not able to get access to credit with reasonable terms and conditions. Because these programs attempt to correct for a market imperfection, it can expose the government to potential costs and losses. The extent of the risk assumed is described in more detail in the notes to the financial statements, and where applicable, is factored into credit reform models and reflected in fair value measurements.

Y. Treaties and Other International Agreements

For accounting purposes, treaties and other international agreements may be understood as falling into three broad categories:

- No commitment to spend money,
- Commitment to spend money, or
- Potential obligation to spend money.

The proper financial reporting of treaties and other international agreements depends on the probable future outflow or other sacrifice of resources as a result of entering into the agreement.

In many cases, treaties and other international agreements establish frameworks that govern cooperative activities with other countries, but leave to the discretion of the parties whether to engage in any such activities. In other cases, the agreements may contemplate specific cooperative activities, but obligations to engage in them are made subject to the availability of funds. Cooperative activities relevant to these treaties and other international agreements fall under the first category, which does not result in the U.S. government incurring any financial liability. Since these treaties and other international agreements have no financial impact, they are not reported or disclosed in this *Financial Report*.

Some treaties and other international agreements fall under the second category, involving specific obligations by the U.S. government to pay money to other countries or international organizations. Examples of such agreements include those that establish international organizations under which the U.S. government undertakes obligations to pay assessed dues to the organization; grant agreements under which the U.S. government provides foreign assistance funds to other countries; and claims settlement agreements under which the U.S. government agrees to pay specific sums of money to settle claims. For further information related to treaties and other international agreements that fall under the second category, refer to Note 19—Commitments.

The last category encompasses those treaties or other international agreements that may result in contingent liabilities arising from litigation or claims. Information relevant to contingent liabilities stemming from the U.S. government's involvement in treaties or other international agreements is captured in the annual legal representation letter process, and, if applicable, reported on the Balance Sheet or disclosed in Note 18—Contingencies.

Note 2. Cash and Other Monetary Assets

Cash and Other Monetary Assets as of September 30, 2018, and 2017

(In billions of dollars)	2018	2017
Unrestricted cash:		
Cash held by Treasury for governmentwide operations	378.5	153.3
Other	4.9	3.7
Restricted	31.6	26.1
Total cash	415.0	183.1
International monetary assets	66.7	63.3
Gold and silver	11.1	11.1
Foreign currency	14.7	13.7
Total cash and other monetary assets	507.5	271.2

Unrestricted cash includes cash held by Treasury for governmentwide operations (Operating Cash) and all other unrestricted cash held by the federal entities. Operating Cash represents balances from tax collections, federal debt receipts, and other various receipts net of cash outflows for federal debt repayments and other payments. Treasury checks outstanding are netted against Operating Cash until they are cleared by the FR System. Other unrestricted cash not included in Treasury's Operating Cash balance includes balances representing cash, cash equivalents, and other funds held by entities, such as undeposited collections, deposits in transit, demand deposits, amounts held in trust, and imprest funds. Operating Cash held by the Treasury increased by $225.2 billion (an increase of approximately 147 percent) in fiscal year 2018 due to Treasury's investment and borrowing decisions to manage the balance and timing of the government's cash position.

Restrictions on cash are due to the imposition on cash deposits by law, regulation, or agreement. Restricted cash is primarily composed of cash held by the Security Assistance Accounts (SAA), which execute Foreign Military Sales. The SAA included $26.3 billion and $21.3 billion as of September 30, 2018, and 2017, respectively.

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

Only a portion of the U.S. financial subscription to the IMF is made in the form of reserve assets; the remainder is provided in the form of a letter of credit from the U.S. to the IMF. The balance available under the letter of credit totaled $100.0 billion and $105.3 billion as of September 30, 2018, and 2017 respectively. The U.S. reserve position in the IMF had a U.S. dollar equivalent of $15.4 billion and $11.5 billion as of September 30, 2018, and 2017, respectively.

The SDR is an international reserve asset created by the IMF to supplement the existing reserve assets of its members. These interest-bearing assets can be obtained by IMF allocations, transactions with IMF member countries, or in the form of interest earnings on SDR holdings and reserve positions in the IMF. U.S. SDR holdings are an interest-bearing asset of Treasury's Exchange Stabilization Fund (ESF). The total amount of SDR holdings of the U.S. was the equivalent of $51.0 billion and $51.5 billion as of September 30, 2018, and 2017, respectively.

The IMF allocates SDRs to its members in proportion to each member's quota in the IMF. *The SDR Act*, enacted in 1968, authorized the Secretary of the Treasury to issue SDR Certificates (SDRCs) to the Federal Reserve in exchange for dollars. The amount of SDRCs outstanding cannot exceed the dollar value of SDR holdings. The Secretary of the Treasury determines when Treasury will issue or redeem SDRCs. SDRCs outstanding totaled $5.2 billion as of September 30, 2018, and 2017, and are included in Note 16—Other Liabilities.

As of September 30, 2018, and 2017, other liabilities included $49.3 billion and $49.9 billion, respectively, of interest-bearing liability to the IMF for SDR allocations. The SDR allocation item represents the cumulative total of SDRs distributed by the IMF to the U.S. in allocations. The U.S. has received no SDR allocations since 2009.

Gold is valued at the statutory price of $42.2222 per fine troy ounce. The number of fine troy ounces of gold was 261,498,927 as of September 30, 2018, and 2017. The market value of gold on the London Fixing was $1,187 and $1,283 per fine troy ounce as of September 30, 2018, and 2017, respectively. In addition, silver is valued at the statutory price of $1.2929 per fine troy ounce. The number of fine troy ounces of silver was 16,000,000 as of September 30, 2018, and 2017. The market value of silver on the London Fixing was $14.31 and $16.86 per fine troy ounce as of September 30, 2018, and 2017, respectively. Gold totaling $11.0 billion as of September 30, 2018, and 2017, was pledged as collateral for gold certificates issued and authorized to the FRBs by the Secretary of the Treasury. Gold certificates were valued at $11.0 billion as of September 30, 2018, and 2017, which are included in Note 16—Other Liabilities. Treasury may redeem the gold certificates at any time. Foreign currency is translated into U.S. dollars at the exchange rate at fiscal year-end. The foreign currency is maintained by the ESF and various U.S. federal entities as well as foreign banks.

Note 3. Accounts and Taxes Receivable, Net

Accounts and Taxes Receivable as of September 30, 2018, and 2017

(In billions of dollars)	2018	2017
Accounts receivable:		
Gross accounts receivable	112.4	117.9
Allowance for uncollectible amounts	(30.5)	(29.8)
Accounts receivable, net	81.9	88.1
Taxes receivable:		
Gross taxes receivable	226.7	203.8
Allowance for uncollectible amounts	(163.7)	(148.6)
Taxes receivable, net	63.0	55.2
Total accounts and taxes receivable, net	144.9	143.3

Gross accounts receivable include related interest receivable of $3.6 billion and $3.4 billion as of September 30, 2018, and 2017, respectively.

Treasury comprises approximately 41.1 percent of the government's reported accounts and taxes receivable, net, as of September 30, 2018. The following list of entities comprise 98.3 percent of the government's accounts and taxes receivable, net, of $144.9 billion as of September 30, 2018. Please refer to the following entities financial statements for details on gross accounts and taxes receivable and the related allowance for uncollectible amounts:

- Treasury
- HHS
- SSA
- DOI
- DHS
- DOD
- PBGC
- DOE
- Federal Deposit Insurance Corporation (FDIC)
- VA
- Tennessee Valley Authority (TVA)
- OPM
- DOL
- USDA
- USPS
- Federal Communications Commission (FCC)
- HUD
- Federal Trade Commission (FTC)
- Environmental Protection Agency (EPA)

Accounts and Taxes receivable, net include amounts related to criminal restitution owed to the government. In fiscal year 2018, accounts and taxes receivable, net included $7.9 billion of gross receivable related to criminal restitution orders monitored by responsible entities, of which $0.7 billion is determined to be collectible. Of this gross receivable amount, Treasury and HHS collectively accounts for $5.7 billion of which $0.5 billion is determined to be collectible as of September 30, 2018. In fiscal year 2017, this balance included $8.8 billion of gross receivables related to criminal restitution orders, of which $0.6 billion is determined to be collectible. Of this gross receivable amount, Treasury, HHS, and SSA collectively account for $8.0 billion of which $0.5 billion is determined to be collectible as of September 30, 2017.

Note 4. Loans Receivable and Loan Guarantee Liabilities, Net

Loans Receivable as of September 30, 2018

(In billions of dollars)	Loans Receivable, gross	Interest Receivable	Foreclosed Property	Allowance for Subsidy	Net Loans Receivable	Subsidy Expense (Income) for the Fiscal Year
Federal Direct Student Loans - Education	1,083.7	72.0	-	(40.7)	1,115.0	4.4
Federal Family Education Loans - Education	95.1	21.1	-	(23.3)	92.9	2.4
Electric Loans - USDA	49.3	0.3	-	(2.2)	47.4	(0.1)
Rural Housing Services - USDA	24.4	0.2	0.1	(2.1)	22.6	0.1
Export-Import Bank Loans	19.4	0.2	-	(2.0)	17.6	-
Housing and Urban Development Loans	30.6	9.3	1.3	(15.1)	26.1	(0.2)
All other programs	108.9	3.8	1.2	(16.4)	97.5	1.7
Total loans receivable	1,411.4	106.9	2.6	(101.8)	1,419.1	8.3

Loans Receivable as of September 30, 2017 (Restated)

(In billions of dollars)	Loans Receivable, gross	Interest Receivable	Foreclosed Property	Allowance for Subsidy	Net Loans Receivable	Subsidy Expense (Income) for the Fiscal Year
Federal Direct Student Loans - Education	998.8	59.5	-	(16.8)	1,041.5	5.3
Federal Family Education Loans - Education	101.6	19.3	-	(18.5)	102.4	2.4
Electric Loans - USDA	48.2	0.3	-	(2.1)	46.4	-
Rural Housing Services - USDA	24.7	0.3	0.1	(2.3)	22.8	0.1
Export-Import Bank Loans	21.7	0.2	-	(1.6)	20.3	0.1
Housing and Urban Development Loans	26.3	6.5	1.6	(13.9)	20.5	-
All other programs	107.1	3.2	1.3	(15.3)	96.3	(0.1)
Total loans receivable	1,328.4	89.3	3.0	(70.5)	1,350.2	7.8

Loan Guarantee Liabilities as of September 30, 2018, and 2017

	Principal Amount of Loans Under Guarantee		Principal Amount Guaranteed by the United States		Loan Guarantee Liabilities		Subsidy Expense (Income) for the Fiscal Year	
		Restated		Restated				
(In billions of dollars)	2018	2017	2018	2017	2018	2017	2018	2017
Federal Housing Administration Loans - HUD	1,470.8	1,409.5	1,326.8	1,277.4	19.1	20.6	(8.9)	13.0
Veterans Housing Benefit Programs - VA	663.7	596.5	167.9	151.9	8.7	10.4	(2.8)	(0.6)
Rural Housing Services - USDA	123.0	120.4	110.6	108.3	(0.2)	0.1	(0.2)	(0.5)
Small Business Loans - SBA	128.8	121.0	105.6	99.5	2.7	2.6	(1.1)	(0.9)
Federal Family Education Loans - Education	157.1	176.4	153.8	172.7	2.6	3.7	(1.2)	1.0
All other guaranteed loan programs	99.8	114.3	95.6	109.3	5.3	5.5	(0.1)	0.5
Total loan guarantee liabilities	2,643.2	2,538.1	1,960.3	1,919.1	38.2	42.9	(14.3)	12.5

The government has two types of loan programs: direct loans and loan guarantees. One major type of loan is direct loans such as the Education Federal Direct Student Loans. The second type is loan guarantee programs, such as the HUD's FHA Loans program.

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

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

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

Loan Programs

The majority of the loan programs are provided by Education, HUD, USDA, Small Business Administration (SBA), VA, and Export-Import (EXIM) Bank. For significant detailed information regarding the direct and guaranteed loan programs listed in the tables above, please refer to the financial statements of the entities.

Education has two major loan programs, authorized by Title IV of the *Higher Education Act of 1965*. The first program is the William D. Ford Federal Direct Loan Program, (referred to as the Direct Loan Program) that was established in fiscal year 1994. The Direct Loan Program offered four types of educational loans: Stafford, Unsubsidized Stafford, PLUS for parents and/or graduate or professional students, and consolidation loans. With this program, the government makes loans directly to students and parents through participating institutions of higher education. Direct loans are originated and serviced through contracts with private vendors. Education disbursed approximately $134.1 billion in Direct Loans to eligible borrowers in fiscal year 2018 and approximately $142.5 billion in fiscal year 2017. The second program is the FFEL Program. This program was established in fiscal year 1965, and is a guaranteed loan program. Like the Direct Loan Program, it offered four types of loans: Stafford, Unsubsidized Stafford, PLUS for parents and/or graduate or professional students, and consolidation loans. The *Student Aid and Fiscal Responsibility Act (SAFRA)*, which was enacted as part of the *Health Care Education and Reconciliation Act of 2010* (P.L. 111-152), eliminated the authority to guarantee new FFEL after June 30, 2010. During fiscal year 2018, Education net loans receivable increased by $64.1 billion, largely the result of increased Direct Loan Program disbursements for new loan originations and FFEL consolidations, net of borrower principal and interest collections.

HUD's Office of Housing plays a vital role for the nation's homebuyers, homeowners, renters, and communities through its nationally administered programs. It includes FHA, the largest mortgage insurer in the world. FHA provides over $1.3 trillion in mortgage insurance on mortgages for Single Family homes, Multifamily properties, and Healthcare facilities. In fiscal year 2018, HUD recognized material misstatements that resulted in corrections to certain prior year amounts reported on the Balance Sheet and Loans Receivable and Loans Guarantee Liabilities, Net (understated by $1.7 billion). Please refer to the Note 1 Restatements section for more information.

USDA's Rural Development offers both direct and guaranteed loans with unique missions to bring prosperity and opportunity to rural areas. The Rural Housing programs provide affordable, safe, and sanitary housing and essential community facilities to rural communities. Rural Utility programs help improve the quality of life in rural areas through a variety of loan programs for electric energy, telecommunications, and water and environmental projects.

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

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

VA operates the following direct loan and loan guarantee programs: Vendee Loans, Acquired Loans, Native American Direct Loans, Housing Guaranteed Loans, Vocational Rehabilitation and Employment Loans, Insurance Loans, and Loan Sale Guarantees. The VA Home Loans program is the largest of the VA loan guarantee programs. The Home Loans program provides loan guarantees and direct loans to veterans, service members, qualifying dependents, and limited non-veterans to purchase homes and retain homeownership with favorable market terms. During fiscal year 2018, the face value of outstanding principal on loans guaranteed by the VA increased by $67.2 billion. This increase was primarily due to $146.3 billion in new loans guaranteed by the VA, partially offset by $77.7 billion in guaranteed loan terminations.

Note 5. Inventories and Related Property, Net

Inventories and Related Property, Net as of September 30, 2018, and 2017

(In billions of dollars)	2018	Reclass 2017
Inventory purchased for resale	68.0	61.8
Inventory and operating material and supplies held for repair	71.1	67.1
Inventory—excess, obsolete, and unserviceable	0.8	0.9
Operating materials and supplies held for use	124.7	143.8
Operating materials and supplies held in reserve for future use	13.8	0.2
Operating materials and supplies-excess, obsolete, and unserviceable	2.9	2.5
Stockpile materials held in reserve for future use	51.9	49.3
Stockpile materials held for sale	4.6	5.1
Other related property	8.6	3.8
Allowance for loss	(8.9)	(7.8)
Total inventories and related property, net	337.5	326.7

Beginning in fiscal year 2018, all entities are now reported together in each line item total for Inventories and Related Property, Net. DOD comprises approximately 81.7 percent of the government's inventories and related property, net, as of September 30, 2018. DOD continues to implement SFFAS No. 48 which permits alternative methods in establishing opening balances for inventories and related property.

The following entities comprise over 98 percent of the government's reported inventories and related property, net of $337.5 billion as of September 30, 2018. Refer to each entities' financial statements for details.

- DOD
- DOE
- HHS

Note 6. Property, Plant, and Equipment, Net

Property, Plant, and Equipment as of September 30, 2018, and 2017

(In billions of dollars)	Cost	Accumulated Depreciation/ Amortization	Net	Cost	Accumulated Depreciation/ Amortization	Net
	2018			2017 Restated		
Buildings, structures, and facilities	728.4	431.1	297.3	692.6	406.9	285.7
Furniture, fixtures, and equipment	1,363.9	782.7	581.2	1,320.6	752.6	568.0
Construction in progress	159.5	N/A	159.5	168.2	N/A	168.2
Land	21.5	N/A	21.5	24.0	N/A	24.0
Other property, plant, and equipment	87.4	56.4	31.0	84.1	43.0	41.1
Total property, plant, and equipment, net	2,360.7	1,270.2	1,090.5	2,289.5	1,202.5	1,087.0

Beginning in fiscal year 2018, all entities are now reported together in each line item total for PP&E. DOD comprises approximately 69.6 percent of the government's reported property, plant, and equipment, net, as of September 30, 2018. DOD continues to implement SFFAS No. 50, *Establishing Opening Balances for General Property, Plant, and Equipment* which permits alternative methods in establishing opening balances for general PP&E. The total acreage of land and land rights excluded in this manner was 20,926,485 as of September 30, 2018.

In fiscal year 2017, restatements due to compilation errors in the presentation of the Balance Sheet and PP&E, net totaled $52.5 billion.

The following entities comprise over 90 percent of the government's reported PP&E net of $1,090.5 billion as of September 30, 2018. Please refer to the entities' financial statements for details.

- DOD
- DOE
- GSA
- VA
- TVA
- DOI
- State
- DOT
- USPS
- DHS
- NASA
- DOC
- DOJ
- HHS

Certain PP&E are multi-use heritage assets, see Note 24—Stewardship Land and Heritage Assets for additional information on multi-use heritage assets.

Note 7. Debt and Equity Securities

Debt and Equity Securities as of September 30, 2018

(In billions of dollars)	Cost	Adjustment	Book Value	Total
Held-To Maturity				
Debt securities:				
Non-U.S. government	-	-	-	
Mortgage/asset backed	0.2	-	0.2	
Equity Securities:				
All other equity securities	3.5	-	3.5	
Total Held-To-Maturity (Net Investment)	3.7	-	3.7	
Available-for-Sale:				
Debt Securities:	3.5	0.2	3.7	
Total Available-for-Sale (Fair Value)	3.5	0.2	3.7	
Trading Securities:				
Debt Securities:				
Non-U.S. government	12.9	(0.2)	12.7	
Commercial	0.2	-	0.2	
Mortgage/asset backed	3.8	(0.1)	3.7	
Corporate and other bonds	15.9	(0.2)	15.7	
All other debt securities	2.5	(1.0)	1.5	
Equity Securities:				
Unit Trust	16.3	9.5	25.8	
Common Stocks	2.0	0.3	2.3	
All other equity securities	14.3	0.9	15.2	
Total Trading Securities (Fair Value)	67.9	9.2	77.1	
Total debt and equity securities categorized as held-to-maturity, available-for-sale or trading				84.5
Total NRRIT debt and equity securities (Fair Value)				25.8
Total debt and equity securities				110.3

Debt and Equity Securities as of September 30, 2017

(In billions of dollars)	Cost	Adjustment	Book Value
Held-To Maturity			
Debt securities:			
Non-U.S. government	-	-	-
Mortgage/asset backed	0.2	-	0.2
Equity Securities:			
All other equity securities	3.6	-	3.6
Total Held-To-Maturity (Net Investment)	3.8	-	3.8
Available-for-Sale:			
Debt Securities:	5.4	0.2	5.6
Total Available-for-Sale (Fair Value)	5.4	0.2	5.6
Trading Securities:			
Debt Securities:			
Non-U.S. government	12.2	0.6	12.8
Commercial	0.2	-	0.2
Mortgage/asset backed	3.9	-	3.9
Corporate and other bonds	16.4	0.6	17.0
All other debt securities	4.0	(0.1)	3.9
Equity Securities:			
Unit Trust	18.0	8.2	26.2
Common Stocks	2.1	0.1	2.2
All other equity securities	15.2	(0.1)	15.1
Total Trading Securities (Fair Value)	72.0	9.3	81.3

	Total
Total debt and equity securities categorized as held-to-maturity, available-for-sale or trading	90.7
*Total RRB debt and equity securities (Fair Value)	25.5
Total debt and equity securities	116.2

*Includes amounts from NRRIT in 2017. In 2018, NRRIT amounts are reported separately.

These debt and equity securities do not include nonmarketable Treasury securities that have been eliminated in consolidation. Held-to-maturity debt and equity securities are reported as total net investment, net of unamortized discounts and premiums. Available-for-sale debt and equity securities are reported at fair value, net of unrealized gain or loss. Trading debt and equity securities are reported at fair value, net of unrealized gain or loss.

NRRIT on behalf of the RRB, manages and invests railroad retirement assets that are to be used to pay retirement benefits to the nation's railroad workers under the Railroad Retirement Program. As an investment company, NRRIT is subject to different accounting standards that do not require the classifications presented above. Please refer to NRRIT's financial statements for more detailed information concerning this specific investment.

Certain significant consolidation entities apply financial accounting and reporting standards issued by the Financial Accounting Standards Board (FASB) (FASB standards), and such entities, as permitted by SFFAS No.47, are consolidated into the U.S. government's consolidated financial statements without conversion to financial and reporting standards issued by the FASAB (FASAB standards). PBGC, NRRIT, and TVA debt and equity securities are recorded at fair value and have been categorized based upon a fair value hierarchy, in accordance with FASB ASC Section 820, Fair Value Measures and Disclosures, in their respective financial statements.

Debt and Equity Securities as of September 30, 2018, and 2017

(In billions of dollars)	2018	2017
Pension Benefit Guaranty Corporation	62.0	66.7
National Railroad Retirement Investment Trust	25.8	-
Tennessee Valley Authority	11.5	11.4
*Railroad Retirement Board	-	25.5
All other	11.0	12.6
Total securities and investments	110.3	116.2

*Includes amounts from NRRIT in 2017. In 2018, NRRIT amounts are reported separately.

PBGC and TVA invest primarily in fixed maturity and equity securities, classified as trading. PBGC reported an unrealized loss related to trading securities as of September 30, 2018 of $1.2 billion, and an unrealized gain related to trading securities as of September 30, 2017 of $3.3 billion. TVA reported gains related to trading securities held as of September 30, 2018 and 2017 of $1.6 billion and $1.2 billion, respectively. The TVA balance includes $8.4 billion and $8.5 billion as of September 30, 2018, and 2017, respectively, for the Tennessee Valley Authority Retirement System (TVARS). TVARS includes unrealized gains of $0.8 billion as of both September 30, 2018 and 2017. PBGC, NRRIT, and TVA base market values on the last sale of a listed security, on the mean of the “bid-and-ask” for nonlisted securities, or on a valuation model in the case of fixed income securities that are not actively traded. These valuations are determined as of the end of each fiscal year. Purchases and sales of securities are recorded on the trade date. Please refer to the individual financial statements of PBGC, NRRIT, and TVA for more detailed information related to debt and equity securities. These entities comprise 90.0 percent of the total reported debt and equity securities of $110.3 billion as of September 30, 2018.

Note 8. Investments in Government-Sponsored Enterprises

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

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

The purpose of such actions is to maintain the solvency of the GSEs so they can continue to fulfill their vital roles in the home mortgage market while the Administration and Congress determine what structural changes should be made to the housing finance system. Draws under the SPSPAs result in an increased investment in the GSEs as further discussed below. For fiscal year 2018, under SFFAS No. 47 criteria Fannie Mae and Freddie Mac were owned or controlled by the federal government only as a result of (a) regulatory actions (such as organizations in receivership or conservatorship) or (b) other federal government intervention actions. Under the regulatory or other intervention actions, the relationship with the federal government was and is not expected to be permanent. These entities are classified as disclosure entities based on their characteristics as a whole. Accordingly, these entities are not consolidated into the financial statements of the government; however, the value of the investments in these entities, changes in value, and related activity with these entities are included in the consolidated financial statements. This treatment is consistent with how these entities were reported prior to fiscal year 2018 under SFFAC No. 2, *Entity and Display*.

Senior Preferred Stock Purchase Agreements

Under the SPSPAs, Treasury initially received from each GSE: 1) 1,000,000 shares of non-voting variable liquidation preference senior preferred stock with a liquidation preference value of $1,000 per share and 2) a non-transferable warrant for the purchase, at a nominal cost, of 79.9 percent of common stock on a fully-diluted basis. The warrants expire on September 7, 2028. Under the amended SPSPAs, the quarterly dividend payment changed from a 10.0 percent per annum fixed rate dividend on the total liquidation preference (as discussed below) to an amount equivalent to the GSE's positive net worth above a capital reserve amount. The capital reserve amount, which was initially set at $3.0 billion for calendar year 2013, declined by $600 million at the beginning of each calendar year thereafter, and was scheduled to reach zero by calendar year 2018. On December 21, 2017, Treasury and the FHFA agreed to modify the SPSPAs between Treasury and the GSEs to increase the capital reserve amount for each GSE back to $3 billion, effective with the December 2017 dividend payment. In exchange for the increase in the capital reserve, Treasury's liquidation preference in each GSE increased by $3 billion on December 31, 2017. The GSEs will not pay a quarterly dividend if their positive net worth is below the required capital reserve threshold. Cash dividends of $9.9 billion and $25.3 billion were received during fiscal years ended September 30, 2018, and 2017, respectively.

The SPSPAs, which have no expiration date, require that Treasury will disburse funds to the GSEs if at the end of any quarter, the FHFA determines that the liabilities of either GSE exceed its assets. Draws from Treasury under the SPSPAs are designed to ensure that the GSEs maintain positive net worth, with a fixed maximum amount available to each GSE under this agreement established as of December 31, 2012 (refer to the "Contingent Liability to GSEs" section below and Note 18—Contingencies). Draws against the funding commitment of the SPSPAs do not result in the issuance of additional shares of senior preferred stock; instead, it increases the liquidation preference of the initial 1,000,000 shares by the amount of the draw. The combined cumulative liquidation preference totaled $199 billion and $189 billion as of September 30, 2018 and 2017, respectively. Actual payments of $4.0 billion were made to the GSEs for the fiscal year ended September 30, 2018. There were no payments to the GSEs for the fiscal year ended September 30, 2017.

Senior Preferred Stock and Warrants for Common Stock

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

The fair value of the senior preferred stock considers the amount of forecasted dividend payments. The fair valuations assume that a hypothetical buyer would acquire the discounted dividend stream as of the transaction date. The fair value of the senior preferred stock increased as of September 30, 2018 when compared to September 30, 2017, reflecting higher forecasted GSE net income, mainly driven by the reduction in the U.S. corporate tax rate resulting from the December 22, 2017 enactment of the *Tax Cuts and Jobs Act* (P.L. 115-97), a lower discount rate driven by lower volatility among comparable companies, as well as a reduction in the market value of the GSEs' other equity securities that comprise their total equity value.

Factors impacting the fair value of the warrants include the nominal exercise price and the large number of potential exercise shares, the market trading of the common stock that underlies the warrants as of September 30, the principal market, and the market participants. Other factors impacting the fair value include, among other things, the holding period risk related directly to the assumption of the amount of time that it will take to sell the exercised shares without depressing the market. The fair value of the warrants decreased at the end of fiscal year 2018, when compared to 2017, primarily due to decreases in the market price of the underlying common stock of each GSE.

Contingent Liability to GSEs

As part of the annual process undertaken by Treasury, a series of long-term financial forecasts are prepared to assess, as of September 30, the likelihood and magnitude of future draws to be required by the GSEs under the SPSPAs within the forecast time horizon. Treasury used 25-year financial forecasts prepared through years 2043 and 2042 in assessing if a contingent liability was required as of September 30, 2018 and 2017, respectively. If future payments under the SPSPAs are deemed to be probable within the forecast horizon, and Treasury can reasonably estimate such payment, they will accrue a contingent liability to the GSEs to reflect the forecasted equity deficits of the GSEs. This accrued contingent liability will be undiscounted and will not take into account any of the offsetting dividends that could be received, as the dividends, if any, would be owed directly to the General Fund. Such recorded accruals will be adjusted in subsequent years as new information develops or circumstances change. If future payments are reasonably possible, they are disclosed but not recorded as an accrued contingent liability.

Based on the annual forecasts as of September 30, 2018 and 2017, Treasury estimated there was no probable future funding draws. As of September 30, 2018, it is reasonably possible that market volatility or non-recurring events—for instance, changes to accounting policies that impact credit loss provisions—could potentially cause the GSEs to generate quarterly losses and, therefore, result in future funding draws against the funding commitment. Due to challenges quantifying future market volatility or the timing, magnitude, and likelihood of non-recurring events, the total amount of this reasonably possible future funding liability could not be estimated as of September 30, 2018.

P.L. 115-97 caused each GSE to reduce the value of its deferred tax assets in the quarter in which the legislation was enacted. The reduction of the GSEs deferred tax assets resulted in $4.0 billion in actual payments made to the GSEs to ensure they maintained positive net worth, which reduced the remaining funding commitment. At September 30, 2018 and 2017, the maximum remaining funding commitment to the GSEs for the remaining life of the SPSPAs was $254.1 billion and $258.1 billion, respectively. Subsequent funding draws will reduce the remaining commitments. Refer to Note 19—Commitments for a full description of other commitments and risks.

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

Estimation Factors

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

Regulatory Environment

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

The *Temporary Payroll Tax Cut Continuation Act of 2011*(P.L. 112-78) was funded by an increase of ten basis points in the GSEs' guarantee fees (referred to as "the incremental fees") which began in April 2012 and is effective through October 1, 2021. The incremental fees are to be remitted to Treasury and not retained by the GSEs and, thus, do not affect the profitability of the GSEs. For fiscal years 2018 and 2017, the GSEs remitted to Treasury the incremental fees totaling $3.6 billion and $3.2 billion, respectively.

As of September 30, 2018, and 2017, GSEs investments consisted of the following:

Investments in GSEs as of September 30, 2018

(In billions of dollars)	Gross Investments	Cumulative Valuation Gain/(Loss)	Fair Value
Fannie Mae senior preferred stock	123.7	(64.5)	59.2
Freddie Mac senior preferred stock	75.4	(31.2)	44.2
Fannie Mae warrants common stock	3.1	3.2	6.3
Freddie Mac warrants common stock	2.3	1.2	3.5
Total investments in GSEs	204.5	(91.3)	113.2

Investments in GSEs as of September 30, 2017

(In billions of dollars)	Gross Investments	Cumulative Valuation Gain/(Loss)	Fair Value
Fannie Mae senior preferred stock	117.0	(74.5)	42.5
Freddie Mac senior preferred stock	72.1	(41.0)	31.1
Fannie Mae warrants common stock	3.1	9.2	12.3
Freddie Mac warrants common stock	2.3	4.4	6.7
Total investments in GSEs	194.5	(101.9)	92.6

Note 9. Other Assets

Other Assets as of September 30, 2018, and 2017

(In billions of dollars)	2018	2017
Advances and prepayments	70.0	97.4
Regulatory assets	17.3	20.0
Investments in Multilateral Development Banks	7.7	7.7
FDIC receivable from resolution activity, net	3.0	9.3
Other	15.7	13.3
Total other assets	113.7	147.7

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

With regard to regulatory assets, the DOE's Power Marketing Administrations (PMAs) and TVA record certain amounts as assets in accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Topic 980, *Regulated Operations*. The provisions of FASB ASC Topic 980 require that regulated enterprises reflect rate actions of the regulator in their financial statements, when appropriate. These rate actions can provide reasonable assurance of the existence of an asset, reduce or eliminate the value of an asset, or impose a liability on a regulated enterprise. In order to defer incurred costs under FASB ASC Topic 980, a regulated entity must have the statutory authority to establish rates that recover all costs, and those rates must be charged to and collected from customers. If the PMAs' or TVA's rates should become market-based, FASB ASC Topic 980 would no longer be applicable, and all of the deferred costs under that standard would be expensed.

On behalf of the U.S., Treasury invests in certain Multilateral Development Banks (MDB), through subscriptions to capital, which allows the MDBs to issue loans at market-based rates to middle-income developing countries. These paid-in capital investments are non-marketable equity investments valued at cost.

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

Other items included in "other" are contract financing payments and estimated future payments to contractors, purchased power generating capacity, deferred nuclear generating units, derivative assets, the balance of assets held by the experience rated carriers participating in the Health Benefits and Life Insurance Program (pending disposition on behalf of OPM), and the cost contribution to buildout the Nationwide Public Safety Broadband.

Note 10. Accounts Payable

Accounts Payable as of September 30, 2018, and 2017

(In billions of dollars)	2018	2017
Department of Defense	29.2	26.4
Department of Veterans Affairs	13.5	3.6
Department of Justice	5.1	6.0
Department of the Treasury	3.8	3.9
Department of Education	3.8	4.2
Department of Energy	3.7	3.7
Department of State	3.6	2.7
General Services Administration	3.1	2.8
Department of Homeland Security	2.5	2.3
U.S. Agency for International Development	2.4	1.8
Department of Commerce	2.0	0.4
Department of Agriculture	1.9	1.8
U.S. Postal Service	1.8	1.6
Tennessee Valley Authority	1.8	1.8
All other	8.5	7.8
Total accounts payable	86.7	70.8

Accounts payable includes amounts due for goods and property ordered and received, services rendered by other than federal employees, cancelled appropriations for which the U.S. government has contractual commitments for payment, and non-debt related interest payable.

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

Federal Debt Securities Held by the Public and Accrued Interest

(In billions of dollars)	Balance September 30, 2017	Net Change During Fiscal Year 2018	Balance September 30, 2018	Average Interest Rate 2018	Average Interest Rate 2017
Treasury securities (public):					
Marketable securities:					
Treasury bills	1,799.6	439.9	2,239.5	2.1%	1.1%
Treasury notes	8,798.9	351.4	9,150.3	2.0%	1.8%
Treasury bonds	1,948.4	166.6	2,115.0	4.1%	4.2%
Treasury inflation-protected securities (TIPS)	1,286.1	90.1	1,376.2	0.8%	0.8%
Treasury floating rate notes (FRN)	342.6	26.5	369.1	2.2%	1.2%
Total marketable Treasury securities	14,175.6	1,074.5	15,250.1		
Nonmarketable securities	497.8	13.3	511.1	2.8%	2.3%
Net unamortized premiums/(discounts)	(39.2)	(5.6)	(44.8)		
Total Treasury securities, net (public)	14,634.2	1,082.2	15,716.4		
Agency securities:					
Tennessee Valley Authority	23.9	(1.5)	22.4		
All other agencies	0.1	-	0.1		
Total agency securities, net of unamortized premiums and discounts	24.0	(1.5)	22.5		
Accrued interest payable	65.9	7.9	73.8		
Total federal debt securities held by the public and accrued interest	14,724.1	1,088.6	15,812.7		

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

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

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

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

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

During fiscal years 2018 and 2017, Treasury faced two delays in raising the statutory debt limit that required it to depart from its normal debt management procedures and to invoke legal authorities to avoid exceeding the statutory debt limit. During these periods, extraordinary actions taken by Treasury have resulted in federal debt securities not being issued to certain federal government accounts with the securities being restored including lost interest to the affected federal government accounts subsequent to the end of the delay period. The first delay occurred from March 16, 2017 through September 7, 2017. On Friday, September 8, 2017 the *Continuing Appropriations Act, 2018 and Supplemental Appropriations for Disaster Relief Requirements Act, 2017* (P.L. 115-56) was enacted suspending the statutory debt limit through December 8, 2017. The second delay in raising the statutory debt limit occurred from December 9, 2017 through February 8, 2018. On Friday, February 9, 2018, the *Bipartisan Budget Act (BBA) of 2018* (P.L. 115-123) was enacted suspending the statutory debt limit through March 1, 2019.

As of September 30, 2018, and 2017, debt subject to the statutory debt limit was $21,474.8 billion and $20,208.6 billion, respectively. The debt subject to the limit includes Treasury securities held by the public and government guaranteed debt of federal agencies (shown in the table above) and intragovernmental debt holdings (shown in the following table). See Note 26─Subsequent Events for additional information.

Intragovernmental Debt Holdings: Federal Debt Securities Held as Investments by Government Accounts as of September 30, 2018, and 2017

(In billions of dollars)	Balance 2017	Net Change During Fiscal Year 2018	Balance 2018
Social Security Administration, Federal Old-Age and Survivors Insurance Trust Fund	2,820.2	(18.9)	2,801.3
Office of Personnel Management, Civil Service Retirement and Disability Fund	905.1	17.9	923.0
Department of Defense, Military Retirement Fund	661.0	82.4	743.4
Department of Defense, Medicare-Eligible Retiree Health Care Fund	225.8	14.4	240.2
Department of Health and Human Services, Federal Hospital Insurance Trust Fund	197.8	5.0	202.8
Department of Health and Human Services, Federal Supplementary Medical Insurance Trust Fund	70.6	27.6	98.2
Federal Deposit Insurance Corporation, Deposit Insurance Fund	80.2	16.2	96.4
Social Security Administration, Federal Disability Insurance Trust Fund	69.7	23.7	93.4
Department of Labor, Unemployment Trust Fund	60.7	11.9	72.6
Department of Energy, Nuclear Waste Disposal Fund	53.0	0.4	53.4
Office of Personnel Management, Postal Service Retiree Health Benefits Fund	49.5	(2.4)	47.1
Office of Personnel Management, Employees Life Insurance Fund	45.7	0.9	46.6
Department of Transportation, Highway Trust Fund	52.3	(11.1)	41.2
Pension Benefit Guaranty Corporation	28.4	3.3	31.7
Office of Personnel Management, Employees Health Benefits Fund	26.0	1.4	27.4
Department of Housing and Urban Development, FHA, Mutual Mortgage Insurance Capital Reserve Account	30.9	(3.9)	27.0
Department of the Treasury, Exchange Stabilization Fund	22.1	0.2	22.3
Department of State, Foreign Service Retirement and Disability Fund	18.8	0.4	19.2
Department of Housing and Urban Development, Guarantees of Mortgage-Backed Securities Capital Reserve Account	17.1	(0.9)	16.2
National Credit Union Share Insurance Fund	13.1	1.8	14.9
Department of Transportation, Airport and Airway Trust Fund	13.4	0.8	14.2
U.S. Postal Service, Postal Service Fund	11.0	(0.5)	10.5
All other programs and funds	99.1	12.9	112.0
Subtotal	5,571.5	183.5	5,755.0
Total net unamortized premiums/(discounts) for intragovernmental	72.2	(2.3)	69.9
Total intragovernmental debt holdings, net	5,643.7	181.2	5,824.9

Intragovernmental debt holdings represent the portion of the gross federal debt held as investments by government entities such as trust funds, revolving funds, and special funds.

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

Note 12. Federal Employee and Veteran Benefits Payable

Federal Employee and Veteran Benefits Payable as of September 30, 2018, and 2017

(In billions of dollars)	Civilian 2018	Civilian Reclass 2017	Military 2018	Military 2017	Total 2018	Total Reclass 2017
Pension and accrued benefits	2,048.9	2,013.8	1,621.3	1,568.0	3,670.2	3,581.8
Veterans compensation and burial benefits	N/A	N/A	2,956.3	2,810.0	2,956.3	2,810.0
Post-retirement health and accrued benefits	403.3	375.7	787.0	781.6	1,190.3	1,157.3
Veterans education benefits	N/A	N/A	65.7	50.7	65.7	50.7
Life insurance and accrued benefits	54.9	53.1	6.3	6.9	61.2	60.0
FECA benefits	27.3	28.8	8.3	8.3	35.6	37.1
Liability for other benefits	1.2	1.2	1.8	2.0	3.0	3.2
Total federal employee and veteran benefits payable	2,535.6	2,472.6	5,446.7	5,227.5	7,982.3	7,700.1

Change in Pension and Accrued Benefits

(In billions of dollars)	Civilian 2018	Civilian 2017	Military 2018	Military 2017	Total 2018	Total 2017
Actuarial accrued pension liability, beginning of fiscal year	2,013.8	1,910.7	1,568.0	1,490.6	3,581.8	3,401.3
Pension expense:						
Prior (and past) service costs from plan amendments or new plans	-	-	8.9	(0.9)	8.9	(0.9)
Normal costs	42.3	38.8	34.2	27.4	76.5	66.2
Interest on liability	68.7	69.5	57.5	57.6	126.2	127.1
Actuarial (gains)/losses (from experience)	(2.0)	(12.0)	9.6	(1.6)	7.6	(13.6)
Actuarial (gains)/losses (from assumption changes)	15.8	94.3	2.1	52.9	17.9	147.2
Other	0.1	-	-	-	0.1	-
Total pension expense	124.9	190.6	112.3	135.4	237.2	326.0
Less benefits paid	(89.8)	(87.5)	(59.0)	(58.0)	(148.8)	(145.5)
Actuarial accrued pension liability, end of fiscal year	2,048.9	2,013.8	1,621.3	1,568.0	3,670.2	3,581.8

Change in Post-Retirement Health and Accrued Benefits

(In billions of dollars)	Civilian 2018	Civilian 2017	Military 2018	Military 2017	Total 2018	Total 2017
Actuarial accrued post-retirement health benefits liability, beginning of fiscal year	375.7	352.3	781.6	799.7	1,157.3	1,152.0
Post-Retirement health benefits expense:						
Prior (and past) service costs from plan amendments or new plans	-	-	(20.9)	-	(20.9)	-
Normal costs	15.8	13.4	20.5	20.5	36.3	33.9
Interest on liability	14.1	13.9	30.0	32.3	44.1	46.2
Actuarial (gains)/losses (from experience)	0.7	4.5	(17.2)	(20.6)	(16.5)	(16.1)
Actuarial (gains)/losses (from assumption changes)	12.9	7.5	14.7	(28.8)	27.6	(21.3)
Total post-retirement health benefits expense	43.5	39.3	27.1	3.4	70.6	42.7
Less claims paid	(15.9)	(15.9)	(21.7)	(21.5)	(37.6)	(37.4)
Actuarial accrued post-retirement health benefits liability, end of fiscal year	403.3	375.7	787.0	781.6	1,190.3	1,157.3

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

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

Change in Civilian Life Insurance and Accrued Benefits

(In billions of dollars)	2018	2017
Actuarial accrued life insurance benefits liability, beginning of fiscal year	53.1	50.9
Life insurance benefits expense:		
New entrant expense	0.6	0.4
Interest on liability	1.9	1.9
Actuarial (gains)/losses (from experience)	(0.6)	(0.4)
Actuarial (gains)/losses (from assumption changes)	0.5	0.9
Total life insurance benefits expense	2.4	2.8
Less costs paid	(0.6)	(0.6)
Actuarial accrued life insurance benefits liability, end of fiscal year	54.9	53.1

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

	Civilian				Military	
	2018		2017		2018	2017
	FERS	CSRS	FERS	CSRS		
Rate of interest	3.60%	3.00%	3.80%	3.20%	3.50%	3.70%
Rate of inflation	1.60%	1.60%	1.80%	1.80%	1.50%	1.70%
Projected salary increases	1.30%	1.30%	1.50%	1.50%	2.00%	2.10%
Cost of living adjustment	1.40%	1.60%	1.40%	1.80%	N/A	N/A

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

	Civilian		Military	
	2018	2017	2018	2017
Rate of interest	3.60%	3.80%	3.60%	3.80%
Single equivalent medical trend rate	4.50%	4.80%	4.16%	4.12%
Ultimate medical trend rate	3.20%	3.40%	4.00%	4.20%

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

	Civilian	
	2018	2017
Rate of interest	3.40%	3.60%
Rate of increase in salary	1.30%	1.50%

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

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

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

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

Civilian Employees

Pensions

OPM administers the largest civilian pension plan, which covers substantially all full-time, permanent civilian federal employees. This plan includes two components of defined benefits, the Civil Service Retirement System (CSRS) and the Federal Employees' Retirement System (FERS). The basic benefit components of the CSRS and the FERS are financed and operated through the Civil Service Retirement and Disability Fund (CSRDF), a trust fund. CSRDF monies are generated primarily from employees' contributions, federal entity contributions, payments from the General Fund, and interest on investments in Treasury securities. As of September 30, 2018, USPS has accrued, but not paid OPM, $5.6 billion in CSRS and FERS retirement benefit expenses since 2014.

The Federal Retirement Thrift Investment Board (FRTIB) administers the Thrift Savings Plan (TSP). The TSP investment options include two fixed income funds (the G and F Funds), three stock funds (the C, S, and I Funds) and five lifecycle funds (L 2050, L 2040, L 2030, L 2020, and L Income). The L Funds diversify participant accounts among the G, F, C, S, and I Funds, using professionally determined investment mixes (allocations) that are tailored to different time horizons. Treasury securities held in the G Fund are included in federal debt securities held by the public and accrued interest on the Balance Sheet. The G Fund held $245.5 billion and $217.9 billion in nonmarketable Treasury securities as of September 30, 2018, and 2017, respectively.

The liability for civilian pension and accrued benefits payable increased $35.1 billion. This increase is partly attributable to changes in actuarial assumptions. The assumption loss results primarily from decreases to the assumed rates of interest, which was partly offset by a modest gain from changes in demographic assumptions.

Post-Retirement Health Benefits

The post-retirement civilian health benefit liability is an estimate of the government's future cost of providing post-retirement health benefits to current employees and retirees. Although active and retired employees pay insurance premiums under the Federal Employees Health Benefits Program, these premiums cover only a portion of the costs. The OPM actuary applies economic and demographic assumptions to historical cost information to estimate the liability.

The *Postal Accountability and Enhancement Act of 2006* (Postal Act of 2006) (P.L. No 109-435, Title VIII), made significant changes in the funding of future retiree health benefits for employees of the USPS, including the requirement for the USPS to make scheduled payments to the Postal Service Retiree Health Benefits (PSRHB) Fund. Various legislation required the USPS to make scheduled payments to the PSRHB Fund ranging from $5.4 billion to $5.8 billion per year from fiscal year 2007 through fiscal year 2016. Thereafter, the law required USPS to make annual payments in the amount of the normal cost plus or minus an amount to amortize the unfunded liability or surplus. USPS currently owes the PSRHB Fund a total of $42.6 billion consisting of $38.2 billion for fiscal years 2011 through 2017 and $4.4 billion for fiscal year 2018. As of September 30, 2018, USPS has indicated payment of the total $42.6 billion due will remain open. At this time, Congress has not taken further action on these payments due to the PSRHB Fund from USPS. The cost for each year's payment, including any defaulted payment, along with all other benefit program costs, are included in USPS' net cost for that year in the consolidated Statements of Net Cost. The liability is not included on the governmentwide balance sheet due to the USPS liability being eliminated with the OPM receivable.

The post-retirement civilian health benefit liability increased $27.6 billion. This increase is due to the accruing cost of benefits, interest on the existing liability and an actuarial loss primarily attributable to updated demographic assumptions used in the fiscal year 2018 calculation.

Life Insurance Benefits

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

Workers' Compensation Benefits

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

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

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

The COLAs and CPIMs used in the projections for fiscal year 2018 are listed below in the table.

Fiscal Year	COLA	CPIM
2019	1.31%	3.21%
2020	1.51%	3.48%
2021	1.89%	3.68%
2022	2.16%	3.71%
2023+	2.21%	4.09%

DOL selected the interest rate assumptions whereby projected annual payments were discounted to present value based on interest rate assumptions on the TNC Yield Curve to reflect the average duration of income payments and medical payments. The average durations for income payments and medical payments were 14.7 years and 9.6 years, respectively. Based on averaging the TNC Yield Curves for the current and prior four years, the interest rate assumptions for income payments and medical payments were 2.72% and 2.38%, respectively.

For the COLAs, CPIMs, average durations, and interest rate assumptions used in the projections for fiscal year 2017, refer to the fiscal year 2017 *Financial Report.*

Military Employees (Including Veterans)

Pensions

The Military Retirement System consists of a funded, noncontributory, defined benefit plan for military personnel (Services of Army, Navy, Air Force, and the Marine Corps) with an entry date prior to January 1, 2018 and the Blended Retirement System (BRS), generally for military personnel with an entry date on or after January 1, 2018. The defined benefit plan includes non-disability retired pay, disability retired pay, survivor annuity programs, and Combat-Related Special Compensation. The Service Secretaries may approve immediate non-disability retired pay at any age with credit of at least 20 years of active duty service. Reserve retirees must be at least 60 years old and have at least 20 qualifying years of service before retired pay commences; however, in some cases, the age can be less than 60 if the reservist performs certain types of active service. P.L. 110-181 provides for a 90-day reduction in the reserve retirement age from age 60 for every 3 months of certain active duty service served within a fiscal year for service after January 28, 2008 (not below age 50). There is no vesting of defined benefits before non-disabled retirement. There are distinct non-disability benefit formulas related to four populations within the Military Retirement System: Final Pay, High-3, Career Status Bonus/Redux, and the BRS enacted in the *National Defense Authorization Act for Fiscal Year 2016*, effective January 1, 2018. The BRS is a new retirement benefit merging aspects of both a defined benefit annuity with a defined contribution account, through the TSP. The date an individual enters the military generally determines which retirement system they would fall under and if they have the option to select, via a one-time irrevocable election, their retirement system. Military personnel with a start date on or after January 1, 2018 are automatically enrolled in BRS. Although all members serving as of December 31, 2017 were grandfathered under the prior retirement system, Active Duty, National Guard and Reserve personnel meeting established criteria may opt into BRS during calendar year 2018. Under the BRS, retiring members are given the option to receive a portion of their retired pay annuity in the form of a lump sum distribution. For more information on these benefits, see DOD's Office of Military Compensation website https://militarypay.defense.gov.

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

The $53.3 billion increase in the Military Retirement Pension liability is attributable to the increase from expected normal and interest costs offset by benefit payments, with additional impacts due to assumption and benefit changes and actuarial experience. Liabilities in the future will depend on interest costs and benefit accruals, future benefit changes, assumption changes, and actuarial experience.

Post-Retirement Health Benefits

Military retirees who are not yet eligible for Medicare (and their eligible non-Medicare eligible dependents) are eligible for post-retirement medical coverage provided by DOD. Depending on the benefit plan selected, retirees and their eligible dependents may receive care from military treatment facilities (MTFs) on a space-available basis or from civilian providers. This TRICARE coverage is available as Select (a preferred provider organization – a health plan that contracts with medical providers to create a network of participating providers; member cost-shares are typically higher for services received out-of-network) and PRIME (a health maintenance organization- a health plan that limits services to a specific network of medical personnel and facilities and usually by requiring referral by a primary-care physician for specialty care; coverage is also available for non-referred and out-of-network care, subject to higher cost-sharing). These postretirement medical benefits are paid by the Defense Health Agency on a pay-as-you-go basis.

Since fiscal year 2002, DOD has provided medical coverage to Medicare-eligible retirees (and their eligible Medicare-eligible dependents). This coverage, called TRICARE for Life (TFL), is a Medicare Supplement plan which includes inpatient, outpatient and pharmacy coverage. Enrollment in Medicare Part B is required to maintain eligibility in TFL. Retirees with TFL coverage can obtain care from MTFs on a space-available basis or from civilian providers.

10 U.S.C., Chapter 56 created the DOD Medicare-Eligible Retiree Health Care Fund (MERHCF), which became operative on October 1, 2002. The purpose of this fund is to account for and accumulate funds for the health benefit costs of Medicare-eligible military retirees, and their dependents and survivors who are Medicare eligible. The Fund receives revenues from three sources: interest earnings on MERHCF assets, Uniformed Services normal cost contributions, and Treasury contributions. The DOD Medicare-Eligible Retiree Health Care Board of Actuaries (the MERHCF Board) approves the methods and assumptions used in actuarial valuations of the MERHCF for the purpose of calculating the per capita normal cost rates (to fund the annual accrued benefits) and determining the unfunded liability amortization payment (the U.S. Treasury contribution). The Secretary of Defense directs the Secretary of Treasury to make DOD's normal cost payments. The MERHCF pays for medical costs incurred by Medicare-eligible beneficiaries at MTFs and civilian providers (including payments to U.S. Family Health Plans for grandfathered beneficiaries), plus the costs associated with claims administration.

DOD's actuaries calculate the actuarial liabilities annually using assumptions and experience (e.g., mortality and retirement rates, health care costs, medical trend rates, and the discount rate). Actuarial liabilities are calculated for all DOD retiree medical benefits, including both the benefits funded through the MERHCF as well as the benefits for pre-Medicare retirees who are paid on a pay-as-you-go basis. Military post-retirement health and accrued benefits payable increased $5.4 billion. This increase is due primarily to changes in actuarial assumptions and expected normal and interest costs, offset by changes due to plan amendments and favorable recent claims experience. The $20.9 billion reduction in the liability due to plan amendments reflects the estimated savings resulting from change to pharmacy copays enacted in the *National Defense Authorization Act for Fiscal Year 2018*, effective February 1, 2018.

In addition to the health care benefits the federal government provides for civilian and military retirees and their dependents, the VA also provides medical care to veterans on an "as available" basis, subject to the limits of the annual appropriations. In accordance with 38 CFR 17.36 (c), VA's Secretary makes an annual enrollment decision that defines the veterans, by priority, who will be treated for that fiscal year subject to change based on funds appropriated, estimated collections, usage, the severity index of enrolled veterans, and changes in cost. While VA expects to continue to provide medical care to veterans in future years, an estimate of such future benefits cannot be reasonably made. Accordingly, medical care expenses are recognized in the period the medical care services are provided and included on the Statement of Net Cost. For the fiscal years 2014 through 2018, the average medical care cost per year was $63.2 billion.

Veterans Compensation and Burial Benefits

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

Eligible veterans who die or are disabled during active military service-related causes, as well as their dependents, and dependents of service members who died during active military service, receive compensation benefits. In addition, service members who die during active military service and veterans who separated under other than dishonorable conditions are provided with a burial flag, headstone/marker, and grave liner for burial in a VA national cemetery or are provided a burial flag, headstone/marker and a plot allowance for burial in a private cemetery. These benefits are provided under 38 U.S.C., Part 2, Chapter 23 in recognition of a veteran's military service and are recorded as a liability in the period the requirements are met.

The liability for veterans' compensation and burial benefits payable is based on an actuarial estimate of future compensation and burial payments. It increased by $146.3 billion in fiscal year 2018. The $146.3 billion increase is primarily attributable to assumption changes and experience. The major impact from experience changes was from veterans who first became eligible for benefits during fiscal year 2018. The major impact from assumption changes was from a decrease in the discount rate. Several significant actuarial assumptions were used in the valuation of compensation and burial benefits to calculate the present value of the liability. A liability was recognized for the projected benefit payments to: 1) those beneficiaries, including veterans and survivors, currently receiving benefit payments; 2) current veterans who will in the future become beneficiaries of the compensation program; and 3) a proportional share of those in active military service as of the valuation date who are expected to be future veterans. Future benefit payments to survivors of those veterans in classes 1, 2, and 3 above are also incorporated into the projection. The projected liability does not include any administrative costs.

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

Change in Veterans Compensation and Burial Benefits

	Compensation		Burial		Total	
(In billions of dollars)	2018	2017	2018	2017	2018	2017
Actuarial accrued liability, beginning of fiscal year	2,805.1	2,491.4	4.9	4.9	2,810.0	2,496.3
Current year expense:						
Interest on the liability balance	102.7	97.9	0.2	0.2	102.9	98.1
Prior (and past) service costs from program amendments or new programs during the period	14.3	-	-	-	14.3	-
Actuarial (gains)/losses (from experience)	45.5	50.7	(0.1)	(0.2)	45.4	50.5
Actuarial (gains)/losses (from assumption changes)	66.8	244.3	2.4	0.2	69.2	244.5
Total current year expense	229.3	392.9	2.5	0.2	231.8	393.1
Less benefits paid	(85.3)	(79.2)	(0.2)	(0.2)	(85.5)	(79.4)
Actuarial accrued liability, end of fiscal year	2,949.1	2,805.1	7.2	4.9	2,956.3	2,810.0

Significant Economic Assumptions Used in Determining Veterans Compensation and Burial Benefits as of September 30, 2018, and 2017

	2018	2017
Rate of interest	3.52%	3.66%
Rate of inflation	2.28%	2.28%

Veterans Education Benefits

For eligible Veterans and their dependents, the VA provides four education/retraining type programs:

- Post 9/11 GI Bill
- Montgomery GI Bill-Active Duty
- Vocational Rehabilitation and Employment
- Dependent Education Assistance

The total liability for the four education/training programs is based on actuarial estimates of future payments and increased by $15.0 billion in fiscal year 2018. The $15.0 billion increase is primarily attributable to assumption changes and experience. The major impact from experiences changes was from veterans who first became eligible for benefits during fiscal year 2018. The major impact from assumption changes was from a $12.0 billion adjustment made outside of the model to account for potential new enrollees in the next year. This adjustment was based on the number of new enrollees who began to use their Post-9/11 GI Bill benefits in 2018. The actuarial modeling estimates are based on beneficiaries who have already started to use those benefits. Currently, these models do not include assumptions for expected future new beneficiaries as an input to calculate the estimated liability. However, based on experience, it is probable that new beneficiaries will enroll in these programs in the future. As of September 30, 2018, VA has not developed a practical way to estimate the future number of new beneficiaries in its models, in accordance to SFFAS No. 5. Since these models have only been placed in operation for the past two years, enhancements and studies such as assumption revisions and possibility of inclusion of multiple years of future enrollees in the models will be examined. Results of these enhancements and studies may lead to significant changes in the future liabilities.

In fiscal year 2016, VA reported an estimated liability for the Post 9/11 GI Bill of $59.6 billion. This was the first time VA had reported this estimated liability and the models and assumptions used were conservative with limited experience studies or assumptions. At that time, VA had not developed models or estimates for the other three programs listed; however, it was management’s assertion that the amount recorded for the Post 9/11 GI Bill was large enough to include any liability for the other three programs. In fiscal year 2017, VA broke out each program and developed individual estimates based on actuarial standards. While not reported in 2016, VA developed an estimate for fiscal year 2016 for each of the new programs to be used for comparisons only in 2017. This estimate reflected an increase in the liability of $8.7 billion. This amount is presented as "Other" for fiscal year 2017 in the schedule of "Changes in Veterans Education Benefits" provided below.

The fiscal year 2017 Actuarial (gains)/losses from assumption changes included the impacts of refinements to the modeling of the Post 9/11 GI Bill program (liability decrease of $29.3 billion); prior service costs associated with the “Forever GI Bill of 2017,” which eliminated the 15-year limitation for using the benefit (liability increase of $8.2 billion); and other assumption changes (liability increase of $6.3 billion).

For details regarding actuarial assumptions and the four education/retraining type programs, please refer to VA’s financial statements.

Change in Veterans Education Benefits

(In billions of dollars)	2018	2017
Actuarial accrued liability, beginning of fiscal year	50.7	59.6
Current year expense:		
Interest on liability	1.3	0.7
Actuarial (gains)/losses (from experience)	14.6	9.3
Actuarial (gains)/losses (from assumption changes)	10.0	(14.8)
Other	-	8.7
Total current year expense	25.9	3.9
Less benefits paid	(10.9)	(12.8)
Actuarial accrued liability, end of fiscal year	65.7	50.7

Life Insurance Benefits

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

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

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

Veterans Life Insurance Liability as of September 30, 2018, and 2017

(In billions of dollars)	2018	2017
Insurance death benefits:		
NSLI	2.3	2.8
VSLI	1.1	1.2
S-DVI	0.7	0.7
Other	0.3	0.3
Total death benefits	4.4	5.0
Death benefit annuities	-	-
Disability income & waiver	0.8	0.8
Insurance dividends payable	0.9	1.1
Unpaid policy claims	0.2	-
Total veterans life insurance liability	6.3	6.9

Insurance dividends payable consists of dividends left on deposit with VA, related interest payable, and dividends payable to policyholders. Unpaid policy claims consists of insurance claims that are pending at the end of the reporting period, an estimate of claims that have been incurred but not yet reported, and disbursements in transit.

The VA supervises Service members Group Life Insurance (SGLI) and Veterans Group Life Insurance programs that provide life insurance coverage to members of the uniformed armed services, reservists, and post-Vietnam Veterans as well as their families. VA has entered into a group policy with the Prudential Insurance Company of America to administer and provide the insurance payments under these programs. All SGLI insureds are automatically covered under the Traumatic

Injury Protection program, which provides for insurance payments to veterans who suffer a serious traumatic injury in service.

Pension Benefits

The VA also provides certain veterans and/or their dependents with pension benefits, based on annual eligibility reviews. The pension program for veterans is not accounted for as a "federal employee pension plan" under SFFAS No. 5 due to differences between its eligibility conditions and those of federal employee pensions. Therefore, a future liability for pension benefits is not recorded. VA pension liabilities are recognized when due and payable. The projected amounts of future payments for pension benefits (presented for informational purposes only) as of September 30, 2018, and 2017, was $104.8 billion and $87.6 billion, respectively.

Note 13. Environmental and Disposal Liabilities

Environmental and Disposal Liabilities as of September 30, 2018, and 2017

(In billions of dollars)	**2018**	**2017**
Department of Energy	494.0	383.8
Department of Defense	70.4	68.3
All other entities	12.9	12.4
Total environmental and disposal liabilities	577.3	464.5

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

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

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

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

DOE's environmental and disposal liabilities also include the estimated cleanup and post-closure responsibilities, including surveillance and monitoring activities, soil and groundwater remediation, and disposition of excess material for sites. The Department is responsible for the post-closure activities at many of the closure sites as well as other sites. The costs for these post-closure activities are estimated for a period of 75 years after the balance sheet date, i.e., through 2093 in fiscal year 2018 and through 2092 in fiscal year 2017. While some post-cleanup monitoring and other long-term stewardship activities post-2093 are included in the liability, there are others DOE expects to continue beyond 2093 for which the costs cannot reasonably be estimated.

A portion of DOE's environmental and disposal liabilities at various field sites includes anticipated costs for facilities managed by DOE's ongoing program operations which will ultimately require stabilization, deactivation, and decommissioning. The estimate is largely based upon a cost-estimating model. Site specific estimates are used in lieu of the cost-estimating model, when available. Cost estimates for ongoing program facilities are updated each year. For facilities newly contaminated since fiscal year 1997, cleanup costs allocated to future periods and not included in environmental and disposal liabilities amounted to $0.9 billion for both fiscal years 2018 and 2017.

The predominant change in the DOE's environmental liabilities estimates in fiscal year 2018 resulted from Waste Treatment and Immobilization Plant (WTP) construction and operating costs, and the updated tank farm retrieval and closure cost. Other changes resulted from inflation adjustments to reflect constant dollars for the current year; improved and updated estimates for the same scope of work, including changes resulting from deferral or acceleration of work; revisions in technical approach or scope, including additional contamination; updated estimates of projected waste volumes; changes in the DOE's allocable percentage share of future costs; legal and regulatory changes; and cleanup activities performed.

On October 9, 2018, the U.S. Court of Appeals for the Fourth Circuit lifted the Preliminary Injunction, allowing DOE to move forward with termination of construction of the Mixed Oxide (MOX) facility. With termination of the MOX facility, which was the fiscal year 2018 approach for plutonium disposition, DOE will pursue a Dilute and Dispose approach in fiscal year 2019. The lower cost of the Dilute and Dispose approach is expected to reduce the program liability. DOE remains committed to disposing of 34 metric tons of plutonium.

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

Beginning in fiscal year 2018, DOD's individual amounts are reported together as a single line total for its portion of Environmental and Disposal Liabilities. DOD must restore active installations, installations affected by base realignment and closure, and other areas formerly used as DOD sites. DOD also bears responsibility for disposal of chemical weapons and environmental costs associated with the disposal of weapons systems (primarily nuclear powered aircraft carriers and submarines).

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

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

For general PP&E placed into service after September 30, 1997, DOD expenses associated environmental costs systematically over the life of the asset using two methods: physical capacity for operating landfills and life expectancy in years for all other assets. DOD expenses the full cost to clean up contamination for stewardship PP&E at the time the asset is placed into service. DOD has expensed the costs for cleanup associated with general PP&E placed into service before October 1, 1997, except for costs intended to be recovered through user charges; for those costs, DOD has expensed cleanup costs associated with that portion of the asset life that has passed since it was placed into service. DOD systematically recognizes the remaining cost over the remaining life of the asset. The unrecognized portion of the estimated total cleanup costs associated with disposal of general PP&E as of September 30, 2018 was $4.8 billion; this amount was unknown as of September 30, 2017.

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

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

Note 14. Benefits Due and Payable

Benefits Due and Payable as of September 30, 2018, and 2017

(In billions of dollars)	2018	2017
Federal Old-Age and Survivors Insurance	75.1	71.3
Grants to States for Medicaid	35.6	34.1
Federal Supplementary Medical Insurance (Medicare Parts B and D)	30.7	30.6
Federal Hospital Insurance (Medicare Part A)	31.5	30.0
Federal Disability Insurance	24.6	26.9
All other benefits programs	13.6	25.9
Total benefits due and payable	211.1	218.8

Benefits due and payable are amounts owed to program recipients or medical service providers as of September 30 that have not been paid. Most of the benefits due and payable relate to programs administered by HHS and SSA. For a description of the programs, see Note 22—Social Insurance and the unaudited RSI—Social Insurance section.

Note 15. Insurance and Guarantee Program Liabilities

Insurance and Guarantee Program Liabilities as of September 30, 2018, and 2017

(In billions of dollars)	2018	2017
Insurance and Guarantee Program Liabilities:		
Pension Benefit Guaranty Corporation - Benefit Pension Plans	158.0	178.6
Department of Agriculture - Federal Crop Insurance	10.3	11.3
Department of Homeland Security - National Flood Insurance Programs	1.7	12.3
National Credit Union Administration - Share Insurance Fund	0.2	0.3
Total insurance and guarantee program liabilities	170.2	202.5

Insurance and guarantee program liabilities are recognized for known losses and contingent losses to the extent that the underlying contingency is deemed probable and a loss amount is reasonably measurable. Please see Note 18—Contingencies for discussion on the meaning of "probable" depending on the accounting framework used by each significant consolidation entity.

As of September 30, 2018, and 2017, $158.0 billion and $178.6 billion, respectively, pertain to the PBGC single-employer and multiemployer pension plans. PBGC insures pension benefits for participants in covered defined benefit pension plans. The total decrease of $20.6 billion in PBGC's liability for insured pension plans includes decreases of $9.5 billion and $11.1 billion for single-employer and multiemployer plans, respectively. For both single-employer and multiemployer plans, the decreases were primarily driven by changes in actuarial assumptions related to changes in interest factors. As of September 30, 2018, and 2017, PBGC had total liabilities of $163.7 billion and $184.4 billion, and its total liabilities exceeded its total assets by $51.4 billion and $76.0 billion, respectively. Refer to PBGC's financial statements for more information.

As of September 30, 2018, and 2017, $10.3 billion and $11.3 billion, respectively, pertain to the USDA's Federal Crop Insurance Program. The Federal Crop Insurance Program is administered by the Federal Crop Insurance Corporation, whose mission is to provide an actuarially sound risk management program to reduce agricultural producers' economic losses due to natural disasters.

As of September 30, 2018, and 2017, $1.7 billion and $12.3 billion, respectively, pertain to the DHS National Flood Insurance Program (NFIP). The NFIP insurance liability represents an estimate based on the loss and loss adjustment expense factors inherent to the NFIP Insurance Underwriting Operations, including trends in claim severity and frequency. The estimate is driven primarily by flooding activity in the U.S. and can vary significantly year over year depending on the timing and severity of flooding activity. A reduced estimated insurance liability for disaster relief efforts for the significant hurricanes in fiscal year 2018 is the primary driver of the $10.6 billion decrease from fiscal year 2017.

As of September 30, 2018, and 2017, $0.2 billion and $0.3 billion, respectively, pertain to NCUA's National Credit Union Share Insurance Fund (NCUSIF). The NCUSIF is administered by the NCUA, and protects members' accounts in insured credit unions in the event of a credit union failure.

Certain significant consolidation entities apply FASB standards, and such entities, as permitted by SFFAS No. 47, are consolidated into the U.S. government's consolidated financial statements without conversion to FASAB standards.

Note 16. Other Liabilities

Other Liabilities as of September 30, 2018, and 2017
(In billions of dollars)

	2018	Restated 2017
Unearned revenue and assets held for others:		
Unearned fees for nuclear waste disposal (DOE) and other unearned revenue	59.5	60.0
Assets held on behalf of others	117.3	111.4
Subtotal	176.8	171.4
Employee-related liabilities:		
Accrued federal employees' wages and benefits	42.1	37.4
Selected DOE contractors' and D.C. employees' pension benefits	53.7	51.5
Subtotal	95.8	88.9
International monetary liabilities and gold certificates:		
Exchange Stabilization Fund	54.5	55.1
Gold certificates	11.0	11.0
Subtotal	65.5	66.1
Subsidies and grants:		
Farm and other subsidies	9.4	13.2
Grant payments due to state and local governments and others	21.3	22.1
Subtotal	30.7	35.3
Miscellaneous liabilities:		
Legal and other contingencies	52.4	56.5
Non-federal power projects and capital lease liabilities, and disposal liabilities	11.4	12.1
Other miscellaneous	46.4	42.8
Subtotal	110.2	111.4
Total	479.0	473.1

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

Unearned Revenue and Assets Held for Others

The government recognizes a liability when it receives money in advance of providing goods and services or assumes custody of money belonging to others. Advances and prepayments include USPS customer deposits used for future mailings. The government's unearned revenue from fees DOE has collected from utility companies for the future cost of managing the disposal of nuclear waste and interest income received is about $41.9 billion and $40.3 billion as of September 30, 2018, and 2017, respectively. Other unearned revenue includes USPS income for prepaid postage and prepaid P.O. Box rentals. Assets held on behalf of others include funds collected in advance for such things as outstanding postal money orders and undelivered Defense articles. SAA holds $89.1 billion and $85.6 billion as of September 30, 2018, and 2017, respectively for articles and services for future delivery to foreign governments.

Employee-Related Liabilities

This category includes amounts owed to employees at year-end and actuarial liabilities for certain non-federal employees. Actuarial liabilities for federal employees and veteran benefits are included in Note 12–Federal Employee and Veteran Benefits Payable. The largest liability in the employee-related liabilities category is the amount owed at the end of the fiscal year to federal employees for wages and benefits (including accrued annual leave). In addition, DOE is liable to certain contractors for contractor employee pension and postretirement benefits, which is about $21.3 billion and $23.1 billion as of September 30, 2018 and 2017, respectively. Also, the government owed about $8.4 billion and $8.7 billion as of September 30, 2018, and 2017 respectively, for estimated future pension benefits of the District of Columbia's judges, police, firefighters, and teachers.

International Monetary Liabilities and Gold Certificates

Consistent with U.S. obligations in the IMF on orderly exchange arrangements and a stable system of exchange rates, the Secretary of the Treasury, with the approval of the President, may use the ESF to deal in gold, foreign exchange, and other instruments of credit and securities. As of September 30, 2018, and 2017, other liabilities includes $49.3 billion and $49.9 billion, respectively, of interest-bearing liability to the IMF for SDR allocations.

Gold certificates are issued in nondefinitive or book-entry form to the Federal Reserve Bank of New York (FRBNY). The government's liability incurred by issuing the gold certificates, as reported on the Balance Sheet, is limited to the gold being held by Treasury at the standard value established by law. Upon issuance of gold certificates to the FRBNY, the proceeds from the certificates are deposited into the operating cash of the U.S. government. All of the Treasury certificates issued are payable to the FRBNY. Gold certificates were valued at $11.0 billion as of September 30, 2018, and 2017, respectively.

See Note 2—Cash and Other Monetary Assets for additional information.

Subsidies and Grants

The government supports the public good through a wide variety of subsidy and grant programs in such areas as agriculture, medical and scientific research, education, and transportation. USDA programs such as Conservation Reserve, and Agricultural Risk Coverage and Price Loss Coverage account for the majority of the subsidies due, about $4.8 billion and $8.9 billion as of September 30, 2018 and 2017, respectively.

The government awards hundreds of billions of dollars in grants annually. These include project grants that are competitively awarded for entity-specific projects, such as HHS grants to fund projects to "enhance the independence, productivity, integration, and inclusion into the community of people with developmental disabilities." Other grants are formula grants, such as matching grants. Formula grants go to state governments for such things as education and transportation programs. These grants are paid in accordance with distribution formulas that have been provided by law or administrative regulations. Of the total liability reported for grants as of September 30, 2018, and 2017, DOT, Education, HHS and USDA collectively owed their grantees about $20.4 billion and $20.6 billion, respectively. Refer to the financial statements of the respective entities for additional information.

Miscellaneous Liabilities

Some of the more significant liabilities included in this category are for (1) legal and other contingencies (see Note 18—Contingencies), (2) Bonneville Power Administration liability to pay annual budgets of several power projects for its electrical generating capacity, (3) payables upon return of securities loaned and (4) September 11th Victim Compensation Fund. Certain HUD amounts have been restated. Refer to Note 1.U—Restatements for more information.

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

Note 17. Collections and Refunds of Federal Revenue

Collections of Federal Tax Revenue for the Year Ended September 30, 2018

(In billions of dollars)	Federal Tax Revenue Collections	Tax Year to Which Collections Relate			
		2018	2017	2016	Prior Years
Individual income tax and tax withholdings	3,089.8	1,932.6	1,096.7	33.5	27.0
Corporate income taxes	262.7	150.3	99.7	1.7	11.0
Excise taxes	98.5	73.3	24.9	0.1	0.2
Unemployment taxes	43.4	34.1	9.1	0.1	0.1
Customs duties	43.4	43.4	-	-	-
Estate and gift taxes	23.9	0.1	20.9	1.1	1.8
Railroad retirement taxes	6.3	4.9	1.4	-	-
Fines, penalties, interest, and other revenue	7.2	7.1	0.1	-	-
Subtotal	3,575.2	2,245.8	1,252.8	36.5	40.1
Less: amounts collected for non-federal entities	(0.5)				
Total	3,574.7				

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

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

Tax and other revenues reported reflect the effects of tax expenditures which are special exclusions, exemptions, deductions, tax credits, preferential tax rates, and tax deferrals that allow individuals and businesses to reduce taxes they may otherwise owe. The *Congressional Budget Act of 1974* (P.L. 93-344 or Budget Act) requires that a list of tax expenditures be included in the annual Budget. Tax expenditures may be viewed as alternatives to other policy instruments, such as spending or regulatory programs. For example, the government supports college attendance through both spending programs and tax expenditures. The government uses Pell Grants to help low- and moderate-income students afford college and allows certain funds used to meet college expenses to grow tax free in special college savings accounts.

Tax expenditures include deductions and exclusions which reduce the amount of income subject to tax. Examples are the deduction for mortgage interest on personal residences and the exclusion of interest on state and local bonds. Tax expenditures also include tax credits, which reduce tax liability dollar for dollar for the amount of credit. For example, the child tax credit reduces liability by $2,000 per child for taxpayers eligible to use it fully. Other credits are targeted at business activity, such as credits for producing electricity from renewable energy or the research and experimentation credit, which encourages businesses in the U.S. to increase investment in research activities. In addition, tax expenditures include some provisions that allow taxpayers to defer tax liability. Examples include provisions that allow immediate expensing or accelerated depreciation of certain capital investments, and others that allow taxpayers to defer their tax liability, such as the deferral of recognition of income on contributions to and income accrued within qualified retirement plans.

The Total Revenues reported in the Statement of Operations and Changes in Net Position and the related information reported in this note, do not include explicit line items for tax expenditures, but the total revenue amounts and budget results reflect the effect of these expenditures. Tax expenditures are discussed in this note, the unaudited MD&A, and in the unaudited Other Information section of the *Financial Report*.

Federal Tax Refunds Disbursed for the Year Ended September 30, 2018

(In billions of dollars)	Refunds Disbursed	Tax Year to Which Refunds Relate 2018	2017	2016	Prior Years
Individual income tax and tax withholdings	401.4	54.4	307.9	29.8	9.3
Corporate income taxes	60.1	4.8	25.9	9.2	20.2
Excise taxes	1.6	0.5	0.6	0.1	0.4
Unemployment taxes	0.1	-	0.1	-	-
Customs duties	1.9	1.1	0.3	0.2	0.3
Estate and gift taxes	1.0	-	0.3	0.4	0.3
Total	466.1	60.8	335.1	39.7	30.5

Reconciliation of Revenue to Tax Collections for the Year Ended September 30, 2018, and 2017

(In billions of dollars)	2018	2017
Consolidated revenue per the Statement of Operations and Changes in Net Position	3,384.3	3,374.6
Tax refunds	466.1	439.1
Earned income tax and child tax credit imputed revenue	(77.2)	(79.1)
Other tax credits and accrual adjustments	(56.8)	(49.0)
Federal Insurance Contributions Act - Tax	22.7	21.9
Federal Reserve earnings	(70.8)	(81.3)
Nontax-related fines and penalties reported by entities	(79.8)	(78.4)
Nontax-related earned revenue	(13.8)	(28.4)
Collections of federal tax revenue	3,574.7	3,519.4

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

Collections of Federal Revenue for the Year Ended September 30, 2017

(In billions of dollars)	Federal Tax Revenue Collections	Tax Year to Which Collections Relate			
		2017	2016	2015	Prior Years
Individual income tax and tax withholdings	2,976.3	1,930.0	988.6	32.3	25.4
Corporate income taxes	338.6	218.6	108.9	1.8	9.3
Excise taxes	89.4	66.7	22.5	-	0.2
Unemployment taxes	44.2	31.4	12.7	-	0.1
Customs duties	34.9	34.9	-	-	-
Estate and gift taxes	23.8	0.2	20.9	1.0	1.7
Railroad retirement taxes	6.0	4.6	1.4	-	-
Fines, penalties, interest and other revenue	6.6	6.5	0.1	-	-
Subtotal	3,519.8	2,292.9	1,155.1	35.1	36.7
Less: amounts collected for non-federal entities	(0.4)				
Total	3,519.4				

Federal Tax Refunds Disbursed for the Year Ended September 30, 2017

(In billions of dollars)	Refunds Disbursed	Tax Year to Which Refunds Relate			
		2017	2016	2015	Prior Years
Individual income tax and tax withholdings	389.2	46.3	306.4	27.8	8.7
Corporate income taxes	44.9	5.2	14.4	7.8	17.5
Excise taxes	2.1	0.4	1.0	0.2	0.5
Unemployment taxes	0.1	-	0.1	-	-
Customs duties	1.7	1.1	0.3	0.1	0.2
Estate and gift taxes	1.1	-	0.2	0.4	0.5
Total	439.1	53.0	322.4	36.3	27.4

Note 18. Contingencies

Financial Treatment of Loss Contingencies

Loss contingencies are existing conditions, situations, or set of circumstances involving uncertainty as to possible loss to an entity. The uncertainty will ultimately be resolved when one or more future events occur or fail to occur. The reporting of loss contingencies depends on the likelihood that a future event or events will confirm the loss or impairment of an asset or the incurrence of a liability. When a loss contingency exists, the likelihood that the future event or events will confirm the loss or the incurrence of a liability can range from probable to remote. SFFAS No. 5, *Accounting for Liabilities of the Federal Government*, identifies the probability classifications used to assess the range for the likelihood of loss as probable, reasonably possible, and remote. Loss contingencies where a past event or exchange transaction has occurred, and where a future outflow or other sacrifice of resources is assessed as probable and measurable are accrued in the financial statements. Loss contingencies that are assessed to be at least reasonably possible are disclosed in this note and loss contingencies that are assessed as remote are not reported in the financial statements, nor disclosed in the notes. The following table provides criteria for how federal entities are to account for loss contingencies, based on the likelihood of the loss and measurability.[3]

Likelihood of future outflow or other sacrifice of resources	Loss amount can be reasonably measured	Loss range can be reasonably measured	Loss amount or range cannot be reasonably measured
Probable Future confirming event(s) are more likely to occur than not.[4]	Accrue the liability. Report on Balance Sheet and Statement of Net Cost.	Accrue liability of best estimate or minimum amount in loss range if there is no best estimate, and disclose nature of contingency and range of estimated liability.	Disclose nature of contingency and include a statement that an estimate cannot be made.
Reasonably possible Possibility of future confirming event(s) occurring is more than remote and less than likely.	Disclose nature of contingency and estimated amount.	Disclose nature of contingency and estimated loss range.	Disclose nature of contingency and include a statement that an estimate cannot be made.
Remote Possibility of future event(s) occurring is slight.	No action is required.	No action is required.	No action is required.

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

[4] For pending or threatened litigation and unasserted claims, the future confirming event or events are considered “probable” if such events are likely to occur.

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

Certain significant consolidation entities apply financial accounting and reporting standards issued by FASB, and such entities, as permitted by SFFAS No. 47, are consolidated into the U.S. government's consolidated financial statements without conversion to financial and reporting standards issued by FASAB.[5] Generally, under FASAB standards, a contingency is considered "probable" if the future event or events are more likely than not to occur. Under FASB standards, a contingency is considered "probable" if the future event or events are likely to occur. "Likely to occur" is considered to be more certain than "more likely than not to occur." Under both accounting frameworks, a contingency is considered "reasonably possible" if occurrence of the future event or events is more likely than remote, but less likely than "probable" ("probable" as defined within each corresponding accounting framework).

Insurance Contingencies

At the time an insurance policy is issued, a contingency arises. The contingency is the risk of loss assumed by the insurer, that is, the risk of loss from events that may occur during the term of the policy. The government has insurance contingencies that are reasonably possible in the amount of $185.4 billion as of September 30, 2018, and $253.1 billion as of September 30, 2017. The major programs are identified below:

- PBGC reported $184.8 billion and $252.2 billion as of September 30, 2018, and 2017, respectively, for the estimated aggregate unfunded vested benefits exposure to the PBGC for private-sector single-employer and multiemployer defined benefit pension plans that are classified as a reasonably possible exposure to loss. The decrease in single employer program contingencies is primarily due to the decline in the number of companies with lower than investment grade bond ratings and/or credit scores, while the primary reason for the decrease in multiemployer program contingencies is due to 14 plans that are no longer classified as reasonably possible. Of these 14 plans, 12 were removed due to improvements in the plans' financial conditions, and the 2 remaining plans were reclassified to other categories. Please refer to the PBGC financial statements for further details.
- FDIC reported $0.3 billion and $0.6 billion as of September 30, 2018, and 2017, respectively, for identified additional risk in the financial services industry that could result in additional loss to the DIF should potentially vulnerable insured institutions ultimately fail. Actual losses, if any, will largely depend on future economic and market conditions.

Deposit Insurance

Deposit insurance covers all types of deposits received at insured financial institutions, including deposits in checking accounts, negotiable order of withdrawal accounts, savings accounts, money market deposit accounts, time deposits such as certificates of deposit, and official items issued by banks, such as cashier's checks or money orders. The insurance covers the balance of depositors' accounts, dollar-for-dollar, including principal and any accrued interest through the date of the insured financial institution's closing, up to the insurance limit. As a result, the government has the following exposure from federally-insured financial institutions:

- FDIC has estimated insured deposits of $7,376.6 billion as of September 30, 2018, and $7,092.0 billion as of September 30, 2017, for the DIF.
- NCUA has estimated insured shares of $1,132.5 billion as of September 30, 2018, and $1,080.9 billion as of September 30, 2017, for the NCUSIF.

[5] Significant consolidation entities that apply FASB standards without conversion to FASAB standards are FDIC, NCUA, PBGC, FCSIC, TVA, Smithsonian Institution, NRRIT, and USPS.

Legal Contingencies

Legal contingencies as of September 30, 2018, and 2017, are summarized in the table below:

	2018			2017		
		Estimated Range of Loss for Certain Cases [2]			Estimated Range of Loss for Certain Cases [2]	
(In billions of dollars)	Accrued Liabilities [1]	Lower End	Upper End	Accrued Liabilities [1]	Lower End	Upper End
Legal contingencies:						
Probable	11.0	10.5	12.4	7.4	6.8	8.6
Reasonably possible............	-	7.0	26.3	-	3.1	12.6

[1] Accrued liabilities are recorded and presented in other liabilities on the Balance Sheet.

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

The government is party in various administrative proceedings, legal actions, and tort claims which may ultimately result in settlements or decisions adverse to the government.

Management and legal counsel have determined that it is "probable" that some of these actions will result in a loss to the government and the loss amounts are reasonably measurable. The estimated liabilities for "probable" cases against the government are $11.0 billion and $7.4 billion as of September 30, 2018, and 2017, respectively, and are included in "Other Liabilities" on the Balance Sheet. For example, the U.S. Supreme Court decision in *Salazar v. Ramah Navajo Chapter*, dated June 18, 2012, and subsequent cases related to contract support costs have resulted in increased claims against the Indian Health Service, which is a component within HHS. As a result of this decision, many tribes have filed claims. Some claims have been paid and others have been asserted but not yet settled. It is expected that some tribes will file additional claims for prior years.

There are also administrative claims and legal actions pending where adverse decisions are considered by management and legal counsel as "reasonably possible" with an estimate of potential loss or a range of potential loss. The estimated potential losses reported for such claims and actions range from $7.0 billion to $26.3 billion as of September 30, 2018, and from $3.1 billion to $12.6 billion as of September 30, 2017. For example, as of September 30, 2018, EPA has received approximately 403 total claims under the *Federal Tort Claims Act* from individuals and businesses situated on or near waterways affected by acid mine water released by Colorado's Gold King Mine in August of 2015. The claims allege lost wages, loss of business income, agricultural and livestock losses, property damage, diminished property value, and personal injury. In addition, EPA has received claims from individuals under the *Federal Tort Claims Act* for alleged injuries and property damages caused by EPA's alleged negligence related to the water health crisis in Flint, Michigan. The estimated losses related to the Gold King Mine and the water health crisis are $2.1 billion and $2.8 billion, respectively. EPA has determined there is a reasonably possible likelihood of unfavorable outcome for these cases.

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

- A number of plaintiffs filed claims in the U.S. Court of Federal Claims requesting that Treasury redeem matured savings bonds not possessed by the applicable states, but which have registered owners with last known addresses in those states. Treasury informed the applicable states it would not redeem these savings bonds since those states are not registered owners of the bonds. On August 20, 2015, the U.S. Court of Federal Claims partially dismissed one claim and denied the U.S. government's motion to dismiss with respect to other claims. On August 8, 2017, the court ruled in favor of two states, and the U.S. government has appealed. At this time, the government is unable to determine the likelihood of an unfavorable outcome or make an estimate of potential loss.

Environmental and Disposal Contingencies

Environmental and disposal contingencies as of September 30, 2018, and 2017, are summarized in the table below:

	2018			2017		
		Estimated Range of Loss for Certain Cases [2]			Estimated Range of Loss for Certain Cases [2]	
(In billions of dollars)	Accrued Liabilities [1]	Lower End	Upper End	Accrued Liabilities [1]	Lower End	Upper End
Environmental and disposal contingencies:						
Probable	30.2	29.5	31.4	28.4	27.7	29.5
Reasonably possible	-	0.6	0.8	-	0.7	1.5

[1] Accrued liabilities are recorded and presented in other liabilities on the Balance Sheet.

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

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

Management and legal counsel have determined that it is “probable” that some of these actions will result in a loss to the government and the loss amounts are reasonably measurable. The estimated liabilities for these cases are $30.2 billion and $28.4 billion as of September 30, 2018, and 2017, respectively, and are included in “Other Liabilities” on the Balance Sheet.

In accordance with the *Nuclear Waste Policy Act of 1982* (NWPA), DOE entered into more than 68 standard contracts with utilities in which, in return for payment of fees into the Nuclear Waste Fund, DOE agreed to begin disposal of spent nuclear fuel (SNF) by January 31, 1998. Because DOE has no facility available to receive SNF under the NWPA, it has been unable to begin disposal of the utilities’ SNF as required by the contracts. Therefore, DOE is subject to significant SNF litigation claiming damages for partial breach of contract as a result of this delay. Based on settlement estimates, the total liability estimate as of September 30, 2018 is $35.5 billion. After deducting the cumulative amount paid of $7.4 billion as of September 30, 2018 under settlements, and as a result of final judgments, the remaining liability is estimated to be approximately $28.1 billion, compared to approximately $27.2 billion as of September 30, 2017. In addition to its SNF litigation, a number of class action and/or multiple plaintiff tort suits have been filed against current and former DOE contractors in which the plaintiffs seek damages for alleged exposures to radioactive and/or toxic substances as a result of the historic operations of DOE’s nuclear facilities. Collectively, damages in excess of $1.1 billion are currently being sought in these cases.

Other Contingencies

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

- The Federal Highway Administration (FHWA) preauthorizes states to establish construction budgets without having received appropriations from Congress for such projects. FHWA has authority to approve projects using advance construction under 23 U.S.C. 115(a). FHWA does not guarantee the ultimate funding to the states for these “advance construction” projects and, accordingly, does not obligate any funds for these projects. When funding becomes available to FHWA, the states can then apply for reimbursement of costs that they have incurred on such projects, at which time FHWA can accept or reject such requests. As of September 30, 2018, and 2017, FHWA has pre-authorized $60.8 billion and $55.2 billion, respectively, under these arrangements. Congress has not provided appropriations for these projects and no liability is accrued in the DOT consolidated financial statements.
- Contingent liabilities have been established as a result of Medicaid audit and program disallowances that are currently being appealed by the states. The Medicaid amounts are $6.3 billion and $12.2 billion for fiscal years ending September 30, 2018, and 2017, respectively. The states could return the funds through payments to HHS, or

HHS could recoup the funds by reducing future grant awards to the states. Conversely, if the appeals are decided in favor of the states, HHS will be required to pay these amounts. In addition, certain amounts for payment have been deferred under the Medicaid program when there is reasonable doubt as to the legitimacy of expenditures claimed by a state. There are also outstanding reviews of the state expenditures in which a final determination has not been made.

- As part of an annual process, Treasury assesses the need to estimate and accrue a contingent liability to the GSEs to reflect the forecasted equity deficits of the GSEs. Based on this assessment, it was estimated there were no probable future funding draws as of September 30, 2018, and 2017, and therefore, no contingent liability was accrued. However, as of September 30, 2018, it is reasonably possible that market volatility or non-recurring events—for instance, changes to accounting policies that impact credit loss provisions—could potentially cause the GSEs to generate quarterly losses and, therefore, result in future funding draws against Treasury's funding commitment. Due to challenges quantifying future market volatility or the timing, magnitude, and likelihood of non-recurring events, an estimate of the total amount of this reasonably possible future funding liability could not be made as of September 30, 2018. See Note 8—Investments in Government-Sponsored Enterprises for further information.

Treaties and Other International Agreements

The government is a party to treaties and other international agreements. These treaties and other international agreements address various issues including, but not limited to, trade, commerce, security, and law enforcement that may involve financial obligations or give rise to possible exposure to losses. When a contingency originates from the U.S. government's involvement in a treaty or other international agreement, the responsible reporting entity must establish a contingent liability, include a required note disclosure to its financial statements, or both, in accordance with guidance in SFFAS No. 5, as amended. A review of potential contingent liabilities arising from litigation related to treaties and other international agreements has been conducted by U.S. government entities. This entity-level review, along with any resulting relevant information, is captured and reported in the annual legal representation letter process and, if applicable, disclosed in the Legal Contingencies section of this note.

Note 19. Commitments

Long-Term Operating Leases as of September 30, 2018, and 2017

(In billions of dollars)	2018	2017
General Services Administration	21.6	22.4
U.S. Postal Service	3.5	7.6
Department of State	1.4	1.6
Department of Defense	0.9	1.0
Department of Health and Human Services	0.8	1.0
Other operating leases	3.9	3.5
Total long-term operating leases	32.1	37.1

The government has entered into contractual commitments that require future use of financial resources. It has significant amounts of long-term lease obligations.

Undelivered Orders and Other Commitments as of September 30, 2018, and 2017

(In billions of dollars)	2018	Restated 2017
Undelivered Orders:		
Department of Defense	319.8	263.8
Security Assistance Accounts	168.4	140.8
Department of Education	132.7	128.1
Department of Health and Human Services	122.7	114.2
Department of Transportation	110.5	103.7
Department of Agriculture	58.3	62.0
Department of Housing and Urban Development	48.9	39.1
Department of Homeland Security	42.3	37.9
Department of Energy	27.0	22.8
Department of State	24.0	21.8
U.S. Agency for International Development	17.4	17.9
All other entities	126.6	126.0
Total undelivered orders	1,198.6	1,078.1
Other Commitments:		
GSE Senior Preferred Stock Purchase Agreements	254.1	258.1
U.S. Participation in the International Monetary Fund	154.9	157.0
Callable Capital Subscriptions for Multilateral Development Banks	121.1	120.6
All other commitments	22.4	30.0
Total other commitments	552.5	565.7

Undelivered Orders and Other Commitments

Undelivered Orders

Undelivered orders represent the value of goods and services ordered that have not yet been received. As of September 30, 2018, and 2017, DOD reported undelivered orders of $319.8 billion and $263.8 billion, respectively. The $56.0 billion increase primarily resulted from an increase in activity (available budgetary resources) and continued refinement of estimation methods used in the classification of non-federal undelivered orders.

Certain amounts related to DOJ have been restated. Refer to Note 1.U—Restatements for more information.

GSE Senior Preferred Stock Purchase Agreements

At September 30, 2018 and 2017, the maximum remaining potential commitment to the GSEs for the remaining life of the SPSPAs was $254.1 billion and $258.1 billion, respectively, which was established on December 31, 2012. Refer to Note 8—Investments in Government-Sponsored Enterprises for a full description of the SPSPAs related commitments and contingent liability, if any, as well as additional information.

U.S. Participation in the International Monetary Fund

The government participates in the IMF through a quota subscription and certain borrowing arrangements that supplement IMF resources. As of September 30, 2018, and 2017, the financial commitment under the U.S. quota and borrowing arrangements was $154.9 billion and $157.0 billion, respectively. Refer to Note 2—Cash and Other Monetary Assets for more information regarding the U.S. participation in the IMF.

Callable Capital Subscriptions for Multilateral Development Banks

The government has callable subscriptions in certain MDBs, which are international financial institutions that finance economic and social development projects in developing countries. Callable capital in the MDBs serves as a supplemental pool of resources that may be redeemed and converted into ordinary paid in shares, if the MDB cannot otherwise meet certain obligations through its other available resources. MDBs are able to use callable capital as backing to obtain favorable financing terms when borrowing from international capital markets. To date, there has never been a call on this capital at any MDBs and none is anticipated. As of September 30, 2018, and 2017, the capital commitment to MDBs was $121.1 billion and $120.6 billion, respectively.

All Other Commitments

Certain amounts related to Treasury have been restated. Refer to Note 1.U—Restatements for more information.

Other Risks

Terrorism Risk Insurance Program

Congress originally enacted the *Terrorism Risk Insurance Act* in November 2002 to address market disruptions resulting from terrorist attacks on September 11, 2001. Most recently, the *Terrorism Risk Insurance Program Reauthorization Act of 2015* extended the Terrorism Risk Insurance Program (TRIP) until December 31, 2020. The TRIP helps to ensure available and affordable commercial property and casualty insurance for terrorism risk, and simultaneously allows private markets to stabilize. The authority to pay claims under the TRIP Program is activated when the Secretary of the Treasury (in consultation with the Secretary of the Department of Homeland Security and the U.S. Attorney General) certifies an “act of terrorism.” In the event of certification of an “act of terrorism” insurers may be eligible to receive reimbursement from the U.S. government for associated insured losses assuming an aggregate insured loss threshold (“program trigger”) has been reached once a particular insurer has satisfied its designated deductible amount. For calendar years 2018 and 2017, the program trigger amount was $160.0 million and $140.0 million, respectively. This amount will increase by $20.0 million annually through calendar year 2020. Insured losses above insurer deductibles will be shared between insurance companies and the U.S. government. The TRIP includes both mandatory and discretionary authority for Treasury to recoup federal payments made under the TRIP through policyholder surcharges under certain circumstances, and contains provisions designed to manage litigation arising from or relating to a certified act of terrorism. There were no claims under the TRIP as of September 30, 2018 or 2017.

U.S. Contributions to International Organizations

The U.S. government enters into agreements to pay future contributions to international organizations in which it participates as a member. These contributions may include financial and in-kind support, including assessed contributions, voluntary contributions, grants, and other assistance to international organizations. Following are examples of international organizations and their underlying missions which are supported by U.S. contributions:

- Office of the United Nations High Commissioner for Refugees, which supports annual and supplementary appeals for Africa, East Asia, Europe, Near East, South Asia, and the Western Hemisphere, as well as protection activities, refugee resettlement, and the global HIV/AIDS initiative;
- International Committee of the Red Cross, which aids in annual emergency and budget extension appeals for Africa, East Asia, Europe, Near East, South Asia, and the Western Hemisphere to support protection and assistance for conflict-affected populations;
- International Organization for Migration, which supports migration programs and the U.S. Refugee Assistance Program;
- North Atlantic Treaty Organization, which promotes conflict prevention and peaceful resolution of disputes;
- United Nations, which enables the world's nations to work together toward freedom, democracy, peace, and human rights;
- World Food Program, which provides emergency nutrition programming;
- Global Environment Facility, which is a multilateral trust fund that provides grants for global environmental projects;
- Green Climate Fund, established to support the efforts of developing countries to respond to the challenge of climate change;
- United Nations Children's Fund, which promotes humanitarian and developmental assistance to children and mothers in developing countries; and
- World Health Organization, which provides support for collaborative efforts in a wide range of health-related activities, including infectious diseases, maternal and child health, family planning, safe motherhood, newborn health, reproductive health, environmental health, and HIV/AIDS.

Note 20. Funds from Dedicated Collections

Funds from Dedicated Collections as of September 30, 2018[1]

(In billions of dollars)	Federal Old-Age and Survivors Insurance Trust Fund	Federal Hospital Insurance Trust Fund (Medicare Part A)	Federal Disability Insurance Trust Fund	Federal Supplementary Medical Insurance Trust Fund (Medicare Parts B and D)	All Other Funds from Dedicated Collections	Total Funds from Dedicated Collections (Combined)
Assets:						
Cash and other monetary assets	-	-	-	-	65.9	65.9
Fund balance with Treasury	(0.2)	1.6	(0.3)	25.8	149.9	176.8
Investments in U.S. Treasury securities, net of unamortized premiums/discounts	2,801.3	202.8	93.4	98.2	272.1	3,467.8
Other federal assets	19.9	38.7	0.7	35.9	24.6	119.8
Non-federal assets	2.6	1.2	5.1	17.4	110.9	137.2
Total assets	2,823.6	244.3	98.9	177.3	623.4	3,967.5
Liabilities and net position:						
Due and payable to beneficiaries	75.3	31.5	25.1	30.7	2.1	164.7
Other federal liabilities	5.6	39.6	0.9	42.6	66.5	155.2
Other non-federal liabilities	-	1.1	-	0.8	183.7	185.6
Total liabilities	80.9	72.2	26.0	74.1	252.3	505.5
Total net position	2,742.7	172.1	72.9	103.2	371.1	3,462.0
Total liabilities and net position	2,823.6	244.3	98.9	177.3	623.4	3,967.5
Change in net position:						
Beginning net position	2,766.6	178.4	46.3	98.6	329.6	3,419.5
Adjustments to beginning net position	-	-	-	-	2.6	2.6
Beginning net position, adjusted	2,766.6	178.4	46.3	98.6	332.2	3,422.1
Investment revenue	81.1	7.2	2.4	2.4	5.4	98.5
Individual income taxes	706.1	264.6	167.0	-	-	1,137.7
Other taxes and miscellaneous earned revenue	-	0.6	-	4.1	138.5	143.2
Other changes in fund balance (e.g., appropriations, transfers)	26.3	23.5	(1.6)	312.8	11.8	372.8
Total financing sources	813.5	295.9	167.8	319.3	155.7	1,752.2
Program gross costs and non-program expenses	837.4	306.2	141.2	411.0	171.5	1,867.3
Less: program revenue	-	(4.0)	-	(96.3)	(54.7)	(155.0)
Net cost	837.4	302.2	141.2	314.7	116.8	1,712.3
Ending net position	2,742.7	172.1	72.9	103.2	371.1	3,462.0

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

Funds from Dedicated Collections as of September 30, 2017 (Restated)[1]

(In billions of dollars)	Federal Old-Age and Survivors Insurance Trust Fund	Federal Hospital Insurance Trust Fund (Medicare Part A)	Federal Disability Insurance Trust Fund	Federal Supplementary Medical Insurance Trust Fund (Medicare Parts B and D)	All Other Funds from Dedicated Collections	Total Funds from Dedicated Collections (Combined)
Assets:						
Cash and other monetary assets	-	-	-	-	65.0	65.0
Fund balance with Treasury	(0.1)	0.8	(0.2)	27.5	139.2	167.2
Investments in U.S. Treasury securities, net of unamortized premiums/discounts	2,820.2	197.8	69.7	70.6	271.6	3,429.9
Other federal assets	20.4	37.9	0.5	36.0	18.5	113.3
Non-federal assets	2.5	11.7	4.8	39.0	112.1	170.1
Total assets	2,843.0	248.2	74.8	173.1	606.4	3,945.5
Liabilities and net position:						
Due and payable to beneficiaries	71.3	30.1	27.4	30.6	14.8	174.2
Other federal liabilities	5.1	38.6	1.1	43.2	72.6	160.6
Other non-federal liabilities	-	1.1	-	0.7	189.4	191.2
Total liabilities	76.4	69.8	28.5	74.5	276.8	526.0
Total net position	2,766.6	178.4	46.3	98.6	329.6	3,419.5
Total liabilities and net position	2,843.0	248.2	74.8	173.1	606.4	3,945.5
Change in net position:						
Beginning net position	2,746.4	174.1	20.8	94.5	338.5	3,374.3
Adjustments to beginning net position	-	-	-	-	0.2	0.2
Beginning net position, adjusted	2,746.4	174.1	20.8	94.5	338.7	3,374.5
Investment revenue	84.1	7.4	1.7	2.4	4.0	99.6
Individual income taxes	702.1	259.7	166.0	-	-	1,127.8
Other taxes and miscellaneous earned revenue	-	0.5	-	4.2	142.3	147.0
Other changes in fund balance (e.g., appropriations, transfers)	27.7	23.4	(0.8)	278.0	(1.1)	327.2
Total financing sources	813.9	291.0	166.9	284.6	145.2	1,701.6
Program gross cost and non-program expenses	793.7	290.8	141.4	366.1	205.4	1,797.4
Less: program revenue	-	(4.1)	-	(85.6)	(51.1)	(140.8)
Net cost	793.7	286.7	141.4	280.5	154.3	1,656.6
Ending net position	2,766.6	178.4	46.3	98.6	329.6	3,419.5

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

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

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

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

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

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

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

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

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

Federal Old-Age and Survivors Insurance Trust Fund

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

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

Federal Hospital Insurance Trust Fund (Medicare Part A)

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

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

Federal Disability Insurance Trust Fund

The Federal Disability Insurance (DI) Trust Fund, administered by SSA, provides assistance and protection against the loss of earnings due to a wage earner's disability in form of monetary payments.

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

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

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

Medicare Part D was created by the *Medicare Modernization Act of 2003* (P.L. No. 108-173). Medicare Part D financing is similar to Part B; it is primarily based on monthly premiums and income from the General Fund, not on payroll taxes. The fund also receives transfers from states.

All Other Funds from Dedicated Collections

The government is responsible for the management of numerous funds from dedicated collections that serve a wide variety of purposes. The funds from dedicated collections presented on an individual basis in the above tables represent the majority of the government's net position attributable to funds from dedicated collections. All other activity attributable to funds from dedicated collections is aggregated in accordance with SFFAS No. 27, *Identifying and Reporting Funds from Dedicated Collections*, as amended by SFFAS No. 43, *Funds from Dedicated Collections: Amending Statement of Federal Financial Accounting Standards 27, Identifying and Reporting Earmarked Funds*. The funds from dedicated collections within the "all other" aggregate, along with the entities that administer them, include the following:

- Highway Trust Fund and Airport and Airway Trust Fund—administered by DOT.
- Unemployment Trust Fund (UTF) and Black Lung Disability Trust Fund (BLDTF)—administered by DOL.
- Land and Water Conservation Fund, Reclamation Fund, and Water and Related Resources Fund—administered by DOI.
- ESF—administered by Treasury.
- NFIP—administered by DHS.

- Railroad Retirement Trust Fund—administered by RRB.
- Uranium Enrichment Decontamination and Decommissioning Fund—administered by DOE.
- Government National Mortgage Association—administered by HUD.
- Crime Victims Fund—administered by DOJ.
- Harbor Maintenance Trust Fund—administered by DOD.

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

Smithsonian Institution comprised the $2.6 billion adjustment to beginning net position for fiscal year 2018. Gulf Coast Ecosystem Restoration Council and HUD contributed to the $0.2 billion in adjustments to beginning net position for fiscal year 2017. Refer to Note 1.S—Adjustments to Beginning Net Position for more information. Certain amounts related to HUD have been restated. Refer to Note 1.U—Restatements for more information.

Other Taxes and Miscellaneous Earned Income

Unemployment Taxes

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

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

Employer taxes provide the primary funding source for the UTF and constitute the largest portion of unemployment tax revenues attributable to funds from dedicated collections as shown on the consolidated Statement of Operations and Changes in Net Position. However, interest earnings on Treasury securities also provide income to the fund. For the years ending September 30, 2018, and 2017, UTF unemployment tax revenues were $43.2 billion and $44.1 billion, respectively. Appropriations have supplemented the fund's income during periods of high and extended unemployment. The UTF was established under the authority of Section 904 of the *Social Security Act of 1935*.

Excise Taxes

There are 9 funds from dedicated collections within the "all other" aggregate that represent 94 percent of the dedicated excise tax revenue attributable to funds from dedicated collections shown on the consolidated Statement of Operations and Changes in Net Position. The Highway Trust Fund and the Airport and Airway Trust Fund, combined, represent 96 percent of the "all other" dedicated excise tax revenues. Both of these funds are administered by the DOT. For more information, please refer to DOT's financial statements.

The Highway Trust Fund was established to promote domestic interstate transportation and to move people and goods. The fund provides federal grants to states for highway construction, certain transit programs, and related transportation purposes. The Highway Trust Fund was created by the *Highway Revenue Act of 1956*. Funding sources include designated excise taxes on gasoline and other fuels, the initial sale of heavy trucks, and highway use by commercial motor vehicles. For the years ending September 30, 2018, and 2017, Highway Trust Fund excise tax revenues were $42.6 billion and $41.0 billion, respectively. As funds are needed for payments, the Highway Trust Fund corpus investments are liquidated and funds are transferred to the FHWA, the Federal Transit Administration, or other DOT entities, for payment of obligations.

The Airport and Airway Trust Fund provides for airport improvement and airport facilities maintenance. It also funds airport equipment, research, and a portion of the Federal Aviation Administration's administrative operational support. The Airport and Airway Trust Fund was authorized by the *Airport and Airway Revenue Act of 1970*. Funding sources include aviation-related excise tax collections from:

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

For the years ending September 30, 2018, and 2017, Airport and Airway Trust Fund excise tax revenues were $15.8 billion and $15.1 billion, respectively.

Miscellaneous Earned Revenues

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

Note 21. Fiduciary Activities

Fiduciary activities are the collection or receipt, and the management, protection, accounting, investment and disposition by the government of cash or other assets in which non-federal individuals or entities have an ownership interest that the government must uphold. Fiduciary cash and other assets are not assets of the government and are not recognized on the consolidated Balance Sheet. Examples of the government's fiduciary activities include the TSP, which is administered by the FRTIB, and the Indian Tribal and individual Indian Trust Funds, which are administered by the DOI.

Schedule of Fiduciary Net Assets as of September 30, 2018, and 2017

(In billions of dollars)	2018	2017
Thrift Savings Plan	589.0	531.5
Department of the Interior	5.4	5.2
All other	5.2	6.6
Total fiduciary net assets	599.6	543.3

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

As of September 30, 2018, total fiduciary investments in Treasury securities and in non-Treasury securities are $250.3 billion and $363.0 billion, respectively. As of September 30, 2017, total fiduciary investments in Treasury securities and in non-Treasury securities were $223.7 billion and $317.9 billion, respectively. Refer to Note 11—Federal Debt Securities Held by the Public and Accrued Interest for more information on the Treasury securities.

As of September 30, 2018, and 2017, the total fiduciary fund balance with Treasury is $1.8 billion and $1.2 billion, respectively. A liability for this fiduciary fund balance with Treasury is reflected as other miscellaneous liabilities in Note 16—Other Liabilities.

As of September 30, 2018, and 2017, collectively, the fiduciary investments in Treasury securities and fiduciary fund balance with Treasury held by all government entities represent $6.6 billion and $7.0 billion, respectively, of unrestricted cash included within cash held by Treasury for governmentwide operations shown in Note 2—Cash and Other Monetary Assets.

Thrift Savings Plan

The Thrift Savings Fund (TSF) maintains and holds in trust the assets of the TSP. The TSP is administered by an independent government entity, the FRTIB, which is charged with operating the TSP prudently and solely in the interest of the participants and their beneficiaries.

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

As of September 30, 2018, and 2017, the TSP held $589.0 billion and $531.5 billion, respectively, in net assets, which included $245.5 billion and $217.9 billion, respectively, of Treasury securities. The TSF combines the net assets of the TSP and the FRTIB in its financial statements. Only the TSP net assets of the TSF financial statements are disclosed in this note. The most recent audited financial statements for the TSF are as of December 31, 2017, and 2016. For further information about FRTIB and the TSP, please refer to the FRTIB website at https://www.frtib.gov.

DOI–Indian Trust Funds

As stated above, DOI has responsibility for the assets held in trust on behalf of American Indian Tribes and individuals. DOI maintains accounts for Tribal and Other Trust Funds (including the Alaska Native Escrow Fund) and Individual Indian Monies (IIM) Trust Funds in accordance with the *American Indian Trust Fund Management Reform Act of 1994.* The fiduciary balances that have accumulated in these funds have resulted from land use agreements, royalties on natural resource depletion, other proceeds derived directly from trust resources, judgment awards, settlements of claims, and investment income. These funds are maintained for the benefit of individual Native Americans as well as for designated Indian tribes. DOI maintains separate financial statements for these trust funds, which are prepared using a cash or modified cash basis of accounting, a comprehensive basis of accounting other than GAAP. The independent auditors' reports on the Tribal and Other Trust Funds were qualified as it was not practical to extend audit procedures sufficiently to satisfy themselves as to the fairness of the trust fund balances. The IIM Trust Funds received an unmodified opinion from the auditors. As of September 30, 2018, and 2017, the DOI held $5.4 billion and $5.2 billion, respectively, in net assets. For further information related to these assets, please refer to the DOI website at https://www.doi.gov.

All Other Entities with Fiduciary Activities

The government is responsible for the management of other fiduciary net assets on behalf of various non-federal entities. The component entities presented individually in the table on the previous page represent the vast majority of the government's fiduciary net assets. All other component entities with fiduciary net assets are aggregated in accordance with SFFAS No. 31. As of September 30, 2018, and 2017, including TSP and DOI, there are a total of 19 and 20 federal entities, respectively, with fiduciary activities at a grand total of 65 and 67 fiduciary funds, respectively. SBA and Library of Congress (LOC) are the significant entities relating to the fiduciary activities of the remaining component entities within the "all other" aggregate balance. As of September 30, 2018, "all other" fiduciary net assets were $5.2 billion, compared to $6.6 billion as of September 30, 2017.

Note 22. Social Insurance

SOSI presents the projected actuarial present value of the estimated future revenue and estimated future expenditures of the Social Security, Medicare, Railroad Retirement, and Black Lung social insurance programs which are administered by the SSA, HHS, RRB, and DOL, respectively. These estimates are based on the intermediate economic and demographic assumptions presented later in this note as set forth in the relevant Social Security and Medicare trustees' reports and in the agency financial reports of HHS, SSA, and DOL, as well as in the relevant entity performance and accountability report for RRB. Due to a change in the presentation of the consolidated SOSI and this note from billions of dollars to trillions of dollars beginning in fiscal year 2016, some amounts in the narrative will not be traceable to the corresponding entity financial statements. The SOSI projections, with one exception related to Medicare Part A and OASDI, are based on current law; that is, they assume that scheduled social insurance benefit payments would continue after related trust funds are projected to be depleted, contrary to current law. By law, once assets are depleted, expenditures cannot be made except to the extent covered by ongoing tax receipts and other trust fund income. The estimates in the consolidated SOSI of the open group measures are for persons who are participants or eventually will participate in the programs as contributors (workers) or beneficiaries (retired workers, survivors, dependents, and disabled) during the 75-year projection period. To enhance comparability of the BLDTF social insurance information and continue to illustrate the fund's long-term condition and sustainability, DOL revised its projection period from a fixed terminus of September 30, 2040 to a rolling 25-year projection period that begins on the September 30 valuation date each year. The revised projection period became effective for the September 30, 2017 valuation date and continued for fiscal year 2018.

Contributions consist of: payroll taxes from employers, employees, and self-employed persons; revenue from federal income taxation of OASDI and railroad retirement benefits; excise tax on the domestic sale of coal (Black Lung); premiums from, and state transfers on behalf of, participants in Medicare; and reimbursements from the General Fund to the OASDI Trust Funds to make up for reductions in payroll tax revenue due to temporary payroll tax rate reductions. Income for all programs is presented from a consolidated perspective. Future interest payments and other future intragovernmental transfers have been excluded upon consolidation. By accounting convention, intragovernmental transactions are eliminated in the consolidation process, and accordingly, the Statements of Social Insurance do not include projected general revenues that, under current law, would be used to finance the remainder of the expenditures in excess of revenues for Medicare Parts B and D that is reported in the Statements of Social Insurance. Expenditures include benefit payments scheduled under current law and administrative expenses. Current Social Security and Medicare law provides for full benefit payments only to the extent that there are sufficient balances in the trust funds. Expenditures reflect full benefit payments even after the point at which assets are projected to be depleted.

Actuarial present values of estimated future income (excluding interest) and estimated future expenditures for the Social Security and Medicare social insurance programs are presented for three different groups of participants: (1) current participants who have not yet attained eligibility age; (2) current participants who have attained eligibility age; and (3) new entrants, who are expected to become participants in the future. Current participants in the Social Security and Medicare programs are the "closed group" of taxpayers and/or beneficiaries who are at least age 15 years at the start of the projection period. Since the projection period for the Social Security, Medicare, and Railroad Retirement social insurance programs consists of 75 years, the period covers virtually all of the current participants' working and retirement years, a period that could be greater than 75 years in a relatively small number of instances. Future participants for Social Security and Medicare include births during the projection period and individuals below age 15 as of January 1 of the valuation year. Railroad Retirement's future participants are the projected new entrants as of October 1 of the valuation year. For fiscal year 2015 and years prior, future participants for Railroad Retirement were the projected new entrants as of January 1 of the valuation year[6].

The present values of estimated future expenditures in excess of estimated future revenue are calculated by subtracting the actuarial present values of future scheduled contributions as well as dedicated tax income by and on behalf of current and future participants from the actuarial present value of the future scheduled benefit payments to them or on their behalf. To determine a program's funding shortfall over any given period of time, the starting trust fund balance is subtracted from the present value of expenditures in excess of revenues over the period.

The trust fund balances as of the valuation date for the respective programs, including interest earned, are shown in the table below[7]. Substantially all of the OASDI, HI, and SMI Trust Fund balances consist of investments in special nonmarketable Treasury securities that are backed by the full faith and credit of the U.S. government. For more information, see Note 20—Funds from Dedicated Collections.

[6] Beginning with the fiscal year 2016 reporting period, the valuation date for the Railroad Retirement program was changed from calendar year to fiscal year.
[7] Trust fund balances for the Railroad Retirement and Black Lung programs are not included, as these balances are less than $50 billion.

Social Insurance Programs Trust Fund Balances [1]

(In trillions of dollars)	2018	2017	2016	2015	2014
Social Security	2.9	2.8	2.8	2.8	2.8
Medicare	0.3	0.3	0.3	0.3	0.3

[1] As of the valuation date of the respective programs.

Social Security

The OASI Trust Fund, established on January 1, 1940, and the DI Trust Fund, established on August 1, 1956, collectively referred to as OASDI or "Social Security," provides cash benefits for eligible U.S. citizens and residents. Eligibility and benefit amounts are determined under the laws applicable for the period. Current law provides that the amount of the monthly benefit payments for workers and their eligible dependents or survivors is based on the workers' lifetime earnings histories.

The primary financing of the OASDI Trust Funds are taxes paid by workers, their employers, and individuals with self-employment income, based on work covered by the OASDI Program. Refer to the Unaudited RSI—Social Insurance section for additional information on Social Security program financing.

That portion of each trust fund not required to pay benefits and administrative costs is invested, on a daily basis, in interest-bearing obligations of the U.S. government. The *Social Security Act* authorizes the issuance by the Treasury of special nonmarketable, intragovernmental debt obligations for purchase exclusively by the trust funds. Although the special issues cannot be bought or sold in the open market, they are redeemable at any time at face value and thus bear no risk of fluctuation in principal value due to changes in market yield rates. Interest on the bonds is credited to the trust funds and becomes an asset to the funds and a liability to the General Fund. These Treasury securities and related interest are eliminated in consolidation at the governmentwide level.

Medicare

The Medicare Program, created in 1965, has two separate trust funds: the HI (Medicare Part A) and SMI (Medicare Parts B and D) Trust Funds. HI helps pay for inpatient hospital stays, home health care following a hospital stay, and skilled nursing facility and hospice care. SMI helps pay for hospital outpatient services, physician services, and assorted other services and products through Part B and for prescription drugs through Part D. Though the events that trigger benefit payments are similar, HI and SMI have different dedicated financing structures. Similar to OASDI, HI is financed primarily by payroll contributions. Other income to the HI Trust Fund includes a small amount of premium income from voluntary enrollees, receipts from fraud and abuse control activities, a portion of the federal income taxes that beneficiaries pay on Social Security benefits and interest credited on Treasury securities held in the HI Trust Fund. These Treasury securities and related interest are eliminated in the consolidation at the governmentwide level.

For SMI, transfers from the General Fund represent the largest source of income for both Parts B and D. Generally, beneficiaries finance the remainder of Parts B and D costs via monthly premiums to these programs. With the introduction of Part D drug coverage, Medicaid is no longer the primary payer of drug costs for full-benefit dually eligible beneficiaries of Medicare and Medicaid. For those beneficiaries, states are subject to a contribution requirement and must pay a portion of their estimated foregone drug costs into the Part D account (referred to as state transfers). The estimated foregone drug costs is the estimated difference between the drug costs that used to be fully covered by Medicaid for full-benefit dually eligible beneficiaries (i.e., for Medicare and Medicaid) prior to the introduction of Part D, and the drug cost that is now covered for such dually eligible beneficiaries by Medicare Part D. Fees related to brand-name prescription drugs, required by the ACA, are included as income for Part B of SMI. As with HI, interest received on Treasury securities held in the SMI Trust Fund is credited to the fund and these Treasury securities as well as related interest are eliminated in consolidation at the governmentwide level. By accounting convention, the transfers of general revenues are eliminated in the consolidation of the SOSI at the governmentwide level and as such, the general revenues that are used to finance Medicare Parts B and D are not included in these calculations. For the fiscal years 2018 and 2017 SOSI, the amounts eliminated totaled $33.0 trillion and $30.0 trillion, respectively. Refer to Unaudited RSI—Social Insurance section for additional information on Medicare program financing.

The financial projections for the Medicare program reflect substantial, but very uncertain, cost savings deriving from provisions of the ACA and the MACRA that lowered increases in Medicare payment rates to most categories of health care providers.

The ACA became law in fiscal year 2010 and provided funding for the establishment by the Centers for Medicare and Medicaid Services (CMS) of a Center for Medicare and Medicaid Innovation to test innovative payment and service delivery models to reduce program expenditures while preserving or enhancing the quality of care furnished to individuals. It also allowed for the establishment of a Center for Consumer Information and Insurance Oversight (CCIIO). One of the main programs under CCIIO is the Affordable Insurance Exchanges (the “Exchanges”). A brief description of these programs is presented below.

Health Insurance Exchanges. Grants have been provided to the states to establish Health Insurance Exchanges. The initial grants were made by HHS to the states “not later than one year after the date of enactment.” Thus, HHS made the initial grants by March 23, 2011. Subsequent grants were issued by CMS through December 31, 2014, after which time no further grants could be made. All Exchanges were launched on October 1, 2013.

Risk Adjustment Program. The Risk Adjustment Program is a permanent program. It applies to non-grandfathered individuals and small group plans inside and outside the Exchanges. It provides payments to health insurance issuers that disproportionately attract higher-risk populations (such as individuals with chronic conditions) and transfers funds from plans with relatively lower risk enrollees to plans with relatively higher risk enrollees to protect against adverse selection. States that operate a state-based Exchange are eligible to establish a risk adjustment program. States operating a risk adjustment program may have an entity other than the Exchange perform this function. CMS operates a risk adjustment program for each state that does not operate its own.

It is important to note that the Medicare projections depend in part on the long-range feasibility of the various cost-saving measures in the ACA–most importantly, the reductions in the annual payment rate updates for most categories of Medicare providers by the growth in economy-wide private nonfarm business multifactor productivity and the specified physician updates put in place by MACRA. Without fundamental changes in the current delivery system, these productivity-related adjustments to Medicare payment rates would probably not be viable indefinitely. However, this outcome is achievable if health care providers are able to realize productivity improvements at a faster rate than experienced historically. On the other hand, if the health sector cannot transition to more efficient models of care delivery and achieve productivity increases commensurate with economy-wide productivity, and if the provider reimbursement rates paid by commercial insurers continue to be based on the same negotiated process used to date, then the availability and quality of health care received by Medicare beneficiaries would, under current law, fall over time compared to that received by those with private health insurance.

A transformation of health care in the U.S., affecting both the means of delivery and the method of paying for care, is also a possibility. Private health insurance and Medicare take important steps in this direction by initiating programs of research into innovative payment and service delivery models, such as accountable care organizations, patient-centered medical homes, improvement in care coordination for individuals with multiple chronic health conditions, better coordination of post-acute care, payment bundling, pay for performance, and assistance for individuals in making informed health choices. Such changes have the potential to reduce health care costs as well as cost growth rates and could, as a result, help lower health care spending to levels compatible with the lower price updates payable under current law.

The ability of new delivery and payment methods to lower cost growth rates is uncertain at this time. Preliminary indications are that some of these delivery reforms have had modest levels of success in lowering costs, but at this time it is too early to tell if these reductions in spending will continue, or if they will grow to the magnitude needed to align with the statutory Medicare price updates. For those providers affected by the productivity adjustments and the specified updates to physician payments, sustaining the price reductions will be challenging, as the best available evidence indicates that most providers cannot improve their productivity to this degree for a prolonged period given the labor-intensive nature of these services and that physician costs will grow at a faster rate than the specified updates. As a result, actual Medicare expenditures are highly uncertain for reasons apart from the inherent difficulty in projecting health care cost growth over time.

The specified rate updates could be an issue in years when levels of inflation are high and would be problematic when the cumulative gap between the price updates and physician costs becomes large. The gap will continue to widen throughout the projection, and it is estimated that physician payment rates under current law will be lower than they would have been under the SGR formula by 2048. Absent a change in the delivery system or level of update by subsequent legislation, access to Medicare-participating physicians may become a significant issue in the long term under current law. Overriding the price updates in current law, as lawmakers repeatedly did in the case of physician payment rates, would lead to substantially higher costs for Medicare in the long range than those projected in this report.

To help illustrate and quantify the potential magnitude of the cost understatement, the Trustees asked the Office of the Actuary at CMS to prepare an illustrative Medicare Trust Fund projection under a hypothetical alternative. This scenario illustrates the impact that would occur if the payment updates that are affected by the productivity adjustments transition from current law to the payment updates assumed for private health plans over the period 2028 to 2042. It also reflects physician payment updates that transition from current law to the increase in the Medicare Economic Index over the same period. Finally, the scenario assumes the continuation of the 5 percent bonuses for physicians in advanced alternative payment models (APMs) and of the $500-million payments for physicians in the merit-based incentive payment system, which are set to expire in 2025. This alternative was developed for illustrative purposes only; the calculations have not been audited; no endorsement of the policies underlying the illustrative alternative by the Trustees, CMS, or the Office of the Actuary should be inferred; and the examples do not attempt to portray likely or recommended future outcomes. Thus, the illustrations are useful only as general indicators of the substantial impacts that could result from future legislation affecting the productivity adjustments and physician updates under Medicare and of the broad range of uncertainty associated with such impacts. The table on the following page contains a comparison of the Medicare 75-year present values of estimated future income and estimated future expenditures under current law with those under the illustrative alternative scenario.

Medicare Present Values (in trillions) (Unaudited)

	2018 Consolidated SOSI Current Law	Illustrative Alternative Scenario [1, 2]
Income:		
Part A	$22.8	$22.9
Part B [3]	$9.4	$11.1
Part D [4]	$3.2	$3.2
Total income	$35.4	$37.2
Expenditures:		
Part A	$27.5	$32.6
Part B	$34.4	$40.9
Part D	$11.1	$11.1
Total expenditures	$73.0	$84.6
Income less expenditures:		
Part A	$4.7	$9.7
Part B	$25.0	$29.8
Part D	$7.9	$7.9
Excess of expenditures over income	$37.6	$47.4

[1] These amounts are not presented in the 2018 Trustees' Report.

[2] At the request of the Trustees, the Office of the Actuary at CMS has prepared an illustrative set of Medicare Trust Fund projections that differ from current law. No endorsement of the illustrative alternative to current law by the Trustees, CMS, or the Office of the Actuary should be inferred.

[3] Excludes $25.0 trillion and $29.8 trillion of General Revenue Contributions from the 2018 Consolidated SOSI Current Law projection and the Illustrative Alternative Scenario's projection, respectively; i.e., to reflect Part B income on a consolidated governmentwide basis.

[4] Excludes $7.9 trillion of General Revenue Contributions from both the 2018 Consolidated SOSI Current Law projection and the Illustrative Alternative projection; i.e., to reflect Part D income on a consolidated governmentwide basis.

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

The difference between the current-law and illustrative alternative projections is substantial for Parts A and B. All Part A fee-for-service providers and roughly half of Part B fee-for-service providers are affected by the productivity adjustments, so the current-law projections reflect an estimated 1.1 percent reduction in annual cost growth each year for these providers. If the payment updates that are affected by the productivity adjustments were to gradually transition from current law to the payment updates assumed for private health plans, the physician updates transitioned to the Medicare Economic Index, and the 5 percent bonuses paid to physicians in advanced APMs did not expire, as illustrated under the alternative scenario, the estimated present values of Part A and Part B expenditures would each be higher than the current-law projections by roughly 18 and 19 percent, respectively. As indicated above, the present value of Part A income is basically unaffected under the alternative scenario.

The Part D values are the same under each projection because the services are not affected by the productivity adjustments or the physician updates. The extent to which actual future Part A and Part B costs exceed the projected amounts due to changes to the productivity adjustments and physician updates depends on what specific changes might be legislated and whether Congress would pass further provisions to help offset such costs. As noted, these examples reflect only hypothetical changes to provider payment rates.

Social Security and Medicare–Demographic and Economic Assumptions

The Boards of Trustees[8] of the OASDI and Medicare Trust Funds provide in their annual reports to Congress short-range (10-year) and long-range (75-year) actuarial estimates of each trust fund. Significant uncertainty surrounds the estimates, especially for a period as long as 75 years. To illustrate the range of uncertainty, the Trustees use three alternative scenarios (low-cost, intermediate, and high-cost) that use specific assumptions. These assumptions include fertility rates, rates of change in mortality, LPR and other-than-LPR immigration levels, emigration levels, changes in real GDP, changes in the CPI, changes in average real wages, unemployment rates, trust fund real yield rates, and disability incidence and recovery rates. The assumptions used for the most recent set of projections shown in Table 1A (Social Security) and Table 1B (Medicare) are generally referred to as the “intermediate assumptions,” and reflect the trustees’ reasonable estimate of expected future experience. For further information on Social Security and Medicare demographic and economic assumptions, refer to SSA’s and HHS’s Agency Financial Reports.

[8] The boards are composed of six members. Four members serve by virtue of their positions in the federal government: the Secretary of the Treasury, who is the Managing Trustee; the Secretary of Labor; the Secretary of Health and Human Services; and the Commissioner of Social Security. The President appoints and the Senate confirms the other two members to serve as public representatives. These two positions are currently vacant.

Table 1A
Social Security – Demographic and Economic Assumptions

Demographic Assumptions

Year	Total Fertility Rate[1]	Age-Sex Adjusted Death Rate (per 100,000)[2]	Net Annual Immigration (persons per year)[3]	Period Life Expectancy at Birth[4] Male	Female
2018	1.81	776.4	1,678,000	76.9	81.5
2020	1.84	762.4	1,498,000	77.2	81.7
2030	2.00	697.7	1,321,000	78.4	82.7
2040	2.00	641.1	1,272,000	79.5	83.6
2050	2.00	591.5	1,247,000	80.5	84.5
2060	2.00	547.9	1,233,000	81.5	85.3
2070	2.00	509.4	1,225,000	82.4	86.0
2080	2.00	475.2	1,221,000	83.2	86.7
2090	2.00	444.7	1,218,000	84.0	87.3

Economic Assumptions

Year	Real Wage Differ-ential (percent change)[5]	Average Annual Wage In Covered Employment (percent change)[6]	CPI (percent change)[7]	Real GDP (percent change)[8]	Total Employ-ment (percent change)[9]	Average Annual Interest Rate (percent)[10]
2018	1.59	3.82	2.23	2.7	1.1	2.7
2020	1.95	4.55	2.60	2.6	0.8	3.9
2030	1.28	3.88	2.60	2.1	0.5	5.3
2040	1.22	3.82	2.60	2.1	0.5	5.3
2050	1.23	3.83	2.60	2.1	0.5	5.3
2060	1.22	3.82	2.60	2.1	0.4	5.3
2070	1.15	3.75	2.60	2.1	0.4	5.3
2080	1.13	3.73	2.60	2.1	0.5	5.3
2090	1.15	3.75	2.60	2.1	0.4	5.3

[1]The total fertility rate for any year is the average number of children that would be born to a woman in her lifetime if she were to experience, at each age of her life, the birth rate observed in, or assumed for, the selected year, and if she were to survive the entire childbearing period.
[2]The age-sex-adjusted death rate is based on the enumerated total population as of April 1, 2010, if that population were to experience the death rates by age and sex observed in, or assumed for, the selected year. It is a summary measure and not a basic assumption; it summarizes the basic assumptions from which it is derived.
[3]Net annual immigration is the number of persons who enter during the year (both as lawful permanent residents and otherwise) minus the number of persons who leave during the year. It is a summary measure and not a basic assumption; it summarizes the effects of the basic assumptions from which it is derived.
[4]The period life expectancy at birth for a given year is the average number of years expected prior to death for a person born on January 1 in that year, using the mortality rates for that year over the course of his or her remaining life. It is a summary measure and not a basic assumption; it summarizes the effects of the basic assumptions from which it is derived.
[5]The real-wage differential is the annual percentage change in the average annual wage in covered employment less the annual percentage change in the CPI for Urban Wage Earners and Clerical Workers (CPI-W). Values are rounded after all computations.
[6]The average annual wage in covered employment is the total amount of wages and salaries for all employment covered by the OASDI program in a year, divided by the number of employees with any such earnings during the year. It is a summary measure and not a basic assumption; it summarizes the basic assumptions from which it is derived.
[7]The CPI is the Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W).
[8]The real GDP is the value of total output of goods and services in 2009 dollars. It is a summary measure and not a basic assumption; it summarizes the effects of the basic assumptions from which it is derived.
[9]Total employment is total U.S. military and civilian employment. It is a summary measure and not a basic assumption; it summarizes the basic assumptions from which it is derived.
[10]The average annual interest rate is the average of the nominal interest rates, which compound semiannually, for special public-debt obligations issuable to the OASI and DI Trust Funds in each of the 12 months of the year. It is a summary measure and not a basic assumption; it summarizes the basic assumptions from which it is derived.

Table 1B
Medicare – Demographic and Economic Assumptions

Year	Demographic Assumptions: Total Fertility Rate[1]	Age-Sex Adjusted Death Rate (per 100,000)[2]	Net Annual Immigration (persons per year)[3]
2018	1.81	776.4	1,678,000
2020	1.84	762.4	1,498,000
2030	2.00	697.7	1,321,000
2040	2.00	641.1	1,272,000
2050	2.00	591.5	1,247,000
2060	2.00	547.9	1,233,000
2070	2.00	509.4	1,225,000
2080	2.00	475.2	1,221,000
2090	2.00	444.7	1,218,000

	Economic Assumptions							
					Per Beneficiary Cost[8] (percent change)			
						SMI		
Year	Real Wage Differ-ential (percent change)[4]	Average Annual Wage In Covered Employment (percent change)[5]	CPI (percent change)[6]	Real GDP (percent change)[7]	HI	Part B	Part D	Real Interest Rate (percent)[9]
2018	1.59	3.82	2.23	2.7	1.4	5.3	0.5	0.1
2020	1.95	4.55	2.60	2.6	3.3	4.7	6.0	0.8
2030	1.28	3.88	2.60	2.1	4.4	5.3	5.3	2.7
2040	1.22	3.82	2.60	2.1	4.6	4.2	4.7	2.7
2050	1.23	3.83	2.60	2.1	3.8	3.8	4.7	2.7
2060	1.22	3.82	2.60	2.1	3.6	3.7	4.5	2.7
2070	1.15	3.75	2.60	2.1	3.8	3.6	4.4	2.7
2080	1.13	3.73	2.60	2.1	3.9	3.7	4.4	2.7
2090	1.15	3.75	2.60	2.1	3.4	3.5	4.3	2.7

[1]Average number of children per woman.

[2]The age-sex-adjusted death rate per 100,000 that would occur in the enumerated population as of April 1, 2010, if that population were to experience the death rates by age and sex observed in, or assumed for, the selected year.

[3]Includes legal immigration, net of emigration, as well as other, non-legal, immigration.

[4]Difference between percentage increases in wages and the CPI.

[5]Average annual wage in covered employment.

[6]Consumer price index represents a measure of the average change in prices over time in a fixed group of goods and services.

[7]Total dollar value of all goods and services produced in the United States, adjusted to remove the impact of assumed inflation growth.

[8]These increases reflect the overall impact of more detailed assumptions that are made for each of the different types of service provided by the Medicare program (for example, hospital care, physician services, and pharmaceutical costs). These assumptions include changes in the payment rates, utilization, and intensity of each type of service.

[9]Average rate of interest earned on new trust fund securities, above and beyond rate of inflation.

Railroad Retirement

The Railroad Retirement and Survivor Benefit program pays full retirement annuities at age 60 to railroad workers with 30 years of service. The program pays disability annuities based on total or occupational disability. It also pays annuities to spouses and divorced spouses of retired workers and to widow(er)s, surviving divorced spouses, remarried widow(er)s, children, and parents of deceased railroad workers. Medicare covers qualified railroad retirement beneficiaries in the same way as it does Social Security beneficiaries.

The RRB and the SSA share jurisdiction over the payment of retirement and survivor benefits. The RRB has jurisdiction over the payment of retirement benefits if the employee has at least 10 years of railroad service, or five years if performed after 1995. For survivor benefits, RRB requires that the employee's last regular employment before retirement or death be in the railroad industry. If a railroad employee or his or her survivors do not qualify for railroad retirement benefits, the RRB transfers the employee's railroad retirement credits to SSA, where they are treated as social security credits.

Payroll taxes paid by railroad employers and their employees are a primary source of funding for the Railroad Retirement and Survivor Benefit Program. By law, railroad retirement taxes are coordinated with Social Security taxes. Employees and employers pay Tier I taxes at the same rate as Social Security taxes and Tier II taxes to finance railroad retirement benefit payments that are higher than Social Security levels.

Revenues in excess of benefit payments are invested to provide additional trust fund income. Legislation enacted in 2001 allowed for Railroad Retirement Account funds transferred to the NRRIT to be invested in non-governmental assets, as well as in governmental securities. Funds transferred from the Social Security Equivalent Benefit (SSEB) Account to the NRRIT are allowed to be invested only in governmental securities. Under the financial interchange provisions, the Railroad Retirement program's SSEB Account and the trust funds interchange amounts on an annual basis so that each trust fund is in the same position it would have been had railroad retirement always been covered under Social Security.

Since its inception, NRRIT has received $21.3 billion from RRB (including $19.2 billion in fiscal year 2003, pursuant to the *Railroad Retirement and Survivors' Improvement Act of 2001*) and returned $22.9 billion. During fiscal year 2018, the NRRIT made net transfers of $1.8 billion to the RRB to pay retirement benefits. Administrative expenses of the trust are paid out of trust assets. The balance as of September 30, 2018, and 2017, of non-federal securities and investments of the NRRIT are disclosed in Note 7—Debt and Equity Securities.

Another major source of income to the Railroad Retirement and Survivor Benefit program consists of financial transactions with the Social Security and Medicare Trust Funds. The RRB, SSA, and CMS are parties to a financing arrangement, the "financial interchange", which is intended to put the OASDI and Medicare HI Trust Funds in the same positions they would have been had railroad employment been covered under the *Social Security* and *FICAs*.

Other sources of program income include revenue resulting from federal income taxes on railroad retirement benefits, and appropriations provided after 1974 as part of a phase out of certain vested dual benefits. From a governmentwide perspective, these future financial interchanges and transactions are intragovernmental transfers and are eliminated in consolidation.

The estimated future revenues and expenditures reflected in the SOSI are based on various economic, employment, and other actuarial assumptions, and assume that the Railroad Retirement program will continue as presently constructed. The calculations assume that all future transfers required by current law under the financial interchange will be made. For further details on actuarial assumptions related to the Railroad Retirement program and how these assumptions affect amounts presented on the SOSI and SCSIA, consult the Technical Supplement to the *27th Actuarial Valuation of the Assets and Liabilities Under the Railroad Retirement Acts as of December 31, 2016* and RRB's financial statements.

Black Lung–Disability Benefit Program

The Black Lung Disability Benefit Program provides for compensation, medical, and survivor benefits for eligible coal miners who are totally disabled due to pneumoconiosis (black lung disease) arising out of their coal mine employment, and the BLDTF provides benefit payments when no responsible mine operator (RMO) can be assigned the liability or when the liability is adjudicated to the BLDTF, which may occur as a result of, among other things, bankruptcy of the RMO. DOL operates the Black Lung Disability Benefit Program.

Black lung disability benefit payments are funded by excise taxes from coal mine operators based on the domestic sale of coal, as are the fund's administrative costs. These taxes are collected by the Internal Revenue Service (IRS) and transferred to the BLDTF, which was established under the authority of the *Black Lung Benefits Revenue Act*, and administered by the Treasury.

P.L. 110-343, *Division B-Energy Improvement and Extension Act of 2008*, enacted on October 3, 2008, among other things, restructured the BLDTF debt by refinancing the outstanding high interest rate repayable advances with low interest rate discounted debt instruments similar in form to zero-coupon bonds, plus a one-time appropriation. This Act also allowed that any subsequent debt issued by the BLDTF may be used to make benefit payments, other authorized expenditures, or to repay debt and interest from the initial refinancing.

The significant assumptions used in the projections for the SOSI are the coal excise tax revenue estimates, the tax rate structure, number of beneficiaries, life expectancy, federal civilian pay raises, medical cost inflation, and interest rates used to discount future cash flows. These assumptions affect the amounts reported on the SOSI and the SCSIA. The program's valuation date is September 30 for each year of information presented in the SOSI and the SCSIA. Refer to DOL's financial statements for further details on significant assumptions related to the Black Lung Disability Benefit Program, and how these assumptions affect amounts presented on the SOSI and SCSIA.

Statement of Changes in Social Insurance Amounts

The SCSIA reconciles the change (between the current valuation and the prior valuation) in the present value of estimated future revenue less estimated future expenditures for current and future participants (the open group measure) over the next 75 years (except Black Lung which has a rolling 25-year projection period through September 30, 2043). The reconciliation identifies several components of the changes that are significant and provides reasons for the changes. The following disclosures relate to the SCSIA including the reasons for the components of the changes in the open group measure during the reporting period from the end of the previous reporting period for the government's social insurance programs.

Social Security

The SCSIA shows two reconciliations for Social Security: (1) changes from the period beginning on January 1, 2017, to the period beginning on January 1, 2018, and (2) changes from the period beginning on January 1, 2016, to the period beginning on January 1, 2017. All estimates relating to the Social Security Program in the SCSIA represent values that are incremental to the prior change. As an example, the present values shown for economic data, assumptions, and methods represent the additional effect of these new data, assumptions, and methods after considering the effects from demography and the change in the valuation period. In general, an increase in the present value of net cash flows represents a positive change (improving financing), while a decrease in the present value of net cash flows represents a negative change (worsening financing).

Assumptions Used for the Components of the Changes for the Social Security Program

The present values included in the SCSIA are for the current and prior years and are based on various economic as well as demographic assumptions used for the intermediate assumptions in the Social Security Trustees Reports for these years. Table 1A summarizes these assumptions for the current year.

From the period beginning on January 1, 2017 to the period beginning on January 1, 2018

Present values as of January 1, 2017 are calculated using interest rates from the intermediate assumptions of the 2017 Social Security Trustees Report. All other present values in this part of the SCSIA are calculated as a present value as of January 1, 2018. Estimates of the present value of changes in social insurance amounts due to changing the valuation period and changing demographic data, assumptions, and methods are presented using the interest rates under the intermediate assumptions of the 2017 Social Security Trustees Report. Because interest rates are an economic estimate and all estimates in the table are incremental to the prior change, all other present values in this part of the SCSIA are calculated using the interest rates under the intermediate assumptions of the 2018 Social Security Trustees Report.

From the period beginning on January 1, 2016 to the period beginning on January 1, 2017

Present values as of January 1, 2016 are calculated using interest rates from the intermediate assumptions of the 2016 Social Security Trustees Report. All other present values in this part of the SCSIA are calculated as a present value as of January 1, 2017. Estimates of the present value of changes in social insurance amounts due to changing the valuation period and changing demographic data, assumptions, and methods are presented using the interest rates under the intermediate assumptions of the 2016 Social Security Trustees Report. Because interest rates are an economic estimate and all estimates in the table are incremental to the prior change, all other present values in this part of the SCSIA are calculated using the interest rates under the intermediate assumptions of the 2017 Social Security Trustees Report.

Changes in Valuation Period

From the period beginning on January 1, 2017 to the period beginning on January 1, 2018

The effect on the 75-year present values of changing the valuation period from the prior valuation period (2017-2091) to the current valuation period (2018-2092) is measured by using the assumptions for the prior valuation and extending them to cover the current valuation. Changing the valuation period removes a small negative net cash flow for 2017, replaces it with a much larger negative net cash flow for 2092, and measures the present values as of January 1, 2018, one year later. Thus, the present value of estimated future net cash flows (excluding the combined OASI and DI Trust Fund asset reserves at the start of the period) decreased (became more negative) when the 75-year valuation period changed from 2017-2091 to 2018-2092. In addition, the effect on the level of asset reserves in the combined OASI and DI Trust Funds of changing the valuation period is measured by assuming all values projected in the prior valuation for the year 2017 are realized. The change in valuation period increased the starting level of asset reserves in the combined OASI and DI Trust Funds. As a result, the present value of the estimated future net cash flows decreased by $0.6 trillion.

From the period beginning on January 1, 2016 to the period beginning on January 1, 2017

The effect on the 75-year present values of changing the valuation period from the prior valuation period (2016-2090) to the current valuation period (2017-2091) is measured by using the assumptions for the prior valuation and extending them to cover the current valuation. Changing the valuation period removes a small negative net cash flow for 2016, replaces it with a much larger negative net cash flow for 2091, and measures the present values as of January 1, 2017, one year later. Thus, the present value of estimated future net cash flows (excluding the combined OASI and DI Trust Fund asset reserves at the start of the period) decreased (became more negative) when the 75-year valuation period changed from 2016-2090 to 2017-2091. In addition, the effect on the level of asset reserves in the combined OASI and DI Trust Funds of changing the valuation period is measured by assuming all values projected in the prior valuation for the year 2016 are realized. The change in valuation period increased the starting level of asset reserves in the combined OASI and DI Trust Funds. As a result, the present value of the estimated net cash flows decreased by $0.6 trillion.

Changes in Demographic Data, Assumptions, and Methods

From the period beginning on January 1, 2017 to the period beginning on January 1, 2018

The ultimate demographic assumptions for the current valuation (beginning on January 1, 2018), with the exception of a small decrease of 10,000 LPR immigrants per annum in the future, are the same as those for the prior valuation. However, the starting demographic values and the way these values transition to the ultimate assumptions were changed.

- Final birth rate data for 2016 indicated slightly lower birth rates than were assumed in the prior valuation.
- Recent fertility data suggests that the short-term increase in the total fertility rate used in the prior valuation to account for an assumed deferral in childbearing (resulting from the recent economic downturn) was no longer warranted. The observed persistent drop in the total fertility rate in recent years is now assumed to be a loss of potential births rather than just a deferral for this period.
- Incorporating 2015 mortality data obtained from the National Center for Health Statistics (NCHS) for ages under 65 and preliminary 2015 mortality data from Medicare experience for ages 65 and older resulted in higher death rates for all future years than were projected in the prior valuation.
- More recent LPR and other-than-LPR immigration data and historical population data were included.

Inclusion of the recent birth rate data, eliminating the short-term increase in fertility, and immigration data decreased the present value of estimated future net cash flows, while the inclusion of the recent mortality data and historical population data increased the present value of estimated future net cash flows.

There was one notable change in demographic methodology:

- Improved the method for projecting mortality rates by marital status by utilizing recent data from NCHS and the American Community Survey.

Inclusion of this new method increased the present value of estimated future net cash flows. Overall, changes to these assumptions caused the present value of the estimated future net cash flows to increase by $0.1 trillion.

From the period beginning on January 1, 2016 to the period beginning on January 1, 2017

The ultimate demographic assumptions for the current valuation (beginning on January 1, 2017) are the same as those for the prior valuation. However, the starting demographic values and the way these values transition to the ultimate assumptions were changed.

- Final birth rate data for 2015 indicated slightly lower birth rates than were assumed in the prior valuation.

- Incorporating 2014 mortality data obtained from NCHS at ages under 65 and preliminary 2014 mortality data from Medicare experience at ages 65 and older resulted in higher death rates for all future years than were projected in the prior valuation.
- More recent legal and other-than-legal immigration data and historical population data were included.

Inclusion of the recent birth rate data and immigration data decreased the present value of estimated future net cash flows, while the inclusion of the recent mortality data increased the present value of estimated future net cash flows.

There were no notable changes in demographic methodology. Overall, changes to these assumptions caused the present value of the estimated net cash flows to decrease by $0.1 trillion.

Changes in Economic Data, Assumptions, and Methods

From the period beginning on January 1, 2017 to the period beginning on January 1, 2018

The ultimate economic assumptions for the current valuation (beginning on January 1, 2018), are the same as those for the prior valuation. However, the starting economic values and the way these values transition to the ultimate assumptions were changed.

- The estimated level of potential GDP was reduced by about 1 percent in 2017 and throughout the projection period, primarily due to the slow growth in labor productivity for 2010 through 2017 and low unemployment rates in 2017. This lower estimated level of potential GDP means that cumulative growth in actual GDP is 1 percent less over the remainder of the projected recovery than was assumed in the prior valuation.
- Near-term interest rates were decreased, reflecting a more gradual path for the rise to the ultimate real interest rate than was assumed in the prior valuation.
- New data from the Bureau of Economic Analysis (BEA) indicated lower-than-expected ratios of labor compensation to GDP for 2016 and 2017, while new data from the IRS indicated lower-than-expected ratios of taxable payroll to GDP for 2016 and 2017. This new data led to assumed extended recoveries in these ratios to the unchanged ultimate ratios.

The changes in near-term interest rates and GDP decreased the present value of estimated future net cash flows. The new data from BEA and IRS and the resulting extended recovery in the ratios of labor compensation to GDP and taxable payroll to GDP increased the present value of estimated future net cash flows.

There was one notable change in economic methodology:

- Improved the method for projecting educational attainment among women in age groups 45-49 and 50-54 in the labor force participation model.

Inclusion of this new method increased the present value of estimated future net cash flows. Overall, changes to these assumptions caused the present value of the estimated future net cash flows to decrease by $0.5 trillion.

From the period beginning on January 1, 2016 to the period beginning on January 1, 2017

For the current valuation (beginning on January 1, 2017), there was one change to the ultimate economic assumptions.

- The ultimate average real-wage differential is assumed to be 1.20 percent in the current valuation, which is close to a 0.01 percent decrease relative to the previous valuation (even though both ultimate average real-wage differentials are 1.20 when rounded to two decimal places).

In addition to this change in ultimate assumption, the assumed path of the real-wage differential in the first 10 years of the projection period was also lower than in the previous valuation. This led to 0.05 percent lower annual growth in the average annual wage in covered employment in the first 10 years. The lower long-term and near-term real-wage differential assumptions are based on new projections by the CMS of faster growth in employer sponsored group health insurance premiums. Because these premiums are not subject to the payroll tax, faster growth in these premiums means that a smaller share of employee compensation will be in the form of wages that are subject to the payroll tax. The lower real-wage differential decreased the present value of estimated future net cash flows.

Otherwise, the ultimate economic assumptions for the current valuation are the same as those for the prior valuation. However, the starting economic values and the way these values transition to the ultimate assumptions were changed. The most notable change was updating the near-term interest rates. Also notable was an assumed weaker recovery from the recent recession than previously expected, which led to a reduction in the ultimate level of actual and potential GDP of about 1.0 percent for all years after the short-range period. The changes in near-term interest rates and GDP decreased the present value of estimated future net cash flows. Other, smaller changes in starting values and near-term growth assumptions combined to decrease the present value of estimated future net cash flows. Overall, changes to these assumptions caused the present value of the estimated future net cash flows to decrease by $0.6 trillion.

Changes in Law or Policy

From the period beginning on January 1, 2017 to the period beginning on January 1, 2018

The monetary effect of the changes in law or policy on the present value of estimated future net cash flows of the OASDI program was not significant at the consolidated level. Please refer to SSA's financial statements for further information related to the impact of the changes in law or policy on the present value of estimated future net cash flows of the OASDI program.

From the period beginning on January 1, 2016 to the period beginning on January 1, 2017

The monetary effect of the changes in law or policy on the present value of estimated future net cash flows of the OASDI program was not significant at the consolidated level. Please refer to SSA's financial statements for further information related to the impact of the changes in law or policy on the present value of estimated future net cash flows of the OASDI program.

Changes in Methodology and Programmatic Data

From the period beginning on January 1, 2017 to the period beginning on January 1, 2018

Several methodological improvements and updates of program-specific data are included in the current valuation (beginning on January 1, 2018). The most significant are identified below.

- The prior valuation assumed 99.0 percent of fully insured women (excluding those who are receiving a disability or widow benefit) were in receipt of a retired-worker benefit at age 70. The current valuation increases this percentage to 99.5 which is equivalent to the assumption for men.
- For the current valuation, a 10 percent sample of newly-entitled worker beneficiaries in 2015 was used to project average benefit levels of retired-worker and disabled-worker beneficiaries. This sample was updated from the 2013 sample used for the prior valuation. In addition, the method used to estimate earnings histories for retired-worker beneficiaries becoming newly entitled in each year after 2017 has been expanded to better match targeted average taxable earnings levels for each of nine birth cohorts (those becoming entitled at ages 62 through 70 in a year).
- Recent data and estimates provided by the Office of Tax Analysis (OTA) at the Treasury were incorporated, which indicate higher ultimate levels of revenue from taxation of OASDI benefits than assumed in the prior valuation. These higher levels are primarily due to changes OTA made in their modeling, resulting in a larger share of benefits being subject to income tax.
- The current valuation incorporates both a better data source for determining the total number of months of retroactive benefits for newly awarded disabled-worker beneficiaries and a new adjustment factor which better aligns projected months of disabled-worker retroactive benefit entitlement with observed historical experience.

Increasing the percentage of fully insured women who are in receipt of a retired-worker benefit at age 70 decreased the present value of estimated cash flows. Updating the sample year for average benefit level calculations, increasing the ultimate taxation of benefits ratios, and the changes to estimates of retroactive benefit payments increased the present value of estimated future net cash flows. Overall, changes to these assumptions caused the present value of the estimated future net cash flows to increase by $0.2 trillion.

From the period beginning on January 1, 2016 to the period beginning on January 1, 2017

The monetary effect of the changes in methodology and programmatic data on the present value of estimated future net cash flows was not significant at the consolidated level. Please refer to SSA's financial statements for further information related to the impact of changes in methodology and programmatic data on the present value of estimated future net cash flows of the OASDI program.

Medicare

The SCSIA shows two reconciliations for Medicare: (1) changes from the period beginning on January 1, 2017, to the period beginning on January 1, 2018, and (2) changes from the period beginning on January 1, 2016, to the period beginning on January 1, 2017. All estimates relating to the Medicare program in the SCSIA represent values that are incremental to the prior change. As an example, the present values shown for demographic data, assumptions, and methods represent the additional effect that these assumptions have, once the effects from the change in the valuation period and projection base have been considered. In general, an increase in the present value of net cash flows represents a positive change (improving financing), while a decrease in the present value of net cash flows represents a negative change (worsening financing).

Assumptions Used for the Components of the Changes for the Medicare Program

The present values included in the SCSIA are for the current and prior years and are based on various economic and demographic assumptions used for the intermediate assumptions in the Medicare Trustees Reports for these years. Table 1B summarizes these assumptions for the current year.

From the period beginning on January 1, 2017 to the period beginning on January 1, 2018

Present values as of January 1, 2017 are calculated using interest rates from the intermediate assumptions of the 2017 Medicare Trustees Report. All other present values in this part of the SCSIA are calculated as a present value as of January 1, 2018. Estimates of the present value of changes in social insurance amounts due to changing the valuation period, projection base, demographic assumptions, and law are presented using the interest rates under the intermediate assumptions of the 2017 Medicare Trustees Report. Since interest rates are an economic estimate and all estimates in the table are incremental to the prior change, the estimates of the present values of changes in economic and health care assumptions are calculated using the interest rates under the intermediate assumptions of the 2018 Medicare Trustees Report.

From the period beginning on January 1, 2016 to the period beginning on January 1, 2017

Present values as of January 1, 2016 are calculated using interest rates from the intermediate assumptions of the 2016 Medicare Trustees Report. All other present values in this part of the SCSIA are calculated as a present value as of January 1, 2017. Estimates of the present value of changes in social insurance amounts due to changing the valuation period, projection base, demographic assumptions, and law are presented using the interest rates under the intermediate assumptions of the 2016 Medicare Trustees Report. Since interest rates are an economic estimate and all estimates in the table are incremental to the prior change, the estimates of the present values of changes in economic and health care assumptions are calculated using the interest rates under the intermediate assumptions of the 2017 Medicare Trustees Report.

Changes in Valuation Period

From the period beginning on January 1, 2017 to the period beginning on January 1, 2018

The effect on the 75-year present values of changing the valuation period from the prior valuation period (2017-2091) to the current valuation period (2018-2092) is measured by using the assumptions for the prior valuation period and extending them, in the absence of any other changes, to cover the current valuation period. Changing the valuation period removes a small negative net cash flow for 2017, replaces it with a much larger negative net cash flow for 2092, and measures the present values as of January 1, 2018, one year later. Thus, the present value of estimated future net cash flow (including or excluding the combined Medicare Trust Fund assets at the start of the period) decreased (became more negative) when the 75-year valuation period changed from 2017-2091 to 2018-2092. In addition, the effect on the level of assets in the combined Medicare Trust Funds of changing the valuation period is measured by assuming all values projected in the prior valuation for the year 2017 are realized. The change in valuation period resulted in a very slight increase in the starting level of assets in the combined Medicare Trust Funds. As a result, the present value of the estimated future net cash flows decreased by $1.3 trillion.

From the period beginning on January 1, 2016 to the period beginning on January 1, 2017

The effect on the 75-year present values of changing the valuation period from the prior valuation period (2016-2090) to the current valuation period (2017-2091) is measured by using the assumptions for the prior valuation period and extending them, in the absence of any other changes, to cover the current valuation period. Changing the valuation period removes a small negative net cash flow for 2016, replaces it with a much larger negative net cash flow for 2091, and measures the present values as of January 1, 2017, one year later. Thus, the present value of estimated future net cash flow (including or excluding the combined Medicare Trust Fund assets at the start of the period) decreased (became more negative) when the 75-year valuation period changed from 2016-2090 to 2017-2091. In addition, the effect on the level of assets in the combined Medicare Trust Funds of changing the valuation period is measured by assuming all values projected in the prior valuation for the year 2016 are realized. The change in valuation period increased the starting level of assets in the combined Medicare Trust Funds. As a result, the present value of the estimated net cash flows decreased by $1.4 trillion.

Changes in the Demographic Data, Assumptions, and Methods

From the period beginning on January 1, 2017 to the period beginning on January 1, 2018

The demographic assumptions used in the Medicare projections are the same as those used for OASDI and are prepared by the Office of the Chief Actuary at SSA.

The ultimate demographic assumptions for the current valuation (beginning on January 1, 2018), with the exception of a small decrease of 10,000 LPR immigrants per annum in the future, are the same as those for the prior valuation. However, the starting demographic values and the way these values transition to the ultimate assumptions were changed.

- Final birth rate data for 2016 indicated slightly lower birth rates than were assumed in the prior valuation.
- Recent fertility data suggests that the short-term increase in the total fertility rate used in the prior valuation to account for an assumed deferral in childbearing (resulting from the recent economic downturn) was no longer warranted. The observed persistent drop in the total fertility rate in recent years is now assumed to be a loss of potential births rather than just a deferral for this period.
- Incorporating 2015 mortality data obtained from the NCHS at ages under 65 and preliminary 2015 mortality data from Medicare experience at ages 65 and older resulted in higher death rates for all future years than were projected in the prior valuation.
- More recent LPR and other-than-LPR immigration data and historical population data were included.

There was one notable change in demographic methodology:

- Improved the method for projecting mortality rates by marital status by utilizing recent data from NCHS and the American Community Survey.

These changes lowered overall Medicare enrollment for the current valuation period and resulted in an increase in the estimated future net cash flow. The present value of estimated income and expenditures are both lower for Part A and Part B but higher for Part D. Overall, changes to these assumptions caused the present value of the estimated future net cash flows to increase by $0.6 trillion.

From the period beginning on January 1, 2016 to the period beginning on January 1, 2017

The demographic assumptions used in the Medicare projections are the same as those used for the OASDI and are prepared by the Office of the Chief Actuary at SSA.

The ultimate demographic assumptions for the current valuation (beginning on January 1, 2017 are the same as those for the prior valuation. However, the starting demographic values and the way these values transition to the ultimate assumptions were changed.

- Final birth rate data for 2015 indicated slightly lower birth rates than were assumed in the prior valuation.
- Incorporating 2014 mortality data obtained from the NCHS at ages under 65 and preliminary 2014 mortality data from Medicare experience at ages 65 and older resulted in higher death rates for all future years than were projected in the prior valuation.
- More recent legal and other-than-legal immigration data and historical population data were included.

There were no consequential changes in demographic methodology.

These changes slightly lowered overall Medicare enrollment for the current valuation period and resulted in a decrease in the estimated future net cash flow. The present value of estimated expenditures is lower for Part A but slightly higher for Parts B and D; and the present value of estimated income is also higher for Parts B and D but lower for Part A. Overall, changes to these assumptions caused the present value of the estimated future net cash flows to decrease by $0.1 trillion.

Changes in Economic and Other Health Care Assumptions

From the period beginning on January 1, 2017 to the period beginning on January 1, 2018

The economic assumptions used in the Medicare projections are the same as those used for the OASDI and are prepared by the Office of the Chief Actuary at SSA.

The ultimate economic assumptions for the current valuation (beginning on January 1, 2018) are the same as those for the prior valuation. However, the starting economic values and the way these values transition to the ultimate assumptions were changed.

- The estimated level of potential GDP was reduced by about 1 percent in 2017 and throughout the projection period, primarily due to the slow growth in labor productivity for 2010 through 2017 and low unemployment rates in 2017. This lower estimated level of potential GDP means that cumulative growth in actual GDP is 1 percent less over the remainder of the projected recovery than was assumed in the prior valuation.
- Near-term interest rates were decreased, reflecting a more gradual path for the rise to the ultimate real interest rate than was assumed in the prior valuation.
- New data from the BEA indicated lower-than-expected ratios of labor compensation to GDP for 2016 and 2017, while new data from the IRS indicated lower-than-expected ratios of taxable payroll to GDP for 2016 and 2017.
- This new data led to assumed extended recoveries in these ratios to the unchanged ultimate ratios.

There was one notable change in economic methodology:

- Improved the method for projecting educational attainment among women in age groups 45-49 and 50-54 in the labor force participation model.

The health care assumptions are specific to the Medicare projections. The following health care assumptions were changed in the current valuation.

- Utilization rate assumptions for inpatient hospital services were decreased.
- Utilization rate and case mix for skilled nursing facilities services were decreased. Payment rates to private health plans are higher than projected in last year's report primarily due to higher risk scores and increased coding by plans.
- Higher projected drug manufacturer rebates.

The net impact of these changes resulted in a decrease in the estimated future net cash flow for total Medicare. For Part A, these changes resulted in an overall decrease in the estimated future net cash flow. For Part B, these changes increased the present value of estimated future expenditures (and also income). For Part D, these changes decreased the present value of estimated expenditures (and also income). Overall, the net impact of these changes caused the present value of estimated future net cash flows to decrease by $1.5 trillion.

From the period beginning on January 1, 2016 to the period beginning on January 1, 2017

The economic assumptions used in the Medicare projections are the same as those used for the OASDI and are prepared by the Office of the Chief Actuary at SSA.

For the current valuation (beginning on January 1, 2017), there was one change to the ultimate economic assumptions.

- The ultimate average real-wage differential is assumed to be 1.20 percent in the current valuation period, which is close to a 0.01 percent decrease relative to the previous valuation (even though both ultimate average real-wage differentials are 1.20 when rounded to two decimal places).

In addition to this change in assumption, the assumed real-wage differential for the first ten years of the projection period averaged 0.05 percent lower than in the previous valuation. The lower long-term and near-term real-wage differential assumptions are based on new projections of faster growth in employer sponsored group health insurance premiums. Because these premiums are not subject to the payroll tax, faster growth in these premiums means that a smaller share of employee compensation will be in the form of wages that are subject to the payroll tax.

Otherwise, the ultimate economic assumptions for the current valuation are the same as those for the prior valuation. However, the starting economic values and the way these values transition to the ultimate assumptions were changed. Most significantly, an assumed weaker recovery from the recent recession than previously expected led to a reduction in the ultimate level of actual and potential GDP of about 1.0 percent for all years after the short-range period.

The health care assumptions are specific to the Medicare projections. The following health care assumptions were changed in the current valuation.

- Utilization rate assumptions for inpatient hospital and skilled nursing facilities services were decreased.
- The number of beneficiaries enrolled in Medicare Advantage plans and their relative costs are slightly different from last year's assumptions.
- Lower productivity increases through 2025, resulting in higher provider payment updates.
- Higher projected drug rebates.
- Change in projection methodology of drug spending for Part B patients with end-stage renal disease.

The net impact of these changes resulted in an increase in the estimated future net cash flow for total Medicare. For Part A, these changes resulted in an increase to the present value of estimated future expenditures and income, with an overall increase in the estimated future net cash flow. For Part B, these changes increased the present value of estimated future expenditures (and also income). For Part D, these changes decreased the present value of estimated expenditures (and also income). Overall, the net impact of these changes caused the present value of the estimated future net cash flows to decrease by $0.3 trillion.

Changes in Law

From the period beginning on January 1, 2017 to the period beginning on January 1, 2018

Most of the provisions enacted as part of Medicare legislation since the prior valuation date had little or no impact on the program. The following provisions did have a financial impact on the present value of the 75-year estimated future income, expenditures, and net cash flow.

- The *Disaster Tax Relief and Airport and Airway Extension Act of 2017* (P.L. 115-63, enacted on September 29, 2017) included one provision that affects the HI and SMI Part B programs.

- *An Act to Provide for Reconciliation Pursuant to Titles II and V of the Concurrent Resolution on the Budget for Fiscal Year 2018* (P.L. 115-97, enacted on December 22, 2017, and also referred to as the Tax Cuts and Jobs Act of 2017) included three provisions that affect the HI program.
- *An Act Making Further Continuing Appropriations for the Fiscal Year Ending September 30, 2018*, and for Other Purposes (P.L. 115-120, enacted on January 22, 2018) included one provision that affects the HI and SMI programs.
- The *BBA of 2018* (P.L. 115-123, enacted on February 9, 2018) included provisions that affect the HI and SMI programs.

Overall, these provisions resulted in a decrease in the estimated future net cash flow for total Medicare. For Part A, these changes resulted in an increase to the present value of estimated future expenditures and a slight decrease to the present value of estimated future income, with an overall net decrease in the estimated future net cash flow. For Part B and Part D, these changes increased the present value of estimated future expenditures (and also income). Overall, these changes to these assumptions caused the present value of the estimated future net cash flows to decrease by $1.0 trillion.

From the period beginning on January 1, 2016 to the period beginning on January 1, 2017

The monetary effect of the changes in law or policy on the present value of estimated future net cash flows of the Medicare programs was not significant at the consolidated level. Please refer to HHS's financial statements for further information related to the impact of the changes in law or policy on the present value of estimated future net cash flows of the Medicare programs.

Change in Projection Base

From the period beginning on January 1, 2017 to the period beginning on January 1, 2018

Actual income and expenditures in 2017 were different than what was anticipated when the 2017 Medicare Trustees Report projections were prepared. Part A payroll tax income in 2017 was lower attributable to lowered wages and expenditures were higher than anticipated based on actual experience. Part B total income and expenditures were higher than estimated based on actual experience. For Part D, actual income and expenditures were both lower than prior estimates. The net impact of the Part A, B, and D projection base changes is a decrease in the estimated future net cash flow. Actual experience of the Medicare Trust Funds between January 1, 2017 and January 1, 2018 is incorporated in the current valuation and is less than projected in the prior valuation. Overall, the net impact of the Part A, B, and D projection base changes is a decrease in the estimated future net cash flows by $0.9 trillion.

From the period beginning on January 1, 2016 to the period beginning on January 1, 2017

Actual income and expenditures in 2016 were different than what was anticipated when the 2016 Medicare Trustees Report projections were prepared. Part A payroll tax income in 2017 was lower attributable to lowered wages, and expenditures were higher than anticipated based on actual experience. Part B total income and expenditures were higher than estimated based on actual experience. For Part D, actual income and expenditures were both lower than prior estimates. The net impact of the Part A, B, and D projection base changes is an increase in the estimated future net cash flow. Actual experience of the Medicare Trust Funds between January 1, 2016 and January 1, 2017 is incorporated in the current valuation and is slightly more than projected in the prior valuation. Overall, the net impact of the Part A, B, and D projection base changes is an increase in the estimated future net cash flows by $0.7 trillion.

Other

The present values included in the SCSIA for the Railroad Retirement program are for the current and prior valuation and are based on various employment, demographic, and economic assumptions that reflect the RRB's reasonable estimate of expected future financial and actuarial status of the trust funds. For a more detailed description of the primary reasons for the changes in the 2018 and 2017 SCSIA, refer to RRB's financial statements.

The significant assumptions used in the projections of the Black Lung social insurance program, referenced earlier in this note, affect the amounts reported on the SCSIA, which presents the net change in the open group measure of the BLDTF for the years ended September 30, 2018 and 2017, and provide information about the change. For a more detailed description of the primary reasons for the changes in the 2018 and 2017 SCSIA, refer to DOL's financial statements.

Note 23. Long-Term Fiscal Projections

The SLTFP are prepared pursuant to SFFAS No. 36, *Comprehensive Long-Term Projections for the U.S. Government*, as amended. The basic financial statement, Note 23, and related unaudited required supplementary information (RSI) provide information to aid readers of the *Financial Report* in assessing whether current policies for federal spending and taxation can be sustained and the extent to which the cost of public services received by current taxpayers will be shifted to future taxpayers. This assessment requires prospective information about receipts and spending, the resulting debt, and how these amounts relate to the size of the economy. A sustainable policy is defined as one where the ratio of federal debt held by the public to GDP (the debt-to-GDP ratio) is ultimately stable or declining. The *Financial Report* does not address the sustainability of State and local government fiscal policy.

The projections and analysis presented here are extrapolations based on an array of assumptions described in detail below. A fundamental assumption is that current federal policy will not change. This assumption is made so as to inform the question of whether current fiscal policy is sustainable and, if it is not sustainable, the magnitude of needed reforms to make fiscal policy sustainable. The projections are therefore neither forecasts nor predictions. If policy changes are implemented, perhaps in response to projections like those presented here, then actual financial outcomes will be different than those projected. The methods and assumptions underlying the projections are subject to continuing refinement.

The projections focus on future cash flows, and do not reflect either the accrual basis or the modified-cash basis of accounting. These cash-based projections reflect receipts or spending at the time cash is received or when a payment is made by the government. In contrast, accrual-based projections would reflect amounts in the time period in which income is earned or when an expense or obligation is incurred. The cash basis accounting underlying the long-term fiscal projections is consistent with methods used to prepare the SOSI and the generally cash-based federal budget.

The basic financial statement, Long-Term Fiscal Projections for the U.S. Government, displays the present value of 75-year projections for various categories of the federal government's receipts and non-interest spending.[9] The projections for fiscal years 2018 and 2017 are expressed in present value dollars and as a percent of the present value of GDP[10] as of September 30, 2018 and September 30, 2017, respectively. The present value of a future amount, for example $1 billion in October 2093, is the amount of money that if invested on September 30, 2018 in an account earning the government borrowing rate would have a value of $1 billion in October 2093.[11]

The present value of a receipt or spending category over 75 years is the sum of the annual present value amounts. When expressing a receipt or spending category over 75 years as a percent of GDP, the present value dollar amount is divided by the present value of GDP over 75 years. Measuring receipts and spending as a percent of GDP is a useful indicator of the economy's capacity to sustain federal government programs.

Fiscal Projections

Receipt categories in the long-term fiscal projections include individual and corporate income taxes, Social Security and Medicare payroll taxes, and a residual remaining category of "other receipts." Non-interest spending categories include discretionary spending that is funded through annual appropriations, such as spending for national security; and mandatory (entitlement) spending that is generally funded with permanent or multi-year appropriations, such as spending for Social Security and Medicare. This year's projections for Social Security and Medicare are based on the same economic and demographic assumptions that underlie the 2018 Social Security and Medicare trustees' reports and the 2018 SOSI, while comparative information presented from last year's report is based on the 2017 Social Security and Medicare trustees' reports and the 2017 SOSI[12]. Projections for the other categories of receipts and spending are consistent with the economic and demographic assumptions in the trustees' reports. The projections assume the continuance of current policy which, as is explained below, can be different than current law in cases where lawmakers have in the past periodically changed the law in a consistent way.

The projections shown in the basic statement are made over a 75-year time frame, consistent with the time frame featured in the Social Security and Medicare trustees' reports. However, these projections are for fiscal years starting on

[9] For the purposes of this analysis, spending is defined in terms of outlays. In the context of federal budgeting, spending can either refer to budget authority – the authority to commit the government to make a payment; to obligations – binding agreements that will result in payments, either immediately or in the future; or to outlays – actual payments made.

[10] GDP is a standard measure of the overall size of the economy and represents the total market value of all final goods and services produced domestically during a given period of time. The components of GDP are: private sector consumption and investment, government consumption and investment, and net exports (exports less imports). Equivalently, GDP is a measure of the gross income generated from domestic production over the same time period.

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

[12] Social Security and Medicare Trustees' Reports can be found at https://www.ssa.gov/OACT/TR/.

October 1, whereas the trustees' reports feature calendar-year projections. Using fiscal years allows the projections to start from the actual budget results from fiscal years 2018 and 2017.

Changes in Long-Term Fiscal Projections

Present Value (PV) of 75-Year Projections	Trillions of $	Percent of GDP
Receipts less non-interest spending as of September 30, 2017.......	(16.2)	(1.2) %
Components of Change:		
Change due to Economic and Demographic Assumptions...........	1.2	0.1
Change due to Program-Specific Actuarial Assumptions..............	(3.8)	(0.3)
Change due to Updated Budget Data.......................................	(15.4)	(1.1)
Change in Reporting Period..	(0.5)	-
Change in Model Technical Assumptions..................................	(11.5)	(0.8)
Total	(29.9)	(2.1)
Receipts less non-interest spending as of September 30, 2018.......	(46.2)	(3.3)

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

This year's estimate of the 75-year present value imbalance of receipts less non-interest spending is 3.3 percent of the 75-year present value of GDP, compared to 1.2 percent as was projected in last year's *Financial Report*.[13] The above table reports the effects of various factors on the updated projections.

- The largest factor, increasing the imbalance by 1.1 percent of the 75-year present value of GDP ($15.4 trillion), is attributable to actual budget results for fiscal year 2018 and the budgetary estimates published in the 2019 Midsession Review. This includes lower corporate and individual income tax receipts resulting from the TCJA of 2017, and higher non-defense discretionary outlays as a result of the increased discretionary spending caps in the BBA.
- The second largest factor is the effect of adjustments to the model's technical assumptions, which increases the imbalance by 0.8 percent of the 75-year present value of GDP ($11.5 trillion). As discussed below in the section on assumptions used in the projections, corporate income tax receipts are held to their proportion of the budget's share of GDP to reflect enactment of the TCJA of 2017. Discretionary spending is assumed to grow from the 2019 cap levels established in the BBA, subject to Joint Select Committee on Deficit Reduction (Joint Committee) sequestration enforcement[14].
- The third largest factor, increasing the imbalance by 0.3 percent of the 75-year present value of GDP ($3.8 trillion) is due to changes in Social Security, Medicare and Medicaid actuarial assumptions[15].
- The next largest change in the table – decreasing the imbalance by 0.1 percent of GDP ($1.2 trillion) – is attributable to changes in economic and demographic assumptions. Higher near-term wage and GDP projections increased individual income tax and social insurance receipts.

The penultimate row in the basic financial statement shows that this year's estimate of the overall 75-year present value of receipts less non-interest spending is -3.3 percent of the 75-year present value of GDP (negative $46.2 trillion, as compared to GDP of $1,406.3 trillion). This imbalance can be broken down by funding source. Spending exceeded receipts by 1.7 percent of GDP ($24.2 trillion) among programs funded by the government's general revenues, and there is an imbalance of 1.6 percent of GDP ($22.1 trillion[16]) for the combination of Social Security (OASDI) and Medicare Part A,

[13] More information on the projections in last year's *Financial Report* can be found in Note 23 to the Financial Statements here: https://fiscal.treasury.gov/reports-statements/#

[14] For further discussion of spending assumptions, see the section "Assumptions Used and Relationship to Other Financial Statements" below.

[15] For more information on Social Security, Medicare and Medicaid actuarial estimates, refer to Note 22—Social Insurance.

[16] The 75-year present value imbalance for Social Security and Medicare Part A of $22.1 trillion is comprised of several line items from the SLTFP – Social Security outlays net of Social Security payroll taxes ($22.0 trillion) and Medicare Part A outlays net of Medicare payroll taxes ($8.8 trillion) – as well as subcomponents of these programs not presented separately in the statement. These subcomponents include Social Security and Medicare Part A administrative costs that are classified as non-defense discretionary spending ($0.7 trillion) and Social Security and Medicare Part A income other than payroll taxes: taxation of benefits (-$4.4 trillion), federal employer share (-$1.3 trillion), and other income (-$3.7 trillion).

which under current law are funded with payroll taxes and not in any material respect with general revenues.[17, 18] By comparison, the fiscal year 2017 projections showed that programs funded by the government's general revenues had an excess of receipts over spending of 0.2 percent of GDP ($3.3 trillion) while the payroll tax-funded programs had an imbalance of spending over receipts of 1.5 percent of GDP ($19.6 trillion).

Sustainability and the Fiscal Gap

As discussed further in the unaudited RSI, the projections in this report indicate that current policy is not sustainable. If current policy is left unchanged, the projections show the debt-to-GDP ratio will rise about 6 percentage points to a level of 84 percent by 2022, exceed 100 percent by 2030, and reach 530 percent in 2093. Moreover, if the trends that underlie the 75-year projections were to continue, the debt-to-GDP ratio would continue to rise beyond the 75-year window.

The fiscal gap measures how much the primary surplus (receipts less non-interest spending) must increase in order for fiscal policy to achieve a target debt-to-GDP ratio in a particular future year. In these projections, the fiscal gap is estimated over a 75-year period, from 2019 to 2093, and the target debt-to-GDP ratio is equal to the ratio at the beginning of the projection period, in this case the debt-to-GDP ratio at the end of fiscal year 2018.

The 75-year fiscal gap under current policy is estimated at 4.1 percent of GDP, which is 21.9 percent of the 75-year present value of projected receipts and 18.6 percent of the 75-year present value of non-interest spending. This estimate of the fiscal gap is 2.1 percentage points larger than was estimated in 2017 (2.0 percent of GDP).

The projections show that projected primary deficits average 3.2 percent of GDP over the next 75 years under current policy. If policies were put in place that would result in a zero fiscal gap, the average primary surplus over the next 75 years would be 0.8 percent of GDP, 4.1 percentage points higher than the projected present value of receipts less non-interest spending shown in the basic financial statement. In these projections, closing the fiscal gap requires running a substantially positive level of primary surplus, rather than simply eliminating the primary deficit. The primary reason is that the projections assume future interest rates will exceed the growth rate of GDP. Achieving primary balance (that is, running a primary surplus of zero) implies that the debt held by the public grows each year by the amount of interest spending, which under these assumptions would result in debt growing faster than GDP.

Assumptions Used and Relationship to Other Financial Statements

A fundamental assumption underlying the projections is that current federal policy (defined below) does not change. The projections are therefore neither forecasts nor predictions, and do not consider large infrequent events such as natural disasters, military engagements, or economic crises. By definition, they do not build in future changes to policy, such as recent proposals to repeal the ACA or increase border infrastructure and security. If policy changes are enacted, perhaps in response to projections like those presented here, then actual fiscal outcomes will be different than those projected.

Even if policy does not change, actual spending and receipts could differ materially from those projected here. Long-range projections are inherently uncertain and are necessarily based on simplifying assumptions. For example, one key simplifying assumption is that interest rates paid on debt held by the public remain unchanged, regardless of the amount of debt outstanding. To the contrary, it is likely that future interest rates would increase if the debt-to-GDP ratio rises as shown in these projections. To help illustrate this uncertainty, projections that assume higher and lower interest rates are presented in the "Alternative Scenarios" discussion in the unaudited RSI section of this *Financial Report*.

As is true for prior long-term fiscal projections for the *Financial Report*, the assumptions for GDP, interest rates, and other economic and demographic variables underlying this year's projections are the same assumptions that underlie the most recent Social Security and Medicare trustees' report projections, adjusted for historical revisions that occur annually. The use

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[17] Social Security and Medicare Part A expenditures can exceed payroll tax revenues in any given year to the extent that there are sufficient balances in the respective trust funds; these balances derive from past excesses of payroll tax revenues over expenditures and interest earned on those balances and represent the amount the General Fund owes the respective trust fund programs. When spending does exceed payroll tax revenues, as has occurred each year since 2008 for Medicare Part A and 2010 for Social Security, the excess spending is financed first with interest due from the General Fund and secondly with a drawdown of the trust fund balance; in either case, the spending is ultimately supported by general revenues or borrowing. Under current law, benefits for Social Security and Medicare Part A can be paid only to the extent that there are sufficient balances in the respective trust funds. In order for the long-term fiscal projections to reflect the full size of these program's commitments to pay future benefits, the projections assume that all scheduled benefits will be financed with borrowing to the extent necessary after the trust funds are depleted.

[18] The fiscal imbalances reported in the long-term fiscal projections are limited to future outlays and receipts. They do not include the initial level of publicly-held debt, which was $15.8 trillion in 2018 and $14.7 trillion in 2017, and therefore they do not by themselves answer the question of how large fiscal reforms must be to make fiscal policy sustainable, or how those reforms divide between reforms to Social Security and Medicare Part A and to other programs. Other things equal, past cash flows (primarily surpluses) for Social Security and Medicare Part A reduced federal debt at the end of 2018 by $3.1 trillion (the trust fund balances at that time); the contribution of other programs to federal debt at the end of 2018 was therefore $18.9 trillion. Because the $22.1 trillion imbalance between outlays and receipts over the next 75 years for Social Security and Medicare Part A does not take account of the Social Security and Medicare Part A trust fund balances, it overstates the magnitude of reforms necessary to make Social Security and Medicare Part A solvent over 75 years by $3.1 trillion. The $3.1 trillion combined Social Security and Medicare Part A trust fund balance represents a claim on future general revenues.

of discount factors consistent with the Social Security trustees' rate allows for consistent present value calculations over 75 years between the SLTFP and the SOSI.

The following bullets summarize the key assumptions used for the categories of receipts and spending presented in the basic financial statement and the disclosures:

- **Social Security:** Projected Social Security (OASDI) spending excludes administrative expenses, which are classified as discretionary spending, and is based on the projected expenditures in the 2018 Social Security trustees' report for benefits and for the Railroad Retirement interchange. The projections of Social Security payroll taxes and Social Security spending are based on future spending and payroll taxes projected in the 2018 Social Security trustees' report, adjusted for presentational differences and converted to a fiscal year basis. More information about the assumptions for Social Security cost growth can be found in Note 22 and the unaudited RSI discussion of Social Insurance.
- **Medicare:** Projected Medicare spending also excludes administrative expenses, which are classified as other mandatory spending, and is based on projected incurred expenditures from the 2018 Medicare trustees' report. The projections here make some adjustments to the trustees' report projections. Medicare Part B and D premiums, as well as State contributions to Part D, are subtracted from gross spending in measuring Part B and Part D spending, just as they are subtracted from gross cost to yield net cost in the financial statements.[19] Here, as in the federal budget, premiums are treated as "negative spending" rather than receipts since they represent payment for a service rather than payments obtained through the government's sovereign power to tax. This is similar to the financial statement treatment of premiums as "earned" revenue as distinct from all other sources of revenue, such as taxes. The projections are based on Medicare spending in the Medicare trustees' report, adjusted for presentational differences and converted to a fiscal year basis. Medicare Part A payroll taxes are projected similarly. More information about the assumptions for Medicare cost growth can be found in Note 22 and the unaudited RSI discussion of Social Insurance. As discussed in Note 22, there is uncertainty about whether the reductions in health care cost growth projected in the Medicare trustees' report will be fully achieved. Note 22 illustrates this uncertainty by considering Medicare cost growth assumptions under varying policy assumptions.
- **Medicaid:** The Medicaid spending projections start with the projections from the *2017 Medicaid Actuarial Report* prepared by CMS's Office of the Actuary[20]. These projections are based on recent trends in Medicaid spending; the demographic, economic, and health cost growth assumptions in the 2017 Medicare Trustees' Report; and projections of the effect of the ACA on Medicaid enrollment. The projections, which end in 2026, are adjusted to accord with the actual Medicaid expenditures in fiscal year 2018. After 2026, the projections assume no further change in State Medicaid coverage under the ACA, and the numbers of old-age beneficiaries (65-plus years) and non-old-age beneficiaries (less than 65 years) are expected to grow at the same rates as the old-age and non-old-age populations, respectively. Medicaid costs per beneficiary are assumed to grow at the same rate as Medicare benefits per beneficiary, as is generally consistent with the experience since 1987. Between 1987 and 2017, the average annual growth rate of spending per beneficiary for Medicaid and Medicare were within 0.3 percentage point of each other. Projections of Medicaid spending are subject to added uncertainty related to: (1) assumed reductions in health care cost growth discussed above in the context of Medicare, (2) the projected size of the Medicaid enrolled population, which depends on a variety of factors, including future State actions regarding the ACA Medicaid expansion, and (3) certain limitations relating to the data used to generate the projected per enrollee expenditures in the 2017 Medicaid actuarial report.
- **Other Mandatory Spending:** Other mandatory spending, which includes federal employee retirement, veterans' disability benefits, and means-tested entitlements other than Medicaid, is projected in two steps. First, spending prior to the automatic spending cuts called for by the enforcement provisions of the BCA is projected and, second, the effect of the BCA enforcement is projected through its statutory expiration in 2027. With regard to pre-BCA spending: (1) current mandatory spending components that are judged permanent under current policy are assumed to increase by the rate of growth in nominal GDP starting in 2019, implying that such spending will remain constant as a percent of GDP[21]; and (2) projected spending for insurance exchange subsidies starting in 2019 grows with growth in the non-elderly population and with the National Health Expenditure (NHE) projected per enrollee cost growth for other private health insurance for the NHE projection period (through 2026 for the fiscal year 2018 projections), and with growth in per enrollee health care costs as projected for the Medicare program after that period. As discussed in Note 22, there is uncertainty about whether the reductions in health care cost growth

[19] Medicare Part B and D premiums and State contributions to Part D are subtracted from the Part B and D spending displayed in the SLTFP. The total 75-year present value of these subtractions is $13.6 trillion, or 1.0 percent of GDP.
[20] Christopher J. Truffer, Christian J. Wolfe, and Kathryn E. Rennie, *2017 Actuarial Report on the Financial Condition for Medicaid*, Office of the Actuary, Centers for Medicare and Medicaid Services, United States Department of Health and Human Services, September 2017.
[21] This assumed growth rate for other mandatory programs exceeds the growth rate in the most recent OMB and CBO 10-year budget baselines.

projected in the Medicare trustees' report will be fully achieved. Projected exchange subsidy spending as a percent of GDP remains below the failsafe provision in the ACA that limits this spending to 0.504 percent of GDP.

- **Defense and Non-defense Discretionary Spending:** Prior to 2018, the projections assumed discretionary spending followed the caps established by the BCA of 2011, as later amended, and then grew with nominal GDP in the years after the caps expired. However, discretionary spending has not been limited to the caps established in the BCA. Instead, budget deals in 2013, 2015, and 2018 raised the caps in each of the years 2014 through 2019. Therefore, as a reasonable representation of current policy, the 2018 projections assume discretionary spending is grown at the same rate as nominal GDP beginning after 2019, rather than being limited to the statutory caps, subject to Joint Committee spending controls[22]. Projected OCO spending, which is not subject to the caps, is assumed to grow from the level in the most recent year at the same rate as nominal GDP. To illustrate sensitivity to different assumptions, present value calculations under alternative discretionary growth scenarios are presented in the unaudited "Alternative Scenarios" RSI section.
- **Receipts (Other than Social Security and Medicare Payroll Taxes):** Individual income taxes equal the same share of wages and salaries as in the current law baseline projection in the President's fiscal year 2019 Budget. That baseline accords with current policy as defined above, including the continuation of the individual income, estate, and gift tax provisions of the TCJA of 2017[23] and the tendency of effective tax rates to increase as growth in income per capita outpaces inflation (also known as "bracket creep"). After reaching about 20 percent of wages and salaries in 2024, individual income taxes increase gradually to 27 percent of wages and salaries in 2093 as real taxable incomes rise over time and an increasing share of total income is taxed in the higher tax brackets. Through the first 10 years of the projections, corporate tax receipts as a percent of GDP reflect the economic and budget assumptions used in developing the 2019 Midsession Review's ten-year advance budgetary estimates[24]. After this time, corporate tax receipts grow at the same rate as nominal GDP. All other receipts also reflect 2019 Midsession Review levels as a share of GDP throughout the budget window and grow with GDP outside of the budget window. Corporate tax receipts peak at 1.6 percent of GDP in 2025 before falling to 1.3 percent of GDP in 2028, where they stay for the remainder of the projection period. The ratio of all other receipts combined, excluding corporate tax receipts, to GDP is estimated to be 1.5 percent in 2019, after which it gradually declines to 1.3 percent of GDP, where it remains through the projection period. To illustrate uncertainty, present value calculations under higher and lower receipts growth scenarios are presented in the "Alternative Scenarios" section.
- **Debt and Interest Spending:** Interest spending is determined by projected interest rates and the level of outstanding debt held by the public. The long-run interest rate assumptions accord with those in the 2018 Social Security trustees' report.[25] The average interest rate over the projection period is 5.0 percent. These rates are also used to convert future cash flows to present values as of the start of fiscal year 2019. Debt at the end of each year is projected by adding that year's deficit and other financing requirements to the debt at the end of the previous year.

The methods described above include two significant revisions from those used to produce the fiscal year 2017 projections. Corporate tax receipts are now projected separately from all other receipts to incorporate the effects of the TCJA of 2017. In prior years, corporate income tax receipts were not modeled independently, they were included in "Other Receipts[26]." To project corporate income tax receipts, the model uses their implied share of GDP over the years 2019 through 2028 from the 2019 Midsession Review to determine receipts in those years, and then grows receipts with nominal GDP thereafter. "Other Receipts" are now projected similarly; instead of using their 30-year historical average share of GDP, the receipts' implied share of GDP over the years 2019 to 2028, as presented in the 2019 Midsession Review, are used to determine receipts over this period. Afterward, receipts grow with GDP. The second significant revision is that discretionary spending no longer follows the caps established under the BCA through 2021. Instead, discretionary spending starts from the outlays implied by BBA 2018's cap level for 2019, and grows with GDP thereafter (subject to Joint Committee enforcement).

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[22] The BCA of 2011 established statutory caps on discretionary spending for fiscal years 2012 through 2021, and established a Joint Committee tasked with identifying $1.2 trillion in deficit reduction. The failure of the Joint Committee to propose, and Congress to enact, legislation sufficient to reduce the deficit triggers automatic spending reductions through adjustments to the discretionary spending limits and sequestration of mandatory spending. Mandatory sequestration has been extended in various statutes and currently extends through 2027. After 2027, the projections assume the automatic reductions continue as a constant share of projected GDP.

[23] The expiring individual income and estate and gift tax provisions of the TCJA are assumed to continue past their legal expiration on December 31, 2025 because of the recent historical pattern of such tax rates being extended; additional discussion may be found in the last section of this note.

[24] The Midsession Review is an annual report to the Congress, delivered on or before July 15th, that contains revised budget estimates resulting from changes in economic assumptions, Presidential initiatives, and enacted legislation that have occurred since transmittal of the President's Budget.

[25] As indicated in the more detailed discussion of Social Insurance in Note 22 to the financial statements.

[26] "Other receipts", which included corporate income tax receipts prior to 2018, were modeled by assuming they maintain their 30-year historical average share of GDP throughout the modeling period.

Departures of Current Policy from Current Law

The long-term fiscal projections are made on the basis of current policy, which in some cases is different from current law. The notable differences between current policy that underlies the projections and current law are: (1) discretionary spending is assumed to not be limited by caps established by the BCA; (2) projected spending, receipts, and borrowing levels assume raising or suspending the current statutory limit on federal debt; (3) continued discretionary appropriations are assumed throughout the projection period; (4) scheduled Social Security and Medicare benefit payments are assumed to occur beyond the projected point of trust fund depletion; (5) many mandatory programs with expiration dates prior to the end of the 75-year projection period are assumed to be reauthorized; and (6) tax changes under the TCJA are assumed to continue beyond 2025. The last difference aligns with the historical pattern of such legislation being routinely extended or made permanent. As is true in the Medicare trustees' report and in the SOSI, the projections incorporate programmatic changes already scheduled in law, such as the ACA productivity adjustment for non-physician Medicare services and the expiration of certain physician bonus payments in 2025.

Note 24. Stewardship Land and Heritage Assets

Stewardship PP&E consists of items whose physical properties resemble those of general PP&E traditionally capitalized in financial statements. However, stewardship PP&E differs from general PP&E in that their values may be indeterminable or may have little meaning (for example, museum collections, monuments, assets acquired in the formation of the nation) or that allocating the cost of such assets to accounting periods that benefit from the ownership of such assets is meaningless. Stewardship PP&E includes stewardship land (land not acquired for or in connection with general property, plant, and equipment) and heritage assets (for example, federal monuments and memorials and historically or culturally significant property). The majority of stewardship land was acquired by the government during the first century of the nation's existence.

Investments in stewardship land are reported on a non-financial basis. For example, measurement may be based on physical units, such as acres of land. National forests, parks, and historic sites are examples of stewardship land.

Additional detailed information concerning stewardship land, such as entity stewardship policies, physical units by major categories, and the condition of stewardship land, can be obtained from the financial statements of DOI, DOD, TVA, and USDA.

Heritage assets are government-owned assets that have one or more of the following characteristics:

- Historical or natural significance;
- Cultural, educational, or artistic importance; or
- Significant architectural characteristics.

Like stewardship land, heritage assets are also reported on a non-financial basis. Measurement may be reported by the total units, such as the total number of National Parks reported by DOI. The public entrusts the government with these assets and holds it accountable for their preservation. Examples of heritage assets include the Declaration of Independence, the U.S. Constitution, and the Bill of Rights preserved by the National Archives. Also included are national monuments/structures such as the Washington Monument, the Lincoln Memorial and the LOC. Many other sites such as battlefields, historic structures, and national historic landmarks are placed in this category, as well.

Heritage assets are classified into two categories: collection and non-collection. Collection type heritage assets include objects gathered and maintained for exhibition, for example, museum collections, art collections, and library collections. Non-collection type heritage assets include parks, memorials, monuments, and buildings. In some cases, heritage assets may serve two purposes: a heritage function and general government operations. In those cases, the heritage asset should be considered a multi-use heritage asset if the predominant use of the asset is in general government operations (e.g., the main Treasury building used as an office building). The cost of acquisition, improvement, reconstruction, or renovation of multi-use heritage assets should be capitalized as general PP&E and depreciated over its estimated useful life.

This discussion of the government's heritage assets is not exhaustive. Rather, it highlights significant heritage assets reported by federal entities. Please refer to the individual financial statements of the DOC, VA, DOT, State, DOD, as well as websites for the LOC (https://loc.gov), the Smithsonian Institution (https://si.edu), and the Architect of the Capitol (https://aoc.gov) for additional information on multi-use heritage assets, entity stewardship policies, and physical units by major categories.

Note 25. Disclosure Entities and Related Parties

SFFAS No. 47, *Reporting Entity* provides criteria for identifying organizations that are consolidation entities, disclosure entities and related parties, and how such organizations are reported within the *Financial Report*. For consolidation entities, the assets, liabilities, results of operations, and related activity are consolidated into the government's financial statements. For disclosure entities and related parties, balances and transactions with such entities are included in the financial statements and certain information about their relationship with the federal government is disclosed in the notes to the consolidated financial statements. Disclosure entities and related parties are important to the *Financial Report* but are not consolidated into the government's financial statements.

Disclosure Entities

Disclosure entities are organizations similar to consolidation entities in that they are either (a) in the budget, (b) majority owned by the government, (c) controlled by the government, or (d) would be misleading to exclude. Disclosure entities have a greater degree of autonomy with the government than consolidation entities. In addition, organizations may be owned or controlled by the government as a result of (a) regulatory actions (such as organizations in receivership or conservatorship) or (b) other government intervention actions. Under such regulatory or other intervention actions, if the relationship with the government is not expected to be permanent, such entities generally would be classified as disclosure entities based on their characteristics taken as a whole.

Based on the criteria in GAAP for federal entities, the disclosure entities in the *Financial Report* are FR System, Fannie Mae, Freddie Mac, and National Railroad Passenger Corporation (more commonly referred to as Amtrak). In addition, there are additional disclosure entities reported by component reporting entities that do not meet the qualitative or quantitative criteria in SFFAS No. 47 to be reported in the *Financial Report*.

Federal Reserve System

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

The 12 FRBs are chartered under the Federal Reserve Act, which requires each member bank to own the capital stock of its FRB. Each FRB has a board of directors that exercises supervision and control of each FRB, with three members appointed by the Board, and six board members elected by their member banks. The FRBs participate in formulating and conducting monetary policy, distributing currency and coin, and serving as the government's fiscal agent, as well as the fiscal agent for other federal entities and fiscal principals. Fiscal principals, generally speaking, relate to banks, credit unions, savings and loans institutions. Additionally, the FRBs provide short-term loans to depository institutions and loans to participants in programs or facilities with broad-based eligibility in unusual and crucial circumstances when approved by the Board and the Secretary of the Treasury.

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

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

- The FRBs are required by Board policy to transfer their excess earnings to the government, which are included in Other Taxes and Receipts on the Statements of Operations and Changes in Net Position.

- **Federal Reserve System Structure**

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

The FOMC is comprised of the seven Board members and five of the 12 FRB presidents, and is charged with formulating and conducting monetary policy primarily through open market operations (the purchase and sale of certain securities in the open market), the principal tool of national monetary policy. These operations affect the amount of reserve balances available to depository institutions, thereby influencing overall monetary and credit conditions.

The 12 FRBs are chartered under the Federal Reserve Act, which requires each member bank to own the capital stock of its FRB. Supervision and control of each FRB is exercised by a board of directors, of which three are appointed by the Board of the FR System, and six are elected by their member banks. The FRBs participate in formulating and conducting monetary policy, distribute currency and coin, and serve as fiscal agents for the government, and other federal entities. Additionally, the FRBs provide short-term loans to depository institutions and loans to participants in programs or facilities with broad-based eligibility in unusual and exigent circumstances when approved by the Board and the Secretary of the Treasury.

- **Federal Reserve Monetary Policy Action**

During fiscal year 2018, the Federal Reserve FOMC gradually raised its target range for the federal funds rate and gradually reduced its securities in the SOMA. The Federal Reserve raised its target range for the federal funds rate from 1.0 – 1.25 percent in September 2017, to 2.0 – 2.25 percent in September 2018. The Federal Reserve reduced its U.S. Treasury and federal agency and government-sponsored enterprise mortgage-backed securities in the SOMA on its balance sheet from approximately $4.4 trillion as of September 30, 2017, to approximately $4.1 trillion as of September 30, 2018.

- **Federal Reserve System Assets, Liabilities, Revenues, Expenses, Gains, and Losses**

The FRBs hold Treasury and other securities in the SOMA for the purpose of conducting monetary policy. As of September 30, 2018, Treasury securities held by the FRBs totaled $1,782.5 billion, which excludes $531.8 billion in Treasury Securities used in overnight reverse repurchase transactions. As of September 30, 2017, Treasury securities held by the FRBs totaled $1,964.7 billion, which excludes $502.0 billion in Treasury securities used in overnight reverse repurchase transactions. Such securities are included in federal debt securities held by the public and accrued interest (see Note 11—Federal Debt Securities Held by the Public and Accrued Interest). For fiscal years ended September 30, 2018, and 2017, Treasury incurred interest cost relating to the FRB's U.S. Treasury holdings amounting to $64.1 billion and $63.8 billion, respectively, which is included in interest on Treasury securities held by the public on the Statement of Net Cost. Unrestricted Cash held on deposit at the FRBs as of September 30, 2018, and 2017, was $378.5 billion and $153.3 billion, respectively, and are included in cash and other monetary assets. In addition, restricted cash as of September 30, 2018, and 2017, was $31.6 billion and $26.1 billion, respectively; a significant portion is held on deposit at the FRBs (see Note 2—Cash and Other Monetary Assets).

Treasury securities are generally subject to the same market (principally interest-rate) and credit risks as other financial instruments. In the open market, the FRBs purchase and sell Treasury securities as a mechanism for controlling the money supply.

Financial and other information concerning the FR System, including financial statements for the Board and the FRBs, may be obtained at https://federalreserve.gov.

- **FRB Residual Earnings Transferred to the Government**

FRBs generate income from interest earned on securities, reimbursable services provided to federal entities, and the provision of priced services to depository institutions, as specified by the *Monetary Control Act of 1980*. Although the FRBs generate earnings from carrying out open market operations (via the earnings on securities held in the SOMA account), their execution of these operations is for the purpose of accomplishing monetary policy rather than generating earnings. Each FRB is required by Board policy to transfer to the government its residual (or excess) earnings, after providing for the cost of operations, payment of dividends, and surplus funds not to exceed an FRB's allocated portion of an aggregate of $7.5 billion for all FRBs. These residual earnings may vary due to, among other things, changes in the SOMA balance levels that may occur in conducting monetary policy. If an FRB's earnings for the year are not sufficient to provide for the cost of operations, payment of dividends, or allocated portion of $7.5 billion aggregate surplus funds limitation, an FRB will suspend its payments to the government until such earnings become sufficient. These funds are part of restricted cash at the Federal Reserve (see Note 2—Cash and Other Monetary Assets). The FRB residual earnings of $70.8 billion and $81.3 billion for fiscal years ended September 30, 2018, and 2017, respectively, are reported as other taxes and receipts on the Statements of Operations and Changes in Net Position. Accounts and taxes receivables, net, includes a receivable for FRB's residual earnings which represents the earnings due to the General Fund as of September 30, but not collected by the General Fund until after the end of the month. As of September 30, 2018, and 2017, accounts receivable on FRB's residual earnings are $0.4 billion and $0.3 billion, respectively (see Note 3—Accounts and Taxes Receivables, Net).

Fannie Mae and Freddie Mac

In 2008, during the financial crisis, the government placed Fannie Mae and Freddie Mac under conservatorship to help ensure their financial stability. For fiscal year 2018, these entities meet the criteria in SFFAS No. 47, for disclosure entities as both (a) "receiverships and conservatorships," and, (b) as entities wherein "federal government intervention actions resulted in control or ownership" with intervention actions not expected to be permanent. Accordingly, these entities are not consolidated into the *Financial Report*. This treatment is consistent with the reporting for these entities in fiscal year 2017 under SFFAC No. 2, *Entity and Display* (see Note 8—Investments in Government-Sponsored Enterprises for additional information).

Amtrak

Amtrak was incorporated in 1971 pursuant to the *Rail Passenger Service Act of 1970* and is authorized to operate a nationwide system of passenger rail transportation. Amtrak is a private, for-profit corporation under 49 U.S.C. § 24301 and District of Columbia law. It is not a department, entity, or instrumentality of the federal government. Amtrak's classification as a disclosure entity is attributed to (a) being listed in the budget, (b) is financed mostly by sources other than taxes, and (c) governed by an independent Board of Directors comprised of 10 directors. The Secretary of Transportation (Secretary), who is a director by statute, and eight of the other Amtrak directors, are appointed by the President with the advice and consent of the U.S. Senate. The 10th board member, appointed by the board, is the President and Chief Executive Officer of Amtrak. Amtrak does not take actions on behalf of the government but benefits the national economy by providing a transportation option in 46 states and the District of Columbia.

The government (through the DOT) owns 100% of Amtrak's preferred stock (109,396,994 shares of $100 par value). Each share of preferred stock is convertible into ten shares of common stock. The common stockholders have voting rights for "amendments to Amtrak's Articles of Incorporation proposed by the Board of Directors and for certain other extraordinary events." Although Section 4.02(g) of the Amtrak Articles of Incorporation allow for the conversion of preferred stock to common stock, the government would not convert its holdings without Congressional authorization. The government does not recognize the Amtrak preferred stock in its financial statements because, under the corporation's current financial structure, the preferred shares do not have a liquidation preference over the common shares, the preferred shares do not have any voting rights, and dividends are neither declared nor in arrears.

In addition to the purchase/ownership of the Amtrak preferred stock, the government has provided funding to Amtrak, since 1972, primarily through grants and loans. Amtrak receives grants from the government that cover a portion of the corporation's annual operating expenses and capital investments. Funding provided to Amtrak through grant agreements are included in the government's annual budget. Amtrak has a history of recurring operating losses and is dependent on subsidies from the government to operate. Amtrak's ability to continue operating in its current form is dependent upon the continued receipt of subsidies from the government.

The government has possession of two long-term notes with Amtrak. The first note is for $4.0 billion and matures in 2975 and, the second note is for $1.1 billion and matures in 2082 with renewable 99-year terms. Interest is not accruing on these notes as long as the current financial structure of Amtrak remains unchanged. If the financial structure of Amtrak changes, both principal and accrued interest are due and payable. The government does not recognize the long-term notes in its financial statements since the notes, with maturity dates of 2975 and 2082, are considered fully uncollectible due to the lengthy terms, Amtrak's history of operating losses, and ability to generate funds for repayment.

Financial and other information concerning Amtrak including financial statements may be obtained at https://www.amtrak.com/reports-documents.

Related Parties

Related parties exist if the existing relationship, or one party to the existing relationship, has the ability to exercise significant influence over the party's policy decisions. Related parties do not meet the principles for inclusion, but are reported in the *Financial Report* if they maintain relationships of such significance that it would be misleading to exclude.

Based on the criteria in SFFAS No. 47, the related parties reported in the *Financial Report* are Federal Home Loan Banks (FHLBanks), IMF, Multilateral Banks, and Private Export Funding Corporation (PEFCO). In addition, there are additional related parties reported by component reporting entities that do not meet the criteria to be reported in the *Financial Report*.

Federal Home Loan Banks

The government is empowered with supervisory and regulatory oversight of the 11 FHLBanks. The government is responsible for ensuring that each regulated entity operates in a safe and sound manner, including maintenance of adequate capital and internal control, and carries out its housing and community development finance missions. Each FHLBank operates as a separate federally chartered corporation with its own board of directors, management, and employees. The FHLBanks were organized under the *Federal Home Loan Bank Act of 1932* and are GSEs. The FHLBanks are not government entities and do not receive financial support from taxpayers. The government does not guarantee, directly or indirectly, the debt securities or other obligations of FHLBanks. The FHLBanks are regulated by the FHFA, an independent federal entity.

By law, in the event of certain adverse circumstances, Treasury is authorized to purchase up to $4.0 billion of obligations of the FHLBanks. Treasury has not used such authority. Also, in accordance with the *Government Corporations Control Act*, Treasury prescribes certain terms concerning the FHLBanks issuance of obligation to the public. Financial and other information concerning FHLBanks including financial statements may be obtained at http://www.fhlbanks.com/.

International Monetary Fund and Multilateral Development Banks

The government currently maintains related party relationships with the IMF and the MDBs. The IMF is an international organization of 189 member countries that works to foster global monetary cooperation, secure financial stability, sustain economic growth, and reduce poverty around the world. The government holds the largest quota subscription of any member. The government's quota subscription serves as the key determinant for the government's 16.5 percent share of voting rights in various IMF decisions for which the government has a substantial voice. Since certain key IMF determinations require approval by at least 85 percent of the total voting power, the government (represented by the Secretary of the Treasury) exercises significant influence via its 16.5 percent voting share. The government's holdings in the IMF are in the form of highly liquid and interest-bearing instruments. The government has a liability due to the IMF, as well as an additional commitment (see Note 16—Other Liabilities and Note 19—Commitments for additional information). Historically, the government has not experienced a loss of value on its IMF holdings and management does not believe it is likely that the government will experience future losses on its holdings or as a result of its additional commitments.

Additionally, the government invests in and provides funding to the MDBs to support poverty reduction and promote sustainable economic growth in developing countries. The MDBs provide financial and technical support to foster economic growth and entrepreneurship, strengthen institutions, address the root causes of instability in fragile and conflict-affected countries, and respond to global crisis. The government's participation in the MDBs is in the form of financial contributions used to ensure the effectiveness and impact of the MDBs' global development agenda. The U.S. has voting power in each of the MDBs to which it contributes, ranging from approximately 6 percent to 50 percent (see Note 19—Commitments for additional information).

Private Export Funding Corporation

The financial statements reflect the results of agreements with PEFCO. PEFCO, which is owned by a consortium of private-sector banks, industrial companies and financial services institutions, makes and purchases from private sector lenders, medium-term and long-term fixed-rate and variable-rate loans guaranteed by EXIM Bank to foreign borrowers to purchase U.S. made equipment "export loans."

EXIM Bank's credit and guarantee agreement with PEFCO provides that EXIM Bank will guarantee the due and punctual payment of interest on PEFCO's secured debt obligations which EXIM Bank has approved, and grants to EXIM Bank a broad measure of supervision over PEFCO's major financial management decisions, including the right to have representatives be present in all meetings of PEFCO's board of directors, advisory board, and exporters' council, and to review PEFCO's financials and other records. However, EXIM Bank does not have voting rights and does not influence normal operations. This agreement extends through December 31, 2020.

In addition, PEFCO has an agreement with EXIM Bank which provides that EXIM Bank will generally provide PEFCO with an unconditional guarantee covering the due and punctual payment of principal and interest on export loans PEFCO makes and purchases. PEFCO's guarantees on the export loans plus the guarantees on the secured debt obligations aggregating to $5,196.6 million at September 30, 2018 and $6,120.0 million at September 30, 2017, are included by EXIM Bank in the total for guarantee, insurance and undisbursed loans and the allowance related to these transactions.

EXIM Bank received fees totaling $40.8 million in fiscal year 2018 and $60.7 million in fiscal year 2017 for the agreements.

Note 26. Subsequent Events

Disaster Relief

In September and October 2018, Hurricanes Florence and Michael struck the continental United States. While the full future effect of these disasters is still unknown, there will be an impact on some federal government entities as a result of assisting these areas as they strive to recover. The fiscal year 2018 *Financial Report* did not reflect any liabilities for additional disaster relief amounts that may be authorized by legislation enacted after September 30, 2018. The SBA has begun to increase its rate of administrative spending as it conducts its disaster response. This spending is consistent with SBA's experience in responding to prior disasters. The SBA could experience future variations in the performance of existing disaster and business loan portfolios as businesses in the affected areas strive to recover.

Statutory Debt Limit

As of September 30, 2018, debt subject to the statutory debt limit was $21,474.8 billion. However, per P.L. 115-56, the statutory debt limit was temporarily suspended through March 1, 2019. Effective March 2, 2019, the statutory debt limit was set at $21,987.7 billion and on March 4, 2019, the Secretary of the Treasury notified the Congress that the statutory debt limit would be reached on or after that day. When delays in raising the debt limit occur, Treasury often must deviate from its normal cash and debt management operations and take a number of what it calls "extraordinary measures" to meet the government's obligations as they come due without exceeding the debt limit. Treasury began taking these extraordinary actions on March 4, 2019.

United States Government Required Supplementary Information (Unaudited) For the Fiscal Years Ended September 30, 2018, and 2017

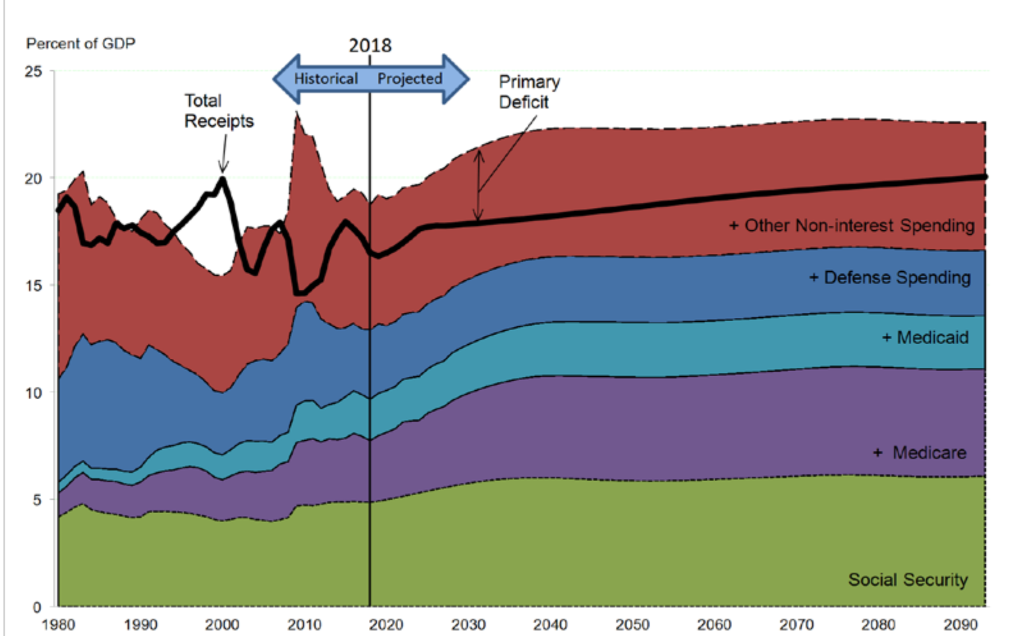
The Sustainability of Fiscal Policy

One of the important purposes of the *Financial Report* is to help citizens and policymakers assess whether current fiscal policy is sustainable and, if it is not, the urgency and magnitude of policy reforms necessary to make fiscal policy sustainable. A sustainable policy is one where the ratio of debt held by the public to GDP (the debt-to-GDP ratio) is ultimately stable or declining.

As discussed below, the projections in this report indicate that current policy is not sustainable. If current policy is left unchanged, the projections show the debt-to-GDP ratio will rise from 78 percent in 2018 to 84 percent by 2022, to over 100 percent by 2030, and to 530 percent in 2093. For comparison, under the 2017 projections, the debt-to-GDP ratio fell about 4 percentage points between 2017 and 2023 before commencing a steady rise, exceeding its 2017 level by 2029, exceeding 100 percent by 2037, and reaching 297 percent in 2092.

These conclusions are rooted in the projected trends in receipts, spending, and deficits in the context of current law and policy, although, as described in the following pages, there is considerable uncertainty surrounding these projections. The projections are on the basis of policies currently in place and are neither forecasts nor predictions. Changes in policy – from repealing the ACA and increasing border security and infrastructure, to more routine developments such as changes in aggregate funding for discretionary program – could have a significant effect on eventual fiscal outcomes.

Chart 1: Historical and Current Policy Projections for Receipts and the Composition of Non-interest Spending



Current Policy Projections for Primary Deficits

A key determinant of growth in the debt-to-GDP ratio and hence fiscal sustainability is the ratio of the primary deficit-to-GDP. The primary deficit is the difference between non-interest spending and receipts, and the primary deficit-to-GDP ratio is the primary deficit expressed as a percent of GDP. As shown in Chart 1, the primary deficit-to-GDP ratio spiked during 2009 through 2012 due to the 2008-09 financial crisis and the ensuing severe recession, as well as the increased spending and temporary tax reductions enacted to stimulate the economy and support recovery. These elevated primary deficits resulted in a sharp increase in the ratio of debt to GDP, which rose from 39 percent at the end of 2008 to 70 percent at the end of 2012. As an economic recovery took hold, the primary deficit ratio fell, averaging 1.9 percent of GDP over 2013 through 2018. This deficit level was still high enough that the debt held by the public increased further relative to GDP, ending 2018 at 78 percent. The primary deficit ratio is projected to rise to 2.9 percent in 2019 and then shrink slightly as the economy grows. After 2024, however, increased spending for Social Security and health programs due in part to the continued retirement of the baby boom generation is projected to result in increasing primary deficits that reach 3.0 percent of GDP in 2028. The primary deficit peaks at 4.1 percent of GDP in 2039, gradually decreases beyond that point as the aging of the population continues at a slower pace, and reaches 2.5 percent in 2093.

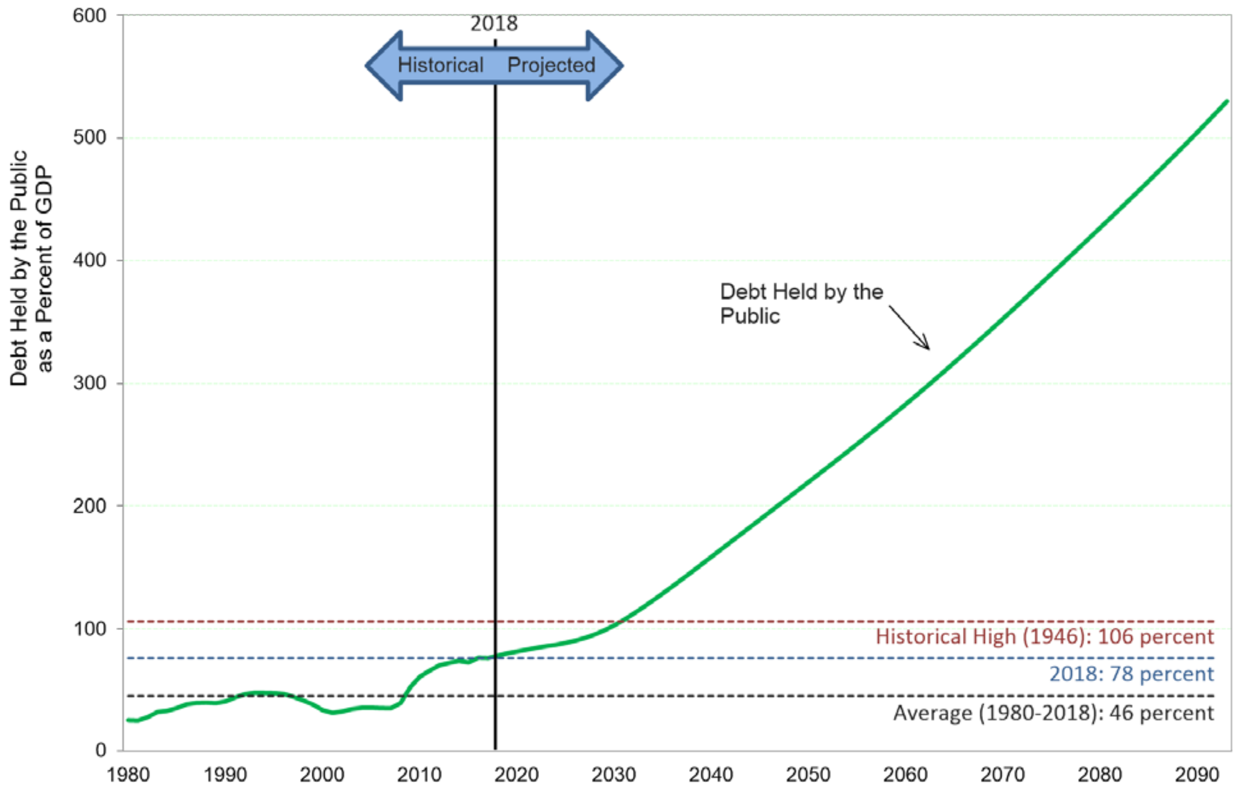
Trends in the primary deficit are heavily influenced by tax receipts. The receipt share of GDP was markedly depressed in 2009 through 2012 because of the recession and tax reductions enacted as part of the ARRA and the *Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010*. The share subsequently increased to 18 percent of GDP by 2015 then decreased to 16.5 percent by 2018, after enactment of the TCJA of 2018 and below its 30-year average of 17.3 percent. Receipts are projected to grow slightly more rapidly than GDP over the projection period as increases in real (i.e., inflation-adjusted) incomes cause more taxpayers and a larger share of income to fall into the higher individual income tax brackets. Other possible paths for the receipts-to-GDP ratio and the implications for projected debt held by the public are analyzed in the “Alternative Scenarios” section.

On the spending side, the non-interest spending share of GDP is projected to rise gradually from 18.7 percent in 2018 to 21.0 percent of GDP in 2029 and ends at 22.6 percent in 2093, the end of the projection period. Beginning in 2020, these increases are principally due to faster growth in Medicare, Medicaid, and Social Security spending (see Chart 1). The aging of the baby boom generation over the next 25 years, among other factors, is projected to increase the Social Security, Medicare, and Medicaid spending shares of GDP by about 1.0 percentage points, 1.7 percentage points, and 0.6 percentage points, respectively. After 2035, the Social Security and Medicaid spending shares of GDP remain relatively stable, while the Medicare spending share of GDP continues to increase, albeit at a slower rate, due to projected increases in health care costs and population aging.

Current Policy Projections for Debt and Interest Payments

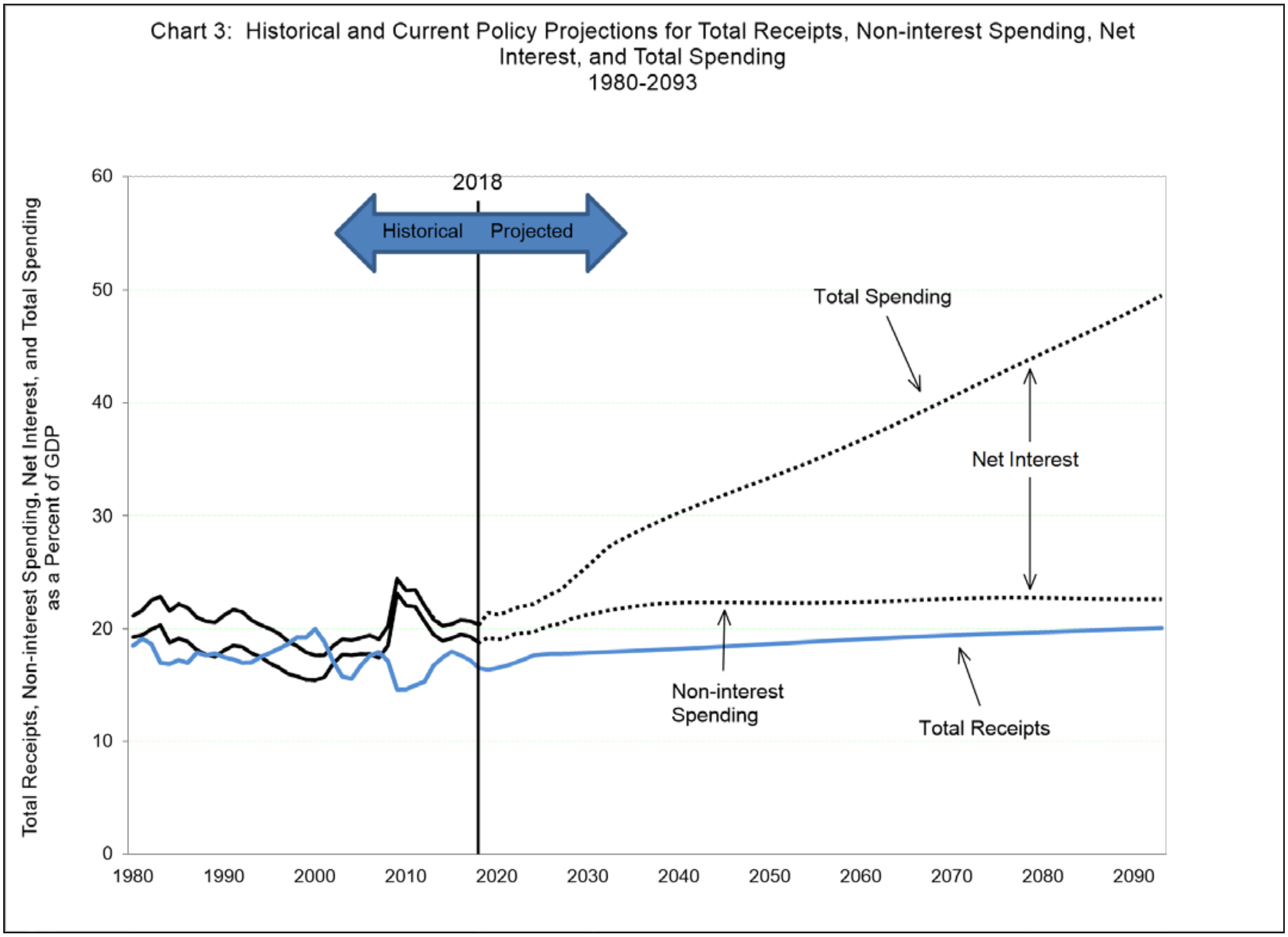
The primary deficit projections in Chart 1, along with projections for interest rates and GDP, determine the projections for the debt-to-GDP ratio shown in Chart 2. That ratio was 78 percent at the end of fiscal year 2018, and under current policy is projected to be 84 percent by 2022, over 100 percent by 2030, and 530 percent in 2093. The continuous rise of the debt-to-GDP ratio indicates that current policy is unsustainable.

Chart 2: Historical and Current Policy Projections for Debt Held by the Public
1980-2093



The change in debt held by the public from one year to the next is approximately equal to the budget deficit, the difference between total spending and total receipts.[1] Total spending is non-interest spending plus interest spending. Chart 3 shows that the rapid rise in total spending and the unified deficit (Total Receipts less Total Spending) is almost entirely due to projected net interest, which results from the growing debt. As a percent of GDP, interest spending was 1.6 percent in 2018, and under current policy is projected to reach 7.4 percent in 2038 and 26.9 percent in 2093.

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



Another way of viewing the change in the financial outlook in this year's report relative to previous years' reports is in terms of the projected debt-to-GDP ratio in 2091, the last year of the 75-year projection period used in the fiscal year 2016 report. This ratio is projected to reach 513 percent in the fiscal year 2018 projections, which compares with 293 percent projected in the fiscal year 2017 projections and 252 percent projected in the fiscal year 2016 projections.[2]

The Cost of Delay in Closing the 75-Year Fiscal Gap

The longer policy action to close the fiscal gap[3] is delayed, the larger the post-reform primary surpluses must be to achieve the target debt-to-GDP ratio at the end of the 75-year period. This can be illustrated by varying the years in which reforms closing the fiscal gap are initiated while holding the target ratio of debt to GDP in 2093 equal to the 2018 ratio (78 percent). Three timeframes for reforms are considered, each one beginning in a different year, and each one increasing the primary surplus relative to current policy by a fixed percent of GDP starting in the reform year. The analysis shows that the longer policy action is delayed, the larger the post-reform primary surplus must be to bring the debt-to-GDP ratio to 78 percent of GDP in 2093. Future generations are burdened by delays in policy changes because delay necessitates higher primary surpluses during their lifetimes, and those higher primary surpluses must be achieved through some combination of lower spending and higher taxes and other receipts.

As previously shown in Chart 1, under current policy, primary deficits occur throughout the projection period. Table 1 shows primary surplus changes necessary to make the debt-to-GDP ratio in 2093 equal to its level in 2018 under each of the three timeframes. If reform begins in 2019, then it is sufficient to raise the primary surplus share of GDP by 4.1 percentage

[2] For further information on changes from the 2016 projections, see the unaudited RSI in the 2017 *Financial Report*.

[3] The fiscal gap reflects how much the primary surplus (receipts less non-interest spending) must increase to maintain the debt-to-GDP ratio at the 2018 level of 78 percent. See Note 23 for a more complete discussion of the fiscal gap.

points in every year between 2019 and 2093 in order for the debt-to-GDP ratio in 2093 to equal its level in 2018 (78 percent). This policy raises the average 2019-2093 primary surplus-to-GDP ratio from -3.5 percent to +0.8 percent.

Table 1
Costs of Delaying Fiscal Reform

Timing of Reforms	Required Change in Average Primary Surplus
Reform in 2019 (No Delay)	4.1 percent of GDP between 2019 and 2093
Reform in 2029 (Ten-Year Delay)	4.9 percent of GDP between 2029 and 2093
Reform in 2039 (Twenty-Year Delay) .	6.0 percent of GDP between 2039 and 2093

Note: Reforms taking place in 2018, 2028, and 2038 from the 2017 Financial Report were 2.0, 2.4, and 3.0 percent of GDP, respectively.

In contrast to a reform that begins immediately, if reform begins in 2029 or 2039, then the primary surpluses must be raised by 4.9 percent and 6.0 percent of GDP, respectively, in order for the debt-to-GDP ratio in 2093 to equal 78 percent. The difference between the primary surplus increase necessary if reform begins in 2029 or 2039 and the increase necessary if reform begins in 2019, an additional 0.8 and 1.9 percentage points, respectively, is a measure of the additional burden policy delay would impose on future generations. The costs of delay are due to the additional debt that accumulates between 2018 and the year reform is initiated, in comparison to the scenario in which reform begins immediately.

Alternative Scenarios

The long-run projections are highly uncertain. This section illustrates this inherent uncertainty by presenting alternative scenarios for the growth rate of health care costs, interest rates, discretionary spending, and receipts. (Not considered here are the effects of alternative assumptions for long-run trends in birth rates, mortality, and immigration.)

The population is aging rapidly and will continue to do so over the next several decades, which puts pressure on programs such as Social Security, Medicare, and Medicaid. A shift in projected fertility, mortality, or immigration rates could have important effects on the long-run projections. Higher-than-projected immigration, fertility, or mortality rates would improve the long-term fiscal outlook. Conversely, lower-than-projected immigration, fertility, or mortality rates would result in deterioration in the long-term fiscal outlook.

Effect of Changes in Health Care Cost Growth

One of the most important assumptions underlying the projections is the future growth of health care costs. These future growth rates – both for health care costs in the economy generally and for federal health care programs such as Medicare, Medicaid, and ACA exchange subsidies – are highly uncertain. In particular, enactment of the ACA in 2010 and the MACRA in 2015 established cost controls for Medicare hospital and physician payments whose long-term effectiveness is still to be demonstrated. The Medicare spending projections in the long-term fiscal projections are based on the projections in the 2018 Medicare Trustees' Report, which assume the ACA and MACRA cost control measures will be effective in producing a substantial slowdown in Medicare cost growth. As discussed in Note 22—Social Insurance, the Medicare projections are subject to much uncertainty about the ultimate effects of these provisions to reduce health care cost growth. For the long-term fiscal projections, that uncertainty also affects the projections for Medicaid and exchange subsidies, because the cost per beneficiary in these programs grows at the same reduced rate as Medicare cost growth per beneficiary.

As an illustration of the dramatic effect of variations in health care cost growth rates, Table 2 shows the effect on the size of reforms necessary to close the fiscal gap of per capita health care cost growth rates that are one percentage point higher or two percentage points higher than the growth rates in the base projection, as well as the effect of delaying closure of the fiscal gap.[4] As indicated earlier, if reform is initiated in 2019, eliminating the fiscal gap requires that the 2019-2093 primary surplus increase by an average of 4.1 percent of GDP in the base case. However, that figure increases to 7.3 percent of GDP if per capita health cost growth is assumed to be 1.0 percentage point higher, and 12.5 percent of GDP if per capita

[4] The base case health cost growth rates are derived from the projections in the 2018 Medicare trustees' report. These projections are summarized and discussed in Note 22 (see Table 1B in particular) and the "Medicare Projections" section of the unaudited RSI for the SOSI.

health cost growth is 2.0 percentage points higher. The cost of delaying reform is also increased if health care cost growth is higher, due to the fact that debt accumulates more rapidly during the period of inaction. For example, the lower part of Table 2 shows that delaying reform initiation from 2019 to 2029 requires that 2029-2093 primary surpluses be higher by an average of 0.8 percent of GDP in the base case, 1.4 percent of GDP if per capita health cost growth is 1.0 percentage point higher, and 2.4 percent of GDP if per capita health cost growth is 2.0 percentage points higher. The dramatic deterioration of the long-run fiscal outlook caused by higher health care cost growth shows the critical importance of managing health care cost growth.

Table 2
Impact of Alternative Health Cost Scenarios on Cost of Delaying Fiscal Reform

	Primary Surplus Increase (% of GDP) Starting in:		
Scenario	**2019**	**2029**	**2039**
Base Case	4.1	4.9	6.0
1.0 p.p. higher per person health cost growth	7.3	8.7	10.8
2.0 p.p. higher per person health cost growth	12.5	14.9	18.6

	Change in Primary Surplus Increase if Reform is Delayed From 2019 to:	
	2029	**2039**
Base Case	0.8	2.0
1.0 p.p. higher per person health cost growth	1.4	3.5
2.0 p.p. higher per person health cost growth	2.4	6.1

Note: Increments may not equal the subtracted difference of the components due to rounding. "p.p." means percentage point(s).

Effects of Changes in Interest Rates

A higher debt-to-GDP ratio is likely to increase the interest rate on government debt, making it more costly for the government to service its debt. Table 3 displays the effect of several alternative scenarios using different nominal (and real) interest rates than assumed in the base case on the size of reforms to close the fiscal gap as well as the effect of delaying closure of the fiscal gap. If reform is initiated in 2019, eliminating the fiscal gap requires that the 2019-2093 primary surplus increase by an average of 4.1 percent of GDP in the base case, 4.7 percent of GDP if the interest rate is 1.0 percentage point higher in every year, and 3.4 percent of GDP if the interest rate is 1.0 percentage point lower in every year. The cost of delaying reform is also increased if interest rates are higher, due to the fact that interest paid on debt accumulates more rapidly during the period of inaction. For example, the lower part of Table 3 shows that delaying reform initiation from 2019 to 2029 requires that 2029-2093 primary surpluses be higher by an average of 0.8 percent of GDP in the base case, 1.2 percent of GDP if the interest rate is 1.0 percentage point higher in every year, and 0.5 percent of GDP if the interest rate is 1.0 percentage point lower in every year.

Table 3
Impact of Alternative Interest Rate Scenarios on Cost of Delaying Fiscal Reform

Scenario	Primary Surplus Increase (% of GDP) Starting in: 2019	2029	2039
Base Case: Average of 5.0 percent over 75 years..........	4.1	4.9	6.0
1.0 p.p. higher interest rate in each year........................	4.7	5.9	7.9
1.0 p.p. lower interest rate in each year..........................	3.4	3.9	4.6

	Change in Primary Surplus Increase if Reform is Delayed From 2019 to: 2029	2039
Base Case: Average of 5.0 percent over 75 years................................	0.8	2.0
1.0 p.p. higher interest rate in each year..	1.2	3.1
1.0 p.p. lower interest rate in each year..	0.5	1.2

Note: Increments may not equal the subtracted difference of the components due to rounding.

Effects of Changes in Discretionary Spending Growth

The growth of discretionary spending has a large impact on long-term fiscal sustainability. The current base projection for discretionary spending assumes that spending stays within the statutory caps that apply through 2019 under the BBA, grows with GDP from the cap level after that point, and remains subject to the reductions required by the Joint Committee[5]. The implications of two alternative scenarios are shown in Table 4. The first alternative scenario allows discretionary spending to grow with inflation and population after 2019 so as to hold discretionary spending constant on a real per capita basis. (This growth rate assumption is slower than growth with GDP but is still higher than the standard 10-year budget baseline assumption, which assumes that discretionary spending grows with inflation but not with population.) The second alternative scenario sets discretionary spending from 2019 onward to statutory cap levels prior to Joint Committee reductions and grows with GDP from that point forward. As shown in Table 4, if discretionary spending grows with inflation and population, eliminating the fiscal gap requires that the 2019-2093 primary surplus increase by an average of 1.9 percent of GDP. If discretionary spending rises to the levels prior to Joint Committee sequestration and grows with GDP, the fiscal gap increases to 4.4 percent of GDP. The cost of delaying reform is greater when discretionary spending levels are higher. Initiating reforms in 2029 requires that the primary surplus increase by an average of 0.9 percent of GDP per year in the base case, and increase by 0.9 percent of GDP if discretionary levels return to pre-Joint Committee sequestration levels in 2020. If delayed until 2039, the primary surplus must increase by an average of 2.0 percent of GDP in the base case, and increase by 2.1 percent of GDP at pre-sequestration levels.

[5] The BCA of 2011 established statutory caps on discretionary spending for fiscal years 2012 through 2021 and established a Joint Committee tasked with identifying $1.2 trillion in deficit reduction. The failure of the Joint Committee to propose and Congress to enact legislation sufficient to reduce the deficit triggers automatic spending reductions through adjustments to the discretionary spending limits and sequestration of mandatory spending. Mandatory sequestration has been extended in various statutes and currently extends through 2027. After 2027, the projections assume the automatic reductions continue as a constant share of projected GDP.

Table 4
Impact of Alternative Discretionary Spending Growth Scenarios on Cost of Delaying Fiscal Reform

Scenario	Primary Surplus Increase (% of GDP) Starting in: 2019	2029	2039
Base Case: Discretionary spending growth with GDP after 2019	4.1	4.9	6.0
Growth with inflation and population after 2019	1.9	2.3	2.8
Growth with GDP after 2019, pre-Joint Committee sequester levels	4.4	5.2	6.5

Scenario	Change in Primary Surplus Increase if Reform is Delayed From 2019 to: 2029	2039
Base Case: Discretionary spending growth with GDP after 2019	0.8	2.0
Growth with inflation and population after 2019	0.4	0.9
Growth with GDP after 2019, pre-Joint Committee sequester levels	0.8	2.1

Note: Increments may not equal the subtracted difference of the components due to rounding.

Effects of Changes in Individual Income Receipt Growth

The growth rate of receipts, specifically individual income taxes, is another key determinant of long-term sustainability. The base projections assume growth in individual income taxes over time to account primarily for the slow shift of individuals into higher tax brackets due to real wage growth ("real bracket creep"). This assumption approximates the long-term historical growth in individual income taxes relative to wages and salaries and is consistent with current policy without change, as future legislation would be required to prevent real bracket creep. As an illustration of the effect of variations in individual income tax growth, Table 5 shows the effect on the size of reforms necessary to close the fiscal gap and the effect of delaying closure of the fiscal gap if long-term receipt growth as a share of wages and salaries is 0.1 percentage point higher than the base case, as well as 0.1 percentage point lower than the base case. If reform is initiated in 2019, eliminating the fiscal gap requires that the 2019-2093 primary surplus increase by an average of 4.1 percent of GDP in the base case, only 3.0 percent of GDP if receipt growth is 0.1 percentage point higher, but 5.2 percent of GDP if receipt growth is 0.1 percentage point lower. The cost of delaying reform is also affected if receipt growth assumptions change, much as was the case in the previous alternative scenarios.

Table 5
Impact of Alternative Revenue Growth Scenarios on Cost of Delaying Fiscal Reform

Scenario	Primary Surplus Increase (% of GDP) Starting in: 2019	2029	2039
Base Case: Individual income tax bracket creep of 0.1% of wages and salaries per year	4.1	4.9	6.0
0.2% of wages and salaries per year after 2028	3.0	3.6	4.4
0.0% of wages and salaries per year after 2028 (no bracket creep)	5.2	6.1	7.7

Scenario	Change in Primary Surplus Increase if Reform is Delayed From 2019 to: 2029	2039
Base Case: Individual income tax bracket creep of 0.1% of wages and salaries per year	0.8	2.0
0.2% of wages and salaries per year after 2028	0.6	1.4
0.0% of wages and salaries per year after 2028 (no bracket creep)	1.0	2.5

Note: Increments may not equal the subtracted difference of the components due to rounding.

Fiscal Projections in Context

In this report, a sustainable fiscal policy has been defined as one where the federal debt-to-GDP ratio is stable or declining. However, this definition does not indicate what a sustainable debt-to-GDP ratio might be. Any particular debt ratio is not the ultimate goal of fiscal policy. Rather, the goals of fiscal policy are many. They include financing public goods, such as infrastructure and government services; promoting a strong and growing economy; and managing the debt so that it is not a burden on future generations. These goals are interrelated, and readers should consider how policies intended to affect one might depend on or affect another.

This report shows that current policy is not sustainable. In evaluating policies that could make policy sustainable, note that debt may play roles in both facilitating and hindering a healthy economy. For example, government deficit spending supports demand and allows economies to emerge from recessions more quickly. Debt may also be a cost-effective means of financing capital investment that promotes future economic growth, which may in turn make future debt levels more manageable. However, economic theory also suggests that high levels of debt may contribute to higher interest rates, leading to lower private investment and a smaller capital stock which the economy can use to grow. Unfortunately, it is unclear what debt-to-GDP ratio would be sufficiently high to produce these negative outcomes, or whether the key concern is the level of debt per se, or a trend that shows debt increasing over time.

While several empirical studies have attempted to discern a definite relationship between debt and economic growth from the past experience of countries, the evidence is mixed. One study suggested that as advanced countries' debt-to-GDP ratios exceeded 90 percent it had significant negative consequences for real GDP growth through rising interest rates, crowding out of private investment, and reduced capital formation.[6] Real GDP growth is generally lower by about 1 percent when the countries' debt-to-GDP ratios are above 90 percent relative to the times when they are below 90 percent.[7] However,

[6] Reinhart, Carmen M., and Kenneth S. Rogoff. 2010. "Growth in a Time of Debt." *American Economic Review*, 100(2): 573-78.
[7] Errata: "Growth in a Time of Debt," Carmen M. Reinhart and Kenneth S. Rogoff. Harvard University, 2013.

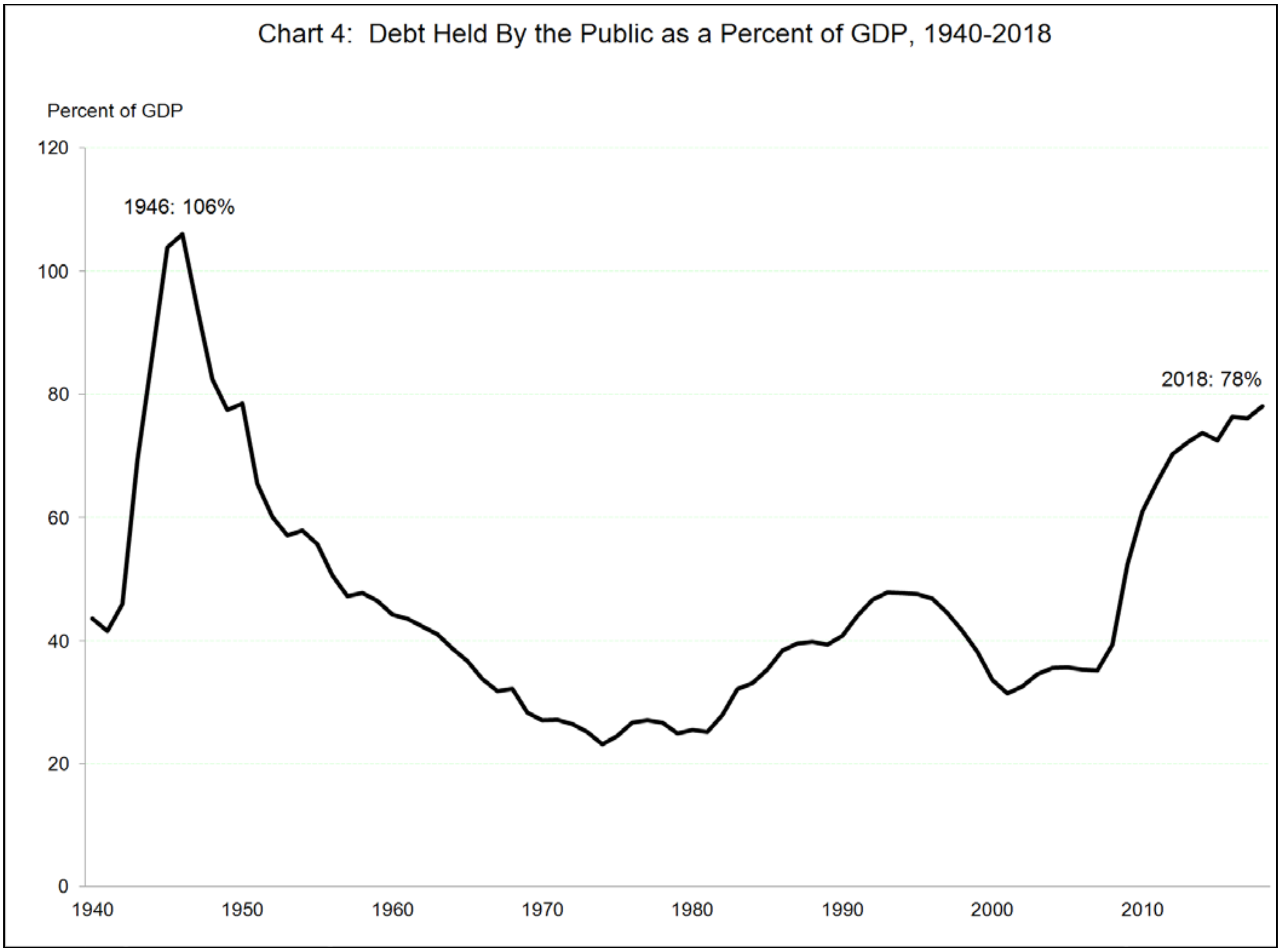
after removing sample countries with very high indebtedness – those with debt-to-GDP ratios of more than 120 percent – and very low indebtedness – those with debt-to-GDP ratios of less than 30 percent – the negative relationship between growth and debt is difficult to determine. Another study reports that differences in average GDP growth in countries with debt-to-GDP ratios between 30-60 percent, 60-90 percent, and 90-120 percent cannot be statistically distinguished.[8] Some countries with high debt-to-GDP ratios have been observed to experience lower-than-average growth, while other countries with similarly high debt ratios have continued to enjoy robust growth. Analogously, low debt-to-GDP ratios are no guarantee of strong economic growth. Moreover, the direction of causality is unclear. High debt may undermine growth through increased interest rates and lower business confidence, or low growth may contribute to high debt by depressed tax revenues and increased deficit spending on social safety net programs.

Nevertheless, to put the current and projected debt-to-GDP ratios in context, it is instructive to examine how the United States experience compares with that of other countries. The U.S. government's debt as a percent of GDP is relatively large compared with central government debt of other countries, but far from the largest among developed countries. Based on historical data as reported by the International Monetary Fund (IMF) for 28 advanced economies, the debt-to-GDP ratio in 2016 ranged from 6.3 percent of GDP to 192.2 percent of GDP.[9] The United States is not included in this set of statistics, which underscores the difficulty in calculating debt ratios under consistent definitions, but the projections in this report show the 2018 debt-to-GDP ratio as 78 percent. Despite using consistent definitions where available, these debt measures are not strictly comparable due to differences in the share of government debt that is debt of the central government, how government responsibilities are shared between central and local governments, how current policies compare with the past policies that determine the current level of debt, and how robustly each economy grows.

The historical experience of the U.S. may also provide some perspective. As Chart 4 shows, the debt-to-GDP ratio was highest in the 1940s, following the debt buildup during World War II. In the projections in this report, the U.S. would reach the previous peak debt ratio in 2030. However, the origins of current and future federal debt are quite different from the wartime debt of the 1940s, which limits the pertinence of past experience.

[8] Herndon, Thomas, Michael Ash, and Robert Pollard, "Does High Public Debt Consistently Stifle Economic Growth? A Critique of Reinhart and Rogoff," *Cambridge Journal of Economics*, 2013.

[9] Government Finance Statistics Yearbook, Main Aggregates and Balances, available at https://data.imf.org. Data is for D1 debt liabilities for the central government, excluding social security funds, for Advanced Economies.



As the cross-country and historical comparisons suggest, there is a very imperfect relationship between the current level of central government debt and the sustainability of overall government policy. Past accrual of debt is certainly important, but current policies and their implications for future debt accumulation are as well.

Conclusion

The past 11 years saw debt held by the public nearly double as a share of GDP, bringing it to a level not seen since shortly after World War II. The projections in this *Financial Report* indicate that if policy remains unchanged, the debt-to-GDP ratio will steadily increase and soon far exceed historical levels, which implies current policy is not sustainable and must ultimately change. Subject to the important caveat that policy changes are not so abrupt that they slow economic growth, the sooner policies are put in place to avert these trends, the smaller are the adjustments necessary to return the nation to a sustainable fiscal path, and the lower the burden of the debt will be to future generations.

Social Insurance

The social insurance programs consisting of Social Security, Medicare, Railroad Retirement, Black Lung, and Unemployment Insurance (UI) were developed to provide income security and health care coverage to citizens under specific circumstances as a responsibility of the government. Because taxpayers rely on these programs in their long-term planning, social insurance program information should indicate whether the current statutory provisions of the programs can be sustained, and more generally what effect these provisions likely have on the government's financial condition. The resources needed to run these programs are raised through taxes and fees. Eligibility for benefits depends in part on earnings and time worked by the individuals. Social Security benefits are generally redistributed intentionally toward lower-wage workers (i.e., benefits are progressive). In addition, each social insurance program has a uniform set of eligibility events and schedules that apply to all participants.

Social Security and Medicare

Social Security

The OASI Trust Fund was established on January 1, 1940, as a separate account in the Treasury. The DI Trust Fund, another separate account in the Treasury, was established on August 1, 1956. The OASI fund pays cash retirement benefits to eligible retirees and their eligible dependents and survivors, and the much smaller DI fund pays cash benefits to eligible individuals who are unable to work because of medical conditions and certain family members of such eligible individuals. Though the events that trigger benefit payments are quite different, both trust funds have the same dedicated financing structure: primarily payroll taxes and income taxes on benefits. All financial operations of the OASI and DI Programs are handled through these respective funds. The two funds are often referred to as the combined OASDI Trust Funds. At the end of calendar year 2017, OASDI benefits were paid to approximately 62 million beneficiaries.

The primary financing source for these two funds are taxes paid by workers, their employers, and individuals with self-employment income, based on work covered by the OASDI Program. Currently, employers and employees each pay 6.2 percent of taxable earnings, and the self-employed pay 12.4 percent of taxable earnings. Payroll taxes are levied on wages and net earnings from self-employment up to a specified maximum annual amount, referred to as maximum taxable earnings ($128,400 in 2018), that increases each year with economy-wide average wages.

Legislation passed in 1984 subjected up to half of OASDI benefits to income tax and allocated the revenue to the OASDI Trust Funds. In 1993 legislation increased the potentially taxed portion of benefits to 85 percent and allocated the additional revenue to the Medicare's HI Trust Fund.

Medicare

The Medicare Program, created in 1965, has two separate trust funds: the HI Trust Fund (otherwise known as Medicare Part A) and the SMI Trust Funds (which consists of the Medicare Part B and Part D[10] accounts). HI helps pay for inpatient hospital stays, home health care following a hospital stay, and skilled nursing facility and hospice care. SMI helps pay for hospital outpatient services, physician services, and assorted other services and products through Part B and for prescription drugs through Part D.

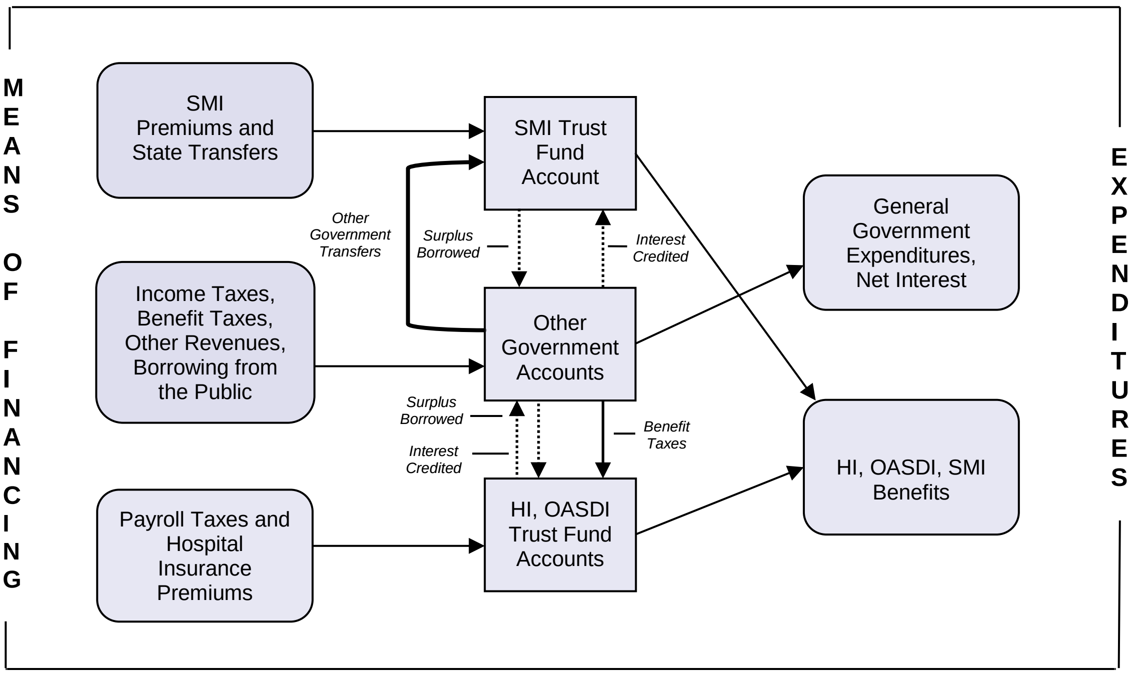
Though the events that trigger benefit payments are similar, HI and SMI have different dedicated financing structures. Similar to OASDI, HI is financed primarily by payroll contributions. Currently, employers and employees each pay 1.45 percent of earnings, while self-employed workers pay 2.9 percent of their net earnings. Beginning in 2013, employees and self-employed individuals with earnings above certain thresholds pay an additional HI tax of 0.9 percent on earnings above those thresholds. Other income to the HI Trust Fund includes a small amount of premium income from voluntary enrollees, a portion of the federal income taxes that beneficiaries pay on Social Security benefits (as explained above), and interest credited on Treasury securities held in the HI Trust Fund. As is explained in the next section, these Treasury securities and related interest have no effect on the consolidated statement of governmentwide finances.

For SMI, direct transfers from the General Fund financed 72 percent and 70 percent of 2018 program costs for Parts B and D, respectively. Premiums paid by beneficiaries and, for Part D state transfers, generally financed the remainder of

[10] Medicare legislation in 2003 created the new Part D account in the SMI Trust Fund to track the finances of a new prescription drug benefit that began in 2006. As is the case for Medicare Part B, a little more than three-quarters of revenues to the Part D account will come from future transfers from the General Fund. Consequently, the nature of the relationship between the SMI Trust Fund and the Federal Budget described below is largely unaffected by the presence of the Part D account though the magnitude will be greater.

expenditures. For beneficiaries dually eligible for Medicare and Medicaid, states must pay the Part D account a portion of their estimated foregone drug costs for this population (referred to as state transfers). As with HI, interest received on Treasury securities held in the SMI Trust Fund is credited to the fund. These Treasury securities and related interest have no effect on the consolidated statement of governmentwide finances. See Note 22—Social Insurance, for additional information on Medicare program financing.

Figure 1
Social Security, Medicare, and Governmentwide Finances



Social Security, Medicare, and Governmentwide Finances

The current and future financial status of the separate OASDI, HI, and SMI Trust Funds is the focus of the Social Security and Medicare Trustees' Reports, a focus that may appropriately be referred to as the "trust fund perspective." In contrast, the government primarily uses the budget concept as the framework for budgetary analysis and presentation. It represents a comprehensive display of all federal activities, regardless of fund type or on- and off-budget status, and has a broader focus than the trust fund perspective that may appropriately be referred to as the "budget perspective" or the "governmentwide perspective." Social Security and Medicare are among the largest expenditure categories of the U.S. federal budget. This section describes in detail the important relationship between the trust fund perspective and the governmentwide perspective.

Figure 1 is a simplified depiction of the interaction of the Social Security and Medicare Trust Funds with the rest of the federal budget.[11] The boxes on the left show sources of funding, those in the middle represent the trust funds and other government accounts, which include the General Fund into which that funding flows, and the boxes on the right show simplified expenditure categories. The figure is intended to illustrate how the various sources of program revenue flow through the budget to beneficiaries. The general approach is to group revenues and expenditures that are linked specifically to Social Security and/or Medicare separately from those for other government programs.

[11] The federal budget encompasses all government financing and is synonymous with a governmentwide perspective.

Each of the trust funds has its own sources and types of revenue. With the exception of General Fund transfers to SMI, each of these revenue sources represents revenue from the public that is dedicated specifically for the respective trust fund and cannot be used for other purposes. In contrast, personal and corporate income taxes as well as other revenue go into the General Fund and are drawn down for any government program for which Congress has approved spending.[12] The arrows from the boxes on the left represent the flow of the revenues into the trust funds and other government accounts.

The heavy line between the top two boxes in the middle of Figure 1 represents intragovernmental transfers to the SMI Trust Fund from other government accounts. The Medicare SMI Trust Fund is shown separately from the two Social Security Trust Funds (OASI and DI) and the Medicare HI Trust Fund to highlight the unique financing of SMI. Currently, SMI is the only one of the programs that is funded through transfers from the General Fund, which is part of the other government accounts (the SMI Part D account also receives transfers from the states). The direct transfers finance roughly three-fourths of SMI Program expenses. The transfers are automatic; their size depends on how much the program requires, not on how much revenue comes into the Treasury. If General Fund revenues become insufficient to cover both the mandated transfer to SMI and expenditures on other general government programs, Treasury has to borrow to make up the difference. In the longer run, if transfers to SMI increase beyond growth in general revenues—and as shown in the Medicare Trustees Report and Chart 5 later in this section, they are projected to increase significantly in coming years—then Congress must either raise taxes, cut other government spending, reduce SMI benefits, or borrow even more.

The dotted lines between the middle boxes of Figure 1 also represent intragovernmental transfers but those transfers arise in the form of "borrowing/lending" between the government accounts. Interest credited to the trust funds arises when the excess of program income over expenses is loaned to the General Fund. The vertical lines labeled *Surplus Borrowed* represent these flows from the trust funds to the other government accounts. These loans reduce the amount the General Fund has to borrow from the public to finance a deficit (or likewise increase the amount of debt paid off if there is a surplus). However, the General Fund has to credit interest on the loans from the trust fund programs, just as if it borrowed the money from the public. The credits lead to future obligations for the General Fund (which is part of the other government accounts). These transactions are indicated in Figure 1 by the vertical arrows labeled *Interest Credited*. The credits increase trust fund income exactly as much as they increase credits (future obligations) in the General Fund. From the governmentwide standpoint, at least in an accounting sense, these interest credits are a wash.

When the trust funds get the receipts that they loan to the General Fund, these receipts provide additional authority to spend on benefits and other program expenses. The General Fund, in turn, has taken on the obligation of paying interest on these loans every year and repaying the principal when trust fund income from other sources falls below expenditures.

How loans from the trust funds to the General Fund and later repayments of those loans affect tax income and expenditures of the General Fund is uncertain. Two extreme cases encompass the possibilities. At one extreme, each dollar the trust funds loan to the General Fund might reduce borrowing from the public by a dollar at the time the loan is extended, in which case the General Fund could repay all trust fund loans by borrowing from the public without raising the level of public debt above the level that would have occurred in the absence of the loans. At the other extreme, each dollar the trust funds loan to the General Fund might result in some combination of higher General Fund spending and lower General Fund revenues amounting to one dollar at the time the loans are extended, in which case General Fund loan repayments to the trust funds might initially be financed with borrowing from the public but must at some point be financed with a combination of higher General Fund taxes and lower General Fund spending than would have occurred in the absence of the loans. In this latter extreme, trust fund loans result in additional largess (i.e., higher spending and/or lower taxes) in General Fund programs at the time the loans are extended, but ultimately that additional largess is financed with additional austerity (i.e., lower spending and/or higher taxes) in General Fund programs at later dates. The actual impact of trust fund loans to the General Fund and their repayment on General Fund programs is at one of these two extremes or somewhere in between.

Actual dollar amounts roughly corresponding to the flows presented in Figure 1 are shown in Table 1 for fiscal year 2018. In Table 1, revenues from the public (left side of Figure 1) and expenditures to the public (right side of Figure 1) are shown separately from transfers between government accounts (middle of Figure 1). Note that the transfers ($318.3 billion) and interest credits ($93.5 billion) received by the trust funds appear as negative entries under "All Other" and are thus offsetting when summed for the total budget column. These two intragovernmental transfers are the key to the differences between the trust fund and budget perspectives.

From the governmentwide perspective, only revenues received from the public (and states in the case of Medicare, Part D) and expenditures made to the public are important for the final balance. Trust fund revenue from the public consists of

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[12] Other programs also have dedicated revenues in the form of taxes and fees (and other forms of receipt) and there are a large number of dedicated trust funds in the federal budget. Total trust fund receipts account for about 40 percent of total government receipts with the Social Security and Medicare Trust Funds accounting for about two-thirds of trust fund receipts. For further discussion, see the report issued by the Government Accountability Office, *Federal Trust and Other Earmarked Funds*, GAO-01-199SP, January 2001. In the figure and the discussion that follows, all other programs, including these other dedicated trust fund programs, are grouped under "Other government Accounts" to simplify the description and maintain the focus on Social Security and Medicare.

payroll taxes, benefit taxes, and premiums. For HI, the difference between total expenditures made to the public ($297.2 billion) and revenues ($293.9 billion) was $3.3 billion in 2018, indicating that HI had a relatively small negative effect on the overall budget outcome *in that year*. For the SMI account, revenues from the public (primarily premiums) fell short of total expenditures made to the public by $291.6 billion in 2018, which resulted in a net draw on the overall budget balance in that year. For OASDI, the difference between total expenditures made to the public ($988.0 billion) and revenues from the public ($908.9 billion) was $79.1 billion in 2018, indicating that OASDI had a negative effect on the overall budget outcome in that year. Combined OASDI payroll and benefit tax revenues were increased by $3.5 billion in fiscal year 2018.

The trust fund perspective is captured in the bottom section of each of the three trust fund columns. For HI, total revenues exceeded total expenditures by $5.7 billion in 2018, as shown at the bottom of the first column. For SMI, total revenues exceeded total expenditures by $27.5 billion. The total revenue for SMI is $441.6 billion ($122.5 + $319.1), which includes $319.1 billion transferred from other government accounts (General Fund). Transfers to the SMI Program from other government accounts (the General Fund), amounting to about 76.5 percent of program costs, are obligated under current law and, therefore, appropriately viewed as revenue from the trust fund perspective. For OASDI, total revenues of $992.7 billion ($908.9 + $83.8) exceeded total expenditures of $988.0 billion by $4.7 billion. Total revenues for OASDI included $83.8 billion in transfers from the General Fund, made up of interest credits of $83.8 billion.

Table 1
Revenues and Expenditures for Medicare and Social Security Trust Funds and the Total Federal Budget for the Fiscal Year ended September 30, 2018

(In billions of dollars)	Trust Funds HI	SMI	OASDI	Total	All Other	Total[1]
Payroll taxes and other public revenues:						
Payroll and benefit taxes	288.8	-	908.9	1,197.7	-	1,197.7
Premiums	5.1	106.7	-	111.8	-	111.8
Other taxes and fees	-	15.8	-	15.8	2,003.4	2,019.2
Total	293.9	122.5	908.9	1,325.3	2,003.4	3,328.7
Total expenditures to the public[2]	297.2	414.1	988.0	1,699.3	2,408.4	4,107.7
Net results for budget perspective[3]	(3.3)	(291.6)	(79.1)	(374.0)	(405.0)	(779.0)
Revenues from other Government accounts:						
Transfers	1.6	316.7	-	318.3	(318.3)	
Interest credits	7.3	2.4	83.8	93.5	(93.5)	
Total	9.0	319.1	83.8	411.8	(411.8)	
Net results for trust fund perspective[3]	5.7	27.5	4.7	37.8	N/A	N/A

[1] This column is the sum of the preceding two columns and shows data for the total federal budget. The figure $779 was the total federal deficit in fiscal year 2018.

[2] The OASDI figure includes $4.9 billion transferred to the Railroad Retirement Board for benefit payments and is therefore an expenditure to the public.

[3] Net results are computed as revenues less expenditures.

Notes: Totals may not equal the sum of components due to rounding.
"N/A" indicates not applicable.

Cash Flow Projections

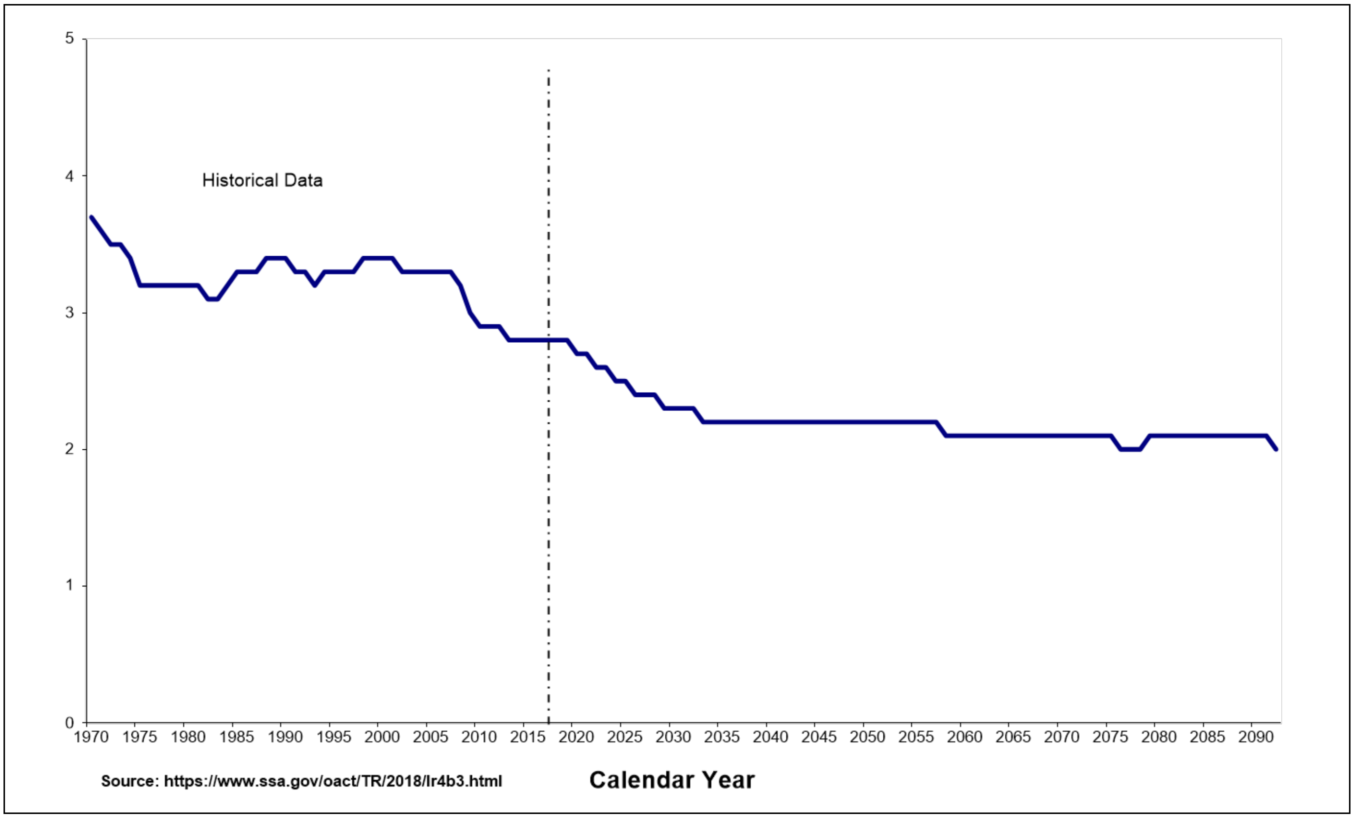
Background

Economic and Demographic Assumptions. The Boards of Trustees[13] of the OASDI and Medicare Trust Funds provide in their annual reports to Congress short-range (10-year) and long-range (75-year) actuarial estimates of each trust fund. Because of the inherent uncertainty in estimates for 75 years into the future, the boards use three alternative sets of economic and demographic assumptions to show a range of possibilities. The economic and demographic assumptions used for the most recent set of intermediate projections for Social Security and Medicare are shown in the "Social Security" and "Medicare" sections of Note 22—Social Insurance.

[13] There are six trustees: the Secretaries of the Treasury (managing trustee), Health and Human Services, and Labor; the Commissioner of the Social Security Administration; and two public trustees who are appointed by the President and confirmed by the Senate for a 4-year term. By law, the public trustees cannot both be members of the same political party.

Worker-to-Beneficiary Ratio. The expenditure projections for both the OASDI and Medicare Programs reflect the aging of the large baby-boom generation, born in the years 1946 to 1964, and its ultimate passing. Under the intermediate assumptions, cost rates are projected to rise rapidly between 2018 and 2035, primarily because the number of beneficiaries rises much more rapidly than the number of covered workers as the baby-boom generation retires. For the most part, current workers pay for current benefits. Due to the lower fertility rates of the baby-boom generation as compared to those of their parents' generation, and the expected low fertility rates of all future generations, there is a relatively smaller number of persons born after the baby boom who will then finance the retirement of the baby-boom generation. Chart 1 shows that in 2017, every OASDI beneficiary had 2.8 workers to pay for his or her benefit. In 2030, however, after the last baby boomer turns 65, there will be only about 2.3 workers per beneficiary. The projected ratio continues to decline until there are just 2.0 workers per beneficiary by 2092. A similar demographic pattern confronts the Medicare Program. The number of workers per HI beneficiary declines from 3.1 in 2017 to 2.4 in 2030, and continues to decline throughout the projection period to 2092, when there are just 2.1 workers per HI beneficiary.

Chart 1—Number of Covered Workers per OASDI Beneficiary
1970-2092

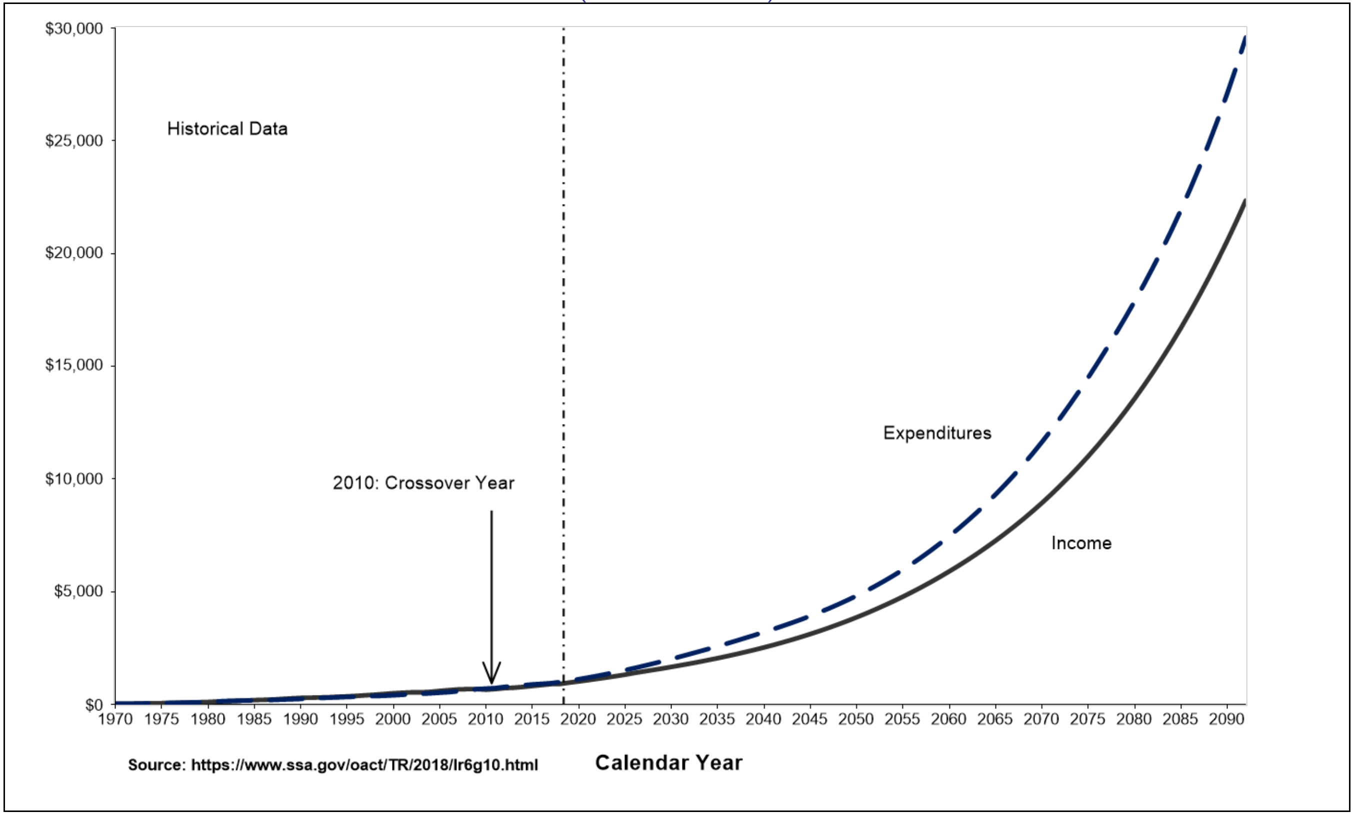


Social Security Projections

Income and Expenditures. Chart 2 shows historical values and actuarial estimates of combined OASDI annual noninterest income and expenditures for 1970-2092. The estimates are for the open-group population of all workers and beneficiaries projected to be alive in each year. The expenditure projections in Chart 2 and all subsequent charts assume all scheduled benefits are paid regardless of whether the income and assets are available to finance them.

Chart 2—OASDI Income (Excluding Interest) and Expenditures 1970-2092

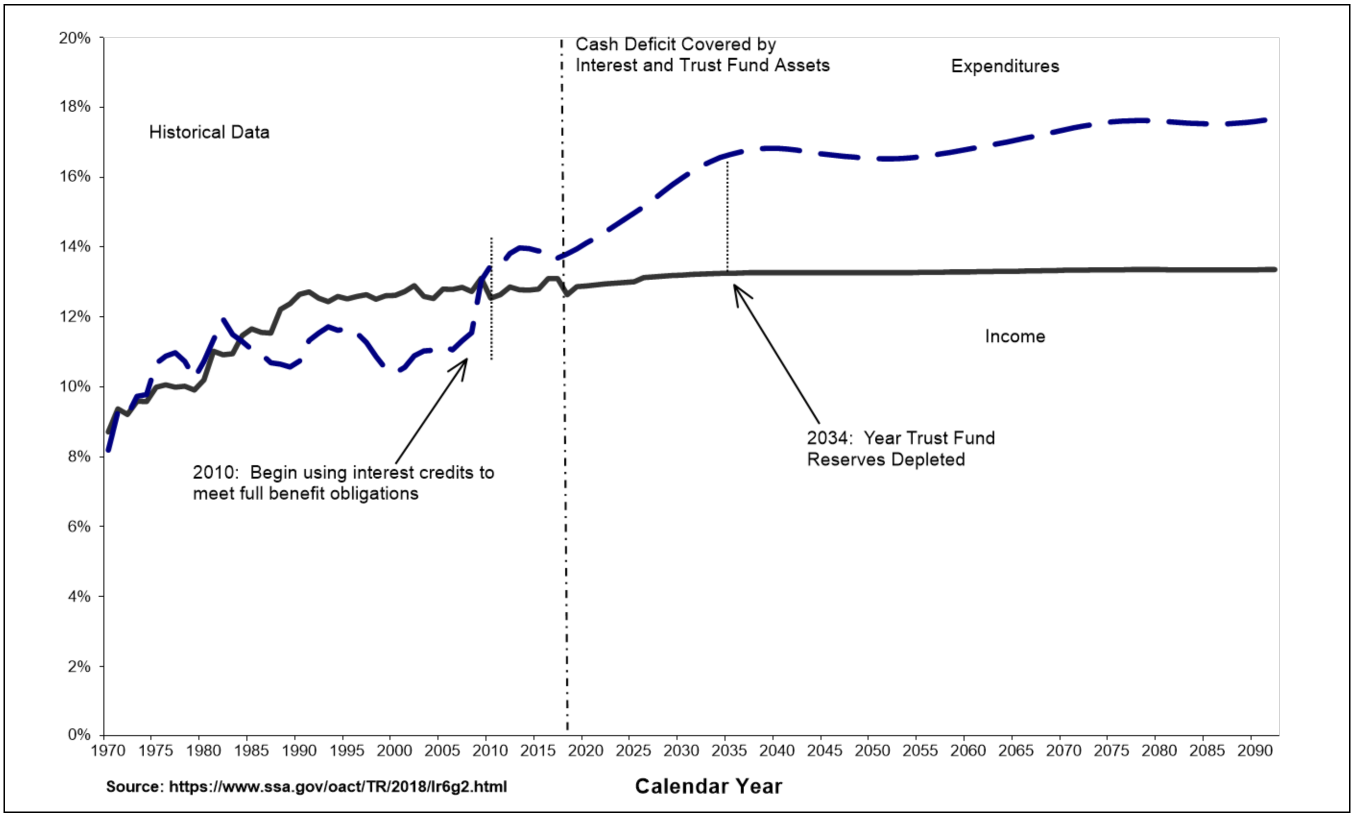
(In billions of dollars)



Annual OASDI cost exceeded noninterest income in 2010 for the first time since 1983. It is projected that cost will continue to exceed noninterest income throughout the 75-year valuation period. Projected OASDI cost increases more rapidly than projected noninterest income through 2039 primarily because the retirement of the baby-boom generation will increase the number of beneficiaries much faster than the number of covered workers increases, as subsequent lower-birth-rate generations replace the baby-boom generation at working ages. From 2040 to 2052, the cost rate (the ratio of program cost to taxable payroll) generally declines because the aging baby-boom generation is gradually replaced at retirement ages by subsequent low-birth-rate generations. Thereafter, increases in life expectancy cause OASDI cost to increase generally relative to noninterest income, but more slowly than between 2010 and 2039. Beginning in 2018, cost exceeds total income, and combined OASI and DI Trust Fund reserves diminish until they become depleted in 2034. After trust fund reserve depletion, continuing income is sufficient to support expenditures at a level of 79 percent of program cost for the rest of 2034, declining to 74 percent for 2092. To meet all OASDI cost on a timely basis, the combined OASI and DI Trust Funds will need to redeem Treasury securities. OASDI cost is projected to exceed total income (including interest) in 2018 for the first time since 1982, and remain higher throughout the 75-year valuation period. Therefore, the combined OASI and DI Trust Funds will be net borrowers from the General Fund going forward, rather than net lenders. The government could finance increased redemptions by increasing its borrowing from the public, raising taxes (other than OASDI payroll taxes), and/or reducing expenditures (other than OASDI cost).

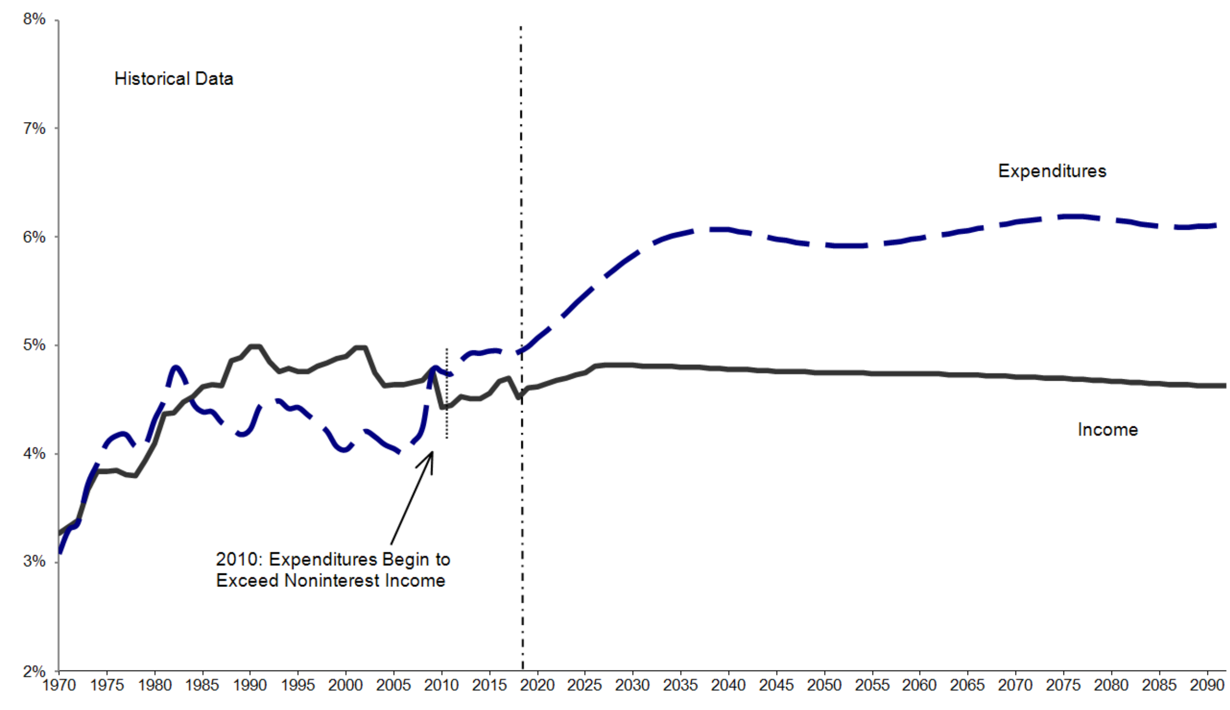
Income and Expenditures as a Percent of Taxable Payroll. Chart 3 shows annual noninterest income and expenditures expressed as percentages of taxable payroll, commonly referred to as the income rate and cost rate, respectively. Under the intermediate assumptions, demographic factors would by themselves cause the projected cost rate to rise rapidly for the next two decades before leveling off in about 2035. However, the recent recession temporarily depressed taxable earnings and increased the number of beneficiaries, which in turn sharply, but temporarily, increased the cost rate starting in 2009. From a peak in 2013, the cost rate generally declines through 2017 under the economic recovery and thereafter returns to a gradually rising trend. The projected income rate is stable at about 13 percent throughout the 75-year period.

Chart 3—OASDI Income (Excluding Interest) and Expenditures as a Percent of Taxable Payroll 1970-2092



Income and Expenditures as a Percent of GDP. Chart 4 shows estimated annual noninterest income and expenditures, expressed as a percent of GDP, which is the total value of goods and services produced in the U.S. This alternative perspective shows the size of the OASDI Program in relation to the capacity of the national economy to sustain it. In calendar year 2017, OASDI cost was about $952 billion, which was about 4.9 percent of GDP. The cost of the program (based on current law) rises rapidly to 6.1 by 2038, then declines to 5.9 percent by 2052, and then generally increases to 6.1 percent by 2092. The rapid increase from 2018 to 2035 is projected to occur as baby boomers become eligible for OASDI benefits, lower birth rates result in fewer workers per beneficiary, and beneficiaries continue to live longer. In 2092, expenditures are projected to exceed income by approximately 1.50 percent of GDP. Social Security's noninterest income is projected to drop to 4.5 percent in 2018, then increase to about 4.8 percent of GDP by 2028. Thereafter, noninterest income as a percent of GDP declines gradually, to about 4.6 percent by 2092, because the Trustees expect the share of employee compensation provided as non-covered fringe benefits to increase gradually.

Chart 4—OASDI Income (Excluding Interest) and Expenditures as a Percent of GDP 1970-2092



Source: https://www.ssa.gov/oact/TR/2018/lr6g4.html

Sensitivity Analysis. Projections of the future financial status of the OASDI program depend on many demographic and economic assumptions, including fertility, mortality, net immigration, average wages, inflation, and interest rates on Treasury securities. The income will depend on how these factors affect the size and composition of the working population and the level and distribution of wages and earnings. Similarly, the cost will depend on how these factors affect the size and composition of the beneficiary population and the general level of benefits.

Because perfect long-range projections of these factors are impossible and actual experience is likely to differ from the estimated or assumed values of these factors, this section is included to illustrate the sensitivity of the long-range projections to changes in assumptions by analyzing six key assumptions: total fertility rate, average annual reduction in death rates, net immigration, real-wage differential, CPI change, and real interest rate. For this analysis, the intermediate assumptions are used as the reference point, and each selected assumption is varied individually. The variation used for each individual assumption reflects the levels used for that assumption in the low-cost (Alternative I) and high-cost (Alternative III) projections. For example, when analyzing sensitivity with respect to variation in real wages, income, and expenditure projections using the intermediate assumptions are compared to the outcome when projections are done by changing only the real wage assumption to either low-cost or high-cost alternatives.

The low-cost alternative is characterized by assumptions that improve the financial status of the program (relative to the intermediate assumption) such as slower improvement in mortality (beneficiaries die younger). In contrast, assumptions under the high-cost alternative worsen the financial outlook. All present values are calculated as of January 1, 2018 and are based on estimates of income and cost during the 75-year projection period 2018-2092.

Table 2 shows the effects of changing individual assumptions on the present value of estimated OASDI expenditures in excess of income (the *shortfall* of income relative to expenditures in present value terms). The assumptions are shown in parentheses. For example, if the annual reduction in death rates were changed from 0.77 percent, the intermediate assumption, to 0.41 percent, meaning that people die younger, the shortfall for the period of estimated OASDI income relative to cost would decrease to $13,574 billion from $16,057 billion; if the annual reduction were changed to 1.15 percent, meaning that people live longer, the shortfall would increase to $18,761 billion.

A higher fertility rate means more workers relative to beneficiaries over the projection period, thereby lowering the shortfall relative to the intermediate assumption. Table 2 demonstrates that if the ultimate total fertility rate were changed from 2.0 children per woman, the intermediate assumption, to 1.8 children per woman, the shortfall for the period of estimated OASDI income relative to cost would increase to $17,591 billion from $16,057 billion; if the ultimate rate were changed to 2.2 children per woman, the shortfall would decrease to $14,509 billion.

The annual real-wage differential is the difference between the percentage increases in: (1) the average annual wage in OASDI covered employment; and (2) the average annual CPI. Higher real wage growth results in faster income growth relative to expenditure growth. As shown in Table 2, if the ultimate real-wage differential were changed from 1.20 percentage points, the intermediate assumption, to 0.58 percentage points, the shortfall for the period of estimated OASDI income relative to cost would increase to $18,489 billion from $16,057 billion; if the ultimate real-wage differential were changed from 1.20 to 1.82 percentage points, the shortfall would decrease to $12,378 billion.

Table 2 demonstrates that if the ultimate annual increase in the CPI were changed from 2.6 percent, the intermediate assumption, to 2.0 percent, the shortfall for the period of estimated OASDI income relative to cost would increase to $16,535 billion from $16,057 billion; if the ultimate annual increase in the CPI were changed to 3.2 percent, the shortfall would decrease to $15,551 billion. The seemingly counter-intuitive result that higher CPI increases result in decreased shortfalls (and vice versa) is explained by the time lag between the effects of the CPI changes on taxable payroll and on benefit payments. The effect on taxable payroll due to a greater increase in average wages is experienced immediately, while the effect on benefits is experienced with a lag of about one year. For this reason, larger increases in the CPI cause earnings and income to increase sooner and, therefore, by more each year, than benefits and cost.

Immigration generally occurs at relatively young adult ages, so there is no significant effect on beneficiaries (and, therefore, on benefits) in the early years of the projection period, but the effect on the numbers of workers (and, therefore, on payroll tax income) is immediate. Therefore, even in the early years, the present values, year by year, are generally higher (less negative in later years) for higher net annual immigration. However, the increased payroll taxes for a given year are eventually offset by benefits paid in that year to earlier immigrant cohorts. Therefore, the present values based on the three assumptions about net annual immigration become more similar at the end of the projection period. Table 2 shows that if the intermediate immigration assumptions were changed so that the average level for the 75-year period decreased from 1,272,000 persons to 952,000 persons, the present value of the shortfall for the period of estimated OASDI income relative to cost would increase to $16,914 billion from $16,057 billion. If, instead, the immigration assumptions were changed so that net annual immigration would be expected to average 1,607,000 persons, the present value of the shortfall would decrease to $15,274 billion.

Finally, Table 2 shows the sensitivity of the shortfall to variations in the real interest rate or, in present value terminology, the sensitivity to alternative discount rates assuming a higher discount rate results in a lower present value. If the ultimate real interest rate were changed from 2.7 percent, the intermediate assumption, to 2.2 percent, the shortfall for the period of estimated OASDI income relative to cost, when measured in present-value terms would increase to $18,999 billion from $16,057 billion; if the ultimate annual real interest rate were changed to 3.2 percent, the present-value shortfall would decrease to $13,713 billion.

Table 2
Present Values of Estimated OASDI Expenditures in Excess of Income Under Various Assumptions, 2018-2092

(Dollar values in billions; values of assumptions shown in parentheses)

	Financing Shortfall Range		
Assumption	**Low**	**Intermediate**	**High**
Average annual reduction in death rates	13,574 (0.41)	16,057 (0.77)	18,761 (1.15)
Total fertility rate	14,509 (2.2)	16,057 (2.0)	17,591 (1.8)
Real-wage differential	12,378 (1.82)	16,057 (1.20)	18,489 (0.58)
CPI change	15,551 (3.2)	16,057 (2.6)	16,535 (2.0)
Net immigration[1]	15,274 (1,607,000)	16,057 (1,272,000)	16,914 (952,000)
Real interest rate	13,713 (3.2)	16,057 (2.7)	18,999 (2.2)

[1] Amounts represent the average annual net immigration over the 75-year projection period.

Source: 2018 OASDI Trustees Report and SSA.

Medicare Projections

Medicare Legislation. The projections in this year's report include the enactment of the MACRA, which was enacted in 2015 and repealed the SGR formula that set physician fee schedule payments. While the physician payment updates and new incentives put in place by MACRA avoid the significant short-range physician payment issues that would have resulted from the SGR system approach, they nevertheless raise important long-range concerns. In particular, additional payments of $500 million per year for one group of physicians and 5 percent annual bonuses for another group are scheduled to expire in 2025, resulting in a significant one-time payment reduction for most physicians. In addition, the law specifies the physician payment update amounts for all years in the future, and these amounts do not vary based on underlying economic conditions, nor are they expected to keep pace with the average rate of physician cost increases. The specified rate updates could be an issue in years when levels of inflation are high and would be problematic when the cumulative gap between the price updates and physician costs becomes large. The gap will continue to widen throughout the projection, and it is estimated that physician payment rates under current law will be lower than they would have been under the SGR formula by 2048. Absent a change in the delivery system or level of update by subsequent legislation, access to Medicare-participating physicians may become a significant issue in the long term under current law.

Incorporated in these projections is the sequestration of non-salary Medicare expenditures as required by the following laws:

- *Budget Control Act of 2011* (P.L. 112-25, enacted on August 2, 2011), as amended by the *American Taxpayer Relief Act of 2012* (P.L. 112-240, enacted on January 2, 2013);
- *Continuing Appropriations Resolution, 2014* (P.L. 113-67, enacted on December 26, 2013);
- Sections 1 and 3 of P.L. 113-82, enacted on February 15, 2014;
- *Protecting Access to Medicare Act of 2014* (P.L. 113-93, enacted on April 1, 2014);
- *BBA of 2015* (P.L. 114-74, enacted on November 2, 2015); and
- *BBA of 2018* (P.L. 115-123, enacted on February 9, 2018).

The sequestration reduces benefit payments by 2 percent from April 1, 2013 through March 31, 2027, and by 4 percent from April 1, 2027 through September 30, 2027. Due to sequestration, non-salary administrative expenses are reduced by an estimated 5 to 7 percent from March 1, 2013 through September 30, 2027.

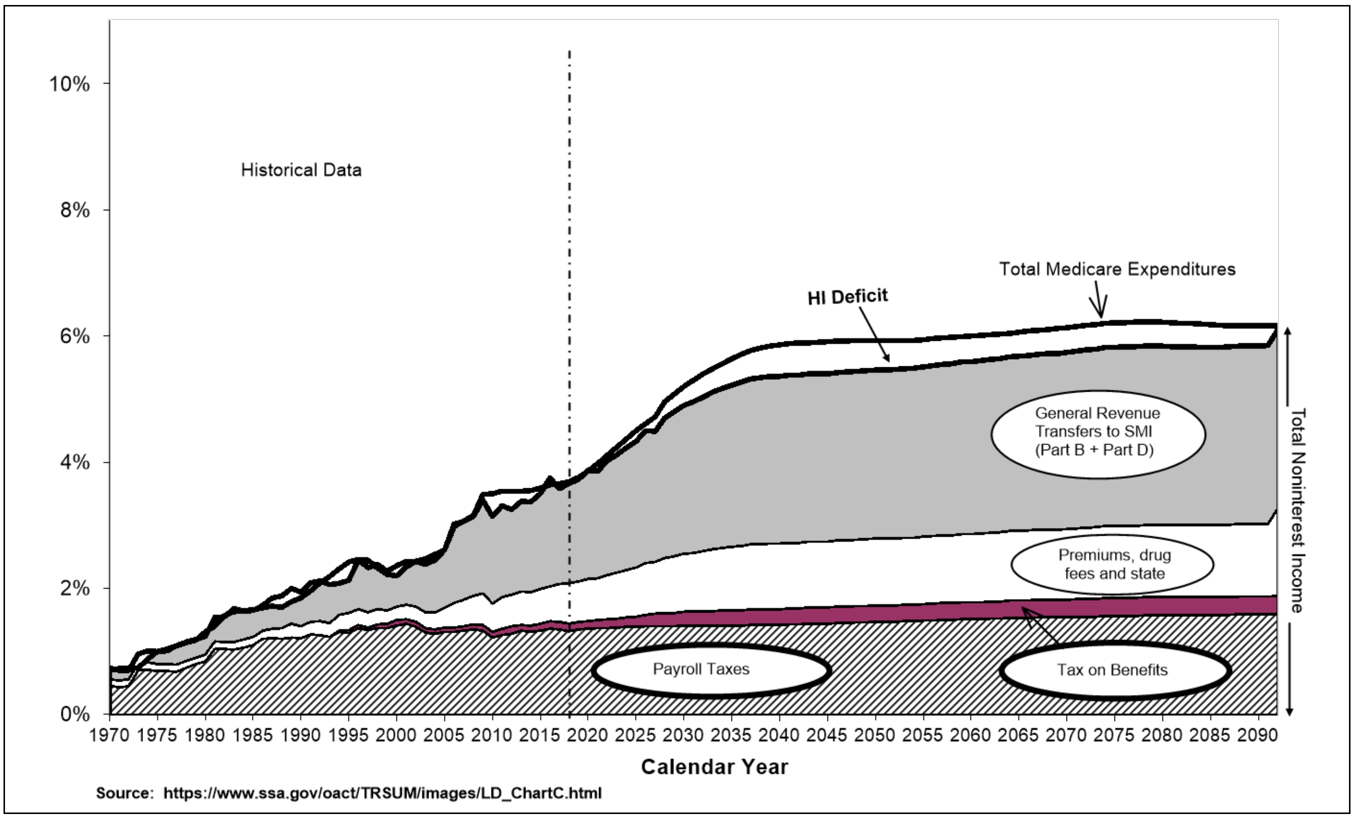
These projections also incorporate the effects of the *Patient Protection and Affordable Care Act,* as amended by the *HCERA of 2010*. This legislation, referred to collectively as the *Affordable Care Act* or ACA, was enacted in 2010 and contains roughly 165 provisions affecting the Medicare program by reducing costs, increasing revenues, improving benefits, combating fraud and abuse, and initiating a major program of R&D to identify alternative provider payment mechanisms, health care delivery systems, and other changes intended to improve the quality of health care and reduce costs.

The 2018 Medicare Trustees' Report warns that the financial projections for the Medicare program reflect substantial, but very uncertain, cost savings deriving from provisions of the ACA and MACRA that lower increases in Medicare payment rates to most categories of health care providers. Without fundamental change in the current delivery system, these adjustments would probably not be viable indefinitely. It is conceivable that providers could improve their productivity, reduce wasteful expenditures, and take other steps to keep their cost growth within the bounds imposed by the Medicare price limitations. For such efforts to be successful in the long range, however, providers would have to generate and sustain unprecedented levels of productivity gains—a very challenging and uncertain prospect. In view of the factors described above, it is important to note that Medicare's actual future costs are highly uncertain for reasons apart from the inherent challenges in projecting health care cost growth over time.

Changes in Projection Methods. The projections in this year's report, with one exception related to Part A, are based on current law; that is, it is assumed that laws on the books will be implemented and adhered to with respect to scheduled taxes, premium revenues, and payments to providers and health plans. The one exception is that the projections disregard payment reductions that would result from the projected depletion of the HI Trust Fund. Under current law, payments would be reduced to levels that could be covered by incoming tax and premium revenues when the HI Trust Fund was depleted.

Total Medicare. Chart 5 shows expenditures and current-law noninterest revenue sources for HI and SMI combined as a percent of GDP. Under the ACA, beginning in 2013 the HI Trust Fund receives an additional 0.9 percent tax on earnings in excess of $250,000 for joint tax return filers and $200,000 for individual tax return filers. As a result of this provision, it is projected that payroll taxes will grow slightly faster than GDP. After 2018, HI revenue from income taxes on Social Security benefits will gradually increase as a share of GDP as the share of benefits subject to such taxes increases. Beginning in 2009, as HI payroll tax receipts declined due to the recession and general revenue transfers increased, the latter income source became the largest single source of income to the Medicare program as a whole. General revenue transfers to the Part B account increased significantly in 2016, as required by the BBA of 2015 to compensate for premium revenue that was not received in 2016 due to the hold harmless provision, which limited the Part B premium increase for a majority of beneficiaries. After decreasing from 2016 to 2017, general revenues will gradually increase as a share of Medicare financing from 2018 through 2032 and grow to about 49 percent, stabilizing thereafter. SMI premiums will also grow in proportion to general revenue transfers, placing a growing burden on beneficiaries. High-income beneficiaries have paid an income-related premium for Part B since 2007 and for Part D since 2011. SMI general revenues equal 1.5 percent of GDP in 2017 and will increase to an estimated 2.8 percent in 2092 under current law.

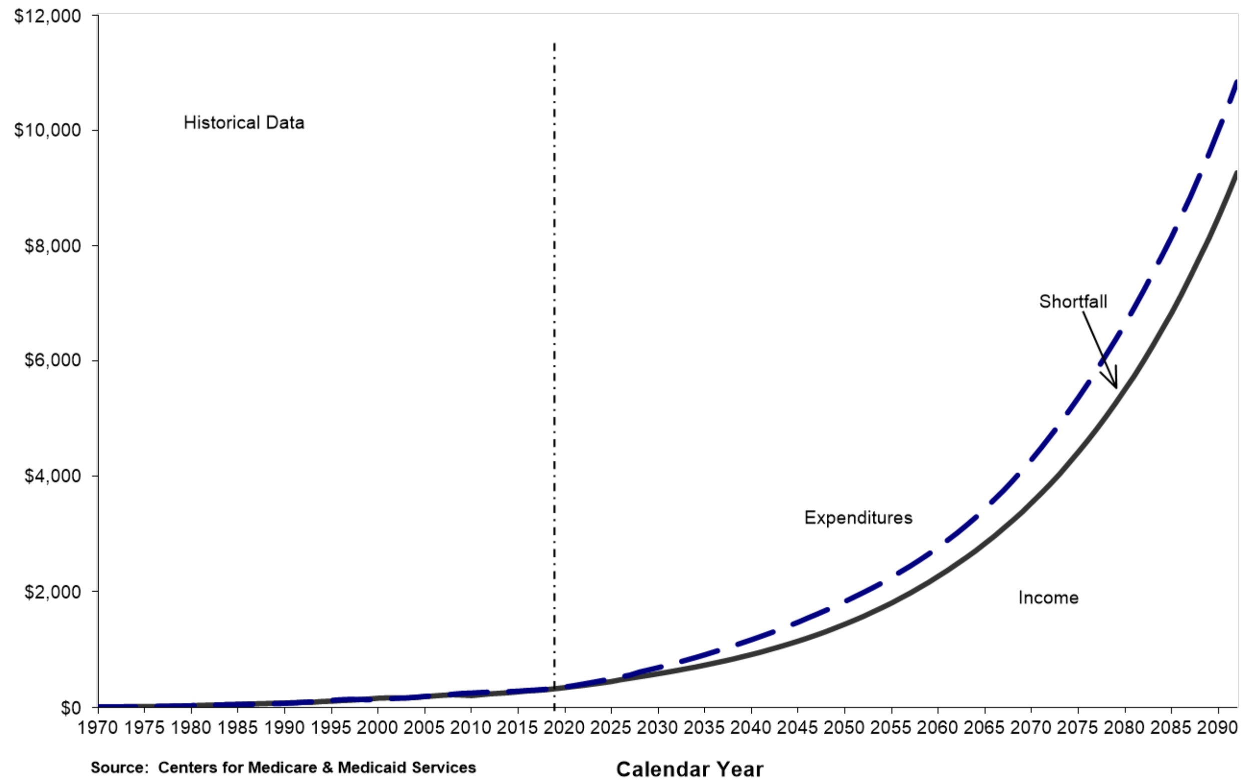
Chart 5—Total Medicare (HI and SMI) Expenditures and Noninterest Income as a Percent of GDP 1970-2092



Medicare, Part A (Hospital Insurance)— Income and Expenditures. Chart 6 shows historical and actuarial estimates of HI annual income (excluding interest) and expenditures for 1970-2092 in nominal dollars. The estimates are for the open-group population.

Chart 6—Medicare Part A Income (Excluding Interest) and Expenditures 1970-2092

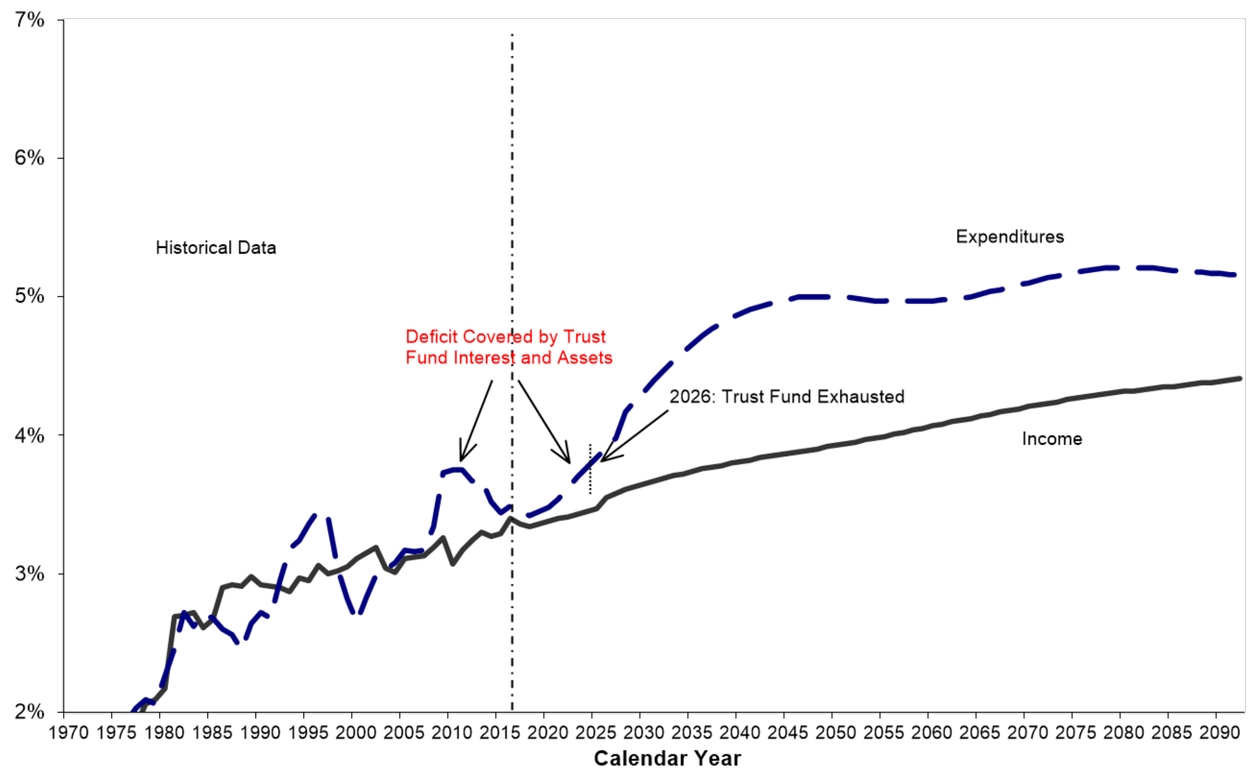
(In billions of dollars)



Source: Centers for Medicare & Medicaid Services

Medicare, Part A Income and Expenditures as a Percent of Taxable Payroll. Chart 7 illustrates income (excluding interest) and expenditures as a percentage of taxable payroll over the next 75 years. The projected HI cost rates shown in the 2018 report are higher than those from the 2017 report for all years largely due to higher spending and lower taxable payroll in all projected years. The standard HI payroll tax rate is scheduled to remain constant at 2.90 percent (for employees and employers, combined). In addition, starting in 2013, high-income workers pay an additional 0.9 percent of their earnings above $200,000 (for single workers) or $250,000 (for married couples filing joint income tax returns). Since these income thresholds are not indexed, over time an increasing proportion of workers and their earnings will become subject to the additional HI tax rate. (By the end of the long-range projection period, an estimated 79 percent of workers would be subject to this tax.) Thus, HI payroll tax revenues will increase steadily as a percentage of taxable payroll. Similarly, after 2019, HI income from taxation of Social Security benefits will also increase faster than taxable payroll because the income thresholds determining taxable benefits are not indexed for price inflation. The cost rate has mostly been declining since 2010, and it is projected to continue to decline in 2018, largely due to (i) expenditure growth that was constrained in part by low utilization and low payment updates, and (ii) a rebound of taxable payroll growth from 2007-2009 recession levels. After 2018 the cost rate is projected to rise primarily due to retirements of those in the baby-boom generation and partly due to a projected return to modest health services cost growth. This cost rate increase is moderated by the accumulating effect of the productivity adjustments to provider price updates, which are estimated to reduce annual HI per capita cost growth by an average of 0.8 percent through 2027 and 1.1 percent thereafter. The noninterest income is projected to decrease from 91 percent in 2026 to 78 percent in 2042, and then to increase to about 85 percent by the end of the projection period.

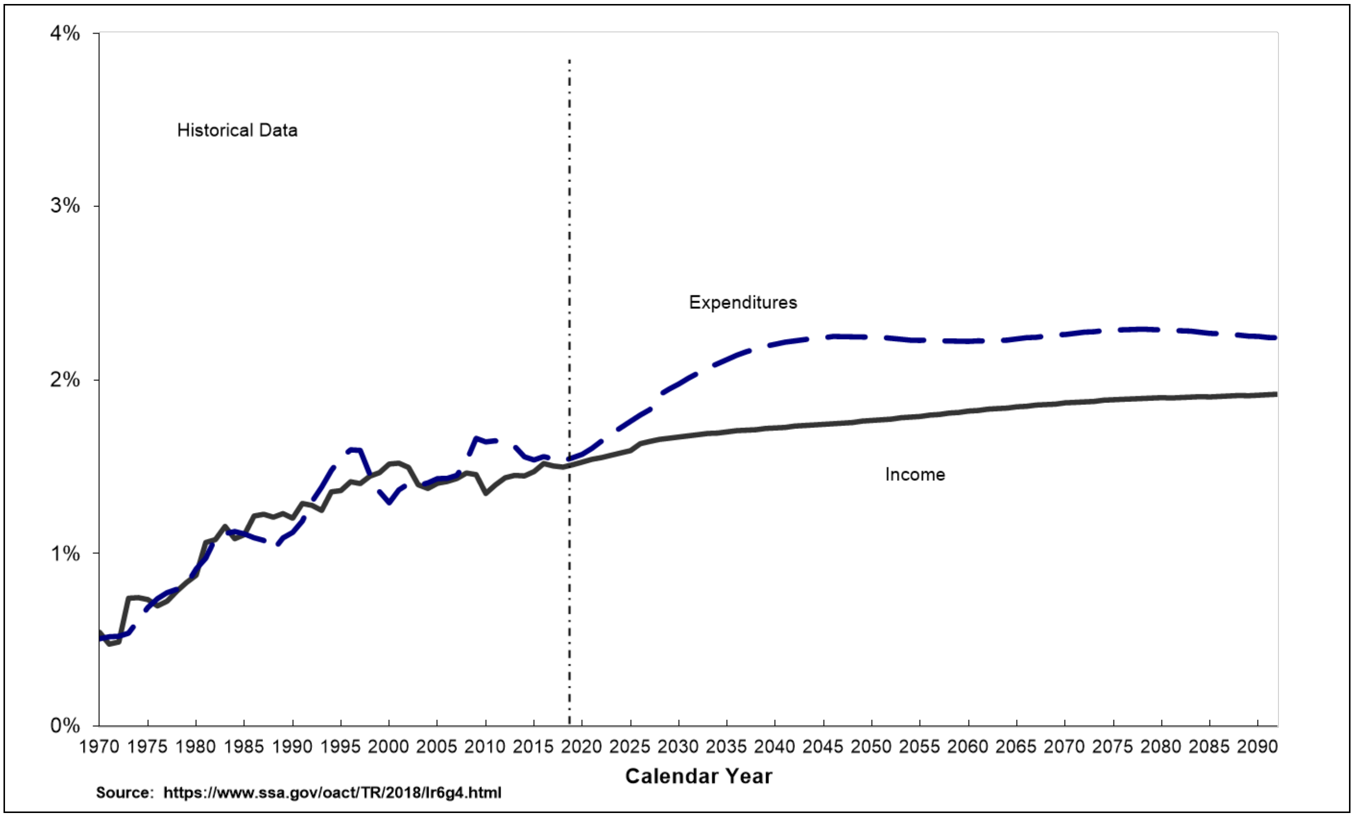
Chart 7—Medicare Part A Income (Excluding Interest) and Expenditures as a Percent of Taxable Payroll 1970-2092



Source: https://www.ssa.gov/OACT/TRSUM/images/LD_ChartB.html

Medicare, Part A Income and Expenditures as a Percent of GDP. Chart 8 shows estimated annual noninterest income and expenditures, expressed as a percent of GDP, the total value of goods and services produced in the U.S. This alternative perspective shows the size of the HI Program in relation to the capacity of the national economy to sustain it. Under the intermediate and high-cost assumptions, the HI annual balance is negative for all years of the projection period. Under the intermediate assumptions, annual deficits generally increase through 2045, and then generally decline thereafter. The gap between expenditure and income shares of GDP widens to 0.50 percent in 2045, and then commences a slight decline, reaching 0.33 percent of GDP in 2092.

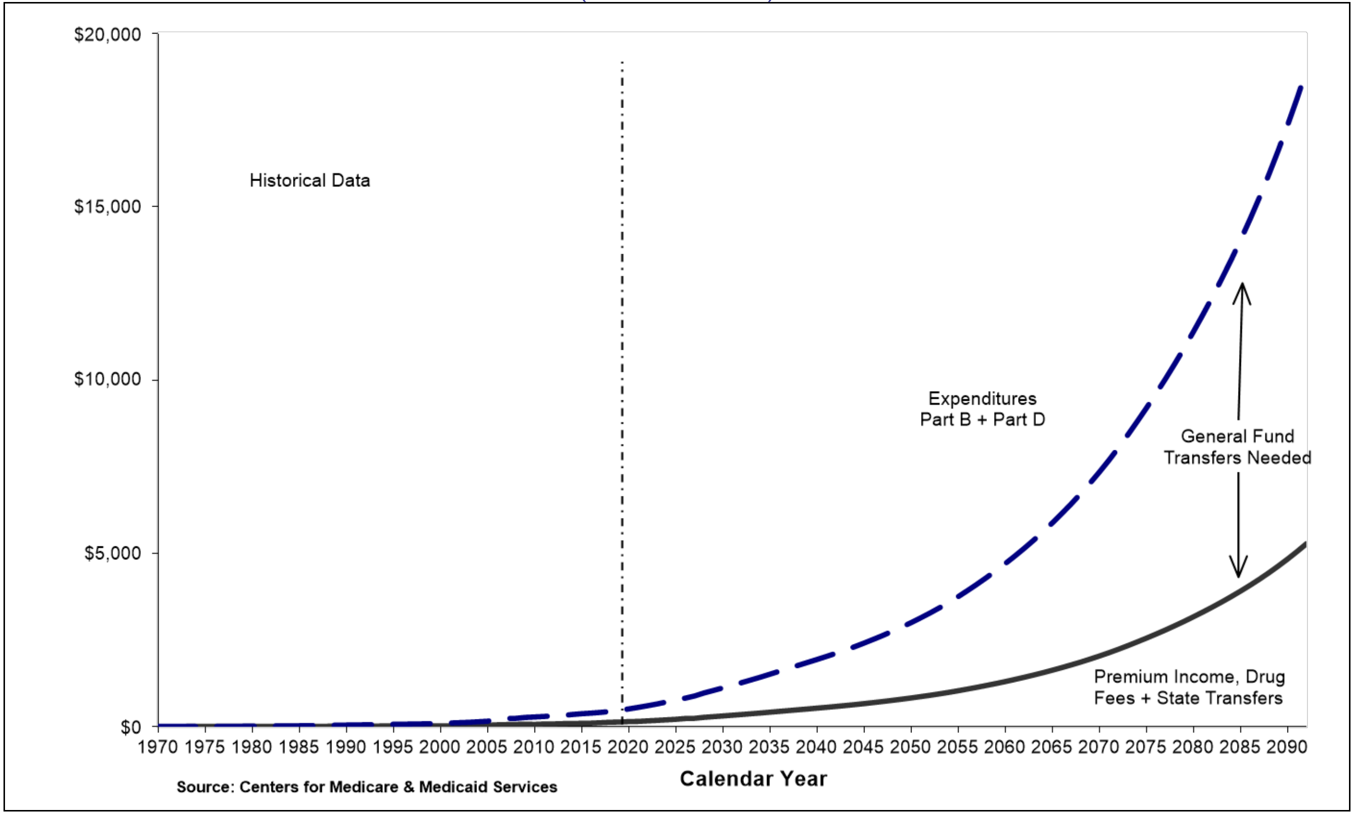
Chart 8—Medicare Part A Income (Excluding Interest) and Expenditures as a Percent of GDP 1970-2092



Medicare, Parts B and D SMI. Chart 9 shows historical and actuarial estimates of Medicare Part B and Part D premiums (and Part D state transfers) as well as expenditures for each of the next 75 years, in dollars. Beneficiary premiums and general revenue contributions for both Part B and Part D are established annually to cover the expected costs for the upcoming year. Should actual costs exceed those anticipated when the financing is determined, future financing rates can include adjustments to recover the shortfall. Likewise, should actual costs be less than those anticipated, the savings would result in lower future financing rates. The gap between program expenditures and revenues from premiums, drug fees, and state transfers grows throughout the projection period. This gap will need to be filled with general revenue transfers.

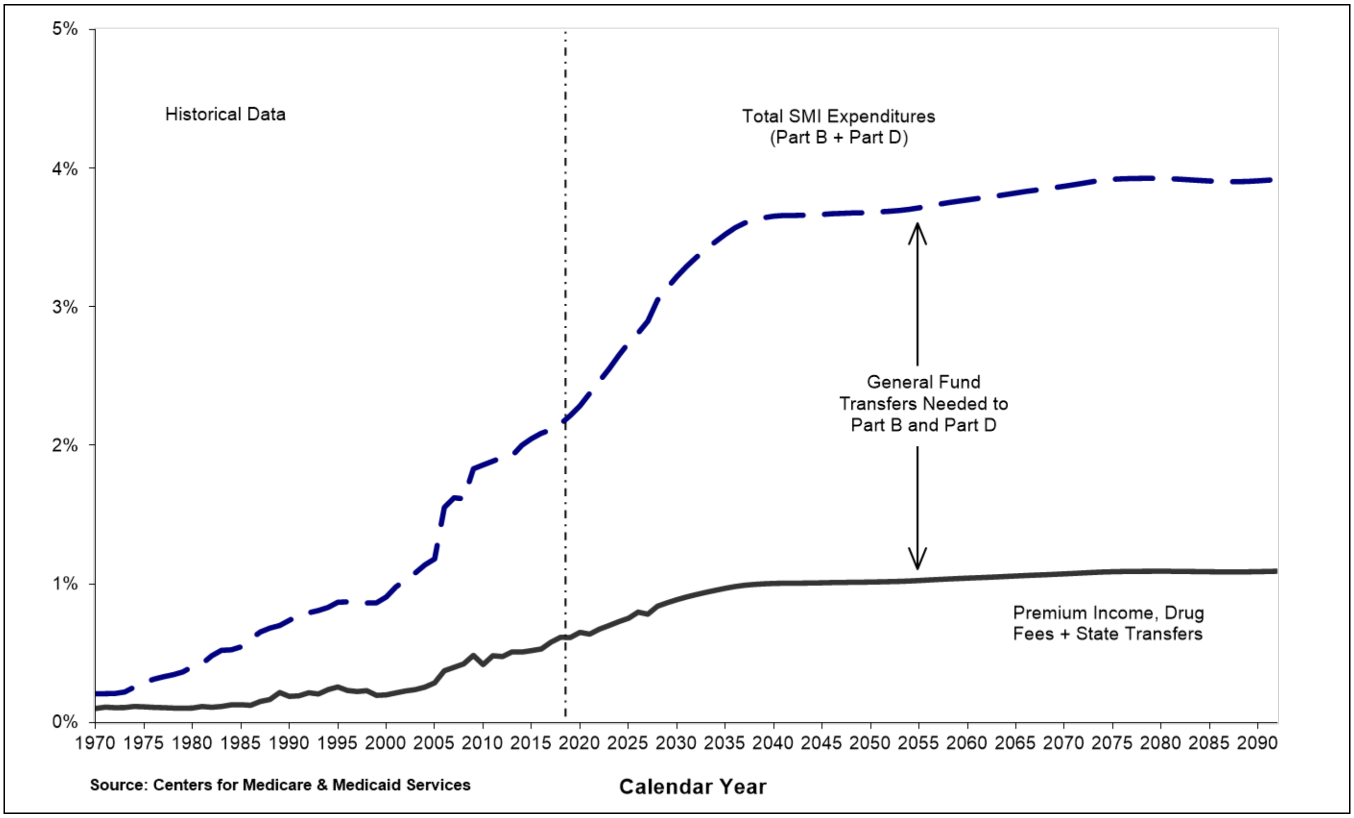
Chart 9—Medicare Part B and Part D Premium and State Transfer Income and Expenditures 1970-2092

(In billions of dollars)



Medicare Part B and Part D Premium as well as State Transfer Income and Expenditures as a Percent of GDP. Chart 10 shows expenditures for the SMI Program over the next 75 years expressed as a percent of GDP, providing a perspective on the size of the SMI Program in relation to the capacity of the national economy to sustain it. SMI costs are projected to continue to outpace growth in GDP but at a slower rate compared to the last 10 years. Total SMI expenditures amounted to 2.1 percent of GDP in 2017 and are projected to grow to about 3.7 percent of GDP within 25 years and to 3.9 percent by the end of the projection period. The relatively high growth during the period 2018-2027 is due to the continuing retirement of the baby-boom generation and modest increases in cost trends. Growth rates are projected to decline during the 2028-2042 period primarily as a result of a deceleration in beneficiary population growth. For the last 50 years of the projection period, cost growth moderates further due to the continued deceleration in beneficiary population growth and lower health care cost growth rate assumptions. To match the faster growth rates for SMI expenditures, beneficiary premiums, along with general revenue contributions, would increase more rapidly than GDP over time but at a slower rate compared to the last 10 years. Average per beneficiary costs for Part B and Part D benefits are projected to increase after 2017 by about 4.3 percent annually. The associated beneficiary premiums—and general revenue financing—would increase by approximately the same rate.

Chart 10—Medicare Part B and Part D Premium and State Transfer Income and Expenditures as a Percent of GDP 1970-2092



Medicare Sensitivity Analysis. This section illustrates the sensitivity of long-range cost and income estimates for the Medicare Program to changes in *selected individual assumptions*. As with the OASDI analysis, the intermediate assumption is used as a reference point, and each selected assumption is varied individually to produce three scenarios. The variation used for each individual assumption reflects the levels used for that assumption in the low-cost and high-cost projections (see description of sensitivity analysis for OASDI). All present values are calculated as of January 1, 2018 and are based on estimates of income and expenditures during the 75-year projection period.

Table 3 shows the net present value of cash flow during the 75-year projection period under three alternative assumptions for the annual growth rate in the aggregate cost of providing covered health care services to beneficiaries. These assumptions are that the ultimate annual growth rate in such costs, relative to taxable payroll, will be 1 percent slower than the intermediate assumptions, the same as the intermediate assumptions, and 1 percent faster than the intermediate assumptions. The assumptions are shown in parentheses. The table demonstrates that if the ultimate growth rate assumption is 1 percentage point lower than the intermediate assumption, the deficit decreases by $7,812 billion. On the other hand, if the ultimate growth rate assumption is 1 percentage point higher than the intermediate assumption, the deficit increases substantially by $12,472 billion. This assumption has a dramatic impact on projected HI cash flow. The present value of the net cash flow under the ultimate growth rate assumption of 1 percentage point lower than the intermediate assumption actually becomes a surplus due to the improved financial outlook for the HI trust fund as a result of the ACA. Several factors, such as the utilization of services by beneficiaries or the relative complexity of services provided, can affect costs without affecting tax income. As the table indicates, the financial status of the HI Trust Fund is extremely sensitive to the relative growth rates for health care service costs.

The fertility rate assumption has a substantial impact on projected HI cash flows. As demonstrated by Table 3, for an increase of 0.2 in the assumed ultimate fertility rate, the projected present value of the HI deficit decreases by approximately $562 billion, and for a decrease of 0.2 in the assumed ultimate fertility rate, the projected present value of the HI deficit increases by approximately $557 billion. Under the higher fertility rate assumptions, there will be additional workers in the labor force after 20 years, and many will become subject to the additional HI tax, thereby lowering the deficit proportionately more on a present-value-dollar basis. On the other hand, under the lower fertility rate assumptions, there will be fewer workers in the workforce with a smaller number subject to the additional tax, in turn raising the HI deficit. It is important to point out that if a longer projection period were used, the impact of a fertility rate change would be more pronounced.

Relative to the intermediate case, for an increase in the ultimate real-wage differential assumption of 0.6 percentage points, the deficit—expressed in present-value dollars—decreases by approximately $2,394 billion. Conversely, for a decrease in the ultimate real-wage differential assumption of 0.6 percentage points, the deficit increases by about $1,271 billion. When expressed in present-value dollars, faster real-wage growth results in smaller HI cash flow deficits. A higher real-wage differential immediately increases both HI expenditures for health care and wages for all workers. There is a full effect on wages and payroll taxes, but the effect on benefits is only partial, since not all health care costs are wage-related. In practice, faster real-wage growth always improves the financial status of the HI trust fund, regardless of whether there is a small or large imbalance between income and expenditures.

As Table 3 indicates, the change in CPI inflation has an impact when the cash flow is expressed as present values. If the ultimate CPI-increase assumption is changed from 2.6 percent, the intermediate assumption, to 3.2 percent, the deficit decreases by $1,060 billion. On the other hand, if the ultimate CPI-increase is changed from 2.6 percent, the intermediate assumption, to 2.0 percent, the deficit increases by $1,375 billion. The projected present values of HI cash flow are relatively insensitive to the assumed level of general price inflation because price inflation has about the same proportionate effect on income as it does on costs. In present value terms, a smaller deficit results under high-inflation conditions because the present values of HI expenditures are not significantly different under the various CPI scenarios, but under high-inflation conditions the present value of HI income increases as more people become subject to the additional 0.9 percent HI tax rate required by the ACA for workers with earnings above $200,000 or $250,000 (for single and joint income-tax filers, respectively). Since the thresholds are not indexed, additional workers become subject to the additional tax more quickly under conditions of faster inflation, and vice versa.

Higher net immigration results in smaller HI cash flow deficits. Since immigration tends to occur most often among people at working ages, who work and pay taxes into the HI system, a change in the net immigration assumption affects revenues from payroll taxes almost immediately. However, the impact on expenditures occurs later as those individuals age and become beneficiaries.

Table 3 also shows that the present value of net HI expenditures is approximately 15 percent lower if the real interest rate is 3.2 percent rather than 2.7 percent, and approximately 18 percent higher if the real interest rate is 2.2 percent rather than 2.7 percent.

Table 3
Present Values of Estimated Medicare Part A Expenditures in Excess of Income Under Various Assumptions, 2018-2092

(Dollar values in billions; values of assumptions shown in parentheses)

	Financing Shortfall Range		
Assumption[1]	**Low**	**Intermediate**	**High**
Average annual growth in health costs[2]	(3,104) (2.7)	4,708 (3.7)	17,180 (4.7)
Total fertility rate[3]	4,146 (2.2)	4,708 (2.0)	5,265 (1.8)
Real wage differential	2,314 (1.8)	4,708 (1.2)	5,979 (0.6)
CPI change	3,648 (3.2)	4,708 (2.6)	6,083 (2.0)
Net immigration[4]	4,503 (1,607,000)	4,708 (1,272,000)	4,973 (952,000)
Real interest rate	4,018 (3.2)	4,708 (2.7)	5,542 (2.2)

[1] The sensitivity of the projected HI net cash flow to variations in future mortality rates also is of interest. At this time, however, relatively little is known about the relationship between improvements in life expectancy and the associated changes in health status and per beneficiary health expenditures. As a result, it is not possible at present to prepare meaningful estimates of the Part A, mortality sensitivity.
[2] Annual growth rate is the aggregate cost of providing covered health care services to beneficiaries. The low-cost and high-cost alternatives assume that costs increase 1 percent slower or faster, respectively, than the intermediate assumption, relative to growth in taxable payroll.
[3] The total fertility rate for any year is the average number of children who would be born to a woman in her lifetime if she were to experience the birth rates by age observed in, or assumed for, the selected year and if she were to survive the entire childbearing period.
[4] Amount represents the average annual net immigration over the 75-year projection period.

Source: CMS

Table 4 shows the effects of various assumptions about the growth in health care costs on the present value of estimated SMI (Medicare Parts B and D) expenditures in excess of income. As with HI, net SMI expenditures are very sensitive to changes in the health care cost growth assumption. For the low-cost alternative, the slower assumed growth in health costs reduces the governmentwide resources needed for Part B from $25,079 billion to $18,175 billion and in Part D from $7,902 billion to $5,587 billion, about a 28 percent and 29 percent difference for Part B and Part D, respectively. The high-cost assumption increases governmentwide resources needed to $35,846 billion for Part B and to $11,585 billion for Part D, about a 43 percent and a 47 percent difference for Part B and Part D, respectively.

Table 4
Present Values of Estimated Medicare Parts B and D Future Expenditures Less Premium Income and State Transfers Under Three Health Care Cost Growth Assumptions, 2018-2092

(In billions of dollars)

	Governmentwide Resources Needed		
Medicare Program[1]	Low (3.3)	Intermediate (4.3)	High (5.3)
Part B	18,175	25,079	35,846
Part D	5,587	7,902	11,585

[1] Annual growth rate is the aggregate cost of providing covered health care services to beneficiaries. The low and high scenarios assume that costs increase one percent slower or faster, respectively, than the intermediate assumption.

Source: CMS

Sustainability of Social Security and Medicare

75-Year Horizon

According to the 2018 Medicare Trustees Report, the HI Trust Fund is projected to remain solvent until 2026 and, according to the 2018 Social Security Trustees Report, the OASI and DI Trust Funds are projected to have sufficient asset reserves to pay full benefits on time until 2034 and 2032, respectively. In each case, some general revenues must be used to satisfy the authorization of full benefit payments until the year of trust fund depletion. This occurs when the trust fund interest income and balances accumulated during prior years are needed to pay benefits, which leads to a transfer from general revenues to the trust funds. Moreover, under current law, General Fund transfers to the SMI Trust Fund will occur into the indefinite future and will continue to grow with the growth in health care expenditures.

The potential magnitude of future financial obligations under these three social insurance programs is, therefore, important from a budget perspective as well as for understanding generally the growing resource demands of the programs on the economy. A common way to present future cash flows is in terms of their *present value*. This approach recognizes that a dollar paid or collected next year is worth less than a dollar today because a dollar today could be saved and earn a year's worth of interest. From the 75-year budget perspective, the present value of the additional resources that would be necessary to meet projected expenditures, for the three programs combined, is $53.7 trillion. To put this figure in perspective, it would represent 4.1 percent of the present value of projected GDP over the same period ($1,298 trillion). These resource needs would be in addition to the payroll taxes, benefit taxes, and premium payments. Asset redemptions and SMI general revenue transfers represent formal budget commitments, but no provision exists for covering the HI and OASDI Trust Fund deficits once assets are depleted.

Table 5 shows the magnitudes of the primary expenditures and sources of financing for the three trust funds computed on an open-group basis for the next 75 years and expressed in present values. The data are consistent with the SOSI included in the principal financial statements. For HI, revenues from the public are projected to fall short of total expenditures by $4,708 billion in present value terms which is the additional amount needed in order to pay scheduled benefits over the next 75 years.[14] From the trust fund perspective, the amount needed is $4,506 billion in present value after subtracting the value of the existing trust fund balances (an asset to the trust fund account but an intragovernmental transfer to the overall budget). For SMI, revenues from the public for Part B and D combined are estimated to be $32,981 billion less than total expenditures for the two accounts, an amount that, from a budget perspective, will be needed to keep the SMI program solvent for the next 75 years. From the trust fund perspective, however, the present values of total revenues and total expenditures for the SMI Program are roughly equal due to the annual adjustment of revenue from other government accounts to meet program costs.[15]

[14] Interest income is not a factor in this table as dollar amounts are in present value terms.
[15] The SMI Trust Fund has $88 billion of existing assets.

For OASDI, projected revenues from the public fall short of total expenditures by $16,057 billion in present value dollars, and by $13,166 billion from the trust fund perspective.

From the governmentwide perspective, the present value of the total resources needed for the Social Security and Medicare Programs over and above current-law funding sources (payroll taxes, benefit taxes, and premium payments from the public) is $53,747 billion. From the trust fund perspective, which counts the trust funds ($3,182 billion in present value) and the general revenue transfers to the SMI Program ($32,981 billion in present value) as dedicated funding sources, additional resources needed to fund the programs are $17,584 billion in present value.

Table 5
Present Values of Costs Less Revenues of 75-Year Open Group Obligations
HI, SMI, and OASDI

(In billions of dollars, as of January 1, 2018)	HI	SMI Part B	SMI Part D	OASDI	Total
Revenues from the public:					
Taxes	22,807	-	-	65,088	87,895
Premiums and state transfers	-	9,374	3,222	-	12,596
Total	22,807	9,374	3,222	65,088	100,491
Total costs to the public	27,515	34,453	11,124	81,146	154,238
Net results - budget perspective[1]	4,708	25,079	7,902	16,057	53,746
Revenues from other government accounts	-	25,079	7,902	-	32,981
Trust fund balances as of 1/1/2018	202	80	8	2,892	3,182
Net results - trust fund perspective[1]	4,506	(80)	(8)	13,166	17,584

[1]Net results are computed as costs less revenues and trust fund balances. Negative values are indicative of surpluses.

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

Source: 2018 OASDI and Medicare Trustees' Reports

Infinite Horizon

The 75-year horizon represented in Table 5 is consistent with the primary focus of the Social Security and Medicare Trustees' Reports. For the OASDI Program, for example, an additional $16.1 trillion in present value will be needed above currently scheduled taxes to pay for scheduled benefits ($13.2 trillion from the trust fund perspective). Experts have noted that limiting the projections to 75 years understates the magnitude of the long-range unfunded obligations because summary measures (such as the actuarial balance and open-group unfunded obligations) reflect the full amount of taxes paid by the next two or three generations of workers, but not the full amount of their benefits. One approach to addressing the limitations of 75-year summary measures is to extend the projection horizon indefinitely, so that the overall results reflect the projected costs and revenues after the first 75 years. Such extended projections can also help indicate whether the financial imbalance would be improving or continuing to worsen beyond the normal 75-year period. The open-group infinite horizon net obligation is the present value of all expected future program outlays less the present value of all expected future program tax and premium revenues. Such a measure is provided in Table 6 for the three trust funds represented in Table 5.

From the budget or governmentwide perspective, the values in line 1 plus the values in line 4 of Table 6 represent the value of resources needed to finance each of the programs into the infinite future. The sums are shown in the last line of the table (also equivalent to adding the values in the second and fifth lines). The total resources needed for all the programs sums to $101.0 trillion in present value terms. This need can be satisfied only through increased borrowing, higher taxes, reduced program spending, or some combination.

The second line shows the value of the trust fund at the beginning of 2018. For the HI and OASDI Programs this represents, from the trust fund perspective, the extent to which the programs are funded. From that perspective, when the trust fund is subtracted, an additional $34.3 trillion is needed to sustain the OASDI program into the infinite future, while the HI program reflects a projected surplus of $2.2 trillion over the infinite horizon. However, looking just at present values ignores timing differences in the underlying projected cash flows; the HI Trust Fund is projected to remain solvent only until 2029. As described above, from the trust fund perspective, the SMI Program is fully funded; from a governmentwide basis, the substantial gap that exists between premiums, state transfer revenue, and program expenditures in the SMI Program ($46.3 trillion and $19.3 trillion for Parts B and D, respectively) represents future general revenue obligations of the federal budget.

In comparison to the analogous 75-year number in Table 5, extending the calculations beyond 2092, captures the full lifetime benefits, plus taxes and premiums of all current and future participants. The shorter horizon understates the total financial needs by capturing relatively more of the revenues from current and future workers and not capturing all of the benefits that are scheduled to be paid to them.

Table 6
Present Values of Costs Less Tax, Premium and State Transfer Revenue through the Infinite Horizon, HI, SMI, OASDI

(in trillions of dollars as of January 1, 2018)	HI	SMI Part B	SMI Part D	OASDI	Total
Present value of future costs less future taxes, premiums, and state transfers for current participants	11.8	21.0	5.8	35.3	73.9
Less current trust fund balance	0.2	0.1	-	2.9	3.2
Equals net obligations for past and current participants	11.6	20.9	5.8	32.4	70.7
Plus net obligations for future participants	(13.7)	25.4	13.5	1.9	27.1
Equals net obligations through the infinite future for all participants	(2.2)	46.3	19.3	34.3	97.7
Present values of future costs less the present values of future income over the infinite horizon	(1.9)	46.4	19.3	37.2	101.0

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

Source: 2018 OASDI and Medicare Trustees' Reports

Railroad Retirement, Black Lung, and Unemployment Insurance

Railroad Retirement

The RRB was created in the 1930s to establish a retirement benefit program for the nation's railroad workers. As the Social Security Program legislated in 1935 would not give railroad workers credit for service performed prior to 1937, legislation was enacted in 1934, 1935, and 1937 (collectively the Railroad Retirement Acts of the 1930s) to establish a railroad retirement system separate from the Social Security Program.

As was discussed previously in this report, railroad retirement pays full retirement annuities at age 60 to railroad workers with 30 years of service. The program pays disability annuities based on total or occupational disability. It also pays annuities to spouses, divorced spouses, widow(er)s, remarried widow(er)s, surviving divorced spouses, children, and parents of deceased railroad workers. Medicare covers qualified railroad retirement beneficiaries in the same way as it does Social Security beneficiaries.

Payroll taxes paid by railroad employers and their employees provide a primary source of income for the Railroad Retirement and Survivors' Benefit Program. Other sources of program income include: the RRB-SSA-CMS Financial Interchanges with the Social Security and Medicare Trust Funds, earnings on investments, federal income taxes on railroad retirement benefits, and appropriations.

For further detail related to Railroad Retirement Program financing and actuarial assumptions, see Note 22—Social Insurance.

Cash Flow Projections

Income and Expenditures. Railroad retirement cash flow projections are based on the intermediate set of assumptions used in the RRB's actuarial valuation of the program. The estimates are for the open-group population, which includes all persons projected to participate in the Railroad Retirement Program as railroad workers or beneficiaries during the period. Thus, the estimates include payments from, and on behalf of, those who will be employed by the railroads during the period as well as those already employed at the beginning of the period. They also include expenditures made to, and on behalf of, such workers during that period. Estimated railroad retirement expenditures are expected to exceed estimated income (excluding interest and financial interchange income), in dollars, for the entire projection period (2018-2092).

Sensitivity Analysis. The projections of the future financial status of the Railroad Retirement Program depend on many economic and demographic assumptions. For further information on the sensitivity of the long-range projections of the Railroad Retirement Program and how the projections are impacted by changes in certain key assumptions, refer to RRB's financial statements.

Sustainability of Railroad Retirement

Consistent with SOSI the primary expenditures and sources of financing for the Railroad Retirement Program are computed on an open-group basis for the next 75 years and are expressed in present values as of October 1, 2017. From a governmentwide perspective, revenues are expected to fall short of expenditures by approximately $108.5 billion, which represents the present value of resources needed to sustain the Railroad Retirement Program. From a trust fund perspective, when the trust fund balance ($27.9 billion) and the financial interchange and transfers ($81.9 billion) are included, the combined balance of the NRRIT, the Railroad Retirement Account, and the SSEB Account show a slight surplus ($1.3 billion). For further detail related to the sustainability of the Railroad Retirement Program, refer to RRB's financial statements.

Black Lung

The *Federal Coal Mine Health and Safety Act of 1969* created the Black Lung Disability Benefit Program to provide compensation, medical, and survivor benefits for eligible coal miners who are totally disabled due to pneumoconiosis (black lung disease) arising out of their coal mine employment and the BLDTF provides benefit payments when no RMO can be assigned the liability.

As was stated in the note to Social Insurance earlier in this report, black lung disability benefit payments are funded by excise taxes from coal mine operators based on the domestic sale of coal, as are the program's administrative costs. These taxes are collected by the IRS and transferred to the BLDTF.

P.L. 110-343, *Division B-Energy Improvement and Extension Act of 2008*, enacted on October 3, 2008, among other things, restructured the BLDTF debt by refinancing the outstanding high interest rate repayable advances with low interest rate discounted debt instruments similar in form to zero-coupon bonds, plus a one-time appropriation. This Act also allowed that any subsequent debt issued by the BLDTF may be used to make benefit payments, other authorized expenditures, or to repay debt and interest from the initial refinancing. For more information on Black Lung Disability Benefit Program financing and actuarial assumptions, see Note 22—Social Insurance.

Cash Flow Projections

Projected Cash Inflows and Outflows, in Constant Dollars, for the Open Group. Effective for fiscal year 2017 reporting, DOL revised its projection period from a fixed terminus of fiscal year 2040 to a rolling 25-year period beginning on the valuation date. In order to be consistent with Executive Branch policy on regulations pursuant to the Clean Power Plan (CPP), DOL's estimates of future excise tax income were based on Energy Information Administration (EIA) projections of future coal production that do not reflect CPP regulation. The EIA projections reflect the continuing trend of lower coal production which would lead to lower future excise tax income. The projections, in constant dollars for the open group, made over the 25-year period ending September 30, 2043, indicate that cash outflows for benefit payments and administrative expenses will exceed cash inflows from excise taxes for all years in the projection period.

Sensitivity Analysis. For the projected cash inflows and outflows with sensitivity analysis, in constant dollars for the open group, the significant assumption for medical cost inflation was increased by one percent. For the sensitivity analysis, the other significant assumptions (coal excise tax revenue estimates, tax rate structure, number of beneficiaries, life expectancy, federal civilian pay raises, interest rate on new debt issued by the BLDTF, and CPI-U for goods and services) were left unchanged. Cash projections depend on the assumptions used and actual experience may differ materially from the projections. These projections with sensitivity analysis, in constant dollars for the open group, made over the 25-year period ending September 30, 2043, indicate cash outflows for benefit payments and administrative expenses will exceed cash inflows from excise taxes for all years in the projection period. For further information on the sensitivity of the projections of the Black Lung Disability Benefit Program and how the projections are impacted by changes in assumptions, refer to DOL's financial statements.

Sustainability of Black Lung

On September 30, 2018, total liabilities of the BLDTF exceeded assets by $5.6 billion. This net position deficit represents the accumulated shortfall of excise taxes necessary to meet benefit payments, administrative costs, and interest expense incurred prior to and subsequent to the debt refinancing pursuant to P.L. 110-343. Prior to the enactment of P.L. 110-343, this shortfall was funded by repayable advances to the BLDTF, which were repayable with interest. Pursuant to P.L. 110-343, any shortfall will be financed with debt instruments similar in form to zero-coupon bonds, with a maturity date of one year and bear interest at the Treasury 1-year rate. For further detailed information on the sustainability of the Black Lung Disability Benefit Program, refer to DOL's financial statements.

Unemployment Insurance

The UI Program was created in 1935 to provide income assistance to unemployed workers who lose their jobs generally through no fault of their own, and are unemployed due to a lack of suitable work. The program protects workers during temporary periods of unemployment through the provision of unemployment compensation benefits. The program is administered through a unique system of federal and state partnerships established in federal law but executed through conforming state laws by state entities. The federal government provides broad policy guidance and program direction through the oversight of DOL, while program details are established through individual state UI statutes, administered through state UI entities.

The UI Program is financed through the collection of federal and state unemployment taxes levied on subject employers and deposited in the UTF and federal appropriations. The fund was established to account for the receipt, investment, and disbursement of unemployment taxes. Federal unemployment taxes are used to pay for the administrative costs of the UI

Program, including grants to each state to cover the costs of state UI operations and the federal share of extended UI benefits. Federal unemployment taxes are also used to fund an account within the UTF to make advances to state UI accounts when a state's UI account balance has been exhausted and the state is unable to make benefit payments.

The UI Program provides regular and extended benefit payments to eligible unemployed workers. Regular UI program benefits are established under state law and are payable for a period not to exceed a maximum duration. In 1970 federal law began to require states to extend this maximum period of benefit duration by 50 percent during periods of high unemployment. These extended benefit payments are paid equally from federal and state accounts.

Cash Flow Projections

The significant assumptions used in the cash flow projections of the UTF include total unemployment rates, civilian labor force levels, percent of unemployed receiving benefits, total wages, distribution of benefit payments by state, state tax rate structures, state taxable wage bases, interest rates on UTF investments, and the CPI-U for goods and services. Cash projections depend on the assumptions used and actual experience may differ materially from the projections. Under expected economic conditions, total cash inflows, excluding interest earnings, are projected to exceed total cash outflows through the end of the projection period.

Sensitivity Analysis. The effect on the accumulated UTF assets of projected total cash inflows and cash outflows of the UTF, in constant dollars, over the ten-year period ending September 30, 2028, are demonstrated in two sensitivity analyses. Each sensitivity analysis uses an open group, which includes current and future participants in the UI Program. Sensitivity Analysis I assumes higher rates of unemployment and Sensitivity Analysis II assumes even higher rates of unemployment compared to expected economic conditions. In Sensitivity Analysis I, which uses a higher unemployment rate of 5.5 percent beginning in fiscal year 2019, net cash inflows are negative in fiscal years 2019 through 2024, but become positive in fiscal year 2025, and continue to be positive through 2028. In Sensitivity Analysis II, net cash outflows, including interest earnings and expenses, are projected in fiscal years 2019 through 2024, but inflows exceed outflows in fiscal years 2025 through 2028. Net cash inflows are reestablished in fiscal year 2025 and peak in fiscal year 2027, with a drop in the unemployment rate to 8.3 percent in fiscal year 2023, and then steadily downward for fiscal years 2024 through 2028. The example of expected economic conditions and two sensitivity analyses, in constant dollars, demonstrate the counter cyclical nature of the UI Program, which experiences net cash inflows during periods of low unemployment that are depleted by net cash outflows during periods of increased unemployment. For further detail on the sensitivity of the projections of the UI Program, refer to DOL's financial statements.

Sustainability of Unemployment Insurance

The ability of the UI Program to meet a participant's future benefit payment needs depends on the availability of accumulated taxes and earnings within the UTF. The effect of projected benefit payments on the accumulated net assets of the UTF is measured, under an open group scenario, which includes current and future participants in the UI Program. As of September 30, 2018, total assets within the UTF exceeded total liabilities by $72.5 billion. At the present time there is a surplus; any surplus of tax revenues and earnings on these revenues over benefit payment expenses is available to finance benefit payments in future periods when tax revenues may be insufficient. For more information on the sustainability of the UI Program, refer to DOL's financial statements.

Unemployment Trust Fund Solvency

Each state's accumulated UTF net assets or reserve balance should provide a defined level of benefit payments over a defined period. To be minimally solvent, a state's reserve balance should provide for one year's projected benefit payment needs based on the highest levels of benefit payments experienced by the state over the last 20 years. A ratio of 1.0 or greater indicates that the state UTF account balance is minimally solvent. States below this level are vulnerable to exhausting their funds in a recession. States exhausting their reserve balance must borrow funds from the Federal Unemployment Account (FUA) to make benefit payments. In fiscal year 2018, there were no FUA borrowings.

The results of DOL's state by state analysis indicate 23 state funds plus the fund of the Virgin Islands were below the minimal solvency ratio of 1.0 at September 30, 2018.

Deferred Maintenance and Repairs

Deferred maintenance and repairs result from maintenance not being performed on a timely basis and is the estimated cost to bring government-owned PP&E to an acceptable condition. Deferred maintenance and repairs exclude the cost of expanding the capacity of assets or upgrading them to serve needs different from those originally intended. The consequences of not performing regular maintenance and repairs could include increased safety hazards, poor service to the public, higher costs in the future, and inefficient operations. Estimated deferred maintenance and repairs costs are not accrued in the Statements of Net Cost or recognized as a liability on the Balance Sheets.

The amounts disclosed for deferred maintenance and repairs are allowed to be measured using one of the following three methods:

- Condition assessment surveys which are periodic inspections of government-owned property to determine the current condition and estimated cost to bring the property to an acceptable condition.
- Life-cycle cost forecast that is an acquisition or procurement technique that considers operation, maintenance, and other costs in addition to the acquisition cost of assets.
- Any other method of choice that is similar to the condition assessment survey or life-cycle costing methods.

The table below of deferred maintenance and repairs is presented as a single estimate in accordance with SFFAS No. 42, *Deferred Maintenance and Repairs: Amending Statements of Federal Financial Accounting Standards 6, 14, 29, and 32.* These amounts were all measured using the condition assessment survey method. Please refer to the individual financial statements of DOI, DOD, USDA, DOE, HHS, NASA, and VA for detailed significant information on deferred maintenance and repairs.

Deferred Maintenance and Repairs as of September 30, 2018, and 2017

(In billions of dollars)	2018	2017
Asset category:		
General property, plant, and equipment	147.3	151.6
Heritage assets	18.9	18.1
Stewardship land	0.4	0.5
Total deferred maintenance and repairs	166.6	170.2

Other Claims for Refunds

Management has estimated amounts that may be paid out as other claims for tax refunds. This estimate represents an amount (principal and interest) that may be paid for claims pending judicial review by the federal courts or, internally, by appeals. The total estimated payout (including principal and interest) for claims pending judicial review by the federal courts is $11.1 billion and $8.2 billion for fiscal years 2018 and 2017, respectively. For those under appeal, the estimated payout is $1.8 billion and $2.2 billion for fiscal years 2018 and 2017, respectively. Although these refund claims have been deemed to be probable, they do not meet the criteria in SFFAS No. 5, *Accounting for Liabilities of the Federal Government*, for reporting the amounts in the Balance Sheets or for disclosure in the notes to the financial statements. However, they meet the criteria in SFFAS No. 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*, as amended, for inclusion as required supplementary information. To the extent judgments against the government for these claims prompt other similarly situated taxpayers to file similar refund claims, these amounts could become significantly greater.

Tax Assessments

The government is authorized and required to make inquiries, determinations, and assessments of all taxes that have not been duly paid. Unpaid assessments result from taxpayers filing returns without sufficient payment, as well as enforcement programs such as examination, under-reporter, substitute for return, and combined annual wage reporting. Under federal accounting standards, unpaid assessments are categorized as taxes receivable if taxpayers agree or a court has determined the assessments are owed. If neither of these conditions are met, the unpaid assessments are categorized as compliance assessments. Assessments with little or no future collection potential are called write-offs. Although compliance assessments and write-offs are not considered receivables under federal accounting standards, they represent legally enforceable claims of the government. There is, however, a significant difference in the collection potential between compliance assessments and receivables.

Compliance assessments and pre-assessment work in process are $67.5 billion and $75.8 billion for fiscal years 2018 and 2017, respectively. The amount of allowance for uncollectible amounts pertaining to compliance assessments cannot be reasonably estimated, and thus the net realizable value of the pre-assessment work-in-process cannot be determined. The amount of assessments that entities have statutory authority to collect at the end of the period but that have been written off and excluded from accounts receivable are $115.0 billion and $111.0 billion for fiscal years 2018 and 2017, respectively.

Federal Oil and Gas Resources

The DOI is responsible for managing the nation's oil and natural gas resources and the mineral revenues on federal lands, both onshore and on the Outer Continental Shelf. This management process can be broken down into six essential analysis components: pre-leasing, post-leasing and pre-production, production and post-production, revenue collection, fund disbursement, and compliance.

Federal Oil and Gas Resources as of September 30, 2018, and 2017

(In billions of dollars)	Offshore		Onshore		Total	
	2018	**2017**	**2018**	**2017**	**2018**	**2017**
Oil and lease condensate..................	20.9	23.7	11.6	12.2	32.5	35.9
Natural gas, wet after lease separation..	1.9	1.8	11.3	9.3	13.2	11.1
Total	22.8	25.5	22.9	21.5	45.7	47.0

The above table presents the estimated present value of future federal royalty receipts on estimated proved reserves[16] as of September 30, 2018 and 2017. The federal government's estimated petroleum royalties have as their basis the DOE's EIA estimates of proved reserves. The EIA provides such estimates directly for federal offshore areas and they are adjusted to extract the federal subset of onshore proved reserves. The federal proved reserves were then further adjusted to correspond with the effective date of the actual production for calendar year 2016, the most recently published EIA proved reserves report and then are projected, separately for oil and natural gas, over time to simulate a schedule of when the reserves would be produced. Future royalties are then calculated from these production streams by applying future price estimates by the OMB, and effective royalty rates, adjusted for transportation allowances and other allowable deductions. The valuation method used for gas captures royalties from three products–dry gas, wet gas, and natural gas liquids–which collectively are reported as natural gas, wet after lease separation. The present value of these royalties are then determined by discounting the revenue stream back to the effective date at a public discount rate assumed to be equal to the OMB's estimates of future 30-year Treasury bill rates. The 30-year rate was chosen because this maturity life most closely approximates the productive lives of the proved reserves estimates.

[16] Per the EIA, lease condensate is a mixture consisting primarily of pentanes and heavier hydrocarbons which is recovered as a liquid from natural gas in lease separation facilities. This category excludes natural gas plant liquids, such as butane and propane, which are recovered at downstream natural gas processing plants or facilities. Also per the EIA, natural gas, wet after lease separation, is the volume of natural gas remaining after removal of lease condensate in lease and/or field separation facilities, if any, and after exclusion of nonhydrocarbon gases where they occur in sufficient quantity to render the gas unmarketable. Natural gas liquids may be recovered from volume of natural gas, wet after lease separation, and at natural gas processing plants (https://www.eia.gov/naturalgas/data.cfm).

Estimated Federal Oil and Gas Petroleum Royalties (Proved Reserves)
As of September 30, 2018, and 2017

Petroleum Category	Quantity (in millions) 2018	Quantity (in millions) 2017	Average Purchase Price ($) 2018	Average Purchase Price ($) 2017	Average Royalty Rate (%) 2018	Average Royalty Rate (%) 2017
Oil and lease condensate (Bbl):						
Offshore	3,491.3	4,022.4	65.41	46.86	12.96	13.06
Onshore	2,361.0	2,278.0	60.16	45.20	12.19	12.12
Total	5,852.3	6,300.4				
Natural gas, wet after lease separation (Mcf):						
Offshore	5,370.3	5,946.4	3.50	3.28	11.89	11.99
Onshore	37,828.7	39,877.7	2.94	3.07	10.36	10.58
Total	43,199.0	45,824.1				

Bbl = barrels

Mcf = 1,000 cubic feet

The table above provides the estimated quantity, a weighted average purchase price, and a weighted average royalty rate by category of estimated federal petroleum royalties at the end of fiscal years 2018 and 2017.[17] The estimated quantities, average purchase prices and royalty rates vary by region; the above table reflects an overall weighted average purchase price and royalty rate, and is not presented on a regional basis, but is instead calculated based on regional averages. The prices and royalty rates are based upon historical (or estimated) averages, excluding prior-period adjustments, if any, and are affected by such factors as accounting adjustments and transportation allowances, resulting in effective average prices and royalty rates. Prices are valued at the lease rather than at the market center, and differ from those used to compute the asset estimated present values, which are forecasted and discounted based upon OMB economic assumptions. For further details on federal oil and gas resources, refer to the financial statements of DOI. In addition to the oil and gas resources discussed above, the federal government also owns oil and gas resources that are not currently under lease.

[17] Gulf of Mexico proved reserves are royalty bearing volumes. In the Gulf of Mexico, an additional 860.6 million Bbl for fiscal year 2018 and 689.7 million Bbl for fiscal year 2017 of proved oil reserves, and 739.9 million Mcf for fiscal year 2018 and 1,180.3 million Mcf for fiscal year 2017 of proved gas reserves are not reflected in these totals as they are estimated to be producible royalty free under various royalty relief provisions. The net present value of the royalty value of the royalty free proved reserves volumes in the Gulf of Mexico is estimated to be $5.4 billion for fiscal year 2018 and $4.4 billion for fiscal year 2017.

Federal Natural Resources Other than Oil and Gas

Federal Natural Resources Other than Oil and Gas as of September 30, 2018, and 2017

(in billions of dollars)

Natural Resource Category	2018	2017
Coal royalties	8.8	9.0
Total	8.8	9.0

The Office of Natural Resources Revenue (ONRR) within DOI is responsible for the management and collection of revenues associated with federal coal leases which are managed by the Bureau of Land Management (BLM) within DOI. The ONRR achieves optimal value by ensuring that all natural resource revenues are efficiently and accurately collected as well as disbursed to recipients in a timely manner by performing audit and revenue compliance activities.

The Mineral Leasing Act of 1920, as amended, and the *Mineral Leasing Act for Acquired Lands of 1947*, as amended, gives DOI the responsibility for coal leasing on approximately 700 million acres of federal mineral estate which includes 570 million of acres where coal development is allowed. The surface estate of these lands may be under the control of BLM, the U.S. Forest Service (within USDA), private or state land owners, or other federal entities.

Public lands are available for coal leasing after the lands have been evaluated through a multiple-use planning process. *The Mineral Leasing Act,* as amended by the *Federal Coal Leasing Amendments Act of 1976*, generally requires that coal be leased competitively and that the federal government must receive a fair market value for land leased for coal development. Once a lease is issued, federal coal leasing laws and lease terms determine the federal government's share of production from coal leasing operations.

DOI receives coal leasing revenues from a bonus paid at the time of the lease, an annual rent payment of $3.00 per acre, and royalties paid on the value of the coal after it has been mined. A portion of the total federal coal royalties will be distributed to other non-federal entities. The royalty rate for surface-mining methods is 12.5 percent and is 8.0 percent for underground mining, and the BLM can approve reduced royalty rates based on maximum economic recovery. Regulations that govern BLM's coal leasing program are contained in Title 43, Groups 3000 and 3400 of the Code of Federal Regulations.

The above table presents the estimated present value of federal coal royalties under lease contract or other long-term arrangements as of September 30, 2018 and 2017. The federal government's estimated coal royalties have as their basis the DOI's BLM estimates of recoverable reserves. The federal recoverable reserves are then further adjusted to correspond with the effective date of the analysis and then are projected over time to simulate a schedule of when the reserves would be produced. Future royalties are then calculated by applying future price estimates and effective royalty rates, adjusted for transportation allowances and other allowable deductions. The present value of these royalties are then determined by discounting the revenue stream back to the effective date at a public discount rate assumed to be equal to the OMB's estimates of future 30-year Treasury bill rates. The 30-year rate was chosen because this maturity life most closely approximates the productive lives of the recoverable reserves estimates.

In addition to the coal resources discussed above, the federal government has other natural resources under lease contract whereby the lessee is required to pay royalties on the sale of the natural resource. These natural resources include soda ash, potash muriates of potash and langbeinite phosphate, lead concentrate, copper concentrate, and zinc concentrate. Soda ash and potash have the largest estimated present value of future royalties. The federal government also owns coal resources and certain other natural resources that are not currently under lease. For further details on federal natural resources-other than oil and gas, refer to the financial statements of DOI.

United States Government Other Information (Unaudited) for the Years Ended September 30, 2018, and 2017

Tax Burden

The Internal Revenue Code provides for progressive tax rates, whereby higher earned income is generally subject to higher tax rates. The following tables present the latest available information on income tax and related income, deductions, and credit: for individuals by income level, and for corporations by size of assets.

Individual Income Tax Liability for Tax Year 2016

Adjusted Gross Income (AGI)	Number of Taxable Returns (In thousands)	AGI (in millions of dollars)	Total Income Tax (in millions of dollars)	Average AGI Per Return (in whole dollars)	Average Income Tax per Return (in whole dollars)	Income Tax as a Percentage of AGI
Under $15,000	34,916	55,654	1,903	1,594	55	3.4%
$15,000 under $30,000	29,646	655,110	18,587	22,098	627	2.8%
$30,000 under $50,000	26,753	1,047,405	58,168	39,151	2,174	5.6%
$50,000 under $100,000	33,199	2,367,475	209,856	71,312	6,321	8.9%
$100,000 under $200,000	18,858	2,552,481	321,564	135,353	17,052	12.6%
$200,000 under $500,000	5,583	1,588,349	308,249	284,497	55,212	19.4%
$500,000 or more	1,318	1,959,465	527,721	1,486,696	400,395	26.9%
Total	150,273	10,225,939	1,446,048			

Corporate Income Tax Liability for Tax Year 2015

Total Assets (In thousands of dollars)	Income Subject to Tax (in millions of dollars)	Total Income Tax After Credits (in millions of dollars)	Percentage of Income Tax After Credits to Taxable Income
Zero Assets	21,291	6,627	31.1%
$1 under $500	8,606	1,619	18.8%
$500 under $1,000	3,942	974	24.7%
$1,000 under $5,000	13,667	4,273	31.3%
$5,000 under $10,000	8,581	2,793	32.5%
$10,000 under $25,000	13,120	4,306	32.8%
$25,000 under $50,000	12,890	4,210	32.7%
$50,000 under $100,000	15,296	4,948	32.3%
$100,000 under $250,000	25,377	8,017	31.6%
$250,000 under $500,000	27,404	8,477	30.9%
$500,000 under $2,500,000	110,454	32,281	29.2%
$2,500,000 or more	1,114,453	251,097	22.5%
Total	1,375,081	329,622	

Tax Gap

The tax gap is the difference between what taxpayers should pay and what they actually pay on time. The most recent estimate of the annual gross tax gap, based on a study released in 2016, is about $458.0 billion for the Tax Year 2008-2010 timeframe. This amount represents the amount of noncompliance with tax laws. This study also estimated that $52.0 billion of the gross tax gap would eventually be collected, resulting in a net tax gap of $406.0 billion. The IRS remains committed to finding ways to increase compliance and reduce the tax gap, while minimizing the burden on the vast majority of taxpayers who pay their taxes accurately and on time.

The tax gap is the aggregate amount of tax (excluding interest and penalties) that is imposed by the tax laws for any given tax year but is not paid voluntarily and timely. The tax gap arises from three types of noncompliance: not filing required tax returns on time or at all (the nonfiling gap), underreporting the correct amount of tax on timely filed returns (the underreporting gap), and not paying on time the full amount reported on timely filed returns (the underpayment gap). Underreporting of income tax, employment taxes, and other taxes represents 84.5 percent of the gross tax gap. Each instance of noncompliance by a taxpayer contributes to the tax gap, whether or not the IRS detects it, and whether or not the taxpayer is even aware of the noncompliance. Some of the tax gap arises from intentional (willful) noncompliance, and some of it arises from unintentional mistakes.

The collection gap is the cumulative amount of assessed tax, penalties, and interest that has been assessed over many years, but has not been paid by a certain point in time and which the IRS expects to remain uncollectible. In essence, it represents the difference between the total balance of unpaid assessments and the net taxes receivable reported on IRS's balance sheet. The tax gap and the collection gap are related and overlapping concepts, but they have significant differences. The collection gap is a cumulative balance sheet concept for a particular point in time, while the tax gap is like an income statement item for a single year. Moreover, the tax gap estimates include all noncompliance, while the collection gap includes only amounts that have been assessed (a small portion of all non-compliance).

Tax Expenditures

As discussed in greater detail in Note 17—Collections and Refunds of Federal Revenue, tax and other revenues reported reflect the effects of tax expenditures, which are special exclusions, exemptions, or deductions or which provide tax credits, preferential tax rates or deferrals of tax liability, that allow individuals and businesses to reduce taxes they may otherwise owe.

The figures reported in the following table are estimates of tax expenditures using data from previous years and economic forecast from the fiscal year 2018 Midsession Review. The largest tax expenditures in fiscal year 2018 are the following (and see the table below):

- The exclusion from workers' taxable income of employers' contributions for health care, health insurance premiums, and premiums for long-term care insurance;
- The exclusion of contributions to and the earnings of employer defined benefit and defined contribution pension funds (minus pension benefits that are included in taxable income);
- Preferential tax rates on long-term capital gains;
- Imputed rental income forms part of the total value of goods and services produced in a country. But unlike returns from other investments, the return on homeownership "imputed rent" is excluded from taxable income. In contrast, landlords must count as income the rent they receive, and renters may not deduct the rent they pay. A homeowner is effectively both landlord and renter, but the tax code treats homeowners the same as renters while ignoring their simultaneous role as their own landlords and exempting potential rent they would have paid themselves; and
- Accelerated depreciation of machinery and equipment.

Largest Income Tax Expenditures

(In billions of dollars)	2018
Exclusion of employer contributions for medical insurance premiums & health care	205.1
Defined benefit & defined contribution pension funds	142.2
Preferential tax rates on long-term capital gains	118.6
Exclusion of net imputed rental income	116.6
Accelerated depreciation of machinery and equipment	67.8

Generally, identifying and measuring a tax expenditure requires defining a baseline tax system against which identified tax provisions are exceptions. The tax expenditures prepared for the *Budget* are estimated relative to a simplified comprehensive income tax, which defines income as the sum of consumption and the change in net wealth in a given period of time. Tax expenditure estimates do not necessarily equal the increase in federal revenues (or the change in the budget balance) that would result from repealing these special provisions, for the following reasons:

- Eliminating a tax expenditure may have incentive effects that alter economic behavior, which can affect the resulting magnitudes of the activity or of other tax provisions or government programs. For example, if capital gains were taxed at ordinary rates, capital gain realizations would be expected to decline, resulting in lower tax receipts. Such behavioral effects are not reflected in the estimates.
- Tax expenditures are interdependent even without incentive effects. Repeal of a tax expenditure provision can increase or decrease the tax revenue effect of other provisions. For example, even if behavior does not change, repeal of an itemized deduction could increase revenue costs from other deductions as some taxpayers move into higher tax brackets. Alternatively, an itemized deduction repeal could lower the revenue foregone from other deductions if taxpayers choose to claim the standard deduction over itemizing. Similarly, if two provisions were repealed simultaneously, the tax liability increase could be greater or less than the sum of the two separate tax expenditures, because each is estimated assuming that the other remains in force.
- Repeal effects may depend on concurrent tax rate changes. Lowering or raising tax rates can decrease or increase the estimated revenues from a particular provision. A $10,000 charitable contributions deduction is worth $3,500 in corporate tax revenues at a 35 percent tax rate, but only $2,100 at a 21 percent tax rate.

The President's fiscal year 2006 *Budget* provided a presentation of the Department of the Treasury's review of the tax expenditure budget. It focused on potential alternative baselines to a comprehensive income tax, including using a consumption tax, and defining negative tax expenditures (provisions that cause taxpayers to pay too much tax). Relative to a consumption tax baseline, a number of current tax provisions would be negative tax expenditures. More specifically, a consumption tax will not extend to saving or capital income. As an example, the exclusion for contributions to and earnings from retirement accounts would not be treated as a tax expenditure. Some of these also may not necessarily be negative tax expenditures under a comprehensive income tax as a baseline; the current reference law and normal law baselines represent a simplified version of comprehensive income. As an example, some medical expenditures may not be discretionary and perhaps should be excluded from income.

A more comprehensive ranking, including rankings over a 10 year period, and descriptions of tax expenditures can be found at the following location from the Treasury's Office of Tax Policy https://home.treasury.gov/policy-issues/tax-policy/tax-expenditures.

Unmatched Transactions and Balances

(in millions of dollars)	Fiscal Year 2018	Restated Fiscal Year 2017
Change in intragovernmental unmatched balances:		
Debt/investment	-	(4,145.3)
Benefit program contributions payable/receivable	0.5	10.6
Accounts payable/receivable	58.6	(574.9)
Advances from/to others & deferred credits/prepayments	(406.8)	61.2
Transfers payable/receivable	-	(50.2)
Other assets/liabilities	-	(61.0)
Fund balance with Treasury	640.1	399.0
	292.4	(4,360.6)
Unmatched intragovernmental transactions:		
Borrowings interest revenue/expense-exchange	62.0	-
Non-expenditure transfers-in/out	(475.1)	(438.4)
Expenditure transfers-in/out	605.3	688.2
Transfers-in/out without reimbursement	7.1	(89.5)
Benefit program revenue/cost	339.7	(896.3)
Non-reciprocating	4,884.5	8,914.8
Revenue and other financing sources	-	297.4
Other non-budgetary financing sources for debt accruals/amortization	-	61.0
Appropriations expended	(92.7)	342.4
Appropriations used	92.7	(342.4)
Appropriations received/warrants issued	154.3	(390.1)
Custodial and non-entity collections transferred out/in	(6,450.7)	(6,865.6)
Other	2,959.2	501.4
	2,086.3	1,782.9
Unmatched transactions and balances, net	2,378.7	(2,577.7)

( ) Parentheses indicate a decrease to Net Position.

The Statement of Operations and Changes in Net Position includes an amount for unmatched transactions and balances that result from the consolidation of federal reporting entities. Transactions between federal entities must be eliminated in consolidation to calculate the financial position of the government. Many of the amounts included in the table represent intragovernmental activity and balances that differed between federal entity trading partners and often totaled significantly more in the absolute than the net amounts shown. The table also reflects other consolidating adjustments and other adjustments that contributed to the unmatched transactions and balances amount. In fiscal year 2017, a number of lines in the unmatched transactions and balances table were adjusted to zero after intragovernmental difference analysis determined they were immaterial at or below $0.1 billion. The adjustments were added to, or subtracted from, gross cost in the Statement of Net Cost.

Unmatched transactions and balances between federal entities impact not only in the period in which differences originate but also in the periods where differences are resolved. As a result, it would not be proper to conclude that increases or decreases in the unmatched amounts shown in the “Unmatched Transactions and Balances” table reflect improvements or deteriorations in the government’s ability to resolve intragovernmental transactions. The federal community considers the identification and accurate reporting of intragovernmental activity a priority.

United States Government Required Supplementary Stewardship Information (Unaudited) for the Years Ended September 30, 2018, and 2017

Stewardship Investments

Stewardship investments focus on government programs aimed at providing long-term benefits by improving the nation's productivity and enhancing economic growth. These investments can be provided through direct federal spending or grants to state and local governments for certain education and training programs, R&D, and federally financed but not federally owned property, such as bridges and roads. When incurred, these investments are included as expenses in determining the net cost of operations. Stewardship investments for the current year and for the immediately preceding four years are shown in the table below.

Stewardship Investments for the Years Ended September 30, 2014, through 2018

(In billions of dollars)	2018	2017	2016	2015	2014
Investments in non-federal physical property	66.3	65.0	65.1	64.8	65.6
Investments in human capital	107.7	111.6	131.1	97.8	108.5
Research and development:					
Investments in basic research	40.1	36.5	35.5	29.4	34.0
Investments in applied research	38.2	32.7	32.5	28.8	28.1
Investments in development	75.0	68.2	64.9	63.3	61.8
Total investments	327.3	314.0	329.1	284.1	298.0

Non-Federal Physical Property

The government makes grants and provides funds for the purchase, construction, and/or major renovation of state and local government physical properties. Costs for non-federal physical property programs are included as expenses in the Statements of Net Cost and are reported as investments in the table. They are measured on the same accrual basis of accounting used in the *Financial Report*. DOT, HUD, EPA, and DOD had $57.9 billion (87.3 percent), $3.4 billion (5.1 percent), $2.9 billion (4.4 percent), and $1.2 billion (1.8 percent), respectively, of the total non-federal physical property investments in fiscal year 2018. Within DOT, the FHWA invested $42.8 billion during fiscal year 2018, primarily via reimbursement from the Highway Trust Fund, for states' construction costs on projects related to the federal highway system. The main programs in which the states participate are the National Highway System, Interstate Systems, Surface Transportation, and Congestion Mitigation/Air Quality Improvement programs. The states' contribution is 10 percent for the Interstate System and 20 percent for most other programs.

Human Capital

The government runs several programs that invest in human capital. Those investments go toward increasing and maintaining a healthy economy by educating and training the general public. Costs do not include training expenses for federal workers.

Education, VA, DOL, and HHS had $78.4 billion (72.8 percent), $17.0 billion (15.8 percent), $6.1 billion (5.7 percent), and $2.1 billion (1.9 percent), respectively, of the total human capital investments in fiscal year 2018. Historically, the changes in Education's annual human capital investments have been primarily attributable to fluctuations in the loan program subsidy estimate and loan modification costs.

Education administers a wide variety of programs related to general public education and training programs that are intended to increase or maintain national economic productive capacity. The Office of Federal Student Aid administers need-based financial assistance programs for students pursuing postsecondary education and makes available federal grants, direct loans, and work-study funding to eligible undergraduate and graduate students.

The significant human capital programs administered by VA include veterans rehabilitation and employment programs which are provided to service disabled veterans; they are designated to improve employability and promote independence for the disabled. They also include education and training programs intended to provide higher education to dependents that might not be able to participate otherwise.

The significant human capital programs administered by DOL relate to grants for job training and employment programs. Investments in human capital administered by HHS primarily relate to National Institutes of Health (NIH) research training and career development programs and Health Resources and Services Administration Health Workforce programs.

Research and Development

Federal investments in R&D comprise those expenses for basic research, applied research, and development that are intended to increase or maintain national economic productive capacity or yield other future benefits.

- Investments in basic research are for systematic studies to gain knowledge or understanding of the fundamental aspects of phenomena and of observable facts without specific applications toward processes or products in mind.
- Investments in applied research are for systematic studies to gain knowledge or understanding necessary for determining the means by which a recognized and specific need may be met.
- Investments in development are the systematic use of the knowledge and understanding gained from research for the production of useful materials, devices, systems, or methods, including the design and development of prototypes and processes.

With regard to basic research, HHS, NASA, DOE, and DOD had $18.7 billion (46.6 percent), $5.5 billion (13.6 percent), $5.1 billion (12.7 percent), and $2.3 billion (5.8 percent), respectively, of the total basic research investments in fiscal year 2018. Further, HHS, DOD, DOE, and NASA had $17.5 billion (45.8 percent), $6.4 billion (16.7 percent), $5.9 billion (15.4 percent), and $2.5 billion (6.5 percent), respectively, of the total applied research investments in fiscal year 2018. The DOD and NASA had $67.0 billion (89.3 percent) and $4.5 billion (6.0 percent), respectively, of total development investments in fiscal year 2018.

Within HHS, NIH-supported research focuses on spurring advances in discovery along the biomedical research continuum, spanning basic, translational, and clinical research. NIH researchers undertake a wide array of research activities in pursuit of the NIH mission, including studying biology in heath and disease states, undertaking observational and population-based research approaches, assessing new treatments or comparing different treatment approaches to provide new options for patients, and supporting a variety of health services research activities to inform medical practice. NIH regards the expeditious transfer of the results of its medical research for further development and commercialization of products an immediate benefit to improved health and an important mandate.

NASA R&D programs include activities to extend the knowledge of Earth, its space environment, and the universe, and to invest in new aeronautics and advanced space transportation technologies that support the development and application of technologies critical to the economic, scientific, and technical competitiveness of the U.S.

DOE R&D programs facilitate the creation, advancement, and deployment of new technologies and support the Department's mission to ensure America's security and prosperity by addressing its energy, environmental, and nuclear challenges through transformative science and technology solutions.

Major outputs of DOD R&D are scientific studies, investigations, research papers, hardware components, software codes, or limited construction of a weapon system component, to include non-system-specific development efforts. Development takes what has been discovered or learned from basic research and uses it to establish technological feasibility, assessment of operability, and production capability. Development is comprised of five stages: 1) advanced technology development, 2) advanced component development and prototypes, 3) system development and demonstration, 4) research, development, test and evaluation management support, and 5) operational systems development.

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Appendix A: Reporting Entity

This appendix lists the entities (consolidation or disclosure entities) included in the U.S. government's *Financial Report*, as well as related parties. SFFAS No. 47, *Reporting Entity*, provides guidance for identifying entities that are consolidation entities, disclosure entities, and related parties.

The *Financial Report* includes all organizations meeting the inclusion principles of (a) budgeted for by elected officials of the government, (b) owned by the government, and (c) controlled by the government with risk of loss or expectation of benefits. In addition, the *Financial Report* includes organizations where it would be misleading to exclude even though the organization does not meet any of the three inclusion principles. If an organization meets the inclusion principles, a determination of consolidation or disclosure is made.

SFFAS No. 47 identifies consolidation entities as organizations that should be consolidated in the financial statements based on the assessment of the following characteristics as a whole, the organization: (a) is financed through taxes and other non-exchange revenues, (b) is governed by the Congress or the President, (c) imposes or may impose risks and rewards to the government, and (d) provides goods and services on a non-market basis. It also includes organizations that would result in misleading or incomplete financial statements, if excluded.

The federal government has relationships with organizations that meet the inclusion criteria in SFFAS No. 47, but are afforded a greater degree of autonomy than consolidation entities. These entities are referred to as disclosure entities. Disclosure entities may maintain a separate legal identity, have a governance structure that vests most decision-making authorities in a governing body to insulate the organization from political influence, and/or have relative financial independence. Other organizations that are owned or controlled by the government as a result of regulatory actions, or other government intervention actions are, generally, deemed to be disclosure entities if the relationship with the government is not expected to be permanent.

Related parties exist if the existing relationship, or one party to the existing relationship, has the ability to exercise significant influence over the other party's policy decisions. Related parties do not meet the principles for inclusion, but are reported in the *Financial Report*, if they maintain relationships of such significance that it would be misleading to exclude.

1. Consolidation Entities included in the Financial Report:

There are a total of 159 entities that meet the consolidation criteria, and as such are included in the *Financial Report*. The lists below describe three groups of consolidation entities that comprise the consolidated governmentwide reporting entity for the *Financial Report* and include entities from all three branches of government.

Twenty-Four Chief Financial Officer Act Consolidation Entities

Department of Agriculture
www.usda.gov
Department of Commerce
www.doc.gov
Department of Defense
www.defense.gov
Department of Education
www.ed.gov
Department of Energy
www.energy.gov
Department of Health and Human Services
www.hhs.gov
Department of Homeland Security
www.dhs.gov
Department of Housing and Urban Development
www.hud.gov
Department of the Interior
www.doi.gov
Department of Justice
www.usdoj.gov
Department of Labor
www.dol.gov
Department of State
www.state.gov
Department of Transportation
www.dot.gov
Department of the Treasury
www.treasury.gov
Department of Veterans Affairs
www.va.gov
Environmental Protection Agency
www.epa.gov
General Services Administration
www.gsa.gov
National Aeronautics and Space Administration
www.nasa.gov
National Science Foundation
www.nsf.gov
Office of Personnel Management
www.opm.gov

Small Business Administration
www.sba.gov
Social Security Administration
www.ssa.gov
U.S. Agency for International Development
www.usaid.gov
U.S. Nuclear Regulatory Commission
www.nrc.gov

Sixteen Additional Significant Consolidation Entities

Export-Import Bank of the U.S.
www.exim.gov
Farm Credit System Insurance Corporation
www.fcsic.gov
Federal Communications Commission
www.fcc.gov
Federal Deposit Insurance Corporation
www.fdic.gov
General Fund of the U.S. Government
www.fiscal.treasury.gov
Millennium Challenge Corporation
www.mcc.gov
National Credit Union Administration
www.ncua.gov
National Railroad Retirement Investment Trust
www.rrb.gov
Overseas Private Investment Corporation
www.opic.gov
Pension Benefit Guaranty Corporation
www.pbgc.gov
Railroad Retirement Board
www.rrb.gov
Securities and Exchange Commission
www.sec.gov
Security Assistance Accounts
www.dsca.mil
Smithsonian Institution
www.si.edu
Tennessee Valley Authority
www.tva.gov
U.S. Postal Service
www.usps.com

One Hundred Nineteen Additional Consolidation Entities

Access Board
Administrative Conference of the U.S.
Advisory Council on Historic Preservation
African Development Foundation
American Battle Monuments Commission
Appalachian Regional Commission
Architect of the Capitol
Armed Forces Retirement Home
Barry Goldwater Scholarship and Excellence in Education Foundation
Broadcasting Board of Governors
Bureau of Consumer Financial Protection
Central Intelligence Agency
Chemical Safety and Hazard Investigation Board
Christopher Columbus Fellowship Foundation
Commission for the Preservation of America's Heritage Abroad
Commission on Civil Rights
Commission of Fine Arts
Commission on International Religious Freedom
Commission on Security and Cooperation in Europe
Commission to Eliminate Child Abuse and Neglect Fatalities*
Committee for Purchase from People Who Are Blind or Severely Disabled
Commodity Futures Trading Commission
Congressional Budget Office
Congressional-Executive Commission on the People's Republic of China
Consumer Product Safety Commission
Corporation for National and Community Service
Council of the Inspector General on Integrity and Efficiency
Court of Appeals for Veterans Claims
Court Services and Offender Supervision Agency for DC
DC Courts
DC Courts–Defender Services
Defense Nuclear Facilities Safety Board
Delta Regional Authority
Denali Commission
Dwight D. Eisenhower Memorial Commission
Election Assistance Commission
Environmental Dispute Resolution Fund
Equal Employment Opportunity Commission
Executive Office of the President
Farm Credit Administration
Federal Election Commission
Federal Financial Institutions Examination Council Appraisal Subcommittee
Federal Housing Finance Agency
Federal Labor Relations Authority
Federal Maritime Commission
Federal Mediation and Conciliation Service
Federal Mine Safety and Health Review Commission

Federal Trade Commission
Government Accountability Office
Government Publishing Office
Gulf Coast Ecosystem Restoration Council
Harry S. Truman Scholarship Foundation
House of Representatives
Indian Law and Order Commission*
Institute of Museum and Library Services
Intelligence Community Management Account
Inter-American Foundation
International Trade Commission
James Madison Memorial Fellowship Foundation
Japan-U.S. Friendship Commission
John C. Stennis Center for Public Service Training and Development
John F. Kennedy Center for the Performing Arts
Judiciary
Library of Congress
Marine Mammal Commission
Medicaid and Children's Health Insurance Program Payment and Access Commission
Medicare Payment Advisory Commission
Merit Systems Protection Board
Military Compensation and Retirement Modernization Commission*
Morris K. Udall and Stewart L. Udall Foundation
National Archives and Records Administration
National Capital Planning Commission
National Commission on Military, National and Public Service
National Council on Disability
National Endowment for the Arts
National Endowment for the Humanities
National Gallery of Art
National Labor Relations Board
National Mediation Board
National Railroad Passenger Corporation, Office of the Inspector General
National Transportation Safety Board
Neighborhood Reinvestment Corporation
Northern Border Regional Commission
Nuclear Waste Technical Review Board
Occupational Safety and Health Review Commission
Office of Compliance
Office of Government Ethics
Office of Navajo and Hopi Indian Relocation
Office of Nuclear Waste Negotiator*
Office of Special Counsel
Office of the Federal Coordination for Alaska Natural Gas Transportation Projects*
Open World Leadership Center
Patient Centered Outcomes Research Trust Fund
Peace Corps
Presidio Trust
Privacy and Civil Liberties Oversight Board
Public Building Reform Board
Public Defender Service
Recovery Act Accountability and Transparency Board*
Selective Service System
Senate Preservation Fund
St. Lawrence Seaway Development Corporation
State Justice Institute
Surface Transportation Board
Thrift Savings Fund
U.S. Capitol Police
U.S. Capitol Preservation Commission
U.S. China Economic and Security Review Commission
U.S. Holocaust Memorial Museum
U.S. Institute of Peace
U.S. Interagency Council on the Homeless
U.S. Senate
U.S. Supreme Court
U.S. Tax Court
U.S. Trade and Development Agency
Vietnam Education Foundation
Women's Suffrage Centennial Commission
Woodrow Wilson International Center for Scholars
WWI Centennial Commission

*These entities are no longer active and have either returned all remaining fund balances to Treasury during fiscal year 2018 or have remaining fund balances pending final return to Treasury as of September 30, 2018.

2. Disclosure Entities and Related Parties of the Financial Report

The entities included below, after considering various factors including quantitative and qualitative materiality, meet the criteria of SFFAS No. 47 to be reported as disclosure entities or related parties in the *Financial Report*. Information about the government's relationship with these entities is disclosed in Note 25—Disclosure Entities and Related Parties. The component entity of each disclosure entity is provided in the brackets below. Additionally, component entities have also identified additional disclosure entities and related parties that do not meet the qualitative or quantitative criteria in SFFAS No. 47 to be reported in the *Financial Report*. Refer to the financial reports of the component entities for more information on these disclosure entities and related parties.

Disclosure Entities

Amtrak (National Railroad Passenger Service Corp) [DOT]
Federal Home Loan Mortgage Corp (Freddie Mac) [Treasury]/[FHFA]
Federal National Mortgage Association (Fannie Mae) [Treasury]/[FHFA]
Federal Reserve System [Treasury]

There are additional disclosure entities within the government that can be found on the component entities financial statements.

Related Parties

Federal Home Loan Banks [FHFA]
International Monetary Fund and Multilateral Development Banks [Treasury]
Private Export Funding Corporation [EXIM]

There are additional related parties within the government that can be found on the component entities financial statements.

Appendix B: Acronyms

This appendix lists the acronyms used in the MD&A, Financial Statements, Notes to the Financial Statements, RSI, RSSI, and Other Information sections of this *Financial Report*.

ACA	Affordable Care Act
AGI	Adjusted Gross Income
APM	Alternative Payment Models
ARRA	American Recovery and Reinvestment Act of 2009
ASC	Accounting Standards Codification
BAR	Budget and Accrual Reconciliation
BBA	Bipartisan Budget Act
Bbl	Barrel
BCA	Budget Control Act
BEA	Bureau of Economic Analysis
BLDTF	Black Lung Disability Trust Fund
BLM	Bureau of Land Management
Board	Federal Reserve Board of Governors
BRS	Blended Retirement System
Budget	Budget of the U.S. Government
CAP	Cross Agency Priority
CCIIO	Center for Consumer Information and Insurance Oversight
CERCLA	Comprehensive Environmental Response, Compensation, and Liability Act
CFO	Chief Financial Officers
CFO Act	Chief Financial Officers Act of 1990
CFOC	Chief Financial Officers Council
CHIP	Children’s Health Insurance Program
CMS	Centers for Medicare and Medicaid Services
COLA	Cost of Living Adjustments
CPI	Consumer Price Index
CPI-U	Consumer Price Index for All Urban Consumers
CPIM	Consumer Price Index–Medical
CPI-W	Consumer Price Index for Urban Wage Earners and Clerical Workers
CPP	Clean Power Plan
CSRDF	Civil Service Retirement and Disability Fund
CSRS	Civil Service Retirement System
DACA	Deferred Action for Childhood Arrivals
DATA Act	Digital Accountability and Transparency Act of 2014
DHS	Department of Homeland Security
DI	Disability Insurance
DIF	Deposit Insurance Fund
DOC	Department of Commerce
DOD	Department of Defense
DOE	Department of Energy

DOI	Department of the Interior
DOJ	Department of Justice
DOL	Department of Labor
DOT	Department of Transportation
DSL	Debt Subject to the Statutory Limit
Education	Department of Education
EIA	Energy Information Administration
ERM	Enterprise Risk Management
ESF	Exchange Stabilization Fund
EXIM Bank	Export-Import Bank of the U.S.
Fannie Mae	Federal National Mortgage Association
FASAB	Federal Accounting Standards Advisory Board
FASB	Financial Accounting Standards Board
FCRA	Federal Credit Reform Act of 1990
FCSIC	Farm Credit System Insurance Corporation
FDIC	Federal Deposit Insurance Corporation
FECA	Federal Employees' Compensation Act
FEGLI	Federal Employees' Group Life Insurance
FERS	Federal Employees' Retirement System
FFEL	Federal Family Education Loan
FFMIA	Federal Financial Management Improvement Act of 1996
FHA	Federal Housing Administration
FHFA	Federal Housing Finance Agency
FHLBanks	Federal Home Loan Banks
FHWA	Federal Highway Administration
FICA	Federal Insurance Contribution Act
Financial Report	Financial Report of the U.S. Government
FOMC	Federal Open Market Committee
FPMRA	Federal Property Management Reform Act of 2016
FRPC	Federal Real Property Council
FR System	Federal Reserve System
FRBNY	Federal Reserve Bank of New York
FRBs	Federal Reserve Banks
Freddie Mac	Federal Home Loan Mortgage Corporation
FRPP	Federal Real Property Profile
FRTIB	Federal Retirement Thrift Investment Board
FUA	Federal Unemployment Account
GAAP	U.S. Generally Accepted Accounting Principles
GAO	Government Accountability Office
GDP	Gross Domestic Product
General Fund	General Fund of the U.S. Government
GPFFR	General Purpose Federal Financial Reports
GSA	General Services Administration
GSE	Government-Sponsored Enterprises

HCERA	Health Care and Education Reconciliation Act
HERA	Housing and Economic Recovery Act of 2008
HHS	Department of Health and Human Services
HI	Hospital Insurance
HQM	High Quality Market
HUD	Department of Housing and Urban Development
IG	Inspector General
IMF	International Monetary Fund
IRS	Internal Revenue Service
JOLTS	Job Openings and Labor Turnover Survey
LOC	Library of Congress
LPR	Lawful Permanent Resident
MACRA	Medicare Access and CHIP Reauthorization Act
MDBs	Multilateral Development Banks
MERHCF	Medicare Eligible Retiree Health Care Fund
MOX	Mixed Oxide
MTFs	Military Treatment Facilities
MTS	Monthly Treasury Statement
NASA	National Aeronautics and Space Administration
NCHS	National Center for Health Statistics
NCUA	National Credit Union Administration
NCUSIF	National Credit Union Share Insurance Fund
NFIP	National Flood Insurance Program
NIH	National Institutes of Health
NRRIT	National Railroad Retirement Investment Trust
NSLI	National Service Life Insurance
NWPA	Nuclear Waste Policy Act of 1982
OASDI	Old-Age, Survivors, and Disability Insurance
OASI	Old-Age and Survivors Insurance
OMB	Office of Management and Budget
OM&S	Operating Materials and Supplies
ONRR	Office of Natural Resources Revenue
OPEB	Other Postemployment Benefits
OPM	Office of Personnel Management
ORB	Other Retirement Benefits
OTA	Office of Tax Analysis
P3s	Public-Private Partnerships
PAR	Performance and Accountability Reports
PAYGO	Pay As You Go
PBGC	Pension Benefit Guaranty Corporation
PCE	Personal Consumption Expenditure
PEFCO	Private Export Funding Corporation
PMA	President’s Management Agenda
PMAs	Power Marketing Administrations
PP&E	Property, Plant, and Equipment

PSRHB	Postal Service Retiree Health Benefits
PV	Present Value
R&D	Research and Development
RCRA	Resource Conservation and Recovery Act
RMO	Responsible Mine Operator
RRB	Railroad Retirement Board
RSI	Required Supplementary Information
RSSI	Required Supplementary Stewardship Information
RTF	Reduce the Footprint
SAA	Security Assistance Accounts
SAFRA	Student Aid and Fiscal Responsibility Act
SAM	System for Award Management
SBA	Small Business Administration
SCSIA	Statements of Changes in Social Insurance Amounts
SDRs	Special Drawing Rights
SDRCs	SDR Certificates
S-DVI	Service-Disabled Veterans Insurance
SECA	Self-Employment Contributions Act
SFFAC	Statement of Federal Financial Accounting Concept
SFFAS	Statement of Federal Financial Accounting Standards
SGLI	Service Members Group Life Insurance
SGR	Sustainable Growth Rate
SLTFP	Statements of Long-Term Fiscal Projections
SMI	Supplementary Medical Insurance
SNF	Spent Nuclear Fuel
SOMA	System Open Market Account
SOSI	Statements of Social Insurance
SPSPA	Senior Preferred Stock Purchase Agreements
SSA	Social Security Administration
SSEB	Social Security Equivalent Benefit
State	Department of State
TCJA	Tax Cuts and Jobs Act of 2018
TFL	TRICARE for Life
TIPS	Treasury Inflation-Protected Securities
TNC yield curve	Yield Curve for Treasury Nominal Coupon Issues
Treasury	Department of the Treasury
TRIP	Terrorism Risk Insurance Program
TSF	Thrift Savings Fund
TSP	Thrift Savings Plan
TVA	Tennessee Valley Authority
TVARS	Tennessee Valley Authority Retirement System
UI	Unemployment Insurance
U.S.C.	United States Code
USDA	U.S. Department of Agriculture

USPS	United States Postal Service
UTF	Unemployment Trust Fund
VA	Department of Veterans Affairs
VSLI	Veterans' Special Life Insurance

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GAO U.S. GOVERNMENT ACCOUNTABILITY OFFICE
441 G St. N.W.
Washington, DC 20548

Independent Auditor's Report

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

In our audits of the U.S. government's consolidated financial statements as of and for the fiscal years ended September 30, 2018, and 2017, we found the following:

- Certain material weaknesses[1] in internal control over financial reporting and other limitations on the scope of our work resulted in conditions that continued to prevent us from expressing an opinion on the accompanying accrual-based consolidated financial statements as of and for the fiscal years ended September 30, 2018, and 2017.[2]

- Significant uncertainties (discussed in Note 22 to the consolidated financial statements), primarily related to the achievement of projected reductions in Medicare cost growth, prevented us from expressing an opinion on the sustainability financial statements,[3] which consist of the 2018 and 2017 Statements of Long-Term Fiscal Projections;[4] the 2018, 2017, 2016, 2015, and 2014 Statements of Social Insurance;[5] and the 2018 and 2017 Statements of Changes in Social

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

[2]The accrual-based consolidated financial statements as of and for the fiscal years ended September 30, 2018, and 2017, consist of the (1) Statements of Net Cost, (2) Statements of Operations and Changes in Net Position, (3) Reconciliations of Net Operating Cost and Budget Deficit, (4) Statements of Changes in Cash Balance from Budget and Other Activities, and (5) Balance Sheets, including the related notes to these financial statements. Most revenues are recorded on a modified cash basis. We previously reported that certain material weaknesses and, for some years, other limitations on the scope of our work prevented us from expressing an opinion on the accrual-based consolidated financial statements of the U.S. government for fiscal years 1997 through 2017.

[3]The sustainability financial statements are based on projections of future receipts and spending, while the accrual-based consolidated financial statements are based on historical information, including the federal government's assets, liabilities, revenue, and net cost.

[4]The 2018 and 2017 Statements of Long-Term Fiscal Projections present, for all the activities of the federal government, the present value of projected receipts and non-interest spending under current policy without change, the relationship of these amounts to projected gross domestic product (GDP), and changes in the present value of projected receipts and non-interest spending from the prior year. These statements also present the fiscal gap, which is the combination of non-interest spending reductions and receipts increases necessary to hold debt held by the public as a share of GDP at the end of the projection period to its value at the beginning of the period. The valuation date for the Statements of Long-Term Fiscal Projections is September 30.

[5]Statements of Social Insurance are presented for the current year and each of the 4 preceding years as required by U.S. generally accepted accounting principles. For the Statements of Social Insurance, the valuation date is January 1 for the Social Security and Medicare programs, October 1 for the Railroad Retirement program (January 1 for 2014 and 2015), and September 30 for the Black Lung program.

Insurance Amounts. A material weakness in internal control also prevented us from expressing an opinion on the 2018 and 2017 Statements of Long-Term Fiscal Projections.

- Material weaknesses resulted in ineffective internal control over financial reporting for fiscal year 2018.
- Material weaknesses and other scope limitations, discussed above, limited tests of compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements for fiscal year 2018.

This audit report discusses the following in more detail.

- Our report on the accompanying consolidated financial statements, which includes (1) two emphasis of matters—equity investments in the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac) and long-term fiscal challenges; (2) required supplementary information (RSI),[6] required supplementary stewardship information (RSSI),[7] and other information[8] included with the consolidated financial statements in the *Fiscal Year 2018 Financial Report of the United States Government* (*2018 Financial Report*), and (3) information on Chief Financial Officers Act of 1990 (CFO Act) agency financial management systems.
- Our report on internal control over financial reporting.
- Our report on compliance with laws, regulations, contracts, and grant agreements.
- The Department of the Treasury's (Treasury) and the Office of Management and Budget's (OMB) comments on a draft of this audit report.

Appendix I discusses our audit objectives, scope, and methodology.

Report on the Consolidated Financial Statements

The Secretary of the Treasury, in coordination with the Director of OMB, is required to annually submit audited financial statements for the U.S. government to the President and Congress. GAO is required to audit these statements.[9] As noted above, the consolidated financial statements consist of the accrual-based consolidated financial statements as of and for the fiscal years ended September 30, 2018, and 2017, and the sustainability financial statements, consisting of the 2018 and 2017 Statements of Long-Term Fiscal Projections; the 2018, 2017, 2016, 2015, and 2014 Statements of

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[6]The RSI consists of Management's Discussion and Analysis and information in the Required Supplementary Information section of the *Fiscal Year 2018 Financial Report of the United States Government*.

[7]The RSSI consists of information on stewardship investments in the Required Supplementary Stewardship Information section of the *Fiscal Year 2018 Financial Report of the United States Government*.

[8]Other information consists of information in the *Fiscal Year 2018 Financial Report of the United States Government* other than the consolidated financial statements, RSI, RSSI, auditor's report, and Statement of the Comptroller General of the United States.

[9]The Government Management Reform Act of 1994 has required such reporting, covering the executive branch of government, beginning with financial statements prepared for fiscal year 1997. 31 U.S.C. § 331(e). The consolidated financial statements include the legislative and judicial branches.

Social Insurance; the 2018 and 2017 Statements of Changes in Social Insurance Amounts; and the related notes to the financial statements.

We performed sufficient audit work to provide this report on the consolidated financial statements. We considered the limitations on the scope of our work regarding the accrual-based consolidated financial statements and the sustainability financial statements in forming our conclusions. We performed our work in accordance with U.S. generally accepted government auditing standards.

Management's Responsibility

Management of the federal government is responsible for (1) the preparation and fair presentation of annual consolidated financial statements of the U.S. government in accordance with U.S. generally accepted accounting principles; (2) preparing, measuring, and presenting the RSI and RSSI in accordance with U.S. generally accepted accounting principles; (3) preparing and presenting other information included in documents containing the consolidated financial statements and auditor's report, and ensuring the consistency of that information with the consolidated financial statements, RSI, and RSSI; and (4) maintaining effective internal control over financial reporting, including the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these consolidated financial statements based on conducting the audit in accordance with U.S. generally accepted government auditing standards. We are also responsible for applying certain limited procedures to the RSI, RSSI, and other information included with the consolidated financial statements. Because of the matters discussed below, we were unable to obtain sufficient appropriate evidence to provide a basis for audit opinions on the consolidated financial statements.

Basis for Disclaimers of Opinion on the Consolidated Financial Statements

Accrual-Based Consolidated Financial Statements

The federal government is not able to demonstrate the reliability of significant portions of the accompanying accrual-based consolidated financial statements as of and for the fiscal years ended September 30, 2018, and 2017, principally because of limitations related to certain material weaknesses in internal control over financial reporting and other limitations affecting the reliability of these financial statements and the scope of our work as discussed below.[10] As a result of these limitations, readers are cautioned that amounts reported in the accrual-based consolidated financial statements and related notes may not be reliable.

The federal government did not maintain adequate systems or have sufficient appropriate evidence to support certain material information reported in the accompanying accrual-based consolidated financial statements. The underlying material weaknesses in internal control, which have existed for years, contributed to our disclaimer of opinion on the accrual-based consolidated financial statements. Specifically, these weaknesses concerned the federal government's inability to

[10]Such limitations include (1) the Department of Defense, the Department of Housing and Urban Development, and the Railroad Retirement Board each received a disclaimer of opinion on their respective fiscal year 2018 and 2017 financial statements and (2) for fiscal year 2018 and 2017, the financial information for Security Assistance Accounts and the General Fund of the U.S. Government was unaudited.

- satisfactorily determine that property, plant, and equipment, inventories and related property, and accounts receivable, primarily held by the Department of Defense (DOD), were properly reported in the accrual-based consolidated financial statements;

- reasonably estimate or adequately support amounts reported for certain liabilities, such as environmental and disposal liabilities, or determine whether commitments and contingencies were complete and properly reported;

- support significant portions of the reported total net cost of operations, most notably related to DOD, and adequately reconcile disbursement activity at certain federal entities;

- adequately account for intragovernmental activity and balances between federal entities;

- reasonably assure that the consolidated financial statements are (1) consistent with the underlying audited entities' financial statements, (2) properly balanced, and (3) in accordance with U.S. generally accepted accounting principles; and

- reasonably assure that the information in the (1) Reconciliations of Net Operating Cost and Budget Deficit and (2) Statements of Changes in Cash Balance from Budget and Other Activities is complete, properly supported, and consistent with the underlying information in the audited entities' financial statements and other financial data.

These material weaknesses continued to (1) hamper the federal government's ability to reliably report a significant portion of its assets, liabilities, costs, and other related information; (2) affect the federal government's ability to reliably measure the full cost, as well as the financial and nonfinancial performance, of certain programs and activities; (3) impair the federal government's ability to adequately safeguard significant assets and properly record various transactions; and (4) hinder the federal government from having reliable, useful, and timely financial information to operate effectively and efficiently. Because of these material weaknesses and other limitations on the scope of our work discussed below, additional issues may exist that were not identified and could affect the accrual-based consolidated financial statements. Appendix II describes these material weaknesses in more detail and highlights the primary effects of these material weaknesses on the accompanying accrual-based consolidated financial statements and on the management of federal government operations.

Sustainability Financial Statements

Significant uncertainties (discussed in Note 22 to the consolidated financial statements), which primarily relate to the achievement of projected reductions in Medicare cost growth, affect the sustainability financial statements. In addition, the material weakness related to the Reconciliations of Net Operating Cost and Budget Deficit and the Statements of Changes in Cash Balance from Budget and Other Activities, discussed above, hampers the federal government's ability to demonstrate the reliability of historical budget information used for certain key inputs to the 2018 and 2017 Statements of Long-Term Fiscal Projections. As a result of these significant uncertainties and this material weakness, readers are cautioned that amounts reported in the 2018 and 2017 Statements of Long-Term Fiscal Projections; the 2018, 2017, 2016, 2015, and 2014 Statements of Social Insurance; the 2018 and 2017 Statements of Changes in Social Insurance Amounts; and the related notes to these financial statements may not fairly present, in all material respects, the sustainability information for those years in accordance with U.S. generally accepted accounting principles.

These significant uncertainties primarily relate to the following.

- Medicare projections in the 2018 and 2017 Statements of Long-Term Fiscal Projections and the 2018, 2017, 2016, and 2015 Statements of Social Insurance were based on benefit formulas under current law and included a significant reduction in Medicare payment rate updates for productivity improvements for most categories of Medicare providers,[11] based on full implementation of the provisions of the Patient Protection and Affordable Care Act, as amended (ACA),[12] and physician payment updates specified by the Medicare Access and CHIP Reauthorization Act of 2015 (MACRA).[13]

- Management has noted that actual future costs for Medicare are likely to exceed those shown by the current law projections presented in the 2018, 2017, 2016, and 2015 Statements of Social Insurance because of, for example, the likelihood of modifications to the scheduled reductions in Medicare payment rate updates for productivity adjustments relating to most categories of Medicare providers and the specified physician payment updates. The extent to which actual future costs exceed the current law amounts because of changes to the scheduled reductions in Medicare payment rate updates for productivity adjustments and specified physician payment updates depends on both the specific changes that might be enacted and whether enacted legislation would include further provisions to help offset such costs. Consequently, there are significant uncertainties concerning the achievement of these projected reductions in Medicare payment rate updates.

- Management has developed an illustrative alternative projection intended to provide additional context regarding the long-term sustainability of the Medicare program and to illustrate the uncertainties in the Statement of Social Insurance projections. The present value of future estimated expenditures in excess of future estimated revenue for Medicare, included in the illustrative alternative projection in Note 22, exceeds the $37.6 trillion estimate in the 2018 Statement of Social Insurance by $9.8 trillion.

- Management noted that these significant uncertainties about projected reductions in health care cost growth also affect the projected Medicare and Medicaid costs reported in the 2018 and 2017 Statements of Long-Term Fiscal Projections.

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[11]Under the Patient Protection and Affordable Care Act's productivity adjustment provisions, productivity improvements are expected to result in lower overall Medicare spending because of smaller annual increases in the Medicare payment rates paid to many health care providers. This is often referred to as a reduction in Medicare payment rate updates. The health care provider categories affected include, but are not limited to, inpatient/outpatient hospital services, skilled nursing facilities, home health care, ambulance, ambulatory surgical centers, durable medical equipment, and prosthetics.

[12]ACA, Pub. L. No. 111-148, 124 Stat. 119 (Mar. 23, 2010), as amended by the Health Care and Education Reconciliation Act of 2010, Pub. L. No. 111-152, 124 Stat. 1029 (Mar. 30, 2010). In this report, references to the ACA include any amendments made by the Health Care and Education Reconciliation Act of 2010.

[13]MACRA, Pub. L. No. 114-10, title I, § 101, 129 Stat. 87, 89 (Apr. 16, 2015). MACRA included many provisions that affect Medicare, including the repeal of the sustainable growth rate formula for calculating annual updates to Medicare reimbursement payment rates to physicians and certain nonphysician medical providers, and established an alternative set of annual updates.

- The 2014 Statement of Social Insurance was affected by significant uncertainties, primarily related to the achievement of projected reductions in Medicare payment rate updates for productivity improvements. Specifically, the 2014 Statement of Social Insurance reflected a projected baseline that assumed that the physician payment rate reductions would not occur and that physician payment rates would annually increase at a rate equal to the average sustainable growth rate override that occurred over the 10-year period ending on March 31, 2015. For 2014, management noted that actual future costs for Medicare were likely to exceed those shown by the current law projections presented in the 2014 Statement of Social Insurance because of, for example, the likelihood of modifications to the scheduled reductions in Medicare payment rates for productivity adjustments.

Projections of Medicare costs are sensitive to assumptions about future policymaker decisions and about consumer, employer, and health care provider behavioral responses as policy, incentives, and the health care sector change over time. Such secondary effects are not fully reflected in the sustainability financial statements but could be expected to influence the excess cost growth rate used in the projections.[14] Key drivers of uncertainty about the excess cost growth rate include the future development and deployment of medical technology, the evolution of personal income, and the cost and availability of insurance, as well as federal policy changes, such as the implementation of the ACA. As discussed in the RSI section of the *2018 Financial Report*, the projections are very sensitive to changes in the health care cost growth assumption.

As discussed in Notes 22 and 23 to the financial statements, the sustainability financial statements are based on management's assumptions. These sustainability financial statements present the present value of the U.S. government's estimated future receipts and future spending using a projection period sufficient to illustrate long-term sustainability.[15] The sustainability financial statements are intended to aid users in assessing whether future resources will likely be sufficient to sustain public services and to meet obligations as they come due.

In preparing the sustainability financial statements, management selects assumptions and data that it believes provide a reasonable basis to illustrate whether current policy is sustainable. As discussed in the *2018 Financial Report*, current policy is based on current law but includes several adjustments. In the Statements of Long-Term Fiscal Projections, notable adjustments to current law include (1) projected spending, receipts, and borrowing levels assume raising or suspending the current statutory limit on federal debt; (2) continued discretionary appropriations are assumed throughout the projection period; (3) scheduled Social Security and Medicare Part A benefit payments are assumed to occur beyond the projected point of trust fund depletion; and (4) many mandatory programs with expiration dates prior to the end of the 75-year projection period are assumed to be reauthorized. In the Statements of Social Insurance, the one adjustment to current law is that scheduled Social Security and Medicare Part A benefit payments are assumed to occur beyond the projected point of trust fund depletion. Assumptions underlying such sustainability information do not consider changes in policy or all potential future events that could affect future income, expenditures, and hence sustainability. Also, the projections assume that debt could continuously rise without severe economic consequences. The RSI section of the *2018 Financial Report* includes unaudited information on how changes in various assumptions would affect the Statements of Long-Term Fiscal Projections and Statements of Social Insurance. The sustainability financial statements are not forecasts or predictions.

[14]The excess cost growth rate is the increase in health care spending per person relative to the growth of GDP per person after removing the effects of demographic changes on health care spending.

[15]The projection period used for the Social Security, Medicare, and Railroad Retirement social insurance programs is 75 years. Beginning in fiscal year 2017, the Black Lung program has a rolling 25-year projection period. For fiscal years 2014 through 2016, the Black Lung program projection period was through September 30, 2040.

As discussed in the unaudited RSI section of the *2018 Financial Report*, the Social Security and Medicare Hospital Insurance (Part A) trust funds are, based on the achievement of the cost growth reductions discussed above, projected to be depleted in 2034 and 2026, respectively, at which time they would be unable to pay the full amount of scheduled future benefits.[16] For Social Security, future revenues were projected to be sufficient to pay 79 percent of scheduled benefits in 2034, the year of projected trust funds (combined) depletion, and decreasing to 74 percent of scheduled benefits in 2092. For Medicare Hospital Insurance (Part A), future revenues were projected to be sufficient to pay 91 percent of scheduled benefits in 2026, the year of projected trust fund depletion, declining to 78 percent by 2042, and then gradually increasing to 85 percent of scheduled benefits in 2092.

Because of the large number of factors that affect the sustainability financial statements and the fact that future events and circumstances cannot be estimated with certainty, even if current policy is continued, there will be differences between the estimates in the sustainability financial statements and the actual results, and those differences may be material.

Other Limitations on the Scope of Our Work

For fiscal years 2018 and 2017, there were other limitations on the scope of our work, in addition to the material weaknesses and significant uncertainties noted above, that contributed to our disclaimers of opinion on the consolidated financial statements. Such limitations primarily relate to our ability to obtain adequate representations from management. Treasury and OMB depend on representations from certain federal entities to provide their representations to us regarding the U.S. government's consolidated financial statements. Treasury and OMB were unable to provide us with adequate representations regarding the U.S. government's accrual-based consolidated financial statements for fiscal years 2018 and 2017, primarily because certain federal entities provided them insufficient or no representations. In addition, the Department of Justice, on behalf of the federal government, was unable to provide us with adequate legal representations regarding the U.S. government's accrual-based consolidated financial statements for fiscal year 2018.

Disclaimers of Opinion on the Consolidated Financial Statements

Accrual-Based Consolidated Financial Statements

Because of the significance of the related matters described in the Basis for Disclaimers of Opinion on the Consolidated Financial Statements above, we were not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the accrual-based consolidated financial statements. Accordingly, we do not express an opinion on the accrual-based consolidated financial statements as of and for the fiscal years ended September 30, 2018, and 2017.

Sustainability Financial Statements

Because of the significance of the related matters described in the Basis for Disclaimers of Opinion on the Consolidated Financial Statements above, we were not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the Statements of Long-Term Fiscal Projections for 2018 and 2017; the Statements of Social Insurance for 2018, 2017, 2016, 2015, and 2014; and the

[16]The combined Social Security trust funds consist of the Federal Old-Age and Survivors Insurance trust fund and the Federal Disability Insurance trust fund. For the Federal Old-Age and Survivors Insurance trust fund, future revenues were projected to be sufficient to pay 77 percent of scheduled benefits in 2034, the year of projected trust fund depletion, decreasing to 73 percent in 2092. For the Federal Disability Insurance trust fund, future revenues were projected to be sufficient to pay 96 percent of scheduled benefits in 2032, the year of projected trust fund depletion, decreasing to 83 percent in 2092.

Statements of Changes in Social Insurance Amounts for 2018 and 2017. Accordingly, we do not express an opinion on these sustainability financial statements.

Emphasis of Matters

The following key items deserve emphasis in order to put the information in the consolidated financial statements and the Management's Discussion and Analysis section of the *2018 Financial Report* into context. However, our disclaimers of opinion noted above are not modified with respect to these matters.

Equity Investments in Fannie Mae and Freddie Mac

In 2008, during the financial crisis, the federal government placed Fannie Mae and Freddie Mac under conservatorship and entered into preferred stock purchase agreements with these government-sponsored enterprises (GSE) to help ensure their financial stability. The agreements with the GSEs could affect the federal government's financial position. As of September 30, 2018, the federal government reported about $113 billion of investments in the GSEs, which is net of about $91 billion in valuation losses.

In valuing these equity investments, management considered and selected assumptions and data that it believed provided a reasonable basis for the estimated values reported in the accrual-based consolidated financial statements. However, as discussed in Note 1 to the consolidated financial statements, there are many factors affecting these assumptions and estimates that are inherently subject to substantial uncertainty arising from the uniqueness of the transactions and the likelihood of future changes in general economic, regulatory, and market conditions. As such, there will be differences between the estimated values as of September 30, 2018, and the actual results, and such differences may be material. Also, as discussed in Note 1 to the consolidated financial statements, the assets, liabilities, and results of operations of Fannie Mae and Freddie Mac are not consolidated into the government's consolidated financial statements. Treasury and OMB have determined that these entities do not meet the criteria for consolidation.[17]

Long-Term Fiscal Challenges

The 2018 Statement of Long-Term Fiscal Projections and related information in Note 23 and in the unaudited RSI section of the *2018 Financial Report* show that absent policy changes, the federal government continues to face an unsustainable long-term fiscal path. For the 2018 projections, debt-to-gross domestic product (GDP) at the end of the 75-year projection period (530 percent) was higher than debt-to-GDP at the end of the 75-year projection period in the 2017 (297 percent) and 2016 (252 percent) projections. The budget deficit increased for the third consecutive year in fiscal year 2018 and is projected to continue to grow in almost all of the next 75 years. Over the long term, the imbalance between spending and revenue that is built into current policy and law is projected to lead to continued growth of the deficit and debt held by the public as a share of GDP. This situation—in which debt grows faster than GDP—means the current federal fiscal path is unsustainable.

Under the *2018 Financial Report* projections, spending for the major health and retirement programs will increase more rapidly than GDP in the coming decades, in part because of an aging population and projected continued increases in health care costs. These projections for Social Security and Medicare are based on the same assumptions underlying the information presented in the Statement of Social

[17]For additional information on the criteria used to determine which federal entities are included in the reporting entity for the consolidated financial statements, as well as the reasons for not including certain entities, such as Fannie Mae and Freddie Mac, see app. A of the *2018 Financial Report*.

Insurance and assume that the provisions enacted in the ACA designed to slow the growth of Medicare costs are sustained and remain effective throughout the projection period.[18] The projections also reflect the effects of MACRA, which, among other things, revised the methodology for determining physician payment rates. If, however, the Medicare cost containment measures and physician payment rate methodology are not sustained over the long term—concerns expressed by the Trustees of the Medicare trust funds, the Centers for Medicare & Medicaid Services' Chief Actuary, the Congressional Budget Office (CBO), and others—spending on federal health care programs will grow more rapidly than assumed in the projections. In addition, under the *2018 Financial Report* projections, spending on net interest (primarily interest on debt held by the public) is projected to grow such that over the long term it surpasses Social Security and becomes the largest category of spending in 2034. Net interest is projected to increase from 1.6 percent of GDP in fiscal year 2018 to 7.4 percent in fiscal year 2038 to 26.9 percent in fiscal year 2093.

GAO and CBO also prepare long-term federal fiscal simulations, using different sets of assumptions, which continue to show federal debt held by the public rising as a share of GDP in the long term.[19] GAO, CBO, and the *2018 Financial Report* all project that debt held by the public as a share of GDP will surpass its historical high (106 percent in 1946) within the next 13 to 20 years. Each of these long-term projections uses somewhat different assumptions, but their overall conclusions are the same: absent policy changes, the federal government's fiscal path is unsustainable.

At the end of fiscal year 2018, debt held by the public reached about 78 percent of GDP, far above the post–World War II (since 1946) average of 46 percent. Debt held by the public at these high levels could limit the federal government's flexibility to address emerging issues and unforeseen challenges, such as another economic downturn or large-scale disaster. These unforeseen events, also known as fiscal risks or fiscal exposures, place additional pressure on the federal budget. They result in responsibilities, programs, and activities that may legally commit or create expectations for future federal spending based on current policy, past practices, or other factors. A more complete understanding of them can help policymakers anticipate changes in future spending and can enhance oversight of federal resources.

Other Matters

Required Supplementary Information and Required Supplementary Stewardship Information

U.S. generally accepted accounting principles issued by the Federal Accounting Standards Advisory Board (FASAB) require that the RSI and RSSI be presented in the *2018 Financial Report* to supplement the financial statements. Although the RSI and RSSI are not a part of the financial statements, FASAB considers this information to be an essential part of financial reporting for placing the financial statements in appropriate operational, economic, or historical context. We were unable to apply certain limited procedures to the RSI and RSSI in accordance with U.S. generally accepted government auditing standards because of the material weaknesses and other scope limitations discussed in this audit report. We did not audit and do not express an opinion or provide any assurance on the RSI or RSSI.

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[18]ACA, Pub. L. No. 111-148, 124 Stat. 119 (Mar. 23, 2010), as amended by the Health Care and Education Reconciliation Act of 2010, Pub. L. No. 111-152, 124 Stat. 1029 (Mar. 30, 2010).

[19]For more information on GAO's simulations, see GAO, *America's Fiscal Future: Fiscal Forecast*, accessed on March 20, 2019, https://www.gao.gov/americas_fiscal_future?t=fiscal_forecast. For more information on CBO's simulations, see Congressional Budget Office, *The 2018 Long-Term Budget Outlook* (Washington, D.C.: June 26, 2018).

Other Information

Other information included in the *2018 Financial Report* contains a wide range of information, some of which is not directly related to the consolidated financial statements. This information is presented for purposes of additional analysis and is not a required part of the consolidated financial statements, RSI, or RSSI. We read the other information included with the consolidated financial statements in order to identify material inconsistencies, if any, with the consolidated financial statements. We did not audit and do not express an opinion or provide any assurance on the other information in the *2018 Financial Report*.

Readers are cautioned that the material weaknesses, significant uncertainties, and other scope limitations discussed in this audit report may affect the reliability of certain information contained in the RSI, RSSI, and other information that is taken from the same data sources as the accrual-based consolidated financial statements and the sustainability financial statements.

CFO Act Agency Financial Management Systems

The federal government's ability to efficiently and effectively manage and oversee its day-to-day operations and programs relies heavily on the ability of entity financial management systems to produce complete, reliable, timely, and consistent financial information for use by executive branch agencies and Congress.[20] The Federal Financial Management Improvement Act of 1996 (FFMIA) was designed to lead to system improvements that would result in CFO Act agency managers routinely having access to reliable, useful, and timely financial information with which to measure performance and increase accountability throughout the year.

The 24 CFO Act agencies are responsible for implementing and maintaining financial management systems that substantially comply with FFMIA requirements. FFMIA requires auditors, as part of the 24 CFO Act agencies' financial statement audits, to report whether those agencies' financial management systems substantially comply with (1) federal financial management systems requirements, (2) applicable federal accounting standards, and (3) the federal government's *U.S. Standard General Ledger* at the transaction level.

For fiscal year 2018, auditors of nine of the 24 CFO Act agencies reported that the agencies' financial management systems did not substantially comply with one or more of the three FFMIA requirements. For fiscal year 2017, auditors of 10 of the 24 CFO Act agencies reported that the agencies' financial management systems did not substantially comply with one or more of the three FFMIA requirements. Agency management at the 24 CFO Act agencies also annually report on FFMIA compliance. For fiscal year 2018, agency management of seven of the 24 CFO Act agencies reported that their agencies' financial management systems did not substantially comply with one or more of the three FFMIA requirements. For fiscal year 2017, agency management of eight of the 24 CFO Act agencies reported that their agencies' financial management systems did not substantially comply with one or more of the three FFMIA requirements. Based on agency financial reports, differences in the assessments of substantial compliance between the auditors and agency management reflect differences in management's and auditors' views regarding the effect of reported deficiencies on agencies' financial management systems.

[20]The Federal Financial Management Improvement Act of 1996, which is reprinted in 31 U.S.C. § 3512 note, defines "financial management systems" to include the financial systems and the financial portions of mixed systems necessary to support financial management, including automated and manual processes, procedures, controls, data, hardware, software, and support personnel dedicated to the operation and maintenance of system functions.

Long-standing financial management systems weaknesses at several large CFO Act agencies, along with the size and complexity of the federal government, continue to present a formidable management challenge in providing accountability and have contributed significantly to certain of the material weaknesses and other limitations discussed in this audit report.

Report on Internal Control over Financial Reporting

Management's Responsibility

Management of the federal government is responsible for (1) maintaining effective internal control over financial reporting, including the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error, and (2) evaluating the effectiveness of internal control over financial reporting, based on criteria established under the Federal Managers' Financial Integrity Act (FMFIA).[21]

Auditor's Responsibility

The purpose of an audit of financial statements is to express an opinion on the financial statements. An audit of financial statements includes considering internal control over financial reporting to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of internal control over financial reporting. We did not consider all internal controls relevant to operating objectives as broadly established under FMFIA, such as those controls relevant to preparing performance information and ensuring efficient operations.

Our responsibility is to report any material weaknesses or significant deficiencies in internal control over financial reporting for fiscal year 2018 that come to our attention as a result of our audit.[22] Based on the scope of our work and the effects of the other limitations on the scope of our audit noted throughout this audit report, our internal control work was not designed to, and would not necessarily, identify all deficiencies in internal control, including those that might be material weaknesses or significant deficiencies. Therefore, additional material weaknesses or significant deficiencies may exist that were not identified. We performed our work in accordance with U.S. generally accepted government auditing standards.

Definitions and Inherent Limitations of Internal Control over Financial Reporting

An entity's internal control over financial reporting is a process effected by those charged with governance, management, and other personnel, the objectives of which are to provide reasonable assurance that (1) transactions are properly recorded, processed, and summarized to permit the preparation of financial statements in accordance with U.S. generally accepted accounting principles, and assets are safeguarded against loss from unauthorized acquisition, use, or disposition, and (2) transactions are executed in accordance with provisions of applicable laws (including those governing the use of budget authority), regulations, contracts, and grant agreements, noncompliance with which could have a material effect on the financial statements.

[21] 31 U.S.C. § 3512 (c), (d) (commonly referred to as FMFIA). This act requires executive agency heads to evaluate and report annually to the President and Congress on the adequacy of their internal control and accounting systems and on actions to correct significant problems.

[22] A significant deficiency is a deficiency, or a combination of deficiencies, in internal control over financial reporting that is less severe than a material weakness yet important enough to merit attention by those charged with governance.

Because of its inherent limitations, internal control over financial reporting may not prevent, or detect and correct, misstatements due to fraud or error.

Material Weaknesses Resulted in Ineffective Internal Control over Financial Reporting

The material weaknesses discussed in this audit report resulted in ineffective internal control over financial reporting. Consequently, the federal government's internal control did not provide reasonable assurance that a material misstatement of the consolidated financial statements would be prevented, or detected and corrected, on a timely basis.

In addition to the material weaknesses that contributed to our disclaimers of opinion on the accrual-based consolidated financial statements and the sustainability financial statements, which were discussed previously, we found three other material weaknesses in internal control. These other material weaknesses were the federal government's inability to

- determine the full extent to which improper payments occur and reasonably assure that appropriate actions are taken to reduce them,
- identify and resolve information security control deficiencies and manage information security risks on an ongoing basis, and
- effectively implement internal controls over estimating the cost of credit programs and determining the value of loans receivable and loan guarantee liabilities.

These material weaknesses are discussed in more detail in appendix III, including the primary effects of the material weaknesses on the accrual-based consolidated financial statements and on the management of federal government operations.

We also found three significant deficiencies in the federal government's internal control related to implementing effective internal controls at certain federal entities for the following areas:

- taxes receivable,
- federal grants management, and
- Medicare social insurance information.

These significant deficiencies are discussed in more detail in appendix IV.

Further, individual federal entity financial statement audit reports identified additional control deficiencies that the entities' auditors reported as either material weaknesses or significant deficiencies at the individual entity level. We do not consider these additional deficiencies to represent material weaknesses or significant deficiencies with respect to the U.S. government's consolidated financial statements.

Intended Purpose of Report on Internal Control over Financial Reporting

The purpose of this report on internal control over financial reporting is solely to describe the scope of our consideration of internal control over financial reporting, and the results of our procedures, and not to provide an opinion on the effectiveness of internal control over financial reporting. This report on internal control over financial reporting is an integral part of an audit performed in accordance with U.S. generally accepted government auditing standards. Accordingly, this report on internal control over financial reporting is not suitable for any other purpose.

Report on Compliance with Laws, Regulations, Contracts, and Grant Agreements

Management's Responsibility

Management of the federal government is responsible for the federal government's compliance with laws, regulations, contracts, and grant agreements.

Auditor's Responsibility

An audit of federal financial statements includes testing compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements that have a direct effect on the determination of material amounts and disclosures in the financial statements, and performing certain other limited procedures. Accordingly, we did not test the federal government's compliance with all laws, regulations, contracts, and grant agreements. Because of the limitations discussed below and the scope of our procedures, noncompliance may occur and not be detected by these tests.

Our objective was not to provide an opinion on the federal government's compliance with laws, regulations, contracts, and grant agreements. Accordingly, we do not express such an opinion. We performed our work in accordance with U.S. generally accepted government auditing standards.

Results of Tests for Compliance with Laws, Regulations, Contracts, and Grant Agreements

Our work to test compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements was limited by certain of the material weaknesses and other scope limitations discussed in this audit report. U.S. generally accepted government auditing standards and OMB guidance require auditors to report on entities' compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements. Certain component entity audit reports contain instances of noncompliance. None of these instances were deemed to be reportable noncompliance with regard to the accompanying U.S. government's consolidated financial statements.

Intended Purpose of Report on Compliance with Laws, Regulations, Contracts, and Grant Agreements

The purpose of this report on compliance with laws, regulations, contracts, and grant agreements is solely to describe the scope of our testing of compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements, and the results of that testing, and not to provide an opinion on compliance. This report on compliance with laws, regulations, contracts, and grant agreements is an integral part of an audit performed in accordance with U.S. generally accepted government auditing standards in considering compliance. Accordingly, this report on compliance with laws, regulations, contracts, and grant agreements is not suitable for any other purpose.

Agency Comments

We provided a draft of this audit report to Treasury and OMB officials, who provided technical comments that we have incorporated as appropriate. Treasury and OMB officials expressed their continuing commitment to addressing the problems this report outlines.

Robert F. Dacey
Chief Accountant
U.S. Government Accountability Office

March 20, 2019

Appendix I

Objectives, Scope, and Methodology

Our objectives were to audit the consolidated financial statements consisting of the (1) accrual-based consolidated financial statements as of and for the fiscal years ended September 30, 2018, and 2017, and (2) sustainability financial statements, which consist of the 2018 and 2017 Statements of Long-Term Fiscal Projections; the 2018, 2017, 2016, 2015, and 2014 Statements of Social Insurance; and the 2018 and 2017 Statements of Changes in Social Insurance Amounts. Our objectives also included reporting on internal control over financial reporting and on compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements.

The Chief Financial Officers Act of 1990 (CFO Act), as expanded by the Government Management Reform Act of 1994 (GMRA), requires the inspectors general of the 24 CFO Act agencies to be responsible for annual audits of agency-wide financial statements prepared by these agencies.[23] GMRA requires GAO to be responsible for the audit of the U.S. government's consolidated financial statements.[24] The Accountability of Tax Dollars Act of 2002 (ATDA) requires most other executive branch entities to prepare financial statements annually and have them audited.[25] The Office of Management and Budget and the Department of the Treasury (Treasury) have identified 40 federal entities that are significant to the U.S. government's fiscal year 2018 consolidated financial statements, including the 24 CFO Act agencies.[26] We consider these 40 entities to be significant component entities for purposes of our audit of the consolidated financial statements. We performed our work in coordination and cooperation with the inspectors general and independent public accountants for these significant component entities to achieve our respective audit objectives. Our audit approach regarding the accrual-based consolidated financial statements primarily focused on determining the current status of the material weaknesses that contributed to our disclaimer of opinion on the accrual-based consolidated financial statements and the other material weaknesses affecting internal control that we reported in our report on the consolidated financial statements for fiscal year 2017.[27] We also separately audited the financial statements of certain component entities, and parts of a significant component entity, including the following.

- We audited and expressed an unmodified opinion on the Internal Revenue Service's (IRS) financial statements as of and for the fiscal years ended September 30, 2018, and 2017.[28] In fiscal years 2018 and 2017, IRS collected about $3.5 trillion and $3.4 trillion, respectively, in tax payments and paid about $464 billion and $437 billion, respectively, in refunds to taxpayers. For fiscal year 2018, we also reported that although internal controls could be improved, IRS maintained, in all material respects, effective internal control over financial reporting. As a result of IRS's efforts to address many of the deficiencies we previously found in its internal control over unpaid assessments, we concluded that long-standing deficiencies related to unpaid assessments no longer represented a

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[23]31 U.S.C. § 3521(e). GMRA authorized the Office of Management and Budget to designate agency components that also must report financial statements and have them audited. See 31 U.S.C. § 3515(c).

[24]GMRA, Pub. L. No. 103-356, § 405(c), 108 Stat. 3410, 3416-17 (Oct. 13, 1994), *codified at* 31 U.S.C. § 331(e)(2).

[25]ATDA, Pub. L. No. 107-289, 116 Stat. 2049 (Nov. 7, 2002), *codified at* 31 U.S.C. § 3515.

[26]See app. A of the *Fiscal Year 2018 Financial Report of the United States Government* for a list of the 40 entities.

[27]GAO, *Financial Audit: Fiscal Years 2017 and 2016 Consolidated Financial Statements of the U.S. Government*, GAO-18-316R (Washington, D.C.: Feb. 15, 2018).

[28]GAO, *Financial Audit: IRS's Fiscal Years 2018 and 2017 Financial Statements*, GAO-19-150 (Washington, D.C.: Nov. 9, 2018).

material weakness; however, we considered these remaining issues affecting IRS's internal control over unpaid assessments collectively to be a significant deficiency in internal control. In addition, we continued to report a significant deficiency in IRS's internal control over financial reporting systems. We also reported that we found no reportable noncompliance for fiscal year 2018 with provisions of applicable laws, regulations, contracts, and grant agreements we tested.

- We audited and expressed an unmodified opinion on the Schedules of Federal Debt managed by Treasury's Bureau of the Fiscal Service (Fiscal Service) for the fiscal years ended September 30, 2018, and 2017.[29] For these 2 fiscal years, the schedules reported (1) approximately $15.8 trillion (2018) and $14.7 trillion (2017) of federal debt held by the public,[30] (2) about $5.7 trillion (2018) and $5.6 trillion (2017) of intragovernmental debt holdings,[31] and (3) about $357 billion (2018) and $296 billion (2017) of interest on federal debt held by the public. We also reported that although internal controls could be improved, Fiscal Service maintained, in all material respects, effective internal control over financial reporting relevant to the Schedule of Federal Debt as of September 30, 2018. In addition, we reported that we found no reportable noncompliance for fiscal year 2018 with provisions of applicable laws, regulations, contracts, and grant agreements we tested related to the Schedule of Federal Debt.

- We audited and expressed unmodified opinions on the U.S. Securities and Exchange Commission's (SEC) and its Investor Protection Fund's (IPF) financial statements as of and for the fiscal years ended September 30, 2018, and 2017.[32] We also reported that SEC maintained, in all material respects, effective internal control over financial reporting for both the entity as a whole and IPF as of September 30, 2018. In addition, we reported that we found no reportable noncompliance for either SEC or IPF for fiscal year 2018 with provisions of applicable laws, regulations, contracts, and grant agreements we tested.

- We audited and expressed an unmodified opinion on the Federal Housing Finance Agency's (FHFA) financial statements as of and for the fiscal years ended September 30, 2018, and 2017.[33] We also reported that FHFA maintained, in all material respects, effective internal control over financial reporting as of September 30, 2018. In addition, we reported that we found no reportable noncompliance for fiscal year 2018 with provisions of applicable laws, regulations, contracts, and grant agreements we tested.

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[29]GAO, *Financial Audit: Bureau of the Fiscal Service's Fiscal Years 2018 and 2017 Schedules of Federal Debt*, GAO-19-113 (Washington, D.C.: Nov. 8, 2018).

[30]Debt held by the public on the Schedules of Federal Debt represents federal debt that Treasury issued and that is held by investors outside of the federal government, including individuals, corporations, state or local governments, the Federal Reserve, and foreign governments.

[31]Intragovernmental debt holdings represent federal debt that Treasury owes to federal government accounts, primarily federal trust funds, such as those established for Social Security and Medicare.

[32]GAO, *Financial Audit: Securities and Exchange Commission's Fiscal Years 2018 and 2017 Financial Statements*, GAO-19-182R (Washington, D.C.: Nov. 15, 2018).

[33]GAO, *Financial Audit: Federal Housing Finance Agency's Fiscal Years 2018 and 2017 Financial Statements*, GAO-19-183R (Washington, D.C.: Nov. 15, 2018).

- We audited and expressed an unmodified opinion on the Office of Financial Stability's (OFS) financial statements for the Troubled Asset Relief Program (TARP) as of and for the fiscal years ended September 30, 2018, and 2017.[34] We also reported that OFS maintained, in all material respects, effective internal control over financial reporting for TARP as of September 30, 2018. In addition, we reported that we found no reportable noncompliance for fiscal year 2018 with provisions of applicable laws, regulations, contracts, and grant agreements we tested.

- We audited and expressed an unmodified opinion on the Bureau of Consumer Financial Protection's (BCFP)[35] financial statements as of and for the fiscal years ended September 30, 2018, and 2017.[36] We also reported that BCFP maintained, in all material respects, effective internal control over financial reporting as of September 30, 2018. In addition, we reported that we found no reportable noncompliance for fiscal year 2018 with provisions of applicable laws, regulations, contracts, and grant agreements we tested.

In addition, we considered the significant entities' fiscal years 2018 and 2017 financial statements and the related auditors' reports that the inspectors general or contracted independent public accountants prepared. Financial statements and audit reports for these entities provide information about the entities' operations. Each entity audit report also contains details about any identified material weaknesses or significant deficiencies and related recommendations for the respective entity. We did not audit, and we do not express an opinion on, any of these individual federal entity financial statements.

Our audit approach included performing work over Treasury processes and controls used to prepare the consolidated financial statements. We also considered our ongoing audit work on the General Fund of the U.S. Government.[37]

The Department of Defense (DOD) underwent an audit of its entity-wide fiscal year 2018 financial statements, which resulted in a disclaimer of opinion issued by the DOD Office of Inspector General (OIG). The disclaimer of opinion was partially based on the disclaimers of opinion for multiple DOD components, including the Army, Navy, Air Force, U.S. Marine Corps, Defense Health Program, Defense Logistics Agency, U.S. Transportation Command, and U.S. Special Operations Command. The DOD OIG also reported 20 material weaknesses in internal control over financial reporting, including those related to (1) property, plant, and equipment; (2) inventory and related property; (3) accounts receivable; (4) environmental and disposal liabilities; (5) reconciliations of disbursement activity; (6) intragovernmental eliminations; (7) financial statement compilation; and (8) financial management systems and information technology.

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[34]GAO, *Financial Audit: Office of Financial Stability (Troubled Asset Relief Program) Fiscal Years 2018 and 2017 Financial Statements*, GAO-19-152R (Washington, D.C.: Nov. 9, 2018).

[35]The Bureau of Consumer Financial Protection (BCFP), which was established by the Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, Title X, § 1011(a), 124 Stat. 1376, 1964 (July 21, 2010), *codified at* 12 U.S.C. § 5491(a), is often referred to as the Consumer Financial Protection Bureau (CFPB).

[36]GAO, *Financial Audit: Bureau of Consumer Financial Protection's Fiscal Years 2018 and 2017 Financial Statements*, GAO-19-184R (Washington, D.C.: Nov. 15, 2018).

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

Our audit approach for the 2018 and 2017 Statements of Long-Term Fiscal Projections focused primarily on assuring that the information relating to the Statements of Social Insurance is properly reflected therein and testing the methodology used as well as evaluating key assumptions. We also evaluated whether the internal control deficiencies related to the accrual-based consolidated financial statements affected certain key inputs used in generating the projections.

Because of the significance of the amounts presented in the Statements of Social Insurance and Statements of Changes in Social Insurance Amounts related to the Social Security Administration (SSA) and the Department of Health and Human Services (HHS), our audit approach regarding these statements focused primarily on these two agencies. For each federal entity preparing a Statement of Social Insurance and Statement of Changes in Social Insurance Amounts,[38] we considered the entity's 2018, 2017, 2016, 2015, and 2014 Statements of Social Insurance and the 2018 and 2017 Statements of Changes in Social Insurance Amounts, as well as the related auditor's reports that the inspectors general or contracted independent public accountants prepared.

We performed sufficient audit work to provide our reports on (1) the consolidated financial statements; (2) internal control over financial reporting; and (3) compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements. We considered the limitations on the scope of our work regarding the accrual-based consolidated financial statements and the sustainability financial statements in forming our conclusions. We performed our work in accordance with U.S. generally accepted government auditing standards.

[38]These entities are SSA, HHS, the Railroad Retirement Board, and the Department of Labor.

Appendix II

Material Weaknesses Contributing to Our Disclaimer of Opinion on the Accrual-Based Consolidated Financial Statements

The material weaknesses discussed below contributed to our disclaimer of opinion on the federal government's accrual-based consolidated financial statements.[39] The federal government did not have sufficient appropriate evidence to support information reported in the accompanying accrual-based consolidated financial statements, as described below.

Property, Plant, and Equipment; Inventories and Related Property; and Accounts Receivable

The federal government could not satisfactorily determine that property, plant, and equipment (PP&E); inventories and related property, and accounts receivable were properly reported in the accrual-based consolidated financial statements. Most of the PP&E and inventories and related property are the responsibility of the Department of Defense (DOD). As in past years, DOD did not maintain adequate systems or have sufficient records to provide reliable information on these assets. Certain other entities' auditors reported continued deficiencies in internal control procedures and processes related to PP&E. In addition, DOD could not adequately support its accounts receivable balance.

Deficiencies in internal control over PP&E and inventories and related property could affect the federal government's ability to fully know the assets it owns, including their location and condition. They can also affect the government's ability to effectively (1) safeguard assets from physical deterioration, theft, or loss; (2) account for acquisitions and disposals of such assets and reliably report asset balances; (3) ensure that the assets are available for use when needed; (4) prevent unnecessary storage and maintenance costs or purchase of assets already on hand; and (5) determine the full costs of programs that use these assets. In addition, deficiencies in internal control over accounts receivable could affect the federal government's ability to identify, record, and collect amounts owed to it.

Liabilities and Commitments and Contingencies

The federal government could not reasonably estimate or adequately support amounts reported for certain liabilities. For example, DOD was not able to estimate with assurance key components of its environmental and disposal liabilities. In addition, DOD could not support a significant amount of its estimated military postretirement health benefits liabilities included in federal employee and veteran benefits payable. These unsupported amounts relate to the cost of direct health care that DOD-managed military treatment facilities provided. Further, the federal government could not determine whether commitments and contingencies, including any related to treaties and other international agreements entered into to further the federal government's interests, were complete and properly reported.

Problems in accounting for liabilities affect the determination of the full cost of the federal government's current operations and the extent of its liabilities. Also, deficiencies in internal control supporting the process for estimating environmental and disposal liabilities could result in improperly stated liabilities, and could adversely affect the federal government's ability to determine priorities for cleanup and disposal activities and to appropriately consider future budgetary resources needed to carry out these activities. In addition, to the extent disclosures of commitments and contingencies are incomplete or incorrect, reliable information is not available about the extent of the federal government's obligations.

[39]The material weakness related to the Reconciliations of Budget Deficit to Net Operating Cost and Changes in Cash Balance also contributed to our disclaimer on the 2018 and 2017 Statements of Long-Term Fiscal Projections.

Cost of Government Operations and Disbursement Activity

Reported net costs were affected by the previously discussed material weaknesses in reporting assets and liabilities; material weaknesses in financial statement preparation, as discussed below; and the lack of adequate disbursement reconciliations at certain federal entities. As a result, the federal government was unable to support significant portions of the reported total net cost of operations, most notably those related to DOD.

With respect to disbursements, auditors of DOD and certain other federal entities reported continued control deficiencies in reconciling disbursement activity. For fiscal years 2018 and 2017, inadequate reconciliations of disbursement activity included (1) unreconciled differences between federal entities' and the Department of the Treasury's (Treasury) records of disbursements and (2) unsupported federal entity adjustments, which could also affect the balance sheet.

Unreliable cost information affects the federal government's ability to control and reduce costs, assess performance, evaluate programs, and set fees to recover costs where required or authorized. If disbursements are improperly recorded, this could result in misstatements in the financial statements and in certain data that federal entities provide for inclusion in *The Budget of the United States Government* (President's Budget) concerning obligations and outlays.

Intragovernmental Activity and Balances

Significant progress has been made over the past few years, but the federal government continues to be unable to adequately account for intragovernmental activity and balances between federal entities. Federal entities are responsible for properly accounting for and reporting their intragovernmental activity and balances in their entity financial statements. When preparing the consolidated financial statements, intragovernmental activity and balances between federal entities should be in agreement and must be subtracted out, or eliminated, from the financial statements. If the two federal entities engaged in an intragovernmental transaction do not both record the same intragovernmental transaction in the same year and for the same amount, the intragovernmental transactions will not be in agreement, and if not properly resolved, would result in errors (i.e., differences or unmatched amounts) in the consolidated financial statements. The Office of Management and Budget (OMB) and Treasury have issued guidance directing component entities to reconcile intragovernmental activity and balances with their trading partners and resolve identified differences. In addition, the guidance directs the chief financial officers (CFO) of significant component entities to report to Treasury, their respective inspectors general, and GAO on the extent and results of intragovernmental activity and balance reconciliation efforts as of the end of the fiscal year.

To support this process during fiscal year 2018, Treasury continued to actively work with significant component entities to provide information and assistance to aid them in resolving intragovernmental differences. Treasury's quarterly scorecard process[40] highlights differences needing the entities' attention, identifies differences that need to be resolved through a formal dispute resolution process,[41] and reinforces the entities' responsibilities to resolve intragovernmental differences. Treasury continued to perform procedures for identifying and monitoring systemic root causes of intragovernmental

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[40]For each quarter, Treasury produces a scorecard for each significant entity, as well as any other component entity reporting significant intragovernmental balances or differences, that reports various aspects of the entity's intragovernmental differences with its trading partners, including the composition of the differences by trading partner and category. Pursuant to Treasury guidance, entities are expected to resolve, with their respective trading partners, the differences identified in their scorecards.

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

differences and related corrective action plans to address the root causes. As a result of these and other actions, a significant number of intragovernmental differences were identified and resolved.

While progress was made, we continued to note that amounts reported by federal entity trading partners to Treasury were not in agreement by material amounts. Reasons for the differences that several CFOs cited included differing accounting methodologies, accounting errors, and timing differences. Auditors reported that several significant component entities did not have effective processes for reconciling intragovernmental activity and balances with their trading partners. For example, DOD components, which contribute significantly to the unresolved amounts, could not accurately identify, provide supporting documentation, or fully reconcile their intragovernmental transactions, which may have resulted in a material misstatement in amounts reported by DOD.

Further, a significant portion of intragovernmental differences are related to unresolved transactions between the General Fund of the U.S. Government (General Fund)[42] and federal entity trading partners related to appropriations and other intragovernmental transactions, which amount to over $100 billion. Over the past few years, Treasury has made progress by (1) developing and implementing procedures to improve the accounting for and reporting of General Fund transactions and balances, (2) working to resolve significant differences between the General Fund and federal entity trading partners, and (3) including differences involving General Fund activity and balances in the quarterly scorecard process. However, further improvements are needed to adequately support and reconcile intragovernmental activity and balances reported by the General Fund with federal entity trading partners.

As a result of the above-noted circumstances, the federal government's ability to determine the effect of these unresolved differences on the amounts reported in the accrual-based consolidated financial statements is significantly impaired. Addressing the intragovernmental transactions problem remains a difficult challenge and will require federal entities' strong and sustained commitment to resolving differences with their trading partners timely, as well as Treasury's and OMB's continued strong leadership.

Preparation of Consolidated Financial Statements

Treasury, in coordination with OMB, has implemented several corrective actions during the past few years related to the preparation of the consolidated financial statements. Corrective actions included improving systems used for compiling the consolidated financial statements, enhancing guidance for collecting data from component entities, and implementing procedures to address certain internal control deficiencies detailed in our previously issued management report.[43] However, the federal government's systems, controls, and procedures were not adequate to reasonably assure that the consolidated financial statements are consistent with the underlying audited entity financial statements, properly balanced, and in accordance with U.S. generally accepted accounting principles (U.S. GAAP). During our fiscal year 2018 audit, deficiencies in the preparation of the consolidated financial statements included the following.

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

[43]Most of the issues we identified in fiscal year 2018 existed in fiscal year 2017, and many have existed for a number of years. In past years, we reported the issues we identified to Treasury and OMB and provided recommendations for corrective action. Most recently, in July 2018, we reported on the status of the open recommendations. See GAO, *Management Report: Continued Improvements Needed in Controls over the Processes Used to Prepare the U.S. Consolidated Financial Statements*, GAO-18-540 (Washington, D.C.: July 16, 2018).

- For fiscal year 2018, auditors reported internal control deficiencies at several component entities regarding their entity-level controls, including the control environment, risk assessment, information and communication, and monitoring components of internal control, that could affect Treasury's ability to obtain reliable financial information from federal entities for consolidation. For example, DOD did not have sufficient entity-level controls to establish an internal control system that will produce reliable financial reporting, Also, the Department of Veterans Affairs (VA) lacked an effective entity-level control system, which, coupled with a decentralized reporting structure and legacy system issues, has led to systemic and pervasive control deficiencies that impede VA's ability to process, summarize and report reliable financial information in a timely manner.

- For fiscal year 2018, auditors reported internal control deficiencies at several component entities related to the entities' financial reporting processes that could affect information in those entities' closing packages.[44] For example, DOD could not demonstrate that its financial statements were consistent with underlying records. Also, the Department of Housing and Urban Development's internal controls did not reasonably assure that all necessary information was included in its consolidated financial statements. To reasonably assure consistency of underlying entity information and financial data with the U.S. government's consolidated financial statements, Treasury guidance directs entity auditors to separately audit and report on the financial information that the significant component entities send to Treasury through closing packages. As in past years, Treasury had to record significant adjustments to correct errors found in federal entities' audited closing package information. As with the last several years, these errors primarily related to intragovernmental activity and balances and totaled tens of billions of dollars.

- While progress has been made, Treasury is unable to properly balance the accrual-based consolidated financial statements because of its inability to fully eliminate intragovernmental activity and balances. To make the fiscal years 2018 and 2017 consolidated financial statements balance, Treasury recorded a net increase of $2.4 billion and a net decrease of $2.6 billion, respectively, to net operating cost on the Statements of Operations and Changes in Net Position, which were identified as "Unmatched transactions and balances."[45] Treasury recorded an additional net $1.3 billion and $2.0 billion of unmatched transactions in the Statements of Net Cost for fiscal years 2018 and 2017, respectively. The material weakness in the federal government's ability to account for intragovernmental activity and balances, discussed above, significantly contributes to this issue.

- Over the past several years, Treasury has taken significant actions to help ensure that financial information is reported or disclosed in the consolidated financial statements in accordance with U.S. GAAP. For example, Treasury has developed and implemented U.S. GAAP compliance operating procedures and checklists. Also, Treasury worked with entities to improve reporting of commitments and contingencies related to treaties and other international agreements. However, Treasury's reporting of certain financial information required by U.S. GAAP continues to be impaired. Because of certain control deficiencies noted in this audit report—for example, commitments and contingencies related to treaties and other international agreements—Treasury is precluded from determining if U.S. GAAP requires additional disclosure in the consolidated financial statements, and we are precluded from determining whether the omitted information is material. Further, Treasury's ability to report information in accordance with U.S. GAAP will also remain impaired until

[44]The closing package methodology links federal significant component entities' audited financial statements to certain line items, note disclosures, and other information on the U.S. government's consolidated financial statements.

[45]Although Treasury was unable to determine how much of the unmatched transactions and balances relates to net operating cost, it reported this amount as a component of net operating cost in the accompanying consolidated financial statements.

federal entities, such as DOD, can provide Treasury with the complete and reliable information required to be reported in the consolidated financial statements.

In fiscal year 2018, Treasury continued to make progress with corrective actions intended to resolve internal control deficiencies in the processes used to prepare the consolidated financial statements. For example, Treasury designed and implemented an internal control review process for monitoring and assessing the effectiveness of internal controls over the processes used to prepare the consolidated financial statements.

However, until these internal control deficiencies have been fully addressed, the federal government's ability to reasonably assure that the consolidated financial statements are consistent with the underlying audited federal component entities' financial statements, properly balanced, and in accordance with U.S. GAAP will be impaired. In recent years, Treasury has continued to improve its systems and processes for preparing the consolidated financial statements. It is important that Treasury (1) continues to improve its systems and (2) remains committed to maintaining the progress that has been made in this area and building on that progress to make needed improvements that fully address the magnitude of the financial reporting challenges it faces. Resolving the remaining internal control deficiencies continues to be a difficult challenge and will require a strong and sustained commitment from Treasury, OMB, and federal entities.

Reconciliations of Budget Deficit to Net Operating Cost and Changes in Cash Balance

The Reconciliations of Net Operating Cost and Budget Deficit and the Statements of Changes in Cash Balance from Budget and Other Activities (Reconciliation Statements) reconcile (1) the accrual-based net operating cost to the primarily cash-based budget deficit and (2) the budget deficit to changes in cash balances. The budget deficit is calculated by subtracting actual budget outlays (outlays) from actual budget receipts (receipts).[46] The outlays and receipts are key inputs to the Statements of Long-Term Fiscal Projections.

Treasury continued to develop its process for preparing the Reconciliation Statements. For example, during fiscal year 2018, Treasury documented its rationale for the reconciling items currently presented on the Reconciliation Statements. Specifically, Treasury documented its detailed analyses related to the accrual-based and cash-based effects of federal entities' transactions included in net operating cost and the budget deficit. Also, Treasury's significant efforts to develop and implement procedures to improve the accounting for and reporting of General Fund transactions and balances, if effective, should support the reconciliation of the records that Treasury uses to compute the budget deficit reported in the consolidated financial statements and Treasury's records of cash transactions processed through its central accounting function. However, as of the end of fiscal year 2018, processes and procedures were not effective in (1) identifying and reporting all the items in the Reconciliation Statements, (2) properly supporting amounts used in calculating the budget deficit, and (3) reasonably assuring that the information in these statements was fully consistent with the underlying information in the significant component entities' audited financial statements and other financial data. Consequently, there may be misstatements in the Reconciliation Statements.

[46]The budget deficit, receipts, and outlays amounts are reported in Treasury's *Monthly Treasury Statement* and the President's Budget.

In fiscal year 2018, we again noted that several entities' auditors reported internal control deficiencies related to monitoring, accounting, and reporting of budgetary transactions. These control deficiencies could affect the reporting and calculation of the net outlay amounts in the entities' Statements of Budgetary Resources. In addition, such deficiencies may also affect the entities' ability to report reliable budgetary information to Treasury and OMB and may affect the budget deficit reported in the accrual-based consolidated financial statements. Treasury also reports the budget deficit in its *Combined Statement of Receipts, Outlays, and Balances* and in other federal government publications.[47]

[47]Treasury's *Combined Statement of Receipts, Outlays, and Balances* presents budget results and cash-related assets and liabilities of the federal government with supporting details. According to Treasury, this report is the recognized official publication of receipts and outlays of the federal government based on entity reporting.

Appendix III

Other Material Weaknesses

Material weaknesses in internal control discussed in this audit report resulted in ineffective controls over financial reporting. In addition to the material weaknesses discussed in appendix II that contributed primarily to our disclaimer of opinion on the accrual-based consolidated financial statements, we found the following three other material weaknesses in internal control.

Improper Payments

The federal government is unable to determine the full extent to which improper payments occur and reasonably assure that appropriate actions are taken to reduce them. Reducing improper payments is critical to safeguarding federal funds.[48] The Improper Payments Information Act of 2002 (IPIA), as amended by the Improper Payments Elimination and Recovery Act of 2010 (IPERA) and the Improper Payments Elimination and Recovery Improvement Act of 2012 (IPERIA),[49] requires federal executive agencies (agencies)[50] to do the following:

1. Review all programs and activities.
2. Identify those that may be susceptible to significant improper payments.
3. Estimate the annual amount of improper payments for those programs and activities identified as risk susceptible.
4. Implement actions to reduce improper payments and set reduction targets with respect to the risk-susceptible programs and activities.
5. Report on the results of addressing the foregoing requirements.

Agency improper payment estimates totaled about $151 billion for fiscal year 2018, based on improper payment estimates reported by federal program or activity.[51] The government-wide total of reported estimated improper payments, among programs and activities that reported estimates, increased by about $10 billion from the prior year estimate of about $141 billion. While decreases in estimated improper payments were reported for several programs and activities, these were offset by increases

[48]Under the Improper Payments Information Act of 2002, as amended, an improper payment is statutorily defined as any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements. It includes any payment to an ineligible recipient, any payment for an ineligible good or service, any duplicate payment, any payment for a good or service not received (except for such payments where authorized by law), and any payment that does not account for credit for applicable discounts. Office of Management and Budget guidance also provides that when an agency's review is unable to discern whether a payment was proper as a result of insufficient or lack of documentation, this payment must also be considered an improper payment.

[49]IPIA, Pub. L. No. 107-300, 116 Stat. 2350 (Nov. 26, 2002), as amended by IPERA, Pub. L. No. 111-204, 124 Stat. 2224 (July 22, 2010), and IPERIA, Pub. L. No. 112-248, 126 Stat. 2390 (Jan. 10, 2013), and reprinted in 31 U.S.C. § 3321 note.

[50]IPIA, as amended, statutorily defines agencies as executive agencies as that term is defined under 31 U.S.C. § 102 to mean departments, agencies, or instrumentalities in the executive branch of the United States.

[51]The *Fiscal Year 2018 Financial Report of the United States Government* did not include a government-wide improper payment estimate or error rate. From fiscal year 2003 through fiscal year 2016, a government-wide estimate and error rate had been reported in financial reports based on the programs and activities that reported estimates.

for certain other programs and activities.[52] For example, the Department of Agriculture (USDA) reported estimated improper payments for its Supplemental Nutrition Assistance Program in excess of $4 billion for fiscal year 2018. USDA did not report estimated improper payments for this program for fiscal year 2017. It is important to note that pursuant to Office of Management and Budget (OMB) implementing guidance, reported improper payment estimates include overpayments, underpayments, and payments for which the agency could not find sufficient documentation, and may also be based on payment data and sampling drawn from periods that do not coincide with the fiscal year for which the estimates are reported.

The specific programs and activities included in the government-wide total of reported improper payment estimates may change from year to year. For example, six agencies did not report fiscal year 2018 estimated improper payment amounts for 10 programs and activities that were identified by the agency or OMB as risk-susceptible, including the Department of Health and Human Services' (HHS) Temporary Assistance for Needy Families (TANF).[53] Further, various inspectors general reported deficiencies related to compliance with the criteria listed in IPERA for fiscal year 2017 at their respective agencies,[54] including risk-susceptible programs and activities that did not report improper payment estimates, estimation methodologies that may not produce reliable estimates, and risk assessments that may not accurately assess the risk of improper payment. For example, the Department of Defense (DOD) Office of Inspector General reported that DOD did not ensure that all required payments were included in certain programs' improper payment estimates, and as a result, DOD published unreliable estimates of improper payments for fiscal year 2017.[55]

[52]For fiscal year 2018, agencies reported decreases in total estimated improper payments in excess of $1 billion for one program and increases in total estimated improper payments in excess of $1 billion for five programs and activities. The one program with a decrease in excess of $1 billion was the Department of Health and Human Services' (HHS) Medicare Fee-for-Service program. The five programs and activities with increases in excess of $1 billion were the Department of Veterans Affairs' (VA) Community Care; the Department of Agriculture's Supplemental Nutrition Assistance Program; the Social Security Administration's (SSA) Old Age, Survivors, and Disability Insurance; the Department of the Treasury's (Treasury) Earned Income Tax Credit (EITC), and HHS's Medicare Advantage (Part C).

[53]The 10 programs and activities were (1) the Federal Communications Commission's (FCC) Universal Service Fund Rural Health Care, (2) HHS's TANF, (3) HHS's Advance Premium Tax Credit, (4) the Department of Housing and Urban Development's (HUD) Office of Multifamily Housing Project-Based Rental Assistance, (5) Treasury's Advance Child Tax Credit, (6) Treasury's Additional Opportunity Tax Credit, (7) Treasury's Premium Tax Credit, (8) USDA's Child and Adult Care Food Program, (9) USDA's Risk Coverage and Price Loss Coverage, and (10) VA's Dependency and Indemnity Compensation.

[54]IPERA established a requirement for agency inspectors general to report annually on agencies' compliance with criteria listed in section 3 of IPERA. The six criteria are that the agency has (1) published an annual financial statement and accompanying materials in the form and content that OMB requires for the most recent fiscal year and posted that report on the agency website; (2) conducted a risk assessment for each specific program or activity that conforms with IPIA, as amended; (3) published estimates of improper payments for all programs and activities identified as susceptible to significant improper payments under the agency's risk assessment; (4) published corrective action plans for programs and activities assessed to be at risk for significant improper payments; (5) published and met annual reduction targets for all programs and activities assessed to be at risk for significant improper payments; and (6) reported a gross improper payment rate of less than 10 percent for each program and activity for which an improper payment estimate was obtained and published. The most recent inspector general reports on compliance with the criteria listed in IPERA were issued in 2018 for fiscal year 2017. Pursuant to the OMB implementing guidance in OMB Memorandum M-18-20, appendix C to OMB Circular No. A-123, *Requirements for Payment Integrity Improvement* (June 26, 2018), inspector general reports are due by May 15 of the following year (or the next business day if May 15 falls on a weekend). Therefore, inspector general reports on fiscal year 2018 compliance with the criteria listed in IPERA are expected to be issued no later than May 15, 2019.

[55]Department of Defense, Office of Inspector General, *The DoD Did Not Comply with the Improper Payment Elimination and Recovery Act in FY 2017*, Report No. DODIG-2018-115 (Alexandria, Va.: May 9, 2018).

For fiscal year 2018, agencies reported estimated improper payment rates of 10 percent or greater for 20 risk-susceptible programs and activities,[56] accounting for about 25 percent of the government-wide total of reported estimated improper payments.[57] Under IPERA, if an agency's inspector general determines that the entity is not in compliance with the criteria listed in IPERA, such as reporting an improper payment rate of 10 percent or greater for any risk-susceptible program or activity, that agency must submit a plan to Congress describing the actions that it will take to come into compliance.

Further, agency auditors continued to report internal control deficiencies over financial reporting in their fiscal year 2018 financial statement audit reports, such as financial system limitations and information system control weaknesses. Such deficiencies could significantly increase the risk that improper payments may occur and not be detected promptly.

The President's fiscal years 2018 and 2019 budgets included program integrity proposals at multiple agencies aimed at reducing improper payments. Also, efforts continue to implement requirements established by IPERIA, which was enacted in January 2013, to intensify efforts to identify, prevent, and recover payment error, waste, fraud, and abuse in federal spending. Among other things, IPERIA established the statutory Do Not Pay initiative, requiring agencies to review prepayment and pre-award procedures and ensure a thorough review of available databases to determine program or award eligibility before the release of any federal funds. IPERIA also directs OMB to annually identify a list of high-priority federal programs for greater levels of oversight and review and requires each agency responsible for administering one of these high-priority programs to annually submit a program report to its inspector general and make the report available to the public.[58]

Until the federal government has implemented effective processes to determine the full extent to which improper payments occur and has taken appropriate actions across agencies and programs and activities to effectively reduce improper payments, it will not have reasonable assurance that the use of federal funds is adequately safeguarded.

Information Security

GAO has reported information security as a high-risk area across government since February 1997. During our fiscal year 2018 audit, we found that serious and widespread information security control deficiencies continued to place federal assets at risk of inadvertent or deliberate misuse, financial information at risk of unauthorized modification or destruction, sensitive information at risk of

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[56]The improper payment rate reflects the estimated improper payments as a percentage of total annual outlays.

[57]The 20 programs and activities that reported estimated improper payment rates of 10 percent or greater for fiscal year 2017 were (1) VA's Community Care; (2) VA's Purchased Long-Term Services and Supports; (3) VA's Communications, Utilities, and Other Rent; (4) VA's Medical Care Contracts and Agreements; (5) VA's Prosthetics; (6) VA's Supplies and Materials; (7) Corporation for National and Community Service's (CNCS) Senior Companion; (8) Treasury's EITC; (9) VA's Beneficiary Travel; (10) HUD's Ginnie Mae Contractor Payments; (11) CNCS's Foster Grandparent; (12) FCC's Universal Service Fund Lifeline; (13) CNCS's Retired and Senior Volunteer; (14) CNCS's AmeriCorps; (15) USDA's Farm Service Agency (FSA) Noninsured Crop Disaster Assistance; (16) the Department of Labor's Unemployment Insurance; (17) USDA's FSA Livestock Forage Disaster; (18) USDA's School Breakfast; (19) the Railroad Retirement Board's Railroad Medicare; and (20) the Consumer Product Safety Commission's Non-Payroll.

[58]OMB has designated high-priority programs as those programs and activities with improper payment estimates that exceed $2 billion annually. The 12 programs and activities with reported improper payment estimates greater than $2 billion in fiscal year 2018 were (1) HHS's Medicaid; (2) HHS's Medicare Fee-for-Service; (3) Treasury's EITC; (4) HHS's Medicare Advantage; (5) VA's Community Care; (6) SSA's Old Age, Survivors, and Disability Insurance; (7) SSA's Supplemental Security Income; (8) USDA's Supplemental Nutrition Assistance Program; (9) the Department of Education's (Education) Direct Loan; (10) the Department of Labor's Unemployment Insurance; (11) Education's Pell Grant; and (12) VA's Purchased Long-Term Services and Support.

inappropriate disclosure, and critical operations at risk of disruption.[59] Specifically, control deficiencies were identified related to (1) security management; (2) access to computer resources (data, equipment, and facilities); (3) changes to and configuration of information system resources; (4) segregation of incompatible duties; and (5) contingency planning.

Such information security control deficiencies unnecessarily increase the risk that data recorded in or transmitted by federal financial management systems are not reliable and available. A primary reason for these deficiencies is that federal entities generally have not yet fully institutionalized comprehensive security management programs, which are critical to identifying information security control deficiencies, resolving information security problems, and managing information security risks on an ongoing basis. Until entities identify and resolve these deficiencies and effectively manage information security risks on an ongoing basis, federal data and systems, including financial information, will remain at risk.

Loans Receivable and Loan Guarantee Liabilities

Internal control deficiencies were identified at certain federal entities that accounted for a majority of the reported balances of loans receivable and loan guarantee liabilities.[60] The deficiencies related to credit program cost estimation, associated control activities, and financial reporting processes. These deficiencies and complexities associated with estimating the costs of loan and loan guarantee programs and related financing activities significantly increase the risk that misstatements in federal entity and government-wide financial statements could occur and go undetected. Further, these deficiencies can adversely affect the entities' ability to support annual budget requests for these programs, make future budgetary decisions, manage program costs, and measure the performance of lending activities.

[59]Eighteen of the 24 agencies covered by the Chief Financial Officers Act of 1990 reported information security as a material weakness or significant deficiency for fiscal year 2018.

[60]Entities contributing to the material weakness for loans receivable and loan guarantee liabilities include the Departments of Education, Housing and Urban Development, Transportation, and Veteran Affairs.

Appendix IV

Significant Deficiencies

In addition to the material weaknesses discussed in appendixes II and III, we found three significant deficiencies in the federal government's internal control related to maintaining effective internal controls at certain federal entities, as described below.

Taxes Receivable

During fiscal year 2018, a significant deficiency, previously reported as a material weakness until this fiscal year, continued to affect the federal government's ability to manage its taxes receivable effectively. While the Department of the Treasury's Internal Revenue Service (IRS) made necessary and appropriate adjustments derived from a statistical estimation process to correct its financial statements, IRS's underlying records did not always reflect the correct amount of taxes owed by the public to the federal government at interim periods and year-end because of financial system limitations and other control deficiencies that led to errors in taxpayers' accounts. Such inaccurate tax records impair management's ability to effectively manage taxes receivable throughout the year and place an undue burden on taxpayers who may be compelled to respond to IRS inquiries caused by errors in their accounts. Further, IRS did not clearly document several key management decisions regarding the design and use of the statistical estimation process used to derive the reported taxes receivable balance. This increases the risk that the process could be implemented in a manner contrary to management intent, potentially rendering the resultant estimates statistically invalid.

Collectively, these deficiencies indicate that internal controls were not effective in (1) ensuring that reported amounts of taxes receivable and other unpaid assessments were accurate on an ongoing basis and could be relied upon by management as a tool to aid in making and supporting resource allocation decisions and (2) supporting timely and reliable financial statements, accompanying notes, required supplementary information, and other information without extensive supplemental procedures and adjustments.

Federal Grants Management

In fiscal year 2018, several federal entities' auditors continued to identify internal control deficiencies related to grants management.[61] Reported deficiencies primarily related to monitoring of grant activities, accounting for grants, and estimating grant accruals. These internal control deficiencies could adversely affect the federal government's ability to provide reliable financial statements as well as reasonable assurance that grants are awarded properly, recipients are eligible, and federal grant funds are used as intended.

Medicare Social Insurance Information

In fiscal year 2018, auditors for the Department of Health and Human Services (HHS) identified internal control deficiencies in certain controls related to HHS's preparation of its Statement of Social Insurance for the Medicare program. The models HHS used for its Statement of Social Insurance are complex, 75-year projections, including spreadsheets and macros that actuaries, auditors, and others heavily review. The reviewers check input into the spreadsheets against original data sources and check output data by comparing the outputs to the results of the prior year and by testing the formulas included in the spreadsheets or macros. The underlying data remains critical to the accuracy of the models. In fiscal

[61] Key entities contributing to the significant deficiency for federal grants management include the Department of Homeland Security, Department of Housing and Urban Development, and Millennium Challenge Corporation.

year 2018, two formula errors in certain spreadsheets that HHS used to prepare its Statement of Social Insurance for the Medicare program were not detected by HHS's monitoring and review function. HHS contributes the majority of the amounts reported on the consolidated Statement of Social Insurance. Such control deficiencies could result in misstatements to the Statement of Social Insurance.