DEPARTMENT OF THE TREASURY

Agency Financial Report

FISCAL YEAR 2009

DECEMBER 15, 2009

The United States Department of the Treasury

Our Vision

Set the global standard in financial and economic leadership

Our Mission

Serve the American people and strengthen national security by managing the U.S. Government's finances effectively, promoting economic growth and stability, and ensuring the safety, soundness, and security of the U.S. and international financial systems

Our Values

SERVICE

Work for the benefit of the American people

INTEGRITY

Aspire to the highest levels ethical standards of honesty, trustworthiness, and dependability

EXCELLENCE

Strive to be the best, continuously improve, innovate, and adapt

OBJECTIVITY

Encourage independent views

ACCOUNTABILITY

Responsible for our conduct and work

COMMUNITY

Dedicated to excellent customer service, collaboration, and teamwork while promoting diversity

DEPARTMENT OF THE TREASURY

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Message from the Secretary of the Treasury

December 15, 2009

The Treasury Department has spent the past fiscal year confronting the worst economic and financial crisis in generations.

While policy interventions at the end of 2008 succeeded in achieving the vital, but narrow, objective of preventing a catastrophic systemic meltdown, by the time President Obama took office, the financial system remained extremely fragile and the Administration faced a rapidly evolving set of challenges.

In the financial sector the flow of credit to businesses and families had frozen; the issuance of new asset-backed securities had essentially come to a halt; and liquidity in a broader range of securities markets had fallen sharply.

In addition, the broader economy was in a free fall. In January we lost 741,000 nonfarm jobs, the largest single monthly decline in 60 years. Our Gross Domestic Product was contracting at rates not seen in decades. American families had lost $11 trillion in household wealth since 2007. And there was genuine concern we were headed toward a second Great Depression.

The Obama Administration responded with a comprehensive strategy unprecedented in size and scope.

First, we worked with Congress to enact the most sweeping economic recovery package in our nation's history. The Recovery Act included a program of immediate tax incentives for businesses and households, support for state and local governments, and investments in critical economic priorities, from infrastructure and energy to health care and education. More than 110 million families – 95 percent of working families – received hundreds of dollars in the Making Work Pay tax benefit.

Second, we moved quickly to stabilize our financial system with as much private capital as possible. Following the release of the "stress test" results, our nation's largest banks were able to raise over $80 billion in private capital and, as of September 30, 2009, have paid roughly $70 billion back to the government for previous investments. More broadly, last December, 70 percent of corporate bond issuance was supported by the government. In September of this year, corporations raised over $100 billion in debt, 82 percent of which was issued without a government guarantee.

Third, we jumpstarted channels of credit that are critical for American families and businesses. Our Term Asset-Backed Securities Loan Facility (TALF) has helped to improve conditions substantially. Issuance of securities backed by consumer and business loans has averaged $14 billion per month since the government launched TALF in March, compared to about $1.6 billion per month in the six months prior to the program's launch.

Fourth, we created a public-private investment program to purchase legacy assets to help clean up the balance sheets of major financial institutions and re-liquefy key markets. Program announcements helped improve prices for these assets in advance of actual purchases. And due to continued improvements in financial market conditions, we are able to proceed with the program at a scale smaller than initially envisioned.

Fifth, we worked to ease the housing crisis by helping to bring mortgage rates to historic lows and establishing new programs to allow responsible homeowners to refinance into affordable mortgages or modify at-risk loans to lower monthly mortgage payments.

And finally, we worked with the major economies of the world on a coordinated program of macroeconomic stimulus and financial stabilization, alongside regulatory reform.

Because of these steps, an economy that was in free-fall in January is now on the road to recovery. It grew at an annual rate of 2.8 percent in the third quarter, and private economists generally expect moderate growth over the next year. Business and consumer confidence has started to improve. The housing market is showing some signs of stabilizing. Home prices have increased modestly over the past six months, reversing consistent declines since 2006, and sales of existing single-family homes have increased by 20 percent over the past year. The cost of credit in securities markets has fallen substantially for businesses, and credit is flowing again in these markets.

These early signs of progress have allowed us to begin evolving our strategy from rescuing the economy to repairing and rebuilding the foundation for future growth.

As we enter this new phase we are winding down some of the extraordinary support put in place for the financial system. But we are also mindful that unemployment is still too high and that small businesses, an important engine of job growth in America, still face enormous difficulty accessing credit.

Going forward we must continue to reinforce recovery until it is self-sustaining and led by private demand. That is our primary objective. And we are working to achieve it by using our resources in the most effective and efficient manner possible.

We quickly established the Office of Financial Stability (OFS) and implemented strong program and financial reporting internal controls. The Department received an unqualified opinion on both our OFS/Troubled Asset Relief Program and Treasury-wide fiscal year 2009 financial statements—a remarkable achievement.

This year, the Department met or exceeded 67 percent of its performance targets, a reduction of three percentage points compared to last year, reflecting the challenges the Department faced in confronting the financial and economic crisis. While the percentage of unmet targets increased over last year, on average performance targets were within 10 percent of desired results. Discretionary budget resources increased 4.8 percent over 2008.

While we continue to resolve major challenges in some areas, overall we are making progress in addressing management and control weaknesses and in meeting federal financial systems requirements. The Department has validated the accuracy, completeness, and reliability of the financial and performance data contained in this report.

Timothy F. Geithner
Secretary of the Treasury

About this Report

The fiscal year 2009 Treasury Agency Financial Report provides information that enables Congress, the President, and the public to assess the Department's performance relative to its mission and stewardship of the resources entrusted to it.

For fiscal year 2009, the Department participated in the Office of Management and Budget's alternative Performance and Accountability Report option for reporting annual results. In this process, the Performance and Accountability Report is divided into two reports, an Agency Financial Report and an Annual Performance Report. The Agency Financial Report is produced prior to the end of the calendar year and includes a Management's Discussion and Analysis with a high level discussion of key agency accomplishments, and performance and financial results. Financial statements and analysis are also included in the Agency Financial Report. The Annual Performance Report will be generated and submitted with the Congressional Budget Justification in February 2010. The Annual Performance Report will contain detailed information on performance for agency outcomes.

The fiscal year 2009 Management's Discussion and Analysis is focused on the contributions Treasury has made on behalf of the American people to restore confidence in the financial system and enable economic recovery. The implementation of efforts aimed at financial stability, easing the housing crisis, and the Recovery Act are included, as well as activities related to financial regulatory reform.

Similar to last year, agency–wide performance results are summarized in the "How Well is Treasury Performing?" section. Results by strategic goal, along with trends in performance, budget, and cost are also included. A key performance measure table is included along with a discussion of results. Management challenges are summarized and assessed for progress and status, and improvements to high-risk areas are discussed. Consolidated financial statements, analysis, and footnote disclosures are presented to provide a comprehensive picture of the Department's financial position. Hyperlinks are used throughout the report providing an option to obtain additional detail.

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Part 1
Management's Discussion & Analysis

Introduction

Fiscal year 2009 began with the passage of historic legislation to support a tenuous financial system. Following the placement of Fannie Mae and Freddie Mac into conservatorship, failures of Lehman Brothers and Washington Mutual, and significant troubles at American International Group (AIG) and other firms, Congress enacted the *Emergency Economic Stabilization Act of 2008* (EESA), providing $700 billion in spending authority to support financial markets. In the months that followed, Treasury played a key role in stabilizing the financial system and limiting damage in the broader economy.

In February 2009, with the economy contracting at the fastest speed in the last quarter century, Congress passed the *American Recovery and Reinvestment Act of 2009* (Recovery Act) to provide economic stimulus. Implementation of tax and other provisions by Treasury under the Recovery Act limited the fallout from the financial crisis and encouraged investment in renewable energy projects and low-income communities. Programs implemented by Treasury under the Recovery Act, *Housing and Economic Recovery Act of 2008* (HERA), and EESA provided support for homeowners and helped avoid unnecessary foreclosures.

In February 2009, Treasury issued the Financial Stability Plan, helping boost confidence in the stability of financial institutions and unlock frozen securitization markets. Since then, Treasury has put in place a series of financial initiatives to help lay the foundation for economic recovery: 1) a broad program to stabilize the housing market by encouraging lower mortgage rates and making it easier for millions to refinance and avoid foreclosure; 2) a new capital program to provide banks with a safeguard against a deeper recession; 3) a major new lending program with the Federal Reserve targeted at the securitization markets critical for consumer and small business lending; and 4) a program to set up funds to provide a market for legacy loans and securities that currently burden the financial system.

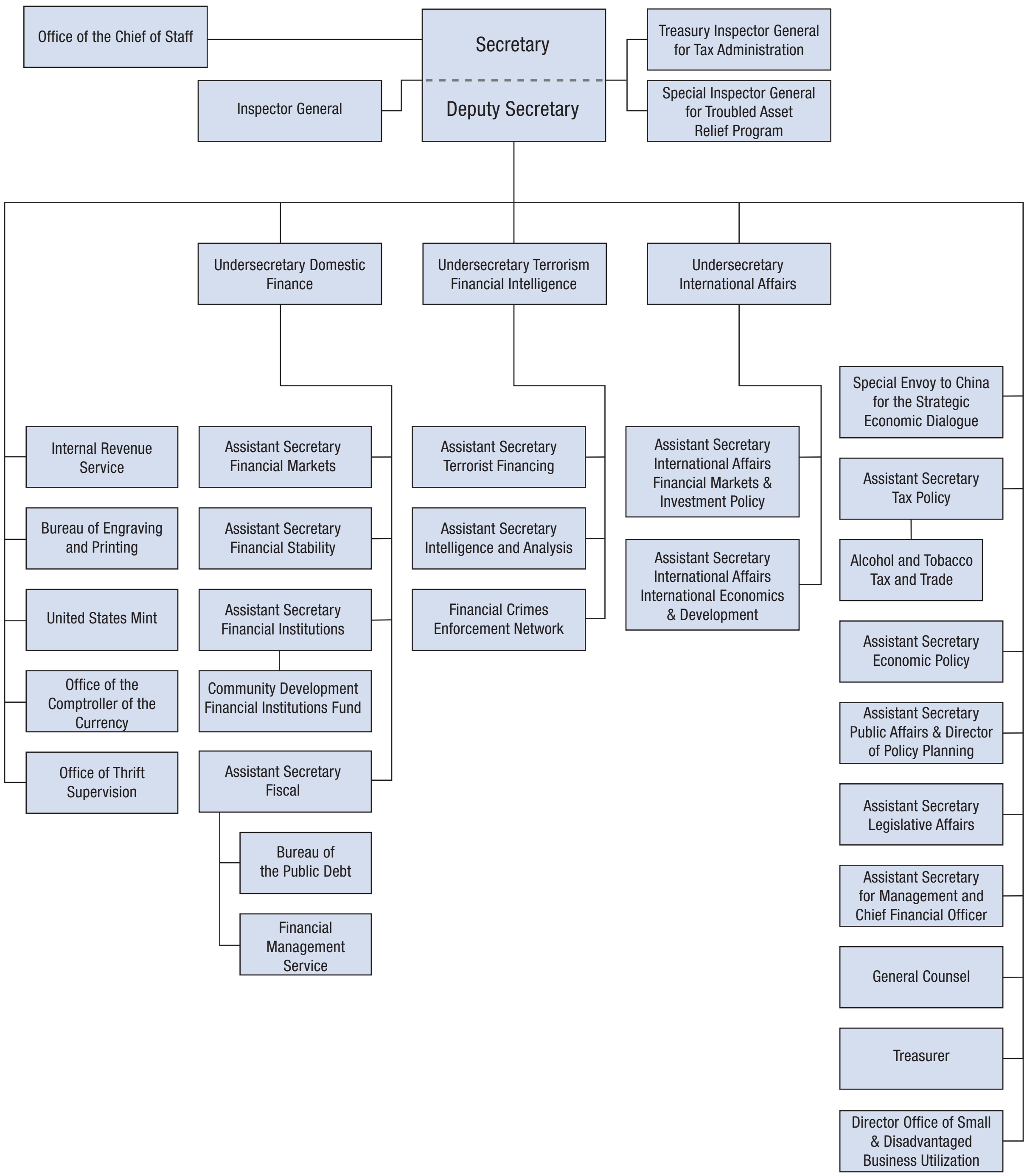
In June 2009, the President announced a comprehensive plan to reform the United States' outdated and ineffective financial regulatory system. The goals of the plan are simple: to protect responsible consumers and investors; to lay the foundation for a safer, more stable financial system that is less prone to panic and crisis; and to safeguard American taxpayers from bearing risks that ought to be borne by shareholders and creditors. Treasury submitted proposed legislative text to implement the plan in August 2009 and is actively working with Congress to pass this critical legislation.

Treasury has initiated the next phase of the strategy to stabilize and rehabilitate financial markets. As the need for the emergency programs that were put in place during the most acute phase of the crisis declines, those programs will wind down. At the same time, the use of those programs, by design, continues to decline as the financial system recovers. But the financial system is still fragile, and some of the improvements that have been realized in many financial markets are still largely dependent on the support of extraordinary policies. Going forward, the U.S. Government must work to promote the public trust, use taxpayer money prudently to repair the financial system, and reassure market participants so that they have the confidence to get credit flowing again to families and businesses.

Treasury will continue to implement the programs set in place to restore essential balance in the U.S. and global economies. In implementing these programs, the Department of the Treasury will exercise diligent stewardship and provide exceptional accountability and transparency in performing its work on behalf of the American people.

Organization

THE DEPARTMENT OF THE TREASURY ORGANIZATIONAL CHART



The Department of the Treasury is the executive agency responsible for promoting economic prosperity and ensuring the financial security of the United States. The Department is organized into two major components, the departmental offices and the bureaus. The departmental offices are primarily responsible for policy formulation, while the bureaus are primarily the operating units of the organization.

Departmental Offices

Domestic Finance advises and assists in areas of domestic finance, banking, and other related economic matters. In addition, this office develops policies and guidance for Treasury Department responsibilities in the areas of financial institutions, federal debt finance, financial regulation, capital markets, financial management, fiscal policy, and cash management decisions.

International Affairs advises and assists in the formulation and execution of U.S. international economic, financial, monetary, trade, investment, bilateral aid, environment, debt, development, and energy policy, including U.S. participation in international financial institutions.

Terrorism and Financial Intelligence (TFI) marshals the Department's intelligence and enforcement functions with the twin aims of safeguarding the financial system against illicit use and combating rogue nations, terrorist facilitators, money launderers, drug kingpins, and other national security threats.

Economic Policy reports on current and prospective economic developments and assists in the determination of appropriate economic policies. The office is responsible for the review and analysis of domestic economic issues and developments in the financial markets.

Tax Policy develops and implements tax policies and programs, reviews regulations and rulings to administer the Internal Revenue Code, negotiates tax treaties, and provides economic and legal policy analysis for domestic and international tax policy decisions. Tax Policy also provides revenue estimates for the President's budget.

Treasurer of the United States advises the Secretary on matters relating to coinage, currency, and the production of other financial instruments. The Treasurer also serves as one of the Department's principal advisors and a spokesperson in the area of financial literacy and education.

The Community Development Financial Institutions Fund (CDFI) expands the capacity of community development financial institutions and community development entities to provide credit, capital, tax credit allocations, and financial services to underserved domestic populations and communities.

The Office of Small and Disadvantaged Business Utilization assists, counsels, and advises small businesses of all types: disadvantaged, women-owned, veteran-owned, service-disabled veteran-owned, and small businesses located in historically underutilized business zones on procedures for contracting with Treasury.

Internally, the Treasury's Departmental Offices are responsible for the overall management of the Department. The *Office of the Assistant Secretary of Management and Chief Financial Officer* is responsible for internal management and controls, and also serves as the Department's Chief Performance Officer. Support organizations include *General Counsel, Legislative Affairs, and Public Affairs*. Also, three inspectors general, the *Treasury Inspector General for Tax Administration, the Office of the Inspector General, and the Special Inspector General for the Troubled Asset Relief Program* provide independent audits, investigations, and oversight of the Department of Treasury and its programs.

Bureaus

Bureaus employ 98 percent of Treasury's workforce and are responsible for carrying out specific operations assigned to the Department.

The Alcohol and Tobacco Tax and Trade Bureau (TTB) collects excise taxes on alcohol, tobacco, and firearms that are lawfully due the government, protects consumers of alcoholic beverages through voluntary compliance programs that are based on education and enforcement to ensure a fair marketplace, and assists industry members in understanding and complying voluntarily with federal tax, product, and marketing requirements.

The Bureau of Engraving and Printing (BEP) designs and manufactures high quality notes and other financial documents that deter counterfeiting and meet customer requirements for quality, quantity, and performance.

The Bureau of the Public Debt (BPD) borrows the money needed to operate the Federal Government through the sale of marketable, savings, and special purpose U.S. Treasury securities. In addition, it accounts for and services the public debt and provides reimbursable support services to federal agencies.

The Financial Crimes Enforcement Network (FinCEN) safeguards the financial system from the abuses of financial crime, including terrorist financing, money laundering, and other illicit activity.

The Financial Management Service (FMS) provides central payment services to federal program agencies, operates the Federal Government's collections and deposit systems, provides government-wide accounting and reporting services, and manages the collection of delinquent debt owed to the U.S. Government.

The Internal Revenue Service (IRS) is the largest of the Department's bureaus and determines, assesses, and collects tax revenue for the Federal Government.

The United States Mint designs, produces, and issues circulating and bullion coins, numismatic coins and other items, Congressional gold medals, and other medals of national significance. The United States Mint maintains physical custody and protection of the nation's gold assets.

The Office of the Comptroller of the Currency (OCC) charters, regulates, and supervises national banks to ensure a safe, sound, and competitive banking system that supports citizens, communities, and the economy.

The Office of Thrift Supervision (OTS) charters, examines, supervises, and regulates federal and many state-chartered thrift associations in order to maintain their safety and soundness and compliance with consumer laws.

The Treasury Department's 2007-2012 Strategic Framework

The Treasury Department's *Strategic Framework* is a summary of our goals, objectives, and outcomes. This framework provides the basis for performance planning and continuous improvement.

	Strategic Goals	Strategic Objectives	Value Chains**	Value Chain Outcomes
FINANCIAL	Effectively Managed U.S. Government Finances	Available cash resources to operate the government	Collect Disburse Borrow Account Invest	• Revenue collected when due through a fair and uniform application of the law at the lowest possible cost • Timely and accurate payments at the lowest possible cost • Government financing at the lowest possible cost over time • Effective cash management • Accurate, timely, useful, transparent, and accessible financial information
ECONOMIC	U.S. and World Economies Perform at Full Economic Potential	Improved economic opportunity, mobility and security with robust, real, sustainable economic growth at home and abroad	Strengthen Regulate	• Strong U.S. economic competitiveness • Free trade and investment • Decreased gap in global standard of living • Competitive capital markets • Prevented or mitigated financial and economic crises
		Trust and confidence in U.S. currency worldwide	Manufacture	• Commerce enabled through safe, secure U.S. notes and coins
SECURITY	Prevented Terrorism and Promoted the Nation's Security Through Strengthened International Financial Systems	Pre-empted and neutralized threats to the international financial system and enhanced U.S. national security	Secure	• Removed or reduced threats to national security from terrorism, proliferation of weapons of mass destruction, narcotics trafficking ,and other criminal activity on the part of rogue regimes, individuals, and their support networks • Safer and more transparent U.S. and international financial systems
MANAGEMENT	Management and Organizational Excellence	Enabled and effective Treasury Department	Manage	• A citizen-centered, results-oriented, and strategically aligned organization • Exceptional accountability and transparency

** Value Chains – Programs grouped by a common purpose.

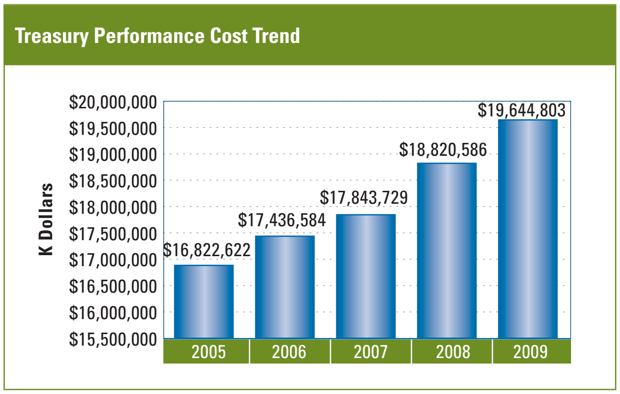
Fiscal Year 2009 Summary of Performance by Strategic Goal

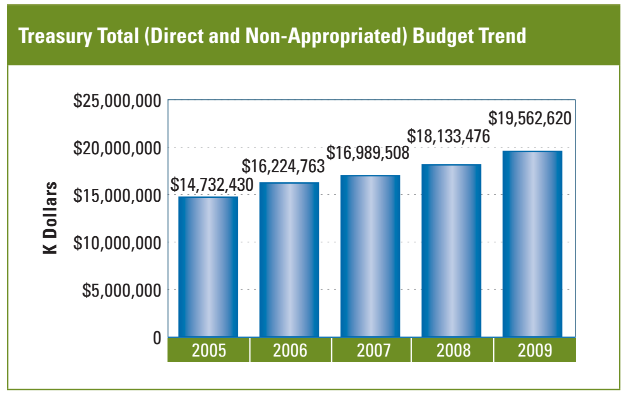
STRATEGIC GOAL	KEY ACCOMPLISHMENTS	KEY CHALLENGES	TREND
U.S. and World Economies Perform at Full Economic Potential Cost: **2008:** \$3.7 Billion **2009:** \$4.4 Billion	• Supported stabilization of the financial system through implementation of the *Emergency Economic Stabilization Act of 2008* and the Financial Stability Plan • Improved mortgage availability and stability of the housing market through implementation of the *Housing and Economic Recovery Act of 2008* • Implemented economic stimulus measures under the *American Recovery and Reinvestment Act of 2009* • Issued "Financial Regulatory Reform: A New Foundation" and drafted legislation for fundamental financial regulatory reform • Contributed to stabilization of the money market through implementation of a Temporary Guarantee Program for Money Market Funds • Implemented measures to bolster regulation of national banks and thrifts • Expanded international economic partnerships to better manage the financial crisis • Hosted G-20 meetings and supported elevation of the G-20 to premier international economic forum • Supported trebling resources for the International Monetary Fund and restructuring of the Financial Stability Forum into the Financial Stability Board • Coordinated the Economic Track of the U.S.-China Strategic and Economic Dialogue • Provided grants, investments, financial services and technical support for underserved and low-income communities through the CDFI Fund	• Repair and reform the regulatory system to improve supervision of financial markets and institutions • Continue to mitigate risks at national banks and thrifts • Reduce mortgage delinquency and foreclosure rates • Reduce direct government support for securitization and other financial markets • Maintain open economies despite rising protectionist interests • Reform Medicare and Social Security to ensure long-term solvency • Continue international movement towards a global agreement on climate change • Increase financial knowledge and access, especially in low-income and underserved communities • Improve productivity management related to coin and currency production • Improve supply management for bullion coin production • Manage cost issues related to the penny and nickel • Encourage robust circulation of the \$1 coin cost-effectively • Increase financial literacy and access to financial services in low-income and underserved communities	Performance ▼ Budget ▲ Cost ▲
Effectively Managed U.S. Government Finances Cost*: **2008:**\$14.0 Billion **2009:** \$14.4 Billion	• Collected \$2.3 trillion in tax revenue and \$20.6 billion in federal excise taxes on tobacco, alcohol, firearms, and ammunition • Processed over 144.4 million individual returns and issued over 111.4 million refunds • Increased individual electronic tax returns processed by 8 percentage points, from 58 to 66 percent • Issued over 54.8 million payments valued at more than \$13.7 billion under the *American Recovery and Reinvestment Act of 2009* • Converted over one million federal benefit check recipients to direct deposit • Conducted more than 290 auctions resulting in the issuance of more than \$8 trillion in marketable Treasury securities • Began the monthly issuance of the three and seven year notes • Collected \$5.07 billion in delinquent debt	• Continue to work toward the Congressional goal of having 80 percent of tax returns filed electronically • Continue to convert from paper to electronic savings bonds • Process 90 percent of Treasury payments and associated information electronically • Reduce the use of illegal international tax shelters • Reduce the erroneous payments rate within the Earned Income Tax Credit (EITC) program • Continue on path to complete CADE implementation by 2011 • Improve audit coverage of high net-worth/high-income taxpayers • Reduce average taxpayer telephone wait time • Accurately forecast government receipts	Performance ▲ Budget ▲ Cost ▲

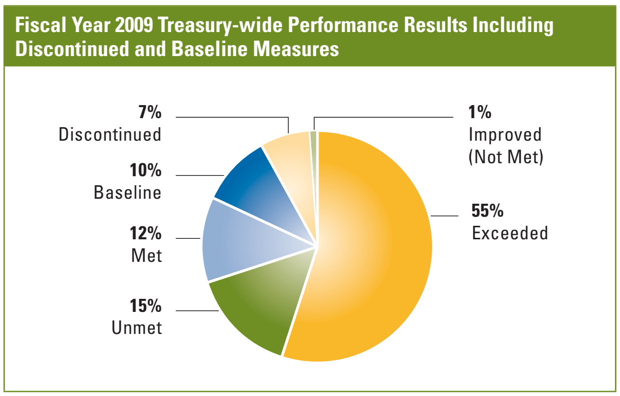
STRATEGIC GOAL	KEY ACCOMPLISHMENTS	KEY CHALLENGES	TREND
Prevented Terrorism and Promoted the Nation's Security Through Strengthened International Financial Systems Cost: **2008:** $555 Million **2009:** $570 Million	• Strengthened measures against Iran to protect U.S. national security • Enhanced mechanisms to combat mortgage and loan modification fraud • Lifted sanctions on 125 individuals or entities from the list of Specially Designated Nationals (SDNs) • Retired magnetic media filing • Strengthened the review process for foreign investment in the United States	• *Modernize Bank Secrecy Act* (BSA) information and analysis • Encourage Pakistan to make its anti-money laundering law permanent • Continue to provide additional guidance to the charitable sector • Establish external performance measure evaluation	Performance ▲ Budget ▲ Cost ▲
Management and Organizational Excellence Cost: **2008:** $508 Million **2009:** $296 Million	• Treasury OIG completed 10 Material Loss Reviews (MLRs) • Treasury OIG issued 68 audit products related to Treasury operations • Treasury Inspector General for Tax Administration issued 142 audit reports of the IRS that could produce $14.7 billion in financial benefits • Employed dynamic new approach to the 2011 Treasury budget process • Expanded human capital initiatives	• Continue to complete an increased number of MLR • Continue to improve management of information technology	Performance ▲ Budget ▼ Cost ▼

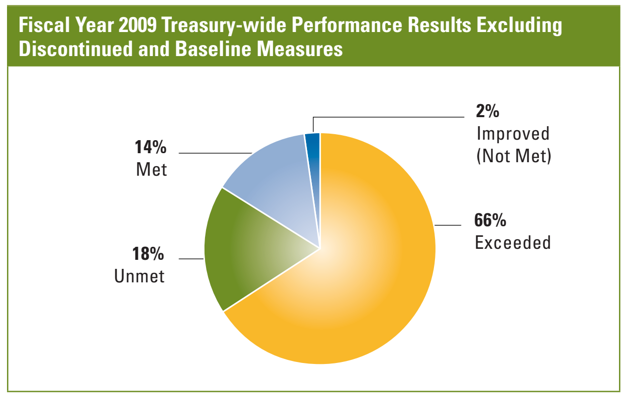
*Cost is stated as "Performance Cost," and in addition to budgetary resources, includes imputed costs, depreciation, losses, and other expenses not requiring budgetary resources.

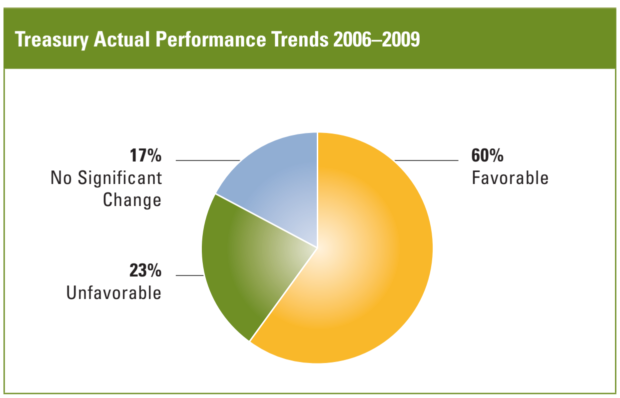
How Well is Treasury Performing?

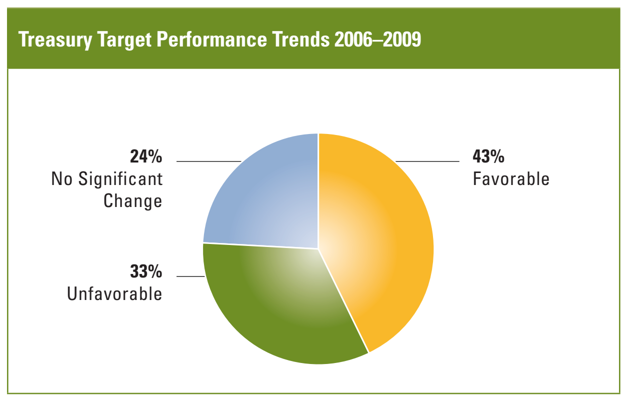


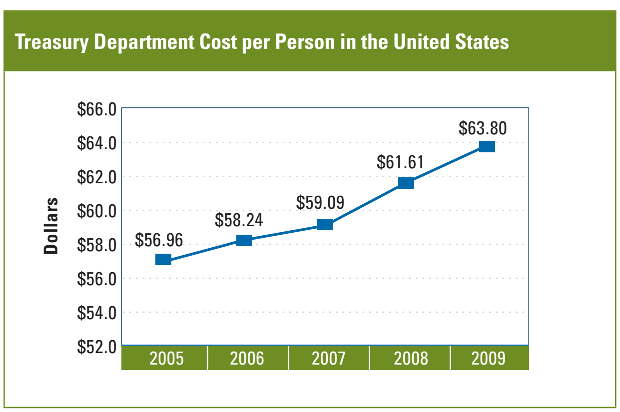


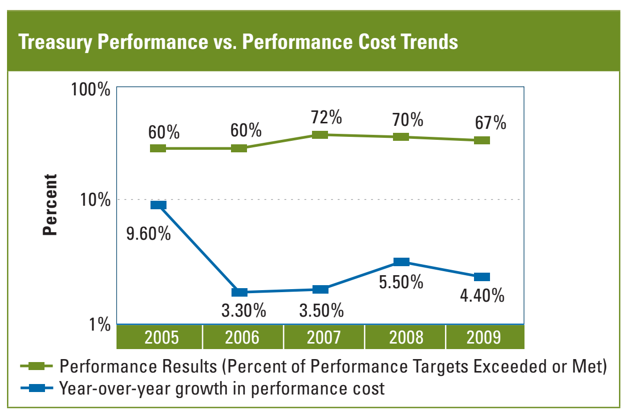












Please see next page for explanation of charts.

HOW WELL IS TREASURY PERFORMING DISCUSSION

PERFORMANCE COST AND BUDGET TRENDS

Performance cost represents the best indication of the total actual cost to operate the Treasury Department. It includes normal operating expenses from the Department's Statement of Net Cost, but also includes adjustments for costs which do not require budgetary resources such as imputed costs, depreciation, amortization, losses, and other non-budgetary expenses. Performance cost in fiscal year 2009 was $19.6 billion, a 4.4 percent increase from fiscal year 2008, and has risen 4 percent per year since fiscal year 2005. The Department's total enacted budget, however, which includes direct appropriations, non-appropriated, and reimbursable amounts, rose by an average of 7.4 percent per year since fiscal year 2005.

PERFORMANCE TO TARGET

In fiscal year 2009, the Treasury Department continued reporting using the revised performance rating system rolled out in 2008. Performance to target is rated as: Exceeded, Met, Improved from the prior year (but not met), Unmet, Baseline, or Discontinued. Prior to 2008, performance measures were rated only as met or unmet. Results are shown in two pie charts, one including all performance measures, and one not including baseline and discontinued measures. While 68 percent of targets were exceeded, met, or improved based on all measures, 82 percent of targets were exceeded, met, or improved based on measures that were not baselined or discontinued.

ACTUAL AND TARGET PERFORMANCE TRENDS

Trends in actual performance and targets have been analyzed since 2005 where data were available. Trends can move upward, downward, or remain flat. Depending on the type of measure, a trend can be favorable, unfavorable, or remain unchanged. Results indicate that 60 percent of actual performance trends were favorable, 23 percent were unfavorable, and 17 percent were unchanged. Target trends were 43 percent favorable, 33 percent unfavorable, and 24 percent unchanged.

TREASURY COST PER PERSON

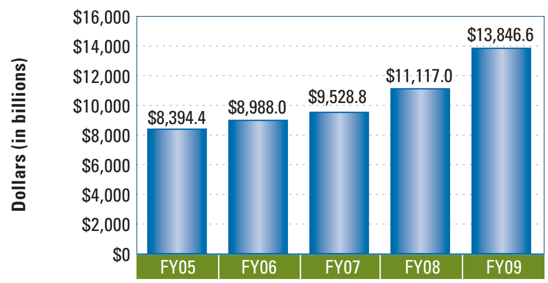
The chart reflecting the approximate cost of the Treasury Department per person in the United States is based on calculations determined by dividing Treasury Performance Cost by an estimate of the U.S. population at the end of fiscal year 2009. This ratio attempts to describe the estimated cost of operating the Treasury Department borne by everyone in the United States on a per person basis. The estimated cost per person for fiscal year 2009 is $63.80, up from $61.61 in fiscal year 2008.

TREASURY PERFORMANCE AND REAL COST

This chart provides information on Treasury's performance to target trends compared with the year-to-year increase in the Department's performance cost. The percent of targets met or exceeded dropped by two percentage points compared to the prior fiscal year, while performance cost increased by 4.4 percent.

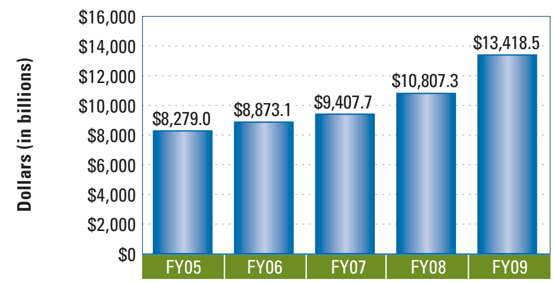
Financial Highlights

Total Assets (in billions)



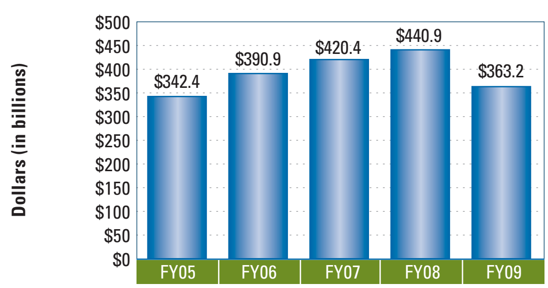
The increase of $2.7 trillion in total assets in fiscal year 2009 is largely due to the increase in future funds required from the General Fund of the U.S. Government to pay for the federal debt owed to the public and other federal agencies.

Total Liabilities (in billions)



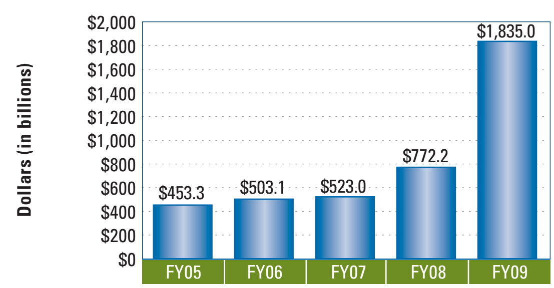
Total liabilities increased by $2.6 trillion from fiscal year 2008 to fiscal year 2009. The majority of the increase is due to borrowings from other federal agencies and debt issued to the public.

Net Federal Debt Interest Costs (in billions)



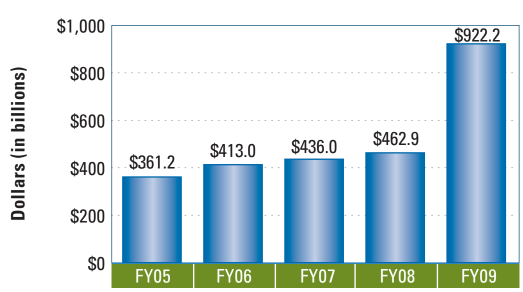
The decrease of $77.7 billion in net interest paid on the federal debt is due to the decrease in the average interest rate for debt held by federal entities and federal debt held by the public.

Total Budgetary Resources (in billions)



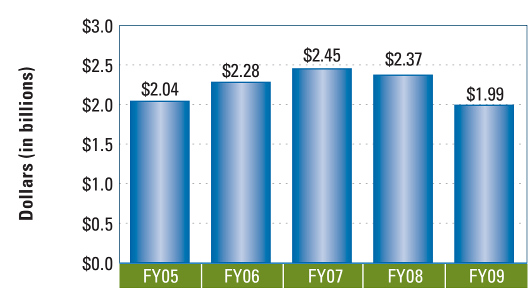
The majority of the increase in total budgetary resources for fiscal year 2009 is due to Troubled Asset Relief Program (TARP) activity and additional investments in the Government-Sponsored Enterprises.

Net Outlays (in billions)



The majority of the $459.3 billion increase in net outlays was due to Troubled Asset Relief Program (TARP) activity and additional investments in the Government-Sponsored Enterprises.

Net Custodial Revenue Received (in trillions)



Net custodial revenue collected on behalf of the U.S. Government decreased by $379.3 billion. This decrease can be contributed to the weakened economic conditions that existed during fiscal year 2009.

Fiscal Year 2009 Performance by Strategic Goal

U.S. AND WORLD ECONOMIES PERFORM AT FULL ECONOMIC POTENTIAL

Treasury remains at the forefront of the U.S. Government's response to the financial crisis and economic recession. Through implementation of the *Housing and Economic Recovery Act of 2008* (HERA), *Emergency Economic Stabilization Act of 2008* (EESA), and *American Recovery and Reinvestment Act of 2009* (Recovery Act); coordination with federal, state, and international partners; regulation of national banks and thrifts; temporary measures to stabilize money markets; and various other initiatives, Treasury worked in fiscal year 2009 to stabilize the financial system and restore economic growth. Ahead is a process of repairing and reforming the financial system to close the gaps and weaknesses in supervision and regulation of financial firms, continuing economic stabilization and stimulus, and defining an appropriate path for unwinding the government programs which have been put in place to support the economy.

TROUBLED ASSET RELIEF PROGRAM/ FINANCIAL STABILITY PLAN

On October 3, 2008, Congress passed EESA to prevent a potentially catastrophic failure of the financial system. Under the legislation, the Office of Financial Stability (OFS) was created within Treasury to purchase and insure up to $700 billion in certain types of assets under the Troubled Asset Relief Program (TARP). Operating in conjunction with Federal Reserve and FDIC programs, TARP has provided resources facilitating stabilization of the financial system and restoration of credit to businesses and consumers. For the period ended September 30, 2009, the face value of the amounts obligated under TARP was $454 billion and funds disbursed totaled $364 billion.

TABLE 1: TARP SUMMARY AS OF SEPTEMBER 30, 2009 $ IN BILLIONS

	Purchase Price or Guarantee Amounts	Total $ Disbursed	Investment Repayments	Outstanding Balance	Cash Received from Investments
Capital Purchase Program	$ 204.6	$ 204.6	$ 70.7	$ 133.9	$ 9.7
Targeted Investment Program	$ 40.0	$ 40.0	$ 0.0	$ 40.0	$ 1.9
Asset Guarantee Program	$ 5.0	$ 0.0	$ 0.0	$ 0.0	$ 0.5
AIG Investments	$ 69.8	$ 43.2	$ 0.0	$ 43.2	$ 0.0
Term Asset-Backed Securities Loan Facility	$ 20.0	$ 0.1	$ 0.0	$ 0.1	$ 0.0
Public Private Investment Program	$ 6.7	$ 0.0	$ 0.0	$ 0.0	$ 0.0
Automotive Industry Financing Program	$ 81.1	$ 75.9	$ 2.1	$ 73.8	$ 0.7
Home Affordable Modification Program	$ 27.1	$ 0.0	NA	NA	$ 0.0
Totals	$ 454.3	$ 363.8	$ 72.8	$ 291.0	$ 12.7

Some figures may not sum to total due to rounding.

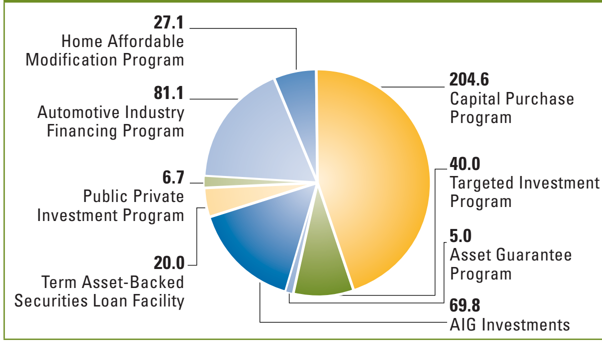
The incoming Obama Administration faced an extremely fragile financial system and deep ongoing economic recession. On February 10, 2009, Secretary Geithner announced a series of new financial programs, most of which relied on TARP, that were designed to help rebuild confidence in the financial system, draw in private capital, and restart critical channels of credit supply. These programs helped bolster confidence in financial markets on the state of the country's financial institutions and ensure the availability of essential capital support for small businesses, consumers and home owners.

TARP operations are managed with four primary goals:

- **Goal 1 –** Ensure the overall stability and liquidity of the financial system
    - a. Make capital available to viable institutions
    - b. Provide targeted assistance as needed
    - c. Increase liquidity and volume in securitization markets
  - Contributing programs:
    - Capital Purchase Program
    - Public-Private Investment Program
    - Consumer and Business Lending Initiative
      - Term Asset-Backed Securities Loan Facility
      - Unlocking Credit for Small Business Initiative
    - Targeted Investment Program
    - American International Group (AIG) Investment Program
    - Asset Guarantee Program
    - Automotive Industry Financing Program
- **Goal 2 –** Prevent avoidable foreclosures and help preserve homeownership
  - Contributing program:
    - Home Affordable Modification Program
- **Goal 3 –** Protect taxpayer interests
- **Goal 4 –** Promote transparency

The purpose of TARP was to restore the liquidity and stability of the financial system. While EESA provided the Secretary of the Treasury with the authority to spend $700 billion to meet the objectives of the Act, it is clear today that TARP will not cost taxpayers $700 billion, based on what has already been disbursed and current program estimates. The current cost estimate of the program is $69 billion, with net costs in the AIG Program, Automotive Industry Financing Program, and Home Affordable Modification Program partially offset by net gains in other programs. (See Table 2, page 19.) On December 9, 2009, Secretary Geithner certified to Congress extension of TARP authority to October 3, 2010 under Section 120(b) of EESA.

FIGURE 1. Total TARP Funds Obligated in Fiscal Year 2009 (in billions)



Capital Purchase Program (CPP)

Treasury created the Capital Purchase Program (CPP) in October 2008 to stabilize the financial system by providing capital to viable financial institutions of all sizes across the country. The program was intended to strengthen banks' capital base to enable them to absorb losses from bad assets while continuing to lend to consumers and businesses. Through the program, Treasury has provided capital to 685 financial institutions across 48 states, the District of Columbia, and Puerto Rico, including more than 300 small and community banks.

Treasury provided capital to qualified financial institutions through the purchase of senior preferred equity or subordinated debentures. Obligations were structured to encourage repayment, with dividends set at five percent for the first five years and nine percent thereafter. In addition, to participate in financial gains, Treasury received from participating institutions warrants to purchase common equity, additional preferred shares, or additional subordinated debentures. All funding recipients were subject to limitations on executive pay to protect taxpayers and encourage early repayment. Treasury initially committed over a third of total TARP funding, $250 billion, to the CPP; which was lowered to $218 billion in March 2009. Treasury is continuing to monitor CPP investments, collect dividends, and ensure compliance with contractual obligations.

As of September 30, 2009, more than 40 banks had repaid TARP investments made by Treasury, including over $70 billion in repayments. The repayments had reduced program commitments to below $135 billion. In addition, dividends and interest from CPP participants was over $6.8 billion and proceeds from the repurchase of warrants and stock was $2.9 billion. Many investments aimed at stabilizing banks are expected to deliver returns for taxpayers.

Capital Purchase Program information on ***FinancialStability.gov***.

Capital Assistance Program (CAP) and the Supervisory Capital Assessment Program (SCAP)

In early 2009, the Federal Reserve, OCC and FDIC conducted a one-time, forward-looking assessment or "stress test" (the SCAP) on the 19 largest U.S. bank holding companies. The goal was to determine whether these banks, which hold two-thirds of U.S. banking system assets, had sufficient capital to withstand losses and sustain lending through a severe economic downturn. Participant banks were encouraged to raise needed capital from private investors, with a backstop financial arrangement available through Treasury's Capital Assessment Program.

For the assessment, supervisors used historically high loss estimates on securities and loans and historically low estimates on potential earnings to determine baseline capital levels. The stress test results published on May 9, 2009 revealed that nine of the 19 banks had sufficient capital buffers while the remaining 10 banks needed to raise their capital buffers by a combined $75 billion. Since the release of the results, U.S. banks have raised over $80 billion in common equity and $40 billion in non-government guaranteed debt. Treasury had not funded any investments through CAP as of the end of fiscal year 2009.

Capital Assistance Program information on ***FinancialStability.gov***.

Public-Private Investment Program (PPIP)

To help clean up the balance sheets of major financial institutions and restore liquidity to financial markets, Treasury proposed creation of a Public-Private Investment Program to purchase legacy loans and securities under the Financial Stability Plan. Under the legacy securities PPIP program, Treasury is investing equity on a dollar-for-dollar basis with private investors in qualified Public-Private Investment Funds and providing access to debt financing for up to 100 percent of the fund's total equity. Funds are required to obtain commitments of at least $500 million in private capital to qualify and are expected to employ a predominately long-term buy-and-hold strategy. Treasury will receive pro rata any profits or losses in the funds alongside private investors. A total of nine asset managers were designated to establish funds for the program in July 2009 (selected out of 100 applicants) and the first fund closing occurred on September 30, 2009. The maximum capital commitment for the first round is $30 billion. As of September 30, 2009, no private fund managers had made any investments and Treasury had not disbursed any funds.

After announcement of the program, non-agency mortgage-backed securities (MBS) rose substantially in price. Prime fixed rate securities issued in 2006 that traded as low as $60 in March had increased in value by over 40 percent by the end of September. That improvement in financial market condition created the positive backdrop to enable introduction of the program at a smaller scale than originally envisioned. The Department will assess the need for additional rounds following the results of the first round.

Public-Private Investment Program information on ***FinancialStability.gov***.

Term Asset-Backed Securities Loan Facility (TALF)

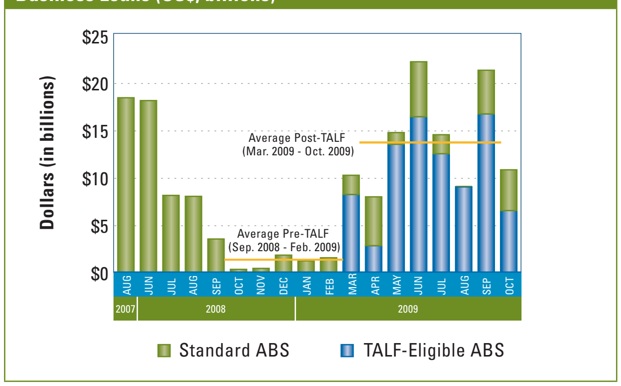
Treasury and the Federal Reserve announced creation of TALF in November 2008 to help unlock credit markets for households and small businesses. Under TALF, the Federal Reserve announced intention to lend up to $200 billion to eligible investors purchasing AAA-rated asset-backed securities (ABS) collateralized by newly and recently originated consumer and small business loans. (Including securities backed by auto loans, student loans, credit card loans, equipment loans, floorplan loans, loans guaranteed by the Small Business Administration, insurance premium finance loans, residential mortgage servicing advances, and commercial mortgage loans.) Borrowers are eligible to borrow up to the market value of the ABS, less a fixed percentage, ensuring they take the first loss if the securities lose value. Under TALF, Treasury provided up to $20 billion to the Federal Reserve in credit protection to be employed in the event of borrower default.

Prior to introduction of the program, the market for newly-issued ABS had largely shut down. Interest rate spreads on the most highly-rated AAA tranches of ABS and CMBS rose to levels outside their historical range, in certain cases well over seven to 15 times their average, respectively. The disruption of these markets contributed to the lack of credit to households and businesses of all sizes, impacting U.S. economic activity. Through October 2009, the TALF program had supported nearly $86 billion of new consumer and small business credit, including over 3.6 million consumer and small business loans and leases, and over 132 million active credit card accounts. TALF has also provided liquidity for $4.1 billion of legacy CMBS securities. This aid to the securitization market has had a clear impact on liquidity, spreads and the availability of consumer and small business credit. Since the peak of the crisis, spreads for the asset classes backed by the program have come down by 60 percent or more, including a reduction in credit card and auto loan ABS rates from six percentage points above the benchmark to only one percentage point above the benchmark.

In August 2009, Treasury and the Federal Reserve announced extension of TALF through March 31, 2010 for newly-issued ABS and legacy commercial mortgage-backed securities (CMBS) and through June 30, 2010 for newly-issued CMBS.

Term Asset-Backed Securities Loan Facility information on the ***Federal Reserve*** website.

FIGURE 2. Issuance of ABS Backed by Consumer and Small Business Loans (US$, billions)



Unlocking Credit for Small Business Initiative

To help restore the confidence needed for financial institutions to increase lending to small businesses, Treasury announced an initiative to expand securitization of small business loans on March 16, 2009. Securitization of small business loans provides community banks and other lenders with an important source of capital for additional loans. However, as a result of the severe dislocations in the credit markets, both lenders that originate loans under SBA programs and the "pool assemblers" that package such loans for securitization experienced significant difficulty selling SBA loans or securities in the secondary market. This, in turn, significantly reduced the ability of such lenders and pool assemblers to obtain funds to make new small business loans. Under the program, Treasury has planned to make up to $15 billion in TARP resources available to purchase securities backed by the SBA guaranteed portions of loans made under the SBA's 7(a) loan program, as well as first-lien mortgage securities made by private sector lenders in connection with

SBA's 504 community development loan program. (The SBA's 7(a) program is the SBA's most basic and widely used loan program.)

Since Treasury's announcement of this program, the credit markets for small businesses have improved somewhat. The secondary market for guaranteed SBA loans, for example, had essentially ceased working last fall and had only $86 million in January re-sales. That market improved notably this spring in the wake of Treasury's announcement, with $399 million settled from lenders to broker-dealers in September 2009. As a result of this improvement, as well as reluctance on the part of market participants to accept TARP funds, Treasury found that demand for its proposed program declined. As of September 30, 2009, no funds had been disbursed under the program, although funding remains available.

Unlocking Credit for Small Business Initiative on ***FinancialStability.gov.***

Targeted Investment Program (TIP)

Treasury provided assistance on a case-by-case basis to stabilize key financial institutions during the height of the financial crisis. Through TIP, Treasury sought to prevent a loss of confidence in critical financial institutions which could have resulted in significant financial market disruption. Assistance was provided through the purchase of preferred shares paying an annual dividend of eight percent. These investments impose greater reporting requirements and harsher restrictions on the companies than under CPP terms, including restrictions on dividend payments to $0.01 per share per quarter, limits on executive compensation and corporate expenses, and other measures. In addition, Treasury received warrants from participant companies to purchase common shares.

Under the TIP, Treasury purchased $20 billion in preferred shares from Citigroup in December 2008 and $20 billion in preferred shares from Bank of America in January 2009. Treasury has exchanged the preferred shares for Citigroup received under the TIP and CPP programs into common shares and trust preferred securities to strengthen Citigroup's capital base. As of September 30, 2009, Treasury had received $1.9 billion in dividends, interest and fees from holdings under the TIP program.

Targeted Investment Program information on ***FinancialStability.gov***.

AIG Investment Program

In November 2008, Treasury purchased $40 billion in cumulative preferred shares from AIG. In April 2009, the $40 billion in cumulative shares were exchanged for $41.6 billion in non-cumulative preferred shares paying a 10 percent dividend. At the same time, an equity capital facility was created providing an additional $29.8 billion as needed, of which $3.2 billion had been drawn as of September 30, 2009. The Federal Reserve provided loans to AIG and a public trust was created to hold convertible preferred shares representing 79.8 percent of the current voting power of AIG common shares. These shares are held in trust for the sole benefit of taxpayers. (The Department of the Treasury does not control the trust and cannot direct the trustees.) As of September 30, 2009, AIG had not made any dividend payments on any of the perpetual preferred stock. Subsequently, AIG failed to make a dividend payment on November 2, 2009. Per the terms of the preferred stock, if AIG misses four dividend payments, Treasury may appoint to the AIG board of directors the greater of two members or 20 percent of the total number of directors of the Company.

AIG Program information on the ***Federal Reserve*** website.

Asset Guarantee Program (AGP)

The Asset Guarantee Program was created in November 2008 to stabilize the financial system by providing guarantees against severe credit losses by large financial institutions. The AGP has been applied with extreme discretion and Treasury does not anticipate wider use of this program. Announced in January 2009, Treasury guaranteed up to $5 billion of potential losses on a $301 billion pool of loans for Citigroup. Under the program, Citigroup will absorb the first $39.5 billion of losses on the pool, with Treasury taking second loss on the next $5 billion. Additionally, Federal Deposit Insurance Corporation (FDIC) will absorb $10 billion in third losses and the Federal Reserve will provide secured loans for 90 percent of the remaining value in the pool, following FDIC and Treasury payments. The guarantee will expire in 2014 for non-residential assets and 2019 for residential assets. In return, Treasury received $4 billion in preferred shares and warrants, which have since been converted into trust preferred securities.

In January 2009, Treasury, the Federal Reserve and FDIC announced agreement to share potential losses on a $118 billion pool of loans at Bank of America. Bank of America terminated the request prior to funding, paying $425 million in fees to Treasury, FDIC and the Federal Reserve.

Asset Guarantee Program information on *FinancialStability.gov*.

Automotive Industry Financing Program (AIFP)

Treasury established the Automotive Industry Financing Program on December 19, 2008, to help prevent a significant disruption to the American automotive industry, which would have posed a systemic risk to financial market stability and had a negative effect on the economy. AIFP loans and equity investments (purchases of preferred and common shares) totaling $76 billion were provided to General Motors (GM), Chrysler and their respective financing entities. GM and Chrysler were provided funds with the requirement that they develop plans to achieve long term viability. Following finalization of the plans, GM and Chrysler conducted orderly bankruptcies (40 days for GM and 42 days for Chrysler). The U.S. Government currently holds 61 percent of common stock in GM and 10 percent of common stock in Chrysler under the program.

As an extension of AIFP, in March 2009 Treasury created an Auto Supplier Support Program providing qualified automotive supply companies financial protection on their receivables from domestic auto manufacturers. Treasury also established a Warranty Commitment Program designed to give consumers considering new car purchases confidence that their warranties from GM and Chrysler would be honored. As of July 10, 2009, the Warranty Commitment program was terminated after New GM and New Chrysler completed the purchase of substantially all of the assets of GM and Chrysler from their respective bankruptcies.

Automotive Industry Financing Program information on *FinancialStability.gov*.

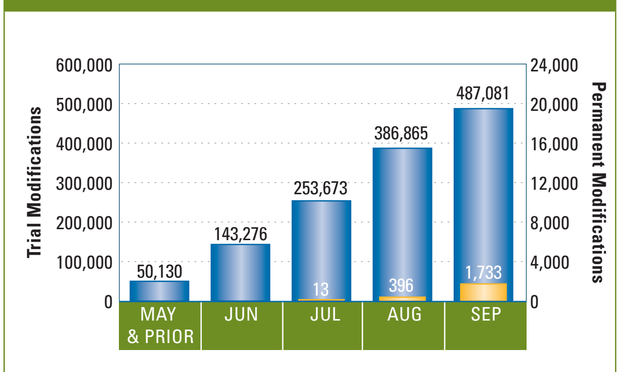
Home Affordable Modification Program (HAMP)

To mitigate foreclosures and help ensure homeownership preservation, Treasury announced the Home Affordable Modification Program in February 2009 to provide incentives for mortgage servicers, borrowers and investors to modify loans that are delinquent or at imminent risk of default. Funded jointly by EESA and HERA, with $50 billion from TARP and $25 billion from HERA, HAMP provides financial support for loan modifications which reduce a borrower's monthly mortgage payment to no more than 31 percent of their monthly gross income. Modifications are intended to provide sustainably affordable mortgage payments for responsible mortgage holders, and mitigate the spillover effects of preventable foreclosures on neighborhoods, communities, the financial system and the economy. With over 85 percent of mortgage loans in the country covered by the program, HAMP is expected to help three to four million eligible homeowners modify their mortgages on more affordable terms before the end of 2012.

At a meeting between Treasury and participating servicers on July 28, 2009, the servicers committed to reaching a cumulative target of 500,000 trial modifications by November 1, 2009. As of September 30, 2009, over 487,000 HAMP trial modifications had been completed, well on the way to achieving the target. Servicers have also agreed to work with Treasury to implement actions designed to improve program effectiveness, including streamlining application procedures. To provide transparency and servicer accountability, servicer-specific results are reported on a monthly basis on ***FinancialStability.gov*** and ***MakingHomeAffordable.gov***. Treasury is also establishing specific performance metrics to measure the performance of each servicer, such as average borrower wait time in response to inquiries and the response time for completed applications, and has implemented a "second look" review of samples of rejected applications to ensure borrower applications are not inadvertently or incorrectly denied.

Home Affordable Modification Program information on ***MakingHomeAffordable.gov***.

FIGURE 3. HAMP Loans Entering Trial and Permanent Modification



TARP accomplishments in fiscal year 2009

Viewed in conjunction with other Federal Government programs, TARP should be evaluated primarily on its impact on stabilizing the financial system. Today, the financial system and the economy are showing signs of stability. The economy grew in the third quarter and private economists generally expect moderate growth in the remainder of this year and next. The cost of borrowing has declined to pre-crisis levels for many banks, non-financial corporations, states and local governments, and the government-sponsored enterprises (GSEs). U.S. equity markets have surged, and prices for bank securities have improved significantly. Credit creation in securities markets has increased, facilitating new credit for consumers and businesses. Housing markets are also stabilizing. Home prices, as measured by the national LoanPerformance index, increased by five percent over the last six months, reversing three straight years of decline. While clear challenges remain, particularly with continuing bank failures, high foreclosure rates, high unemployment and concerns in commercial real estate markets, the worst of the crisis has passed.

The ultimate return on the TARP investments that remain outstanding will depend on how the economy and financial markets evolve. The improvement in economic and financial prospects that has already occurred has had a significant impact on the expected cost. As of September 30, 2009, the estimated cost of TARP programs is $110 billion lower than the initial estimates made at the time the programs were initiated. (See table 2.) About $10 billion of that decline in costs stems from early repayments of TARP funds. The rest of the decline is primarily a function of improvements in the economic and financial environment since TARP programs were initiated.

TABLE 2: ESTIMATED CHANGE IN COST FOR THE TARP PROGRAMS
$ IN BILLIONS

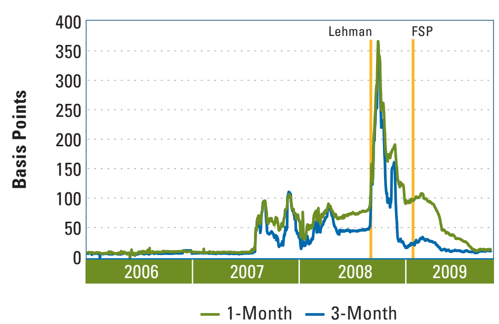
	Original Estimate[1]	Current Estimate	Net Change
Capital Purchase Program	- 57.4	+ 15.0	+ 72.4
Targeted Investment Program	- 19.6	+ 1.9	+ 21.5
Asset Guarantee Program	+ 1.0	+ 2.2	+ 1.2
AIG Investments	- 31.5	- 30.4	+ 1.1
Automotive Industry Financing Program	- 43.7	- 30.4	+ 13.3
Term Asset-Backed Securities Loan Facility	+ 0.1	+ 0.3	+ 0.2
Subtotal	**- 151.1**	**- 41.4**	**+ 109.7**
Home Affordable Modification Program	- 27.1	- 27.1	0.0
Total	**- 178.2**	**- 68.5**	**+ 109.7**

1 Original estimates completed on or near the initiation of each program. Amounts shown based on total program disbursements through fiscal year 2009.

Measuring the impact of TARP in isolation is challenging. Most TARP programs were part of a coordinated government response to restore confidence in the financial system. The health of the overall system and its impact on the U.S. economy are therefore the most important metrics by which the effectiveness of these policies can be assessed. However, a few TARP programs were uniquely targeted to specific markets and institutions, allowing for more direct assessment of performance.

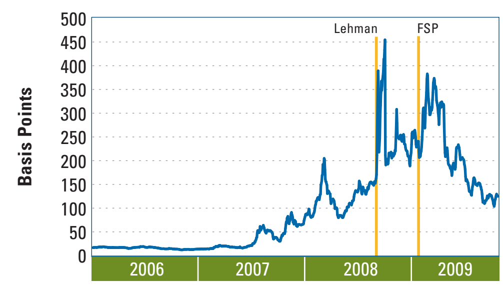
Below are several accepted indicators of financial market stress. The London Inter-Bank Offered Rate – Overnight Index Swap (LIBOR-OIS) spread measures the difference between short-term borrowing rates between banks and expected short-term borrowing rates for banks from the Federal Reserve. The spread reflects the additional risk banks perceive when lending to other banks, versus borrowing costs from the Federal Reserve. Historically, LIBOR-OIS spreads have been 0.1 percent or less. With greater stress in financial markets in October 2008, the three-month LIBOR-OIS spread spiked to 3.64 percent. At the end of the fiscal year, LIBOR-OIS spreads were 0.25 percent, within reach of historical levels.

FIGURE 4. Libor-OIS Spread (basis points)



Credit-default swap spreads for financial institutions, which measure investor confidence in their health, have also fallen significantly. A measure of credit-default swaps for the largest U.S. banks reached 450 basis points last fall, as shown in Figure 5, and is just over 100 basis points today. The TARP was a necessary step, but not the only step, to achieving this recovery.

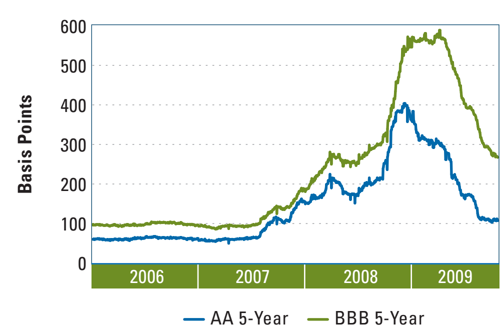
FIGURE 5. Credit Default Spreads for Financial Institutions (basis points)



Notes: Includes Bank of America, Citigroup, Goldman Sachs, JPMorgan, Morgan Stanley, and Wells Fargo.

In conjunction with lower credit default swap rates, borrowing costs have declined for many businesses. Investment-grade corporate bond rates have fallen by over 70 percent since last fall, and high-yield bond rates have fallen by more than half. Businesses have issued about $900 billion in investment-grade debt and over $100 billion in high-yield debt this year. While much of the new issuance earlier in the year was supported by the government, private investors have funded most new corporate debt in recent months.

FIGURE 6. Corporate Bond Spreads (basis points)



An indicator of borrowing costs for homeowners is the spread between the 30-year fixed mortgage rate and 10-year Treasuries. Higher spreads indicate that banks perceive greater risks in issuing mortgages and homeowners face higher borrowing costs. In mid-December

2008, the 30-year mortgage to 10-year Treasury spread reached almost 3.3 percent, its highest level since January 2002. On September 30, 2009, the spread was 1.85 percent, well below its height during the crisis.

FIGURE 7. Spread between 30 year Mortgage and 10 year Treasury Rates

Finally, the Chicago Board Options Exchange Volatility Index (VIX) is a gauge of the expected volatility of the S&P 500 equity index. The VIX is often referred to as the "Fear Index", since high levels imply investors "fear" sharp moves in the market in either direction (up or down). Historically, the VIX has ranged between 10 and 30. In November 2008 the VIX reached nearly 81, its highest level on record. On September 30, 2009, the VIX was nearly 26, still relatively high by historic levels, but well below its height during the crisis.

FIGURE 8. Market Volatility Index of S&P 500 (VIX)

Taxpayer protection and promoting transparency

In implementing EESA, Treasury has sought to carefully and assertively manage taxpayer resources. No investments have been made unless they are compliant with statutory requirements, necessary for restoring or maintaining financial stability, and structured to protect the taxpayer. Programs have been designed to achieve these objectives by:

- setting commercial terms and conditions on financial assistance;
- taking warrants to capture gains from assistance;
- requiring private capital or risk sharing;
- restricting executive compensation and other related activities;
- minimizing self-dealing and other conflicts of interest;
- managing the role of the U.S. Government as a shareholder, but only a "reluctant shareholder".

Given its unusual position in managing financial market stress, EESA designated four reviewing bodies to oversee TARP operations: a Financial Stability Oversight Board, a Special Inspector General for TARP (SIGTARP), a Congressional Oversight Panel (COP), and the Government Accountability Office (GAO). The Assistant Secretary for Financial Stability meets weekly with the SIGTARP and makes frequent reports and/or updates to Congress and the COP to ensure transparency and accountability for OFS activities. OFS involves the oversight bodies early in the design process for new programs or investments to benefit from any suggestions.

Treasury has made every effort to communicate program activities in a fully transparent and timely manner, through correspondence with oversight authorities, activity reports, testimony, speeches and publication of program information. To provide transparency and accountability for TARP and other programs designed to repair and reform the financial system, Treasury created ***FinancialStability.gov***. The website includes reports and information on Treasury programs, including transaction reports, program guidelines, speeches, press releases and other information. As of September 30, 2009, Treasury had published 86 Transaction Reports, 10 Section 105(a) monthly Congressional Reports, seven Tranche Reports, three dividend and interest reports, and two MHA Program Reports, all of which are posted on ***FinancialStability.gov***. This information is intended to answer the basic questions many Americans have about how TARP monies are invested. In keeping with principles of good stewardship, Treasury has never missed a deadline for a report. Additionally, Treasury posts program guidelines on the website within two business days of any program launch, all obligations made under TARP, and all contracts with Treasury service providers involved with TARP programs. Additional information on the Making Home Affordable program can be found at ***MakingHomeAffordable.gov***.

Managing TARP assets

Treasury manages TARP investments under several core principles:

First, the U.S. government is a shareholder reluctantly and out of necessity. The government intends to dispose of its interests as soon as practicable, with the dual goals of achieving financial stability and protecting taxpayer interests.

Second, there is no intention to be involved in the day-to-day management of any company. Government involvement in daily management of a company could possibly reduce the value of these investments, impede the ability of companies to return to full private ownership, and frustrate attainment of broader economic policy goals.

Third, consistent with these goals, the Department takes a commercial approach to the exercise of shareholder rights. Voting participation only corresponds to four core matters: board membership; amendments to the charter and by-laws; liquidations, mergers and other substantial transactions; and significant issuances of common shares.

While some new investments are still being made to support financial markets and the economy, the Administration intends to exit TARP investments as soon as prudent judgment allows.

Exiting TARP

TARP was designed as an emergency response to a major financial crisis. Because financial conditions have started to improve, Treasury has begun the process of exiting from some emergency programs. As of September 30, 2009, Treasury had received over $73 billion in principal repayments and warrant repurchases from CPP participants. For banks that have elected not to repurchase their CPP warrants, Treasury began auctioning their warrants in December 2009. In addition, many programs were structured to encourage early repayment of funds, including interest rates on preferred stock and subordinated debentures which increase over time and restrictions on executive compensation. Most TARP programs also have defined lives with clear end dates. For example, new lending under CPP is scheduled to end December 31, 2009 and TALF is scheduled to end in June 30, 2010. For investments in the automobile industry and for other companies that have received exceptional assistance, clear principles have been outlined ensuring support is limited and temporary. Specifically under AIFP, Chrysler Financial has already repaid its assistance, and an initial public offering for GM is expected next year.

The financial and economic recovery is fragile and faces significant headwinds. The unemployment rate reached 10.2 percent in October and may remain elevated for some time. Delinquencies of subprime residential mortgages reached over 26 percent and conforming mortgages nearly seven percent in the third quarter. A contraction in bank lending, particularly for smaller businesses which do not have access to bond markets, has had a significant impact on economic growth. The number of bank failures and "problem institutions" as classified by FDIC has increased significantly, and will likely remain elevated through 2010. Financial stability is a necessary precondition for the resumption of economic growth. Treasury and other institutions of government have accomplished a great deal in a short amount of time. Still, there is more work ahead. While a number of TARP initiatives have begun to wind down, Treasury continues to focus on stabilizing housing markets as well as improving access to credit for small businesses. For these reasons, Treasury determined in December 2009 to extend TARP spending authority beyond the initial expiration date of December 31, 2009. The authority to make new TARP investments will now expire on October 3, 2010, two years from the enactment of EESA, under provisions of the Act's Section 120(b).

FINANCIAL REGULATORY REFORM

On June 17, 2009, the President announced a comprehensive plan to reform an outdated and ineffective financial regulatory system. Treasury submitted proposed legislative text to implement the plan in July and August 2009, and is currently working with Congress to promulgate legislation by the end of the calendar year. The plan has five key objectives: promote robust supervision and regulation of financial firms; establish comprehensive regulation of financial markets; protect consumers and investors; provide the government with the ability to manage financial crises; and improve international cooperation.

Promote robust supervision and regulation of financial firms

Financial institutions that are critical to market functioning should be subject to strong oversight. No financial firm that poses a significant risk to the financial system should be unregulated or weakly regulated.

- *Create a Financial Services Oversight Council.* The Administration's regulatory reform plan will create a Financial Services Oversight Council to facilitate the coordination of financial regulatory policy, provide a forum for the resolution of jurisdictional disputes, and identify emerging risks in financial markets. This Council would include the heads of the principal federal financial regulators and be chaired by Treasury. The Council will replace the President's Working Group on Financial Markets and have a permanent, full-time staff at Treasury.
- *Supervise and regulate all of the largest, most interconnected financial firms.* Under the reform plan, the largest, most interconnected financial firms will be subjected to strong, comprehensive and consolidated oversight by the Federal Reserve, regardless of whether the firm owns an insured depository institution. Larger and more interconnected firms will be subjected to higher prudential standards and prompt corrective action will be required should their capital levels decline. Shareholders and creditors should bear the risks and the ultimate costs of failure, ending the implicit guarantee of public support for the largest, most interconnected financial firms.
- *Raise standards for all financial firms.* Tougher standards should be imposed on all financial firms so that the system is not compromised by the failure of one firm. Capital and liquidity requirements must be raised and exposures between financial firms should carry added capital charges. These tougher standards should incentivize firms to shrink, increase their capacity to absorb losses, and reduce their leverage, complexity and interconnectedness.
- *Establish a National Bank Supervisor and eliminate loopholes in banking regulation.* Merging the Office of the Comptroller of the Currency (OCC) and the Office of Thrift Supervision (OTS) into a National Bank Supervisor (NBS) and eliminating the federal thrift charter would streamline the regulatory system and reduce potential for regulatory arbitrage. The proposed legislation also requires the Federal Reserve, the FDIC, and NBS adopt joint rules on bank regulatory fees to eliminate arbitrage between regulators based on bank examination fees.
- *Establish an Office of National Insurance.* The regulatory reform legislation includes a proposal to establish an Office of National Insurance (ONI) to serve as an advisor to the Secretary and coordinate

and develop federal policy in the insurance sector. As part of Treasury, ONI will monitor all aspects of the insurance industry, including identifying issues and gaps in the regulation of insurers that could contribute to a systemic crisis in the insurance industry or within the broader financial system. ONI would also assist the Secretary in negotiating international insurance agreements on prudential measures.

- *Register hedge funds.* Hedge funds and other private pools of capital, including private equity and venture capital funds, will be required to register with the Securities and Exchange Commission (SEC). Due to insufficient oversight and regulation prior to the financial crisis, the government lacked the data necessary to monitor these funds' activities and assess potential risks in the market. The legislation would help to protect investors from fraud and abuse, provide increased transparency, and supply the information necessary to assess whether risks in the aggregate or risks in any particular fund pose a threat to our overall financial stability.
- *Realign executive compensation.* Treasury delivered draft "say-on-pay" legislation to Congress that would require all publicly traded companies establish non-binding shareholder votes on executive compensation packages, encouraging greater accountability and disclosure of compensation practices. In addition, the draft legislation would help ensure the independence of board compensation committees. Overall, federal standards and guidelines should better align executive compensation practices of financial firms with long-term shareholder value and prevent these practices from providing incentives that could threaten the safety and soundness of supervised institutions.

Regulatory reform information at ***FinancialStability.gov***.

Establish comprehensive supervision of financial markets

New requirements for transparency and improved risk management capacity should be built into the financial market infrastructure to improve understanding of the risks associated with new financial instruments. In addition, regulation of financial markets should be enhanced to better manage system-wide stress and the failure of one or more large institutions.

- ***Strengthen supervision and regulation of securitization markets***. Securitization, by breaking down the traditional relationship between borrowers and lenders, created conflicts of interest that market discipline failed to correct. To better align investor and issuer interests, regulation should require that originators or sponsors retain an economic stake in a material portion of the credit risk of these securitized credit exposures. The SEC should continue its efforts to increase the transparency and standardization of securitization markets and be given clear authority to require robust reporting by issuers of asset-backed securities.
- ***Strengthen credit rating agency regulation***. The Administration's financial regulatory reform effort includes legislation to increase transparency, improve oversight, and reduce reliance on credit rating agencies. Credit rating agencies often failed to accurately describe the risks associated with certain products, preventing investors from understanding the underlying risks which contributed to the severity of the crisis. The legislation includes provisions expanding transparency and disclosure requirements for credit rating agencies, establishing mandatory registration with the SEC, instituting tougher examination of internal controls and processes, and ending the practice of firms providing consulting services to companies they rate.
- ***Regulate over-the-counter derivatives markets, including credit default swaps***. One of the most significant developments in the financial sector in recent decades has been the growth and rapid innovation in credit default swaps and other

over-the-counter (OTC) derivatives. The proposed legislation will regulate OTC derivative markets for the first time. This legislation will provide regulation and transparency for all OTC derivative transactions, stronger prudential and business conduct regulation of all major participants in OTC derivative markets, and improved regulatory and enforcement tools to prevent manipulation, fraud and other abuses.

- ***Strengthen oversight of systemically important payment, clearing and settlement systems***. To mitigate systemic risk and promote financial stability, the plan proposes giving the Federal Reserve stronger statutory authority to oversee systemically important payment, clearing and settlement systems. The Federal Reserve is the only agency with sufficiently broad and deep knowledge of financial institutions and capital markets to effectively assume this responsibility. Under the Administration's plan, the Federal Reserve will be required to consult with the Financial Services Oversight Council to identify systemically important systems and set appropriate standards. In the case of clearing and settlement systems for regulated markets, the Federal Reserve will be required to coordinate its risk management oversight with the CFTC or the SEC, which will remain the primary regulators for these markets.
- ***Harmonize futures and securities regulation***. The legislation proposes to harmonize statutory and regulatory regimes for futures and securities markets to better address gaps in regulation between the CFTC and SEC.

Protect consumers and investors from financial abuse

To rebuild trust in U.S. markets, it is critical to ensure strong, consistent regulation and supervision of consumer financial services and investment markets.

- ***Create a Consumer Financial Protection Agency***. Failure of the consumer protection regime significantly contributed to the financial crisis. On June 30, 2009, the President proposed creation of the Consumer Financial Protection Agency (CFPA) to protect consumers against deceptive and unscrupulous financial practices and improve innovation, efficiency and access in the marketplace. This agency will consolidate the current fragmented regulatory regime into a single, independent federal consumer protection agency with the authority to write rules, oversee compliance, and address violations by non-bank and banking institutions.
- ***Strengthen investor protection***. The Administration's financial regulatory reform legislation includes a provision to strengthen the SEC's authority to protect investors. The legislation outlines steps to establish consistent standards of conduct and accountability for broker-dealers and investment advisors, and improve the timing and the quality of disclosures. The proposed legislation also establishes a permanent Investor Advisory Committee to ensure investor representation at the SEC.

Provide the government with the tools it needs to manage financial crises

The government should have the tools necessary to address the potential failure of a bank holding company or other non-bank financial firm when the stability of the financial system is at risk.

- ***Enhance resolution authority***. Plans should be in place to resolve the failure of any large interconnected financial firm which could threaten the stability of the financial system. Bankruptcy will remain the primary option, but the recent financial crisis demonstrates the need for enhanced resolution capacity. Major financial firms will be required to develop rapid resolution plans to better prepare for the potential of failure. This authority will also give Treasury the ability to appoint FDIC or SEC as conservator for a failing firm that poses a threat to the system. Under the legislation, the Federal Reserve would be required to receive prior written approval from the Secretary of the Treasury before providing emergency lending under its "unusual and exigent circumstances" authority.

Raise international regulatory standards and improve international cooperation

As witnessed during the financial crisis, problems in any single country can easily and quickly spread across borders. As financial regulatory reform progresses within the United States, stronger standards need to be established across global markets to ensure international financial stability.

- ***Enhance international cooperation and reform of global financial markets***. To ensure that U.S. safeguards are not undermined abroad, the U.S. Government has taken the lead in calling for strong, modern regulation and supervision around the world through the G-20, the Financial Stability Board, the Basel Committee on Banking Supervision, and other organizations. Led by the United States, the leaders of the Group of Twenty (G-20) pledged to take action to build a stronger, more globally consistent supervisory and regulatory framework to oversee today's international markets. The United States is seeking consensus on four core issues: regulatory capital standards, oversight of global financial markets, supervision of internationally active financial firms, and crisis prevention and management.

TREASURY HOUSING GOVERNMENT-SPONSORED ENTERPRISE PROGRAMS

To provide stability to the financial markets, increase the availability of mortgage finance and protect taxpayer interests, Treasury implemented three emergency programs in September 2008 with respect to Fannie Mae, Freddie Mac and the Federal Home Loan Banks (FHLBs). Authority for the action was provided by Section 1117 of the Housing and Economic Recovery Act of 2008, which authorized Treasury to purchase obligations and other securities issued by Fannie Mae, Freddie Mac and any FHLB. The programs include:

- Preferred Stock Purchase Agreements (PSPAs) with Fannie Mae and Freddie Mac providing backstop funding for program operations
- A Mortgage-Backed Securities (MBS) Purchase Program limited to securities issued by Fannie Mae and Freddie Mac
- An emergency credit facility for Fannie Mae, Freddie Mac and the FHLBs

Preferred Stock Purchase Agreements

The PSPAs were created to instill confidence in investors that Fannie Mae and Freddie Mac would remain viable entities critical to the functioning of the housing and mortgage markets. Investors purchased securities issued or guaranteed by Fannie Mae and Freddie Mac in part because ambiguities in their Congressional charters created a perception of government backing. These ambiguities fostered enormous growth in the obligations issued or guaranteed by Fannie Mae and Freddie Mac, which by the scale and breadth of public holdings eventually posed a systemic risk to global financial markets in the event of their failure. The focus of the PSPAs is to enhance market stability by providing additional security to holders of Fannie Mae and Freddie Mac securities to avoid a mandatory triggering of receivership. Because the U.S. government created these ambiguities, it had a responsibility to both avert and ultimately address this systemic risk. In February 2009, the PSPAs were increased from $100 billion per GSE to $200 billion per GSE to provide additional security for financial markets. As of September 30, 2009, Fannie Mae and Freddie Mac had utilized $95.6 billion dollars of the $400 billion set aside under the PSPAs.

GSE MBS Purchase Program

The GSE MBS Purchase Program was created to help support the availability of mortgage credit by temporarily providing additional capital to the mortgage market. By purchasing these securities, Treasury has sought to broaden access to mortgage funding for current and prospective homeowners as well as to promote market stability.

Program priorities:

- Support mortgage availability for both current and prospective homeowners
- Promote secondary market stability
- Ensure zero principal loss on outlays

As of September 30, 2009, Treasury had purchased $192.2 billion in agency MBS and received back $22.2 billion in principal and $5.0 billion in interest.

GSE Credit Facility

The GSE Credit Facility was created to ensure credit availability to Fannie Mae, Freddie Mac, and the FHLBs by providing secured funding on an as-needed basis under terms and conditions established by the Treasury Secretary. Funding is provided directly by Treasury from its general fund held at the Federal Reserve Bank of New York in exchange for eligible collateral limited to guaranteed MBS issued by Fannie Mae and Freddie Mac and advances made by the FHLBs. Loans will be for short-term durations, but would in general be expected to be for between one week and one month. To date, this facility has not been used. The facility is scheduled to be terminated on December 31, 2009.

TEMPORARY GUARANTEE PROGRAM FOR MONEY MARKET MUTUAL FUNDS

At the height of the crisis in September 2008, Treasury established a Temporary Guarantee Program for Money Market Mutual Funds to provide stability in the wake of the failure of Lehman Brothers and well-publicized troubles at several large funds. Program participants were charged a fee of four to six basis points on an annualized basis, with coverage provided to guarantee maintenance of each fund's typical stable share price of $1. Eligibility was open to all money market mutual funds regulated under Rule 2a-7 of the *Investment Company Act of 1940* and registered with the SEC, upon payment of an up-front participation fee and satisfaction of certain criteria related to their net asset value on September 19, 2008. Shortly after its inception, the program provided guarantees to 93 percent of the money market mutual fund market, covering $3.62 trillion in assets. At its expiration, utilization had fallen to 68 percent of the market. Treasury had no losses under the program and in fact earned the U.S. Government $1.2 billion in fees.

The program expired on its scheduled end date of September 18, 2009 under improved general market conditions and restored confidence in the money market industry.

EXPANDED INTERNATIONAL ECONOMIC PARTNERSHIPS

Managing financial crises, trade flows, financial security, climate change, and aid for developing economies in a global economy requires coordination with international partners. In all of these areas, Treasury worked with international partners to improve joint stewardship of the global economy. Throughout the financial crisis, Treasury officials have been in constant communication with international colleagues, showing clear and compelling results. Treasury helped facilitate international cooperation in responding to the global financial crisis, averting a more serious economic downturn, and anchoring the largest, most coordinated fiscal and monetary stimulus ever undertaken.

Demonstrated U.S. leadership at G-20 meetings

The G-20 is a multilateral forum bringing together the leaders from the 20 largest economies in the world, accounting for 85 percent of world output. At the G-20 Summits in Washington (November 2008), London (April 2009), and Pittsburgh (September 2009), Treasury took a lead role in developing a dynamic global recovery formula and securing G-20 leaders' commitments on measures to combat the economic and financial crisis. Through these summits, G-20 members agreed to pursue a globally-coordinated policy response to stabilize the financial system and provide monetary policy support, fiscal stimulus, and emergency capital for emerging and developing economies. In addition to coordinating national fiscal and monetary policies, major accomplishments included decisions to:

- Treble resources for the IMF from $250 billion to $750 billion, enabling it to provide emergency loans to countries adversely affected by the financial crisis
- Restructure the Financial Stability Forum into the Financial Stability Board, by adding G-20 members not previously part of the Financial Stability Forum, broadening its capacity to manage global banking regulation and supervision
- Establish a *Framework for Strong, Sustainable, and Balanced Growth*, formulated around peer reviews of national economic policies and regulatory standards to collaboratively identify and prevent imbalances in the global economy
- Establish processes to ensure that all systemically important financial institutions, markets and instruments are subject to appropriate regulation
- Improve coordination in international crisis management
- Determine common rules for compensation practices at large financial institutions
- Improve international accounting standards
- Jointly manage concerns related to tax havens and non-cooperative jurisdictions
- Jointly manage oversight of credit rating agencies

At the G-20 summit in Pittsburgh, the leaders announced that the G-20 would replace the G-7 as the main economic council of wealthy nations. Through the G-20 process, Treasury has participated in developing a strong multilateral system to coordinate a global policy response to reverse the economic slide and do what is necessary to restore public confidence, economic growth, and job creation.

Deepened U.S. engagement with key emerging market and priority countries

Given that the global economy is increasingly impacted by emerging market countries, more inclusive representation in international bodies is essential for long-term global recovery and growth. Treasury strongly supported the transition from reliance on the G-7 negotiation process to the G-20 process, the trebling of the IMF's resources, and creation of the Financial Stability Board. Treasury also supported quota reforms at the World Bank and IMF to allow greater participation by developing nations and increased financial support for multilateral development banks (MDBs) that will boost lending by $100 billion over the next three years. To manage key partnerships, the Treasury Department has established bilateral strategic dialogues with China, India, Russia, Afghanistan, Pakistan and Iraq. (The U.S.-China Strategic and Economic Dialogue is discussed in a following section.)

Promoted free international trade and investment

Treasury promoted open investment policies at home and for U.S. investors abroad through bilateral and multilateral outreach. Announcement of the intention to complete the Doha Round of World Trade Organization negotiations by the end of 2010 increased activity in fiscal year 2009 surrounding trade negotiations. Treasury staff participated in the launching, negotiation or implementation of 15 trade and investment agreements, including free trade agreements with Oman, Costa Rica and Peru; the Trans-Pacific Agreement; the Asia-Pacific Economic Cooperation cross-border services initiative; and the Mauritius Bilateral Investment Treaty. Treasury has supported efforts by G-20 leaders to refrain from new protectionist measures and keep markets open. Finally, Treasury played a key role in establishing the U.S.-EU Investment Dialogue and the U.S.-China Investment Forum to discuss high-priority investment issues, and efforts to codify investment criteria for sovereign wealth funds.

U.S.–China Strategic and Economic Dialogue

In April 2009, President Barack Obama and Chinese President Hu Jintao announced the establishment of the U.S.-China Strategic and Economic Dialogue (S&ED). The Dialogue provides an overarching framework bringing together the two countries' highest-level officials to address a range of critical bilateral and global economic, environmental and diplomatic issues. In fiscal year 2009, the Dialogue contributed to coordinated monetary and fiscal policy actions to restore growth and the successful restructuring of multilateral economic institutions. The S&ED builds on its predecessor, the Strategic Economic Dialogue (SED), which was created in 2006, and includes two tracks, one economic track led by Secretary Geithner, and a strategic track led by Secretary Clinton. The last meeting of the S&ED was held in Washington in July 2009. The next meeting will be held in Beijing in 2010.

Supported a Global Agreement on Climate Change

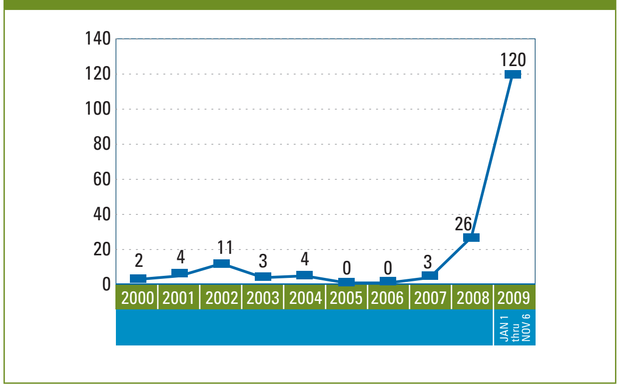
With the parties to the United Nations Framework Convention on Climate Change scheduled to meet in Copenhagen in December 2009, Treasury is working closely with other federal agencies and international partners to secure an effective global agreement. Treasury's efforts were critical to establishing and launching the Climate Investment Funds, two new multilateral trust funds hosted by the World Bank that promote clean energy in developing countries, and establishment of an Experts Group on Climate Finance at the G-20. The Clean Technology Fund (CTF), the first of the two new funds, aims to reduce global emissions growth by helping to close the price gap in developing countries between dirtier conventional technologies and commercially available cleaner alternatives. The CTF is currently co-chaired by the Treasury's Deputy Assistant Secretary for Environment and Energy.

CONTINUED EFFORTS TO BOLSTER REGULATION OF NATIONAL BANKS AND THRIFTS

OCC and OTS are the primary regulators of national banks and thrifts, respectively. Given continuing concerns about the soft economy and bank solvency following the financial crisis, both made extensive efforts to monitor evolving conditions at financial institutions they regulate and implement measures intended to restore financial health. In fiscal year 2009, the Inspector General again indicated regulation of national banks and thrifts as a Management Challenge.

Despite efforts to identify and correct potential issues at an early stage, a number of national banks and thrifts were closed by federal regulators in fiscal year 2009 due to difficult market conditions. In total, 107 financial institutions regulated by FDIC with $111.3 billion in deposits failed over the year. Of these, 13 were national banks with $14.8 billion in deposits, 14 were federal thrifts with $35.8 billion in deposits, and 80 were state banks with $60.8 billion in deposits. Work-out solutions, whereby some or all deposits and assets were assumed by another existing bank, were arranged by FDIC and regulators for almost all failed institutions.

FIGURE 9. Failed Banks in USA from 2000-2009



OCC and OTS supervisory activities in fiscal year 2009 focused on monitoring and responding to adverse conditions in credit and financial markets. OCC's on-site supervisory assessments focused on the quality of national banks' credit risk management practices (including effective credit risk rating systems and problem loan identification), adequacy of loan-loss reserves, and effective loan work-out strategies. Primary emphasis was placed on ensuring the strength of capital buffers to weather earnings pressures and asset quality deterioration. Other critical areas included sound liquidity risk management through diversified funding sources and realistic contingency funding plans, and maintenance of consistent underwriting standards regardless of intent to hold or sell a loan. OTS examinations emphasized assessment of risk management structures, liquidity plans, capital management, concentration risk and maintenance of strong underwriting standards. Given the natural exposure of thrifts to the real estate market, OTS utilized the Net Portfolio Value model (enhanced in 2008) extensively to value financial instruments and evaluate interest risk related to real estate and other investments. (Thrifts are required to hold 65 percent of their holdings in mortgages.) For troubled institutions, OCC and OTS employed a number of remedial measures, including Prompt Corrective Action determinations when institution capital deteriorated below specified thresholds, requirements to increase available capital and liquidity, required changes in bank management, and required approval for changes in business plans. To combat mismanagement, formal enforcement actions such as cease-and-desist orders, removal or prohibition orders, civil money penalties and formal agreements were utilized. In severe cases, financial institutions were required to enter into sales, mergers, liquidation or enter FDIC receivership.

To minimize real estate losses and avoid unnecessary foreclosures, both agencies encouraged financial institutions and at-risk mortgage holders to work constructively to find effective work-out solutions. Both OCC and OTS urged adoption of loan modification programs and other foreclosure mitigation practices and provided information for consumers on ways to identify and avoid foreclosure fraud. In November 2008, the federal banking agencies issued the *Interagency Statement on Meeting the Needs of Creditworthy Borrowers*, providing guidance to financial institutions on managing mortgage delinquency. OCC and OTS worked closely with HUD and other Treasury officials to develop the Making Home Affordable Program, including establishing transparent capital standards for treatment of mortgage loans modified under the program to encourage bank participation. OCC was also actively involved in identifying potential bank responses to the foreclosure crisis, including working with community development organizations to rehabilitate foreclosed properties and working with HUD to stabilize neighborhoods.

In fiscal year 2009, OCC's Annual Survey of Credit Underwriting Practices indicated a continuation of tighter underwriting standards begun in mid-2007. In contrast with the period of "originate and sell", where banks originated loans and then sold them to other investors, survey results showed that the majority of banks applied the same tight underwriting standards regardless of intent to hold or sell. With increased weakness in commercial real estate markets, both agencies warned of the accumulating risks in many small and medium-sized institutions' portfolios. At an inter-agency level, both OCC and OTS have worked directly with the Federal Reserve and FDIC to review large syndicated loans held by multiple banks through the Shared National Credit Program. This year's review covered 8,955 credit facilities with commitments totaling $2.9 trillion. OCC and OTS will continue to coordinate their licensing and supervisory procedures with other federal agencies to keep regulations current, transparent and supportive of financial industry stability and growth.

OCC and OTS have issued direct warnings to financial institutions of the risks posed by excessive asset or liability concentrations in their portfolios. During the last four years, OCC has conducted asset quality reviews of all the OCC community and mid-sized banks with significant commercial real estate concentrations, to ensure they have adequate credit underwriting, problem loan identification, and loan-loss reserves. More recently, the federal banking agencies issued guidance on managing concentration risks that may emerge from correspondent banking relationships, to reduce any carryover effect from one bank's failure.

Given the global nature of the financial crisis, OCC and OTS worked closely with both domestic and international banking supervisors to identify problems and coordinate actions to restore functioning markets and strengthen risk management. The Federal Reserve, OCC and SEC worked with key global regulators and market participants to strengthen operational infrastructure and processes used to oversee OTC derivatives. OCC was actively involved in developing and implementing a package of measures announced by the Basel Committee of Banking Supervisors in July 2009 to capture the credit risk of complex trading activities and institute higher capital requirements for certain activities. OCC and OTS also joined other global supervisors in endorsing the Basel Committee's *Principles for Sound Liquidity Risk Management and Supervision*, underscoring the importance of liquidity management. Through the Financial Stability Board's Working Group of Provisioning, chaired by the Comptroller of the Currency, OCC has actively promoted use of credit valuation processes to reduce the pro-cyclicality of loan-loss requirements. During the year, OCC and OTS provided significant support for TARP, including reviewing financial institutions' Capital Purchase Program (CPP) applications; participating on the TARP CPP Council (which provides advisory support to OFS); conducting "stress tests" for regulated entities; providing legal analysis on financial institution participation in TARP; and establishing credit rules promoting use of the Making Home Affordable Program. OCC and OTS also continued to jointly issue the Mortgage Metrics Report, providing detailed information on 34.7 million mortgages serviced by their regulated institutions, including new sections in 2009 on loan modifications.

To strengthen its unfair or deceptive acts and practices rules, OTS, Federal Reserve and National Credit Union Association issued final rules in December 2008 governing practices for credit cards and overdraft protection programs. For credit cards, these addressed unfair practices in the areas of providing reasonable time periods for making payments, payment allocations, interest rate increases on outstanding balances, security deposits and fees charged to an account prior to the issuance of credit.

PROVIDED ASSISTANCE TO LOW-INCOME AND UNDERSERVED COMMUNITIES

The Community Development Financial Institutions (CDFI) Fund expands the capacity of financial institutions to provide credit, capital, and financial services to underserved populations and low-income communities. With the economic downturn, demand for the Fund's services increased as mainstream lenders reduced lending activities. At the same time, constrained debt and equity markets limited CDFIs' access to private capital. To address the shortfall, Treasury increased funding through the CDFI program in fiscal year 2009 to help meet demand. This year, the CDFI Program competitively made 194 awards totaling $160.8 million (including $98 million in Recovery Act awards) to CDFIs and Native American CDFIs for loans, investments, financial services, and technical assistance (a 158 percent increase over fiscal year 2008). Under the New Markets Tax Credit Program (NMTC), which provides tax credit allocation authority to designated financial institutions for investments in low-income communities, Treasury awarded $6.5 billion in fiscal year 2009 (including $3 billion in Recovery Act awards), compared with $3.5 billion in fiscal year 2008, a nearly 86 percent increase. Treasury will continue to provide funding through the CDFI program to mitigate tight capital conditions in underserved markets.

MANAGEMENT OF CURRENCY AND COIN MANUFACTURING IN TODAY'S ECONOMY

Record low demand for currency and coins

The economic and financial crises significantly affected note and coin demand in fiscal year 2009. Manufacturing of currency notes experienced a 1.5 billion unit (19.5 percent) reduction in quantity ordered by the Federal Reserve, a drop from 7.7 billion notes in fiscal year 2008 to 6.2 billion notes in fiscal year 2009. This reduction in the Federal Reserve order was large enough to increase BEP's average cost per note produced by 7 percent over the prior fiscal year. The U.S. Mint shipped an estimated 5.2 billion coins, down from 10.0 billion in fiscal year 2008, representing a 45-year low for coin demand. As a result, the U.S. Mint transferred $475 million to the Treasury General Fund in fiscal year 2009, significantly lower than the $750 million transferred in fiscal year 2008. To compensate for weak demand, both the U.S. Mint and BEP are optimizing manufacturing and administrative efficiencies, focusing on maintenance, capital improvements, and employee cross-training.

Responding to record high demand for bullion products

As the economy and financial markets weakened, investors sought the perceived safety of precious metals. U.S. Mint revenue from the sale of gold, platinum, and silver bullion products increased by 79 percent in fiscal year 2009, from $949 million in fiscal year 2008 to $1,695 million in fiscal year 2009. However, these record-breaking demand levels and successful sales efforts in the bullion product line posed a new set of challenges. The number of bullion coins produced by the U.S. Mint was constrained in fiscal year 2009 by limited availability of precious metal blanks from suppliers. These constraints compelled the U.S. Mint to suspend the sale of certain bullion coins during the fiscal year. In order to satisfy its legislative mandate to fulfill public demand for bullion products, the U.S. Mint shifted available blank supply to production of bullion coins from proof coins and worked with suppliers to augment blank volumes and sources. Subsequent increases in allocation and ordering limits towards the end of the year allowed the U.S. Mint to satisfy all investor demand for 22-karat one-ounce gold and silver bullion coins by the third quarter of fiscal year 2009. However, at the end of the fiscal year, one-ounce gold and silver eagle proof coins remained unavailable.

Completion of the most ambitious currency redesign in U.S. history

The redesign of the $100 note will mark the completion of a multi-year initiative to implement the most ambitious currency redesign in United States history. Finalized and presented for approval in fiscal year 2009, BEP expects to produce and deliver 2.4 billion redesigned $100 notes in fiscal year 2010. In cooperation with the Federal Reserve, BEP administers a public education program to support the introduction of new currency designs. To maintain trust and confidence in U.S. currency, BEP is continuously engaged in improving note design to keep the nation's currency a step ahead of counterfeiters. While no specific timetable has been set, the next currency redesigns will include improvements to the nation's currency to better serve the blind and visually impaired.

Implementing the Presidential and Native American $1 Coin Acts

The *Presidential $1 Coin Act* (Public Law 109-145) and the *Native American $1 Coin Act* (Public Law 110-82) mandate that the U.S. Mint take cost-effective measures to identify, analyze and overcome barriers to circulation of $1 coins. The increased circulation of $1 coins could save the Federal Government money because $1 coins last longer than $1 notes. A four-city pilot focusing on new messaging and retail activation showed American acceptance of $1 coins is growing. However, despite U.S. Mint advertising campaigns, consumer acceptance of $1 coins has remained low and inventories at the Federal Reserve Bank have continued to rise.

AMERICAN RECOVERY AND REINVESTMENT ACT

The *American Recovery and Reinvestment Act of 2009* (Recovery Act) was signed into law on February 17th, 2009. The Recovery Act is an unprecedented effort to jumpstart the economy, create or save millions of jobs, and address long-neglected challenges. It includes extraordinary measures to modernize the nation's infrastructure, enhance energy independence, expand educational opportunities, preserve and improve affordable health care, and provide tax relief. Of the $787 billion provided through the Recovery Act, Treasury is managing programs that will contribute over $300 billion in benefits to the American people through the year 2019.

Making Work Pay credit. Taxpayers can receive this benefit through a reduction in the amount of federal income tax that is withheld from their paychecks, or through claiming the credit on their tax returns. It is estimated that over 120 million households will benefit from this provision through 2010.

Expanded tax break for 2009 first-time home-buyers. Taxpayers who qualify for the First-Time Homebuyer Credit and purchase a home this year before December 1 may claim a maximum $8,000 credit on their 2009 tax return. The estimated benefit claimed by 479,622 taxpayers through fiscal year 2009 was over $3.5 billion. The credit has been extended through April 30, 2010, with closing required by June 30, 2010.

American Opportunity Credit. Under the Recovery Act, more parents and students will qualify over the next two years for a tax credit, the American Opportunity Credit, to pay for college expenses. The new credit modifies the existing Hope Credit for tax years 2009 and 2010, making the Hope Credit available to a broader range of taxpayers, including many with higher incomes and those who owe no tax. It also adds required course materials to the list of qualifying expenses and allows the credit to be claimed for four post-secondary education years instead of two. The full credit is available to individuals whose modified adjusted gross income is $80,000 or less, or $160,000 or less for married couples filing a joint return. The credit is phased out for taxpayers with incomes above these levels. Many of those eligible will qualify for the maximum annual credit of $2,500 per student. The estimated benefit in 2009 is $328 million.

COBRA health insurance continuation premium subsidy. To help people maintain health care coverage, the Recovery Act provides a 65 percent subsidy for COBRA continuation premiums for themselves and their families, up to nine months, for workers who have been involuntarily terminated. Eligible workers are required to pay 35 percent of the premium to their former employers. Employers are required to pay the full premium, but are entitled to a credit of 65 percent on their payroll tax return. To qualify, a worker must have been involuntarily terminated between September 1, 2008 and December 31, 2009. Over $313 million in COBRA credits have been claimed by employers through fiscal year 2009.

Build America Bonds. State and local governments issuing taxable bonds are eligible to receive direct federal subsidies of 35 percent of bond interest. Through September 30, 2009, over $35.6 billion in Build America Bonds had been issued to help finance projects across the nation, including schools, utilities, public safety and transportation.

Sales tax deduction for vehicle purchases. Taxpayers can deduct state and local sales and excise taxes paid on the purchase of new cars, light trucks, motor homes and motorcycles through 2009.

Economic recovery payments. The Recovery Act provided $250 one-time economic recovery payments to eligible retirees, veterans and other high-need recipients. FMS, in coordination with the Social Security Administration, the Railroad Retirement Board, and the Department of Veterans Affairs, issued over 54.9 million economic recovery payments to beneficiaries, totaling more than $13.7 billion.

Community Development Financial Institutions (CDFI) awards. The CDFI Fund makes monetary awards (grants, loans and other investments) on a competitive basis to certified CDFIs. The Recovery Act appropriated $98 million to expand funding for the CDFI and Native American CDFI Assistance (NACA) programs. All $98 million was awarded to CDFI recipients by July 1, 2009.

New Markets Tax Credit (NMTC). The NMTC Program, administered by the CDFI Fund, facilitates investment in low-income communities by permitting credits against federal income taxes for equity investments in designated Treasury-certified Community Development Entities (CDEs).

CDEs are required to use substantially all NMTC proceeds to make loans and investments in businesses and real estate developments in low-income and distressed urban and rural communities. The Recovery Act provided a total of $3 billion for the credits. The first NMTC award of $1.5 billion was allocated in May 2009 to 32 organizations. The second allocation of $1.5 billion was awarded in October 2009 to 24 organizations.

Health Coverage Tax Credit (HCTC). HCTC was created to help displaced workers and retirees who have lost their jobs due to promulgation of free trade agreements. The Trade Adjustment Assistance Reform Act of 2002 created HCTC to assist eligible beneficiaries between the ages of 55 and 64 receive affordable health care. The program originally provided a refundable tax credit for 65 percent of the cost of qualified insurance. In May 2009, the tax credit was increased from 65 percent to 80 percent of qualified health insurance premiums, allowing participants to only pay 20 percent for health insurance each month. The increased credit expires on December 31, 2010. The number of new enrollees has increased more than four times since April 2009, to over 6,000 recipients.

Payments for Specified Energy Property in Lieu of Tax Credits. Because of the impact of current economic conditions on taxable income, the value of energy property tax credits to investors who finance renewable energy projects has decreased. Designed with the Department of Energy, this program's objective is to provide an alternative means to attract financing for renewable energy projects by providing direct payments in lieu of tax credits. The program began accepting applications on July 31, 2009 and by September 30, 2009 had made awards for 37 projects totaling more than $1 billion. The high demand for this program is expected to continue in fiscal year 2010.

Payments for Low-Income Housing Projects in Lieu of Tax Credits. Current economic conditions have severely undermined the effectiveness of tax credits intended to attract private capital investment for the construction, acquisition or rehabilitation of qualified low-income housing projects. The Recovery Act gives state housing credit agencies the choice to receive cash assistance for all or a part of their 2009 low-income tax credit allocation. Through September 30, 2009, the Department has received 57 applications and approved payments to 40 state housing agencies for over $2.5 billion. However, only $29 million has been drawn down so far. Initial feedback suggests that states are evaluating their financial capacity and determining how to provide funding needed to complete qualifying projects.

EFFECTIVELY MANAGED U.S. GOVERNMENT FINANCES

The Treasury Department manages the nation's finances by collecting money due to the United States, making its payments, managing its borrowing, investing when appropriate, and performing central accounting functions. With the financial crisis and recession, fiscal year 2009 provided unique challenges in implementing Recovery Act provisions, forecasting government receipts, and conducting a record number of auctions of government securities. Treasury continues to focus on its ongoing efforts to increase the total volume of electronic payments and receipts and improve taxpayer service and enforcement.

TAX RETURNS FILED ELECTRONICALLY

In fiscal year 2009, Treasury processed 144.4 million individual returns and issued 114.4 million refunds totaling $339.6 billion. Sixty-six percent of individual returns were filed electronically, up from 58 percent in fiscal year 2008. Although this is a clear improvement, Treasury has not yet reached the Congressional goal of 80 percent of tax returns filed electronically. Treasury continues to promote the use of the IRS Free File program and engage in national and local outreach efforts to increase electronic filing by businesses and tax return preparers.

IMPROVED SERVICE TO MAKE VOLUNTARY TAX COMPLIANCE EASIER

Treasury makes every effort to ensure that taxpayers have access to the necessary information and support to meet their tax obligations. In fiscal year 2009, the IRS fielded over 107 million taxpayer calls. The second "Super Saturday" tax information event was held on March 21, 2009, providing on-site support at more than 250 local IRS offices and 1,700 Volunteer Income Tax Assistance (VITA) sites. Over the year, 82,000 volunteers at the VITA and Tax Counseling for the Elderly sites helped file over 3 million returns and provided face-to-face assistance to 3.4 million taxpayers. To track their refunds, more than 54 million taxpayers used the online service "Where's My Refund?", an increase of 39 percent over 2008. Outreach efforts and service locations for U.S. overseas taxpayers were increased to facilitate information availability and support. IRS is making every effort to restore its level of service, which dropped from 82 percent in 2007 to 53 percent in 2008, due largely to increased volume of inquiries related to economic stimulus payments. The level of service for fiscal year 2009 was 70 percent.

EXPANDED ENFORCEMENT OF TAX LAWS TO ENSURE TAX COMPLIANCE

Treasury has expanded its international enforcement presence, continued to pursue high net-worth/high income non-compliant taxpayers, and initiated efforts to improve coordination with the tax return preparer community. In fiscal year 2009, Treasury focused on detecting and bringing to justice individuals and businesses who hide assets overseas to avoid paying taxes. The largest bank in Switzerland agreed to pay a $780 million fine and provide the names of 4,450 U.S. account holders in response to a summons. Another bank entered into a deferred prosecution agreement and forfeited $340 million in connection with violations of the International Emergency Economic Powers Act. An Offshore Merchant Account Initiative increased focus on U.S. businesses that deposit unreported business receipts from debit and credit card sales in bank accounts domiciled in secrecy jurisdictions. For high-net-worth individuals, 11.2 percent of taxpayers with incomes over $200,000 were audited and 29 percent of taxpayers with incomes over $1 million were audited. Audits were also increased on self-employed taxpayers by over 21 percent. In fiscal year 2009, the IRS developed a comprehensive set of recommendations to ensure consistent standards for tax preparer qualifications, ethics and service, with the intention of establishing a foundation for improving enforcement coordination with the tax preparer community.

The *Children's Health Insurance Program Reauthorization Act* (CHIPRA) was enacted in February 2009. CHIPRA imposes significantly increased tax rates on tobacco products and introduced requirements for permits and taxes on products which had not previously been taxed or regulated (cigarettes went from a tax rate of $.39 to $1.01). Implementing the provisions was a major undertaking for TTB, including mailing of almost 500,000 information packets and fielding 50,000 inquiries about the tax increase and permit requirements, resulting in an additional $6 billion in Federal tax revenues. CHIPRA also levies a floor stocks tax (FST), a one-time excise tax placed on a commodity undergoing a tax increase, on all tobacco products held for sale as of April 1, 2009. In fiscal year 2009, TTB processed more than 133,000 receipts and collected a record $1.2 billion dollars of FST.

TTB is using automated data analysis techniques to target non-filers for audit, and is reviewing sales data to find unusual patterns that may indicate a business was stock piling product prior to the effective date of the new tax rates. TTB will use this information to identify tobacco dealers to target for audit in fiscal year 2010.

IMPROVED ELECTRONIC RETURN PROCESSING THROUGH BUSINESS SYSTEMS MODERNIZATION

Treasury continues to make efforts to improve business systems for tax processing. Upgrades to the Customer Account Data Engine (CADE) in 2009 enabled the system to process 40 million returns, 34.9 million refunds and over seven million payments. Treasury is committed to completing CADE implementation by 2011. Modernized e-File (MeF) release 5.5 enabled system processing of 33 percent more Form 1120s and 307 percent more Form 990s. (Returns submitted through the MeF system have an average processing error rate of seven percent, versus 19 percent for transcription-based paper processing.) MeF return receipts increased to about 4.5 million, an increase of 21 percent over 2008.

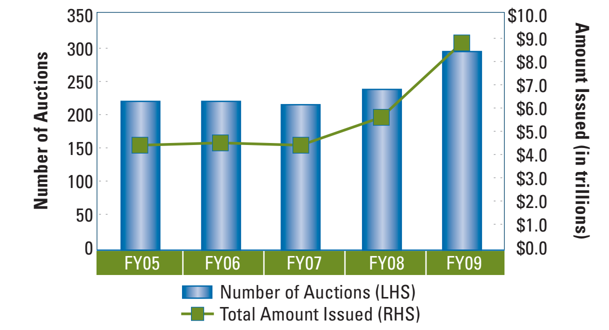
CHALLENGES ASSOCIATED WITH IMPLEMENTING RECOVERY ACT TAX PROVISIONS

Upon enactment of the Recovery Act, Treasury worked to ensure timely implementation of tax provisions, including creating and issuing forms and publications, developing and disseminating information through the internet, print media and television, and implementing safeguards against tax fraud. Despite the successes implementing these provisions, increased customer inquiries and payments added strains to existing management systems. The increased volume of taxpayer calls resulted in increased waiting times and busy signals, with the average caller waiting nearly 9 minutes. Average wait time in 2007 was 4.5 minutes. The additional payments also increased the incidence of improper payments, particularly for the First-Time Homebuyer Credit. The IRS will continue to make efforts to reduce service wait time and improper payments.

MANAGED INCREASED ISSUANCE OF DEBT FINANCING

In fiscal year 2009, the Department conducted over 290 government securities auctions, resulting in the issuance of over $8 trillion dollars in marketable securities. The results of each auction were released within the target time of two minutes plus or minus 30 seconds after the auction close. The prompt release of auction results reduced the amount of time bidders were exposed to adverse market movements, encouraging more competitive bidding and allowing the Department to secure lower borrowing rates for the U.S. Government. Treasury also successfully began the monthly issuance of three and seven year notes in order to meet the demand for borrowing and allow for greater flexibility in borrowing options.

FIGURE 10. Number of Auctions and Amount Issued by Fiscal Year



IMPROVED RETAIL SECURITIES SERVICES

BPD's Retail Securities Services program serves more than 50 million retail investors in marketable securities and savings bonds. In fiscal year 2009, BPD achieved its long-term goal of completing 90 percent of time-sensitive retail customer service transactions within 10 business days, one year ahead of schedule. BPD will transition to a new performance measure in fiscal year 2010 targeting completion of these transactions within 5 business days. TreasuryDirect, which provides investors electronic savings bonds, continues to grow. In fiscal year 2009, the system was enhanced to enable entities such as trusts, corporations, fiduciaries, and estates to open accounts and conduct transactions.

EXPANDED USE OF ELECTRONIC FUND TRANSFERS

During fiscal year 2009, FMS continued to expand the use of electronic fund transfers to deliver federal payments, improve service to payment recipients, and reduce government program costs. The Go Direct campaign, which encourages current federal benefit check recipients to switch to direct deposit, concluded a successful fourth year with over one million conversions. The total number of conversions since inception of the campaign is over 3 million. Overall, 81 percent of Treasury payments and associated information were made electronically, an increase of two percent from fiscal year 2008. This helped decrease the number of paper checks issued, minimizing costs associated with postage and the re-issuance of lost, stolen and misplaced checks.

CHALLENGES FORECASTING GOVERNMENT RECEIPTS DURING THE RECESSION

The financial and economic crisis made fiscal year 2009 an extremely challenging year to forecast government tax receipts. Expanded tax credit programs under the Recovery Act and rising unemployment levels reduced tax receipts and increased the difficulty of forecasting accurately. Given the severity of the recession and uncertainty surrounding future private consumption and investment, predicting the timing and rate of recovery in fiscal year 2010 could be equally challenging. Treasury missed its performance target of five percent maximum variance between estimated and actual fiscal receipts in fiscal year 2009, with an actual variance of 5.5 percent.

PREVENTED TERRORISM AND PROMOTED THE NATION'S SECURITY THROUGH STRENGTHENED INTERNATIONAL FINANCIAL SYSTEMS

While promoting financial and economic growth at home and abroad, the Treasury Department performs a unique role in preserving national security. In fiscal year 2009, Treasury continued to safeguard the nation's financial security while carrying out critical law enforcement responsibilities pertaining to predatory lending practices. These expectations require that Treasury continue to modernize its technological infrastructure to ensure a safer and more transparent financial system while protecting U.S. national security.

STRENGTHENED MEASURES AGAINST IRAN TO PROTECT U.S. NATIONAL SECURITY

Since the designation of a large Iranian bank, Bank Saderat, in September 2006, Treasury has led an ongoing effort to warn the world about the threat Iran poses to U.S. security and the integrity of the international financial system. This effort has developed a global consensus. In fiscal year 2009, the Financial Action Task Force (FATF), the global standard-setting body to combat money laundering and terrorist financing, issued its fourth warning alerting countries to strengthen measures to protect their financing sectors. Treasury has continued to strengthen its efforts to ensure that Iran is restricted from the U.S. financial system, while encouraging other countries to do the same.

The Department of the Treasury responded to the FATF warning one month after it was issued. Treasury hindered Iran's ability to financially support illicit activities by revoking an existing "U-turn" license for Iran, further restricting Iran's access to the U.S. financial system. This license had allowed funds transfers to pass though the U.S. financial system for the benefit of Iranian entities. Following this action, U.S. financial institutions are no longer allowed to process such transactions.

Treasury maintained its designations of Iranian financial institutions and individuals due to proliferation concerns and implemented several new designations. The Department, through the FATF, will continue to strengthen its measures and encourage other countries to enhance vigilance over all business with Iran.

ENHANCED MECHANISMS TO COMBAT MORTGAGE AND LOAN MODIFICATION FRAUD

A series of initiatives have been announced to help American homeowners and address the housing crisis. The United States government continues to intensify its efforts to ensure predatory scams do not rob Americans of their savings and potentially their homes. On April 6, 2009, Secretary Geithner announced a coordinated proactive effort to be led by Treasury, to combat fraudulent loan modification schemes and coordinate ongoing efforts across a range of federal and state agencies that investigate fraud and assist with enforcement and prosecutions. Treasury simultaneously issued an advisory to alert financial institutions to the risks of emerging schemes related to loan modification. These efforts are designed to facilitate the detection, deterrence, investigation and prosecution of those who would exploit consumers facing possible home foreclosures, in particular to target fraudulent scams against consumers seeking loan modification assistance.

This advisory was intended to identify "red flags" that may indicate a loan modification or foreclosure rescue scam and warrant the filing of a Suspicious Activity Report (SAR). These red flags alert financial institutions to scams victimizing their customers and provide an opportunity to stop predatory loan modification. The advisory reminded financial institutions of the requirement to implement appropriate risk-based policies, procedures and processes. Financial institutions must conduct customer due diligence on a risk-assessed basis to prevent fraudulent actors from accessing the financial system and to aid in the identification of potentially suspicious transactions.

The advisory required the term "foreclosure rescue scam" to be included in the narrative sections of all relevant SARs. This inclusion allowed law enforcement to more easily search for and identify fraudulent activity when reviewing SAR information, improving the focus of investigative resources. Utilizing the initiative's advanced targeting methods, 30 case referrals were made to law enforcement investigators involving over 140 suspects. Treasury, at the request of civil and criminal law enforcement, also contributed to 35 investigations involving multiple suspects and hundreds of BSA reports. These results have illustrated the benefits of proactive threat identification and preemption of fraudulent activity. However, the management of capital investments is still considered to be a management challenge.

LIFTED SANCTIONS ON 125 INDIVIDUALS OR ENTITIES FROM THE LIST OF SPECIALLY DESIGNATED NATIONALS (SDNs)

Treasury's Office of Foreign Assets Control (OFAC) administers and enforces economic and trade sanctions based on U.S. foreign policy and national security goals against targeted foreign countries and regimes, terrorists, international narcotics traffickers, those engaged in activities related to the proliferation of weapons of mass destruction, and other threats to the national security, foreign policy or economy of the United States. Key to OFAC's success is the reaction of the private sector when financial measures are utilized, such as designations, to disrupt or dismantle the forces at work in illicit finance or other criminal behavior. When private sector organizations, particularly those in the international banking community, voluntarily go beyond their legal requirement and demonstrate good corporate citizenship by refusing to handle illicit business, they strengthen the effectiveness of government-imposed measures.

In fiscal year 2009, OFAC had success with financial institutions in South Africa, Latin-America, Mexico, Europe, China, and the Middle East in closing accounts and denying access to the financial system for criminals involved in activities that could jeopardize U.S. national security. Additionally, OFAC took several actions to lift sanctions on 125 individuals or entities, where an individual or entity had to divest themselves of any ownership interest in any OFAC designated companies. As a result, dozens of front companies within the target networks have been liquidated and no longer facilitate illicit business activities.

STRENGTHENED THE REVIEW PROCESS FOR FOREIGN INVESTMENT IN THE UNITED STATES

Treasury chairs the sixteen-member Committee on Foreign Investment in the United States (CFIUS) which reviews certain foreign investments into the United States to identify and resolve national security concerns.

The *Foreign Investment and National Security Act of 2007* (FINSA) required Treasury to issue new regulations governing the CFIUS process. CFIUS agencies took into account over 30 public comments received from domestic and foreign parties in response to proposed regulations that Treasury published on April 21, 2008. Treasury issued final regulations on November 21, 2008, which went into effect on December 22, 2008. On December 8, Treasury also published guidance on the types of transactions that CFIUS has reviewed which have raised national security concerns. Though the guidance does not have the force of law, it provides helpful insight about how the CFIUS process works.

MODERNIZE BANK SECRECY ACT (BSA) INFORMATION AND ANALYSIS

The current BSA data infrastructure is ill-equipped to meet 21st century realities and unable to quickly adapt to changing financial indicators and patterns of illicit activity. The number of financial institutions falling under the purview of the BSA has grown exponentially in the last six years and will continue to experience robust growth in the future. Treasury developed a strategy in fiscal year 2007 to modernize the BSA data architecture to better serve its internal and more than 10,000 external users that rely on accurate, timely, and reliable BSA data to identify money laundering, terrorist financing, tax evasion, and vulnerabilities in the financial industry.

The modernization will reengineer the BSA data architecture, update antiquated infrastructure required to support data capture and dissemination, implement innovative web-services, enhance electronic-filing, and provide analytical tools. This investment will begin to enrich and standardize BSA data to maximize value, evaluate and deploy advanced analytical technologies, and establish more effective security technologies to enhance data confidentiality and integrity. After two years of analysis, the Department anticipates beginning implementation of this modernization in fiscal year 2010.

ENCOURAGE PAKISTAN TO MAKE ITS ANTI-MONEY LAUNDERING LAW PERMANENT

A key aspect of strengthening anti-money laundering/counter-terrorist financing (AML/CFT) regimes is conducting country assessments to determine the level of compliance with international AML/CFT standards that country has. These evaluation reports also identify deficiencies and ways to strengthen each country's regime. Adopting one of these mutual evaluations triggers a follow-up review, which establishes an avenue for Treasury to encourage additional measures to strengthen a country's AML/CFT regime. Despite the work Treasury has done in fiscal year 2009 and before, there is still room for improvement to implement AML/CFT laws in key countries. In particular, Pakistan needs to build on the progress it made as a result of its mutual evaluation. Its anti-money laundering law must be made permanent and investigations and prosecutions for money laundering and terrorist financing offenses must occur.

CONTINUE TO PROVIDE ADDITIONAL GUIDANCE TO THE CHARITABLE SECTOR

The Department strives to create a robust and aggressive strategy to conduct outreach to the charitable sector to combat terrorist exploitation and abuse of charities. The Department works with various community organizations in order to raise awareness of the risk of terrorist financing and measures to minimize such risks. Outreach events include participation in several interagency outreach efforts, hosted by the Department of Justice as well as the Department of Homeland Security. One key component is that Treasury issues guidance to the charitable sector as part of this comprehensive strategy to raise awareness and minimize the risk of terrorist exploitation through charities. During fiscal year 2009, the Treasury Guidelines Working Group (TGWG) met, which represents major U.S.-based charities, foundations and philanthropic groups, and began revising its *Anti-Terrorist Financing Guidelines: Voluntary Best Practices for U.S-Based Charities (Guidelines).* It is expected that the TGWG will submit a proposal concerning the revision of the Guidelines by the close of the 2009 calendar year. This is just one component to ensuring risks are minimized by the charitable sector, Treasury will need to continue to develop and implement its strategy to combat further exploitation.

ESTABLISH EXTERNAL PERFORMANCE MEASURE EVALUATION

Treasury introduced and began to apply a composite performance measure to assess the Department's impact in preventing terrorism and safeguarding U.S. and international financial systems. The measure incorporates four focus areas: the impact of policymaking, outreach and diplomacy; economic sanctions; information and analysis; and regulatory activity on transparency of financial systems. Moving forward, refinement of the specific methodologies for data collection and validation related to these focus areas will need to be further refined and reviewed externally.

MANAGEMENT AND ORGANIZATIONAL EXCELLENCE

The Department of the Treasury strives to maintain public trust and confidence in U.S. and international economic and financial systems through exemplary leadership, best-in-class processes, and a culture of excellence, integrity and teamwork. Achieving and maintaining exemplary accountability and transparency is critical for the Treasury Department as the primary financial agency for the U.S. Government. Management of Treasury programs provided significant challenges in fiscal year 2009 associated with implementation and oversight of new programs to manage the economy.

COMPLETED AN INCREASED NUMBER OF MATERIAL LOSS REVIEWS (MLRS)

OIG is mandated to conduct MLRs of any Treasury-regulated bank failure resulting in material losses greater than $25 million, or two percent of the institution's assets. An MLR examines the cause(s) of the failure, with specific attention paid to effectiveness of bank supervision and potential preventative measures to improve regulation. The review also looks for examples of fraud that may lead to criminal or civil prosecution.

In fiscal year 2009, 107 banks failed, of which 27 were regulated by OCC or OTS. Of these Treasury-regulated bank failures, 23 required an MLR by OIG. In fiscal year 2009, OIG completed 10 MLRs, including five MLRs for failures that occurred in fiscal year 2008. The estimated loss to the Federal Deposit Insurance Fund of the 10 reviewed bank failures totaled $14.7 billion, including a $10.7 billion loss resulting from the failure of IndyMac Bank, the largest institution to date to be the subject of an MLR. As of September 30, 2009, 18 MLRs were still in progress.

OIG has reported on several trends from the MLRs. Three primary causes of the failures were identified:

asset quality issues (e.g. risky non-traditional loan products, poor underwriting, commercial real estate); liquidity issues (e.g. reliance on volatile brokered deposits to fund aggressive growth); and management issues (e.g. management systems not commensurate with level of risk, non-responsive to regulator concerns). With respect to supervision, OIG reported that OCC or OTS usually identified the problems early on but did not forcefully act to address them. Both regulators have been responsive to OIG's recommendations for improving supervision processes.

TIGTA AUDITS

TIGTA conducts audits and investigations to ensure fair administration of the nation's tax system and accountability for the more than $2 trillion in tax revenue collected each year. The audits identify high-risk issues and deficiencies related to the administration of programs and operations, ensuring taxpayers are appropriately served and their rights adequately protected. In fiscal year 2009, TIGTA issued 142 audit reports focusing on the areas of improved tax compliance (including the international arena), security maintenance, systems modernization and operations. The audit reports isolated $14.7 billion in potential financial benefits, the majority stemming from a possible $8.9 billion savings over five years from the disallowance of the Additional Child Tax Credit to filers without a valid social security number.

TIGTA conducted a special audit on a major Recovery Act activity for IRS associated with the First-Time Homebuyer Tax Credit. TIGTA found that although the IRS developed controls to identify many questionable claims for the First-Time Homebuyer Tax Credit, some key documentation requirements to substantiate the purchase of a house were inadequate. As a result, 19,351 Tax Year 2008 income tax returns included erroneous or fraudulent claims for the credit, totaling over $139 million for homes that had not yet been purchased. In addition, taxpayers who appeared not to be first-time homebuyers claimed the credit on their returns. The IRS has implemented filters to identify these taxpayers and ensure the credits are properly applied. In addition, IRS identified 48,580 taxpayers who may not have been aware of the changes to the credit and did not claim the full amount. IRS is planning an outreach campaign to inform those taxpayers of the additional credit, if they do not otherwise amend their returns.

EFFECTIVE MANAGEMENT OF TREASURY'S INFORMATION TECHNOLOGY

The Department relies on information technology (IT) infrastructure to manage more than $8 trillion dollars in debt, collect more than $2 trillion in revenue, and conduct more than $58 billion in daily cash transactions. In fiscal year 2009, the Department defined strategic IT management priorities to strengthen cyber security, reduce infrastructure operations costs, increase bureau collaboration and productivity, and improve Treasury IT workforce proficiency. As part of operations management, the Department uses OMB's IT Dashboard to gauge the effectiveness of its IT systems. Each month, Treasury's Chief Information Officer evaluates the Department's 59 major investments on cost and schedule performance metrics. As of October 1, 2009, Treasury had 58 out of 59 investments (98.3 percent) reported as Green or Yellow for Cost Variance and 1 investment (1.7 percent Red) reported as Red. As of October 1, 2008, 37 out of 62 investments (59.7 percent) reported Green for Cost Variance and the remainder (40.3 percent) reported red. As of October 1, 2009, Treasury had 59 out of 59 investments (100.0 percent) reported as Green or Yellow for Schedule Variance and no investments reported as Red. As of October 1, 2008, 50 out of 62 investments (80.6 percent) reported Green for Schedule Variance and the remainder (19.4 percent) reported red. Additionally, the information security management challenge was closed in fiscal year 2009.

EXPANDED HUMAN CAPITAL INITIATIVES

The Office of the Deputy Assistant Secretary for Human Resources/Chief Human Capital Officer (DASHR/CHCO) endeavors to broaden and diversify Treasury's talent pool; develop and retain an effective workforce; effectively manage and utilize human capital; and develop human capital practitioners as strategic business partners. In fiscal year 2009, DASHR/CHCO was directly involved in ramping up emergency programs to support economic stabilization efforts, improving applicant outreach and supporting new hires through the Hamilton Fellows Program and other initiatives, and expanding the diversity of Treasury's workforce. A major challenge in future years will be managing the retirement of a significant percentage of Treasury's employees as baby boomers leave the workforce. Improving retention of new hires and providing executive leadership development for current employees is essential to ensuring Treasury has a strong and professional talent pool.

Department of the Treasury Key Performance Measures for 2009

The following table contains ten key performance metrics providing a representative overview of the Department's performance for 2009. Discussion of the factors contributing to each measure's performance results, and plans to improve the measure's results in future years, follows the table.

ANNUAL FINANCIAL REPORT FOR FISCAL YEAR 2009

Treasury Department Key Performance Measure Table

Performance Measure Official Title	Bureau	2005 Target	2005 Actual	2006 Target	2006 Actual	2007 Target	2007 Actual	2008 Target	2008 Actual	2009 Target	2009 Actual	Percent Target Achieved 2009	2009 Actual vs. Target	Target Trend	Actual Trend
Percentage collected electronically of total dollar amount of Federal government receipts (%)	FMS	82	79	83	79	80	79	79	80	80	83	104%	Exceeded	▶	▲
Customer Service Representative (CSR) Level of Service (%)	IRS	82.0	82.6	82.0	82.0	82.0	82.1	82.0	52.8	70.0	70.0	100%	Met	▼	▼
Percent of Business Returns Processed Electronically (%)	IRS	17	17.8	18.6	16.6	19.5	19.1	20.8	19.4	21.6	22.8	106%	Exceeded	▲	▲
Percent of Individual Returns Processed Electronically (%)	IRS	51	51.1	55	54.1	57	57.1	61.8	57.6	64	65.9	103%	Exceeded	▲	▲
Number of full-time equivalent jobs created or maintained in underserved communities by businesses financed by CDFI program awardees	CDFI	26,995	23,656	29,158	22,329	34,009	35,022	28,676	29,539	30,000	70,260	234%	Exceeded	▶	▲
Rehabilitated national banks as a percentage of problem national banks one year ago (CAMELS 3, 4 or 5) (%)	OCC	40	44	40	46	40	52	40	47	40	29	73%	Unmet	▶	▼
Clean audit opinion on TARP financial statements	DO									Baseline	Met	100%	Met	B	B
Percentage of SIGTARP and GAO oversight recommendations responded to on time	DO									Baseline	100	100%	Met	B	B
Average days to close a FOIA case	DO									Baseline	67	100%	Met	B	B
Impact of TFI programs and activities	DO									Baseline	7.81	100%	Met	B	B

Legend	Symbol
Favorable upward trend	▲
Favorable downward trend	▼
Unfavorable upward trend	▲
Unfavorable downward trend	▼
No change in trend, no effect	▶
No change in trend, favorable effect	▶
No change in trend, unfavorable effect	▶
Baseline	B

In fiscal year 2009, FMS' total dollar collections decreased from $3.2 trillion to $2.9 trillion as a result of both businesses and individuals being impacted by the economic downturn. However, paper tax receipts collected through a lockbox network and paper federal tax deposits decreased by more than 28 percent compared with 2008, while electronic tax collections only decreased by 11 percent. This caused FMS' metric "Percentage collected electronically of total dollar amount of Federal government receipts" to exceed its performance target by four percent, and show a four percent improvement over 2008.FMS regularly reaches out to the banking community to promote electronic collection, and is implementing marketing programs to encourage migration of paper-based collections to electronic collection systems and Pay.gov. Two initiatives to promote this migration would eliminate paper coupons for employment taxes, transferring them completely to electronic collection systems by 2011, and require certain classes of non-tax collections be paid electronically. Both proposals would help to significantly increase the percentage of electronic collections going forward.

The IRS metric "Customer Service Representative (CSR) Level of Service" met its performance target in fiscal year 2009 and improved on the prior fiscal year's result by 33 percent. Demand for IRS customer service was unusually high in 2009, due largely to inquiries related to the Recovery Act, Rebate Recovery Credit and interest in electronic filing. Given the sunset for Recovery Act provisions and the Recovery Rebate Credit, the IRS does not anticipate a significant increase in the CSR Level of Service for fiscal year 2010.

IRS electronic filing metrics "Percent of Business Returns Processed Electronically" and "Percent of Individual Returns Processed Electronically" exceeded their performance targets by six percent and three percent, respectively, and each improved significantly over their fiscal year 2008 results by 18 percent and 14 percent, respectively. Their favorable results can be attributed to changes in filing patterns, economic and demographic trends, legislative requirements, and IRS administrative processes. IRS expects the percentage of both business and individual returns filed electronically to increase in fiscal year 2010 based on recent experience, historical growth trends, increased marketing, and expanded programs aimed at boosting electronic filing. IRS will continue to pursue additional legislative mandates to increase electronic filing for businesses taxpayers, such as a provision for 2011 requiring taxpayers filing more than ten individual returns during a calendar year file electronically.

CDFI's metric "Number of full-time equivalent jobs created or maintained in underserved communities by businesses financed by CDFI program awardees" in fiscal year 2009 exceeded its performance target by 134 percent and improved over the prior fiscal year's actual result by 138 percent. The primary reason for this increase was the additional $90 million in Recovery Act funds added to the $57 million received under the regular budget. Targeted performance without the additional Recovery Act funding was 30,000 full-time jobs created or maintained; with Recovery Act funding, 70,000 full-time jobs were created. In addition, the amount of money CDFIs were able to attract from private investment reached nearly $1.3 billion, more than double the 2008 target of $635 million, due to commitments made before the full onset of the financial crisis. Based on the increased funding and private sector matching, in 2009 CDFIs were able to invest in projects that created or maintained 70,260 jobs, more than double the target of 30,000 jobs. With an anticipated drop in Recovery Act funding and private sector matching in 2009, it is unlikely that these results will be repeated in 2010.

During fiscal year 2009, OCC's metric "Rehabilitated national banks as a percentage of problem national banks one year ago (CAMELS 3, 4 or 5)" only achieved 73 percent of its performance target, dropping by 38 percent compared with fiscal year 2008. During fiscal year 2009, national banks continued to operate in a highly challenging and volatile environment. Deterioration in the housing and commercial real estate markets and the decline in general economic conditions directly impacted national banks' financial condition and performance. OCC is identifying banks most vulnerable to current economic conditions, and is allocating bank supervision resources to areas and institutions of highest risk. For problem banks, OCC is working to develop specific plans to correct deficiencies in a timely manner and return the bank to a safe and sound condition. For all national banks, OCC is continuing to focus on quick response to deteriorating bank credit quality and on ensuring banks maintain adequate liquidity, loan loss reserves, and capital buffers.

In fiscal year 2009, DO's Office of Financial Stability, responsible for managing TARP, established new performance measures. These measures included the following:

- Clean audit opinion on TARP financial statements: For 2009, OFS received a clean audit opinion on TARP financial statements, a significant accomplishment given OFS's very challenging first year of operations after standing up the organization.
- Percentage of SIGTARP and GAO oversight recommendations responded to on time: In fiscal year 2009, OFS responded to 100 percent of these oversight bodies' recommendations on time. Going forward, OFS will continue working to ensure that all recommendations from the oversight bodies are responded to efficiently and effectively.
- Average days to close a FOIA case (after received by OFS): During fiscal year 2009, OFS went to great lengths to reduce the time required to respond to FOIA requests, and by the end of the fiscal year, averaged 67 days to close a FOIA case, a response time faster than the overall Treasury average. Going forward, OFS will continue working to further reduce the time taken to respond to all incoming FOIA requests.

TFI began applying its composite performance metric "Impact of TFI programs and activities" during fiscal year 2009. This metric consists of four overall focus areas, with additional detailed focus area components. These components align to performance goals established by TFI. In fiscal year 2009 this metric achieved a 7.81 rating out of 10 possible points. The external review process for this measure still needs to be developed, but the implementation of this measure is a large step in the effort to measure performance for a policy office that also has operational responsibilities.

Summary of Management and Performance Challenges and High Risk Areas

Annually, the Treasury Office of Inspector General (OIG) and the Treasury Inspector General for Tax Administration (TIGTA) identify the most significant management and performance challenges facing the Department. The Government Accountability Office (GAO) identifies High Risk areas biennially. These challenges do not necessarily indicate deficiencies in performance; rather, some represent inherent risks that must be monitored continuously. Treasury made much progress on these issues in fiscal year 2009, and will continue to focus on resolving them during fiscal year 2010.

Summaries of the IG-identified management challenges and GAO-identified high risks are below, along with Treasury's progress and status ratings for each management challenge. For details, please refer to Appendix C for this year's OIG and TIGTA memoranda identifying major management and performance challenges, and the Secretary's responses.

TREASURY-WIDE MANAGEMENT CHALLENGES – AS IDENTIFIED BY OIG

MANAGEMENT CHALLENGE	IMPORTANCE	PROGRESS*	STATUS*
Treasury's New Authorities Related to Distressed Financial Markets	Protection of the taxpayer from unnecessary risk associated with the implementation of the program	Reasonable	Meets Expectations
Regulation of National Banks and Thrifts	Prevent or better mitigate unsafe and unsound practices and protect the financial health of the banking industry	Reasonable	Meets Expectations
Management of Recovery Act Programs	Ensure the programs achieve their intended purposes, provide for accountability and transparency, and are free from fraud and abuse	New	New
Management of Capital Investments	Effective use of taxpayer funds for large capital investments	Significant	Meets Expectations
Anti-Money Laundering and Terrorist Financing/ Bank Secrecy Act Reporting	U.S. and international financial systems that are safe	Reasonable	Meets Expectations
Information Security	Ensure compliance to federal standards for protection of systems and information	Closed	Closed
Corporate Management	Overall agency performance/improved value for the taxpayer	Closed	Closed

* Determined by management

IRS MANAGEMENT CHALLENGES – AS IDENTIFIED BY TIGTA

MANAGEMENT CHALLENGE	IMPORTANCE	PROGRESS*	STATUS*
Modernization	Improved taxpayer service and efficiency of operations	Reasonable	Meets Expectations
Security	Appropriate protection of financial, personal, and other information	Reasonable	Meets Expectations
Tax Compliance Initiatives	Improved compliance and fairness in the application of the tax laws	Reasonable	Meets Expectations
Implementing Tax Law Changes	Responsiveness to new tax provisions, including the Recovery Act, and adjusting to expiring ones	Reasonable	Meets Expectations
Providing Quality Taxpayer Service Operations	Improved taxpayer service	Reasonable	Meets Expectations
Human Capital	Enables the IRS to achieve its mission	Significant	Meets Expectations
Erroneous and Improper Payments and Credits	Effective use of taxpayer funds	Reasonable	Adequate
Globalization	Increased outreach efforts to foreign governments on cross border transactions	New	New
Taxpayer Protection and Rights	Fairness in the application of the tax laws	Reasonable	Meets Expectations
Leveraging Data to Improve Program Effectiveness and Reduce Costs	Resources that are focused on producing the best value for stakeholders	Significant	Exceeds Expectations

* Determined by management

LEGEND

Progress Rating	Description
New	A new management challenge in fiscal year 2009
None	No progress was made on the management challenge
Marginal	Minimal progress was made on the management challenge compared to the prior year
Reasonable	Progress was made in addressing the management challenge, improving from the prior year
Significant	A large amount of progress was made compared to the prior year assessment

LEGEND

Status Rating	Description
New	A new management challenge in fiscal year 2009
Inadequate	Regardless of progress made in fiscal year, the status of the management challenge remains incomplete and falls significantly short of expectations
Adequate	The current status of the management challenge is acceptable but falls slightly short of expectations set for the fiscal year
Meets Expectations	The current status of the management challenge meets expectations set for the fiscal year
Exceeds Expectations	The current status of the management challenge exceeds expectations set for the fiscal year
Closed	Actions taken resulted in the elimination of the management challenge

HIGH RISK AREAS – AS IDENTIFIED BY GAO

ENFORCEMENT OF THE TAX LAWS

Problem: The IRS needs to improve its enforcement of tax laws, not only to catch tax cheats, but also to promote broader compliance by giving taxpayers confidence that others are paying their fair share.

Goal: Improve research on noncompliance, increase the use of third party information reporting, focus on improving standards among tax return preparers, and increase emphasis on international noncompliance.

Challenges and Actions Taken/Planned:

Reduce the opportunity for evasion

- Offshore Private Banking Initiative – The largest bank in Switzerland agreed to provide the names of 4,450 of their U.S. account holders and to pay a $780 million fine, including $380 million to the IRS. Another bank entered into a deferred prosecution agreement to forfeit $340 million, the largest seizure in IRS history, in connection with violations of the International Emergency Economic Powers Act. Over 7,500 people submitted "voluntary disclosure" applications under the partial amnesty program that ended October 15, 2009.
- Offshore Merchant Account Initiative – A summons was issued to a large processor of merchant accounts to identify U.S. businesses that deposit unreported business receipts from debit and credit card sales in accounts in banks domiciled in secrecy jurisdictions.

Target specific areas of noncompliance and improve voluntary compliance with extensive research

- The IRS maintained its focus on high-net worth individuals, flow through entities, and large corporations (assets > $10 million). The IRS conducted over 145,000 high-net worth audits, an increase of 11.2 percent. Audits of large corporations increased by 3.6 percent and the number of flow through audits remained over 31,000.
- In fiscal year 2010, IRS will continue to expand its efforts to address international tax evasion, to expand the focus on corporate and high net-worth returns, to integrate significant new information reporting authorities into compliance programs, and to implement higher standards within the practitioner community to ensure that the proper amount of tax is paid.

IRS BUSINESS SYSTEMS MODERNIZATION

Problem: The Business Systems Modernization (BSM) program is developing and delivering a number of modernized systems to replace the aging business and tax processing systems currently in use. This effort is highly complex and scheduled to be carried out over a numbers of years, ultimately creating a more efficient and effective IRS. Though the IRS experienced delays and cost overruns in the early years of the effort, improved practices and oversight are now contributing to better delivery of outcomes.

Goal: Meet all BSM project milestones within a cost and schedule variance of 10 percent of the initial estimate.

Challenges and Actions Taken/Planned:

Fully implement all projects and programs for the BSM program

- In fiscal year 2009, the IRS revised its Customer Account Data Engine (CADE) strategy. BSM will continue the revised CADE strategy to implement the new taxpayer account database by the end of 2011 for the 2012 filing season. The new database will result in the migration of all 140 million individual taxpayers to a modernized, relational database that will support daily processing and result in faster refunds for all individual refund filers. Daily updating of all individual taxpayer accounts by 2012 also will improve taxpayer service and accuracy, reduce interest paid on late refunds, improve data security, and create new tools to combat fraud and improve enforcement activities. Completion of the taxpayer account database is the prerequisite for other major initiatives, including significant expansion of online services and transactions and the next generation of enforcement technologies.

MODERNIZING THE OUTDATED U.S. REGULATORY SYSTEM (NEWLY IDENTIFIED IN 2009)

Problem: The current financial system is a fragmented, complex arrangement of federal and state regulators that arose over the past 150 years, often in response to past crises.

Goal: Establish regulatory reform goals and a measurement plan.

Challenges and Actions Taken/Planned:

Promote robust supervision and regulation of financial firms

- A new Financial Services Oversight Council of financial regulators to identify emerging systemic risks and improve interagency cooperation.
- New authority for the Federal Reserve to supervise all firms that could pose a threat to financial stability, even those that do not own banks.
- Stronger capital and other prudential standards for all financial firms, and even higher standards for large, interconnected firms.
- A new National Bank Supervisor to supervise all federally chartered banks.
- Elimination of the federal thrift charter and other loopholes that allowed some depository institutions to avoid bank holding company regulation by the Federal Reserve.
- The registration of advisers of hedge funds and other private pools of capital with the Securities and Exchange Commission.

Establish comprehensive supervision of financial markets

- Enhanced regulation of securitization markets, including new requirements for market transparency, stronger regulation of credit rating agencies, and a requirement that issuers and originators retain a financial interest in securitized loans.
- Comprehensive regulation of all over-the-counter derivatives.
- A new regime to resolve nonbank financial institutions whose failure could have serious systemic effects.
- Revisions to the Federal Reserve's emergency lending authority to improve accountability.
- New authority for the Federal Reserve to oversee payment, clearing, and settlement systems.

Protect comprehensive supervision of financial markets

- A new Consumer Financial Protection Agency to protect consumers across the financial sector from unfair, deceptive, and abusive practices.
- Stronger regulations to improve the transparency, fairness, and appropriateness of consumer and investor products and services.
- A level playing field and higher standards for providers of consumer financial products and services, whether or not they are part of a bank.

Provide the government with the tools it needs to manage financial crises

- A new regime to resolve nonbank financial institutions whose failure could have serious systemic effects.
- Revisions to the Federal Reserve's emergency lending authority to improve accountability.

Raise international regulatory standards and improve international cooperation

- International reforms to support our efforts at home, including strengthening the capital framework; improving oversight of global financial markets; coordinating supervision of internationally active firms; and enhancing crisis management tools.

Analysis of Financial Statements

CONDENSED BALANCE SHEET: (in Millions)	2009	2008
Due From the General Fund	$ 11,992,719	$ 10,100,763
Other Intra-governmental Assets	923,457	551,115
Cash, Foreign Currency, and Other Monetary Assets	341,308	387,270
Gold and Silver Reserve	11,062	11,062
Investments and Related Interest	13,565	10,576
Tax, Other Related Interest Receivables, Net	30,408	30,878
Asset Guarantee	1,765	0
Investments-Credit Reform	203,141	0
Investments in Government Sponsored Enterprises	64,679	7,032
Credit Program Receivables, Direct Loans	219,170	3,385
Beneficial Interest in Trust	23,472	0
Other Assets	21,855	14,957
Total Assets	$ 13,846,601	$ 11,117,038
Federal Debt and Interest Payable	$ 11,962,385	$ 10,075,108
Other Intra-governmental Liabilities	1,275,613	681,621
Other Liabilities	180,547	50,598
Total Liabilities	13,418,545	10,807,327
Unexpended Appropriations	455,144	271,968
Cumulative Results of Operations	(27,088)	37,743
Total Net Position	$ 428,056	$ 309,711
Total Liabilities and Net Position	$ 13,846,601	$ $11,117,038

CONDENSED STATEMENT OF NET COST: (in Millions)	2009	2008
Net Financial Program Cost	$ 13,055	$ 12,287
Net Economic Program (Revenue)/Cost	195,705	14,048
Net Security Program Cost	322	342
Net Management Program Cost	509	466
Total Net Cost of Treasury Operations	209,591	27,143
Net Federal Costs (primarily interest on the Federal Debt)	$ 313,341	$ 442,208

CONDENSED STATEMENT OF CUSTODIAL ACTIVITY: (in Millions)	2009	2008
Individual and FICA Taxes	$ 2,036,557	$ 2,294,326
Corporate Income Taxes	225,482	354,063
Other Revenues	139,648	144,218
Total Revenue Received	2,401,687	2,792,607
Less Refunds	(437,972)	(426,074)
Net Revenue Received	1,963,715	2,366,533
Beneficial Interest in Trust	23,472	–
Accrual Adjustment	(1,097)	3,132
Total Custodial Revenue	1,986,090	2,369,665
Amounts Provided to Fund the Federal Government	1,963,228	2,366,126
Other Agencies	487	407
Beneficial Interest in Trust	23,472	–
Accrual Adjustment	(1,097)	3,132
Total Disposition of Custodial Revenue	1,986,090	2,369,665
Net Custodial Revenue Activity	$ 0	$ 0

CONDENSED STATEMENT OF CHANGES IN NET POSITION: (in Millions)	2009	2008
Beginning Balance	$ 37,743	$ 48,782
Budgetary Financing Sources	668,894	482,150
Other Financing Sources (Uses)	(210,793)	(23,838)
Total Financing Sources	458,101	458,312
Net Cost of Operations	(522,932)	(469,351)
Net Change	(64,831)	(11,039)
Cumulative Results of Operations	**(27,088)**	**37,743**
Beginning Balance	$ 271,968	$ 72,317
Appropriations Received	855,762	681,473
Appropriations Used	(668,153)	(481,735)
Other	(4,433)	(87)
Total Budgetary Financing Sources	183,176	199,651
Total Unexpended Appropriations	**455,144**	**271,968**
Net Position - Year End	**$ 428,056**	**$ 309,711**

CONDENSED STATEMENT OF BUDGETARY RESOURCES: (in Millions)	2009	2008
Unobligated Balances, Brought Forward	$ 284,630	$ 57,450
Recoveries of Prior Year Obligations	8,096	413
Budget Authority	1,814,086	722,859
Other Budget Authority	(271,778)	(8,558)
Total Budgetary Resources	$ 1,835,034	$ 772,164
Obligations Incurred	1,387,195	487,534
Unobligated Balance	413,998	273,235
Unobligated Balance, Not Available	33,841	11,395
Total Status of Budgetary Resources	$ 1,835,034	$ 772,164
Total Unpaid Obligated Balances, Net	$ 56,977	$ 57,393
Obligations Incurred, Net	$ 1,387,195	$ 487,534
Gross Outlays	$ (1,248,916)	$ (487,608)
Recoveries of Prior Year Unpaid Obligations, Actual	$ (8,096)	$ (413)
Changes in Uncollected Customer Payments Federal	$ (28,748)	$ 71
Total Unpaid Obligated Balance, Net, End of Year	$ 158,412	$ 56,977
Net Outlays	$ 922,165	$ 462,868

SUMMARY OF AUDITOR'S REPORT ON THE TREASURY DEPARTMENT'S FINANCIAL STATEMENTS

The Department received an unqualified audit opinion on its fiscal year 2009 financial statements. As summarized in the table below, the auditor reported two material weaknesses. The auditor also reported significant deficiencies related to financial reporting at the Office of Financial Stability and information system controls at the Financial Management Service. The auditor also reported an instance of noncompliance with laws and regulations related to Section 6325 of the Internal Revenue Code and that the Department's financial management systems did not substantially comply with the requirements of the *Federal Financial Management Improvement Act of 1996*.

SUMMARY OF FINANCIAL STATEMENT AUDIT

AUDIT OPINION	UNQUALIFIED				
Restatement	No				
Material Weaknesses	Beginning Balance	New	Resolved	Consolidated	Ending Balance
Financial Systems and Reporting at the IRS Financial Management Practices at the Departmental Level (new)	1	1	0	0	2

LIMITATIONS ON THE PRINCIPAL FINANCIAL STATEMENTS

The principal financial statements have been prepared to report the financial position and results of operations of the Department of the Treasury, pursuant to the requirements of 31 U.S.C. 3515 (b). While the statements have been prepared from the books and records of the Department of the Treasury, in accordance with generally accepted accounting principles (GAAP) for federal entities and the formats prescribed by OMB, the statements are in addition to the financial reports used to monitor and control budgetary resources which are prepared from the same books and records.

The financial statements should be read with the realization that they are for a component of a sovereign entity, that liabilities not covered by budgetary resources cannot be liquidated without the enactment of an appropriation, and that the payment of all liabilities other than for contracts can be abrogated by the sovereign entity.

MAJOR HIGHLIGHTS

The following provides the highlights of Treasury's financial position and results of operations for fiscal year 2009.

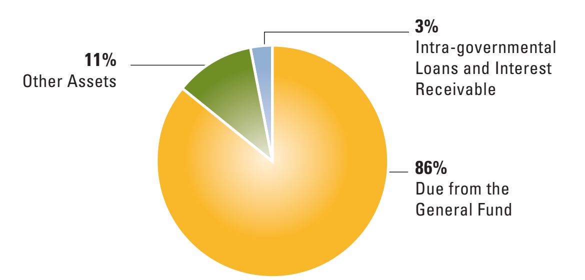
MAJOR HIGHLIGHTS

The following provides the major highlights of Treasury's financial position and results of operations for fiscal year 2009.

Assets. Total assets increased from $11.1 trillion at September 30, 2008 to $13.8 trillion at September 30, 2009. The primary reason for the increase is the rise in the federal debt, which causes a corresponding rise in the "Due from the General Fund of the U.S. Government" account ($12.0 trillion). This account represents future funds required from the General Fund of the U.S. Government to pay borrowings from the public and other federal agencies.

The majority of loans and interest receivable ($410.6 billion) included in "Intra-governmental" assets are the loans issued by the Bureau of the Public Debt to other federal agencies for their own use or to private sector borrowers, whose loans are guaranteed by the federal agencies.

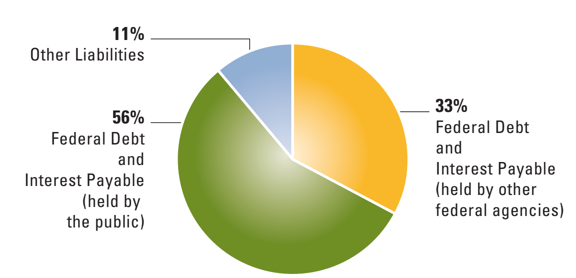
Total Assets



Liabilities. Intra-governmental liabilities totaled $5.7 trillion, and include $4.4 trillion of principal and interest payable to various federal agencies, such as the Social Security Trust Fund. These borrowings do not include debt issued separately by other governmental agencies, such as the Tennessee Valley Authority or the Department of Housing and Urban Development.

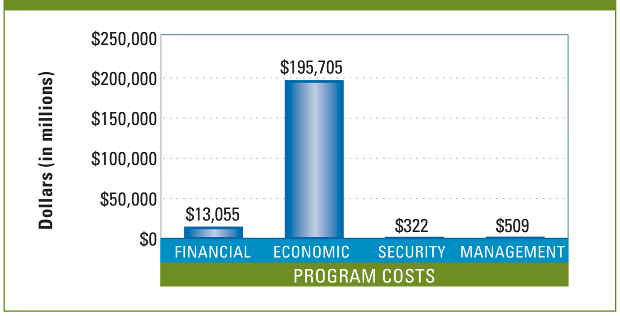
Liabilities also include federal debt held by the public, including interest, of $7.6 trillion; this debt was mainly issued as Treasury Notes. The increase in total liabilities in fiscal year 2009 over fiscal year 2008 ($2.6 trillion and 24.2 percent), is the result of increases in borrowings from various federal agencies ($140.7 billion), and federal debt held by the public, including interest, ($1.75 trillion). Debt held by the public increased primarily because of the need to finance budget deficits.

Total Liabilities

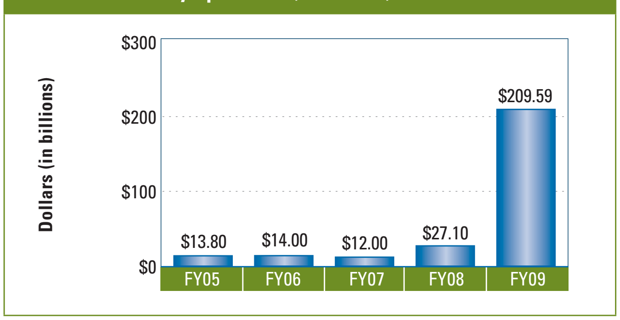


Net Cost of Treasury Operations. The Consolidated Statement of Net Cost presents the Department's gross and net cost for its four strategic missions: financial program, economic program, security program, and management program. The majority of the Net Cost of Treasury Operations is in the economic program which includes Troubled Asset Relief Program (TARP) activity and investments in the Government Sponsored Enterprises (GSEs). Financial program costs include costs associated with Treasury's role as the primary fiscal agent for the Federal Government in managing the nation's finances by collecting revenue, making federal payments, managing federal borrowing, performing central accounting functions, and producing coins and currency sufficient to meet the demand.

Net Cost of Treasury Operations (in millions)

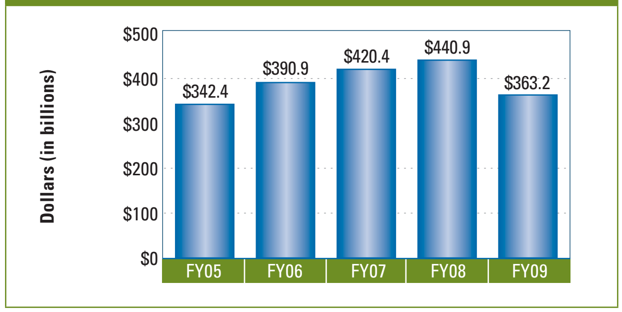


Net Cost of Treasury Operations (in billions)



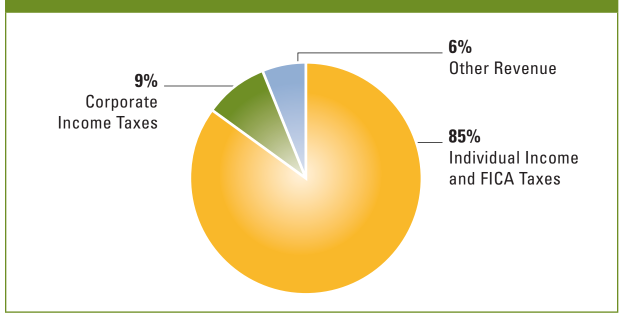
Net Federal Debt Interest Costs. The decrease of $77.7 billion in net interest paid on the federal debt is due to the decrease in the average interest rate for debt held by federal entities and federal debt held by the public.

Net Federal Debt Interest Cost (in billions)

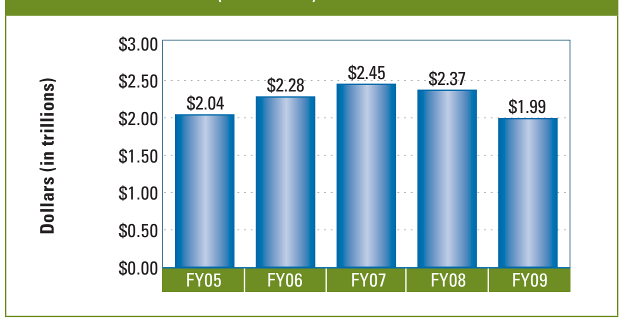


Custodial Revenue. Total net revenue collected by Treasury on behalf of the Federal Government includes various taxes, primarily income taxes, user fees, fines and penalties, and other revenue. Over 94.2 percent of the revenues are from income and social security taxes.

Total Revenue



Net Revenue Received (in trillions)



Improper Payments Information Act and Recovery Auditing Act

IMPROPER PAYMENTS INFORMATION ACT

BACKGROUND

The Improper Payments Information Act of 2002 (IPIA) requires agencies to review their programs and activities annually to identify those susceptible to significant improper payments. According to Office of Management and Budget (OMB) Circular A-123, *Management's Responsibility for Internal Control*, Appendix C, *Requirements for Effective Measurement and Remediation of Improper Payments* (A-123, Appendix C), "significant" means that an estimated error rate and a dollar amount exceed the threshold of 2.5 percent and $10 million of total program funding. A-123, Appendix C also requires the agency to implement a corrective action plan that includes improper payment reduction targets.

However, some federal programs are so complex that developing an annual error rate is not feasible. The government-wide Chief Financial Officers Council developed an alternative for such programs to assist them in meeting the IPIA requirements. Agencies may establish an annual estimate for a high-risk component of a complex program (e.g., a specific program population) with OMB approval. Agencies must also perform trend analyses to update the program's baseline error rate in the interim years between detailed program studies. When development of a statistically valid error rate is possible, the reduction targets are revised and become the basis for future trend analyses.

TREASURY'S RISK ASSESSMENT METHODOLOGY AND RESULTS FOR FISCAL YEAR 2009

Each year, Treasury develops a comprehensive inventory of all funding sources and conducts a risk assessment for improper payments on all of its programs and activities. The risk assessment performed on all of Treasury's programs and activities in fiscal year 2009 resulted in low and medium risk susceptibility for improper payments except for the Internal Revenue Service's (IRS) Earned Income Tax Credit (EITC) program. The high-risk status of this program is well-documented and has been deemed a complex program for the purposes of the IPIA.

EARNED INCOME TAX CREDIT

The EITC is a refundable tax credit that offsets income tax owed by low-income taxpayers and, if the credit exceeds the amount of taxes due, provides a lump-sum payment in the form of a refund to those who qualify. The fiscal year 2009 estimate is that a maximum of 28 percent ($13.3 billion) and a minimum of 23 percent ($11.2 billion) of the EITC total program payments are overclaims.

The IRS has a robust base enforcement program for the EITC which consists of examinations (audits), math error notices, and document matching. In fiscal year 2009 the IRS expanded its approach to decrease improper payments.

RECOVERY AUDITING ACT

BACKGROUND

In accordance with the *Recovery Auditing Act of 2002*, OMB Circular A-123, Appendix C, requires agencies issuing $500 million or more in contracts to establish and maintain recovery auditing activities and report on the results of those recovery efforts annually. Recovery auditing activities include the use of (1) contract audits, in which an examination of contracts pursuant to the audit and records clause incorporated in the contract is performed, (2) contingency contracts for recovery services in which the contractor is paid a percentage of the recoveries, and (3) internal review and analysis in which payment controls are employed to ensure that contract payments are accurate.

For Recovery Auditing Act compliance, Treasury requires each bureau and office to review their post-payment controls and report on recovery auditing activities, contracts issued, improper payments identified, and recoveries achieved. Bureaus and offices may use recovery auditing firms to perform many of the steps in their recovery program and identify candidates for recovery action.

RESULTS FOR FISCAL YEAR 2009

During fiscal year 2009, $5.3 billion in contracts (defined as issued and obligated contracts, modifications, task orders, and delivery orders) were issued. Improper payments in the amount of $1.5 million were identified from recovery auditing efforts and $1.4 million has been recovered, including prior year recoveries, with $117,630 outstanding as accounts receivable on September 30, 2009.

Note: Additional detail on Treasury's IPIA and Recovery Auditing Act Programs can be found in Appendix B.

Management Assurances

THE SECRETARY'S LETTER OF ASSURANCE

The Department of the Treasury's management is responsible for establishing and maintaining effective internal control and financial management systems that meet the objectives of the Federal Managers' Financial Integrity Act (FMFIA). Treasury has evaluated its management controls, internal controls over financial reporting, and compliance with federal financial systems standards. As part of the evaluation process, we considered results of extensive testing and assessment across the Department and independent audits.

Treasury provides assurance that the objectives of the Federal Managers' Financial Integrity Act over operations have been achieved, except for the material weaknesses noted below. In accordance with OMB Circular A-123, Appendix A, we provide qualified assurance on internal control over financial reporting based on the results of the assessment for the period ending June 30, 2009. Treasury is not in substantial compliance with the Federal Financial Management Improvement Act due to the material weakness involving revenue accounting systems.

As of September 30, 2009, Treasury has five material weaknesses as follows (with resolution time frames indicated):

Operations:

Internal Revenue Service

- Improved Modernization Management Controls Processes (fiscal year 2011)
- Computer Security (fiscal year 2012)

Financial Management Service

- Systems, Controls, and Procedures to Prepare the Government-wide Financial Statements (fiscal year 2012)

Financial Reporting:

Internal Revenue Service

- Financial Accounting of Revenue-Custodial (fiscal year 2010)

Treasury Departmental Offices

- Financial Management Practices (fiscal year 2010)

The external auditors identified one new material weakness in 2009. Treasury is taking action to address this issue in fiscal year 2010. Overall, Treasury continues to make progress in reducing management and control weaknesses and in meeting federal financial systems requirements.

Timothy F. Geithner

Timothy F. Geithner
December 15, 2009

Material Weaknesses, Audit Follow-up, and Financial Systems

SUMMARY OF MANAGEMENT ASSURANCES

SUMMARY OF MATERIAL WEAKNESSES

Material Weaknesses	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
IRS - Financial Accounting of Revenue - Custodial	1	0	0	0	0	1
IRS - Improve Modernization Management Controls and Processes	1	0	0	0	0	1
IRS - Computer Security	1	0	0	0	0	1
FMS - Systems, Controls, and Procedures to Prepare the Government-wide Financial Statements	1	0	0	0	0	1
DO - Financial Management Practices	0	1	0	0	0	1
Total Material Weaknesses	4	1	0	0	0	5

As of September 30, 2009, Treasury has five material weaknesses under Section 2 of the *Federal Managers' Financial Improvement Act* as shown in the tables below.

EFFECTIVENESS OF INTERNAL CONTROL OVER FINANCIAL REPORTING (FMFIA § 2)

Statement of Assurance	Qualified					
Material Weaknesses	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
IRS - Financial Accounting for Revenue - Custodial	1	0	0	0	0	1
DO - Financial Management Practices	0	1	0	0	0	1
Total Material Weaknesses	1	1	0	0	0	2

EFFECTIVENESS OF INTERNAL CONTROL OVER OPERATIONS (FMFIA § 2)

Statement of Assurance	Qualified					
Material Weaknesses	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
IRS - Improve Modernization Management Controls and Processes	1	0	0	0	0	1
IRS - Computer Security	1	0	0	0	0	1
FMS - Systems, Controls, and Procedures to Prepare the Government-wide Financial Statements	1	0	0	0	0	1
Total Material Weaknesses	3	0	0	0	0	3

CONFORMANCE WITH FINANCIAL MANAGEMENT SYSTEM REQUIREMENTS (FMFIA § 4)

Statement of Assurance	Systems conform to financial management system requirements					
Non-Conformances	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
Total Non-conformances	0	0	0	0	0	0

COMPLIANCE WITH FEDERAL FINANCIAL MANAGEMENT IMPROVEMENT ACT (FFMIA)		
	Agency	Auditor
Overall Substantial Compliance	No	No
1. System Requirements	No	
2. Accounting Standards	No	
3. USSGL at Transaction Level	No	

FEDERAL MANAGERS' FINANCIAL INTEGRITY ACT (FMFIA)

The management control objectives under FMFIA are to reasonably ensure that:

- programs achieve their intended results
- resources are used consistent with overall mission
- programs and resources are free from waste, fraud, and mismanagement
- laws and regulations are followed
- controls are sufficient to minimize any improper or erroneous payments
- performance information is reliable
- system security is in substantial compliance with all relevant requirements
- continuity of operations planning in critical areas is sufficient to reduce risk to reasonable levels
- financial management systems are in compliance with federal financial systems standards

Deficiencies that seriously affect an agency's ability to meet these objectives are deemed "material weaknesses." Treasury can provide assurance that the objectives of the FMFIA have been achieved, except for the material weaknesses noted in the Secretary's Letter of Assurance, which include one new weakness identified by the external auditors in November 2009. Although the last open material weakness is targeted to be closed in fiscal year 2012, Treasury is focusing on making sufficient progress to downgrade the weakness sooner.

Each year material weaknesses, both the resolution of existing ones and the prevention of new ones, receive special attention from management. In fiscal year 2009, Treasury continued to make resolution of material weaknesses a performance requirement for every executive, manager, and supervisor.

OFFICE OF MANAGEMENT AND BUDGET CIRCULAR A-123, APPENDIX A

The Department continues to strengthen and improve the execution of the Treasury mission through the application of sound internal controls over financial reporting. In response to Office of Management and Budget (OMB) Circular A-123, *Management's Responsibility for Internal Control*, Appendix A, Internal Control over Financial Reporting, Treasury developed and implemented an extensive annual testing and assessment methodology that identified and documented internal controls over financial reporting at the transaction level integrated with the Government Accountability Office's Standards for Internal Control. The testing and assessment were completed across all material Treasury bureaus and offices by June 30, 2009. Treasury provides qualified assurance that internal controls over financial reporting are effective as of June 30, 2009, due in large part to the computer security and financial accounting of revenue - custodial weaknesses at the Internal Revenue Service.

FEDERAL FINANCIAL MANAGEMENT IMPROVEMENT ACT (FFMIA)

FFMIA mandates that agencies "... implement and maintain financial management systems that comply substantially with federal financial management systems requirements, applicable federal accounting standards, and the United States Government Standard General Ledger at the transaction level." FFMIA also requires that remediation plans be developed for any entity that is unable to report substantial compliance with these requirements.

As of September 30, 2009, the Treasury Department's financial management systems were not in substantial compliance with FFMIA due to deficiencies with the IRS's financial management systems. The IRS has a remediation plan in place to correct the deficiencies. For each FFMIA recommendation, the remediation plan identifies specific remedies, target dates, responsible officials, and resource estimates required for completion. This plan is reviewed and updated quarterly. (Refer to Appendix D for detailed information.)

AUDIT FOLLOW-UP

During fiscal year 2009, Treasury continued its efforts to improve both the general administration of management and internal control issues throughout the Department and the timeliness of the resolution of all findings and recommendations identified by the Office of the Inspector General (OIG), the Treasury Inspector General for Tax Administration (TIGTA), the Special Inspector General for the Troubled Asset Relief Program (SIGTARP), the Government Accountability Office, and external auditors.

Treasury management at every level will maintain the momentum on accomplishing Planned Corrective Actions (PCAs) to resolve and implement sound solutions for all audit recommendations. Although Treasury has made great progress, considerably more work remains. Specifically, Treasury must provide timely and accurate performance to address PCA schedules and implementation and integrate the effects of those actions more fully into management decision-making processes. Treasury needs to identify more precisely what it costs to accomplish its varied missions and develop ways to improve overall performance. This will entail building upon the progress made in expanding the communication and coordination among offices variously involved in strategic planning, budget formulation, budget execution, performance management, and financial management.

FINANCIAL MANAGEMENT SYSTEMS FRAMEWORK

The Department's overall financial management systems framework consists of a Treasury-wide financial data warehouse, supported by a financial reporting tool and separate bureau financial systems. Currently, 14 bureaus are serviced by the Bureau of the Public Debt's Administrative Resource Center (BPD ARC) for core financial system processing. Bureaus submit their monthly financial data to the data warehouse within three business days of the month-end. The Department then produces monthly financial statements and reports for management analysis. This framework satisfies both the bureaus' diverse financial operational and reporting needs, as well as the Department's internal and external reporting requirements. The financial data warehouse is part of the overarching Treasury-wide Financial Analysis and Reporting System (FARS), which also includes applications for the bureaus to report the status of their performance measures and the status of their planned audit corrective actions. In addition to the existing FARS applications, the Department is reviewing options for implementing a new fleet management application. The fleet application would maintain a consolidated inventory of Treasury vehicles to enhance management control and reporting. Treasury is evaluating existing government owned and operated systems to support this functionality.

Treasury's FARS applications operate at a contractor operated hosting facility. In accordance with the guidance contained in the American Institute of Certified Public Accountants' Statement of Auditing Standards (SAS) No. 70, *Service Organizations,* the service provider's independent auditors examined the controls for the dedicated hosting service. In the opinion of the auditors, the description of the controls presents fairly, in all material respects, the relevant aspects of the provider's controls that had been placed in operation as of September 30, 2009. Also, the controls described are suitably designed to provide reasonable assurance that the specified control objectives would be achieved if the described controls were complied with satisfactorily and customer organizations applied the controls contemplated in the design of the provider's controls.

The Department continues to eliminate redundant and outdated financial management systems with the goal of consolidating financial management activities to improve productivity. As of September 30, 2009, the number of financial management systems decreased to 55, down from 60 at the end of fiscal year 2008. Many of these systems support bureau-specific program functions, while others support internal bureau financial management. These systems are either maintained and operated by the individual bureaus, or provided on a cross-serviced basis by BPD ARC.

BPD ARC has been designated by OMB as a Financial Management Line of Business Shared Service Provider (SSP). A SSP provides financial management systems and services for other federal organizations. BPD ARC currently services 29 federal entities for core financial systems, including 14 Treasury bureaus and reporting entities. Using a SSP enables the bureaus to streamline their financial management activities and achieve more efficient and cost effective business performance by reducing maintenance and operational costs. Treasury will continue to evaluate opportunities to consolidate financial management systems and better utilize existing federal resources. The Department will work with the remaining bureaus to develop plans to migrate to Treasury's SSP for core financial systems in accordance with the Financial Management Line of Business requirements.

As part of the Department's E-Government initiative, BPD ARC also provides systems and service support to 14 Treasury bureaus in the processing of their human resources and travel activities. BPD ARC's human resource management system supports the bureaus' specific human resources needs and provides consolidated systems and resources. BPD ARC's consolidated travel system and activity processing has reduced redundant systems and merged travel processes.

The Department's FARS applications have also been used to support other federal agencies. Since the initial start of the Department of Homeland Security (DHS), Treasury serviced DHS in the preparation of its consolidated financial statements. Beginning with fiscal year 2009, DHS implemented the FARS financial applications in its own systems environment and is now generating its financial statements and reports. As a result of this arrangement, DHS was able to take advantage of existing government systems and did not have to develop new systems to support its financial reporting requirements.

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Part 2
Annual Financial Report

Message from the Assistant Secretary for Management and Chief Financial Officer

December 15, 2009

Secretary Geithner's message describes the extraordinary actions the Department of the Treasury has taken to help stabilize the nation's financial systems and provide the foundation for a sustainable economic recovery. Following the enactment of the Housing and Economic Recovery Act in July 2008 and the Emergency Economic Stabilization Act in early fiscal year 2009, Treasury took bold and assertive action to restore confidence in the financial system and ease the housing crisis.

Building upon this effort, with the enactment of the American Recovery and Reinvestment Act (Recovery Act) just weeks after the new Administration took office, Treasury quickly implemented additional new programs to stimulate the economy. Treasury's Recovery Act programs include:

- tax benefits to more than 110 million families, or 95 percent of working families;
- providing numerous tax incentives for businesses and households;
- supporting local and state government development;
- creating new methods of low cost borrowing; and
- investing in renewable energy, low income housing, and health care.

These programs have positively impacted the lives of millions of Americans. Treasury has taken a risk-based approach and is focused on balancing the requirements of speed, quality, and accountability to ensure that Recovery Act funds are distributed quickly and accurately.

The magnitude and complexity of these new economic stabilization programs coupled with the large volume and dollar amounts of these programs made the preparation and audit of the fiscal year 2009 financial statements a difficult undertaking. Despite these challenges, the Department received an unqualified audit opinion on both our new Office of Financial Stability/Troubled Asset Relief Program and again on our Treasury-wide fiscal year 2009 financial statements. The Department has five material weaknesses, including one new area of concern, regarding financial management practices at the departmental level. This new area of weakness is directly related to Treasury's expanded roles and programs. We are taking corrective action to address this area in 2010. We also made substantial progress on the four existing material weaknesses open as of September 30, 2008. Those weaknesses involve complex solutions that will require several years of sustained efforts to resolve. The Department is also continuing to devote special attention to programs included in the Government Accountability Office's High Risk List and management and performance challenges identified by the Department's Inspectors General. These challenges do not necessarily indicate deficiencies in performance – rather, they represent inherent risks based on the nature of Treasury's programs and will be monitored continuously.

While Treasury has already executed extraordinary measures to stabilize our economy, we will continue to take bold and assertive action to restore America's confidence in the financial system, ease the housing crisis, and put our country back on a path of sustainable economic and job growth.

Dan Tangherlini
Assistant Secretary for Management
and Chief Financial Officer

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

OFFICE OF
INSPECTOR GENERAL

December 16, 2009

INFORMATION MEMORANDUM FOR SECRETARY GEITHNER

FROM: Eric M. Thorson
Inspector General

SUBJECT: Audit of the Department of the Treasury's Financial Statements for Fiscal Years 2009 and 2008

INTRODUCTION

I am pleased to transmit KPMG LLP's report on the Department of the Treasury's (the Department) financial statements as of and for the fiscal years (FY) ending September 30, 2009 and 2008.

The Department of the Treasury Office of Inspector General is responsible for ensuring that the financial statement audit of the Department of the Treasury is conducted in accordance with the Chief Financial Officers' Act of 1990, as amended by the Government Management Reform Act of 1994.

The Department was granted a reporting extension from the Director of the Office of Management and Budget to complete its Agency Financial Report (AFR) by December 15, 2009. This extension was provided due to the unprecedented challenges that the Department faced in FY 2009 with the establishment of the Office of Financial Stability. However, since the AFR was not completed timely, this report could not be issued until December 16, 2009.

RESULTS OF INDEPENDENT AUDIT

Under a contract monitored by my office, KPMG LLP, an independent certified public accounting firm, performed an audit of the Department's FY 2009 and 2008 financial statements. Among other things, the contract required that the audit be performed in accordance with generally accepted government auditing standards issued by the Comptroller General of the United States; Office of Management and Budget Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements*, as amended; and the GAO/PCIE Financial Audit Manual.

In its audit of the Department, KPMG LLP

- found that the financial statements were fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles;
- reported that weaknesses related to 1) financial management practices at the Departmental level, and 2) financial systems and reporting at the Internal Revenue Service represent material weaknesses for the Department as a whole;

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- reported that weaknesses related to 1) financial accounting and reporting at the Office of Financial Stability, and 2) information system controls at the Financial Management Service represent significant deficiencies for the Department as a whole;

- reported an instance of noncompliance with laws and regulations related to the Internal Revenue Code Section 6325; and

- reported that the Department's financial management systems did not substantially comply with the requirements of the Federal Financial Management Improvement Act of 1996

EVALUATION OF AUDITORS' PERFORMANCE

To ensure the quality of the audit work performed, we reviewed KPMG LLP's approach and planning of the audit, evaluated the qualifications and independence of the auditors, monitored the progress of the audit at key points, reviewed and accepted KPMG LLP's audit report, and performed other procedures that we deemed necessary. Additionally, we provide oversight of the audits of financial statements and certain accounts and activities conducted at 13 component entities of the Department. Our review, as differentiated from an audit performed in accordance with generally accepted government auditing standards, was not intended to enable us to express, and we do not express, an opinion on the financial statements or conclusions about the effectiveness of internal control or on whether the Department's financial management systems substantially complied with the Federal Financial Management Improvement Act of 1996 or conclusions on compliance with laws and regulations. KPMG LLP is responsible for the attached auditors' report dated December 15, 2009, and the conclusions expressed in that report. However, our review disclosed no instances where KPMG LLP did not comply, in all material respects, with generally accepted government auditing standards.

I appreciate the courtesies and cooperation extended to KPMG LLP and my staff during the audit. Should you or your staff have questions, you may contact me at (202) 622-1090 or Marla A. Freedman, Assistant Inspector General for Audit, at (202) 927-5400.

Attachment

cc: Daniel Tangherlini
Assistant Secretary for Management
and Chief Financial Officer

KPMG LLP
2001 M Street, NW
Washington, DC 20036

Independent Auditors' Report

Inspector General
U.S. Department of the Treasury:

We have audited the accompanying consolidated balance sheets of the U.S. Department of the Treasury (Treasury Department) as of September 30, 2009 and 2008, and the related consolidated statements of net cost, and changes in net position, combined statements of budgetary resources, and the statements of custodial activity (hereinafter referred to as "consolidated financial statements") for the years then ended. The objective of our audits was to express an opinion on the fair presentation of these consolidated financial statements. These consolidated financial statements are incorporated in the accompanying *U.S. Department of the Treasury Fiscal Year 2009 Agency Financial Report (AFR).*

We did not audit the amounts included in the consolidated financial statements related to the Internal Revenue Service (IRS) and the Office of Financial Stability (OFS), component entities of the Treasury Department. The financial statements of the IRS and the OFS were audited by another auditor whose reports thereon have been provided to us. Our opinions, insofar as they relate to the amounts included for the IRS and the OFS, are based solely on the reports of the other auditor.

In connection with our fiscal year 2009 audit, we, and the other auditor, also considered the Treasury Department's internal control over financial reporting and tested the Treasury Department's compliance with certain provisions of applicable laws, regulations, contracts, and grant agreements that could have a direct and material effect on these consolidated financial statements. Our conclusions on internal control over financial reporting and compliance and other matters, insofar as they relate to the IRS and the OFS, are based solely on the reports of the other auditor.

Summary

As stated in our opinion on the consolidated financial statements, based on our audits and the reports of the other auditor, we concluded that the Treasury Department's consolidated financial statements as of and for the years ended September 30, 2009 and 2008, are presented fairly, in all material respects, in conformity with U.S. generally accepted accounting principles.

As discussed in Note 29, the Treasury Department is a participant in significant legislation and transactions whose purpose is to assist in stabilizing the financial markets.

Notes 1A, 8, 9, and 12, respectively, discuss the following matters:

- Treasury Department's consolidated financial statements do not include the assets, liabilities, or results of operations of commercial entities in which the Treasury Department has a significant equity interest as the Treasury Department has determined that none of these entities meet the criteria of a federal entity and are therefore not included in the Treasury Department's consolidated financial statements.
- The valuation of certain Treasury Department's investments, loans, and asset guarantees is based on estimates. These estimates are inherently subject to substantial uncertainty arising from the likelihood of future changes in general economic, regulatory, and market conditions. As such, there will be differences between the net estimated value of these investments, loans, and asset guarantees at

September 30, 2009, and the amounts that the Treasury Department will ultimately realize from these assets. Such differences may be material and will also affect the ultimate cost of the programs to the Treasury Department.

Our, and the other auditor's, consideration of internal control over financial reporting identified significant deficiencies in the following areas:

- Financial Management Practices at the Departmental Level (Repeat Condition)
- Financial Systems and Reporting at the IRS (Repeat Condition)
- Financial Accounting and Reporting at the Office of Financial Stability (OFS)
- Information System Controls at the Financial Management Service (FMS)

We consider the significant deficiencies related to Financial Management Practices at the Departmental Level, and Financial Systems and Reporting at the IRS noted above to be material weaknesses.

The results of our tests, and the tests performed by the other auditor, of compliance with certain provisions of laws, regulations, contracts, and grant agreements disclosed an instance of noncompliance with *Internal Revenue Code* (IRC) Section 6325, that is required to be reported under *Government Auditing Standards*, issued by the Comptroller General of the United States, and Office of Management and Budget (OMB) Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements*, as amended. In addition, the Treasury Department's financial management systems did not substantially comply with the *Federal Financial Management Improvement Act of 1996* (FFMIA) requirements related to compliance with Federal financial management system requirements (FFMSR), applicable Federal accounting standards, and the U.S. Government Standard General Ledger (SGL) at the transaction level.

The following sections discuss our opinion on the Treasury Department's consolidated financial statements; our, and the other auditor's, consideration of the Treasury Department's internal controls over financial reporting; our, and the other auditor's tests of the Treasury Department's compliance with certain provisions of applicable laws, regulations, contracts, and grant agreements; and management's and our responsibilities.

Opinion on the Financial Statements

We have audited the accompanying consolidated balance sheets of the Department of the Treasury as of September 30, 2009 and 2008, and the related consolidated statements of net cost, changes in net position, the combined statements of budgetary resources, and the statements of custodial activity, for the years then ended.

We did not audit the amounts included in the consolidated financial statements related to the IRS, a component entity of the Treasury Department, which reflect total assets of $36.8 billion and $35.6 billion, net costs of operations of $12.5 billion and $12.2 billion, budgetary resources of $12.8 billion and $12.2 billion, and custodial revenues of $2.3 trillion and $2.7 trillion, before applicable eliminating entries, as of and for the years ended September 30, 2009 and 2008, respectively. The financial statements of the IRS as of and for the years ended September 30, 2009 and 2008, were audited by another auditor whose report dated November 5, 2009, has been provided to us, and our opinion, insofar as it relates to the amounts included for the IRS, is based solely on the report of the other auditor.

We did not audit the amounts included in the consolidated financial statements related to the OFS, a component entity of the Treasury Department, which reflect total assets of $337.4 billion, net costs of operations of $41.6 billion and budgetary resources of $699.4 billion, before applicable eliminating entries, as of and for the year ended September 30, 2009. The financial statements of the OFS as of and for the year ended September 30, 2009, were audited by another auditor whose report dated December 4, 2009, has been provided to us, and our opinion, insofar as it relates to the amounts included for the OFS, is based solely on the report of the other auditor.

In our opinion, based on our audits, and the reports of the other auditor, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Department of the Treasury as of September 30, 2009 and 2008, and its net costs, changes in net position, budgetary resources, and custodial activity for the years then ended, in conformity with U.S. generally accepted accounting principles.

As discussed in Note 29, the Treasury Department is a participant in significant legislation and transactions whose purpose is to assist in stabilizing the financial markets.

Notes 1A, 8, 9, and 12, respectively, discuss the following matters:

- Treasury Department's consolidated financial statements do not include the assets, liabilities, or results of operations of commercial entities in which the Treasury Department has a significant equity interest as the Treasury Department has determined that none of these entities meet the criteria of a federal entity and are therefore not included in the Treasury Department's consolidated financial statements.
- The valuation of certain Treasury Department's investments, loans, and asset guarantees is based on estimates. These estimates are inherently subject to substantial uncertainty arising from the likelihood of future changes in general economic, regulatory, and market conditions. As such, there will be differences between the net estimated value of these investments, loans, and asset guarantees at September 30, 2009, and the amounts that the Treasury Department will ultimately realize from these assets. Such differences may be material and will also affect the ultimate cost of the programs to the Treasury Department.

The information in the *AFR* in Part 1: *Management's Discussion and Analysis (MD&A)*, and the Required Supplemental Information in Part 2: *Annual Financial Report*, is not a required part of the consolidated financial statements, but is supplementary information required by U.S. generally accepted accounting principles. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of this information. However, we did not audit this information and, accordingly, we express no opinion on it.

Our audits, and the audits of the other auditor, were conducted for the purpose of forming an opinion on the consolidated financial statements taken as a whole. The information in the *Message from the Secretary of the Treasury*, the *Message from the Assistant Secretary for Management and Chief Financial Officer* in Part 2, and *Other Accompanying Information* in Part 3 is presented for purposes of additional analysis and is not required as part of the consolidated financial statements. This information has not been subjected to auditing procedures and, accordingly, we express no opinion on it.

Internal Control Over Financial Reporting

Our, and the other auditor's, consideration of the internal control over financial reporting was for a limited purpose described in the Responsibilities section of this report, and was not designed to identify all deficiencies in the internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. This report also includes our consideration of the results of the other auditor's testing of internal control over financial reporting that is reported on separately by the other auditor. The other auditor performed an examination of internal control over financial reporting for the purpose of providing an opinion on the effectiveness of IRS's and OFS's internal controls. This report, insofar as it relates to the results of the other auditor, is based solely on the reports of the other auditor.

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. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. A material weakness is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the Treasury Department's financial statements will not be prevented or detected and corrected on a timely basis.

In our fiscal year 2009 audit, we, and the other auditor, identified the significant deficiencies in internal control over financial reporting, discussed below. The significant deficiencies related to Financial Management Practices at the Departmental Level and Financial Systems and Reporting at the IRS are considered to be material weaknesses. Because of the IRS material weakness in internal controls discussed below, the other auditor's opinion on IRS' internal control stated that the IRS did not maintain effective internal control over financial reporting as of September 30, 2009.

Material Weaknesses

Financial Management Practices at the Departmental Level (Repeat Condition)

We identified the following two significant deficiencies that we collectively consider to be a material weakness at the Departmental level. Both are repeat conditions related to Department-wide control environment weaknesses.

Department-wide Entity Level Controls Affecting Financial Reporting

The Office of Accounting and Internal Control (AIC) within the Office of the Deputy Chief Financial Officer (ODCFO), and the Office of Performance Budgeting and Strategic Planning (OPBSP) are responsible for establishing and maintaining financial policies that guide financial reporting throughout the Treasury Department, and ensure the overall integrity of financial data reported at the consolidated level. The Treasury Department's financial management offices are understaffed and have not grown proportionally in relation to the Treasury Department's rapid growth in new programs and operations in fiscal year 2009. Specifically, the Department lacked sufficient personnel in key accounting and managerial functions, who had the experience and core technical competencies to ensure that the Department's financial statements were prepared accurately, and in compliance with generally accepted accounting principles on a consistent basis.

For example, we noted the following:

- Two senior key accounting positions with responsibility for supervisory review and management of the Department's consolidation process were vacant from April 2009 through July 2009 creating a gap in continuity and technical knowledge. Specifically, one key senior staff accounting position and one key supervisory accounting position went unfilled for a period of one month and four months, respectively.
- A key position within OPBSP that has significant responsibilities for review and oversight of departmental budget activities was vacant for two months;
- Staffing shortages continue to exist within AIC and the Treasury Department's Office of Financial Management (OFM). These offices have significant program management and accounting responsibilities; and
- A comprehensive, formalized succession plan has not been prepared for key personnel in AIC and other OFM officials who have significant institutional knowledge of the Treasury Department's accounting and reporting processes that are at or near retirement eligibility status and bear excessive workloads.

These conditions occurred during a period when the Treasury Department was undergoing significant program changes as well as addressing unique accounting and reporting issues related to new programs. We identified several material financial reporting errors resulting from a lack of experienced and qualified senior staff to support the Departmental financial accounting and reporting consolidation effort. The lack of adequate experienced senior accounting staff within AIC and OFM, including the lack of capable support staff with sufficient knowledge and experience led to significant delays in preparing supporting accounting documentation and information as well as communication of issues when addressing critical accounting matters.

In previous years, we reported a significant deficiency in this area, and although steps have been taken towards filling key open positions, the Treasury Department has not addressed long-term human capital needs in the area of financial management. The risk of material misstatement in the consolidated financial statements increases without sufficient personnel who have the requisite financial accounting background, knowledge, and expertise to perform these functions at the Department level.

Financial Accounting and Reporting

The Departmental level accounting and financial reporting infrastructure, including policies, procedures, processes and internal controls, need improvement. We identified the following weaknesses that had a pervasive impact on the effectiveness of internal controls over the Treasury Department's consolidated financial reporting.

- Supervisory and monitoring control procedures were not consistently performed over certain financial data and other information transmitted by Treasury Department components. Monitoring control procedures to examine and resolve differences between subsidiary records and the general ledger, misclassified assets, and various over and understatements of proprietary and budgetary account balances were not performed timely.

- Written policies and procedures to account for and report various non-routine, complex, and unique transactions, such as accounting and reporting of General Fund transactions, U.S. Mint's Seigniorage, accrued interest and discount on debt, transfers to the General Fund, and non-entity transactions were either not documented or required further improvement.

- AIC has not developed adequate written procedures for the consolidation process nor procedures for performing certain key financial statements analyses such as that for proprietary and budgetary relationships, and cumulative results of operations.

- As a result of the Housing and Economic Recovery Act of 2008, the Treasury Department is involved in various unique financial transactions that are to be accounted for under the Federal Credit Reform Act of 1990, as amended (FCRA). FCRA has significant documentation requirements and the Treasury Department did not have documentation in place for a majority of the year.

- AIC procedures for monitoring compliance with existing, as well as new laws and regulations that apply to the Treasury Department need improvement. Specifically, we noted a lack of communication during the year between the Treasury Department's Office of General Counsel (OGC) and AIC on matters related to new legislation, the assessment of compliance requirements, if any, and subsequent actions to be taken by the Treasury Department. We noted an instance where legislation impacting the Treasury Department's financial reporting had not been identified or communicated to AIC and the legislation, the Supplemental Appropriation Act of 2009 (PL 111-32 Section 14), was also not identified in OGC's listing of laws and regulations provided at year-end.

- Our review of Department-wide testing and reporting on internal control over financial reporting, in accordance with OMB Circular No. A-123, *Management's Responsibility for Internal Control* (A-123), identified implementation issues similar to the prior year. The Treasury Department established an implementation plan (Plan) to assess, document, test, and report on internal control over financial reporting. However, this Plan was not updated timely for new events and transactions. Specifically, procedures and controls identified in the Plan for testing various transactions, information technology, and assessing compliance with laws and regulations need further improvement. In addition, implementation of A-123 requirements including the preparation of supporting documentation for work conducted at Treasury components should be improved.

These conditions resulted in material financial statement account balance variances that remained unexplained, and account balances without adequate supporting documentation. In addition, material adjustments were recorded without proper analysis and documentation. We also noted several instances where the reviews conducted were not effective, allowing errors to remain undetected until discovered during audit procedures.

The *Federal Managers' Financial Integrity Act of 1982* (FMFIA) requires that agencies establish internal controls according to standards prescribed by the Comptroller General and specified in the Government Accountability Office's (GAO) *Standards for Internal Control in the Federal Government (Standards).* The GAO defines "internal control" as an integral component of an organization's management that provides reasonable assurance that the following objectives are achieved: effectiveness and efficiency of operations, reliability of financial reporting, and compliance with applicable laws and regulations. The GAO *Standards* identify the control environment as one of the five key elements of control, which emphasizes the importance of control conscientiousness in management's operating philosophy and commitment to internal control. These standards cover controls such as human capital practices, supervisory reviews, and segregation of duties, policies, procedures, and monitoring.

A-123 states that monitoring the effectiveness of internal control should occur in the normal course of business. In addition, periodic reviews, reconciliations or comparisons of data should be included as part of the regular assigned duties of personnel. Periodic assessments should be integrated as part of management's continuous monitoring of internal control, which should be ingrained in the agency's operations. An effective, continuous monitoring program can level the resources needed to maintain effective internal controls throughout the year.

Recommendations

We recommend that the Assistant Secretary for Management and Chief Financial Officer (ASM/CFO):

Department-wide Entity Level Controls Affecting Financial Reporting

1. Conduct a review of the current status of staffing, skill competencies, contract support, and training, within the AIC, OPBSP, and OFM to identify gaps between existing skills sets and those needed to fully perform the daily operations of AIC, OPBSP, and OFM as well as to establish or refine policy and procedures, where necessary.

   The review should be conducted either internally or by an independent specialist, and should identify the additional managerial skill sets needed, such as financial accounting background, knowledge, and expertise required to strengthen the financial accounting and reporting infrastructure, and, once strengthened, to effectively manage the processes necessary to be conducted throughout the year.

2. Once the review is completed (per recommendation 1 above), hire staff, or consider transferring suitable staff from other offices within the Treasury Department to meet these needs. In addition, provide training and guidance to staff as necessary to enhance the quality and timeliness of work products in light of the increased responsibilities discussed above.

Financial Accounting and Reporting

3. Conduct a detailed review of the existing processes to analyze and review the consolidated financial reporting process.

4. Establish new policies or improve existing policies and procedures to ensure that:

   a. Quality control reviews are performed on the consolidated financial reporting process as well as on the consolidated financial statements by responsible officials to ensure that all errors and inconsistencies are identified and corrected in a timely manner;

   b. Effective reviews are conducted by senior AIC officials on documentation prepared to support consolidated financial statement amounts to ensure that the supporting documents and information are accurate and complete, and such review is documented; and

   c. Key consolidation accounting and reporting activities are captured in a manner that is easily followed by staff not familiar with the consolidation process.

5. Require that documentation is developed to support all new and/or unique accounting and reporting requirements as well as non-routine or complex accounting and reporting matters, and periodically updated (at least annually). For example, any new financial statement footnote disclosures that are developed should include a policy memo, financial statement footnote disclosure format, as well as evidence of review by responsible officials within AIC of both the policy and the format to be followed.

6. Require periodic monitoring by senior management of the implementation of policy and procedures. For example, policies and procedures related to FCRA transactions should require periodic examination of the performance of the credit programs to re-estimate cash flow projections and assumptions.

7. Require that communication is initiated on a periodic basis with OGC, to obtain information and documentation of any laws and regulations that apply at the Treasury Department/component level, including documentation of OGC's assessment of compliance requirements especially those having a financial impact. Such communication should be documented and referred to by management in monitoring the population of laws and regulations that are material to the financial statements.

8. Update the Treasury Department's A-123 Plan annually to incorporate new events and transactions, and require components to fully comply with the requirements of the Plan. Further, implement a more robust monitoring process of the A-123 work being conducted by components to ensure that the Treasury Department's A-123 guidance is fully implemented and complied with, and supports components' assurance statements on internal control.

Financial Systems and Reporting at the IRS (Repeat Condition)

The IRS continued to make strides in addressing its internal control deficiencies. However, internal control and financial management system deficiencies continued to make it necessary for IRS to use resource-intensive compensating processes to prepare its financial statements.

The challenges the IRS faces as a result of these remaining deficiencies adversely affect IRS's ability to (1) produce reliable financial statements without significant compensating procedures, and (2) obtain current, complete, and accurate information needed to make well-informed decisions. As the IRS continues to progress towards increasingly automated financial management processes, the continued material weakness in internal control over information security that jeopardizes the reliability of the financial information that IRS processes, could have serious implications in determining whether IRS's financial statements are fairly stated. This weakness also continues to increase the risk that sensitive taxpayer information may be compromised.

The material weaknesses in internal control over financial reporting identified by the auditors of the IRS's financial statements, which are repeat conditions and collectively considered a material weakness for the Treasury Department as a whole, are summarized as follows:

- Weaknesses in internal control over unpaid tax assessments resulted in the IRS's inability to effectively manage unpaid tax assessments on an ongoing basis and in errors in taxpayer accounts leading to increased taxpayer burden. Specifically, systems limitations and weaknesses in processing controls resulted in the following issues: (1) IRS's reported balances for taxes receivable and other unpaid assessments were not supported by its core general ledger system for tax administration-related transactions, (2) IRS lacked a subsidiary ledger for unpaid tax assessments that would allow it to produce reliable, useful, and timely information with which to manage and report externally, and (3) IRS experienced errors and delays in recording taxpayer information, payments, and other activities.

- New and previously identified weaknesses in internal control over information security continue to place IRS systems at risk. Specifically, controls over information systems are not effectively established and maintained. Further, during the fiscal year 2009 audit, additional significant weaknesses in internal control over information security, along with previously identified weaknesses, continued to jeopardize the confidentiality, availability, and integrity of information processed by IRS's key systems, increasing the risk of material misstatement for financial reporting.

The material weaknesses in internal control noted above may adversely affect decisions by IRS's management that are based, in whole or in part, on information that is inaccurate because of these deficiencies.

Additional details related to the material weakness identified above have been provided to IRS management by the auditors of the IRS's financial statements in their report dated November 5, 2009.

Recommendations

Recommendations to address prior year issues that encompass the material weakness discussed above have previously been provided to IRS management by the auditors of the IRS's financial statements. New recommendations to address issues identified in the fiscal year 2009 IRS financial statement audit that comprise the material weakness discussed above will be provided to IRS management by the auditors of IRS's financial statements in separate reports. We recommend that the ASM/CFO provide effective oversight to ensure that corrective actions are taken by the IRS to fully address this material weakness.

SIGNIFICANT DEFICIENCIES

Financial Accounting and Reporting at the OFS

The OFS has made progress in building a financial reporting structure, including developing an internal control system over Troubled Assets Recovery Program (TARP) activities and transactions and addressing key accounting and financial reporting issues necessary to enable it to prepare financial statements. However, OFS's financial reporting structure continued to evolve throughout the year as new TARP programs were implemented, which posed a challenge to OFS's ability to establish a comprehensive system of internal control while simultaneously reacting to market events and implementing TARP initiatives. This challenge contributed to the significant deficiencies in OFS's internal control that the other auditor identified. These OFS deficiencies collectively constitute a significant deficiency for the Treasury Department as a whole and are summarized as follows.

- Control deficiencies were identified related to accounting and financial reporting processes. OFS did not effectively implement its review and approval process for preparing its financial statements and related disclosures for TARP. The other auditor identified incorrect amounts and inaccurate, inconsistent, and incomplete disclosures in OFS's draft financial statements, footnotes, and MD&A for TARP that are significant, but not material, and that were not detected by OFS. OFS had not finalized its procedures related to its processes for accounting for certain program transactions, preparing its financial statements, and its oversight and monitoring of financial-related services provided to OFS by asset managers and certain financial agents. OFS did not have proper segregation of duties over a significant accounting database it uses in valuing its assets in that the same individual was responsible for performing both the data entry and the reconciliation of the data output.

- OFS did not effectively implement its verification procedures for certain assumptions and related data that were input into the economic and financial credit subsidy models used for the valuation of OFS's loans, equity investments, and asset guarantees. Specifically, the other auditor identified data input errors to the estimation models, such as incorrect dividend rates and maturity dates that were not detected by OFS's verification procedures.

Additional details related to the significant deficiency identified above have been provided to OFS management by the auditors of the OFS's financial statements in their report dated December 4, 2009.

Recommendations

We recommend that the ASM/CFO provide effective oversight to ensure that corrective actions are taken by the OFS to fully address this significant deficiency.

Information System Controls at the FMS

Information controls and security programs managed by the FMS need improvement. Current year tests conducted over IT general controls revealed that the necessary policies and procedures to detect and correct control and functionality weaknesses have not been consistently documented, implemented, or enforced. Specifically, issues were identified in the areas of (1) security management; (2) access; (3) change configuration; (4) segregation of duties; and (5) contingency planning. Individually or collectively, the conditions identified could compromise FMS's ability to ensure security over sensitive financial data and reliability of key systems.

The above weaknesses collectively serve to weaken the IT general control environment at FMS.

Recommendations

The detailed findings and related recommendations have been provided to FMS management in a separate report. We recommend that the ASM/CFO provide effective oversight and the resources necessary to ensure that information security requirements over financial systems are implemented at FMS.

Compliance

The results of certain of our tests, and the tests performed by the other auditor, of compliance as described in the Responsibilities section of this report, exclusive of those referred to in FFMIA, disclosed the following instance of noncompliance that is required to be reported herein under *Government Auditing Standards* or OMB Bulletin No. 07-04.

- ***Noncompliance with IRC Section 6325* -** The IRC grants the IRS the power to file a lien against the property of any taxpayer who neglects or refuses to pay all assessed Federal taxes. Under IRC Section 6325, the IRS is required to release a Federal tax lien within 30 days after the date the tax liability is satisfied, or has become legally unenforceable, or the Secretary of the Treasury has accepted a bond for the assessed tax. Despite actions the IRS has taken to date to improve its lien release process, instances continued to be identified where the IRS did not timely release the applicable Federal tax lien within 30 days of the tax liability being either paid off or abated as required by the IRC (Repeat Condition).

The results of our other tests, and the tests performed by the other auditor, of compliance as described in the Responsibilities section of this report, exclusive of those referred to in FFMIA, disclosed no instances of noncompliance or other matters that are required to be reported herein under *Government Auditing Standards* or OMB Bulletin No. 07-04.

The results of our tests of FFMIA, and the tests performed by the other auditor, disclosed instances where the Department's financial management systems did not substantially comply with FFMIA Section 803(a) requirements (Repeat Condition) related to compliance with (1) FFMSR, (2) applicable Federal accounting standards, and (3) the SGL at the transaction level, as described below.

Instances of noncompliance with FFMSR are summarized below:

- IRS's core general ledger system does not conform to the requirements of FFMSR, contained in OMB Circular A-127, *Financial Management Systems*.

- Material weaknesses in IRS's internal control over information security continue to threaten (1) integrity of the financial statements and the accuracy and availability of financial information needed to support day-to-day decision making, and (2) confidentiality of proprietary information.

An instance of noncompliance with Federal accounting standards is summarized below:

- IRS's automated systems for tax related transactions did not support the net taxes receivable amount on IRS's balance sheet and other required supplemental information related to uncollected taxes - compliance assessments and tax write-offs - in accordance with Statement of Federal Financial Accounting Standards No. 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*.

An instance of noncompliance with the SGL at the transaction level is summarized below:

- IRS's core general ledger system for tax-related activities does not comply with the SGL at the transaction level and also does not post transactions in conformance with SGL posting models.

The Secretary of the Treasury also stated in his Letter of Assurance, included in Part 1: *Management's Discussion and Analysis*, of the accompanying *AFR* that the Treasury Department cannot provide assurance that its financial management systems are in substantial compliance with FFMIA. The IRS has established a remediation plan to address the conditions that lead to its systems' substantial noncompliance with the requirements of FFMIA. This plan outlines the actions to be taken to resolve these issues, many of which are long-term in nature and are tied to IRS's system modernization efforts. The Treasury

Department's remedial actions and related timeframes are presented in Appendix D: *Material Weaknesses, Audit Follow-up, Financial Systems, and Recovery Act Risk Management* of the *AFR*.

Recommendation

We recommend that the ASM/CFO provide effective oversight to ensure that (1) IRS implements appropriate controls so that Federal tax liens are released in accordance with Section 6325 of the IRC; and (2) IRS implements its plan of action to solve financial management problems so as to enable resolving the identified instances of financial management systems' noncompliance with the requirements of FFMIA. Detailed recommendations to address the noncompliance findings discussed above have been provided to IRS management by the auditors of the IRS's financial statements.

Management's Response to Internal Control and Compliance Findings

The Department's management has indicated, in a separate letter immediately following this report, that it concurs with the findings presented in this section of our report. Further, it has responded that it will take corrective action, as necessary, to ensure the matters presented are addressed by the respective component management within the Treasury Department. We did not audit the Treasury Department's response and, accordingly, we express no opinion on it.

* * * * *

We noted certain additional matters involving internal control over financial reporting and its operation that we will report to the Treasury Department's management in a separate letter.

Responsibilities

Management's Responsibilities. Management is responsible for the consolidated financial statements; establishing and maintaining effective internal control; and complying with laws, regulations, contracts, and grant agreements applicable to the Treasury Department.

Auditors' Responsibilities. Our responsibility is to express an opinion on the fiscal year 2009 and 2008 consolidated financial statements of the Treasury Department based on our audits and the reports of the other auditor. We, and the other auditor, conducted our audits in accordance with the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Also, we conducted our audit in accordance with auditing standards generally accepted in the United States of America and OMB Bulletin No. 07-04. Those standards and OMB Bulletin No. 07-04 require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Treasury Department's internal control over financial reporting. Accordingly, we express no such opinion.

An audit also includes:

- Examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements;
- Assessing the accounting principles used and significant estimates made by management; and
- Evaluating the overall consolidated financial statement presentation.

We believe that our audits, and the reports of the other auditor, related to the amounts included for the IRS and OFS, provide a reasonable basis for our opinion.

In planning and performing our fiscal year 2009 audit, we considered the Treasury Department's internal control over financial reporting, exclusive of the internal control over financial reporting related to the IRS and OFS, by obtaining an understanding of the design effectiveness of the Treasury Department's internal control, determining whether internal controls had been placed in operation, assessing control risk, and performing tests of controls as a basis for designing our auditing procedures for the purpose of expressing our opinion on the consolidated financial statements. Internal control over financial reporting related to the IRS and the OFS was considered by the other auditor whose reports thereon dated November 5, 2009, and December 4, 2009 respectively, have been provided to us. We, and the other auditor, did not test all internal controls relevant to operating objectives as broadly defined by the *Federal Managers' Financial Integrity Act of 1982*. The objective of our audit was not to express an opinion on the effectiveness of the Treasury Department's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Treasury Department's internal control over financial reporting. The objective of the other auditor's audits was to express an opinion on the effectiveness of the IRS's and the OFS's internal control over financial reporting. Because of the IRS material weakness in internal controls discussed above, the other auditor's opinion on the IRS' internal control stated that the IRS did not maintain effective internal control over financial reporting as of September 30, 2009.

As part of obtaining reasonable assurance about whether the Treasury Department's fiscal year 2009 consolidated financial statements are free of material misstatement, we, and the other auditor, performed tests of the Treasury Department's compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of the consolidated financial statement amounts, and certain provisions of other laws and regulations specified in OMB Bulletin No. 07-04, including the provisions referred to in Section 803(a) of FFMIA. We, and the other auditor, limited our tests of compliance to the provisions described in the preceding sentence, and we, and the other auditor, did not test compliance with all laws, regulations, contracts, and grant agreements applicable to the Treasury Department. However, providing an opinion on compliance with laws, regulations, contracts, and grant agreements was not an objective of our audits and, accordingly, we, and the other auditor, do not express such an opinion.

This report is intended solely for the information and use of the Treasury Department's management, the Treasury Department's Office of Inspector General, OMB, the GAO, and the U.S. Congress and is not intended to be and should not be used by anyone other than these specified parties.

KPMG LLP

December 15, 2009

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C.

ASSISTANT SECRETARY

December 15, 2009

KPMG LLP
2001 M Street, N.W.
Washington, D.C. 20036

Ladies and Gentlemen:

On behalf of Secretary Geithner, I am responding to your draft audit report on the Department of the Treasury's fiscal year 2009 consolidated financial statements. Our bureaus and program offices all can be proud of the Department's success in achieving an unqualified opinion on the Department's financial statements for the tenth consecutive year. We are particularly proud of the unqualified opinion from the Government Accountability Office (GAO) on the Office of Financial Stability's financial statements – a remarkable achievement considering the magnitude and complexity of the new economic stabilization programs.

These successful results also are due in large part to the high level of professionalism, technical expertise, and partnership demonstrated by KPMG in conducting the audit. Treasury appreciates your efforts during the audit process to provide timely, constructive advice on how to improve our financial reporting. Treasury is equally appreciative of the expertise and commitment demonstrated by the other organizations involved in the audit process – the Office of Inspector General, GAO, and the firms that audited several of our bureaus.

In 2009, KPMG identified a new material weakness at the departmental level, Financial Management Practices. We agree with your related recommendations, and have already started taking corrective action to resolve the issues and close this material weakness in 2010. Treasury continued to make significant progress during fiscal year 2009 to address previously identified financial and information management deficiencies. As reported by GAO, the Internal Revenue Service made significant strides in addressing its internal control deficiencies in financial reporting and tax revenue collection and refund issuance.

We acknowledge the material weaknesses, significant deficiencies, and instances of noncompliance with laws and regulations described in your report. We agree with your recommendations, and will focus on necessary corrective actions to address each of the issues quickly and aggressively.

Dan Tangherlini
Assistant Secretary for Management
and Chief Financial Officer

CONSOLIDATED BALANCE SHEETS
AS OF SEPTEMBER 30, 2009 AND 2008
(IN MILLIONS)

ASSETS	2009	2008
Intra-governmental Assets		
Fund Balance (Note 2)	$ 504,582	$ 275,368
Loans and Interest Receivable (Note 3)	410,591	264,854
Advances to the Black Lung Trust Fund (Notes 1 & 4)	0	10,484
Advances to the Unemployment Trust Fund (Notes 1 & 4)	7,981	0
Due From the General Fund (Note 4)	11,992,719	10,100,763
Accounts Receivable and Related Interest (Note 5)	298	396
Other Intra-governmental Assets	5	13
Total Intra-governmental Assets	$ 12,916,176	$ 10,651,878
Cash, Foreign Currency, and Other Monetary Assets (Note 6)	341,308	387,270
Gold and Silver Reserves (Note 7)	11,062	11,062
Asset Guarantee (Note 8)	1,765	0
Investments – Credit Reform (Note 8)	203,141	0
Investments in Government Sponsored Enterprises (Note 9)	64,679	7,032
Investments in International Financial Institutions (Note 10)	5,575	5,546
Other Investments and Related Interest (Note 11)	13,565	10,576
Credit Program Receivables, Direct Loans, Net (Note 12)	219,170	3,385
Loans and Interest Receivable (Note 13)	168	172
Reserve Position in the International Monetary Fund (Note 14)	13,469	4,750
Tax, Other, and Related Interest Receivables, Net (Note 15)	30,408	30,878
Beneficial Interest in Trust (Note 29)	23,472	0
Inventory and Related Property, Net (Note 16)	598	698
Property, Plant, and Equipment, Net (Note 17)	2,036	2,077
Other Assets	9	1,714
Total Assets	$ 13,846,601	$ 11,117,038
Heritage Assets (Note 17)		

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

CONSOLIDATED BALANCE SHEETS
AS OF SEPTEMBER 30, 2009 AND 2008
(IN MILLIONS)

LIABILITIES	2009	2008
Intra-governmental Liabilities		
Federal Debt and Interest Payable (Notes 4 and 19)	$ 4,403,080	$ 4,262,414
Other Debt and Interest Payable (Note 20)	12,060	14,164
Due to the General Fund (Notes 4, 6, and 27)	1,263,128	667,112
Other Intra-governmental Liabilities (Note 22)	425	345
Total Intra-governmental Liabilities	**$ 5,678,693**	**$ 4,944,035**
Federal Debt and Interest Payable (Notes 4 and 19)	7,559,305	5,812,694
Certificates Issued to the Federal Reserve (Note 6)	5,200	2,200
Allocation of Special Drawing Rights (Note 6)	55,953	7,630
Gold Certificates Issued to the Federal Reserve Banks (Note 7)	11,037	11,037
Refunds Payable (Notes 4 and 26)	4,040	3,076
D.C. Pensions and Judiciary Retirement Actuarial Liability (Note 21)	9,049	8,803
Liabilities to GSEs (Note 9)	91,937	13,800
Other Liabilities (Note 22)	3,331	4,052
Total Liabilities	**$ 13,418,545**	**$ 10,807,327**
Commitments and Contingencies (Note 31)		
NET POSITION		
Unexpended Appropriations:		
Earmarked Funds (Note 27)	$ 200	$ 200
Other Funds	454,944	271,768
Subtotal	455,144	271,968
Cumulative Results of Operations:		
Earmarked Funds (Note 27)	41,653	37,586
Other Funds	(68,741)	157
Subtotal	(27,088)	37,743
Total Net Position (Note 23)	**$ 428,056**	**$ 309,711**
Total Liabilities and Net Position	**$ 13,846,601**	**$ 11,117,038**

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

CONSOLIDATED STATEMENTS OF NET COST
FOR THE YEARS ENDED SEPTEMBER 30, 2009 AND 2008
(IN MILLIONS)

Cost of Treasury Operations: (Note 24)	2009	2008
Financial Program:		
Gross Cost	$ 15,313	$ 14,569
Less Earned Revenue	(2,258)	(2,282)
Net Program Cost	**$ 13,055**	**$ 12,287**
Economic Program:		
Gross Cost	$ 210,490	$ 19,139
Less Earned Revenue	(14,785)	(5,091)
Net Program Cost	**$ 195,705**	**$ 14,048**
Security Program:		
Gross Cost	$ 325	$ 346
Less Earned Revenue	(3)	(4)
Net Program Cost	**$ 322**	**$ 342**
Management Program:		
Gross Cost	$ 569	$ 631
Less Earned Revenue	(60)	(165)
Net Program Cost	**$ 509**	**$ 466**
Total Program Gross Costs	**$ 226,697**	**$ 34,685**
Total Program Gross Earned Revenues	**(17,106)**	**(7,542)**
Total Net Cost of Treasury Operations	**$ 209,591**	**$ 27,143**
Federal Costs: (Note 24)		
Federal Debt Interest	$ 380,519	$ 453,347
Less Interest Revenue from Loans	(17,326)	(12,439)
Net Federal Debt Interest Costs	**$ 363,193**	**$ 440,908**
Net GSE Non-Entity Revenue (Note 9)	**(61,983)**	**(7,032)**
Other Federal Costs (Note 24)	$ 12,131	$ 8,332
Total Net Federal Costs	**$ 313,341**	**$ 442,208**
Net Cost of Treasury Operations, Federal Debt Interest, Other Federal Costs, and Net GSE Non-Entity Revenue	**$ 522,932**	**$ 469,351**

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

CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION
FOR THE YEAR ENDED SEPTEMBER 30, 2009
(IN MILLIONS)

CUMULATIVE RESULTS OF OPERATIONS	Combined Earmarked Funds	Combined All Other Funds	Elimination	Consolidated Total
Beginning Balances	$ 37,586	$ 157	$ 0	$ 37,743
Budgetary Financing Sources:				
Appropriations Used	408	667,745	0	668,153
Non-exchange Revenue	263	234	(4)	493
Donations and Forfeitures of Cash/Equivalent	257	0	0	257
Transfers In/Out Without Reimbursement	(16)	(7)	2	(21)
Other	10	2	0	12
Other Financing Sources (non-exchange)				
Donation/Forfeiture of Property	127	0	0	127
Accrued Interest and Discount on Debt	0	6,027	0	6,027
Transfers In/Out Without Reimbursement	(63)	29	(2)	(36)
Imputed Financing Sources	61	1,206	(474)	793
Transfers to the General Fund and Other (Note 23)	(31)	(217,673)	0	(217,704)
Total Financing Sources	**1,016**	**457,563**	**(478)**	**458,101**
Net Cost of Operations	3,051	(526,461)	478	(522,932)
Net Change	4,067	(68,898)	0	(64,831)
Cumulative Results of Operations	**$ 41,653**	**$ (68,741)**	**$ 0**	**$ (27,088)**
UNEXPENDED APPROPRIATIONS				
Beginning Balances	$ 200	$ 271,768	$ 0	$ 271,968
Budgetary Financing Sources:				
Appropriations Received (Note 23)	408	855,354	0	855,762
Appropriations Transferred In/Out	0	11	0	11
Other Adjustments	0	(4,444)	0	(4,444)
Appropriations Used	(408)	(667,745)	0	(668,153)
Total Budgetary Financing Sources	**0**	**183,176**	**0**	**183,176**
Total Unexpended Appropriations	**$ 200**	**$ 454,944**	**$ 0**	**$ 455,144**
Net Position	**$ 41,853**	**$ 386,203**	**$ 0**	**$ 428,056**

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

CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION
FOR THE YEAR ENDED SEPTEMBER 30, 2008
(IN MILLIONS)

CUMULATIVE RESULTS OF OPERATIONS	Combined Earmarked Funds	Combined All Other Funds	Elimination	Consolidated Total
Beginning Balances	$ 35,385	$ 13,397	$ 0	$ 48,782
Budgetary Financing Sources:				
Appropriations Used	458	481,277	0	481,735
Non-exchange Revenue	134	144	(24)	254
Donations and Forfeitures of Cash/Equivalent	159	0	0	159
Transfers In/Out without Reimbursement	0	(10)	0	(10)
Other	38	(26)	0	12
Other Financing Sources (non exchange)				
Donation/Forfeiture of Property	112	0	0	112
Accrued Interest and Discount on Debt	0	(3,870)	0	(3,870)
Transfers In/Out Without Reimbursement	(52)	31	0	(21)
Imputed Financing Sources	60	1,147	(478)	729
Transfers to the General Fund and Other (Note 23)	(23)	(20,765)	0	(20,788)
Total Financing Sources	**886**	**457,928**	**(502)**	**458,312**
Net Cost of Operations	1,315	(471,168)	502	(469,351)
Net Change	2,201	(13,240)	0	(11,039)
Cumulative Results of Operations	**$ 37,586**	**$ 157**	**$ 0**	**$ 37,743**
UNEXPENDED APPROPRIATIONS				
Beginning Balances	$ 200	$ 72,117	$ 0	$ 72,317
Budgetary Financing Sources:				
Appropriations Received (Note 23)	458	681,015	0	681,473
Appropriations Transferred In/Out	0	24	0	24
Other Adjustments	0	(111)	0	(111)
Appropriations Used	(458)	(481,277)	0	(481,735)
Total Budgetary Financing Sources	**0**	**199,651**	**0**	**199,651**
Total Unexpended Appropriations	**$ 200**	**$ 271,768**	**$ 0**	**$ 271,968**
Net Position	**$ 37,786**	**$ 271,925**	**$ 0**	**$ 309,711**

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

COMBINED STATEMENT OF BUDGETARY RESOURCES
FOR THE YEAR ENDED SEPTEMBER 30, 2009
(IN MILLIONS)

	Budgetary	Non-Budgetary Financing	Total
Budgetary Resources			
Unobligated balance, brought forward	$ 260,173	$ 24,457	$ 284,630
Recoveries of prior year unpaid obligations	8,097	(1)	8,096
Budget authority:			
Appropriations (Note 23)	952,185	0	952,185
Borrowing authority	493	548,242	548,735
Spending Authority from Offsetting Collections			
Earned: Collected	11,681	272,768	284,449
Change in receivables from Federal sources	(44)	0	(44)
Change in unfilled customer orders:			
Advance received	(31)	0	(31)
Without advance from Federal sources	(134)	28,926	28,792
Subtotal	964,150	849,936	1,814,086
Non-expenditure transfers, net	(43)	0	(43)
Temporarily not available pursuant to Public Law	2	0	2
Permanently not available	(92,001)	(179,736)	(271,737)
Total Budgetary Resources	$ 1,140,378	$ 694,656	$ 1,835,034
Status of Budgetary Resources			
Obligations incurred (Note 25): Direct	$ 729,697	$ 652,829	$ 1,382,526
Reimbursable	4,669	0	4,669
Subtotal	734,366	652,829	1,387,195
Unobligated Balance: Apportioned	349,889	19,612	369,501
Exempt from apportionment	44,497	0	44,497
Subtotal	394,386	19,612	413,998
Unobligated balance not available	11,626	22,215	33,841
Total Status of Budgetary Resources	$ 1,140,378	$ 694,656	$ 1,835,034
Change in Obligated Balance			
Obligated balance, net: (Note 1 AC)			
Unpaid obligations brought forward, Oct. 1	$ 57,314	10	$ 57,324
Uncollected customer payments from Federal sources brought forward	(346)	(1)	(347)
Total unpaid obligated balance, net	**56,968**	**9**	**56,977**
Obligations incurred, net	734,366	652,829	1,387,195
Gross outlays	(675,286)	(573,630)	(1,248,916)
Recoveries of prior year unpaid obligations, actual	(8,097)	1	(8,096)
Change In uncollected customer payments Federal source	178	(28,926)	(28,748)
Obligated balance, net, end of period:			
Unpaid obligations	108,297	79,209	187,506
Uncollected customer payments Federal sources	(168)	(28,926)	(29,094)
Total unpaid obligated balance, net, end of period	108,129	50,283	158,412
Net Outlays			
Gross outlays	675,286	573,630	1,248,916
Offsetting collections	(9,369)	(272,768)	(282,137)
Distributed offsetting receipts	(40,114)	(4,500)	(44,614)
Net Outlays	$ 625,803	$ 296,362	$ 922,165

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

COMBINED STATEMENT OF BUDGETARY RESOURCES
FOR THE YEAR ENDED SEPTEMBER 30, 2008
(IN MILLIONS)

	Budgetary	Non-Budgetary Financing	Total
Budgetary Resources			
Unobligated balance, brought forward	$ 57,450	$ 0	$ 57,450
Recoveries of prior year unpaid obligations	413	0	413
Budget authority:			
Appropriations (Note 23)	679,563	0	679,563
Borrowing authority	4	34,304	34,308
Spending Authority from Offsetting Collections			
Earned: Collected	8,705	335	9,040
Change in receivables from Federal sources	(32)	0	(32)
Change in unfilled customer orders: Advance received	19	0	19
Without advance from Federal sources	(39)	0	(39)
Subtotal	688,220	34,639	722,859
Non-expenditure transfers, net	844	0	844
Temporarily not available pursuant to Public Law	(9)	0	(9)
Permanently not available	(4,626)	(4,767)	(9,393)
Total Budgetary Resources	**$ 742,292**	**$ 29,872**	**$ 772,164**
Status of Budgetary Resources			
Obligations incurred (Note 25): Direct	$ 477,384	$ 5,415	$ 482,799
Reimbursable	4,735	0	4,735
Subtotal	482,119	5,415	487,534
Unobligated Balance: Apportioned	214,114	24,122	238,236
Exempt from apportionment	34,999	0	34,999
Subtotal	249,113	24,122	273,235
Unobligated balance not available	11,060	335	11,395
Total Status of Budgetary Resources	**$ 742,292**	**$ 29,872**	**$ 772,164**
Change in Obligated Balance			
Obligated balance, net:			
Unpaid obligations brought forward, Oct. 1	$ 57,811	$ 0	$ 57,811
Uncollected customer payments from Federal sources brought forward	(418)	0	(418)
Total unpaid obligated balance, net	**57,393**	**0**	**57,393**
Obligations incurred, net	482,119	5,415	487,534
Gross outlays	(482,199)	(5,409)	(487,608)
Recoveries of prior year unpaid obligations, actual	(413)	0	(413)
Change In uncollected customer payments Federal source	71	0	71
Obligated balance, net, end of period:			
Unpaid obligations	57,318	6	57,324
Uncollected customer payments Federal sources	(347)	0	(347)
Total unpaid obligated balance, net, end of period	**56,971**	**6**	**56,977**
Net Outlays			
Gross outlays	482,199	5,409	487,608
Offsetting collections	(8,194)	(335)	(8,529)
Distributed offsetting receipts	(16,211)	0	(16,211)
Net Outlays	**$ 457,794**	**$ 5,074**	**$ 462,868**

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

STATEMENTS OF CUSTODIAL ACTIVITY
FOR THE YEARS ENDED SEPTEMBER 30, 2009 AND 2008
(IN MILLIONS)

	2009	2008
Sources of Custodial Revenue (Note 26):		
Revenue Received		
Individual Income and FICA Taxes	$ 2,036,557	$ 2,294,326
Corporate Income Taxes	225,482	354,063
Estate and Gift Taxes	24,677	29,824
Excise Taxes	67,248	66,293
Railroad Retirement Taxes	4,711	4,939
Unemployment Taxes	6,765	7,331
Deposit of Earnings, Federal Reserve System	34,318	33,598
Fines, Penalties, Interest and Other Revenue	1,929	2,233
Total Cash Revenue Received	$ 2,401,687	$ 2,792,607
Less Refunds	(437,972)	(426,074)
Net Cash Revenue Received	$ 1,963,715	$ 2,366,533
Non-Cash Custodial Transactions		
Beneficial Interest in Trust (Note 29)	23,472	0
Accrual Adjustment	(1,097)	3,132
Total Custodial Revenue	$ 1,986,090	$ 2,369,665
Disposition of Custodial Revenue:		
Amounts Provided to Fund Non-Federal Entities	487	407
Amounts Provided to Fund the Federal Government (Notes 26 and 29)	1,963,228	2,366,126
Total Disposition of Cash Revenue	$ 1,963,715	$ 2,366,533
Non-cash Revenue – Beneficial Interest in Trust	23,472	0
Accrual Adjustment	(1,097)	3,132
Total Disposition of Custodial Revenue	1,986,090	2,369,665
Net Custodial Revenue	$ 0	$ 0

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

Notes to the Financial Statements

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1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. REPORTING ENTITY

The accompanying financial statements include the operations of the U.S. Department of the Treasury (Treasury Department), one of 24 CFO Act agencies of the Executive Branch of the United States Government, and certain custodial activities managed on behalf of the entire U.S. Government. The following paragraphs describe the activities of the reporting entity.

The Treasury Department was created by Act (1 Stat.65) on September 2, 1789. Many subsequent acts affected the development of the Treasury Department, delegating new duties to its charge and establishing the numerous bureaus and divisions that now comprise the Treasury Department. As a major policy advisor to the President, the Secretary has primary responsibility for formulating and managing the domestic and international tax and financial policies of the U.S. Government.

Further, the Secretary is responsible for recommending and implementing United States domestic and international economic and fiscal policy; governing the fiscal operations of the government; maintaining foreign assets control; managing the federal debt; collecting income and excise taxes; representing the United States on international monetary, trade, and investment issues; overseeing Departmental overseas operations; and directing the manufacturing of coins, currency, and other products for customer agencies and the public.

The *Emergency Economic Stabilization Act of 2008* (EESA) was signed into law on October 3, 2008. EESA authorized the establishment of the Troubled Asset Relief Program (TARP) to be administered by the Treasury Department. EESA established two new offices within the Treasury Department: the Office of Financial Stability to administer the TARP, and a new Special Inspector General for TARP (SIGTARP). Under EESA, the Special Inspector General has the responsibility, among other things, to conduct, supervise, and coordinate audits and investigations of the purchase, management, and sale of assets under TARP.

The Treasury Department includes the Departmental Offices (DO) and nine operating bureaus. For financial reporting purposes, DO is composed of: International Assistance Programs (IAP), Office of Inspector General (OIG), the Special Office of Inspector General for the Troubled Asset Relief Program (SIGTARP), Treasury Forfeiture Fund (TFF), Exchange Stabilization Fund (ESF), Community Development Financial Institutions Fund (CDFI), Office of D.C. Pensions (DCP), Treasury Inspector General for Tax Administration (TIGTA), Federal Financing Bank (FFB), Office of Financial Stability (OFS), and the DO policy offices, which include the Government Sponsored Enterprise and Mortgage Backed Securities programs.

The nine operating bureaus are: Office of the Comptroller of the Currency (OCC); Bureau of Engraving and Printing (BEP); Financial Crimes Enforcement Network (FinCEN); Financial Management Service (FMS); Internal Revenue Service (IRS); U.S. Mint (Mint); Bureau of the Public Debt (BPD); Office of Thrift Supervision (OTS); and the Alcohol and Tobacco Tax and Trade Bureau (TTB).

The Treasury Department's financial statements reflect the reporting of its own entity activities, which include appropriations it receives to conduct its operations and revenue generated from those operations. They also reflect the reporting of certain non-entity (custodial) functions it performs on behalf of the U.S. Government and others. Non-entity activities include collecting federal revenue, servicing the federal debt, disbursing certain federal funds, and maintaining certain assets and liabilities for the U.S. Government, as well as for other federal entities.

The Treasury Department's reporting entity does not include the "General Fund" of the U.S. Government, which maintains receipt, disbursement, and appropriation accounts for all federal agencies.

Transactions and balances among the Treasury Department's entities have been eliminated from the Consolidated Balance Sheets, the Consolidated Statements of Net Cost, and the Consolidated Statements of Changes in Net Position.

Following GAAP for federal entities, the Treasury Department has not consolidated into its financial statements the assets, liabilities, or results of operations of any financial organization or commercial entity in which it holds either a direct, indirect, or beneficial majority equity investment. Even though some of the equity investments are significant, these entities meet the criteria of "bailed out" entities under paragraph 50 of the Statement of Federal Financial Accounting Standards (SFFAS) No. 2, which directs that such "bailout" investments should not be consolidated into the financial reports of the Federal Government, either in part or as a whole.

B. BASIS OF ACCOUNTING AND PRESENTATION

The financial statements have been prepared from the accounting records of the Treasury Department in conformity with accounting principles generally accepted in the United States for federal entities, and the Office of Management and Budget (OMB) Circular No. A-136, *Financial Reporting Requirements*, as amended. Accounting principles generally accepted for federal entities are the standards prescribed by the Federal Accounting Standards Advisory Board (FASAB). FASAB is recognized by the American Institute of Certified Public Accountants as the official accounting standards-setting body of the U.S. Government. As such, the FASAB is responsible for identifying the Generally Accepted Accounting Principles (GAAP) hierarchy for Federal reporting entities.

In July 2009, the FASAB issued SFFAS No. 34, *The Hierarchy of Generally Accepted Accounting Principles for Federal Entities, Including the Application of Standards Issued by the Financial Accounting Standards Board*. SFFAS No. 34 incorporates the hierarchy of the sources of accounting principles and the framework for selecting the principles used in the preparation of general purpose financial reports of Federal reporting entities that are presented in conformity with federal GAAP.

These financial statements are provided to meet the requirements of the *Government Management Reform Act of 1994*. They consist of the Consolidated Balance Sheets, the Consolidated Statements of Net Cost, the Consolidated Statements of Changes in Net Position, the Combined Statements of Budgetary Resources, and the Statements of Custodial Activity. The statements and the related notes are prepared in a comparative form to present both fiscal year 2009 and fiscal year 2008 information.

While these financial statements have been prepared from the books and records of the Treasury Department in accordance with the formats prescribed by OMB, these financial statements are in addition to the financial reports used to monitor and control budgetary resources which are prepared from the same books and records.

Intra-governmental assets and liabilities are those from or to other federal entities. Intra-governmental earned revenues are collections or accruals of revenue from other federal entities, and intra-governmental costs are payments or accruals of expenditures to other federal entities.

The financial statements should be read with the realization that they are for a component of a sovereign entity, that liabilities not covered by budgetary resources cannot be liquidated without the enactment of an appropriation, and that the payment of all liabilities other than for contracts can be abrogated by the sovereign entity.

Liabilities represent the probable and measurable future outflow or other sacrifice of resources as a result of past transactions or events. Since Treasury Department is a component of the United States Government, a sovereign entity, Treasury's liabilities cannot be liquidated without legislation that provides resources or an appropriation. Liabilities covered by budgetary resources are those liabilities for which Congress has appropriated funds or funding is otherwise available to pay amounts due. Liabilities not covered by budgetary or other resources represent amounts owed in excess of available, congressionally appropriated funds or other amounts, and there is no certainty that the appropriations will be enacted. The United States government, acting in its sovereign capacity, can abrogate liabilities of Treasury arising from other than contracts.

C. INVESTMENTS

Investments – Credit Reform

Troubled Asset Relief Program (TARP) equity investments, including investments in preferred and common stock and warrants of public companies are accounted for pursuant to the provisions of the *Federal Credit Reform Act* (FCRA) and the associated FASAB accounting standard SFFAS No. 2, *Accounting for Direct Loans and Loan Guarantees*, as amended. As consideration for investments made, Treasury received common stock warrants, preferred shares (referred to as warrant preferred shares) or additional notes. Treasury concluded that GAAP accounting for such investments using SFFAS No. 2 was appropriate analogous accounting guidance based on the similarity between the equity investments made by Treasury and direct loans. Consequently, TARP equity investments, including investments in preferred and common stock and warrants of public companies are accounted for by Treasury using credit reform accounting in accordance with SFFAS No. 2, as amended, and reported in accordance with FCRA in these financial statements. Treasury calculates and accounts for equity investments using a market risk adjusted discount rate. In addition, the inclusion of market risk required by EESA in the valuation calculation results in accounting for these investments at estimated fair value, which is consistent with the accounting for other equity investments held by Treasury (i.e., Investments in GSEs).

Treasury recognizes dividend revenue associated with equity investments when declared by the entity in which Treasury has invested and when received in relation to any repurchases and restructuring. Treasury reflects changes in the present value of the projected cost value of direct loans, equity investments, and asset guarantees in the subsidy cost on the Statement of Net Cost annually, as required by FCRA. The estimated values associated with these additional instruments are disclosed in Note 8.

Investments in Government Sponsored Enterprises

The senior preferred stock liquidity preference (preferred stock) and associated common stock warrant (warrant(s)) in GSEs are presented at their fair value as permitted by OMB Circular No. A-136. This Circular includes language that generally requires agencies to value non-federal investments at acquisition cost, and also permits the use of other measurement basis, such as fair value, in certain situations. OMB issued guidance to the Department of the Treasury on October 7, 2009, noting that while OMB Circular No. A-136 focuses primarily on federal securities, which are normally accounted for at amortized cost, it is reasonable to interpret OMB Circular No. A-136 to permit non-federal investments, on an instrument by instrument election, to be reported on a basis other than cost. OMB's guidance allows the use of fair value accounting for non-federal securities beginning with reporting for fiscal year 2009. OMB Circular No. A-136 also directs agencies with non-federal securities to consult FASB's Statement of Financial Accounting Standards No. 115, *Accounting for Certain Investments in Debt and Equity Securities*, for additional guidance. The Investments in GSEs disclosed as of

September 30, 2008, were recorded at acquisition cost at the date of purchase with disclosure of fair values as of fiscal year end 2008.

Treasury performs annual valuations, as of September 30th, of the preferred stock and warrants. Any changes in valuation, including impairment, is recorded and disclosed in accordance with SFFAS No. 7, *Accounting for Revenue and Other Financing Sources*. Since the valuation is an annual process, the changes in valuation of the preferred stock and warrants are deemed usual and recurring. Accordingly, changes in valuation are recorded as an exchange transaction that is either an expense or revenue. Since the costs of preferred stock and warrants are exchange transactions, any change in valuation is also recorded as an exchange transaction.

In addition, the preferred stock, warrants, and related dividends, and changes in valuation are accounted for as non-entity transactions. Furthermore, any related revenue, gains, or losses to the preferred stock or warrants are reported as non-entity exchange revenue. Dividends are accrued when declared; therefore, no accrual is made for future dividends.

Increases in the non-entity preferred stock liquidity preference occur when quarterly payments to the GSEs are made pursuant to the preferred stock purchase agreements (i.e., when a GSE's liabilities exceed its assets at the end of any quarter). These quarterly payments (liquidity commitments) are made from funds appropriated directly to the Treasury Department. Therefore, quarterly liquidity payments are recorded as costs in the Treasury Department's entity accounts and appear as costs on the Statement of Net Cost economic program section.

Investments in International Financial Institutions

The Treasury Department invests in Multilateral Development Banks (MDB) to support poverty reduction, private sector development, and transition to market economies and sustainable economic growth and development, thereby advancing the United States' economic, political, and commercial interests abroad. These investments are non-marketable equity investments valued at cost.

Other Investments and Related Interest

The ESF holds most of the Treasury Department's other investments. Securities that the Treasury Department has both the intent and ability to hold to maturity are classified as investment securities held to maturity and are carried at historical cost, adjusted for amortization of premiums and accretion of discounts, in accordance with OMB Circular No. A-136. The GSE securities held by ESF are in this category. "Other Foreign Currency Denominated Assets" are considered "available for sale" securities and recorded at fair value as permitted by OMB Circular No. A-136 beginning in fiscal year 2009. (Prior to fiscal year 2009, A-136 required reporting at cost.) These holdings are normally invested in interest bearing securities issued or held through foreign governments or monetary authorities.

D. TAX AND OTHER NON-ENTITY RECEIVABLES

Federal taxes receivable, net and the corresponding liability, due to Treasury are not accrued until related tax returns are filed or assessments are made by the IRS and agreed to by either the taxpayer or the court. Additionally, the prepayments are netted against liabilities. Accruals are made to reflect penalties and interest on taxes receivable through the balance sheet date.

Taxes receivable consist of unpaid assessments (taxes and associated penalties and interest) due from taxpayers. The existence of a receivable is supported by a taxpayer agreement, such as filing of a tax return without sufficient payment, or a court ruling in favor of the IRS. The allowance reflects an estimate of the portion of total taxes receivable deemed to be uncollectible.

Compliance assessments are unpaid assessments which neither the taxpayer nor a court has affirmed the taxpayer owes to the Federal Government. Examples include assessments resulting from an IRS audit or examination in which the taxpayer does not agree with the results. Write-offs consist of unpaid assessments for which the IRS does not expect further collections due to factors such as taxpayers' bankruptcy, insolvency, or death. Compliance assessments and write-offs are not reported on the balance sheet. Statutory provisions require the accounts to be maintained until the statute for collection expires.

E. INVENTORY AND RELATED PROPERTY

Inventory and related property include inventory, operating materials and supplies, and forfeited property. The Treasury Department values inventories at either standard cost, or lower of cost or latest acquisition cost, except for finished goods inventories, which are valued at weighted-average unit cost. All operating materials and supplies are recorded as an expense when consumed in operations.

Forfeited property is recorded at estimated fair market value as deferred revenue, and may be adjusted to reflect the current fair market value at the end of the fiscal year. Property forfeited in satisfaction of a taxpayer's assessed liability is recorded when title to the property passes to the U.S. Government and a corresponding credit is made to the related taxes receivable. Direct and indirect holding costs are not capitalized for individual forfeited assets.

Mortgages and claims on forfeited assets are recognized as a valuation allowance and a reduction of deferred revenue from forfeited assets when the asset is forfeited. The allowance includes mortgages and claims on forfeited property held for sale and a minimal amount of claims on forfeited property previously sold. Revenue from the forfeiture of property is deferred until the property is sold or transferred to a state, local, or federal agency. Revenue is not recognized if the forfeited property is ultimately destroyed or cannot be legally sold.

F. LOANS AND INTEREST RECEIVABLE, INTRAGOVERNMENTAL – ENTITY AND NON-ENTITY

Intra-governmental entity Loans and Interest Receivable from other federal agencies represent loans and interest receivable held by the Treasury Department. No credit reform subsidy costs were recorded for loans purchased from federal agencies or for guaranteed loans made to non-federal borrowers, because of outstanding balances guaranteed (interest and principal) by those agencies.

Intra-governmental non-entity Loans and Interest Receivable from other federal agencies represent loans issued by the Treasury Department to federal agencies on behalf of the U.S. Government. The Treasury Department acts as an intermediary issuing these loans, because the agencies receiving these loans will lend these funds to others to carry out various programs of the Federal Government. Because of the Treasury Department's intermediary role in issuing these loans, the Treasury Department does not record an allowance related to these intra-governmental loans. Instead, loan loss allowances and subsidy costs are recognized by the ultimate lender, the federal agency that issued the loans to the public.

G. ADVANCES TO THE BLACK LUNG TRUST FUND

Advances were provided to the Department of Labor's Black Lung Disability Trust Fund from the General Fund of the U.S. Government. BPD accounted for the advances on behalf of the General Fund of the U.S. Government. Advances to the Black Lung Disability Trust Fund were accounted for pursuant to the *Benefits Revenue Act* which states: "In the event that fund resources are not adequate to meet fund obligations, then, advances of interest and principal are paid to the General Fund of the U.S. Government when the Secretary of the Treasury determines that funds are available in the trust fund for such purposes." The advances to the Black Lung Trust Fund were repayable with interest at a rate determined by the Secretary of the Treasury to be equal to the current average market yield on outstanding marketable obligations of the United States with remaining periods to maturity comparable to the anticipated period during which the advance will be outstanding. Advances made prior to 1982 carried rates of interest equal to the average rate borne by all marketable interest-bearing obligations of the United States then forming a part of the public debt.

The *Benefits Revenue Act* authorized restructuring of the Trust Fund debt by the repayment of the market value of outstanding repayable advances with the proceeds of Authorized Trust Fund borrowing and a one-time appropriation of $6,498 million. As a result of the refinancing, the General Fund of the U.S. Government recognized a gain of $2,496 million for the difference between the market value of the outstanding advances plus accrued interest of $12,994 million and the carrying value of the outstanding advances plus accrued interest of $10,498 million.

H. ADVANCES TO THE UNEMPLOYMENT TRUST FUND

Advances have been issued to the Department of Labor's Unemployment Trust Fund from the General Fund of the U.S. Government to states for unemployment benefits. The Bureau of the Public Debt accounts for the advances on behalf of the General Fund. As outlined in 42 USC § 1323, these repayable advances bear an interest rate of 3.375 percent, and were computed as the average interest rate, as of the end of the calendar month preceding the issuance date of the advance, for all interest bearing obligations of the United States then forming the public debt, to the nearest lower one-eighth of one percent. Interest on the repayable advances is due on September 30th of each year. Advances will be repaid by transfers from the Unemployment Trust Fund to the General Fund when the Secretary of the Treasury, in consultation with the Secretary of Labor, has determined that the balance in the Unemployment Trust Fund is adequate to allow repayment.

I. RECEIVABLE ON DEPOSIT OF EARNINGS, FEDERAL RESERVE SYSTEM

Reserve Banks are required by the Board of Governors of the Federal Reserve System to transfer to the U.S. Treasury excess earnings, after providing for the cost of operations, payment of dividends, and reservation of an amount necessary to equate surplus with capital paid in. In the event of losses, or a substantial increase in capital, a Reserve Bank will suspend its payments to the U.S. Treasury until such losses or increases in capital are recovered through subsequent earnings. Weekly payments to the U.S. Treasury may vary significantly. The Receivable on Deposit of Earnings, Federal Reserve System, represents the earnings due Treasury as of September 30, but not collected by the U.S. Treasury until after the end of the month.

J. PROPERTY, PLANT, AND EQUIPMENT

General

Property, plant, and equipment (PP&E) is composed of capital assets used in providing goods or services. It also includes assets acquired through capital leases, which are initially recorded at the amount recognized as a liability for the capital lease at its inception. PP&E is stated at full cost, including costs related to acquisition, delivery, and installation, less accumulated depreciation. Major alterations and renovations including leasehold and land improvements are capitalized, while maintenance and repair costs are charged to expenses as incurred.

Internal use software encompasses software design, development, and testing of projects adding significant new functionality and long-term benefits. Costs for developing internal use software are accumulated in work in development until a project is placed into service, and testing and final acceptance are successfully completed. Once completed, the costs are transferred to depreciable property.

Costs for construction projects are recorded as construction-in-progress until completed, and are valued at actual (direct) cost, plus applied overhead and other indirect costs.

The Treasury Department leases land and buildings from the General Services Administration (GSA) to conduct most of its operations. GSA charges a standard level users fee which approximates commercial rental rates for similar properties. Therefore, GSA-owned properties are not included in the Department's PP&E.

The Treasury Department's bureaus are diverse both in size and in operating environment. Accordingly, the Department's capitalization policy provides minimum capitalization thresholds which range from $25,000 to $50,000. The Treasury Department also uses a capitalization threshold range for bulk purchases: $250,000 to $500,000 for non manufacturing bureaus and $25,000 to $50,000 for manufacturing bureaus. Bureaus determine the individual items that comprise bulk purchases. In addition, Treasury bureaus may expense bulk purchases if they conclude that total period costs would not be materially distorted and the cost of capitalization is not economically feasible.

Depreciation is expensed on a straight-line basis over the estimated useful life of the asset with the exception of leasehold improvements, which are depreciated over the useful life of the lease or the useful life of the improvement, whichever is shorter. Service life ranges are high due to the Treasury Department's diversity of PP&E. Construction in progress and internal use software in development are not depreciated.

Heritage Assets

The Treasury Department owns the Treasury building -- a multi-use heritage asset. The building housing the United States Mint in Denver, Colorado, is also considered a multi-use heritage asset. Multi-use heritage assets are assets of historical significance for which the predominant use is general government operations. All acquisition, reconstruction, and betterment costs for the Treasury Department building are capitalized as general PP&E and depreciated over their service life.

K. NON-ENTITY GOVERNMENT-WIDE CASH

Non-entity government-wide cash is held in depositary institutions and Federal Reserve accounts. Agencies can deposit funds that are submitted to them directly into either a Federal Reserve Treasury General Account (TGA) or a local TGA depositary. The balances in these TGA accounts are transferred to the FRBNY's TGA at the end of each day.

Operating Cash of the U.S. Government represents balances from tax collections, customs duties, other revenue, federal debt receipts, and other various receipts net of cash outflows for budget outlays and other payments held in the Federal Reserve Banks, foreign and domestic financial institutions, and in U. S. Treasury Tax and loan accounts. Outstanding checks are netted against operating cash until they are cleared by the Federal Reserve System.

The Treasury General Account (TGA) is maintained at the Federal Reserve Bank of New York (FRBNY) and functions as the government's checking account for deposits and disbursements of public funds. The Treasury Tax and Loan (TT&L) program includes about 9,000 depositories that accept tax payments and remit them the day after receipt to FRBNY's TGA. Certain TT&L depositaries also hold Non-entity Government-wide Cash in interest bearing accounts. Cash in the TGA and the TT&L program is restricted for Government-wide operations.

U. S. Treasury Tax and Loan Accounts include funds invested through the Term Investment Option program and the Repo program. Under the Term Investment Option program Treasury auctions funds for a set term, usually in the range of one day to three weeks. Under the Repo program, Treasury invests funds through overnight reverse repurchase agreements. However, under both programs, Treasury reserves the right to call the funds prior to maturity under special circumstances.

The Supplementary Financing Program (SFP) Account is maintained at FRBNY. SFP is a temporary program announced by Treasury and the Federal Reserve on September 14, 2008, to provide emergency cash for Federal Reserve initiatives aimed at addressing the ongoing crisis in financial markets. The program consists of a series of Treasury bills, apart from Treasury's current borrowing program.

To promote stability in the mortgage market, a Federal Reserve account was established at JP Morgan Chase. Treasury uses this account to purchase Government Sponsored Enterprise (GSE) mortgage-backed securities in the open market.

Other cash is mostly comprised of Automated Clearinghouse transfers and other deferred items.

L. FEDERAL DEBT

Debt and associated interest are reported on the accrual basis of accounting. Interest costs are recorded as expenses 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. The Treasury Department 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.

M. LOAN COMMITMENTS

The FFB recognizes loan commitments when the FFB and the other parties fully execute the promissory notes and reduces loan commitments when the FFB issues loans or when the commitments expire. Most obligations of the FFB give a borrower the contractual right to a loan or loans immediately or at some point in the future. The FFB limits the time available for a loan under an obligation, where applicable.

N. PENSION COSTS, OTHER RETIREMENT BENEFITS, AND OTHER POST EMPLOYMENT BENEFITS

The Treasury Department recognizes the full costs of its employees' pension benefits. However, the liabilities associated with these costs are recognized by the Office of Personnel Management (OPM) rather than the Treasury Department.

Most employees of the Treasury Department hired prior to January 1, 1984, participate in the Civil Service Retirement System (CSRS), to which the Treasury Department contributes 8.51percent of salaries for regular CSRS employees.

On January 1, 1987, the Federal Employees Retirement System (FERS) went into effect pursuant to Public Law 99-335. Employees hired after December 31, 1983, are automatically covered by FERS and Social Security. A primary feature of FERS is that it offers a savings plan to which the Treasury Department automatically contributes 1 percent of base pay and matches any employee contributions up to an additional 4 percent of base pay. For most employees hired after December 31, 1983, the Treasury Department also contributes the employer's matching share for Social Security. For the FERS basic benefit, the Treasury Department contributes 11.2 percent for regular FERS employees.

Similar to federal retirement plans, OPM, rather than the Treasury Department, reports the liability for future payments to retired employees who participate in the Federal Employees Health Benefits Program (FEHBP) and Federal Employees' Group Life Insurance (FEGLI) Program. The Treasury Department reports the full cost of providing other retirement benefits (ORB). The Treasury Department also recognizes an expense and liability for other post employment benefits (OPEB), which includes all types of benefits provided to former or inactive (but not retired) employees, their beneficiaries, and covered dependents. Additionally, the Treasury Department bureaus, OCC and OTS, separately sponsor certain benefit plans for their employees. OCC sponsors a defined life insurance benefit plan for current and retired employees. Additionally, OTS provides certain health and life benefits for all retired employees who meet eligibility requirements

O. SPECIAL DRAWING RIGHTS (SDR)

The ESF was established for use by the Secretary of the Treasury to account for the purchase or sale of foreign currencies, to hold U.S. foreign exchange and Special Drawing Rights (SDR) holdings, and to provide financing to foreign governments. SDR transactions of the ESF require the explicit authorization of the Secretary of the Treasury.

The International Monetary Fund (IMF) has authority to cancel, in part or in whole, SDRs created under previous allocations. Decisions of the IMF to cancel an SDR are adopted by the IMF's Board of Governors on a basis of proposal by the IMF Managing Director, with concurrence by the IMF Executive Board. The same majority requirements as those for allocations apply to the Executive Board's concurrence and to the Board of Governor's decision on an SDR cancellation proposal.

Allocations and Holdings

Allocations of SDR are recorded as liabilities. These liabilities represent the amount that is payable in the event of liquidation of, or U.S. withdrawal from the SDR department of the IMF, or cancellation of the SDR.

SDR holdings represent transactions resulting from ESF SDR activities. These activities are primarily the result of IMF allocations. Other transactions reported in this account are recorded as incurred. They include SDR acquisitions and sales, interest received on SDR holdings, interest charges on SDR allocations, and valuation adjustments. The U.S. Government receives remuneration in SDRs from the IMF. This is based on claims on the IMF, represented by the U.S. Reserve Position. The allocations and holdings are revalued monthly based on the SDR valuation rate calculated by the IMF.

Certificates

The *SDR Act of 1968* authorized the Secretary of the Treasury to issue certificates, not to exceed the value of SDR holdings, to the Federal Reserve Banks in return for interest-free dollar amounts equal to the face value of certificates issued. The certificates may be issued to finance the acquisition of SDR from other countries or to provide resources for financing other ESF operations. Certificates issued are to be redeemed by the Treasury Department at such times and in such amounts as the Secretary may determine. Certificates issued to Federal Reserve Banks are stated at their face value. It is not practical to estimate the fair value of certificates issued to Federal Reserve Banks, since these certificates contain no specific terms of repayment.

P. FEDERAL EMPLOYEE BENEFITS PAYABLE—FECA ACTUARIAL LIABILITY

The *Federal Employees' Compensation Act* (FECA) provides income and medical cost protection to covered federal civilian employees injured on the job, and employees who have incurred a work-related injury or occupational disease. These future workers' compensation estimates were generated from an application of actuarial procedures developed to estimate the liability for FECA benefits. The actuarial liability estimates for FECA benefits include the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases.

Q. ANNUAL, SICK, AND OTHER LEAVE

Annual and compensatory leave earned by Treasury employees, but not yet used, is reported as an accrued liability. The accrued balance is adjusted annually to current pay rates. Any portions of the accrued leave, for which funding is not available, are recorded as an unfunded liability. Sick and other leave are expensed as taken.

R. REVENUE AND FINANCING SOURCES

Treasury Department activities are financed either through exchange revenue it receives from others or through non-exchange revenue and financing sources (such as appropriations provided by the Congress and penalties, fines, and certain user fees collected). User fees primarily include IRS reimbursable costs to process installment agreements and accompanying photocopy and reproduction charges. Exchange revenues are recognized when earned; i.e., goods have been delivered or services have been rendered. Non-exchange revenues are recognized when received by the respective Treasury Department collecting bureau. Appropriations used are recognized as financing sources when related expenses are incurred or assets are purchased. Revenue from reimbursable agreements is recognized when the services are provided. The Treasury Department also incurs certain costs that are paid in total or in part by other federal entities, such as pension costs. These subsidized costs are recognized on the Consolidated Statement of Net Cost, and the imputed financing for these costs is recognized on the Consolidated Statement of Changes in Net Position. As a result, there is no effect on net position. Other non-exchange financing sources such as donations and transfers of assets without reimbursements also are recognized for the period in which they occurred on the Consolidated Statement of Changes in Net Position.

The Treasury Department recognizes revenue it receives from disposition of forfeited property as non-exchange revenue on the Consolidated Statement of Changes in Net Position. The costs related to the Forfeiture Fund program are reported on the Consolidated Statement of Net Cost.

S. CUSTODIAL REVENUES AND COLLECTIONS

Non-entity revenue reported on the Treasury Department's Statement of Custodial Activity includes cash collected by the Treasury Department, primarily taxes. It does not include revenue collected by other federal agencies, such as user fees and other receipts, which are remitted for general operating purposes of the U.S. Government or are earmarked for certain trust funds. The Statement of Custodial Activity is presented on the "modified accrual basis." Revenues are recognized as cash is collected. The "accrual adjustment" is the net increase or decrease, during the reporting period, in net revenue related-assets and liabilities, mainly taxes receivable. The Balance Sheets include an estimated amount for taxes receivable and payable to the General Fund of the U.S. Government at September 30, 2009 and September 30, 2008.

T. TAX ASSESSMENTS, ABATEMENTS, AND REFUNDS PAYABLE

Under Internal Revenue Code Section 6201, the Treasury Department is authorized and required to make inquiries, determinations, and assessments of all taxes which have not been duly paid (including interest, additions to the tax, and assessable penalties) under the law. Unpaid assessments result from taxpayers filing returns without sufficient payment, as well as from tax compliance programs such as examination, under-reporter, substitute for return, and combined annual wage reporting. The Treasury Department also has authority to abate the paid or unpaid portion of assessed tax, interest, and penalty. Abatements occur for a number of reasons and are a normal part of the tax administration process. Abatements may result in claims for refunds or a reduction of the unpaid assessed amount.

Refunds payable arise in the normal course of tax administration when it is determined that taxpayers have paid more than the actual taxes they owe. Amounts the Treasury Department has concluded to be valid refunds owed to taxpayers are recorded as a liability (Refunds Payable on the Balance Sheet), with a corresponding receivable from the General Fund. This receivable is included on the Balance Sheet in the line entitled "Due from the General Fund."

U. PERMANENT AND INDEFINITE APPROPRIATIONS

Permanent and indefinite appropriations are used to disburse tax refunds, income tax credits, and child tax credits. These appropriations are not subject to budgetary ceilings established by Congress. Therefore, refunds payable at year end are not subject to funding restrictions. Refund payment funding is recognized as appropriations are used. Permanent indefinite authority for refund activity is not stated as a specific amount and is available for an indefinite period of time. Although funded through appropriations, refund activity, in most instances, is reported as a custodial activity of the Treasury Department, since refunds are, in substance, a custodial revenue-related activity resulting from taxpayer overpayments of their tax liabilities.

The Treasury Department also receives two permanent and indefinite appropriations related to debt activity. One is used to pay interest on the public debt securities; the other is used to redeem securities that have matured, been called, or are eligible for early redemption. These accounts are not annual appropriations and do not have refunds. Debt activity appropriations are related to the Treasury Department's liability and are reported on the Treasury Department's Balance Sheet. Permanent indefinite authority for debt activity is available for an indefinite period of time.

Treasury receives permanent indefinite appropriations annually to fund increases in the projected subsidy costs of credit programs as determined by the reestimation process required by the FCRA.

Additionally, the Treasury Department receives other permanent and indefinite appropriations to make certain payments on behalf of the U.S. Government. These appropriations are provided to make payments to the Federal Reserve Banks for services provided. They also include appropriations provided to make other disbursements on behalf of the U.S. Government, including payments made to various parties as the result of certain claims and judgments rendered against the United States.

V. INCOME TAXES

As an agency of the Federal Government, the Treasury Department is exempt from all income taxes imposed by any governing body, whether it is a federal, state, commonwealth, local, or foreign government.

W. USE OF ESTIMATES

The Treasury Department 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. Actual results could differ from these estimates. Significant transactions subject to estimates include loan receivables (including Mortgage Backed Securities (MBS) and TARP); investments in non-federal securities (including Government Sponsored Enterprises (GSEs) foreign and domestic public entities) and related impairment, if any; tax receivables; loan guarantees; depreciation; liability for liquidity commitment (GSEs); imputed costs; actuarial liabilities; cost and earned revenue allocations; contingent legal liabilities; and credit reform subsidy costs.

The Treasury 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. Two of the emergency economic programs that Treasury implemented in the latter part of September 2008, the purchase program for MBS and the GSE credit line facility, both operate under the provisions of credit reform and the use of estimates as dictated by the *Federal Credit Reform Act* (Note 12). Additionally, all TARP credit activity, including investments in common and preferred stock and warrants of public companies and loans and loan guarantees or guaranty-like insurance activities, are also subject to credit reform subsidy cost estimates and valuation of direct loans, equity investments and asset guarantees. (Notes 8 and 12)

The forecasted future cash flows used to determine these amounts as of September 30, 2009, are sensitive to slight changes in model assumptions, such as general economic conditions, specific stock price volatility of the entities in which the Treasury Department has an equity interest, estimates of expected default, and prepayment rates. Forecasts of future financial results have inherent uncertainty and the TARP Direct Loans and Equity Investments, Net, and Asset Guarantee Program line items as of September 30, 2009, are reflective of relative illiquid, troubled assets whose values are particularly sensitive to future economic conditions and other assumptions. Additional discussion related to sensitivity analysis can be found in the Management's Discussion and Analysis section of the Agency Financial Report.

The GSE preferred stock agreements provide that the Treasury Department will increase its investment in the GSE's senior preferred stock if at the end of any quarter the Federal Housing Finance Agency (FHFA), acting as the conservator, determines that the liabilities of either GSE, individually, exceed its respective assets. Based on U.S. GAAP, these contingent liquidity commitments predicated on the future occurrence of any shareholders' deficits of the GSEs at the end of any reporting quarter, are potential liabilities of Treasury. Valuation analyses were performed to attempt to provide a "sufficiently reliable" estimate of the outstanding commitment in order for Treasury to record the remaining liability in accordance with SFFAS 5. The valuation incorporated various forcasts, projections and cash flow analysis to develop an estimate of potential liability. Note 9 discusses the results of the valuation and the liability recorded as of September 30, 2009.

X. CREDIT RISK

Credit risk is the potential, no matter how remote, for financial loss from a failure of a borrower or a counterparty to perform in accordance with underlying contractual obligations. The Treasury Department takes on possible credit risk when it makes direct loans or credits to foreign entities or becomes exposed to institutions which engage in financial transactions with foreign countries (Note 11). Given the history of the Treasury Department with respect to such exposure and the financial policies in place in the U. S. Government and other institutions in which the United States participates, the Treasury Department expectations of credit losses is nominal.

The Treasury Department also takes on credit risk related to committed but undisbursed direct loans, its liquidity commitment to GSE, its MBS portfolio, investments, loans, and asset guarantees of the TARP, its insurance of non-FDIC insured money market funds, and its Terrorism Risk Insurance Program. Except for the Terrorism Risk Insurance Program, these activities focus on the underlying problems in the credit markets, and the ongoing instability in those markets exposes the Department to potential unknown costs and losses. The extent of the risk assumed by the Treasury Department 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 (Notes 8, 9 & 12).

In addition, for EESA programs, the statute requires that market risk be considered in the subsidy cost of the asset, through an adjustment to the discount rate. Within the TARP programs, Treasury has invested in many assets that would traditionally be held by private investors and their valuation would inherently include market risk. Thus, for all TARP direct loan, guarantee, and equity purchase programs, Treasury calculates a Market Risk Adjusted Discount Rate (MRADR). Therefore, the Treasury cost estimates for the TARP programs are adjusted for unexpected loss and the estimated risk of expected cash flows. Under SFFAS No. 2, including market risk in the cash flow estimates is consistent with the type of assets and liabilities being valued. The inclusion of the MRADR is the mechanism for providing the fair market value of the assets.

Y. EARMARKED FUNDS

Treasury has accounted for revenues and other financing sources for earmarked funds separately from other funds. Earmarked funds are financed by specifically identified revenues, 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 or purposes. SFFAS No. 27, *Identifying and Reporting Earmarked Funds*, defines the following three criteria for determining an earmarked fund: (1) A statute committing the Federal Government to use specifically identified revenues and other financing sources not used in the current period for future use to finance the designated activities, benefits, or purposes; (2) Explicit authority for the earmarked fund to retain revenues and other financing sources not used in the current period for future use to finance the designated activities, benefits, or purposes; and (3) A requirement to account for and report on the receipt, use, and retention of the revenues and other financing sources that distinguished the earmarked fund from the Federal Government's general revenues.

Z. ALLOCATION TRANSFERS

The Treasury Department is a party to allocation transfers with other federal agencies as both a transferring (parent) entity and/or a receiving (child) entity. Allocation transfers are legal delegations by one department of its authority to obligate budget authority and outlay funds to another department. A separate fund account (allocation account) is created in the U.S. Treasury as a subset of the parent fund account for tracking and reporting purposes. All allocation transfers of balances are credited to this account, and subsequent obligations and outlays incurred by the child entity are charged to this allocation account as they execute the delegated activity on behalf of the parent. Beginning in fiscal year 2007, parent federal agencies report both the proprietary and budgetary activity and the child agency does not report any financial activity related to budget authority allocated from the parent federal agency to the child federal agency.

The Treasury Department allocates funds, as the parent, to the Department of Energy. OMB allows certain exceptions to allocation reporting for certain funds. Accordingly, the Treasury Department has reported certain funds for which the Treasury Department is the child in the allocation transfer, but in compliance with OMB guidance (A-136 III.4.2 section 5 for three exceptions), will report all activities relative to these allocation transfers in the Treasury Department's financial statements. Also, the Treasury Department receives allocation transfers, as the child, from the Agency for International Development and Department of Transportation. The Treasury Department had no significant allocation transfers to report in fiscal years 2009 and 2008.

AA. CREDIT REFORM ACCOUNTING

The authoritative guidance for the credit reform portion of these statements is contained primarily in SFFAS No. 2, *Accounting for Direct Loans and Loan Guarantees*, as amended by SFFAS No. 18, *Amendments to Accounting Standards for Direct Loans and Loan Guarantees*, and SFFAS No. 19, *Technical Amendments to Accounting Standards for Direct Loans and Loan Guarantees*. This guidance was promulgated as a result of the *Federal Credit Reform Act of 1990* (FCRA).

The FCRA requires that the ultimate costs of a credit program be calculated, and the budgetary resources obtained, before the direct loan obligations are incurred. The cost of loan guarantee programs is the net present value of the estimated future cash flows from payments (for claims and interest rate subsidies). The primary purpose of the FCRA, which became effective on October 1, 1991, is to more accurately measure the cost of federal credit programs and to place the cost of such credit programs on a basis equivalent with other federal spending.

SFFAS No. 2, which generally mirrors the requirements of the FCRA, established guidance for estimating the cost of direct and guaranteed loan programs, as well as for recording direct loans and liabilities for loan guarantees for financial reporting purposes. SFFAS No. 2 states that the actual and expected costs of federal credit programs should be fully recognized in both budgetary and financial reporting. To accomplish this, agencies first predict or estimate the future performance of direct and guaranteed loans when preparing their annual budgets. The data used for these budgetary estimates are reestimated after the fiscal year-end to reflect changes in actual loan performance and actual interest rates in effect when the loans were issued. The data used for these estimates were reestimated at the fiscal year-end to reflect adjustments for market risk, asset performance, and other key variables and economic factors. The reestimate data are then used to report the cost of the loans disbursed under the direct or guaranteed loan program as a "Program Cost" in the agencies' Statement of Net Cost.

The FCRA establishes budgetary and financing control for each credit program through the use of the program, financing and negative subsidy receipt accounts for direct loans obligated after September 30, 1991. The FCRA establishes the use of the program, financing, and general fund receipt for direct loans obligated after September 30, 1991. These accounts are classified as either budgetary or non-budgetary in the Combined Statements of Budgetary Resources. The budgetary accounts include the program accounts and receipt accounts. The non-budgetary accounts consist of the credit reform financing accounts.

The program account is a budget account that receives and obligates appropriations to cover the subsidy cost of a direct loan or guarantee and disburses the subsidy cost to the financing account. The program account also receives appropriations for administrative expenses. The financing account is a non-budgetary account that records all of the cash flows resulting from Credit Reform direct loans or loan guarantees. It disburses loans, collects repayments and fees, makes claim payments, holds balances, borrows from BPD, earns or pays interest, and receives the subsidy cost payment from the program account.

The General Fund receipt account is a budget account used for the receipt of amounts paid from the financing account when there is a negative subsidy or negative modification from the original estimate or a downward reestimate. They are available for appropriations only in the sense that all General Fund receipts are available for appropriations. Any assets in this account are non-entity assets and are offset by intragovernmental liabilities. At the end of the fiscal year, the fund balance transferred to the U.S. Treasury through the General Fund receipt account is no longer included in Treasury's fund balance reporting.

The Department of Treasury accounts for TARP direct loans, equity investments and Asset Guarantees, MBS purchased as a part of GSEs assistance program, and the GSE Credit Facility program, in accordance with the FCRA and the provisions under the FASAB accounting standard SFFAS No. 2, as amended. Treasury determined it was acceptable to include an estimate of market risk in the calculation of subsidy cost under SFFAS No. 2.

AB. FIDUCIARY ACTIVITIES

Treasury has adopted SFFAS No. 31, *Accounting for Fiduciary Activities*, which is effective for years beginning after September 30, 2008. SFFAS No. 31, prescribes that fiduciary type activities and related transactions will no longer be reported in proprietary financial statements. Fiduciary activities are the collection or receipt, and the management, protection, accounting, investment, and disposition by the Federal Government of cash or other assets in which non-Federal individuals or entities have an ownership interest that the Federal Government must uphold. Fiduciary cash and other assets are not assets of the Federal Government. While these activities are no longer reported in the proprietary financial statements, they are required to be reported on schedules in the notes to financial statements (Note 30).

AC. RECLASSIFICATIONS

Certain fiscal year 2008 balances on the Statements of Budgetary Resources (SBR) and Net Cost (SNC) have been reclassified to conform to the fiscal year 2009 presentations. In fiscal year 2009, certain SBR budgetary and non-budgetary amounts were disaggregated whereas in fiscal year 2008 they were reported in the aggregate. The change was made to appropriately disclose the significant TARP and GSEs non-budgetary credit reform activity that occurred in fiscal year 2009. In addition, the Investments in GSEs accrued year-end liquidity payment disclosed as of September 30, 2008 were reported in the Statement of Net Cost (SNC) separate from the four Treasury strategic goals. In fiscal year 2009, Treasury concluded that the cost of this program helps accomplish the Treasury strategic goal of ensuring that the U.S. economy performs at its full economic potential. Thus, as of September 30, 2009 the cost of investments in GSEs and the related year-end accrual are included in the Economic Program section of the SNC. The GSE transaction reclassification in the SNC also caused a similar reclassification for the GSE transaction in Note 28, Reconciliation of Net Cost of Operations to Budget, as well.

AD. RELATED PARTIES

The primary "related parties" with whom the Treasury Department conducts business are other federal agencies, mainly through the normal lending activities of the BPD and the Federal Financing Bank. These activities are disclosed in these financial statements. The Treasury Department utilizes the services of the Federal Reserve to execute a variety of transactions on behalf of the BPD and the Exchange Stabilization Fund. The Federal Reserve is serving as the Treasury Department's fiscal agent in executing these transactions and receives fees for its services. The Treasury Department also consults with the Federal Reserve on matters affecting the economy, such as the structuring of bailout financing for American International Group and other companies affected by the current economic situation. However, these actions do not involve transactions between the Treasury Department and the Federal Reserve.

Finally, the Secretary of the Treasury serves on the Federal Housing Finance Administration (FHFA) Oversight Board, and consults with the Director of FHFA in matters involving Fannie Mae and Freddie Mac. This provides the Treasury Department a voice in the FHFA's actions as the conservator for Fannie Mae and Freddie Mac, and thus some influence over major decisions involving Fannie Mae and Freddie Mac. The Treasury Department has no transactions with FHFA; transactions and balances arising from transactions with Fannie Mae and Freddie Mac are accounted for and disclosed in these financial statements.

2. FUND BALANCE

Fund Balance with Treasury is the aggregate amount of the Treasury Department's accounts with the U.S. Government's central accounts from which the Treasury Department is authorized to make expenditures and pay liabilities. It is an asset because it represents the Treasury Department's claim to the U.S. Government's resources. Fund balance with Treasury is not equivalent to unexpended appropriations, because it also includes non-appropriated revolving and enterprise funds, suspense accounts, and custodial funds such as deposit funds, special funds, and trust funds.

Appropriated funds consist of amounts appropriated annually by Congress to fund the operations of the Department. Appropriated funds include clearing funds, which represent reconciling differences with Treasury balances.

Revolving funds are used for continuing cycles of business-like activity, in which the fund charges for the sale of products or services and uses the proceeds to finance its spending, usually without requirement for annual appropriations. A public enterprise revolving fund is an account that is authorized by law to be credited with offsetting collections from the public and those monies are used to finance operations. The Working Capital Fund is a fee-for-service fund established to support operations of Department Components. Also included are the financing funds for credit reform. The GSA and TARP programs were the main drivers for the increase in appropriated and revolving funds.

Trust funds include both receipt accounts and expenditure accounts that are designated by law as a trust fund. Trust fund receipts are used for specific purposes.

Deposit funds represent amounts received as an advance that are not accompanied by an order and include non-entity collections that do not belong to the Federal Government. See Note 30, Schedule of Fiduciary Activity for Non-Entity collections.

Special funds include funds designated for specific purposes including the disbursement of non-entity monies received in connection with the Presidential Election Campaign.

Fund Balances: As of September 30, 2009 and September 30, 2008, fund balances consisted of the following (in millions):

	2009	2008
Appropriated Funds	$ 455,983	$ 272,561
Revolving Funds	47,897	1,837
Trust Funds	5	2
Clearing Funds	93	26
Deposit Funds	146	587
Special Funds	455	299
Other Funds (Receipts and Suspense Funds)	3	56
Total Fund Balances	**$ 504,582**	**$ 275,368**

Status of Fund Balance with Treasury

Portions of the Unobligated Balance Unavailable include amounts appropriated in prior fiscal years that are not available to fund new obligations. However, it can be used for upward and downward adjustments for existing obligations in future years. The Obligated Balance Not Yet Disbursed represents amounts designated for payment of goods and services ordered but not received or goods and services received but for which payment has not yet been made.

Since the following line items do not post to budgetary status accounts, the following adjustments are required to reconcile the budgetary status to non-budgetary Fund Balance with Treasury as reported in the accompanying Balance Sheets:

- Adjustments for Non-Budgetary Funds are receipt, clearing, and deposit funds that represent amounts on deposit with Treasury that have no budget status.
- Borrowing authority is in budgetary status but not in Fund Balance with Treasury.
- Budgetary resources have investments included; however, the money has been moved from the Fund Balance with Treasury asset account to Investments.
- Impress funds represent monies moved from Fund Balance with Treasury to Cash and Other Monetary Assets with no change in the budgetary status.
- Adjustments for IMF– monies moved from Fund Balance with Treasury to Other Monetary Assets related to IMF accounts that are with the Federal Reserve Bank of New York. They also include the IMF Reserve Position based on SDRs.
- Adjustment for Unavailable for Obligations reduced the budgetary resources; however, did not impact the Fund Balance with Treasury.

As of September 30, 2009 and September 30, 2008, the status of fund balances consisted of the following (in millions):

	2009	2008
Unobligated Balance – Available	$ 382,047	$ 242,939
Unobligated Balance – Unavailable	33,841	11,395
Obligated Balance not yet Disbursed	158,324	56,868
Subtotal	**$ 574,212**	**$ 311,202**
Adjustment for Non-Budgetary Funds	241	669
Adjustment for Borrowing Authority	(51,510)	(29,810)
Adjustment for Intra-Treasury Investments	(8,554)	(5,530)
Adjustment for Imprest Funds	(4)	(4)
Adjustment for IMF	(13,513)	(4,838)
Adjustments for Temporary Reduction	30	0
Authority Unavailable for Obligation	3,680	3,679
Total Status of Fund Balance	**$ 504,582**	**$ 275,368**

For ESF, the above balances only include unobligated balances related to the ESF insurance program that began in fiscal year 2008, and expired on September 18, 2009. Otherwise, ESF does not have Fund Balance with Treasury. Accordingly, while other ESF balances are included on the Statement of Budgetary Resources (SBR), they are not a component of Fund Balance with Treasury. The ESF balances displayed on the SBR include components of cash, foreign currency, and other monetary assets (Note 6).

As of September 30, 2009 and September 30, 2008, the Treasury Department did not have any budgetary authority in Fund Balance with Treasury that was specifically withheld from apportionment by OMB. The balances in non-entity funds, such as certain deposit funds (e.g., seized cash), are being held by the Treasury Department for the public or for another federal entity, such as the General Fund of the U.S. Government. Such funds have an offsetting liability equal to fund balance. See Note 14 regarding restrictions related to the line of credit held on the U.S. Quota in the International Monetary Fund.

3. LOANS AND INTEREST RECEIVABLE - INTRA-GOVERNMENTAL

As of September 30, 2009 and September 30, 2008, intra-governmental loans (issued by the Federal Financing Bank) and interest receivable consisted of the following (in millions):

Entity Intra-governmental:

	Loans Receivable	Interest Receivable	2009 Total	Loans Receivable	Interest Receivable	2008 Total
Department of Agriculture	$ 28,438	$ 52	$ 28,490	$ 26,326	$ 50	$ 26,376
National Credit Union Administration	18,384	22	18,406	1,109	0	1,109
United States Postal Service	10,200	37	10,237	7,200	1	7,201
General Services Administration	2,037	36	2,073	2,098	37	2,135
Department of Energy	908	0	908	0	0	0
Department of Housing and Urban Development	587	71	658	691	84	775
Executive Office of the President	546	6	552	680	8	688
Department of Education	453	2	455	338	3	341
Department of Defense	0	0	0	17	0	17
Other Agencies	12	0	12	18	0	18
Subtotal-Entity	**$ 61,565**	**$ 226**	**$ 61,791**	**$ 38,477**	**$ 183**	**$ 38,660**

The FFB issues the above loans to federal agencies for their own use or to private sector borrowers, whose loans are guaranteed by the federal agencies. When a federal agency has to honor its guarantee because a private sector borrower defaults, the federal agency that guaranteed the loan must obtain an appropriation or use other resources to repay the FFB. Loan principal and interest are backed by the full faith and credit of the U.S. Government, except for loans to the U.S. Postal Service. The FFB has not incurred and does not expect to incur any credit-related losses on its loans and accordingly, has not recorded an allowance for uncollectible intra-governmental loans.

Non-Entity Intra-governmental:

	Loans Receivable	Interest Receivable	2009 Total	Loans Receivable	Interest Receivable	2008 Total
Department of Education	$ 234,918	$ 12	$ 234,930	$ 128,331	$ 0	$ 128,331
Department of Agriculture	55,627	2	55,629	51,192	9	51,201
Department of Homeland Security	19,004	0	19,004	17,360	359	17,719
Small Business Administration	10,873	0	10,873	9,463	0	9,463
Department of Labor	6,371	0	6,371	0	0	0
Other Agencies	5,961	1	5,962	3,944	0	3,944
Department of Housing and Urban Development	4,425	0	4,425	4,832	0	4,832
Export Import Bank of the U. S.	3,805	0	3,805	2,929	0	2,929
Railroad Retirement Board	3,359	58	3,417	3,096	69	3,165
Department of Energy	2,131	18	2,149	2,186	20	2,206
Department of Veterans Affairs	1,545	0	1,545	1,575	0	1,575
Department of the Interior	316	328	644	323	393	716
Federal Communications Commission	46	0	46	113	0	113
Subtotal Non-Entity	**$ 348,381**	**$ 419**	**$ 348,800**	**$ 225,344**	**$ 850**	**$ 226,194**
Total Intra-governmental Loans and Interest Receivable Entity and Non-Entity			**$ 410,591**			**$ 264,854**

BPD accounts for and reports on the principal borrowings from and repayments to the General Fund of the United States for approximately 80 funds managed by other federal agencies, as well as the related interest due to the General Fund. These agencies are statutorily authorized to borrow from the General Fund, through BPD, to make loans for a broad range of purposes, such as education, housing, farming, and small business support.

4. DUE FROM THE GENERAL FUND AND DUE TO THE GENERAL FUND

The Treasury Department is responsible for managing various assets and liabilities on behalf of the U.S. Government as a whole. Due from the General Fund represents amounts required to fund liabilities managed by Treasury Department on behalf of the U.S. Government. Liabilities managed by the Treasury Department are comprised primarily of the federal debt. Due to the General Fund represents assets held for the General Fund of the U.S. Government.

As of September 30, 2009 and September 30, 2008, Due from and Due to the General Fund, included the following non-entity assets and liabilities (in millions):

Liabilities Requiring Funding from the General Fund:	2009	2008
Federal Debt and Interest Payable	$ 7,559,305	$ 5,812,694
Federal Debt and Interest Payable - Intra-governmental	4,403,080	4,262,414
Refunds Payable	4,040	3,076
Adjustment for Eliminated Liabilities	26,294	22,579
Total Due from the General Fund	$ 11,992,719	$ 10,100,763

Assets to be Distributed to the General Fund:		
Fund Balance	$202	$215
Advances to the Black Lung Trust Fund	0	10,484
Advances to the Unemployment Trust Fund	7,981	0
Cash Held by the Treasury Department	269,311	364,594
Foreign Currency	26	31
Custodial Gold and Silver held by the U.S. Mint without certificates	25	25
Loans and Interest Receivable - Intra-governmental	348,800	226,194
Loans and Interest Receivable	127	130
Investments in GSEs	64,679	7,032
Credit Reform Downward Subsidy Reestimate	118,139	0
Accounts Receivable - Intra-governmental	285	372
Tax and Other Non-Entity Receivables	30,353	30,489
Beneficial Interest in Trust	23,472	0
Miscellaneous Assets	3	12
Adjustment for Eliminated Assets	399,725	27,534
Total Due to the General Fund	$ 1,263,128	$ 667,112

The Adjustment for Eliminated Intra-Treasury liabilities mainly represents investments in U.S. Government securities held by Treasury reporting entities that were eliminated against Federal Debt and Interest Payable. The Adjustment for Eliminated Intra-Treasury assets mainly represents loans and interest payable owed by Treasury reporting entities, which were eliminated against Loans and Interest Receivable held by the BPD.

The non-entity Credit Reform Downward Subsidy Reestimates represents amounts for the downward subsidy reestimates for the Treasury's discretionary GSE MBS Credit Program Receivables ($8,392 million) and TARP Direct Loan, Equity Investments and Asset Guarantees ($109,747 million). Downward subsidy reestimates indicates that too much subsidy will be or has been paid to the credit reform financing account. Because these credit programs are discretionary, the downward reestimates are not available to Treasury and they are returned to the U.S. Government General Fund Receipt Account (GFRA) in the fiscal year following the accrual of the reestimates. Generally, during the year, these GFRAs contain prior year reestimates. At year-end, the prior year funds are "swept" by the General Fund. Since fiscal year 09 is the first year Treasury has reported reestimates there were no prior year balances in the GFRAs. Also at year-end, the Treasury accrues the current year's reestimates, including downward reestimates as applicable. For the downward reestimates, in the loan financing funds, the Treasury records an inter-governmental accrual adjustment that records a transfer out to the non-entity fund, a reduction of subsidy allowance or loan guarantee liability, and an account payable to the GFRA non-entity fund. In the loan program funds, the Treasury records a reduction of loan subsidy expense and the associated impact on the net cost. The non-entity GFRAs contain a corresponding inter-governmental account receivable in anticipation of the receipt of the downward reestimates in the following year and a Downward Reestimate Liability for Non-Entity Asset due to the general fund. For consolidated financial statement presentation, Treasury is required to eliminate the financing fund's inter-governmental payable due to the GFRA and the GFRA's inter-governmental receivable due from the financing funds; since both are included in Treasury reporting entity. The Downward Reestimate Liability for Non-Entity Asset Due to the General Fund is reflected on the Balance Sheet's intra-governmental liability Due to the General Fund line.

On the Balance Sheet, the Treasury Department reported $30,408 million in Tax, Other, and Related Interest Receivables as of September 30, 2009 ($30,878 million as of September 30, 2008). However, only $30,353 million is reported as Due to the General Fund of the U.S. Government ($30,489 million as of September 30, 2008). The difference is attributable to the exclusion of amounts which will be paid to others outside the U.S. Government, and miscellaneous entity receivables (see Notes 5 and 15).

5. ACCOUNTS RECEIVABLE AND RELATED INTEREST—INTRA-GOVERNMENTAL

Intra-governmental accounts receivable and interest mainly represents non-entity payments made by the Treasury Department under the *Contract Disputes Act* ($285 million of the $298 million and $368 million of the $396 million displayed on the balance sheet for 2009 and 2008, respectively). Other federal agencies are required to reimburse the Treasury Department for payments made on their behalf, related to the *Contract Disputes Act* and the No Fear Act. These amounts are a receivable on the Treasury Department's books, specifically the Financial Management Service, and a payable on the other federal agencies' books until reimbursement is made. The remaining amount displayed as intra-governmental accounts receivable and interest is related to miscellaneous intra-governmental transactions.

6. CASH, FOREIGN CURRENCY, AND OTHER MONETARY ASSETS

Cash, foreign currency, and other monetary assets held as of September 30, 2009 and September 30, 2008 were as follows (in millions):

	2009	2008
Entity:		
Cash	$ 23	$ 19
Foreign Currency and Foreign Currency Denominated Assets	13,701	12,758
Other Monetary Assets:		
Special Drawing Rights	57,961	9,464
Other	44	88
Subtotal - Entity	**$ 71,729**	**$ 22,329**
Non-Entity:		
Operating Cash of the U.S. Government	$ 269,052	$ 364,273
Foreign Currency	26	31
Miscellaneous Cash held by all Treasury sub-components	501	637
Subtotal - Non-Entity	**$ 269,579**	**$ 364,941**
Total Cash, Foreign Currency, and Other Monetary Assets	**$ 341,308**	**$ 387,270**

Non-entity Operating Cash and Other Cash of the U.S. Government held by the Treasury Department disclosed above consisted of the following (in millions):

	2009	2008
Operating Cash of the U.S. Government	$ 2,063	$ 39,209
Operating Cash - Federal Reserve Bank Account	273,269	332,480
Subtotal	**$ 275,332**	**$ 371,689**
Outstanding Checks	(6,280)	(7,416)
Total Operating Cash of the U.S. Government	**$ 269,052**	**$ 364,273**
Other Cash	366	386
Subtotal	**$ 269,418**	**$ 364,659**
Amounts Due to the Public	(107)	(65)
Total Cash Due to the General Fund (See Note 4)	**$ 269,311**	**$ 364,594**

Entity

Entity cash, foreign currency, and other monetary assets primarily include Foreign Currency Denominated Assets (FCDA), Special Drawing Rights (SDR), and forfeited cash. SDR and FCDA are valued as of September 30, 2009 and September 30, 2008, using current exchange rates plus accrued interest. "Other" includes U.S. dollars restricted for use by the International Monetary Fund (IMF), which are maintained in two accounts at the FRBNY.

The foreign currency holdings are normally invested in interest bearing securities issued by or held through foreign governments or monetary authorities. FCDA with original maturities of three months or less, were valued at $8.7 billion as of September 30, 2009 ($9.3 billion as of September 30, 2008). Other FCDAs having terms of less than or equal to a year but greater than three months are classified as available for sale. As of September 30, 2009, FCDA with maturities greater than three months were valued at $2.4 billion ($3.5 billion as of September 30, 2008).

The SDR are international reserve assets created by the IMF. They were created as a supplement to existing reserve assets and on several occasions SDR have been allocated by the IMF to members participating in the IMF's SDR department. The SDR derives their value as reserve assets, essentially, from the commitments of participants to hold and accept SDR and to honor various obligations connected with their proper functioning as a reserve asset.

The *Special Drawing Rights Act of 1968* authorizes the Secretary of the Treasury Department to issue certificates, not to exceed the value of SDR holdings, to the Federal Reserve Banks in return for interest free dollar amounts equal to the face value of certificates issued. The certificates may be issued for the purpose of financing the acquisition of SDR from other countries or to provide resources for financing exchange stabilization activities. Certificates issued are to be redeemed by the Treasury Department at such times and in such amounts as the Secretary of the Treasury Department may determine. As of September 30, 2009, the value of the certificates issued to Federal Reserve Banks amounted to $5.2 billion ($2.2 billion as of September 30, 2008).

On a daily basis, the IMF calculates the value of the SDR using the market value, in terms of the U.S. dollar, from the amounts of each of four freely usable weighted currencies, as defined by the IMF. These currencies are the U.S. dollar, the European euro, the Japanese yen, and the British pound sterling. Treasury Department's SDR holdings (assets resulting from various SDR related activities including remuneration received on interest earned on the U.S. reserve position – see Note 14) and allocations from the IMF (liabilities of the U.S. coming due only in the event of a liquidation of, or U.S. withdrawal from the SDR department of the IMF, or cancellation of SDR) are revalued monthly based on the SDR valuation rate calculated by the IMF.

Pursuant to the IMF Articles of Agreement, SDR allocated to or otherwise acquired by the United States are permanent resources unless:

a. cancelled by the Board of Governors based on an 85 percent majority decision of the total voting power of the Executive Board of the IMF

b. the SDR Department of the IMF is liquidated

c. the IMF is liquidated or

d. the United States chooses to withdraw from the IMF or terminate its participation in the SDR Department.

Except for the payment of interest and charges on SDR allocations to the United States, the payment of the Treasury Department's commitment related to SDR allocations is conditional on events listed above, in which the United States has a substantial or controlling voice. Allocations of SDR were made in 1970, 1971, 1972, 1979, 1980, and 1981, and 2009. On August 28, 2009, the ESF received 27.5 billion SDRs (equivalent of $43 billion in U.S.) as the U.S. share of a general allocation from the IMF. On September 9, 2009, the ESF received 2.9 billion SDRs (equivalent of $4.5 billion in U.S.) as the U.S. share of a special allocation from the IMF. As of September 30, 2009, the amount of SDR holdings and related accruals of the United States was the equivalent of $ 57.9 billion, and the amount of SDR allocations to the United States was the equivalent of $ 55.9 billion. As of September 30, 2008, the amount of SDR holdings and related accruals of the United States was the equivalent of $ 9.4 billion and the amount of SDR allocations to the United States was the equivalent of $7.6 billion.

In fiscal year 2009, Treasury entered into a voluntary arrangement with the IMF for the purpose of providing additional hard currency liquidity to certain countries. The voluntary arrangement allows Treasury to purchase up to approximately 16 billion SDRs. As of September 30, 2009 and September 30, 2008, the value of SDR allocations was the equivalent of $55.9 and $7.6 billion, respectively.

During fiscal year 2009, the Treasury Department received remuneration on the U.S. reserve position in the IMF, at the prevailing rates, in the amount of $39.6 million equivalent of SDR ($59 million equivalent of SDR during fiscal year 2008), and paid the General Fund of the Federal Government $0.0038 million ($0.01 million in fiscal year 2008) in interest on these funds until they were transferred to the General Fund.

Securities Purchased Under Agreement to Resell are issued in book entry form and denominated in Euro, and issued or guaranteed in full by Belgium, France, Germany, Italy, the Netherlands and Spain. Maturities of the Securities will not exceed 10.5 years. The duration of individual repo transactions will not exceed 90 days. These agreements are generally treated as collateralized financial transactions and are carried at amounts at which the securities were acquired. ESF has $2.6 billion securities which are pledged on behalf of their fiscal agent, Federal Reserve Bank of New York (FRBNY). The fair value of such securities is monitored throughout the contract term to insure that asset values remain sufficient to protect against counterparty default.

Non-Entity

Non-entity cash, foreign currency, and other monetary assets include the Operating Cash of the U.S. Government, managed by the Treasury Department. Also included is foreign currency maintained by various U.S. and military disbursing offices. It also includes seized monetary instruments, undistributed cash, and offers in compromises which are maintained as the result of the Treasury Department's tax collecting responsibilities.

The Operating Cash of the U.S. Government represents balances from tax collections, other revenues, federal debt receipts, and other various receipts net of checks outstanding, which are held in the Federal Reserve Banks, foreign and domestic financial institutions, and in U.S. Treasury tax and loan accounts at commercial banks. Operating Cash of the U.S. Government is either insured (for balances up to $250,000), as of September 30, 2009, by the FDIC or collateralized by securities pledged by the depository institutions and held by the Federal Reserve Banks, or through securities held under reverse repurchase agreements.

The Supplementary Financing Program (SFP) is a temporary program announced on September 17, 2008, by Treasury and the Federal Reserve, to provide emergency cash for Federal Reserve initiatives aimed at addressing the ongoing crisis in financial markets. At the height of this program's activity, during the week of November 6, 2008, there were a total of 15 cash management bills outstanding that totaled $560 billion. As of September 30, 2009, there were a total of five SEP cash management bills outstanding that totaled $165 billion. The decrease is a result of outstanding SFP bills that have matured and have not been reinvested in the program. On September 16, 2009, Treasury announced its intention to reduce the balance to $15 billion in the short run to preserve flexibility in the conduct of debt management policy.

7. GOLD AND SILVER RESERVES, AND GOLD CERTIFICATES ISSUED TO THE FEDERAL RESERVE BANKS

The Treasury Department is responsible for safeguarding most of the U.S. Government's gold and silver reserves in accordance with 31 USC 5117. The Consolidated Balance Sheets also reflect the value of the gold being held in the FRBNY.

Gold reserves being held by the Treasury Department are offset by a liability for gold certificates issued by the Secretary of the Treasury Department to the Federal Reserve Banks as provided in 31 USC 5117. Since 1934, Gold Certificates have been issued in non-definitive or book-entry form to the Federal Reserve Banks. The Treasury Department's liability incurred by issuing the Gold Certificates is limited to the gold being held by the Treasury Department at the legal standard value established by law. Upon issuance of Gold Certificates to the Federal Reserve Banks, the proceeds from the certificates are deposited into the operating cash of the U.S. Government. All of the Treasury Department's certificates issued are payable to the Federal Reserve Banks.

The deep storage gold and silver reserves are reported at the values stated in 31 U. S. C. §§ 5116 – 5117 (statutory rates) which are $42.2222 per fine troy ounce (FTO) of gold and no less than $1.292929292 per FTO of silver. Accordingly, the silver is valued at $1.292929292 per FTO. The gold and silver reserves are in the custody of the U.S. Mint and FRBNY. The U.S. Mint holds gold and silver reserves without certificates (See Note 4). As of September 30, 2009 and September 30, 2008, the gold and silver reserves consisted of the following (in millions):

	FTOs	Statutory Rate	9/30/09 Statutory Value	Market Rate	9/30/09 Market Value
Gold	248,046,116	$ 42.2222	$ 10,473	$ 995.75	$ 246,992
Gold Held by Federal Reserve Banks	13,452,784	$42.2222	568	$ 995.75	13,396
Subtotal - Gold	261,498,900		$ 11,041		$ 260,388
Silver	16,000,000	$ 1.292929292	21	$ 16.45	263
Total Gold and Silver Reserves			**$ 11,062**		**$ 260,651**

	FTOs	Statutory Rate	9/30/08 Statutory Value	Market Rate	9/30/08 Market Value
Gold	248,046,116	$ 42.2222	$ 10,473	$ 884.50	$ 219,397
Gold Held by Federal Reserve Banks	13,452,784	42.2222	568	$ 884.50	11,899
Subtotal - Gold	261,498,900		$ 11,041		$ 231,296
Silver	16,000,000	1.292929292	21	$ 12.96	207
Total Gold and Silver Reserves			$ 11,062		$ 231,503

8. INVESTMENTS – CREDIT REFORM AND ASSET GUARANTEE

The F*ederal Credit Reform Act of 1990* (FCRA) and associated FASAB accounting standard SFFAS No. 2, as amended, governs direct loans and asset guarantees made after fiscal year 1991. FCRA loans are valued at the present value of expected future cash flows, discounted at the interest rate of marketable Treasury securities. The subsidy allowance account represents the difference between the outstanding loan receivables balance and the net present value of the estimated cash flows of the loans over their remaining term. The subsidy allowance is subtracted from the outstanding loans receivable balance to obtain the net loans receivable balance.

Under the provisions of the EESA, Treasury implemented the TARP which resulted in the development of several equity investment programs and transactions including: the Capital Purchase Program; the American International Group, Inc. Investment Program (formerly known as Systemically Significant Failing Institution Program); the Targeted Investment Program; the Automotive Industry Investment Program; the Public-Private Investment Program; and the Asset Guarantee Program.

Treasury applies the provisions of SFFAS No. 2 to account for equity investments (including asset guarantees). This standard requires measurement of the asset or liability at the present value of the estimated future cash-flows. The cash flow estimates for each equity investment transaction reflect the actual structure of the instruments. Analytical cash flow models generate estimated cash flows to and from Treasury over the estimated term of the facility. Further, each cash-flow model reflects the specific terms and conditions of the program, technical assumptions regarding the underlying assets, risk of default or other losses, and other factors as appropriate. The models also incorporate an adjustment for market risk to reflect the additional return required by the market to compensate for variability around the expected losses reflected in the cash flows (the "unexpected loss"). The basic methods for these models as well as a description of each equity investment program are outlined below.

Equity Investments

Preferred stock cash flows are projected using an analytical model developed to incorporate the risk of losses associated with adverse events, such as failure of the institution or increases in market interest rates. The model estimates how cash flows vary depending on 1) current interest rates, which may affect the decision whether to repay the preferred stock; and 2) the strength of a financial institution's assets. Inputs to the model include institution specific accounting data obtained from regulatory filings; an institution's stock price volatility, historical bank failure information as well as market prices of comparable securities trading in the market. Treasury estimates the values and projects the cash flows of warrants using an option-pricing approach based on the current stock price and its volatility. Investments in common stock which are exchange traded is valued at the market price. The result of using market prices, either quoted prices for the identical asset or quoted prices for comparable assets, is that the equity investments are recorded at estimated fair value.

Asset Guarantees

The value of the asset guarantee reflect the net present value of estimated default-claim payments by the Government, net of income from recoveries on defaults, fees, or other income. Guarantee fees to date have been paid in the form of preferred stock subsequently converted to trust preferred stocks and a warrant to purchase common stock of the financial institution, whose value is modeled using the same methodology for other equity purchase programs, discussed above. Default-claim payments are based on estimated losses on the guaranteed assets. Key inputs into these estimates are forecasted gross domestic product, unemployment rates and home price depreciation, in a base scenario and a stress scenario.

Subsidy Cost

The recorded subsidy cost of a direct loan, equity investment or asset guarantee is based on a set of estimated future cash flows. Government actions that change these estimated future cash flows change subsidy costs and are recorded as a modification. The cost of a modification is recognized as a modification expense, included in subsidy cost, when the direct loan, equity investment, or asset guarantee is modified. During fiscal year 2009, modifications occurred within the Capital Purchase Program, Consumer and Business Lending Initiative, the AIG Investment Program, and the Automotive Industry Financing Program. See detailed discussion related to each program and related modifications below. Total net modification costs for the period ended September 30, 2009 approximated $412.1 million.

CAPITAL PURCHASE PROGRAM (CPP)

In October 2008, Treasury began implementation of the TARP with the Capital Purchase Program (CPP), designed to stabilize the financial system by assisting in building the capital base of certain viable U.S. financial institutions to increase the capacity of those institutions to lend to businesses and consumers and support the economy. Under this program, Treasury purchases senior perpetual preferred stock from qualifying U.S. controlled banks, savings associations, and certain bank and savings and loan holding companies (Qualified Financial Institution or QFI). The senior preferred stock has a stated dividend rate of 5.0 percent through year five, increasing to 9.0 percent in subsequent years. The dividends are cumulative for bank holding companies and subsidiaries of bank holding companies and non-cumulative for others and payable when and if declared by the institution's board of directors. Under the original terms of the senior preferred stock, the QFI may not redeem the shares within the first three years of the date of the investment, unless it has received the proceeds of one or more Qualified Equity Offerings (QEOs)[1] which results in aggregate gross proceeds to the QFI of not less than 25.0 percent of the issue price of the senior preferred shares. QFIs that are Sub-chapter S Corporations issued subordinated debt in order to maintain compliance with the Internal Revenue Code. The maturity of the subordinated debentures is 30 years and interest rates are 7.7 percent for the first 5 years and 13.8 percent for the remaining years.

In February 2009 and May 2009, the United States Congress passed the *American Recovery and Reinvestment Act of 2009* and the *Helping Families Save Their Homes Act of 2009*, respectively. These acts contained amendments to the EESA (EESA Amendments) which require the Secretary to allow QFIs to repay at any time, subject to regulatory approval, regardless of whether the 25.0 percent or greater QEO was accomplished. The ability of a QFI to repay the Treasury investment prior to year 3 or a 25.0 percent QEO was not considered in the original subsidy cost estimate. Therefore, a modification cost of $77.7 million was recorded as a result of these amendments.

In addition to the senior preferred shares, Treasury received warrants as required by section 113(d) of EESA from public QFIs to purchase a number of shares of common stock. The warrants have an aggregate market price equal to 15.0 percent of the total senior preferred share investment. The exercise price and market value used to determine the number of shares of common stock subject to the warrant was calculated based on the average of closing prices of the common stock on the 20 trading days ending on the last day prior to the date the QFIs application

1 A Qualified Equity Offering is defined as the sale by the QFI after the date of the senior preferred stock investment of Tier 1 perpetual preferred stock or common stock for cash.

was preliminarily approved for participation in the program. The warrants include customary anti-dilution provisions. In the event that a public QFI completes, prior to December 31, 2009, one or more QEOs with aggregate gross proceeds of not less than 100.0 percent (100.0 percent QEO) of the senior perpetual preferred stock investment, the number of shares subject to the warrants will be reduced by 50.0 percent. As of September 30, 2009, 19 QFIs reduced the number of shares available under the warrants as a result of this provision. The warrants have a 10 year term. The Treasury may exercise one half of the warrants prior to the earlier of a 100.0 percent QEO, or December 31, 2009. Subsequent to December 31, 2009, Treasury may exercise any warrants held in whole or in part. Treasury considers the impact of potential future QEOs in the valuation process.

The Treasury received warrants from non-public QFIs for the purchase of additional senior preferred stock (or subordinated debentures, if appropriate) with a stated dividend rate of 9.0 percent (13.8 percent interest rate for subordinate debentures) and a liquidation value equal to 5.0% of the total senior preferred share (additional subordinate debenture) investment. These warrants were immediately exercised and resulted in Treasury holding additional senior preferred stock (subordinated debentures) (collectively referred to as "warrant preferred stock") of non-public QFIs. The Treasury did not receive warrants from banks considered Community Development Financial Institutions (CDFIs). As of September 30, 2009, Treasury has invested in 20 institutions considered CDFIs. The EESA Amendments previously discussed also allows the Secretary to liquidate warrants associated with repurchased senior preferred stock at the market price. In addition, a QFI, upon the repurchase of its senior preferred stock, also has the contractual right to repurchase the common stock warrants at the market price.

In June 2009, Treasury entered into an exchange agreement with Citigroup. Under the terms of the agreement, Treasury exchanged $25,000 million of its investment in senior preferred stock for a new series (Series M) of mandatorily convertible preferred stock. The initial conversion price was $3.25 per share. In July 2009, Treasury received the Series M shares, which were subsequently converted in September 2009 to approximately 7,700 million common shares of Citigroup. This exchange transaction was not considered in the original subsidy cost estimate for CPP. As a result, Treasury recorded a modification cost of approximately $1,866 million for the fiscal year ended 2009. The Treasury also has investments in Citigroup through the Targeted Investment Program (TIP) and Asset Guarantee Program (AGP).

During the period ending September 30, 2009, Treasury has invested approximately $204,619 million in 685 institutions, including small, community, regional, and national banks, as well as CDFIs, in 48 states, the District of Columbia, and Puerto Rico. Approximately $70,718 million of Treasury investments have been repurchased or redeemed bringing the total gross investment balance as of September 30, 2009 to approximately $133,901 million. In addition, during the period ending September 30, 2009, Treasury received under CPP approximately $6,800 million in dividends on senior preferred and warrant preferred stock and approximately $2,900 million in proceeds from the repurchase of warrants and warrant preferred shares. Thirty-eight QFIs have not declared and paid one or more dividends to Treasury under CPP as of September 30, 2009.

Further details on the outstanding senior preferred stock investments and subordinated debentures under CPP and the net investment amount including estimated cash flows associated with the sale or exercise of the warrants, as of September 30, 2009, are presented in the table at the end of this section.

AMERICAN INTERNATIONAL GROUP, INC. (AIG)

Treasury provides assistance to certain systemically significant financial institutions on a case-by-case basis in order to provide stability to institutions that are critical to a functioning financial system and are at substantial risk of failure as well as to prevent broader disruption to financial markets.

In November 2008, Treasury invested $40,000 million in AIG's Cummulative Series D perpetual cumulative preferred stock with a dividend rate of 10.0 percent compounded quarterly. On April 17, 2009, AIG and Treasury restructured their November 2008 agreement. Under the restructuring, Treasury exchanged $40,000 million of cumulative Series D preferred stock for $41,603 million of non-cumulative 10.0 percent Series E preferred stock. The amount of Series E preferred stock is equal to the original $40,000 million, plus approximately $733.0 million in undeclared dividends as of the February 1, 2009 scheduled quarterly dividend payment date, $15.0 million in dividends compounded on the undeclared dividends, and an additional $855.0 million in dividends from February 1, 2009, but not paid as of April 17, 2009. AIG's restructured agreement kept the quarterly dividend payment dates of May 1, August 1, November 1, and February 1, as established by the original November 2008 agreement. The original subsidy cost estimate did not consider this restructuring which resulted in a modification cost of $127.2 million.

In addition to the exchange, Treasury agreed to make available an additional $29,800 million capital facility to allow AIG to draw additional funds if needed to assist in AIG's restructuring. Treasury investment consists of Series F non-cumulative perpetual preferred stock with an initial liquidation amount of $0.0. This liquidation amount increases with any drawdown by AIG on the facility. The dividend rate applicable to these stock is 10.0 percent and is payable quarterly, if declared, on the outstanding liquidation amount. As of September 30, 2009, approximately $3,200 million has been funded by Treasury to AIG under this additional capital facility. Consistent with SFFAS No. 2, the unused portion of the AIG capital facility is not recognized as an asset as of September 30, 2009.

As of September 30, 2009, AIG has not made any dividend payments on any of the perpetual preferred stock. Subsequently, AIG failed to make a dividend payment on November 2, 2009. Per the terms of the preferred stock, if AIG misses 4 dividend payments, Treasury may appoint to the AIG board of directors the greater of two members or 20.0 percent of the total number of directors of the Company.

TARGETED INVESTMENT PROGRAM (TIP)

The Targeted Investment Program (TIP) was designed to prevent a loss of confidence in financial institutions that could result in significant market disruptions, threatening the financial strength of similarly situated financial institutions, impairing broader financial markets, and undermining the overall economy. Treasury considers institutions as candidates for the TIP on a case-by-case basis, based on a number of factors described in the program guidelines. These factors include the threats posed by destabilization of the institution, the risks caused by a loss of confidence in the institution, and the institution's importance to the nation's economy.

Treasury completed the first transaction under the TIP in December 2008, when it invested $20,000 million in Citigroup cumulative perpetual preferred stock and received a warrant for the purchase of Citigroup common stock. Under the agreement with Citigroup, Treasury receives an 8.0 percent annual dividend, payable quarterly, if and when declared by Citigroups' Board of Directors. As part of this agreement, Citigroup must implement rigorous compensation standards and other restrictions on corporate expenditures. In June 2009, Treasury and

Citigroup agreed to an exchange of the cumulative perpetual preferred stock issued under the TIP for a new series of trust preferred securities. Citigroup issued subordinated debentures to a trust established by Citigroup, and the trust issued trust preferred securities to Treasury. Interest and principal payments on the subordinated debentures are passed-through to the trust preferred security holders. The trust preferred securities pay a quarterly distribution at an annual rate of 8.0 percent to Treasury. The subordinated debentures contains an interest deferral provision allowing Citigroup to defer payment of interest for up to 5 years. Treasury will not receive distributions from the trust preferred securities during a deferral period. Deferred interest is required to be paid upon termination of the deferral period. The subordinated debentures will mature in 2039. As a result, the trust is scheduled to pay out the proceeds to the holders of the trust preferred securities. In addition, the subordinate debentures can be prepaid by Citigroup at any time prior to maturity, subject to consultation with the Federal Reserve, as long as the U.S. Government holds the trust preferred securities. The terms of the new securities are substantially the same as the preferred share originally received by Treasury and therefore the exchange transaction did not result in a modification. Treasury has investments in Citigroup through the CPP and the Asset Guarantee Program (AGP).

In January 2009, Treasury completed its second transaction under the TIP, investing $20,000 million in Bank of America. Under the agreement with Bank of America, Treasury purchased $20,000 million of cumulative perpetual preferred stock and received a warrant for the purchase of Bank of America common stock. The preferred stock purchased from Bank of America contains a stated annual dividend rate of 8.0 percent, payable quarterly, if declared. Bank of America's agreement under the TIP stipulates that the institution must implement rigorous executive compensation standards and other restrictions on corporate expenditures. Treasury also has investments in Bank of America through the CPP. (See Note 33.)

During the period ending September 30, 2009, Treasury received approximately $1,900 million in dividends under the TIP.

AUTOMOTIVE INDUSTRY FINANCING PROGRAMS (AIFP)

The objective of the Automotive Industry Financing Program was to prevent a significant disruption of the American automotive industry, which could have a negative effect on the economy of the United States. The discussion below details the various investments made by the Treasury in the automotive industry.[2]

GMAC Preferred Stock

In December 2008, the Treasury purchased preferred membership interest for $5,000 million which were converted to senior preferred stock with an 8.0 percent annual distribution right (dividends) from GMAC. Under the agreement, GMAC issued warrants to Treasury to purchase, for a nominal price, additional preferred equity in an amount equal to 5.0 percent of the preferred equity purchased. These warrants were exercised at closing of the investment transaction. The additional preferred stock provided for a 9.0 percent annual distribution right. The purpose of this investment was to enable GMAC to restore liquidity to its finance businesses and restore stability to the domestic automobile industry in the United States. As of September 30, 2009, Treasury has received $265.2 million in dividends associated with these preferred and warrant preferred stock.

2 Included in the TARP Direct Loans net, are equity interests acquired during the restructuring of GM and Chrysler. These equity amounts are included with the original loans portfolio in Note 12.

GMAC Mandatorily Convertible Preferred Stock

In May 2009, the Treasury published a non-binding term sheet to invest $13,140 million to support GMAC, subject to definitive documentation and GMAC's capital needs. The Treasury has invested $7,500 million (of the $13,140 million) in 9.0 percent Mandatorily Convertible Preferred Stock in GMAC to support its ability to originate new loans to Chrysler dealers and consumers, and help address GMAC's capital needs. The preferred stock have a liquidation amount of $50 per share and are convertible, in whole or in part, at any time, at the option of GMAC, subject to the approval of the Federal Reserve. Furthermore, GMAC shall not convert any of the stock to the extent such conversion would result in the Treasury owning in excess of 49 percent of GMAC's common equity except (1) with the prior written consent of the Treasury, (2) pursuant to GMAC's Capital Plan, or (3) pursuant to an order of the Federal Reserve compelling such a conversion. The determination of the percentage of common equity owned by the Treasury would take into account the common stock currently owned by the Treasury as a result of the conversion of the GMAC Rights Offering, previously discussed. Absent a previous conversion, the preferred stock will automatically convert after 7 years. The conversion rate is .00432 units of common stock per unit of convertible preferred stock. The remaining $5,600 million (per the non-binding term sheet) is subject to FRB's review of GMAC's capital plan assessment of whether additional capital is needed. As of September 30, 2009, the remaining $5,600 million has not been funded. The Treasury has received approximately $165.4 million in dividends associated with these preferred and warrant preferred stock.

PUBLIC-PRIVATE INVESTMENT PARTNERSHIP (PPIP) EQUITY

The Public-Private Investment Program is part of Treasury's efforts to help restart the markets and provide liquidity for legacy assets. Under this program Treasury will make equity and debt investments in investment vehicles (referred to as Public Private Investment Funds or "PPIFs") established by private investment managers. The equity investment will be used to match private capital and will equal not more than 50.0 percent of the total equity invested. The debt investment will be, at the option of the investment manager, equal to 50.0 percent or 100.0 percent of the total equity (including private equity). The PPIFs are only allowed to purchase commercial mortgage-backed securities and non-agency residential mortgage-backed securities issued prior to January 1, 2009 that were originally rated AAA or an equivalent rating by two or more nationally recognized statistical rating organizations without external credit enhancement and that are secured directly by the actual mortgage loans, leases or other assets and not other securities. The PPIFs are also permitted to invest in certain temporary securities, including bank deposits, U.S. Treasury Securities, and certain money market mutual funds. At least 90 percent of the assets underlying any eligible asset must be situated in the United States. On September 30, 2009, Treasury signed definitive agreements with two investment managers, committing to potentially disburse up to $6,700 million. As of September 30, 2009, no private fund managers had made any investments and Treasury had not disbursed any funds.

ASSET GUARANTEE PROGRAM (AGP)

The AGP provides guarantees for assets held by systemically significant financial institutions that face a risk of losing market confidence due in large part to a portfolio of distressed or illiquid assets. The AGP is applied with extreme discretion in order to improve market confidence in the systemically significant institution and in financial markets broadly.

Section 102 of the EESA established the AGP to guarantee troubled assets originated or issued prior to March 14, 2008, including mortgage-backed securities, and established the Troubled Assets Insurance Financing Fund

(TAIFF). In accordance with Section 102(c) and (d) of the EESA, premiums from financial institutions, are collected and all fees are recorded by Treasury in the TAIFF. In addition, Section 102(c)(3) of the EESA requires that the original premiums assessed are "set" at a minimum level necessary to create reserves sufficient to meet anticipated claims. In the event there are insufficient funds within the TAIFF for the payment of claims, amounts are borrowed from the U.S. Treasury until sufficient funds are received into the TAIFF. In the event that the estimate of claims exceeds the estimated future cash inflows, an upward reestimate would be recorded and amounts would be transferred to the TAIFF as a subsidy expense.

Treasury completed its first transaction under the AGP in January 2009, when it finalized the terms of a guarantee agreement with Citigroup. Under the agreement, Treasury, the Federal Reserve Bank (FRB), the Federal Deposit Insurance Corporation (FDIC), and the Federal Reserve Bank of New York (FRBNY) provided protection against the possibility of large losses on an asset pool of approximately $301,000 million of loans and securities backed by residential and commercial real estate and other such assets, which remain on Citigroup's balance sheet. The following loss-sharing terms apply to the transaction: Citigroup absorbs the first $39,500 million in losses, and losses over the $39,500 million are shared by the U. S. government (90.0 percent) and Citigroup (10.0 percent) (the "second loss"). For the second loss, Treasury absorbs up to $5,000 million, then the FDIC absorbs up to $10,000 million, and lastly the FRBNY funds any U.S. government losses above Treasury and the FDIC commitments through a non-recourse loan. The guarantee is in place for ten years for residential assets and five years for non-residential assets.

As a premium for the guarantee, Citigroup issued $7,034 million of cumulative perpetual preferred stock with an 8.0 percent stated dividend rate and a warrant for the purchase of common stock; $4,034 million was issued to Treasury and approximately $3,000 million was issued to the FDIC. Treasury received the warrant. As part of the agreement, Citigroup submitted an executive compensation plan to Treasury and the FDIC for approval and must comply with certain common stock dividend restrictions. Treasury has received approximately $174.8 million in dividends on the preferred stock received as compensation for this arrangement. These dividends have been deposited into the TAIFF. The preferred stock originally issued to Treasury and the FDIC were exchanged for the trust preferred securities discussed above under the TIP. Treasury has also invested in Citigroup through the CPP and the TIP.

The net present value of the estimated cash inflows from the preferred stock and warrant received by Treasury from Citigroup as a premium is greater than the estimated net present value of future claim payments, resulting in an asset of approximately $1,765 million, after reestimates, as of September 30, 2009.

In January 2009, Treasury, FDIC, FRBNY (together the USG Parties), and Bank of America signed a Summary of Terms (Term Sheet) pursuant to which the USG Parties agreed to guarantee or lend against a pool of up to $118,000 million of financial instruments consisting of securities backed by residential and commercial real estate loans and corporate debt and related derivatives. In May 2009, prior to completing definitive documentation, Bank of America notified the USG Parties of its desire to terminate negotiations with respect to the guarantee contemplated in the Term Sheet. All parties agreed that Bank of America received value for entering into the Term Sheet with the USG Parties and that the USG Parties should be compensated for out-of-pocket expenses and a fee equal to the amount Bank of America would have paid for the guarantee from the date of the signing of the Term Sheet through the termination date. Under the terms of the settlement, the U.S. Treasury received $276.0 million for its role in the guarantee agreement through Treasury, the FRBNY received $57.0 million, and the FDIC received $92.0 million. All Treasury funds received for the settlement were deposited in the TAIFF and subsequently paid to the U.S. Treasury General Fund. The $276 million received by Treasury pursuant to the settlement is reflected in the Statement of Net Cost as a reduction of subsidy cost.

The tables below provide an analysis of the TARP equity investments including allowance for subsidy costs, modifications, reestimates, and administrative costs. The TARP programs were created in fiscal year 2009 and thus there are no fiscal year 2008 comparative balances to disclose.

Troubled Asset Relief Programs - Equity Investments, Net (in millions)

Programs	Equity Investments, Gross	Interest Receivable	Foreclosed Property	Allowance for Subsidy Cost and Loan Guarantee Liability—Present Value	2009 Value of Assets Related to Equity Investments
CPP	$ 133,901	$ 0	$ 0	$ 7,770	$ 141,671
AIG	43,206	0	0	(30,054)	13,152
TIP	40,000	0	0	341	40,341
AIFP	12,500	0	0	(4,523)	7,977
Total	**$ 229,607**	**$ 0**	**$ 0**	**$ (26,466)**	**$ 203,141**

Total Amount of Disbursements, Equity Investments (in millions):

Programs	2009
CPP	$ 204,618
AIG	43,206
TIP	40,000
AIFP	12,500
Total	**$ 300,324**

Subsidy Expense, Equity Investments (in millions):

Programs	Interest Differential	Defaults	Fees and Other Collections	Other	2009 Total
CPP	$ 12,279	$ 52,655	$ $0	$ (9,414)	$ 55,520
AIG	(17,280)	46,906	0	1,799	31,425
TIP	3,724	19,352	0	(3,536)	19,540
AIFP	5,319	3,694	0	(2,196)	6,817
Total	**$ $4,042**	**$ 122,607**	**$ 0**	**$ (13,347)**	**$ 113,302**

Modifications and Reestimates, Equity Investments (in millions):

Programs	Total Modifications	Interest Rate Reestimates	Technical Reestimates	Total Reestimates
CPP	$ 1,866	$ 0	$ (72,419)	$ (72,419)
AIG	127	0	(1,125)	(1,125)
TIP	0	0	(21,467)	(21,467)
AIFP	0	0	(2,710)	(2,710)
Total	**$ 1,993**	**$ 0**	**$ (97,721)**	**$ (97,721)**

Total Subsidy Expense, Equity Investments, (in millions):

Programs	2009
CPP	$ (15,033)
AIG	30,427
TIP	(1,927)
AIFP	4,107
Total	**$ 17,574**

Subsidy Rates by Program and Component, Equity Investments:*

Programs	Interest Differential	Defaults	Fees and Other Collections	Other	2009 Total
CPP	5.97%	25.60%	0.00%	-4.58%	26.99%
AIG	-45.52%	123.56%	0.00%	4.74%	82.78%
TIP	9.31%	48.38%	0.00%	-8.84%	48.85%
AIFP	42.55%	29.55%	0.00%	-17.57%	54.53%

(*) The rates reflected in the "Subsidy Rate" table above are weighted rates for the program. To compensate for the weighting of the various risk category subsidy rates, the "by component" dollar amounts reflected were computed as a ratio of the component rate to the total weighted subsidy rate multiplied by the subsidy expense for the program.

Schedule for Reconciling Subsidy Cost Allowance Balances (in millions):

Fiscal Year 2009	CPP	AIG	TIP	AIFP	Totals
Beginning Balance of the subsidy cost allowance	$ 0	$ 0	$ 0	$ 0	$ 0
Add: subsidy expense for disbursements					
(a) Interest rate differential cost	12,279	(17,280)	3,724	5,319	4,042
(b) Default costs (net of recoveries)	52,655	46,906	19,352	3,694	122,607
(c) Fees and other collections	0	0	0	0	0
(d) Other subsidy costs	(9,414)	1,799	(3,536)	(2,196)	(13,347)
Total of the above subsidy expense components	$ 55,520	$ 31,425	$ 19,540	$ 6,817	$ 113,302
Adjustments:					
(a) Loan modifications	1,866	127	0	0	1,993
(b) Fees received	9,691	0	1,862	431	11,984
(c) Foreclosed property acquired	0	0	0	0	0
(d) Loans written off	0	0	0	0	0
(e) Subsidy allowance amortized	(2,428)	(373)	(276)	(15)	(3,092)
(f) Other	0	0	0	0	0
	0				
Ending Balance subsidy cost allowance before reestimates	$ 64,649	$ 31,179	$ 21,126	$ 7,233	$ 124,187
Add or subtract subsidy reestimates by component:					
(a) Interest rate reestimate	0	0	0	0	0
(b) Technical default reestimate	(72,419)	(1,125)	(21,467)	(2,710)	(97,721)
Total of the above reestimate components	(72,419)	(1,125)	(21,467)	(2,710)	(97,721)
Ending Balance of the subsidy cost allowance	**$ (7,770)**	**$ 30,054**	**$ (341)**	**$ 4,523**	**$ 26,466**

Administrative Expense of TARP programs (in millions):

Programs	2009
Troubled Asset Relief Programs	$ 167
Total	$ 167

Troubled Asset Relief Programs – Asset Guarantee Program (AGP)

As of September 30, 2009, Asset Guarantees consisted of the following (in millions):

Asset Guarantees Outstanding (in millions):

Programs	Outstanding Principal of Guaranteed Assets	2009 Amount of Outstanding Principal Guaranteed
AGP	$301,000	$5,000

Asset for Asset Guarantee (in millions):

Programs	2009 Asset for Asset Guarantee Present Value
AGP	*$1,765

(*)The net present value of the preferred stock received by Treasury from the TAIFF as a premium ($4,034 million) is greater than the liability ($2,269), resulting in a net asset of $1,765 million included as a line item on the face of the balance sheet, after reestimates, as of September 30, 2009.

Subsidy Expense, Guarantee (in millions):

Programs	Interest Differential	Defaults	Fees and Other Collections	Other	2009 Total
AGP	$ 0	$ 2,181	$ (2,662)	$ (270)	$ (751)

Modifications and Reestimates (in millions):

Programs	Total Modifications	Interest Rate Reestimates	Technical Reestimates	2009 Total Reestimates
AGP	$ 0	$ 0	$ (1,174)	$ (1,174)

Total Guarantee Subsidy Expense (in millions):

Programs	2009
AGP	$(1,925)

Subsidy Rates for Guarantee by Program and Component:

Programs	Interest Differential	Defaults	Fees and Other Collections	Other	2009 Total
AGP	0.00%	43.62%	-53.23%	-5.37%	-14.98%

Schedule for Reconciling Asset Guatrantee Program Balances (in millions)

BEGINNING BALANCES, CHANGES, AND ENDING BALANCE	2009
Beginning Balance of the Asset Guarantee liability	$ 0
Add: subsidy expense for disbursements	
(a) Interest rate supplement costs	0
(b) Default costs (net of recoveries)	2,181
(c)Fees and other collections	(2,662)
(d) Other subsidy costs	(270)
Total of the above subsidy expense components	(751)
Adjustments:	
(a) Loan guarantee modifications	0
(b) Fees received	175
(c) Interest supplements paid	(15)
(d) Foreclosed property acquired	0
(e) Claim payments to lenders	0
(f) Interest accumulation on the liability balance	0
(g) Other	0
Ending Balance of loan guarantee liability before reestimates	(591)
Add or subtract subsidy reestimates by component:	
(a) Interest rate reestimate	0
(b) Technical default reestimate	(1,174)
Total of the above reestimate components	(1,174)
Ending Balance of Asset for Asset Guarantee	$ (1,765)

9. INVESTMENTS IN GOVERNMENT SPONSORED ENTERPRISES

The *Housing and Economic Recovery Act* (HERA), P.L. 110–289, dated July 30, 2008, authorized Treasury to enter into several different types of financing arrangements with Government Sponsored Enterprises (GSEs) to:

- provide stability to the financial markets;
- prevent disruptions in the availability of mortgage finance; and
- protect the taxpayer

As authorized by HERA, the Secretary of the Treasury entered into a Senior Preferred Stock Purchase Agreements (SPSPA) with Fannie Mae and Freddie Mac on September 7, 2008 and began providing substantial financial support to the enterprises; thereby minimizing potential systemic financial risks associated with the deteriorating financial condition of Fannie Mae and Freddie Mac. Per SFFAC No. 2, *Entity and Display*, these entities meet the criteria of "bailed out" entities under paragraph 50. Accordingly, Treasury has not consolidated them into the financial statements, but include "disclosure of the relationship(s) with the bailed out entities and any actual or potential material costs or liabilities" in the consolidated financial statements.

Under the SPSPA, 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-transferrable 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. The senior preferred stock accrues dividends at 10 percent per year, payable quarterly. This rate will increase to 12 percent if, in any quarter, the dividends are not paid in cash, until all accrued dividends have been paid. As of September 30, 2009, dividends of $4,336 million have been received. In addition, beginning on March 31, 2010, the GSEs will pay Treasury a periodic commitment fee on a quarterly basis. This fee will be initially set by December 31, 2009, based on mutual agreement between Treasury and each GSE, in consultation with the Chairman of the Federal Reserve Board. The fee will be established for five-year periods, and may be waived by Treasury for one year at a time if warranted by adverse mortgage market conditions. It may be paid in cash or may be added to the liquidation preference.

These agreements, which have no expiration date, provide that Treasury will increase its investment in the senior preferred stock if at the end of any quarter the Federal Housing Finance Agency (FHFA) determines that the liabilities of either GSE exceed its assets. The maximum amount available to each GSE under this agreement is $200,000 million. Actual payments to the GSEs to date are $95,600 million, of which $15,000 million has been accrued as a liability for the quarter ended September 30, 2009 ($13,800 million at September 30, 2008). As of September 30, 2009, $140,100 million and $149,300 million remain available to Fannie Mae and Freddie Mac, respectively, after quarterly payments made or accrued.

The Treasury Department determined the estimated amount of the remaining liability to the GSEs under the SPSPA as of September 30, 2009. The valuation analysis resulted in estimates ranging from the "best case" scenario of $76,937 million to an "extreme case" scenario of $206,700 million. The results also noted that no value within the range is a better estimate than any other amount. However, future payments under the SPSPA are deemed to be probable. SFFAS 5 provides that when a probable contingent liability is a range of amounts and no amount within the range is a better estimate than any other amount, the estimated liability should be based on the minimum value in the range. Accordingly, $76,937 million is recorded as a contingent liability as of September 30, 2009.

As described below, the SPSPA payments are treated as entity expenses and liabilities, while the increases in liquidity preference of the GSE preferred stock resulting from actual liquidity payments are non-entity transactions. Accordingly, the contingent liability recorded is the gross estimated amount, without considering the increase in preferred stock liquidity preference, future dividend payments, or future commitment fees.

As funds for these payments are appropriated directly to the Treasury Department, these payments are treated as entity expenses and reflected as such on the Statement of Net Cost (SNC) and Cumulative Results of Operations. In fiscal year 2008, these costs were reported on the SNC, as a below the line entity cost, separate from the four Treasury strategic goals. In fiscal year 2009, Treasury concluded that the cost of this program helps accomplish the Treasury strategic goal of ensuring that the U.S. economy performs at its full economic potential. Thus, as of September 30, 2009, the entity cost of these Investments in GSEs are included in the Economic Program section of the SNC. These payments also results in an increase to the non-entity investment in GSE preferred stock, with a corresponding increase in Due to the General Fund, as the Treasury Department holds the investment on behalf of the U.S. Government General Fund. Such investments are subject to impairment testing as noted below.

The Investments in GSEs disclosed as of September 30, 2008 were recorded at acquisition cost at the date of purchase with disclosure of market values as of fiscal year end 2008. OMB issued guidance to Treasury on October 7, 2009 allowing the use of fair value accounting for non-federal securities beginning with reporting for fiscal year 2009. As a result, the GSE investments are reported at fair value at September 30, 2009. The preferred stock and warrants for common stock were valued as of September 30, 2009. In accordance with SFFAS 7, the annual valuation is classified as usual and recurring and thus recorded as an expense or revenue to the financial statements. In addition, since Treasury holds the investment on behalf of the U.S. Government General Fund, any valuation impairment is recorded as a non-entity cost/revenue and reported on the SNC below the line. As of September 30, 2009 and September 30, 2008, GSE investments consisted of the following (in millions):

GSE Investment	Value at Begin of Year	Current Year Investments	Net Investments	Valuation Gain/(Loss)	9/30/09 Fair Value at Reporting Date
Fannie Mae Sr. Preferred Stock	$ 840	$ 44,900	$ 45,740	$ (20,658)	$ 25,082
Freddie Mac Sr. Preferred Stock	824	50,700	51,524	(23,273)	28,251
Fannie Mae Warrants Common Stock	3,104	0	3,104	3,603	6,707
Freddie Mac Warrants Common Stock	2,264	0	2,264	2,375	4,639
Total GSE Investment	**$ 7,032**	**$ 95,600**	**$ 102,632**	**$ (37,953)**	**$ 64,679**

GSE Investment	Cost at Purchase Date	9/30/08 Investment Balance	Valuation Gain/(Loss)	9/30/08 Fair Value at Reporting Date
Fannie Mae Sr. Preferred Stock	$ 840	$ 840	$ (99)	$ 741
Freddie Mac Sr. Preferred Stock	824	824	(97)	727
Fannie Mae Warrants Common Stock	3,104	3,104	3,403	6,507
Freddie Mac Warrants Common Stock	2,264	2,264	2,135	4,399
Total GSE Investment	**$ 7,032**	**$ 7,032**	**$ 5,342**	**$ 12,374**

Summary of GSE Non-Entity Costs

	2009	2008
General Fund Revenue from Increase in Liquidity Preference of GSE Preferred Stock	$ (95,600)	$ –
Net Valuation Loss on GSE Warrants/Pfd Stock	37,953	–
GSE Pfd Stock Dividends	(4,336)	–
Pfd Stock Commitment Fee	–	$ (7,032)
	$ (61,983)	**$ (7,032)**

10. INVESTMENTS IN INTERNATIONAL FINANCIAL INSTITUTIONS

The Treasury Department participates in Multilateral Development Banks (MDB) to support poverty reduction, private sector development, and transition to market economies and sustainable economic growth and development, thereby advancing the United States' economic, political, and commercial interests abroad. The MDB consist of the World Bank Group (International Bank for Reconstruction and Development, International Finance Corporation, and Multilateral Investment Guarantee Agency), and five regional development banks (the African, Asian, European, Inter-American, and North American institutions), as enumerated in the table below. These investments are non-marketable equity investments valued at cost.

As of September 30, 2009 and September 30, 2008, investments in international financial institutions consisted of the following (in millions):

	2009	2008
African Development Bank	$ 175	$ 172
Asian Development Bank	458	458
European Bank for Reconstruction and Development	636	633
Inter-American Development Bank	1,482	1,482
International Bank for Reconstruction and Development	1,985	1,985
International Finance Corporation	569	569
Multilateral Investment Guarantee Agency	45	45
North American Development Bank	225	202
Total	**$ 5,575**	**$ 5,546**

Refer to Note 31 for a description of the additional commitments related to these institutions.

11. OTHER INVESTMENTS AND RELATED INTEREST

Investments in U.S. Government securities held by Treasury Department entities have been eliminated against the federal debt liability for financial reporting purposes (See Note 4). The ESF holds most of the Treasury Department's Other Investments, including Foreign Investments. Foreign investment holdings are normally invested in interest bearing securities issued or held through foreign governments or monetary authorities (see Note 6). During fiscal year 2009, ESF transferred other FCDA and Investment Securities to the available-for-sale classification, and reported at fair value. The Other Investments represent securities that the Treasury Department has both the positive intent and ability to hold to maturity and are carried at historical cost, adjusted for amortization of premiums and accretion of discounts.

As of September 30, 2009 and September 30, 2008, entity investments in foreign investment holdings and other investments consisted of the following (in millions):

Type of Investment	Cost/ Acquisition Value	Unamortized (Premium)/ Discount	Interest Receivable	9/30/09 Investment Balance	Unrealized Gain/ (Loss)	9/30/09 Fair Value
Foreign Investments:						
Euro Bonds & Notes	$ 4,827	$ 52	$ 116	$ 4,995	$ 184	$ 5,179
Japanese Government Bonds	7,192	9	12	7,213	43	7,256
Other Investments	1,137	(7)	0	1,130	0	1,130
Total Non-Federal	**$ 13,156**	**$ 54**	**$ 128**	**$ 13,338**	**$ 227**	**$ 13,565**

Type of Investment	Cost/ Acquisition Value	Unamortized (Premium)/ Discount	Net Investment	Interest Receivable	9/30/08 Investment Balance	Unrealized Gain/ (Loss)	9/30/08 Market Value
Foreign Investments:							
Euro Bonds & Notes	$ 4,477	$ 29	$ 4,506	$ 115	$ 4,621	$ 20	$ 4,641
Japanese Government Bonds	5,908	3	5,911	11	5,922	13	5,935
Other Investments	39	(6)	33	0	33	0	33
Total Non-Federal	**$ 10,424**	**$ 26**	**$ 10,450**	**$ 126**	**$ 10,576**	**$ 33**	**$ 10,609**

12. CREDIT PROGRAM RECEIVABLES, DIRECT LOANS

The table below summarizes, by program, Treasury's credit program assets net of subsidy allowance. As of September 30, 2009 and September 30, 2008, Credit Program Receivables and Direct Loans consisted of the following (in millions):

	2009	2008
GSE MBS Purchase Program Receivables	$ 184,419	$ 3,385
Troubled Asset Relief Program Direct Loans	34,751	0
Total Credit Program Receivables and Direct Loans	**$ 219,170**	**$ 3,385**

CREDIT PROGRAM RECEIVABLES, GSE MBS PURCHASE PROGRAM AND GSE CREDIT FACILITY:

The *Housing and Economic Recovery Act* (HERA), P.L. 110–289, dated July 30, 2008, authorized Treasury to enter into several different types of financing arrangements with Government Sponsored Enterprises (GSEs) to provide stability to the financial markets; prevent disruptions in the availability of mortgage finance; and protect the taxpayer. Two of these arrangements include the GSE Mortgage-Backed Securities (MBS) Purchase Program and GSE Credit Facility (GSECF).

The GSE Mortgage-Backed Securities Purchase Program is a program to further support the availability of mortgage financing for millions of Americans and to mitigate pressures on mortgage rates. Under this program, Treasury, via Asset Managers, purchases GSE MBS in the open market. By purchasing these credit-guaranteed securities, Treasury seeks to broaden access to mortgage funding for current and prospective homeowners and to promote stability in the mortgage market. The Asset Managers are also authorized to enter into other trade/sell transactions such as Pair Offs, Turns, Assignments, and Dollar Rolls to further support the market under the HERA provisions/mandate. While the size and timing of the MBS purchases is subject to the discretion of the Secretary, the authority granted by Congress to purchase MBS expires on December 31, 2009. The scale of the program has been based on developments in the capital and housing market but will moderate once the program expires.

Treasury purchases mortgage-backed pass-through securities through the Government Sponsored Enterprise Mortgage-Backed Securities (GSE MBS) Purchase Program. Consistent with the Federal Credit Reform Act, these securities are treated as direct loans, and the value of Treasury's position and the associated credit subsidy requirements are determined based on the net present value of the securities' forecasted future cash flows. Treasury estimates nominal future cash flows using a financial model that incorporates each security's payment characteristics together with assumptions about the future prepayment, default, and loss severity performance of underlying loan collateral and the GSEs' ability to uphold their guarantee. Nominal cash flow forecasts are discounted at interest rates of Treasury securities with comparable maturities using the Office of Management and Budget's Credit Subsidy Calculator. Cash flows are estimated under the assumption that all securities will be held to maturity.

Security-level data used as the basis for cash flow model forecasts are obtained directly from Treasury's program custodian. Assumptions about security and program performance are drawn from widely available market sources as well as information published by the GSEs. Key inputs to the cash flow forecast include:

- Security characteristics such as unpaid principal balance, pass-through coupon rate, weighted-average loan age, and weighted-average maturity

- Forecast prepayment rates and default rates

The GSE Credit Facility was established to ensure credit availability to the GSEs and the Federal Home Loan Banks. This lending facility will provide secured funding on an as needed basis under terms and conditions established by the Secretary to protect taxpayers. Fannie Mae, Freddie Mac, and the Federal Home Loan Banks are eligible to borrow under this program. The GSECF provides liquidity, if needed, until December 31, 2009. There were no loans made through the GSECF in fiscal year 2009 or 2008, and therefore the GSECF program is not disclosed in tables below.

Treasury's GSE Mortgage Backed Security (MBS) Purchase Program portfolio consists of mortgage pass-through securities issued by Freddie Mac and Fannie Mae. At the end of fiscal year 2009, Treasury held $173.3 billion in outstanding MBS principal and estimated the net present value of future cash flows on these holdings to be $184.4 billion. The difference between the outstanding MBS principal balance and the value of the MBS to Treasury is the negative subsidy allowance- Treasury expects the portfolio to generate the spread income between coupon rates on the MBS and Treasury's discount rate which exceeds its estimate of potential credit losses on the securities.

The tables below provide an analysis of the GSE MBS Credit Program Receivables including allowance for subsidy costs, modifications, reestimates, and administrative costs. As of September 30, 2009 and September 30, 2008, the Direct Mortgage-Backed Securities (MBS) Purchases Outstanding consisted of the following (in millions):

Programs	Credit Program Receivable, Gross	Interest Receivable	Foreclosed Property	Allowance for Subsidy Cost (Present Value)	2009 Value of Assets Related to Credit Program Receivable
MBS	$ 173,326	$ 0	$ 0	$ 11,093	$ 184,419

Programs	Credit Program Receivable, Gross	Interest Receivable	Foreclosed Property	Allowance for Subsidy Cost (Present Value)	2008 Value of Assets Related to Credit Program Receivable
MBS	$ 3,311	$ 0	$ 0	$ 74	$ 3,385

*Total amount of MBS Purchase Program, Disbursed (in millions):**

Programs	2009	2008
MBS	$ 192,263	$ 3,311

(*) Total fiscal year 2009 disbursements for MBS purchases was $192,263 million. These disbursements include fiscal year 2009 settled MBS purchases of $190,651 million and $1,612 million of fiscal year 2008 pre funded settled purchases. Negative subsidy for the fiscal year 2009 purchases has been calculated based on the negative subsidy rate of 2.36%. In 2008, $5,000 million was initially prefunded for the MBS purchase program. During fiscal year 2008 , $3,300 million of MBS purchases were made and negative subsidy was calculated on the settled amounts only. The negative subsidy amount calculated on 2008 purchase was based on a negative subsidy factor of 1.62%. In fiscal year 2009, the remaining $1,612 million of the initial $5,000 million prefunding were settled. The associated negative subsidy of $26 million related to these settled purchases was not reported on the fiscal year 2008 financial statements and has been captured in the 2009 negative subsidy reestimate.

Subsidy Expense (in millions):

Programs	*Interest Differential	*Defaults	Fees and Other Collections	Other	2009 Total
MBS	$ (4,977)	$ 477	$ 0	$ 0	$ (4,500)

Programs	Interest Differential	Defaults	Fees and Other Collections	Other	2008 Total
MBS	$ (62)	$ 8	$ 0	$ 0	$ (54)

*The change in defaults and interest differential between fiscal year 2009 and fiscal year 2008 is driven by the an increase in the mortgage rate default assumptions and fluctuation in pricing/interest rate curves, respectively, between years.

Modifications and Reestimates (in millions):

Programs	Total Modifications	Interest Rate Reestimates	Technical Reestimates	2009 Total Reestimates
MBS	$ 0	$ 0	$ (8,392)	$ (8,392)

Programs	Total Modifications	Interest Rate Reestimates	Technical Reestimates	2008 Total Reestimates
MBS	$ 0	$ 0	$ 0	$ 0

Total MBS Purchases Subsidy Expense (in millions):

Programs	2009	2008
MBS	$ (12,892)	$ (54)

Subsidy Rates for MBS Purchases:

Programs	Interest Differential	Defaults	Fees and Other Collections	Other	2009 Total
MBS, Cohort 2009	-2.61%	0.25%	0.00%	0.00%	-2.36%

Programs	Interest Differential	Defaults	Fees and Other Collections	Other	2008 Total
MBS, Cohort 2008	-1.86%	0.24%	0.00%	0.00%	-1.62%

Schedule for Reconciling Subsidy Cost Allowance Balances (in millions):

	2009	2008
Beginning Balance of the subsidy cost allowance	$ (74)	$ 0
Add: subsidy expense for disbursements		
(a) Interest rate differential cost	(4,977)	(62)
(b) Default costs (net of recoveries)	477	8
(c)Fees and other collections	0	0
(d) Other subsidy costs	0	0
Total of the above subsidy expense components	(4,500)	(54)
Adjustments:		
(a) Loan modifications	0	0
(b) Fees received	0	0
(c) Foreclosed property acquired	0	0
(d) Loans written off	0	0
(e) Subsidy allowance amortized	1,873	(20)
Ending Balance subsidy cost allowance before reestimates	$ (2,701)	(74)
Add or subtract subsidy reestimates by component:		
(a) Interest rate reestimate	0	0
(b) Technical default reestimate	(8,392)	0
Total of the above reestimate components	(8,392)	0
Ending Balance of the subsidy cost allowance	$ (11,093)	$ (74)

Administrative Expense of GSE Program Receivables – MBS (in millions):

Programs	2009	2008
GSE Related Credit Program Receivables-MBS	$ 12	$ 0

TROUBLED ASSET RELIEF PROGRAM DIRECT LOANS

FCRA and associated FASAB accounting standard SFFAS No. 2, as amended, governs direct loans made after fiscal year 1991. FCRA loans are valued at the present value of expected future cash flows, discounted at the interest rate of marketable Treasury securities. The subsidy allowance account represents the difference between the outstanding loan receivables balance and the net present value of the estimated cash flows of the loans over their remaining term. The subsidy allowance is subtracted from the outstanding loans receivable balance to obtain the net loans receivable balance.

Under the provisions of the EESA, Treasury implemented the TARP which resulted in the development of several direct loan programs and transactions including: the Automotive Industry Financing Program; the Consumer and Business Lending Initiative; and the Public-Private Investment Partnership.

Treasury applies the provisions of SFFAS No. 2 to account for direct loans. This standard requires measurement of the asset or liability at the present value of the estimated future cash flows. The cash flow estimates for each direct loan transaction reflect the actual structure of the instruments. Analytical cash flow models generate estimated cash flows to and from the Government over the life of a facility. Further, each cash-flow model reflects the specific terms and conditions of the program, technical assumptions regarding the underlying assets, risk of default or other losses, and other factors as appropriate. The models also incorporate an adjustment for market risk to reflect the additional return required by the market to compensate for variability around the expected losses reflected in the cash flows (the "unexpected loss"). The basic methods for these models are outlined below.

Direct Loans

The estimated future cash flows for direct loans are derived using analytical models that estimate the cash flows to and from Treasury over the life of the loan. These cash flows include the scheduled principal, interest, and other payments to Treasury, including estimated proceeds from equity interest obtained or additional notes. These models also include estimates of default and recoveries, incorporating the value of any collateral provided by the contract. The probability and timing of default and losses related to a default are estimated by using applicable historical data when available, or publicly available proxy data, including credit rating agency historical performance data.

In the case of the Term Asset-Backed Securities Loan Facility (TALF), Treasury uses an analytical model to project cash flows to and from Treasury-based on the estimated loan collateral performance, the estimated mix of collateral funded through the TALF, and the terms of the contracts.

The models include an adjustment for market risk which is intended to capture the risk of unexpected losses, but are not intended to represent fair value, i.e. the proceeds that would be expected to be received if the loans were sold to a market participant.

AUTOMOTIVE INDUSTRY FINANCING PROGRAMS (AIFP)

The objective of the Automotive Industry Financing Program was to prevent a significant disruption of the American automotive industry, which would pose a systemic risk to financial market stability and have a negative effect on the economy of the United States. The discussion below details the various loans made by the Treasury to the automotive industry.[3]

General Motors (GM or old GM) General Purpose Loan including Working Capital Advances

The Treasury provided GM with a total of $13,400 million in a three-year direct loan bearing interest at 3 Month LIBOR (subject to a 2.0 percent floor), plus 3.0 percent and secured by various types of collateral. Approximately $4,000 million of this loan was funded in December 2008, an additional $5,400 million in January 2009, and an additional $4,000 million in February 2009. In April 2009, the Treasury and GM amended this loan agreement to increase the maximum loan amount from $13,400 million to $15,400 million, and on May 20, 2009 to increase the maximum loan amount from $15,400 million to $19,400 million (these amendments are referred to as the Working Capital Advances) to provide GM with adequate working capital to assist in the restructuring effort. The additional amounts were funded upon amendment, bringing the total funded under this loan to $19,400 million. The agreement required GM to develop and implement a restructuring plan to achieve long-term financial viability and required compliance with certain enhanced executive compensation and expense control requirements.

3 Included in the TARP Direct Loans net, are equity interests acquired during the restructuring of GM and Chrysler. These equity amounts are included with the original loans portfolio in this note.

Furthermore, the Treasury received warrants for shares of GM common stock and an additional senior unsecured note in the principal amount of $748.6 million. The purpose of this loan was to enhance the ability of GM and its subsidiaries to pursue timely and aggressive production of energy-efficient advanced technology vehicles; preserve and promote the jobs of American workers employed directly by GM and its subsidiaries; safeguard the ability of GM and its subsidiaries to provide retirement and health care benefits for retirees and their dependents; and stimulate manufacturing and sales of automobiles produced by GM. On June 1, 2009, GM filed for Chapter 11 bankruptcy. All rights under this loan were transferred to a newly created entity (GM NewCo) and subsequently extinguished in connection with a successful credit bid for the assets of old GM. In addition, Treasury received $134.4 million in interest while the loan was outstanding. See further discussion below under GM Debtor-In-Possession.

Chrysler Holding LLC General Purpose

The Treasury provided a three-year, $4,000 million loan to Chrysler in January 2009, bearing interest at 3 Month LIBOR (subject to a 2.0 percent floor) plus 3.0 percent. The loan was secured by various collateral including parts inventory, real estate, and certain equity interests held by Chrysler. This agreement required Chrysler to submit a restructuring plan to achieve long-term viability and required compliance with certain enhanced executive compensation and expense-control requirements. Furthermore, the Treasury received a senior unsecured note from Chrysler in the principal amount of approximately $266.8 million, containing the same terms as the General Purpose loan. The purpose of this loan was to: enhance the ability of Chrysler and its subsidiaries to pursue timely and aggressive production of energy-efficient advanced technology vehicles; preserve and promote the jobs of American workers employed directly by Chrysler and its subsidiaries; safeguard the ability of Chrysler and its subsidiaries to provide retirement and health care benefits for retirees and their dependents; and stimulate manufacturing and sales of automobiles produced by Chrysler.

On April 30, 2009, Chrysler filed for Chapter 11 bankruptcy. Upon entering bankruptcy, a portion of Chrysler was sold to a newly created entity (New Chrysler). Under the terms of the bankruptcy agreement, $500.0 million of this loan was assumed by New Chrysler (see discussion under Chrysler Exit for discussion of note terms). The balance remains outstanding and is in default. Any recovery of the remainder of this loan will depend on: (a) Chrysler Holding's obligation to pay the greater of $1,375 million or 40.0 percent of the equity value of Chrysler Financial to Treasury should Chrysler Holding receive certain distributions from Chrysler Financial and (b) proceeds received from the sale of assets remaining in the bankrupt company. In addition, Treasury received $52.1 million in interest payments on this note.

Chrysler Financial

In January 2009, the Treasury loaned $1,500 million to Chrysler LB Receivables Trust (Chrysler Trust), a special purpose entity created by Chrysler Financial, to finance the extension of new consumer auto loans. The five-year loan bore interest at 1 Month LIBOR plus 1.0 percent for the first year, 1.5 percent for the remaining term and was secured by a senior secured interest in a pool of newly originated consumer automotive loans, and Chrysler served as a guarantor for certain covenants of Chrysler Financial. Under the agreement, Chrysler Financial was required to comply with the executive compensation and corporate governance requirements of Section 111(b) of the EESA, as well as enhanced restrictions on executive compensation including the need to reduce by 40.0 percent its bonus pool for Senior Executive Officers and Senior Employees. In lieu of warrants, the Treasury received additional notes in an amount equal to five percent of the maximum loan amount. The additional notes would vest 20.0 percent on the closing date and 20.0 percent on each anniversary of the closing date and had other terms similar to the loan. The purpose of this loan was to assist Chrysler Financial in providing retail financing to purchasers of automobiles, light duty trucks and recreational vehicles; to stimulate manufacturing and sales of automobiles produced by Chrysler's affiliates; preserve and promote the jobs of American workers employed directly by Chrysler's affiliates and in related industries; and safeguard the ability of Chrysler to provide retirement and health care benefits for their retirees and their dependents. On July 14, 2009, the loan and additional note of $15.0 million were paid in full. In addition, Treasury received $7.4 million in interest payments while this loan was outstanding.

Auto Supplier Support Program

In April 2009, the Treasury committed $5,000 million in financing for the Auto Supplier Support Program, as follows: $3,500 million for GM suppliers and $1,500 million for Chrysler suppliers. These commitments were subsequently reduced to $2,500 million for GM and $1,000 million for Chrysler per the loan agreement. Under the program, suppliers are able to sell their receivable to a special purpose vehicle, created by the respective automaker, at a discount. The purchases of the receivables are funded by equity investments made by the automaker, cash payments made by the automaker on previously purchased receivables or from draws on the Treasury funding commitment. The duration of the program is 12 months, extendable at the option of the Treasury. Interest is charged on advances under the facility at a rate of 3 Month LIBOR (subject to a 2.0 percent floor) plus 3.5 percent. In addition, the Treasury received a contingent payment note comprised of an exit fee equal to 4.0 percent of the adjusted commitment amount and 50.0% of the residual equity in the special purpose vehicle after the program's end date. This program provides suppliers with access to government backed protection ensuring that money owed to them for the products they ship will be paid regardless of what happens to the recipient car company. This provided suppliers with needed funding to operate their businesses and help unlock credit more broadly in the supplier industry. Purchases of receivables and collection of amounts due from GM and Chrysler is performed by a third party service provider. Suppliers must maintain qualifying commercial terms with the automakers to participate in the program. The Treasury has provided approximately $413.1 million, collectively, of funding to this program. The bankruptcy of Chrysler and GM did not impact this program, as both companies were allowed to continue paying suppliers while in bankruptcy. As of September 30, 2009, Treasury had received $5.9 million in interest under the Auto Supplier Support Program.

Auto Warranty Program

In April 2009 and May 2009, the Treasury loaned approximately $280.0 million to Chrysler and $360.6 million to GM, respectively, to capitalize certain SPVs created by Chrysler and GM to finance participation in the Warranty Commitment Program (warranty program). The Treasury also received additional notes as consideration for its loans in an amount equal to 6.67 percent of the funded amounts. The warranty program covered all warranties on new vehicles purchased from Chrysler and GM during the period in which Chrysler and GM were restructuring. The program was run by a third party program administrator with the backing of financial resources allocated by the Treasury, Chrysler and GM. Chrysler and GM contributed 15.0 percent of the projected cost for warranty service on each covered vehicle, with the Treasury providing additional funds to cover 110.0 percent of the projected cost. The SPVs holding the funds operated separately from Chrysler and GM and would transfer the necessary funds to a third-party to handle all warranty claims even if Chrysler and GM entered into bankruptcy or went out of business. Both Chrysler and GM have completed the Section 363[4] sales in June 2009 and July 2009, respectively. Upon completion of the sale, the Treasury received principal amounts due from both GM and Chrysler and terminated the warranty program. Interest in the amount of $3.1 million was received by Treasury from Chrysler. No interest was received in connection with the GM repayment. The GM additional note was assigned to the New GM as part of the bankruptcy proceedings and extinguished as part of the credit bid for the assets of old GM. The Chrysler additional note is still outstanding.

Chrysler Debtor-In-Possession

In May 2009, the Treasury and the Canadian government jointly agreed to make a loan in the total amount of $4,100 million ($3,000 million by the Treasury and $1,100 million by Canada) to Chrysler LLC in its capacity as debtor-in-possession (DIP) in its bankruptcy case. In May 2009, the Treasury increased its loan commitment in the DIP credit agreement to $3,800 million, and the Canadian government increased its commitment to $1,200 million, bringing the maximum loan amount to $5,000 million. The loan interest rate was the 3 Month Eurodollar rate plus 3.0 percent. The stated maturity was September 2009, with earlier maturity depending on the bankruptcy proceedings. Of the $3,800 million committed by the Treasury, approximately $1,900 million was funded during the bankruptcy. This DIP loan provided the necessary liquidity to sustain Chrysler during the bankruptcy period. Upon the Section 363 sale of the Chrysler assets, the funding commitment was reduced to amounts previously drawn. As such, no additional amounts were drawn from this facility. Recovery of the DIP loan is subject to the bankruptcy process associated with the Chrysler assets remaining after the sale to New Chrysler.

Chrysler Exit

In May 2009, the Treasury committed to make a loan to in New CarCo Acquisition LLC (New Chrysler or Chrysler Group LLC), the company that purchased the assets of Chrysler. The final terms of the credit agreement resulted in a loan to New Chrysler for $7,140 million. This amount consists of $6,640 million of new funding and $500.0 million of assumed debt[5] from the Treasury January 2, 2009 credit agreement with Chrysler Holding LLC. The loan was secured by a first priority lien on the assets of Chrysler Group LLC. Funding of the loan was available in two installments or tranches (B and C), each with varying availability and terms. The following describes the terms of Tranches B and C.

The maximum funding under Tranche B was $2,000 million and was funded on the closing date of the agreement. Interest on Tranche B is 3 Month Eurodollar plus 5.0 percent margin (in certain situations, defined in the agreement, a rate other than the 3 Month Eurodollar rate will be applied. This rate, referred to as the Alternative Base Rate, will be the greater of the Prime Rate, the Federal Funds Effective rate plus 0.5 percent or the 3 Month Eurodollar rate plus 1.0 percent. If this Alternative Base Rate is applied, the margin will be 4.0 percent versus the 5.0 percent if the 3 Month Eurodollar Rate). Tranche B is due and payable on December 10, 2011, provided that the Chrysler Group LLC may elect to extend the maturity of up to $400.0 million of Tranche B to the Tranche C maturity date. If so elected, the applicable margin will increase to 6.5 percent for Eurodollar and 5.5 percent for ABR loans, respectively.

The maximum funding under Tranche C is $4,640 million, of which $2,580 million was funded on the closing date. Interest on Tranche B is 3 Month Eurodollar plus 7.91 percent margin (in certain situations, defined in the agreement, a rate other than the 3 Month Eurodollar rate will be applied. This rate, referred to as the Alternative

4 Section 363 refers to Section 363 of the Federal Bankruptcy Code, which allows companies in bankruptcy to sell assets in reorganization.
5 The assumed debt contains the same terms as the Tranche C loan with respect to mandatory prepayment, interest and maturity.

Base Rate, will be the greater of the Prime Rate, the Federal Funds Effective rate plus 0.5 percent or the 3 Month Eurodollar rate plus 1.0 percent. If this Alternative Base Rate is applied, the margin will be 6.91 percent versus the 7.91 percent if the 3 Month Eurodollar Rate is used). On June 10, 2016, the Tranche C loan shall be prepaid to the extent funded amount is greater than 50.0 percent of the closing date commitment amount, taking into consideration amounts previously prepaid as a voluntary prepayment. The remaining balance of the Tranche C loan is due and payable on June 10, 2017.

Interest on both the Tranche B and Tranche C will be payable in-kind through December 2009 and will be added to the principal balance of the respective Tranche. In addition, additional in-kind interest will accrue in the amount of $17.0 million per quarter. Such amount will be added to the Tranche C loan balance subject to interest at the appropriate rate.

The Treasury also obtained other consideration, including a 9.85 percent equity interest in Chrysler Group LLC (included in Notes) and additional notes[6] with principal balances of $288.0 million and $100.0[7] million. As of September 30, 2009, the Treasury has funded approximately $4,600 million under this facility.

GM Debtor-In-Possession

On June 1, 2009, GM filed for Chapter 11 bankruptcy. As part of the filing the Treasury and the Canadian government agreed to lend up to $33,300 million under the terms of the DIP credit agreement; the Treasury's commitment amount was $30,100 million. The Treasury funded the $30,100 million of which approximately $986 million remains outstanding. In July 2009, the DIP credit agreement was amended to reflect the fact that the amounts there under (other than $986 million that remained with GM for wind-down in bankruptcy and $7,100 million that was assumed by GM NewCo) were extinguished in connection with a successful credit bid for the assets of old GM.

The Treasury has assigned its rights in this loan as well as the General Purpose and Working Capital loans and previously received common stock warrants to a newly created entity (GM NewCo or General Motors Company). The purpose of this GM NewCo is to obtain sufficient assets of GM out of bankruptcy to satisfy the original disbursed to GM and discussed above, which it accomplished through a successful credit bid for the assets in a sale pursuant to Section 363 of the Bankruptcy Code. Upon closing of the Section 363 sale, the General Motors Company has assumed $7,100 million of the DIP loan, simultaneously paying $400 million (return of warranty program funds), resulting in a balance of $6,700 million. The loan has a term of 6 years and bears interest at 3 Month Eurodollar (subject to a 2.0 percent floor) plus 5.0 percent and has a first lien security interest in the assets of General Motors Company. The Treasury also received $2,100 million in 9.0 percent cumulative perpetual preferred shares and 60.8 percent of the common equity interest in General Motors Company. The assets received by the Treasury as a result of the assignment and Section 363 sale are considered recoveries of the original loans for subsidy cost estimation purposes. As of September 30, 2009, Treasury had received $34.1 million in dividends on GM preferred stock.

6 The additional note bears the same interest rate and maturity as the Tranche C loan.
7 Interest begins to accrue on this note after certain events, defined in the credit agreement, have taken place.

GMAC Limited Liability Company (LLC) Rights Offering

In December 2008, the Treasury agreed, in principal, to lend up to $1,000 million to GM for participation in a rights offering by GMAC in support of GMAC's reorganization as a bank holding company. The loan was secured by the GMAC common interest acquired in the rights offering. The loan agreement specified that at any time, at the option of the lender (Treasury), the unpaid principal and accrued interest was exchangeable for the membership interest purchased, by GM, during the rights offering. The note was funded for $884.0 million. In May 2009, the Treasury exercised its exchange option under the loan and received 190,921 membership interests, representing approximately 35.36 percent of the voting interest, in GMAC in full satisfaction of the loan. In addition, Treasury received $9.1 million in interest while the loan was outstanding. The conversion to GMAC shares was not considered in the original subsidy cost. As a result a modification was recorded reducing the estimated subsidy cost by approximately $1,600 million.

THE CONSUMER AND BUSINESS LENDING INITIATIVE (CBLI)

Term Asset-Backed Securities Loan Facility

The Term Asset-Backed Securities Loan Facility (TALF) was created by the Federal Reserve Board (FRB) to provide low cost funding to investors in certain classes of Asset Backed Securities (ABS). Treasury agreed to participate in the program by providing liquidity and credit protection to the FRB.

Under the TALF, the FRBNY, as implementer of the TALF program, originated loans on a non-recourse basis to holders of certain AAA rated ABS secured by recently originated consumer and commercial loans and commercial mortgage backed securities (New Issue CMBS). In addition to securities secured by recently originated loans, CMBS issued prior to January 2009 and originally AAA rated (Legacy CMBS) are eligible collateral. TALF loans have a term of 3 or 5 years and are secured solely by eligible collateral. Haircuts (a percentage reduction used for collateral valuation) are determined based on the riskiness of each type of eligible collateral and the maturity of the eligible collateral pledged to the FRBNY. The "haircuts" provide additional protection to Treasury by exposing the TALF borrowers to risk of loss. Interest rates charged on the TALF loans depend on the weighted average maturity of the pledged collateral, the collateral type and whether the collateral pays a fixed or variable coupon.

As part of the program, the FRBNY has entered into a put agreement with the TALF, LLC, a special purpose vehicle created by the FRBNY. In the event of a TALF borrower default, the FRBNY will seize the collateral and sell it to the TALF, LLC under this agreement. The TALF, LLC receives a monthly fee equal to the difference between the TALF loan rate and the FRBNY's fee (spread) as compensation for entering into the put agreement. The accumulation of this fee will be used to fund purchases. In the event there are insufficient funds to purchase the collateral, the Treasury has committed to invest up to $20,000 million in non-recourse subordinate notes issued by the TALF, LLC. The subordinate notes bear interest at 1 Month LIBOR plus 3.0 percent and mature 10 years from the closing date, subject to extension. The Treasury disbursed $100.0 million upon creation of the TALF, LLC and the remainder can be drawn to purchase collateral in the event the spread is not sufficient to cover purchases. Any amounts needed in excess of the Treasury commitment and the fee would be provided through a loan from the FRBNY. Upon wind-down of TALF, LLC (collateral defaults, reaches final maturity or is sold), the cash balance will be disbursed according to the following payment priority:

1. FRBNY principal balance
2. Treasury principal balance
3. FRBNY interest

4. Treasury interest

5. Remaining cash balance – 90.0 percent to Treasury, 10.0 percent to FRBNY

Subsequent to the initial cost estimates prepared for the TALF, certain changes were made to the terms of the program, including increasing the term to 5 years and the addition of different types of acceptable collateral. These program changes resulted in a modification, increasing the original cost estimate by $8.0 million.

The TALF, LLC is owned and controlled by the FRBNY. The credit agreement entered into between the Treasury and the TALF, LLC provides the Treasury with certain rights consistent with a creditor but would not constitute control. As such TALF, LLC is not a federal entity and the assets, liabilities, revenue and cost of TALF, LLC are not included in the Treasury financial statements. The discussion below provides information on 1) the amount of TALF loans issued by the FRBNY, by collateral class, and 2) the assets, liabilities, income and expense of the TALF, LLC.

The FRBNY has originated $50,900 million in TALF loans[8], of which about $42,700 million is outstanding as of September 30, 2009. The average "haircut" was approximately 9.9 percent of the originated balance. As of September 30, 2009, all TALF loans performed as agreed. The table below shows the outstanding balance of the TALF loans as of September 30, 2009, by collateral type:

Collateral Type	Loan Amount (in millions)	% of Total
Auto	$ 7,430	17.3%
Credit Cards	21,610	50.6 %
Equipment	890	2.1 %
Floorplan	1,010	2.4 %
Premium Finance	990	2.3 %
Servicing Advances	580	1.4 %
Small Business	460	1.1 %
Student Loans	5,630	13.1 %
New Issue CMBS	0	0.0 %
Legacy CMBS	4,130	9.7 %
Total	**$ 42,730**	**100%**

As of September 30, 2009, the TALF, LLC has assets of approximately $198.9 million consisting primarily of investments in U.S. Treasury and Agency securities[9]. Total liabilities of the TALF, LLC are $101.8 million consisting of Treasury subordinated note plus accrued interest. During the period ended September 30, 2009, TALF, LLC collected $99.1 million in fees and investment income and incurred $2.3 million in expenses, $1.8 million of which is accrued interest on Treasury subordinated note. As of September 30, 2009 there were no TALF borrower defaults and consequently no purchases of collateral by TALF, LLC.

The tables below provide an analysis of the TARP direct loans including allowance for subsidy costs, modifications, and reestimates. The description of the TARP direct loan programs are described above. The TARP programs were created in fiscal year 2009 and thus there are no fiscal year 2008 comparitive balances to disclose.

8 These represent loans originated by the FRBNY and not Treasury. The intention of this disclosure is to show the activity in the program and the types of collateral that could eventually be purchased by the TALF, LLC with funding provided by Treasury.

9 Agency securities refer to securities issued by either Ginnie Mae, Fannie Mae, Freddie Mac, or the Federal Home Loan Banks.

Troubled Asset Relief Programs - Direct Loans Receivables, Net (in millions):

Programs	Direct Loans Receivable, Gross	Interest Receivable	Foreclosed Property	Allowance for Subsidy Cost (Present Value)	2009 Value of Assets Related to Direct Loans
AIFP	$ 61,262	$ 0	$ 0	$ (26,955)	$ 34,307
CBLI	100	0	0	344	444
Total	**$ 61,362**	**$ 0**	**$ 0**	**$ (26,611)**	**$ 34,751**

Total Amount of Disbursements, Direct Loans (in millions):

Programs	2009
AIFP	$63,402
CBLI	100
Total	**$63,502**

Subsidy Expense, Direct Loans (in millions):

Programs	Interest Differential	Defaults	Fees and Other Collections	Other	2009 Total
AIFP	$ (33)	$ 38,787	$ 0	$ (184)	$ 38,570
CBLI	6	0	0	(110)	(104)
Total	**$ (27)**	**$ 38,787**	**$ 0**	**$ (294)**	**$ 38,466**

Modifications and Reestimates, Direct Loans (in millions):

Programs	Total Modifications	Interest Rate Reestimates	Technical Reestimates	2009 Total Reestimates
AIFP	$ (1,589)	$ 0	$ (10,610)	$ (10,610)
CBLI	8	0	(243)	(243)
Total	**$ (1,581)**	**$ 0**	**$ (10,853)**	**$ (10,853)**

Total Subsidy Expense, Direct Loans (in millions):

Programs	2009
AIFP	26,371
CBLI	(339)
Total	**$ 26,032**

Subsidy Rates by Program and Component, Direct Loans:

Programs	Interest Differential	Defaults	Fees and Other Collections	Other	2009 Total
AIFP	-0.05%	59.07%	0.00%	-0.28%	58.74%
CBLI	5.87%	0.00%	0.00%	-110.10%	-104.23%

Schedule for Reconciling Subsidy Cost Allowance Balances (in millions):

DIRECT LOANS

	AIFP	CBLI	2009 Totals
Beginning Balance of the subsidy cost allowance	$ 0	$ 0	$ 0
Add: subsidy expense for disbursements			
(a) Interest rate differential cost	(33)	6	(27)
(b) Default costs (net of recoveries)	38,787	0	38,787
(c) Fees and other collections	0	0	0
(d) Other subsidy costs	(184)	(110)	(294)
Total of the above subsidy expense components	$ 38,570	$ (104)	$ 38,466
Adjustments:			
(a) Loan modifications	(1,589)	8	(1,581)
(b) Fees received	261	0	261
(c) Foreclosed property acquired	0	0	0
(d) Loans written off	0	0	0
(e) Subsidy allowance amortized	323	(5)	318
(f) Other	0	0	0
Ending Balance subsidy cost allowance before reestimates	$ 37,565	$ (101)	$ 37,464
Add or subtract subsidy reestimates by component:			
(a) Interest rate reestimate	0	0	0
(b) Technical default reestimate	(10,610)	(243)	(10,853)
Total of the above reestimate components	(10,610)	(243)	(10,853)
Ending Balance of the subsidy cost allowance	**$ 26,955**	**$ (344)**	**$ 26,611**

HOME AFFORDABLE MODIFICATION PROGRAM (HAMP)

The Home Affordable Modification Program (HAMP) is designed to assist eligible homeowners who are experiencing financial hardships to remain in their homes by providing reductions in their monthly mortgage payments for up to five years. The HAMP provides for one-time, monthly, and annual incentives to servicers, borrowers, and investors who participate in the program. On an ongoing basis, beyond such incentive, the Treasury shares equally in the cost of the reductions with the mortgage investors. Lastly, investors are paid a Home Price Decline Protection payment to partially offset losses from home price declines.

For the HAMP, Fannie Mae provides direct programmatic support as a third party agent on behalf of Treasury, Freddie Mac provides compliance oversight as a third party agent on behalf of Treasury, and the servicers work directly with the borrowers to modify and service the borrowers' loans.

As of September 30, 2009, the Treasury had entered into agreements with 63 servicers to provide up to approximately $27,100 million in payments and incentives to borrowers, servicers, and investors. It should be noted that all HAMP payments are made to servicers either for themselves or for the benefit of borrowers and investors. Furthermore, all payments are contingent on borrowers remaining current on their mortgage payments. As of September 30, 2009, approximately $0.95 million in incentive payments had been paid to three servicers in incentive payments for 743 borrowers who had completed official loan modifications. Servicers have until December 31, 2012, to enter into mortgage modifications with borrowers.

The HAMP is not subject to the FCRA per ESSA. The liability for payments to servicers and investors, and principal balance reduction payments for the account of borrowers under the HAMP are accounted for in accordance with SFFAS No. 5, *Accounting for Liabilities of the Federal Government*. Under SFFAS No. 5, the liability is recognized in the period in which the exchange occurs. The exchange of consideration between the parties and the Treasury occurs on a month to month basis. Executed contract and program documentation identifies servicing requirements by the servicer, certain incentives for investors to participate in the modifications and/or not assert any rights to object or dissent to the modification and the nature and timing of the actions the borrower must agree to and take, in order for the Treasury to be liable for payment. A key requirement of program continuance is the servicer's ongoing responsibility under the servicing agreement to closely monitor and perform loss mitigation when required to assist the borrowers to remain current on their payments. As of September 30, 2009, the Treasury had accrued approximately $1.4 million of first lien incentive for modifications under the HAMP program, and reported in other liabilities in the financial statements.

13. LOANS AND INTEREST RECEIVABLE

Entity and Non-Entity Non-Federal:

As of September 30, 2009 and September 30, 2008, loans and interest receivable from non-federal entities consisted of the following, excluding TARP Loans (in millions):

	Entity	Non-entity	2009 Total	Entity	Non-entity	2008 Total
Direct Loans	$ 61	$ 125	$ 186	$ 62	$ 128	$ 190
Interest Receivable	0	2	2	0	2	2
Less: Allowance and Subsidy Cost	(20)	0	(20)	(20)	0	(20)
Total Non-Federal Loans and Related Interest Receivable	**$ 41**	**$ 127**	**$ 168**	**$ 42**	**$ 130**	**$ 172**

Loans and Interest Receivable amounts include certain loans and credits issued by the United States to various foreign governments and other entities. The agreements with each debtor government vary as to dates, interest rates, method of payment, and billing procedures. All such loans and credits represent legally valid and outstanding obligations of foreign governments, other entities, and the U.S. Government has not waived or renounced its rights with respect to any of them. The loans are due and payable in U.S. denominations.

14. RESERVE POSITION IN THE INTERNATIONAL MONETARY FUND

The United States participates in the IMF through a quota subscription. Quota subscriptions are paid partly through the transfer of reserve assets, such as foreign currencies or SDR, which are international reserve currency assets created by the IMF, and partly by making domestic currency available as needed through a non-interest-bearing letter of credit. This letter of credit, issued by the Treasury Department and maintained by the FRBNY, represents the bulk of the IMF's holdings of dollars. Approximately one quarter of 1 percent of the U.S. quota is maintained in cash balances in an IMF account at FRBNY.

While resources for transactions between the IMF and the United States are appropriated, they do not result in net budgetary outlays. This is because U.S./IMF quota transactions constitute an exchange of monetary assets in which the United States receives an equal offsetting claim on the IMF in the form of an increase in the U.S. reserve position in the IMF, which is interest-bearing and can be drawn at any time for balance of payments needs. When the IMF draws dollars from the letter of credit to finance its operations and expenses, the drawing does not represent a net budget outlay on the part of the United States because there is a commensurate increase in the U.S. reserve position. When the IMF repays dollars to the United States, no net budget receipt results because the U.S. reserve position declines concurrently in an equal amount.

As of September 30, 2009, the U.S. quota in the IMF was 37.1 billion SDR, valued at approximately $66.6 billion. (The quota as of September 30, 2008, was 37.1 billion SDR, valued at approximately $57.9 billion.) The quota consisted of the following (in millions):

	2009	2008
Letter of Credit /1	$ 53,056	$ 53,012
U.S. Dollars Held in Cash by the IMF /1	44	88
Reserve Position /2	13,469	4,750
U.S. Quota in the IMF	**$ 66,569**	**$ 57,850**

1/ This amount is included in entity appropriated funds under Note 2, Fund Balance with Treasury, and unexpended appropriations – Obligations/ Undelivered orders.

2/ This amount is included in the Cumulative Results of Operations.

On June 24, 2009, the Supplemental Appropriations Act, 2009 (Public Law 111-32) was enacted and it provides authorization and appropriations for an increase in the United States quota share in the IMF by the dollar equivalent of 4.97 billion SDRs which at the SDR/dollar exchange rate applicable September 30, 2009 is equivalent to $7.9 billion. However, this increase in the United States quota share is not effective as of September 30, 2009 and will not come into effect until other IMF member countries undertake certain actions with respect to the IMF.

The U.S. reserve position is denominated in SDR, as is the U.S. quota. Consequently, fluctuations in the value of the dollar with respect to the SDR results in valuation changes in dollar terms for the U.S. reserve position in the IMF as well as the IMF letter of credit. The Treasury Department periodically adjusts these balances to maintain the SDR value of the U.S. quota and records the change as a deferred gain or loss in its cumulative results of operations. These adjustments, known as maintenance of value adjustments, are settled annually after the close of the IMF financial year on April 30. Such adjustments do not involve a flow of funds. At April 30, 2009, the annual settlement with the IMF resulting from the appreciation of the dollar against the SDR since April 30, 2008, called for an downward adjustment of the U.S. quota by $4.3 billion and a corresponding increase to

Unexpended Appropriations on the Statement of Changes in Net Position (At April 30, 2008, the depreciation of the dollar against the SDR since April 30, 2007, called for an upward adjustment of the U.S. quota by $3.4 billion and a corresponding increase to Unexpended Appropriations.) The dollar balances shown above for the U.S. quota includes accrued valuation adjustments. At September 30, 2009, the Treasury Department recorded a net deferred valuation gain in the amount of $498 million for deferred maintenance of value adjustments needed at year end ($15.5 million loss at September 30, 2008).

The United States earns "remuneration" (interest) on its reserve position in the IMF except for the portion of the reserve position originally paid in gold. Remuneration is paid quarterly and is calculated on the basis of the SDR interest rate. The SDR interest rate is a market-based interest rate determined on the basis of a weighted average of interest rates on short-term instruments in the markets of the currencies included in the SDR valuation basket. Payment of a portion of this remuneration is deferred as part of a mechanism for creditors and debtors to share the financial consequences of overdue obligations to the IMF, such as unpaid overdue interest, and to similarly share the burden of establishing any contingency accounts deemed necessary to reflect the possibility of non-repayment of relevant principal amounts. As overdue interest is paid, previously deferred remuneration corresponding to the creditors' share of the burden of earlier nonpayment is included in the next payment of remuneration. The deferred remuneration corresponding to the creditors' share of establishing the contingency accounts is usually paid when there are no longer any relevant overdue obligations or when the IMF Executive Board determines to pay the remuneration. There was no deduction in the remuneration paid by the IMF as a result of burden-sharing during fiscal years 2009 or 2008. For fiscal years 2009 and 2008, the Treasury Department received $40 million and $59 million as remuneration, respectively. (See Note 6.)

In addition to quota subscriptions, the IMF maintains borrowing arrangements to supplement its resources in times of crisis when IMF liquidity is low. The United States currently participates in two such arrangements – the General Arrangements to Borrow (GAB) and the New Arrangements to Borrow (NAB). There were no U.S. loans outstanding under these arrangements in fiscal year 2009 and fiscal year 2008. The dollar equivalent of SDR 6.7 billion has been appropriated to finance U.S. participation in the GAB and NAB; as of September 30, 2009 and September 30, 2008, this amounted to $10.6 billion and $10.5 billion, respectively, in standing appropriations available for lending through the GAB or NAB as needed. As is the case for the U.S. quota in the IMF, budgetary treatment of U.S. participation in the GAB and NAB does not result in net budgetary outlays, since transactions under the GAB or NAB result in concurrent adjustments to the U.S. reserve position in the IMF.

Public Law 111-32 also provided the authorization and appropriations for an increase in the United States participation in the NAB by the dollar equivalent of SDR 75 billion which at the SDR/dollar exchange rate applicable on September 30, 2009 is equivalent to $119 billion. However, this increase in the United States participation in the NAB is not effective as of September 30, 2009 and will not come into effect until all IMF member countries participating in the NAB come to a final agreement on certain modifications to the decision governing the NAB. Although $119 was appropriated under Public Law 111-32, the United States has publicly stated that it will limit its commitment to $100 billion whenever a final decision is reached.

15. TAX, OTHER, AND RELATED INTEREST RECEIVABLES, NET

Tax, other, and related interest receivables include receivables from tax assessments, excise taxes, fees, penalties, and interest assessed and accrued that were not paid or abated, reduced by an estimate for uncollectible amounts. In addition to amounts attributed to taxes, interest income due on monies deposited in Federal Reserve Banks is also included in this line item.

As of September 30, 2009 and September 30, 2008, Tax, Other, and Related Interest Receivables, and Net, consisted of the following (in millions):

Non-Entity:	2009	2008
IRS Federal Tax Receivable, Gross	$ 128,115	$ 112,067
Less: Allowance on Taxes Receivable	(99,027)	(83,046)
Receivable, Deposit of Earnings, Federal Reserve Banks	1,254	1,465
Other Receivables and Interest	33	28
Less: Allowance on Other and Related Interest Receivable	(15)	(19)
Total Tax, and Other Non-Entity Receivables, Net	**$ 30,360**	**$ 30,495**
Entity:		
Miscellaneous Entity Receivables and Related Interest	48	383
Total Tax, Other, and Related Interest Receivables, Net	**$ 30,408**	**$ 30,878**

IRS federal taxes receivable constitute the largest portion of the receivables. IRS federal taxes receivable consists of tax assessments, penalties, and interest which were not paid or abated, and which were agreed to by either the taxpayer and IRS, or the courts. An allowance for doubtful accounts is established for the difference between the gross receivables and the portion deemed collectible. The portion of tax receivables estimated to be collectible and the allowance for doubtful accounts are based on projections of collectability from a statistical sample of taxes receivable. The Treasury Department does not establish an allowance for the receivable on deposits of Federal Reserve Bank earnings.

16. INVENTORY AND RELATED PROPERTY, NET

Inventory and related property includes inventory, operating materials and supplies, and forfeited property held by Treasury Department. The Treasury Department's operating materials and supplies are maintained for the production of bureau products. The Treasury Department maintains inventory accounts or balances (e.g., metals, paper, etc.) for use in manufacturing currency and coins. The cost of these items is included in inventory costs, and is recorded as cost of goods sold upon delivery to customers. Inventory for check processing activities is also maintained. As of September 30, 2009 and September 30, 2008, inventory and related property consisted of the following (in millions):

	2009	2008
Operating materials and supplies held for use	$ 17	$ 16
Operating materials and supplies held in reserve for future use	24	24
Forfeited property	62	100
Inventory – raw materials	239	355
Inventory – work in process	128	86
Inventory – finished goods	142	135
Allowance for inventories and related property	(14)	(18)
Total Inventories and Related Property, Net	$ 598	$ 698

17. PROPERTY, PLANT, AND EQUIPMENT, NET

As of September 30, 2009 and September 30, 2008, property, plant, and equipment consisted of the following (in millions):

2009	Depreciation Method	Service Life	Cost	Accumulated Depreciation	Net Book Value
Buildings, structures, and facilities	S/L	3 - 50 years	$ 676	$ (308)	$ 368
Furniture, fixtures, and equipment	S/L	2 - 20 years	3,048	(2,268)	780
Construction in progress	N/A	N/A	38	0	38
Land and land improvements	N/A	N/A	12	0	12
Internal use software	S/L	2 -10 years	1,352	(807)	545
Internal use software in development	N/A	N/A	112	0	112
Assets under capital lease	S/L	2 - 25 years	25	(23)	2
Leasehold improvements	S/L	2 - 25 years	482	(303)	179
Total			$ 5,745	$ (3,709)	$ 2,036

2008	Depreciation Method	Service Life	Cost	Accumulated Depreciation	Net Book Value
Buildings, structures, and facilities	S/L	3 - 50 years	$ 669	$ (297)	$ 372
Furniture, fixtures, and equipment	S/L	2 - 20 years	3,376	(2,608)	768
Construction in progress	N/A	N/A	35	0	35
Land and land improvements	N/A	N/A	12	0	12
Internal use software	S/L	2-10 years	1,151	(664)	487
Internal use software in development	N/A	N/A	205	0	205
Assets under capital lease	S/L	2 - 25 years	30	(20)	10
Leasehold improvements	S/L	2 - 25 years	580	(392)	188
Total			$ 6,058	$ (3,981)	$ 2,077

The service life ranges vary significantly due to the diverse nature of PP&E held by the Treasury Department.

HERITAGE ASSETS

The Treasury Department Complex (Main Treasury Building and Annex) was declared a national historical landmark in 1972. The Treasury Department Complex is treated as a multi-use heritage asset and is expected to be preserved indefinitely. The building housing the United States Mint in Denver, Colorado, is also considered a multi-use heritage asset.

18. NON-ENTITY ASSETS

Non-entity assets are those that are held by the Treasury Department but are not available for use by the Treasury Department. For example non-entity Fund Balance with Treasury represents unused balances of appropriations received by various Treasury Department entities to conduct custodial operations such as the payment of interest on the federal debt and refunds of taxes and fees. Non-entity loans and interest receivable represents loans managed by the Treasury Department on behalf of the U.S. Government. These loans are provided to federal agencies, and the Treasury Department is responsible for collecting these loans and transferring the proceeds to the General Fund of the U.S. Government. Non-entity cash, foreign currency, and other monetary assets include the operating cash of the U.S. Government, managed by the Treasury Department. It also includes foreign currency maintained by various U.S. and military disbursing offices, as well as seized monetary instruments. Non-Entity Investments in GSEs include the GSE senior preferred stock and warrants held by Treasury on behalf of the General Fund. As the stock and warrants are liquidated all proceeds are returned to the General Fund.

As of September 30, 2009 and September 30, 2008, non-entity assets consisted of the following (in millions):

	2009	2008
Intra-governmental Assets:		
Fund Balance (Note 2)	$ 513	$ 889
Loans and Interest Receivable (Note 3)	348,800	226,194
Accounts Receivable and Related Interest (Note 5)	285	372
Advances to the Black Lung Trust Fund (Note 1G)	0	10,484
Advances to the Unemployment Trust Fund (Note 1H)	7,981	0
Due from the General Fund (Note 4)	11,992,719	10,100,763
Total Non-Entity Intra-governmental Assets	$ 12,350,298	$ 10,338,702
Cash, Foreign Currency, and Other Monetary Assets (Note 6)	$ 269,579	$ 364,941
Gold and Silver Reserves (Note 7)	11,062	11,062
Loans and Interest Receivable (Note 13)	127	130
Investments in GSEs (Note 9)	64,679	7,032
Tax, Other, and Related Interest Receivable, Net (Note 15)	30,360	30,495
Beneficial Interest in AIG Trust	23,472	0
Miscellaneous Assets	3	12
Total Non-Entity Assets	$ 12,749,580	$ 10,752,374
Total Entity Assets	1,097,021	364,664
Total Assets	$ 13,846,601	$ 11,117,038

19. FEDERAL DEBT AND INTEREST PAYABLE

The Treasury Department is responsible for administering the federal debt on behalf of the U.S. Government. The federal debt includes borrowings from the public as well as borrowings from federal agencies. The federal debt managed by the Treasury Department does not include debt issued by other governmental agencies such as the Tennessee Valley Authority or the Department of Housing and Urban Development.

The federal debt as of September 30, 2009 and September 30, 2008 was as follows (in millions):

Intra-governmental	2009	2008
Beginning Balance	$ 4,179,570	$ 3,922,548
New Borrowings/Repayments	140,322	257,022
Subtotal at Par Value	**$ 4,319,892**	**$ 4,179,570**
Premium/(Discount)	33,779	32,489
Interest Payable Covered by Budgetary Resources	49,409	50,355
Total	**$ 4,403,080**	**$ 4,262,414**

Owed to the Public	2009	2008
Beginning Balance	$ 5,808,691	$ 5,049,305
New Borrowings/Repayments	1,743,171	759,386
Subtotal at Par Value	**$ 7,551,862**	$ 5,808,691
Premium/(Discount)	(33,906)	(36,124)
Interest Payable Covered by Budgetary Resources	41,349	40,127
Total	**$ 7,559,305**	**$ 5,812,694**

Debt held by the public approximates the U.S. Government's competition with other sectors in the credit markets. In contrast, debt held by federal entities, primarily trust funds, represents the cumulative annual surpluses of these funds (i.e., excess of receipts over disbursements plus accrued interest) that have been used to finance general government operations.

FEDERAL DEBT HELD BY OTHER FEDERAL AGENCIES

Certain federal agencies are allowed to invest excess funds in debt securities issued by the Treasury Department on behalf of the U.S. Government. The terms and the conditions of debt securities issued are designed to meet the cash needs of the U.S. Government. The vast majority is non-marketable securities issued at par value, but some are issued at market prices whose prices and interest rates reflect market terms. The average interest rate for debt held by the federal entities in fiscal year 2009 was 4.3 percent (4.83 percent in fiscal year 2008).

The federal debt also includes intra-governmental marketable debt securities that certain agencies are permitted to buy and sell on the open market. The debt, at par value (not including interest receivable), owed to federal agencies as of September 30, 2009 and September 30, 2008 was as follows (in millions):

	2009	2008
Social Security Administration	$ 2,504,248	$ 2,367,138
Office of Personnel Management	828,952	797,107
Department of Defense Agencies	375,519	335,672
Department of Health and Human Services	376,512	380,540
All Other Federal Entities - Consolidated	234,661	299,113
Total Federal Debt Held by Federal Entities	$ 4,319,892	$ 4,179,570

The above balances do not include premium/discount and interest payable.

FEDERAL DEBT HELD BY THE PUBLIC

As of September 30, 2009 and September 30, 2008, Federal Debt held by the Public consisted of the following:

(at par value, in millions)	Term	Average Interest Rates	2009
Marketable:			
Treasury Bills	1 Year or Less	0.3%	$ 1,986,174
Treasury Notes	2 - 10 Years	3.0%	3,772,964
Treasury Bonds	Over 10 Years	6.5%	677,491
Treasury Inflation Protected Security (TIPS)	5 Years or More	2.1%	551,308
Total Marketable			$ 6,987,937
Non-Marketable	On Demand to Over 10 Years	3.7%	563,925
Total Federal Debt (Public)			$ 7,551,862

(at par value, in millions)	Term	Average Interest Rates	2008
Marketable:			
Treasury Bills	1 Year or Less	1.6%	$ 1,484,332
Treasury Notes	2 - 10 Years	4.1%	2,623,364
Treasury Bonds	Over 10 Years	7.1%	578,504
Treasury Inflation Protected Security (TIPS)	5 Years or More	2.0%	523,951
Total Marketable			$ 5,210,151
Non-Marketable	On Demand to Over 10 Years	4.1%	598,540
Total Federal Debt (Public)			$ 5,808,691

The above balances do not include premium/discount and interest payable.

The Treasury Department issues marketable bills at a discount or at par and pays the par amount of the security upon maturity. The average interest rate on Treasury bills represents the original issue effective yield on securities outstanding as of September 30, 2009 and September 30, 2008, respectively. Treasury bills are issued with a term of one year or less.

The Treasury Department issues marketable notes and bonds as long-term securities that pay semi-annual interest based on the securities' stated interest rates. These securities are issued at either par value or at an amount that reflects a discount or a premium. The average interest rate on marketable notes and bonds represents the stated interest rate adjusted by any discount or premium on securities outstanding as of September 30, 2009 and September 30, 2008. Treasury notes are issued with a term of 2 to 10 years and Treasury bonds are issued with a term of more than 10 years. The Treasury Department also issues inflation–indexed securities (TIPS) that have interest and redemption payments, which are tied to the Consumer Price Index, a widely used measurement of inflation. TIPS are issued with a term of five years or more. At maturity, TIPS are redeemed at the inflation-adjusted principal amount, or the original par value, whichever is greater. TIPS pay a semi-annual fixed rate of interest applied to the inflation-adjusted principal.

Over the course of fiscal year 2009, changes in economic conditions, financial markets, and fiscal policy as well as a reduction in nonmarketable debt issuance have caused an increase in Treasury's marketable borrowing needs. Financial market strains have impacted the real economy, and the nation has experienced lower economic growth, lower receipts, and increased outlays. The Treasury Department has responded to the increase in marketable borrowing requirements by increasing issuance sizes of regular bills, the frequency, terms, and issuance sizes of cash management bills, and the issuance sizes of nominal coupon security offerings.

Federal Debt Held by the Public includes federal debt held outside of the U. S. Government by individuals, corporations, Federal Reserve Banks (FRB), state and local governments, foreign governments and central banks. As of September 30, 2009, the FRB had total holdings of $769 billion, with a very small amount lent to dealers and not collateralized by other Treasury securities. As of September 30, 2008, the FRB owned $221 billion, net of $256 billion in securities lent to dealers and not collateralized by other Treasury securities, for total holdings of $477 billion. These securities are held in the FRB System Open Market Account (SOMA) for the purpose of conducting monetary policy.

The amount of outstanding federal debt is limited by the statutory debt ceiling. Outstanding debt is projected to reach the statutory debt ceiling in late December 2009. Congressional actions to increase the debt ceiling are currently pending. In the event Congressional action is delayed, the Treasury Department has various options available to it to issue additional debt to fund government operations until Congressional action is completed.

20. OTHER DEBT AND INTEREST PAYABLE

Borrowings outstanding are with the Civil Service Retirement and Disability Fund (CSR&DF), which is administered by the Office of Personnel Management (OPM). At September 30, 2009 and September 30, 2008, FFB had borrowings of $11.9 billion and $14.0 billion and an associated unamortized premium of $229 million and $288 million, respectively. These borrowings are at stated interest rates ranging from 4.625 percent to 5.250 percent, effective interest rate of 4.125 percent, and with maturity dates range from June 30, 2010 to June 30, 2019.

21. D.C. PENSIONS AND JUDICIARY RETIREMENT ACTUARIAL LIABILITY

Pursuant to Title XI of the *Balanced Budget Act of 1997*, as amended (the Act), on October 1, 1997, Treasury became responsible for certain District of Columbia retirement plans. The Act was intended to relieve the District of Columbia government of the burden of unfunded pension liabilities transferred to the District by the U.S. Government in 1979. To fulfill its responsibility, Treasury manages two funds — the D.C. Teachers', Police Officers' and Firefighters' Federal Pension Fund (the D.C. Federal Pension Fund) and the District of Columbia Judicial Retirement and Survivors Annuity Fund (the Judicial Retirement Fund). The Treasury Department is required to make annual amortized payments from the General Fund of the U.S. Government to the D.C. Federal Pension Fund and the Judicial Retirement Fund. The actuarial cost method used to determine costs for the retirement plans is the Aggregate Entry Age Normal Actuarial Cost Method. The actuarial liability is based upon long term assumptions selected by the Treasury Department. The pension benefit costs incurred by the plans are included on the Consolidated Statements of Net Cost.

D.C. FEDERAL PENSION FUND

The purpose of the D.C. Federal Pension Fund is to make federal benefit payments and pay necessary administrative expenses for the District of Columbia Police Officers', Firefighters', and Teachers' Retirement Plans for benefits earned based upon service on or before June 30, 1997. The amount paid into the D.C. Federal Pension Fund from the General Fund of the U.S. Government was $400.3 million for fiscal year 2009 ($340.2 million during fiscal year 2008). As of September 30, 2009, the unobligated budgetary resources of the D.C. Federal Pension Fund were approximately $3,557.8 million, and the pension actuarial liability was $8,892.5 million, resulting in an unfunded liability of $5,334.7 million. (As of September 30, 2008, the unobligated budgetary resources of the D.C. Federal Pension Fund were approximately $3,564.2 million, and the pension actuarial liability was $8,640.8 million, resulting in an unfunded liability of $5,076.6 million.) In fiscal year 2009, the assumption for the annual rate of investment return in fiscal year 2010 was 4.5 percent for the D.C. Federal Pension Fund with a gradual increase to 6.0 percent by fiscal year 2016; and the assumption for the future annual rate of inflation and future cost-of-living adjustments was 3.5 percent. In fiscal year 2008, the assumption for the annual rate of investment return in fiscal year 2009 was 4.7 percent for the D.C. Federal Pension Fund with a gradual increase to 6 percent by fiscal year 2014; and the assumption for the future annual rate of inflation and future cost of-living adjustments was 3.5 percent. In fiscal year 2009, the assumption for the future annual rate of salary increases ranged from 3.5 percent to 6.5 percent for police officers and firefighters, based on years of service, and ranged from 3.5 percent to 5.5 percent for teachers, based on years of service. In fiscal year 2008, the assumption for the future annual rate of salary increases was 6.5 percent for police officers and firefighters, and 5.5 percent for teachers.

JUDICIAL RETIREMENT FUND

The purpose of the Judicial Retirement Fund is to make federal benefit payments and pay necessary administrative expenses for the Judges' Retirement Plans for all benefits earned. The amount paid into the Judicial Retirement Fund from the General Fund of the U.S. Government was $7.04 million for fiscal year 2009 ($6.98 million during fiscal year 2008). As of September 30, 2009, the unobligated budgetary resources of the Judicial Retirement Fund were approximately $122.4 million, and the pension actuarial liability was $156.6 million, resulting in an unfunded liability of $34.2 million. (As of September 30, 2008, the unobligated budgetary resources of the Judicial Retirement Fund were approximately $118.5 million, and the pension actuarial liability was $161.6 million, resulting in an unfunded liability of $43.1 million.) In fiscal year 2009, the assumption for the annual rate of investment return in fiscal year 2010 was 5.2 percent for the Judicial Retirement Fund with a gradual increase to 6 percent by fiscal year 2017; and the assumption for the future annual rate of inflation and future cost-of-living adjustments was 3.5 percent. In fiscal year 2008, the assumption for the annual rate of investment return in fiscal year 2009 was 5.2 percent for the Judicial Retirement Fund with a gradual increase to 6 percent by fiscal year 2015; and the assumption for the future annual rate of inflation and future cost of-living adjustments was 3.5 percent. In fiscal year 2009, the assumption for the future annual rate of salary increases was 3.5 percent for judges. This assumption was unchanged from fiscal year 2008.

22. LIABILITIES

Liabilities Not Covered by Budgetary and Other Resources

As of September 30, 2009 and September 30, 2008, liabilities not covered by budgetary and other resources consisted of the following (in millions):

	2009	2008
Intra-governmental Liabilities Not Covered by Budgetary and Other Resources:		
Federal Debt Principal, Premium/Discount (Note 19)	$ 4,353,671	$ 4,212,059
Other Intra-governmental Liabilities	105	105
Total Intra-governmental Liabilities Not Covered by Budgetary and Other Resources	**$ 4,353,776**	**$ 4,212,164**
Federal Debt Principal, Premium/Discount (Note 19)	7,517,956	5,772,567
Gold and Silver Reserves held by the U.S. Mint	10,494	10,494
D.C. Pensions Liability (Note 21)	5,369	5,120
Liabilities to GSEs	91,937	13,800
Other Liabilities	1,057	1,085
Total Liabilities Not Covered by Budgetary and Other Resources	**$ 11,980,589**	**$ 10,015,230**
Total Liabilities Covered by Budgetary and Other Resources	**1,437,956**	**792,097**
Total Liabilities	**$ 13,418,545**	**$ 10,807,327**

Other Liabilities

Total "Other Liabilities" displayed on the Balance Sheets consists of both liabilities that are covered and not covered by budgetary resources.

The amounts displayed of $3,331 million and $4,052 million, respectively, at September 30, 2009 and September 30, 2008 consisted of the following (in millions):

	2009		
	Current	Non-Current	Total
Intra-governmental			
Unfunded Federal Workers Compensation Program Liability (FECA)	$ 46	$ 57	$ 103
Accounts Payable	61	0	61
Accrued Interest Payable	(3)	0	(3)
Other Accrued Liabilities	263	1	264
Total Intra-governmental	**$ 367**	**$ 58**	**$ 425**
With the Public			
Actuarial Federal Workers Compensation Program Liability (FECA)	0	533	533
Liability for Deposit Funds (Held by the Federal Government for Others) and Suspense Accounts	71	0	71
Accrued Funded Payroll and Benefits	488	0	488
Capital Lease Liabilities	1	0	1
Accounts Payable and Other Accrued Liabilities	2,194	44	2,238
Total with the Public	**$ 2,754**	**$ 577**	**$ 3,331**

	2008		
	Current	Non-Current	Total
Intra-governmental			
Unfunded Federal Workers Compensation Program Liability (FECA)	$ 45	$ 57	$ 102
Accounts Payable	76	0	76
Other Accrued Liabilities	165	2	167
Total Intra-governmental	$ 286	$ 59	$ 345
With the Public			
Actuarial Federal Workers Compensation Program Liability (FECA)	0	594	594
Liability for Deposit Funds (Held by the Federal Government for Others) and Suspense Accounts	526	0	526
Accrued Funded Payroll and Benefits	424	0	424
Capital Lease Liabilities	4	1	5
Accounts Payable and Other Accrued Liabilities	2,460	43	2,503
Total with the Public	$ 3,414	$ 638	$ 4,052

23. NET POSITION

Unexpended Appropriations represents the amount of spending authorized as of year-end that is unliquidated or unobligated and has not lapsed, been rescinded, or withdrawn. No-year appropriations remain available for obligation until expended. Annual appropriations remain available for upward or downward adjustment of obligations until expired.

Cumulative Results of Operations represents the net results of operations since inception, and includes cumulative amounts related to investments in capitalized assets and donations and transfers of assets in and out without reimbursement. Also included as a reduction in Cumulative Results of Operations are accruals for which the related expenses require funding from future appropriations and assessments. These future funding requirements include, among others (a) accumulated annual leave earned but not taken, (b) accrued workers compensation, (c) credit reform cost reestimates, and (d) expenses for contingent liabilities.

The amount reported as "appropriations received" are appropriated from the Treasury General Fund of the U.S. Government receipts, such as income taxes, that are not earmarked by law for a specific purpose. This amount will not necessarily agree with the "appropriation received" amount reported on the Statement of Budgetary Resources (SBR) because of differences between proprietary and budgetary accounting concepts and reporting requirements. For example, certain dedicated and earmarked receipts are recorded as "appropriations received" on the SBR, but are recognized as exchange or non-exchange revenue (i.e., typically in special and non-revolving trust funds) and reported on the Statement of Changes in Net Position in accordance with Statement of Federal Financial Accounting Standards (SFFAS No. 7).

TRANSFERS TO THE GENERAL FUND AND OTHER

The amount reported as "Transfers to the General Fund and Other" on the Consolidated Statements of Changes in Net Position under "Other Financing Sources" includes the credit reform downward reestimates to be collected by the General Fund and current year negative subsidy transferred of $118,139 million and $7,220 million, respectively, for the year ended September 30, 2009. Also included is $95,600 million in GSE General Fund exchange revenue from the gross increase in value of the GSE preferred stock. In addition, these transfers also include distribution of interest revenue to the General Fund of the U.S. Government of $30.1 billion and $13.5 billion, for the years ended September 30, 2009 and September 30, 2008, respectively. The interest revenue is accrued on inter-agency loans held by the Treasury Department on behalf of the U.S. Government. A corresponding balance is reported on the Consolidated Statement of Net Cost under "Federal Costs: Less Interest Revenue from Loans." The amount reported on the Consolidated Statement of Net Cost is reduced by eliminations with Treasury bureaus. Also included in "Transfers to the General Fund and Other" is $4,336 million (GSE Dividends) and $7,032 million (initial GSE preferred stock) transferred to the general fund for the years ended September 30, 2009 and September 30, 2008, respectively. In addition, $(37,953) million of GSE senior preferred stock valuation loss and other transfers of $238 million are included as of September 30, 2009.

The Treasury Department also includes seigniorage in "Transfers to the General Fund and Other." Seigniorage is the face value of newly minted circulating coins less the cost of production. The United States Mint is required to distribute the seigniorage that it recognizes to the General Fund of the U.S. Government. The distribution is also included in "Transfers to the General Fund and Other." In any given year, the amount recognized as seigniorage may differ for the amount distributed to the General Fund by an insignificant amount due to timing differences.

Seigniorage in the amounts of $447.1 million and $728.6 million was recognized, respectively, for the years ended September 30, 2009 and September 30, 2008. Total distributions from the Mint to the General Fund, including seigniorage and numismatic profit, amounted to $ 475 million and $750 million, respectively, for the years ended September 30, 2009 and September 30, 2008.

The transfers are summarized in the following table:

	2009	2008
Downward Reestimates of Credit Reform Subsidies	$ 118,139	$ 0
Credit Reform Negative Subsidies	7,220	0
Interest Revenue	30,124	13,500
Increase in Liquidity Preference of GSE Preferred Stock	95,600	0
GSE Preferred Stock Dividends	4,336	0
GSE Warrants and Stock Valuation (net)	(37,953)	0
GSE Warrants and Stock - Fee for SPPS Agreement	0	7,032
Other	238	256
	$ 217,704	**$ 20,788**

24. CONSOLIDATED STATEMENT OF NET COST AND NET COSTS OF TREASURY SUB-ORGANIZATIONS

The Treasury Department's Consolidated Statement of Net Cost displays information on a consolidated basis. The complexity of the Treasury Department's organizational structure and operations requires that supporting schedules for Net Cost be included in the notes to the financial statements. These supporting schedules provide consolidating information, which fully displays the costs of each sub-organization (Departmental Offices and each operating bureau).

The classification of sub-organizations has been determined in accordance with SFFAS No. 4, *Managerial Cost Accounting Concepts and Standards for the Federal Government* which states that the predominant factor is the reporting entity's organization structure and existing responsibility components, such as bureaus, administrations, offices, and divisions within a department.

Each sub-organization is responsible for accumulating costs. The assignment of the costs to Treasury-wide programs is the result of using the following cost assignment methods: (1) direct costs, (2) cause and effect, and (3) cost allocation.

Intra-Departmental costs/revenues resulting from the provision of goods and/or services on a reimbursable basis among Departmental sub-organizations are reported as costs by providing sub-organizations. Accordingly, such costs/revenues are eliminated in the consolidation process.

To the extent practical or reasonable to do so, earned revenue is deducted from the gross costs of the programs to determine their net cost. There are no precise guidelines to determine the degree to which earned revenue can reasonably be attributed to programs. The attribution of earned revenues requires the exercise of managerial judgment.

OMB Circular No. A-136, *Financial Reporting Requirements*, requires that the presentation of the Statements of Net Cost align directly with the goals and outcomes identified in the Strategic Plan. Accordingly, Treasury Department has presented the gross costs and earned revenues by the applicable strategic goals in its fiscal years 2007 - 2012 Strategic Plan. The majority of Treasury bureaus' and reporting entities' net cost information falls within one strategic goal in the Statement of Net Cost. Two of Treasury's components, TTB and DO allocate costs to multiple programs using a net cost percentage calculation.

In the last quarter of 2008, the Treasury Department began incurring cost in association with the GSE Senior Preferred Stock Purchase Program. The amount included in the SNC as economic program entity cost is $173,737 million for fiscal year 2009 and $13,800 million for fiscal year 2008. The 2009 amount represents the current year liquidity payment of $81,800 million to the GSEs; fourth quarter liquidity payment accrual of $15,000 million payable to Fannie Mae; and accrual of $76,937 million contingent liability for future liquidity payments to GSEs. In addition, $43,931 million of preferred stock valuation loss (expense) and $5,978 million of common stock valuation gain (revenue) are reported in the SNC as non-entity. Also, reported in the SNC as non-entity revenue is $4,336 million in GSE dividends. The fiscal year 2008 amount represents the expense portion of the quarter ended September 30, 2008 accrual of the payment to Freddie Mac, which was disbursed in December 2008. There was no payment for Fannie Mae for fiscal year 2008. Nor was there a fiscal year 2009 year-end accrual to Freddie Mac as of September 30, 2009. In fiscal year 2008, Treasury disclosed these GSE costs separately as a below the line item on the SNC. However, Treasury concluded that the cost of this program helps accomplish the Treasury strategic goal of ensuring that the U.S. economy performs at its full economic potential. Thus, as of September 30, 2009 the cost of these investments in GSEs are aligned in the Economic Program section of the SNC. (See Note 9)

In fiscal year 2009, new program activity cost incurred by the OFS and SIGTARP are aligned in the Statement of Net Cost as Economic cost and Management cost, respectively. The establishment of the OFS helps to ensure that the U.S. economy performs at its full potential by stabilizing the financial system through implementation of the Financial Stability Plan. SIGTARP's objective is to promote and ensure management and organizational excellence by providing accountability and transparency. Fiscal year 2009 OFS equity program costs were $15,650 million; direct loan program costs were $26,032 million. Details of these costs are provided in Notes 8 and 12, respectively. These OFS program costs, and the GSE Senior Preferred Stock Purchase Program costs described above, comprise the major portion of Economic Program costs in the Statement of Net Cost.

As of September 30, 2009 and September 30, 2008, the Economic Program gross cost consisted of the following (in millions):

Economic Program Gross Cost	2009	2008
GSE SPSPA - Liquidity Payments	$ 81,800	$ -
GSE SPSPA - Year-End Accrual	15,000	13,800
GSE SPSPA - Contingent Commitments	76,937	-
GSE SPSPA Gross Cost	173,737	13,800
GSE MBS Subsidy, Reestimates & Admin Cost	(12,880)	-
GSE MBS - Other Intragovernmental Gross Cost	5,569	-
Total GSE SPSPA & MBS Economic Gross Cost	**$ 166,426**	**$ 13,800**
DO Combined (exluding GSE)	4,187	2,202
BEP	475	530
MNT	2,453	2,036
OCC	732	680
OFS	47,994	-
OTS	239	251
TTB	50	49
	56,130	5,748
Combined Economic Program Gross Cost	**222,556**	**19,548**
Eliminations	(12,066)	(409)
Consolidated Economic Program Gross Cost	**$ 210,490**	**$ 19,139**

The Treasury Department's SNC also presents interest expense on the Federal Debt and other federal costs incurred as a result of assets and liabilities managed on behalf of the U.S. Government. These costs are not reflected as program costs related to the Treasury Department's strategic plan missions. Such costs are eliminated in the consolidation process to the extent that they involve transactions with Treasury Department sub-organizations.

Other federal costs for the years ended September 30, 2009 and September 30, 2008 consisted of the following (in millions):

	2009	2008
Credit Reform Interest on Uninvested Funds (Intra-governmental)	$ 6,534	$ 5,043
Resolution Funding Corporation	2,120	1,393
Judgment Claims and Contract Disputes	2,305	786
Corporation for Public Broadcasting	461	448
Legal Services Corporation	388	347
All Other Payments	323	315
Total	$ 12,131	$ 8,332

24. Consolidated Statement of Net Cost and Net Costs of Treasury Sub-organizations (in millions):

For Year Ended September 30, 2009 Program Costs:	Bureau of Engraving and Printing	Bureau of the Public Debt	Departmental Offices	Financial Crimes Enforcement Network	Financial Management Service	Internal Revenue Service	U.S. Mint
Financial Program:							
Intra-governmental Gross Costs	$ 0	$ 111	$ 1,440	$ 0	$ 184	$ 4,145	$ 0
Less: Earned Revenue	0	(22)	(1,948)	0	(167)	(55)	0
Intra-governmental Net Costs	$ 0	$ 89	$ (508)	$ 0	$ 17	$ 4,090	$ 0
Gross Costs with the public	$ 0	$ 221	$ 829	$ 0	$ 1,153	$ 8,725	$ 0
Less: Earned Revenue	0	(8)	(1)	0	0	(313)	0
Net Costs with the public	$ 0	$ 213	$ 828	$ 0	$ 1,153	8,412	$ 0
Net Cost: Financial Program	**$ 0**	**$ 302**	**$ 320**	**$ 0**	**$ 1,170**	**$ 12,502**	**$ 0**
Economic Program:							
Intra-governmental Gross Costs	$ 83	$ 0	$ 12,151	$ 0	$ 0	$ 0	$ 73
Less: Earned Revenue	(3)	0	(6,146)	0	0	0	(10)
Intra-governmental Net Costs	$ 80	$ 0	$ 6,005	$ 0	$ 0	$ 0	$ 63
Gross Costs with the public	$ 392	$ 0	$ 206,456	$ 0	$ 0	$ 0	$ 2,380
Less: Earned Revenue	(481)	0	(10,824)	0	0	0	(2,456)
Net Costs with the public	$ (89)	$ 0	$ 195,632	$ 0	$ 0	$ 0	$ (76)
Net Cost: Economic Program	**$ (9)**	**$ 0**	**$ 201,637**	**$ 0**	**$ 0**	**$ 0**	**$ (13)**
Security Program:							
Intra-governmental Gross Costs	$ 0	$ 0	$ 121	$ 68	$ 0	$ 0	$ 0
Less: Earned Revenue	0	0	(16)	(1)	0	0	0
Intra-governmental Net Costs	$ 0	$ 0	$ 105	$ 67	$ 0	$ 0	$ 0
Gross Costs with the public	$ 0	$ 0	$ 147	$ 55	$ 0	$ 0	$ 0
Less: Earned Revenue	0	0	0	0	0	0	0
Net Costs with the public	$ 0	$ 0	$ 147	$ 55	$ 0	$ 0	$ 0
Net Cost: Security Program	**$ 0**	**$ 0**	**$ 252**	**$ 122**	**$ 0**	**$ 0**	**$ 0**
Management Program:							
Intra-governmental Gross Costs	$ 0	$ 56	$ 145	$ 0	$ 0	$ 0	$ 0
Less: Earned Revenue	0	(159)	(222)	0	0	0	0
Intra-governmental Net Costs	$ 0	$ (103)	$ (77)	$ 0	$ 0	$ 0	$ 0
Gross Costs with the public	$ 0	$ 104	$ 329	$ 0	$ 0	$ 0	$ 0
Less: Earned Revenue	0	0	0	0	0	0	0
Net Costs with the public	$ 0	$ 104	$ 329	$ 0	$ 0	$ 0	$ 0
Net Cost: Management Program	**$ 0**	**$ 1**	**$ 252**	**$ 0**	**$ 0**	**$ 0**	**$ 0**
Net Cost of Operations	$ (9)	$ 303	$ 202,461	$ 122	$ 1,170	$ 12,502	$ (13)

24. Consolidated Statement of Net Cost and Net Costs of Treasury Sub-organizations (in millions):

For Year Ended September 30, 2009 Program Costs:	Office of the Comptroller of the Currency	Office of Thrift Supervision	Alcohol, Tobacco Tax and Trade Bureau	Combined Total	Eliminations and Adjustments	9/30/2009 Consolidated
Financial Program:						
Intra-governmental Gross Costs	$ 0	$ 0	$ 14	$ 5,894	$ (1,548)	$ 4,346
Less: Earned Revenue	0	0	0	(2,192)	258	(1,934)
Intra-governmental Net Costs	$ 0	$ 0	$ 14	$ 3,702	$ (1,290)	$ 2,412
Gross Costs with the public	$ 0	$ 0	$ 39	$ 10,967	$ 0	$ 10,967
Less: Earned Revenue	0	0	(2)	(324)	0	(324)
Net Costs with the public	$ 0	$ 0	$ 37	$ 10,643	$ 0	$ 10,643
Net Cost: Financial Program	**$ 0**	**$ 0**	**$ 51**	**$ 14,345**	**$ (1,290)**	**$ 13,055**
Economic Program:						
Intra-governmental Gross Costs	$ 100	$ 37	$ 13	$ 12,457	$ (12,066)	$ 391
Less: Earned Revenue	(22)	(11)	0	(6,192)	6,166	(26)
Intra-governmental Net Costs	$ 78	$ 26	$ 13	$ 6,265	$ (5,900)	$ 365
Gross Costs with the public	$ 632	$ 202	$ 37	$ 210,099	$ 0	$ 210,099
Less: Earned Revenue	(752)	(245)	(0)	(14,758)	(1)	(14,759)
Net Costs with the public	$ (120)	$ (43)	$ 37	$ 195,341	$ (1)	$ 195,340
Net Cost: Economic Program	**$ (42)**	**$ (17)**	**$ 50**	**$ 201,606**	**$ (5,901)**	**$ 195,705**
Security Program:						
Intra-governmental Gross Costs	$ 0	$ 0	$ 0	$ 189	$ (66)	$ 123
Less: Earned Revenue	0	0	0	(17)	14	(3)
Intra-governmental Net Costs	$ 0	$ 0	$ 0	$ 172	$ (52)	$ 120
Gross Costs with the public	$ 0	$ 0	$ 0	$ 202	$ 0	$ 202
Less: Earned Revenue	0	0	0	0	0	0
Net Costs with the public	$ 0	$ 0	$ 0	$ 202	$ 0	$ 202
Net Cost: Security Program	**$ 0**	**$ 0**	**$ 0**	**$ 374**	**$ (52)**	**$ 322**
Management Program:						
Intra-governmental Gross Costs	$ 0	$ 0	$ 0	$ 201	$ (65)	$ 136
Less: Earned Revenue	0	0	0	(381)	321	(60)
Intra-governmental Net Costs	$ 0	$ 0	$ 0	$ (180)	$ 256	$ 76
Gross Costs with the public	$ 0	$ 0	$ 0	$ 433	$ 0	$ 433
Less: Earned Revenue	0	0	0	0	0	0
Net Costs with the public	$ 0	$ 0	$ 0	$ 433	$ 0	$ 433
Net Cost: Management Program	**$ 0**	**$ 0**	**$ 0**	**$ 253**	**$ 256**	**$ 509**
Net Cost of Operations	**$ (42)**	**$ (17)**	**$ 101**	**$ 216,578**	**$ (6,987)**	**$ 209,591**

24. Consolidated Statement of Net Cost and Net Costs of Treasury Sub-organizations (in millions):

Fiscal Year Ended September 30, 2008 Program Costs:	Bureau of Engraving and Printing	Bureau of the Public Debt	Departmental Offices	Financial Crimes Enforcement Network	Financial Management Service	Internal Revenue Service	U.S. Mint
Financial Program:							
Intra-governmental Gross Costs	$ 0	$ 71	$ 1,392	$ 0	$ 202	$ 4,107	$ 0
Less: Earned Revenue	0	(15)	(2,009)	0	(159)	(72)	0
Intra-governmental Net Costs	$ 0	$ 56	$ (617)	$ 0	$ 43	$ 4,035	$ 0
Gross Costs with the public	$ 0	$ 256	$ 373	$ 0	$ 1,120	$ 8,441	$ 0
Less: Earned Revenue	0	(10)	(1)	0	0	(287)	0
Net Costs with the public	$ 0	$ 246	$ 372	$ 0	$ 1,120	$ 8,154	$ 0
Net Cost: Financial Program	**$ 0**	**$ 302**	**$ (245)**	**$ 0**	**$ 1,163**	**$ 12,189**	**$ 0**
Economic Program:							
Intra-governmental Gross Costs	$ 81	$ 0	$ 14,262	$ 0	$ 0	$ 0	$ 78
Less: Earned Revenue	(8)	0	(811)	0	0	0	(10)
Intra-governmental Net Costs	$ 73	$ 0	$ 13,451	$ 0	$ 0	$ 0	$ 68
Gross Costs with the public	$ 449	$ 0	$ 1,740	$ 0	$ 0	$ 0	$ 1,958
Less: Earned Revenue	(509)	0	(1,529)	0	0	0	(2,063)
Net Costs with the public	$ (60)	$ 0	$ 211	$ 0	$ 0	$ 0	$ (105)
Net Cost: Economic Program	**$ 13**	**$ 0**	**$ 13,662**	**$ 0**	**$ 0**	**$ 0**	**$ (37)**
Security Program:							
Intra-governmental Gross Costs	$ 0	$ 0	$ 139	$ 58	$ 0	$ 0	$ 0
Less: Earned Revenue	0	0	(18)	(2)	0	0	0
Intra-governmental Net Costs	$ 0	$ 0	$ 121	$ 56	$ 0	$ 0	$ 0
Gross Costs with the public	$ 0	$ 0	$ 171	$ 52	$ 0	$ 0	$ 0
Less: Earned Revenue	0	0	0	0	0	0	0
Net Costs with the public	$ 0	$ 0	$ 171	$ 52	$ 0	$ 0	$ 0
Net Cost: Security Program	**$ 0**	**$ 0**	**$ 292**	**$ 108**	**$ 0**	**$ 0**	**$ 0**
Management Program:							
Intra-governmental Gross Costs	$ 0	$ 51	$ 143	$ 0	$ 0	$ 0	$ 0
Less: Earned Revenue	0	(237)	(224)	0	0	0	0
Intra-governmental Net Costs	$ 0	$ (186)	$ (81)	$ 0	$ 0	$ 0	$ 0
Gross Costs with the public	$ 0	$ 207	$ 300	$ 0	$ 0	$ 0	$ 0
Less: Earned Revenue	0	0	0	0	0	0	0
Net Costs with the public	$ 0	$ 207	$ 300	$ 0	$ 0	$ 0	$ 0
Net Cost: Management Program	**$ 0**	**$ 21**	**$ 219**	**$ 0**	**$ 0**	**$ 0**	**$ 0**
Net Cost of Treasury Operations	$ 13	$ 323	$ 13,928	$ 108	$ 1,163	$ 12,189	$ (37)

24. Consolidated Statement of Net Cost and Net Costs of Treasury Sub-organizations (in millions):

Fiscal Year Ended September 30, 2008 Program Costs:	Office of the Comptroller of the Currency	Office of Thrift Supervision	Alcohol, Tobacco Tax and Trade Bureau	Combined Total	Eliminations and Adjustments	9/30/2008 Consolidated
Financial Program:						
Intra-governmental Gross Costs	$ 0	$ 0	$ 13	$ 5,785	$ (1,442)	$ 4,343
Less: Earned Revenue	0	0	0	(2,255)	272	(1,983)
Intra-governmental Net Costs	$ 0	$ 0	$ 13	$ 3,530	$ (1,170)	$ 2,360
Gross Costs with the public	$ 0	$ 0	$ 36	$ 10,226	$ 0	$ 10,226
Less: Earned Revenue	0	0	(1)	(299)	0	(299)
Net Costs with the public	$ 0	$ 0	$ 35	$ 9,927	$ 0	$ 9,927
Net Cost: Financial Program	$ **0**	$ **0**	$ **48**	$ **13,457**	$ **(1,170)**	$ **12,287**
Economic Program:						
Intra-governmental Gross Costs	$ 96	$ 34	$ 13	$ 14,564	$ (409)	$ 14,155
Less: Earned Revenue	(27)	(14)	0	(870)	845	(25)
Intra-governmental Net Costs	$ 69	$ 20	$ 13	$ 13,694	$ 436	$ 14,130
Gross Costs with the public	$ 584	$ 217	$ 36	$ 4,984	$ 0	$ 4,984
Less: Earned Revenue	(710)	(254)	(1)	(5,066)	0	(5,066)
Net Costs with the public	$ (126)	$ (37)	$ 35	$ (82)	$ 0	$ (82)
Net Cost: Economic Program	$ **(57)**	$ **(17)**	$ **48**	$ **13,612**	$ **436**	$ **14,048**
Security Program:						
Intra-governmental Gross Costs	$ 0	$ 0	$ 0	$ 197	$ (74)	$ 123
Less: Earned Revenue	0	0	0	(20)	16	(4)
Intra-governmental Net Costs	$ 0	$ 0	$ 0	$ 177	$ (58)	$ 119
Gross Costs with the public	$ 0	$ 0	$ 0	$ 223	$ 0	$ 223
Less: Earned Revenue	0	0	0	0	0	0
Net Costs with the public	$ 0	$ 0	$ 0	$ 223	$ 0	$ 223
Net Cost: Security Program	$ **0**	$ **0**	$ **0**	$ **400**	$ **(58)**	$ **342**
Management Program:						
Intra-governmental Gross Costs	$ 0	$ 0	$ 0	$ 194	$ (70)	$ 124
Less: Earned Revenue	0	0	0	(461)	296	$ (165)
Intra-governmental Net Costs	$ 0	$ 0	$ 0	$ (267)	$ 226	$ (41)
Gross Costs with the public	$ 0	$ 0	$ 0	$ 507	$ 0	$ 507
Less: Earned Revenue	0	0	0	0	0	0
Net Costs with the public	$ 0	$ 0	$ 0	$ 507	$ 0	$ 507
Net Cost: Management Program	$ **0**	$ **0**	$ **0**	$ **240**	$ **226**	$ **466**
Net Cost of Treasury Operations	$ (57)	$ (17)	$ 96	$ 27,709	$ (566)	$ 27,143

25. ADDITIONAL INFORMATION RELATED TO THE COMBINED STATEMENTS OF BUDGETARY RESOURCES

Federal agencies are required to disclose additional information related to the Combined Statements of Budgetary Resources (per OMB Circular No. A-136). In accordance with SFFAS No. 7, the Department must report the value of goods and services ordered and obligated which have not been received. This amount includes any orders for which advance payment has been made but for which delivery or performance has not yet occurred. The information for the fiscal years ended September 30, 2009 and September 30, 2008 was as follows (in millions):

	2009	2008
Undelivered orders:		
Paid	$ 171	$ 1,888
Unpaid	185,641	55,625
Undelivered orders at the end of the year	**$ 185,812**	**$ 57,513**

	2009	2008
Contributed Capital	$ 40	$ 24

Apportionment Categories of Obligations Incurred:
Direct vs. Reimbursable Obligations

	2009	2008
Obligations Incurred		
Direct - Category A	$ 14,715	$ 7,050
Direct - Category B	977,506	20,623
Direct - Exempt from Apportionment	390,305	455,126
Total Direct	**1,382,526**	**482,799**
Reimbursable - Category A	1	2
Reimbursable - Category B	3,386	3,287
Reimbursable - Exempt from Apportionment	1,282	1,446
Total Reimbursable	**4,669**	**4,735**
Total Direct and Reimbursable	**$ 1,387,195**	**$ 487,534**

TERMS OF BORROWING AUTHORITY USED

The GSE MBS Purchase and TARP equity investment programs (excluding HAMP) have authority to borrow under the *Federal Credit Reform Act of 1990* (FCRA), as amended. The FFB and IAP also have borrowing authority. The FCRA provides indefinite borrowing authority to financing accounts to fund the unsubsidized portion of direct loans and to satisfy obligations in the event the financing account's resources are insufficient. Repayment requirements are defined by OMB Circular A-11. Interest expense due is calculated based on the beginning balance of borrowings outstanding and the borrowings/repayments activity that occurred during the fiscal year. Undisbursed Treasury Department borrowings earn interest at the same rate as the financing account pays on its debt owed to BPD. In the event that principal and interest collections exceed the interest expense due, the excess will be repaid to the Treasury Department. If principal and interest do not exceed interest expense due, the Treasury Department will borrow the difference. The Treasury Department makes periodic principal repayments based on the analysis of cash balances and future disbursement needs. All interest on borrowing were due the last day of the fiscal year, on September 30, 2009. Interest rates on FCRA borrowings range from 1.00% to 6.48%.

Available Borrowing, End of Year:

	2009	2008
Beginning Balance	$ 29,810	$ 5,716
Current Authority	548,734	34,308
Decreases	(107,475)	(4,767)
Borrowing Authority Converted to Cash	(419,559)	(5,447)
Ending Balance	**$ 51,510**	**$ 29,810**

Reconciliation of the President's Budget

The *Budget of the United States* (also known as the President's Budget), with actual numbers for fiscal year 2009, was not published at the time that these financial statements were issued. The President's Budget is expected to be published in 2010. It will be available from the United States Government Printing Office. The following chart displays the differences between the Combined Statement of Budgetary Resources (SBR) in the fiscal year 2008 *Performance and Accountability Report* and the actual fiscal year 2008 balances included in the fiscal year 2010 President's Budget (PB).

RECONCILIATION OF FISCAL YEAR 2008 COMBINED STATEMENT OF BUDGETARY RESOURCES TO THE FISCAL YEAR 2010 PRESIDENT'S BUDGET (IN MILLIONS)

	Budgetary Resources	Outlays (net of offsetting collections)	Offsetting Receipts	Net Outlays	Obligations Incurred
Statement of Budgetary Resources Amounts	$ 772,164	$ 479,079	$ (16,211)	$ 462,868	$ 487,534
Included in the Treasury Department Chapter of the President's Budget (PB) but not in the Statement of Budgetary Resources (SBR):					
IRS non-entity tax credit payments (1)	94,505	94,506	(21)	94,485	94,506
Tax and Trade Bureau (TTB) non-entity collections for Puerto Rico	373	373	0	373	373
Non-Treasury offsetting receipts included in Treasury chapter of PB	0	0	(35)	(35)	0
Treasury offsetting receipts considered to be "General Fund" transactions for reporting purposes (2)	0	0	(214)	(214)	0
Continued dumping subsidy – CBP	396	265	0	265	265
Other	2	(2)	0	(2)	0
Subtotal	95,276	95,142	(270)	94,872	95,144
Included in the SBR but not in the Treasury Department chapter of the PB:					
Treasury resources shown in non-Treasury chapters of the PB, included in SBR (3)	(29,532)	(3,359)	0	(3,359)	(3,018)
Offsetting collections net of collections shown in PB	(8,246)	0	(640)	(640)	0
Treasury offsetting receipts shown in other chapters of PB, part of which is in SBR	0	0	147	147	0
Unobligated balance carried forward, recoveries of prior year funds and expired accounts	(1,332)	0	0	0	(19)
Exchange Stabilization Fund resources not shown in PB (4)	(30,576)	0	0	0	(247)
Treasury Financing Accounts (CDFI and ATSB)	(34,312)	(5,074)	0	(5,074)	(5,415)
IRS user fees and 50% Transfer Accounts and Capital Transfers to General Fund not included in PB	4,798	0	0	0	0
Other	5	(1)	0	(1)	(3)
Subtotal	(99,195)	(8,434)	(493)	(8,927)	(8,702)
Trust Fund – Comptroller of the Currency (OCC)	(81)	81	0	81	0
President's Budget Amounts*	$ 768,164	$ 565,868	$ (16,974)	$ 548,894	$ 573,976

1. These are primarily Earned Income Tax Credit and Child Tax Credit payments that are reported with refunds as custodial activities in Treasury's financial statements and thus are not reported as budgetary resources.
2. These are receipt accounts that Treasury manages on behalf of other agencies and considered to be "General Fund" receipts rather than receipts of the Treasury Department reporting entity.
3. The largest of these resources relate to Treasury's International Assistance Programs.
4. Exchange Stabilization Fund (ESF) is a self-sustaining component that finances its operations with the buying and selling of foreign currencies to regulate the fluctuations of the dollar. Because of the nature of the activities of the component, it does not receive appropriations, and therefore is excluded from the PB.

* Per President's Budget for fiscal year 2010 – Budgetary Resources and Outlays are from the Analytical Perspective. Offsetting Receipts and Obligations Incurred are from the Appendix.

LEGAL ARRANGEMENTS AFFECTING USE OF UNOBLIGATED BALANCES

The use of unobligated balances is restricted based on annual legislation requirements or enabling authorities. Funds are presumed to be available for only one fiscal year unless otherwise noted in the annual appropriation language. Unobligated balances in unexpired fund symbols are available in the next fiscal year for new obligations unless some restrictions had been placed on those funds by law. In those situations, the restricted funding will be temporarily unavailable until such time as the reasons for the restriction have been satisfied or legislation has been enacted to remove the restriction.

Amounts in expired fund symbols are not available for new obligations, but may be used to adjust obligations and make disbursements that were recorded before the budgetary authority expired or to meet a bona fide need that arose in the fiscal year for which the appropriation was made.

26. COLLECTION AND DISPOSITION OF CUSTODIAL REVENUE

The Treasury Department collects the majority of federal revenue from income and excise taxes. Collection activity, by revenue type and tax year, was as follows for the years ended September 30, 2009 and September 30, 2008 (in millions):

	Tax Year				
	2009	2008	2007	Pre-2007	2009 Collections
Individual Income and FICA Taxes	$ 1,296,427	$ 702,557	$ 22,250	$ 15,323	$ 2,036,557
Corporate Income Taxes	138,144	69,016	1,692	16,630	225,482
Estate and Gift Taxes	92	3,979	796	19,810	24,677
Excise Taxes	54,502	12,512	102	132	67,248
Railroad Retirement Taxes	3,559	1,148	3	1	4,711
Unemployment Taxes	4,772	1,859	36	98	6,765
Federal Reserve Banks Earnings	24,552	9,766	0	0	34,318
Beneficial Interest in AIG Trust	23,472	0	0	0	23,472
Fines, Penalties, Interest, and Other Revenue	1,892	37	0	0	1,929
Subtotal	**$ 1,547,412**	**$ 800,874**	**$ 24,879**	**$ 51,994**	**$ 2,425,159**
Less Amounts Collected for Non-federal Entities					(487)
Total					**$ 2,424,672**

	Tax Year				
	2008	2007	2006	Pre-2006	2008 Collections
Individual Income and FICA Taxes	$ 1,455,017	$ 799,244	$ 23,498	$ 16,567	$ 2,294,326
Corporate Income Taxes	222,000	113,949	2,010	16,104	354,063
Estate and Gift Taxes	23	19,248	1,266	9,287	29,824
Excise Taxes	48,106	17,909	119	159	66,293
Railroad Retirement Taxes	3,769	1,164	1	5	4,939
Unemployment Taxes	5,146	2,026	42	117	7,331
Federal Reserve Banks Earnings	25,879	7,719	0	0	33,598
Fines, Penalties, Interest, and Other Revenue	1,936	297	0	0	2,233
Subtotal	**$ 1,761,876**	**$ 961,556**	**$ 26,936**	**$ 42,239**	**$ 2,792,607**
Less Amounts Collected for Non-federal Entities					(407)
Total					**$ 2,792,200**

Amounts reported for Corporate Income Taxes collected in fiscal year 2009 include corporate taxes of $9 billion for tax year 2010 (similarly, amounts reported for Corporate Income Taxes collected in fiscal year 2008 include corporate taxes of $10 billion for tax year 2009). Individual Income and FICA Taxes includes $83 billion in payroll taxes collected from other federal agencies ($79 billion in fiscal year 2008).

Amounts Provided to Fund the Federal Government

For the years ended September 30, 2009 and September 30, 2008, collections of custodial revenue transferred to other entities were as follows (in millions):

	2009	2008
Department of the Interior	$ 487	$ 407
General Fund	1,963,228	2,366,126
Total	**$ 1,963,715**	**$ 2,366,533**

Federal Tax Refunds Paid

Refund activity, broken out by revenue type and by tax year, was as follows for the years ended September 30, 2009 and September 30, 2008 (in millions):

	Tax Year				
	2009	2008	2007	Pre-2007	2009 Refunds
Individual Income and FICA Taxes	$ 1,075	$ 293,971	$ 30,361	$ 14,222	$ 339,629
Corporate Income Taxes	6,626	32,646	17,370	38,558	95,200
Estate and Gift Taxes	0	324	566	358	1,248
Excise Taxes	535	541	81	626	1,783
Railroad Retirement Taxes	0	2	0	1	3
Unemployment Taxes	1	66	13	29	109
Total	**$ 8,237**	**$ 327,550**	**$ 48,391**	**$ 53,794**	**$ 437,972**

	Tax Year				
	2008	2007	2006	Pre-2006	2008 Refunds
Individual Income and FICA Taxes	$ 935	$ 342,216	$ 19,217	$ 6,980	$ 369,348
Corporate Income Taxes	2,206	19,610	10,446	22,078	54,340
Estate and Gift Taxes	0	343	428	251	1,022
Excise Taxes	439	497	107	208	1,251
Railroad Retirement Taxes	0	1	1	(9)	(7)
Unemployment Taxes	1	65	14	39	119
Fines, Penalties, Interest, and Other Revenue	1	0	0	0	1
Total	**$ 3,582**	**$ 362,732**	**$ 30,213**	**$ 29,547**	**$ 426,074**

Federal Tax Refunds Payable

As of September 30, 2009 and September 30, 2008, refunds payable to taxpayers consisted of the following (in millions):

	2009	2008
Alcohol, Tobacco Tax and Trade Bureau	$ 9	$ 12
Internal Revenue Service	4,031	3,064
Total	**$ 4,040**	**$ 3,076**

27. EARMARKED FUNDS

Earmarked funds are financed by specifically identified revenues, 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 or purposes. SFFAS No. 27, *Identifying and Reporting Earmarked Funds*, issued by the FASAB defines the following three criteria for determining an earmarked fund: 1) A statute committing the Federal Government to use specifically identified revenues and other financing sources only for designated activities, benefits or purposes; 2) Explicit authority for the earmarked fund to retain revenues and other financing sources not used in the current period for future use to finance the designated activities, benefits, or purposes; and 3) A requirement to account for and report on the receipt, use, and retention of the revenues and other financing sources that distinguishes the earmarked fund from the government's general revenues.

The majority of Treasury Department's earmarked fund activities are attributed to the ESF and the pension and retirement funds managed by the Office of DCP. In addition, several Treasury bureaus operate with "public enterprise revolving funds" and receive no appropriations from the Congress. These bureaus are BEP, U.S. Mint, OCC, and OTS. Other miscellaneous earmarked funds are managed by BPD, DO, FMS, IRS, and TFF.

The following is a list of earmarked funds and a brief description of the purpose, accounting, and uses of these funds.

Exchange Stabilization Fund (ESF)		
ESF	20X4274	ESF Money Market Guaranty Facility
ESF	20X4444	Exchange Stabilization Fund

D.C. Pensions		
DCP	20X1713	Federal payment – D.C. Judicial Retirement
DCP	20X1714	Federal payment – D.C. Federal Pension Fund
DCP	20X5511	D.C. Federal Pension Fund
DCP	20X8212	D.C. Judicial Retirement and Survivor's Annuity Fund

Public Enterprise Revolving Funds		
BEP	20X4502	Bureau of Engraving and Printing Fund
MNT	20X4159	Public Enterprise Revolving Fund
OCC	20X8413	Assessment Funds
OTS	20X4108	Public Enterprise Revolving Fund
IRS	20X4413	Federal Tax Lien Revolving Fund

Other Earmarked Funds		
BPD	20X5080	Gifts to Reduce Public Debt
DO	20X5407	Sallie Mae Assessments
DO	20X5816	Confiscated and Vested Iraqi Property and Assets
DO	20X8790	Gifts and Bequests Trust Fund
FMD	205445	Debt Collection
FMD	20X5081	Presidential Election Campaign
FMD	20X8902	Esther Cattell Schmitt Gift Fund

FMS	203/45445	Debt Collection Special Fund
FMS	204/55445	Debt Collection Special Fund
FMS	205/65445	Debt Collection Special Fund
FMS	206/75445	Debt Collection Special Fund
FMS	207/85445	Debt Collection Special Fund
FMS	208/95445	Debt Collection Special Fund
FMS	209/05445	Debt Collection Special Fund
IRS	20X5510	Private Collection Agent Program
IRR	20x5433	Informant Reimbursement
TFF	20X5697	Treasury Forfeiture Fund

The ESF uses funds to purchase or sell foreign currencies, to hold U.S. foreign exchange and SDR assets, and to provide financing to foreign governments. ESF accounts and reports its holdings to FMS on the SF224, "Statement of Transactions," as well as to the Congress and Treasury Department's policy office. The *Gold Reserve Act of 1934*, *Bretton Woods Agreement Act of 1945*, P.L. 95-147 and P.L. 94-564 established and authorized the use of the Fund. SDR in the IMF, Investments in U.S. Securities (BPD), and Investments in Foreign Currency Denominated Assets are the sources of revenues or other financing sources. ESF's earnings and realized gains on foreign currency denominated assets represent inflows of resources to the government, and the revenues earned are the result of intra-governmental inflows.

D.C. Pension Funds provide annuity payments for retired D.C. teachers, police officers, judges, and firefighters. The sources of revenues are through annual appropriations, employees' contributions, and interest earnings from investments. All proceeds are earmarked. Note 21 provides detailed information on various funds managed by the Office of DCP.

Treasury Department's four non-appropriated bureaus, BEP, Mint, OCC, and OTS, operate "public enterprise funds" that account for the revenue and expenses related to the production and sale of numismatic products and circulating bureaus coinage (Mint), the currency printing activities (BEP), and support of oversight functions of banking (OCC) and thrift operations (OTS). 31 USC § 5142 established the revolving fund for BEP to account for revenue and expenses related to the currency printing activities. Public Law 104-52 (31 USC § 5136) established the Public Enterprise Fund for the Mint to account for all revenue and expenses related to the production and sale of numismatic products and circulating coinage. Revenues and other financing sources at the Mint are mainly from the sale of numismatic and bullion coins, and the sale of circulating coins to the Federal Reserve Bank system. 12 USC § 481 established the Assessment Funds for OCC, and 103 Stat. 278 established the Public Enterprise Revolving Fund for OTS. Revenue and financing sources are from the bank examination and assessments for the oversight of the national banks, savings associations, and savings and loan holding companies. These earmarked funds do not directly contribute to the inflows of resources to the government; however, revenues in excess of costs are returned to the General Fund of the U.S. Government. There are minimal transactions with other government agencies.

There are other earmarked funds at several Treasury bureaus, such as donations to the Presidential Election Campaign Fund, funds related to the debt collection program, gifts to reduce the public debt, and other enforcement related activities. Public laws, statutory laws, U.S. Code, and the *Debt Collection Improvement Act* established and authorized the use of these funds. Sources of revenues and other financing sources include contributions, cash and property forfeited in enforcement activities, public donations, and debt collection.

INTRA-GOVERNMENTAL INVESTMENTS IN TREASURY SECURITIES

The Federal Government does not set aside assets to pay future benefits or other expenditures associated with earmarked funds. Treasury Department bureaus and other federal agencies invest some of the earmarked funds that they collect from the public. The funds are invested in securities issued by Treasury Department's Bureau of the Public Debt (BPD). The cash collected by BPD is deposited in the General Fund of the U.S. Government, which uses the cash for general government purposes.

The investments provide Treasury Department bureaus and other federal agencies with authority to draw upon the General Fund of the U.S. Government to make future benefit payments or other expenditures. When the Treasury Department bureaus or other federal agencies require redemption of these securities to make expenditures, the government finances those expenditures out of accumulated cash balances, by raising taxes or other receipts, by borrowing from the public or repaying less debt, or by curtailing other expenditures. This is the same way that the government finances all other expenditures.

The securities are an asset to the Treasury Department bureaus and other federal agencies and a liability of the BPD. The General Fund of the U.S. Government is liable to BPD. Because the Treasury Department bureaus and other federal agencies are parts of the U.S. Government, these assets and liabilities offset each other from the standpoint of the government as a whole. For this reason, they do not represent an asset or a liability in the U.S. Government-wide financial statements.

The balances related to the investments made by the Treasury Department bureaus are not displayed on the Treasury Department's financial statements because the bureaus are subcomponents of the Treasury Department. However, the General Fund of the U.S. Government remains liable to BPD for the invested balances and BPD remains liable to the investing Treasury Department bureaus (see Note 4).

Summary Information for Earmarked Funds as of and for the Year ended September 30, 2009 (in millions):

	Exchange Stabilization Fund	D.C. Pensions	Public Enterprise Revolving Funds	Other Earmarked Funds	Combined Earmarked Funds	Eliminations*	9/30/2009 Totals
Balance Sheet							
ASSETS:							
Fund Balance	$ 0	$ 0	$ 573	$ 312	$ 885	$ 0	$ 885
Investments/Related Interest (Intra-governmental)	19,816	3,866	1,346	707	25,735	25,735	0
Cash, Foreign Currency/Other Monetary Assets	71,662	0	0	18	71,680	0	71,680
Investments and Related Interest	13,537	0	0	0	13,537	0	13,537
Other Assets	0	13	1,207	104	1,324	10	1,314
Total Assets	**$ 105,015**	**$ 3, 879**	**$ 3,126**	**$ 1,141**	**$ 113,161**	**$ 25,745**	**$ 87,416**
LIABILITIES:							
Intra-governmental Liabilities	0	0	37	194	231	28	203
Certificates Issued to Federal Reserve Banks	5,200	0	0	0	5,200	0	5,200
Allocation of Special Drawing Rights	55,953	0	0	0	55,953	0	55,953
Other Liabilities	16	9,104	623	181	9,924	0	9,924
Total Liabilities	61,169	9,104	660	375	71,308	28	71,280
NET POSITION:							
Unexpended Appropriations	200	0	0	0	200	0	200
Cumulative Results of Operations	43,646	(5,225)	2,466	766	41,653	0	41,653
Total Liabilities and Net Position	**$ 105,015**	**$ 3,879**	**$ 3,126**	**$ 1,141**	**$ 113,161**	**$ 28**	**$ 113,133**
Statement of Net Cost							
Gross Cost	$ 1,117	$ 785	$ 3,899	$ 214	$ 6,015	$ 60	$5,955
Less Earned Revenue	(4,951)	(134)	(3,981)	0	(9,066)	(187)	(8,879)
Total Net Cost of Operations	**$ (3,834)**	**$ 651**	**$ (82)**	**$ 214**	**$ (3,051)**	**$ (127)**	**$ (2,924)**
Cumulative Results of Operations							
Beginning Balance, as adjusted	$ 39,618	$ (4,982)	$ 2,350	$ 575	$ 37,561	$ 0	$ 37,561
Budgetary Financing Sources	194	408	0	345	947	1	946
Other Financing Sources	0	0	34	60	94	(27)	121
Total Financing Sources	194	408	34	405	1,041	(26)	1,067
Net Cost of Operations	3,834	(651)	82	(214)	3,051	127	2,924
Net Change	4,028	(243)	116	191	4,092	101	3,991
Total Cumulative Results of Operations	**$ 43,646**	**$ (5,225)**	**$ 2,466**	**$ 766**	**$ 41,653**	**$ 101**	**$ 41,552**

* The eliminations reported above include both inter and intra eliminations for the Earmarked Funds. The total eliminations amount will not agree with the eliminations reported in the Statement of Changes in Net Position, which include eliminations for Other Funds.

Summary Information for Earmarked Funds as of and for the Year ended September 30, 2008 (in millions):

	Exchange Stabilization Fund	D.C. Pensions	Public Enterprise Revolving Funds	Other Earmarked Funds	Combined Earmarked Funds	Eliminations*	9/30/2008 Totals
Balance Sheet							
ASSETS:							
Fund Balance	$ 33	$ 0	$ 459	$ 228	$ 720	$ 0	$ 720
Investments/Related Interest Intra-governmental	16,847	3,859	1,251	592	22,549	22,549	0
Cash, Foreign Currency/Other Monetary Assets	22,221	0	0	16	22,237	0	22,237
Investments and Related Interest	10,543	0	0	0	10,543	0	10,543
Other Assets	298	16	1,292	133	1,739	9	1,730
Total Assets	**$ 49,942**	**$ 3,875**	**$ 3,002**	**$ 69**	**$ 57,788**	**$ 22,558**	**$ 35,230**
LIABILITIES:							
Intra-governmental Liabilities	$ 0	$ 0	$ 37	$ 150	$ 187	$ 29	$ 158
Certificates Issued to Federal Reserve	2,200	0	0	0	2,200	0	2,200
Allocation of Special Drawing Rights	7,630	0	0	0	7,630	0	7,630
Other Liabilities	330	8,856	617	182	9,985	0	9,985
Total Liabilities	$ 10,160	$ 8,856	$ 654	$ 332	$ 20,002	$ 29	$ 19,973
NET POSITION:							
Unexpended Appropriations	$ 200	$ 0	$ 0	$ 0	$ 200	$ 0	$ 200
Cumulative Results of Operations	39,582	(4,981)	2,348	637	37,586	0	37,586
Total Liabilities and Net Position	**$ 49,942**	**$ 3,875**	**$ 3,002**	**$ 969**	**$ 57,788**	**$ 29**	**$ 57,759**
Statement of Net Cost							
Gross Cost	$ 250	$ 339	$ 3,496	$ 337	$ 4,422	$ 62	$ 4,360
Less Earned Revenue	(1,986)	(152)	(3,593)	(6)	(5,737)	(650)	(5,087)
Total Net Cost of Operations	**$ (1,736)**	**$ 187**	**$ (97)**	**$ 331**	**$ (1,315)**	**$ (588)**	**$ (727)**
Cumulative Results of Operations							
Beginning Balance	$ 37,846	$ (5,141)	$ 2,206	$ 474	$ 35,385	$ 0	$ 35,385
Budgetary Financing Sources	0	347	0	442	789	23	766
Other Financing Sources	0	0	45	52	97	(31)	128
Total Financing Sources	0	347	45	494	886	(8)	894
Net Cost of Operations	1,736	(187)	97	(331)	1,315	588	727
Net Change	1,736	160	142	163	2,201	580	1,621
Total Cumulative Results of Operations	**$ 39,582**	**$ (4,981)**	**$ 2,348**	**$ 637**	**$ 37,586**	**$ 580**	**$ 37,006**

* The eliminations reported above include both inter and intra eliminations for the Earmarked Funds. The total eliminations amount will not agree with the eliminations reported in the Statement of Changes in Net Position, which include eliminations for Other Funds.

28. RECONCILIATION OF NET COST OF OPERATIONS TO BUDGET

The Reconciliation of Net Cost of Operations to Budget explains the difference between the budgetary net obligations and the proprietary net cost of operations. For fiscal years 2009 and 2008, OMB did not prescribe a format for this reconciliation in OMB Circular No. A-136, *Financial Reporting Requirements*, as amended, so that preparers might develop a more robust presentation tailored to their agency. As of September 30, 2009 and September 30, 2008, the Reconciliation of Net Cost of Operations to Budget consisted of the following (in millions):

	2009	2008
RESOURCES USED TO FINANCE ACTIVITIES:		
Budgetary Resources Obligated:		
Obligations Incurred	$ 1,387,195	$ 487,534
Less: Spending Authority from Offsetting Collections and Recoveries	(321,262)	(9,401)
Obligations Net of Offsetting Collections and Recoveries	1,065,933	478,133
Less: Offsetting Receipts	(44,614)	(16,211)
Net Obligations	**$ 1,021,319**	**$ 461,922**
Other Resources:		
Donations and Forfeiture of Property	127	112
Financing Sources for Accrued and Discount on the Debt	6,027	(3,870)
Transfers In/Out Without Reimbursement	(36)	(21)
Imputed Financing from Cost Absorbed by Others	793	729
Transfers to the General Fund and Other (Note 23)	(217,704)	(20,788)
Net Other Resources Used to Finance Activities	(210,793)	(23,838)
Total Resources Used to Finance Activities (Note 1 AC)	**$ 810,526**	**$ 438,084**
RESOURCES USED TO FINANCE ITEMS NOT PART OF THE NET COST OF OPERATIONS:		
Change in Budgetary Resources Obligated for Goods, Services, and Benefits Ordered but not yet Provided	$ 49,063	$ 1,229
Credit Program Collections that Increase Liabilities for Loans Guarantees or Allowances for Subsidy	(6)	(5)
Adjustment to Accrued Interest and Discount on the Debt	8,687	(6,731)
Other (primarily resources that finance the acquisition of assets or liquidation of liabilities)	320,755	(10,745)
Total Resources Used to Finance Items Not Part of the Net Cost of Operations	378,499	(16,252)
Total Resources Used to Finance the Net Cost of Operations (Note 1 AC)	**$ 432,027**	**$ 454,336**
Total Components of Net Cost of Operations that will Require or Generate Resources in Future Periods (Note 1 AC)	87,673	13,814
Total Components of Net Cost of Operations that will not Require or Generate Resources	3,232	1,201
Total Components of Net Cost of Operations that will not Require or Generate Resources in the Current Period (Note 1 AC)	**90,905**	**15,015**
Net Cost of Operations	**$ 522,932**	**$ 469,351**

29. FINANCIAL STABILITY AND STIMULUS ACTIVITIES

GOVERNMENT SPONSORED ENTERPRISES (GSEs)

The Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac) are stockholder-owned GSEs. Congress established these GSEs to increase the supply of mortgage loans and to reduce the accompanying costs. A key responsibility is to package purchased mortgages into securities. These securities are subsequently sold to investors. Proceeds from sales are used to buy additional mortgages and keep money flowing through the mortgage markets.

Increasingly difficult conditions in the housing market challenged the soundness and profitability of GSEs, thereby undermining the entire housing market. This led Congress to pass the *Housing and Economic Recovery Act of 2008* in July 2008 (HERA). This Act created the new Federal Housing Finance Agency (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 GSE, if necessary.

Due to deteriorating conditions in the housing mortgage markets and the resulting negative financial impact on the GSEs, they were placed under FHFA conservatorship on September 7, 2008. This action was taken to preserve GSE assets, ensure a sound and solvent financial condition, and mitigate systemic risks that contributed to current market instability. The FHFA director will terminate the conservatorship once safe and solvent conditions are established.

Pursuant to the authorities provided to the Secretary under the HERA, the Treasury Department, also on September 7, 2008, took three additional steps to help ensure the liquidity of the GSEs. This included:

Senior Preferred Stock Purchase Agreements (Note 9)

The Secretary of the Treasury entered into a Senior Preferred Stock Purchase Agreements (SPSPA) with Fannie Mae and Freddie Mac to provide substantial financial support to the enterprises; thereby minimizing potential systemic financial risks associated with the deteriorating financial condition of Fannie Mae and Freddie Mac. The agreement provides for the Treasury Department to increase its investment in the senior preferred stock of the GSEs if at the end of any quarter the FHFA, acting as the conservator, determines that the liabilities of either GSE, individually, exceed its respective assets. The gross amount available for this purpose is $200 billion per GSE and these preferred stock agreements have no expiration date.

GSE Credit Facility (Note 12)

The Government Sponsored Enterprise Credit Facility (GSECF) was established to ensure credit availability to the GSEs and the Federal Home Loan Banks. This lending facility will provide secured funding on an as needed basis under terms and conditions established by the Secretary to protect taxpayers. The GSEs and the Federal Home Loan Banks are eligible to borrow under this program. The GSECF provides liquidity, if needed, until December 31, 2009.

Funding will be provided directly by the Treasury Department from its account held at the Federal Reserve Bank of New York (FRBNY) in exchange for eligible collateral from the GSE which will be limited to guaranteed MBS issued by the GSE as well as advances made by the Federal Home Loan Banks. Loan requests will require approval from the Treasury Department and verification by the FRBNY that adequate collateral has been pledged. Loans made through the GSECF are subject to the federal debt limit. Loans will be for short-term durations and are in general expected to be for less than one month but no shorter than one week. Loans will not be made with a maturity date beyond December 31, 2009. The rate on a loan request ordinarily will be based on the daily London Interbank Borrowing Rate (LIBOR) for a similar term loan plus 50 basis points. The rate is set at the discretion of the Secretary with the objective of protecting the taxpayer, and is subject to change. There is no stated limitation on loans provided through the GSECF. However, loans are limited to the amounts of available collateral. There were no loans made through the GSECF in fiscal year 2008 or 2009.

GSE Mortgage-Backed Securities (MBS) Purchase Program (Note 12)

Under this program, the Treasury Department, via Asset Managers, purchases GSE MBS in the open market. The Asset Managers are also authorized to enter into other trade/sell transactions such as Pair Offs, Turns, Assignments, and Dollar Rolls. By purchasing these credit-guaranteed securities, the Treasury Department seeks to broaden access to mortgage funding for current and prospective homeowners and to promote stability in the mortgage market. The size and timing of the MBS purchases is subject to the discretion of the Secretary. The scale of the program will be based on developments in the capital and housing markets. As these securities are backed by individual mortgages, they are accounted for under the *Federal Credit Reform Act of 1990*.

The actions taken by the Department thus far are temporary, as defined by section 1117 of HERA, and are intended to provide financial stability until Fannie Mae and Freddie Mac can return to normal operations or until the Administration and Congress address how they should be structured going forward. As of September 30, 2009, there are no plans to bring these organizations into the government; rather, the purpose of these financial arrangements 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 deliberate what, if any, structural changes should be made.

TEMPORARY GUARANTEE PROGRAM MONEY MARKET FUNDS

In September 2008, the Treasury Department established a Temporary Guarantee Program (Program) for Money Market Funds. Under this Program the Treasury Department guaranteed to investors that they would receive the stable share price (SSP) for shares held in participating money market funds up to the number of shares held as of the close of business on September 19, 2008. To participate in the Program, eligible money market funds had to submit an application and pay a premium of 1 basis point if the fund's net asset value (NAV) is greater than or equal to 99.75 percent of the SSP, or 1.5 basis points of the SSP if the fund's NAV is less than 99.75 percent of the SSP but greater than or equal to 99.50 percent of the SSP.

Under this program, any outlays would have been paid out initially from the ESF, and then under the provisions of Section 131 of the *Emergency Economic Stabilization Act of 2008*. Such outlays would then be reimbursed from funds available under the Troubled Asset Relief Program. The temporary guarantee program was extended and continued to provide coverage through September 19, 2009 to shareholders up to amounts that they held in participating money market funds as of the close of business on September 19, 2008. As of September 30, 2009, the program had expired. Treasury did not receive any claims for payment. As of September 30, 2009, the Treasury Department had collected a total of approximately $1.2 billion in program participation payments. All participant payments are invested into U.S. Government securities.

HOME OWNERSHIP PRESERVATION ENTITY (HOPE BOND)

The *Home Ownership Preservation Entity (HOPE) Fund for Homeowners Act of 2008*, of the *Housing and Recovery Act of 2008*, authorizes the Secretary of the Treasury to issue HOPE bonds without any limitations as to the purchaser of the issuance. Due to the cost of issuing special purpose bonds to the public, the Secretary of the Treasury has decided to issue the HOPE bonds to the Federal Financing Bank (FFB). The total outstanding HOPE bonds may not exceed $300,000 million. The FFB's purchase of HOPE bonds issued by the Secretary is consistent with the core mission of the FFB. FFB purchased $462.5 million in bonds at par value in fiscal year 2009 and one bond at par value of $29.5 million in fiscal year 2008, with floating interest rate to be reset quarterly. The interest rate is 0.183 percent and 1.6 percent as of September 30, 2009 and September 30, 2008, respectively. The bonds have 30 year maturity dates starting on August 27, 2038 and ending on July 15, 2039. The HOPE bonds are reported as investments held-to-maturity and the related interest receivable is reported as accrued interest receivable in FFB's stand-alone financial statements. The HOPE bond transactions are subsequently eliminated at the Departmental level.

TROUBLED ASSET RELIEF PROGRAM (TARP)

The *Emergency Economic Stabilization Act of 2008* (EESA) established the Troubled Asset Relief Program (TARP) on October 3, 2008 to be administered by the Treasury Department and established the Office of Financial Stability within the Department's Office of Domestic Finance. The Act gave the Treasury Secretary broad and flexible authority to purchase and insure mortgages and other troubled assets, as well as to inject capital into banks and other commercial companies by taking equity positions in those entities, if needed, to stabilize the financial markets or an industry. The TARP is intended to promote market stability and protect the U.S. economy by authorizing Treasury Department to purchase and guarantee troubled mortgage-related assets and other financial assets. EESA also provides for the purchase of any other financial instruments that the Secretary determines, after consultation with the Federal Reserve Banks' Board Chairman, is necessary in order to promote financial market stability.

The EESA established certain criteria under which the TARP would operate, including provisions that impact the budgeting, accounting, and reporting of troubled assets acquired under the Act. Section 101(a) of the EESA provided the authority for the Secretary to purchase troubled assets, and Section 101(a)(3) of the EESA established the Office of Financial Stability (OFS) to implement the TARP. Section 102 of the EESA required the Secretary to establish a program to guarantee troubled assets originated or issued prior to March 14, 2008, including mortgage-backed securities. Section 115 of the EESA limits the authority of the Secretary to purchase troubled assets to $700 billion[10] outstanding at any one time, calculated at the aggregate purchase prices of all troubled assets held. There was approximately $291 billion outstanding (the amount on the original investment that is due to be repaid to Treasury) against the Section 115 authority as of September 30, 2009. Section 120 of the EESA established that the authorities under Sections 101(a), excluding Section 101(a)(3) and Section 102 of the EESA shall terminate on December 31, 2009. Section 120 of the EESA further establishes that the Secretary, upon submission of a written certification to Congress, may extend the authority provided under the Act to expire no later than 2 years from the date of the enactment of the Act (October 3, 2008).

10 *The Helping Families Save Their Homes Act of 2009* (PubL.No. 111-22, Div. A, 123 Stat., 1632 (2009), amended the act to reduce the maximum allowable amount of outstanding troubled assets under the act by approximately $1.3 billion, from $700.0 billion to $698.7 billion.

TARP has engaged in purchases of equity including preferred stock and common stock Warrants from financial institutions and insurance companies. In addition, the TARP has established a guarantee program for financial institutions. TARP has made direct loans as well as equity investments in preferred stock to support the automotive industry and to unfreeze secondary credit markets. TARP funds are being used to help families stay in their homes. TARP also has funded an initiative to address the challenge of legacy assets in the financial marketplace. Details concerning the specific TARP programs is provided in Notes 8 and 12.

Subsidy Reestimates

The purpose of reestimates is to update original program subsidy estimates to reflect actual cash flow experience as well as changes in forecasts of future cash flows. Forecasts of future cash flows are updated based on actual program performance to date, additional publicly available relevant historical market data on securities performance, revised expectations for future economic conditions, and enhancements to cash flow projection methods. Financial statement reestimates for all programs were performed using actual financial transaction data through September 30, 2009. In accordance with credit reform guidance and to ensure the timely completion of the credit reform reestimate process, market and security specific data publicly available as of September 30, 2009, was used for the CPP, AGP, TIP, and direct loan AIFP, and data through August 31, 2009 was used for the equity portion of AIFP, AIG, and TALF in the reestimate calculations. Treasury assessed the key inputs of the reestimates using data publicly available as of September 30, 2009, and in its determination, there were no significant changes to the key inputs for the three programs for which August 31, 2009 data was used that would require a revision to the reestimates.

Downward reestimates for the fiscal year ended September 30, 2009, are as follows:

	Downward Reestimate Amounts (in millions)		
Program	Subsidy	Interest	Total
AGP	$ (1,097)	$ (77)	$ (1,174)
Direct Loan			
AIFP	$ (9,039)	$ (1,571)	$ (10,610)
CBLI/TALF	(222)	(21)	(243)
Subtotal Direct	$ (9,261)	$ (1,592)	$ (10,853)
Equity Investment			
CPP	$ (68,558)	$ (3,861)	$ (72,419)
TIP	(20,366)	(1,101)	(21,467)
AIG	(845)	(280)	(1,125)
AIIP	(2,331)	(379)	(2,710)
Subtotal Equity	$ (92,100)	$ (5,621)	$ (97,721)
Total	$ (102,458)	$ (7,290)	$ (109,748)

Descriptions of the reestimates, by TARP Program, are as follows:

All of the approximately $1,174 million in downward reestimates for the AGP is due to improvements in market conditions from when the guarantee was committed in January 2009. The improved market conditions resulted in an increase in the projected AGP asset due to the net present value of the estimated cash inflows from the preferred stock and warrants received by Treasury from Citigroup as a premium being greater than the estimated value of future claim payments associated with the $5,000 million guarantee.

All of the approximately $10,610 million in downward reestimates for the Automotive Industry Direct Loan Financing Programs (AIDLFP) direct loans is the result of the post bankruptcy improved financial position of one of the major companies participating in the program. The $243 million in downward reestimates for the TALF is entirely due to projected improved performance of the securities within the program versus the original estimate.

The approximately $70,718 million in repurchases during fiscal year 2009 accounts for approximately $9,700 million of the $72,419 million in downward reestimates in the CPP. Projected repurchases of approximately $30,000 million in the next 12 months accounts for approximately $5,410 million, with the $57,309 million balance in downward reestimates in the CPP due to improved market conditions from when the original estimate was made in December 2008.

The $21,467 million in downward reestimates in the Targeted Investment Program (TIP) is mostly due to improved market conditions from when the original estimates were made in December 2008 and January 2009. Approximately $2,300 million is due to a $20,000 million repurchase forecast within 12 months following September 30, 2009.

All of the $1,125 million in downward reestimates for the AIG Investment Program and $2,710 million in downward reestimates for the AIIP equity programs are due to improvements in market conditions from when the equities were purchased resulting in a reduction in the projected costs of the programs.

AMERICAN INTERNATIONAL GROUP (AIG)

As described in Note 8, in fiscal year 2009, the Department ultimately invested $42 billion in Series E perpetual, non-cumulative 10% preferred shares of AIG through the Systemically Significant Failing Institutions Program. And, to further assist the stability and restructuring of AIG, the Treasury Department agreed to make an additional $29 billion available to AIG under the Treasury credit facility. In return, the Department received $29 billion of AIG series F perpetual, non-cumulative 10% preferred stock (300,000 shares) and a warrant to purchase 3,000 shares of AIG common stock. The initial liquidation preference of the Series F preferred shares is zero and increases pro rata by the amount of each drawdown by AIG. As of September 30, 2009, AIG had drawn $1.1 billion through the credit facility, leaving an outstanding commitment to AIG at September 30 of $27.9 billion.

Under the initial terms of the credit facility agreement with AIG and the Federal Reserve Bank of New York (FRBNY), a 77.9% equity interest in AIG (in the form of Series C Convertible Participating Serial Preferred Stock convertible into approximately 77.9% of the issued and outstanding shares of common stock) was issued to a trust established by the FRBNY. Subsequent to the initial agreement, a reverse stock split of AIG's common stock increased this to 79.8%. The U.S. Government is the sole beneficiary of that trust, so that when the stock is ultimately liquidated the proceeds will be deposited into the General Fund of the U.S. Government. The U.S. Government will be the ultimate recipient of any dividends on the stock and any proceeds from the liquidation of the stock. The accounting and reporting for any activities related to the government's beneficial interest in the stock held by the trust will be done by the Treasury Department. The trustees of the trust are independent of both the Department and the FRBNY, and are not involved in day-to-day management of AIG.

As the U.S. Government is the sole beneficiary of the trust, and as it is anticipated that the U.S. Government will ultimately realize an economic benefit from its beneficial interest in the trust, the Treasury Department has recorded a non-entity asset of $23,472 million as of September 30, 2009, and corresponding custodial revenue for the same amount. The value recorded is based on the market value of the trust's AIG holdings at September 30, 2009; as the underlying AIG common stock is actively traded on the New York Stock Exchange, this represents the best independent valuation available for the government's beneficial interest. The U.S. Government's proceeds will be received when AIG's credit line with the FRBNY is terminated, AIG has redeemed the preferred stock owned by the Treasury Department through TARP, and the trustees sell the stock held by the trust. The Treasury Department will re-value its beneficial interest in the trust each year until the trust is liquidated. Like any asset, future events may increase or decrease the value of the U.S. Government's interest in the trust. The amount ultimately realized by the U.S. Government upon liquidation of the trust is inherently subject to substantial uncertainty regarding future economic events that could affect the future value of AIG common stock.

The Department's participation in enhancing AIG's capital and liquidity in order to facilitate an orderly restructuring of the company are in addition to the FRBNY activities in this regard.

THE AMERICAN RECOVERY AND REINVESTMENT ACT OF 2009 (RECOVERY ACT)

President Obama signed the Recovery Act into law on February 17, 2009. The Recovery Act is an extraordinary response to a crisis unlike any since the Great Depression, and includes measures to modernize the nation's infrastructure, enhance energy independence, expand educational opportunities, preserve and improve affordable health care, provide tax relief, and protect those in greatest need.

The Department of the Treasury has various responsibilities related to Recovery Act programs, including the implementation of some sixty tax incentives for households and businesses; local and state government support; and investments in renewable energy, low income housing, and health care. Treasury has taken a risk-based approach and focused on balancing the requirements of speed, quality, and accountability to ensure Recovery Act funds are distributed timely and accurately. To achieve these objectives, Treasury established a Recovery Act implementation team housed within the purview of the Assistance Secretary for Management/Chief Financial Officer responsible for working with the program offices across the Department. The Recovery Act team facilitates all Recovery Act implementation department-wide and interfaces with the broader Recovery Act community. As part of this broad responsibility, the team establishes internal processes, addresses external data requirements, manages risk inherent in Recovery Act implementation, and coordinates Treasury Recovery Act audits.

Here are some of the Recovery Act programs implemented by Treasury during fiscal year 2009:

- The Recovery Act provided $250 one-time *Economic Recovery Payments* to eligible retirees, veterans, and other high-need recipients. The Financial Management Service received $7 million to cover administrative expenses incurred in sending these payments, either via electronic funds transfer or by check, to millions of recipients of Social Security, Supplemental Security Insurance, Railroad Retirement, and Veterans Administration benefits.
- The Community Development Financial Institutions (CDFI) Fund received $2 million to cover administrative expenses related to implementing Recovery Act provisions that apply to two existing programs. These existing programs and related Recovery Act funding are the *CDFI Program*, which received $90

million in additional funds to make grants, loans, equity investments, deposits, and secondary capital investments to certified CDFIs that deploy the funds in underserved, low-income communities, and to targeted populations; and the *Native American CDFI Assistance Program*, which received $8 million in additional funds under the Recovery Act to make grants, loans, equity investments, deposits, and secondary capital investments to certified CDFIs that deploy the funds in Native American communities or to Native American populations.

- The *New Markets Tax Credit (NMTC) Program*, which does not provide direct funding to CDFI because it is a tax credit, was provided an additional $1.5 billion of allocation authority for 2009; NMTC facilitates investment in low-income communities by permitting taxpayers to receive a non-refundable credit against federal income taxes for making Qualified Equity Investments in Treasury-certified Community Development Entities (businesses and real estate developments) in low-income communities. The Recovery Act authorizes the CDFI Fund to allocate $3 billion of tax credit authority to qualified Community Development Entities (CDEs) under the New Markets Tax Credit (NMTC) Program, as follows: $1.5 billion to CDEs that applied for allocation authority under the 2008 NMTC allocation round, and $1.5 billion to CDEs that applied for allocation authority under the 2009 NMTC allocation round. This $3 billion in allocation authority is in addition to the $3.5 billion in non-Recovery Act funds that was already allocated for the NMTC in 2009.
- The *Cash Assistance for Specified Energy Property in Lieu of Tax Credits Program* promotes renewable energy. The Office of the Fiscal Assistant Secretary (OFAS) designed the program in conjunction with the Department of Energy. Energy reviews the applications for completeness and initial approval. OFAS then reviews the applications and either approves or denies the request. Payment is made by the Office of Financial Management which follows its standard procedures for making payments. The energy program payments are treated as an expense in the Treasury financial statements. This program provides an alternative means to attract financing for renewable energy projects by providing direct payment in lieu of tax credits. The program began accepting applications on July 31, 2009, and by September 30, 2009, had made awards for 37 projects totaling over $1 billion.
- The *Cash Assistance to States for Low-Income Housing Projects in Lieu of Tax Credits Program* allows construction or acquisition and rehabilitation of low-income housing projects to continue where developers were unable to proceed due to insufficient financing. The program addresses the near-term goal of creating and retaining jobs, as well as the long-term benefit of increasing the affordable housing supply. OFAS administers this program. Funds are awarded to State Housing Credit Agencies to make sub-awards to fund the construction and/or acquisition and rehabilitation of low-income housing projects, creating jobs and increasing the supply of low-income housing. In lieu of tax credits, forty housing agencies had received approval for over $2.5 billion as of September 30, 2009.
- In 2009, the Internal Revenue Service (IRS) implemented a number of Recovery Act tax provisions impacting both individuals and businesses, including the Making Work Pay credit; the First-Time Home Buyer credit; a new COBRA health insurance continuation premium subsidy; and several new bond programs.

30. SCHEDULE OF FIDUCIARY ACTIVITY

Fiduciary activities are the collection or receipt, and the management, protection, accounting, investment, and disposition by the Federal Government of cash or other assets, in which non-Federal individuals or entities have an ownership interest that the Federal Government must uphold.

Fiduciary cash and other assets are not assets of the Federal Government, and accordingly are not recognized on the Balance Sheet.

The following funds have been identified by the Treasury Department as meeting the criteria for fiduciary activity. Details of the funds, as well as fiduciary relationships, is provided below.

Bureau	Fund Code	Authority	Fund Title
BEP	20X6513.013	31 USC 5119	Mutilated Currency Claims Funds
BPD	20X6008	31 USC 3513	Payment Prin. & Interest Govt. Agencies
FMD	20X6045	31 USC 3328	Proceeds, Payments of Unpaid Checks
FMD	20X6048	31 USC 3329, 3330	Proceed of Withheld Foreign Check
FMD	2015X6078	50 APP. USC 2012	War Claims FD, FCSC
FMD	20X6092	31 USC 1321	Debt Management Operations
FMD	20X6104	22 USC 1627	Albanian Claims Fund, Treasury
FMD	20X6133	31 USC 1322	Payment of Unclaimed Moneys
FMD	20X6309	22 USC 1627(a)	Libyan Claims Settlement Fund
FMD	20X6311	98 Stat. 1876	Kennedy Center Revenue Bond
FMD	20X6312	22 USC 1627	Iranian Claims Settlement Fund
FMD	20X6314	22 USC 1644g	German Democrat Settlement Fund
FMD	20X6315	22 USC 1645h	Vietnam Claims Settlement Fund
FMD	20X6501.018	31 USC 3513	Small Escrow Amounts
FMD	20X6720	31 USC 3513	SM DIF Account for Dep. & Check Adj.
FMD	20X6830	104 Stat. 1061	Net Interest Payments to/from State
FMD	20X6999	31 USC 3513	Accounts Payable, Check Issue UNDDR
IRR	20X6737	90 Stat. 269-270	Collections for Northern Mariana Islands
IRR	20X6738	31 USC 3513	Coverover Withholding-US Virgin Islands
IRR	20X6740	31 USC 3515	Coverover Withholdings-Guam
IRR	20X6741	31 USC 3513	Coverover Withhold Samoa
OAS	20X6317.001	22 USC 2431	Belize Escrow, Debt Reduction
OAS	20X6501.018	31 USC 3513	Small Escrow Amounts
OTS	20X6501.76	31 USC 3513	Small Escrow Amounts

Unclaimed monies were authorized by 31 U.S.C. 5119, which authorized Financial Management Service, Department of the Treasury, to collect unclaimed monies on behalf of the public. Other fiduciary activities by the Department of the Treasury as listed above are included in All Other Fiduciary Funds

Schedule of Fiduciary Activity (in millions):

	Unclaimed Monies-FMD	All Other Fiduciary Funds	2009 Total Fiduciary Funds
Fiduciary Net Assets, Beginning of the Year	$ 366	$ 43	$ 409
Increases			
Contributions to Fiduciary Net Assets	28	1,063	1,091
Investment earnings	0	1	1
Total Increases	28	1,064	1,092
Decreases			
Disbursements to and on behalf of beneficiaries	(4)	(899)	(903)
Total Decreases	(4)	(899)	(903)
Net Increase (Decrease) in fiduciary assets	24	165	189
Fiduciary Net Assets, End of Year	$ 390	$ 208	$ 598

Schedule of Fiduciary Net Assets (in millions):

	Unclaimed Monies-FMD	All Other Fiduciary Funds	2009 Total Fiduciary Funds
Fiduciary Assets			
Cash and cash equivalents	$ 390	$ 193	$ 583
Investments	0	15	15
Total Fiduciary Assets	390	208	598
Total Fiduciary Net Assets	$ 390	$ 208	$ 598

31. COMMITMENTS AND CONTINGENCIES

LEGAL CONTINGENCIES

The Treasury Department is a party in various administrative proceedings, legal actions, and claims, including equal opportunity matters which may ultimately result in settlements or decisions adverse to the U.S. Government. These contingent liabilities arise in the normal course of operations and their ultimate disposition is unknown. Treasury Department has one contingent liability in fiscal year 2009 related to legal action taken in the case, *American Council of the Blind and Others*, where losses are determined to be probable and amount of loss can be estimated. The Treasury Department has disclosed contingent liabilities where the conditions for liability recognition have not been met and the likelihood of unfavorable outcome is more than remote. The Treasury Department does not accrue for possible losses related to cases where the potential loss cannot be estimated or the likelihood of an unfavorable outcome is less than probable.

In some cases, a portion of any loss that may occur may be paid by the Treasury Department's Judgment Fund, which is separate from the operating resources of the Treasury Department. For cases related to the *Contract Disputes Act of 1978* and awards under federal anti-discrimination and whistleblower protection acts, the Treasury Department must reimburse the Judgment Fund from future appropriations.

In the opinion of the Treasury Department's management and legal counsel, based on information currently available, the expected outcome of legal actions, individually or in the aggregate, will not have a materially adverse effect on the Treasury Department's financial statements, except for the legal actions described below.

PENDING LEGAL ACTIONS

- *The American Council of the Blind and Others, et. al. v. Paulson*: Plaintiffs have filed suit against the Department under Section 504 of the Rehabilitation Act seeking the redesign of U.S. currency. In 2007, a judge ruled that the current U.S. currency design violates this Act and this ruling was appealed. In 2008, the United States Court of Appeals for the District of Columbia Circuit affirmed the District Court's ruling. No monetary damages were awarded by the Court. However, the Treasury Department is required to provide meaningful access to United States currency for blind and other visually impaired persons. This may require changes to U.S. currency (excluding the one-dollar note.) The Court ordered such changes to be completed in connection with each denomination of currency, not later than the date when a redesign is next approved by the Secretary of the Treasury. Because the cost of implementing these changes will be incorporated into future currency redesign costs, no redesign costs have been accrued in the accompanying financial statements as of September 30, 2009 and September 30, 2008.

  The Court of Appeals in the above mentioned case ordered the parties to confer and attempt to negotiate attorney fees and costs to be awarded the plaintiffs. In December 2008, the parties filed a joint stipulation agreeing to $800 thousand in attorney fees and costs that was paid from the Judgment Fund in February 2009.

- *Amidax Trading Group v. S.W.I.F.T.* makes allegations that the Treasury Department's Terrorist Finance Tracking Program has involved unlawful disclosure of information by the Society for Worldwide Interbank Financial Telecommunications (S.W.I.F.T.). Defendants include the Department of the Treasury as well as several Treasury officials. The case was dismissed on February 13, 2009, and the plaintiff has subsequently appealed that ruling. The Treasury Department is unable to determine the likelihood of an unfavorable outcome or an estimate of potential loss at this time.

- *Cobell et al. v. Salazar et al. (formerly Cobell v. Kempthorne)*: Native Americans allege that the Department of Interior and the Department of the Treasury have breached trust obligations with respect to the management of the plaintiffs' individual Indian monies. On August 7, 2008, the Federal District Court issued an opinion awarding $455 million to the plaintiffs. This decision was overturned on appeal in July 2009. The appellate court found that the government owes a cost-effective accounting, in scale with available funds. The District Court is considering further proceedings. The Treasury Department is unable to determine the likelihood of an unfavorable outcome or an estimate of potential loss at this time. (Please refer to Note 33, Subsequent Events, for additional information.)

- Tribal Trust Fund Cases: Numerous cases have been filed in U.S. District Courts in which Native American Tribes seek a declaration that the U.S. has not provided the tribes with a full and complete accounting of their trust funds, and seek an order requiring the government to provide such an accounting. In addition, there are a number of other related cases seeking damages in the United States Court of Federal Claims which do not name the Department as a defendant. It is not possible at this time to determine the likelihood of an unfavorable outcome or an estimate of the amount or range of any potential loss.

- Other Legal Actions: The Treasury Department is also involved in employment related legal actions (e.g., Discrimination, Equal Employment Opportunity Commission, Merit System Protection Board, etc.) for which an unfavorable outcome is reasonably possible, but for which an estimate of potential loss cannot be determined at this time. It is not expected that these cases will have a material effect on the Treasury Department's financial position or results.

- There are other legal actions pending for which the possibility of loss could not be determined, and where the ultimate resolution of the legal actions may materially affect the Treasury Department's financial position or results. As of September 30, 2009, four legal claims amounting to approximately $113 million existed for which the possibility of loss could not be determined.

OTHER COMMITMENTS AND CONTINGENCIES

Treaties and International Agreements

The Office of Management and Budget, Circular No. A-136, *Financial Reporting Requirements and the Treasury Financial Manual, Volume 1, Part 2-4700* require the recognition and disclosure of financial information related to Treaties and International Agreements for fiscal year 2009 financial reporting. The focus of this requirement is to identify Departmental Treaties and International Agreements that commit and obligate the Federal Government and may result in a possible exposure to loss. Any recognition and disclosure of Treaty and International Agreement loss contingencies would be presented in accordance with SFFAS No. 5, *Accounting for Liabilities of the Federal Government*. Any recognition would depend on the likelihood of the future event occurring and the measurability of an amount or range of loss.

The Treasury Department does not have any treaties or international agreements to report for fiscal year 2009.

Multilateral Development Banks (MDB)

The Treasury Department has subscribed to capital for certain MDB, portions of which are callable under certain limited circumstances to meet the obligations of the respective MDB. There has never been, nor is there anticipated, a call on the Treasury Department's commitment for these subscriptions. As of September 30, 2009 and September 30, 2008, U.S. callable capital in MDB was as follows (in millions):

	2009	2008
African Development Bank	$ 1,634	$ 1,634
Asian Development Bank	5,911	5,911
European Bank for Reconstruction and Development	1,805	1,805
Inter-American Development Bank	28,687	28,687
International Bank for Reconstruction and Development	22,641	22,641
Multilateral Investment Guarantee Agency	301	301
North American Development Bank	1,275	1,275
Total	$ 62,254	$ 62,254

Terrorism Risk Insurance Program

The *Terrorism Risk Insurance Act* (TRIA or the Act) was signed into law on November 26, 2002. This law was enacted to address market disruptions resulting from terrorist attacks on September 11, 2001. The Act helps to ensure available and affordable commercial property and casualty insurance for terrorism risk, and simultaneously allows private markets to stabilize. The Terrorism Risk Insurance Program is activated upon the certification of an "act of terrorism" by the Secretary of the Treasury Department in concurrence with the Secretary of State and the Attorney General. If a certified act of terrorism occurs, insurers may be eligible to receive reimbursement from the U.S. Government for insured losses above a designated deductible amount. Insured losses above this amount will be shared between insurance companies and the U.S. Government. The Act also gives the Treasury Department authority to recoup federal payments made under the Program through policyholder surcharges under certain circumstances and contains provisions designed to manage litigation arising from or relating to a certified act of terrorism.

The original TRIA program was to expire on December 31, 2005, but the Program was extended through December 31, 2007 by the *Terrorism Risk Insurance Extension Act of 2005* (Extension Act). This law included the following significant changes: it reduced the federal role in terrorism risk insurance markets by increasing insurer deductibles and excluding certain types of previously covered insurance. The Extension Act also reduced the U.S. Government's share of insured losses and added a "Program Trigger" provision which precludes federal payments unless insured losses from a certified act of terrorism exceed $100 million.

On December 26, 2007, the *Terrorism Risk Insurance Program Reauthorization Act of 2007* (Reauthorization Act) was enacted extending the Program through December 31, 2014. The Reauthorization Act, among other Program changes, revised the definition of "Act of Terrorism" to remove the certification requirement that the act be committed by an individual acting on behalf of a foreign person or foreign interest; revised the provisions of the Act with regard to the cap on annual liability for insured losses of $100 billion; and established deadlines by which recoupment of federal payments made under the Program would have to be accomplished.

In 2008, the Treasury Department published interim guidance and an interim final rule conforming regulations to statutory changes in the Reauthorization Act pertaining to the mandatory insurance availability and insurer disclosure requirements of the Program as well as the addition of coverage for domestic acts of terrorism. On April 21, 2009, Treasury Department published the interim final rule as final.

In September 2008, the Treasury Department issued two notices of proposed rulemaking with requests for comment. One proposed rule incorporates and clarifies statutory requirements of the Reauthorization Act for capping the annual liability for insured losses at $100 billion. The proposed rule describes how the Treasury Department will determine the pro rata share of insured losses to be paid by each insurer that incurs losses under the Program when insured losses would otherwise exceed the cap and how the Federal share of compensation will be calculated. The Treasury Department expects to issue a final rule incorporating public comments early in fiscal year 2010.

The other proposed rule sets forth the requirements for recoupment of the Federal share of compensation for insured losses. The rule describes how the Treasury Department will determine the amounts to be recouped and the requirements for insurers to collect, report, and remit surcharges to the Treasury Department. The Treasury Department expects to issue a final rule incorporating public comments early in fiscal year 2010. There were no claims under TRIA as of September 30, 2008 and September 30, 2009.

Exchange Stabilization Agreement (ESA)

In April 1994, Treasury signed the North American Framework Agreement (NAFA), which includes the ESA with Mexico. The Treasury Department has a standing swap line for $3 billion with Mexico under the NAFA and its implementing ESA. The amounts and terms (including the assured source of repayment) of any borrowing under NAFA and ESA will have to be negotiated and agreed to before any actual drawing can occur. The ESA does provide sample clauses that state that transactions shall be exchange rate neutral for the ESF and shall bear interest based on a then current rate tied to U.S. Treasury bills. There were no drawings outstanding on the ESF swap line as of September 30, 2009 and 2008. On December 10, 2008, the Treasury renewed its participation in the agreement until December 2010.

Contingent Liability to Government Sponsored Enterprises

The Treasury Department has recorded a contingent liability at September 30, 2009 (zero at September 30, 2008) of $76.9 billion to the Government Sponsored Enterprises, Fannie Mae and Freddie Mac, based on probable future liability under the Senior Preferred Stock Purchase Agreement between the Treasury Department and the GSEs. Refer to Note 9 for a full description of the agreements and related contingent liability.

32. IMPUTED FINANCING COSTS

In accordance with SFFAS No. 30, *Inter-Entity Cost Implementation Amending SFFAS 4, Managerial Cost Accounting Standards and Concepts*, the material Imputed Inter-departmental financing sources currently recognized by the Department include the actual cost of future benefits for the federal pension plans that are paid by other federal entities, the Federal Employees Health Benefits Program (FEHB), and any un-reimbursed payments made from the Treasury Judgment Fund on behalf of the Department.

SFFAS No. 5, *Accounting for Liabilities for the Federal Government*, requires that employing agencies recognize the cost of pensions and other retirement benefits during their employees' active years of service. SFFAS No. 5 requires OPM to provide cost factors necessary to calculate cost. OPM actuaries calculate the value of pension benefits expected to be paid in the future, and then determines the total funds to be contributed by and for covered employees, such that the amount calculated would be sufficient to fund the projected pension benefits. For employees covered by Civil Service Retirement System (CSRS), the cost factors are 25.8% of basic pay for regular, 43.5% law enforcement officers, 20% regular offset, and 38% law enforcement officers offset. For employees covered by Federal Employees Retirement System (FERS), the cost factors are 12.3% of basic pay for regular and 26.7% for law enforcement officers. The information for the fiscal years ended September 30, 2009 and September 30, 2008 was as follows (in millions):

	2009	2008
U.S. Treasury Judgment Fund	$ 0.8	$ 6.5
Pension	264.0	254.1
Health Insurance	501.1	449.8

33. SUBSEQUENT EVENTS

Housing Finance Agency Initiative

Under the *Housing and Economic Recovery Act of 2008* (HERA), the Treasury Department, together with the Federal Housing Finance Agency, Fannie Mae, Freddie Mac, and the Department of Housing and Urban Development announced in October 2009 an initiative to provide support to state and local housing finance agencies (HFAs). HFAs have historically played a central role in providing a safe, sustainable path to homeownership for working families in all 50 states and many localities across the country. This initiative will continue to support low mortgage rates and expand resources for low and middle income borrowers to purchase or rent homes, making them more affordable over the long term. The HFA Initiative includes two separate programs: (1) the Temporary Credit and Liquidity Program (TCLP) and (2) the New Issue Bond Program (NIBP).

The Treasury Department has received preliminary apportionments in the amounts of $9 billion for the TCLP and $19 billion for the NIBP. On December 4, 2009, Treasury entered into a participation interest under the TCLP with the Pennsylvania Housing Finance Agency. As of this date, however, no bonds have been provided to Fannie Mae or Freddie Mac requiring the Treasury Department to disburse funds. On December 9, 2009, under the NIBP, the Treasury Department entered into an obligation of approximately $7 billion to purchase securities of Fannie Mae and Freddie Mac which are backed by HFA revenue bonds and/or escrow funds.

Troubled Asset Relief Program

On December 9, 2009, the Secretary of the Treasury, pursuant to Section 120(b) of EESA, certified that he was extending the spending authority provided under the Act to October 3, 2010. The spending authority was originally set to expire on December 31, 2009. This extension was necessary to assist American families and stabilize financial markets because it will, among other things, enable the Treasury Department to continue to implement programs that address housing markets and the needs of small businesses, and to maintain the capacity to respond to unforeseen threats to the economy stemming from financial instability.

On December 9, 2009, Bank of America repaid all amounts received under the CPP and TIP totaling $45 billion plus dividends accrued since November 15, 2009, thereby terminating its participation in TARP. The Treasury Department still holds the warrants issued under these programs, but has no other investment in Bank of America.

On November 1, 2009, a CPP participant, CIT Group, filed for Chapter 11 Bankruptcy. The Treasury Department had invested $2.3 billion in senior preferred shares of CIT Group and received a warrant for the purchase of common shares. Treasury does not expect a significant recovery of its preferred stock investment. As such, this investment has been reduced to zero. The ultimate amount received, if any, from this investment will depend on the outcome of the bankruptcy proceedings.

On November 6, 2009, a CPP participant, United Commerce Bank, was closed by its regulators. The Treasury Department had invested approximately $298.7 million in senior preferred stock and received a warrant for the purchase of the common stock. The value of these shares, including the warrant, reflected in these financial statements is approximately $22.5 million as of September 30, 2009. The ultimate amount received, if any, from this investment will depend on the outcome of the receivership.

In November 2009, a CPP participant, Pacific Coast National Bank, was closed by its regulators. The Treasury Department had invested approximately $4.1 million in senior preferred stock and received a warrant for preferred stock in the amount of $0.2 million. The value of these shares, including the warrant, reflected in these financial statements is approximately $0.15 million as of September 30, 2009. The ultimate amount received, if any, from this investment will depend on the outcome of the receivership.

On December 11, 2009, the Treasury Department announced that it priced a secondary public offering of 88,401,697 warrants to purchase common stock of JPMorgan Chase & Co. at $10.75 per warrant. The net proceeds to the Treasury Department are expected to be approximately $936 million. These proceeds are in addition to the dividend payments received on the related preferred stock. Closing is expected to occur on or about December 16, 2009.

Legal Contingency

Cobell, et al. v. Salazar

On December 8, 2009, a settlement was announced related to the claims raised in this lawsuit, as well as other claims for the mismanagement of assets and land. The settlement is contingent on the passage of new legislation to authorize the settlement terms and court approval, which would not occur until March 2010 at the earliest. If Congress enacts authorizing legislation, the Government will pay $12 million immediately to fund notice to the class. If the court approves the settlement after notice to the class, the government will pay an additional $1.4 billion from the Judgment Fund to settle the claims for an historical accounting and for mismanagement of assets and land. The Government will also make available an additional sum of $2 billion from the Judgment Fund to purchase numerous small interests in land from Native Americans, as well as for other purposes. It has not been determined which federal agency will be assigned responsibility for the payment through the Judgment Fund.

REQUIRED SUPPLEMENTAL INFORMATION (UNAUDITED)

INTRODUCTION

This section provides the Required Supplemental Information as prescribed by Office of Management and Budget (OMB) Circular No. A-136, *Financial Reporting Requirements*.

Other Claims for Refunds

The Treasury Department has estimated that $11.0 billion may be payable as other claims for tax refunds. This estimate represents amounts (principal and interest) that may be paid for claims pending judicial review by the federal courts or internally. The total estimated payout (including principal and interest) for claims pending judicial review by the federal courts is $4.7 billion and by appeals is $6.3 billion.

Federal Taxes Receivable, Net

In accordance with SFFAS No. 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*, some unpaid tax assessments do not meet the criteria for financial statement recognition as discussed in Note 1 to the financial statements. Although compliance assessments and write-offs are not considered receivables under federal accounting standards, they represent legally enforceable claims of the U.S. Government. There is, however, a significant difference in the collection potential between compliance assessments and receivables.

The components of the total unpaid assessments at September 30, 2009, were as follows (in billions):

Total Unpaid Assessments	$ 308
Less: Compliance Assessments	(75)
Write Offs	(105)
Gross Federal Taxes Receivable	**$ 128**
Less: Allowance for Doubtful Accounts	(99)
Federal Taxes Receivables, Net	**$ 29**

To eliminate double counting, the compliance assessments reported above exclude trust fund recovery penalties, totaling $3 billion, assessed against officers and directors of businesses who were involved in the non-remittance of federal taxes withheld from their employees. The related unpaid assessments of those businesses are reported as taxes receivable or write-offs, but the Treasury Department may also recover portions of those businesses' unpaid assessments from any and all individual officers and directors against whom a trust fund recovery penalty is assessed.

Internal Revenue Service (IRS)

The unpaid assessments balance represents assessments resulting from taxpayers filing returns without sufficient payment, as well as from the IRS's enforcement programs such as examination, under-reporter, substitute for return, and combined annual wage reporting. A significant portion of this balance is not considered a receivable. Also, a substantial portion of the amounts considered receivables is largely uncollectible.

Under federal accounting standards, unpaid assessments require taxpayer or court agreement to be considered federal taxes receivable. Assessments not agreed to by taxpayers or the courts are considered compliance assessments and are not considered federal taxes receivable. Due to the lack of agreement, these compliance assessments are less likely to have future collection potential than those unpaid assessments that are considered federal taxes receivable.

Assessments with little or no future collection potential are called write-offs. Write-offs principally consist of amounts owed by deceased, bankrupt, or defunct taxpayers, including many failed financial institutions liquidated by the Federal Deposit Insurance Corporation (FDIC) and the former Resolution Trust Corporation (RTC). As noted above, write-offs have little or no future collection potential, but statutory provisions require that these assessments be maintained until the statute for collection expires.

Alcohol and Tobacco Tax and Trade Bureau (TTB)

As an agent of the Federal Government and as authorized by 26 U.S.C., the TTB collects excise taxes from alcohol, tobacco, firearms, and ammunition industries. In addition, special occupational taxes are collected from certain alcohol and tobacco businesses. During fiscal year 2009, TTB collected nearly $20.6 billion in taxes, interest, and other revenues.

Substantially all of the taxes collected by TTB net of related refund disbursements are remitted to the General Fund of the U.S. Government. The Department of Treasury further distributes this revenue to Federal agencies in accordance with various laws and regulations. The firearms and ammunition excise taxes are an exception. Those revenues are remitted to the Fish and Wildlife Restoration Fund under provisions of the *Pittman-Robertson Act of 1937*.

Deferred Maintenance

In fiscal year 2009, the Treasury Department had no material amounts of deferred maintenance costs to report on vehicles, buildings, and structures owned by the Treasury Department.

Deferred maintenance applies to owned PP&E. Deferred maintenance is maintenance that was not performed when it should have been, or was scheduled to be, and is put off or delayed for a future period. Maintenance is defined as the act of keeping capitalized assets in an "acceptable condition" to serve their required mission. It includes preventive maintenance, normal repairs, replacement of parts and structural components, and other activities needed to preserve the asset so that it continues to provide acceptable services and achieves its expected useful life. Maintenance excludes activities aimed at expanding the capacity or significantly upgrading the assets to a different form than it was originally intended (i.e., activities related to capitalized improvements, modernization, and/or restoration).

Logistic personnel use condition assessment surveys and/or the total life-cycle cost methods to determine deferred maintenance and acceptable operating condition of an asset. Periodic condition assessments, physical inspections, and review of manufacturing and engineering specifications, work orders, and building and other structure logistics reports can be used under these methodologies.

Fiscal Year 2009 Statement of Budgetary Resources Disaggregated by Sub-organization Accounts (in millions):

Budgetary Resources	Engraving and Printing	Bureau of the Public Debt	Departmental Offices	Fin. Crimes Enforcement Network	Financial Management Service	Internal Revenue Service
Unobligated balance brought forward	$ 96	$ 175	$ 282,340	$ 18	$ 240	$ 682
Recoveries prior year unpaid obligations	0	81	7,841	2	14	95
Budget Authority:						
Appropriations	0	463,484	450,242	92	26,417	11,851
Borrowing authority	0	0	548,735	0	0	0
Spending authority offsetting collections:						
Earned: Collected	502	208	279,849	15	228	149
Change in receivable federal	(18)	(14)	1	0	5	(19)
Change in unfilled customer order:						
Advance received	1	0	(16)	0	0	0
Without advance from federal sources	0	(152)	28,939	1	(1)	5
Subtotal	485	463,526	1,307,750	108	26,649	11,986
Non-expenditure transfers, net	0	(3)	(149)	0	(21)	130
Temporarily not available	0	(5)	7	0	0	0
Permanently not available	0	(80,108)	(184,490)	0	(6,991)	(112)
Total Budgetary Resources	$ 581	$ 383,666	$1,413,299	$ 128	$ 19,891	$ 12,781
Status of Budgetary Resources						
Obligations incurred						
Direct	$ 0	$ 383,379	$ 967,769	$ 96	$ 19,390	$ 11,791
Reimbursable	535	195	355	7	228	114
Subtotal	535	383,574	968,124	103	19,618	11,905
Unobligated Balance						
Apportioned	46	64	368,489	20	254	380
Exempt from apportionment	0	15	43,370	0	9	0
Subtotal	46	79	411,859	20	263	380
Unobligated balance not available	0	13	33,316	5	10	496
Total Status of Budgetary Resources	$ 581	$ 383,666	$1,413,299	$ 128	$ 19,891	$ 12,781
Relationship Obligations to Outlays						
Obligated balance, net (Note 1)						
Unpaid obligations brought forward	$ 103	$ 159	$ 54,795	$ 13	$ 329	$ 1,436
Uncollected customer payments Federal sources brought forward	(47)	(189)	(16)	(3)	(33)	(47)
Total unpaid obligated balance, net	56	(30)	54,779	10	296	1,389
Obligations incurred, net	535	383,574	968,123	103	19,618	11,905
Gross Outlays	(523)	(383,578)	(830,165)	(100)	(19,594)	(11,625)
Recoveries prior year unpaid obligations	0	(81)	(7,841)	(2)	(14)	(95)
Change uncollected customer payments	18	166	(28,940)	(1)	(4)	14
Obligated balance net, end of period						
Unpaid obligations	115	75	184,910	15	339	1,621
Uncollected customer payments federal	(29)	(24)	(28,954)	(5)	(37)	(33)
Total unpaid obligated balance, net	86	51	155,956	10	302	1,588
Net Outlays						
Gross outlays	523	383,578	830,165	100	19,594	11,625
Offsetting collections	(503)	(208)	(277,552)	(15)	(228)	(149)
Distributed offsetting receipts	0	(31,250)	(12,154)	0	(451)	(759)
Net Outlays	$ 20	$ 352,120	$ 540,459	$ 85	$ 18,915	$ 10,717

Fiscal Year 2009 Statement of Budgetary Resources Disaggregated by Sub-organization Accounts (in millions):

Budgetary Resources	U.S. Mint	Comptroller of the Currency	Office of Thrift Supervision	Alcohol Tobacco Tax & Trade	Budgetary Total	9/30/2009 Non-Budgetary Financing
Unobligated balance brought forward	$ 51	$ 734	$ 292	$ 2	$ 260,173	$ 24,457
Recoveries prior year unpaid obligations	55	0	4	4	8,097	(1)
Budget Authority:						
Appropriations	0	0	0	99	952,185	0
Borrowing authority	0	0	0	0	493	548,242
Spending authority offsetting collections:						
Earned: Collected	2,467	775	253	3	11,681	272,768
Change in receivable federal	0	0	0	1	(44)	0
Change in unfilled customer order:						
Advance received	(10)	0	(6)	0	(31)	0
Without advance from federal sources	0	0	0	0	(134)	28,926
Subtotal	2,457	775	247	103	964,150	849,936
Non-expenditure transfers, net	0	0	0	0	(43)	0
Temporarily not available	0	0	0	0	2	0
Permanently not available	(35)	0	0	(1)	(92,001)	(179,736)
Total Budgetary Resources	**$ 2,528**	**$ 1,509**	**$ 543**	**$ 108**	**$ 1,140,378**	**$ 694,656**
Status of Budgetary Resources						
Obligations incurred						
Direct	$ 0	$ 0	$ 0	$ 101	$ 729,697	$ 652,829
Reimbursable	2,282	716	233	4	4,669	0
Subtotal	2,282	716	233	105	734,366	652.829
Unobligated Balance						
Apportioned	246	0	0	2	349,889	19,612
Exempt from apportionment	0	793	310	0	44,497	0
Subtotal	246	793	310	2	394,386	19,612
Unobligated balance not available	0	0	0	1	11,626	22,215
Total Status of Budgetary Resources	**$ 2,528**	**$ 1,509**	**$ 543**	**$ 108**	**$ 1,140,378**	**$ 694,656**
Relationship Obligations to Outlays						
Obligated balance, net (Note 1)						
Unpaid obligations brought forward	$ 260	$ 166	$ 44	$ 19	$ 57,314	$ 10
Uncollected customer payments Federal sources brought forward	(7)	(4)	0	1	(346)	(1)
Total unpaid obligated balance, net	253	162	44	18	56,968	9
Obligations incurred, net	2,282	716	233	105	734,366	652,829
Gross Outlays	(2,296)	(704)	(232)	(99)	(675,286)	(573,630)
Recoveries prior year unpaid obligations	(55)	0	(4)	(4)	(8,097)	1
Change uncollected customer payments	0	0	0	(1)	178	(28,926)
Obligated balance net, end of period						
Unpaid obligations	191	178	41	21	108,297	79,209
Uncollected customer payments federal	(7)	(4)	0	(2)	(168)	(28,926)
Total unpaid obligated balance, net	184	174	41	19	108,129	50,283
Net Outlays						
Gross outlays	2,296	704	232	99	675,286	573,630
Offsetting collections	(2,457)	(775)	(247)	(3)	(9,369)	(272,768)
Distributed offsetting receipts	0	0	0	0	(40,114)	(4,500)
Net Outlays	**$ (161)**	**$ (71)**	**$ (15)**	**$ 96**	**$ 625,803**	**$ 296,362**

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Part 3
Other Accompanying Information

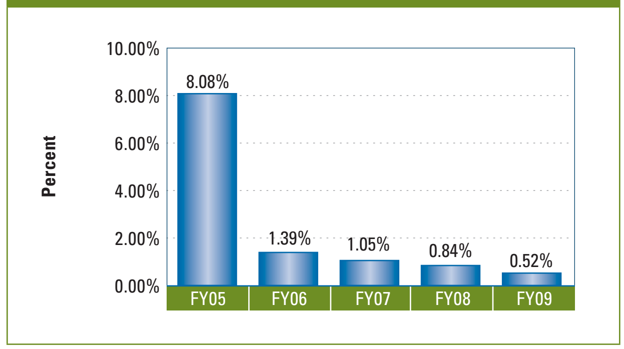
Appendix A: Other Accompanying Information (Unaudited)

This section provides Other Accompanying Information as prescribed by OMB Circular No. A-136, *Financial Reporting Requirements.*

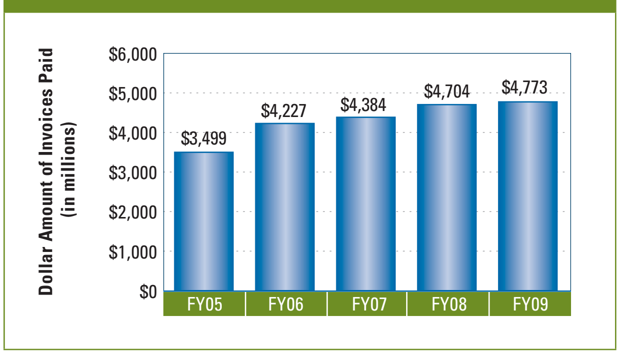
PROMPT PAYMENT

The *Prompt Payment Act* requires Federal agencies to make timely payments to vendors for supplies and services, to pay interest penalties when payments are made after the due date, and to take cash discounts only when they are economically justified. Treasury bureaus report Prompt Payment data on a monthly basis to the Department, and periodic quality control reviews are conducted by the bureaus to identify potential problems.

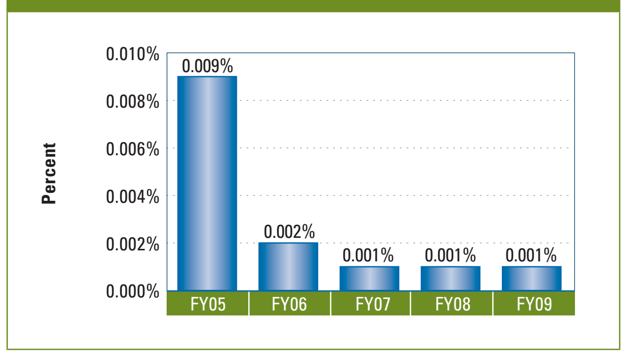
Percentage of Number of Invoices Paid Late



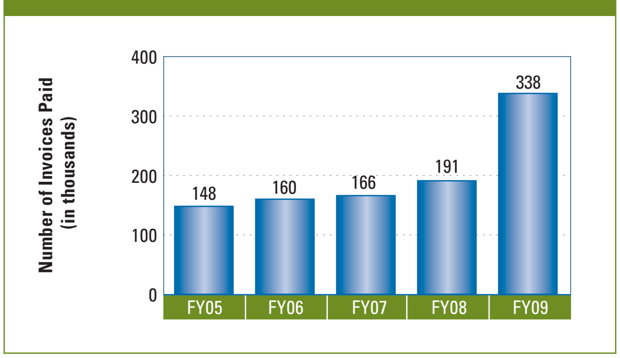
Total Dollar Amount of Invoices Paid (in millions)



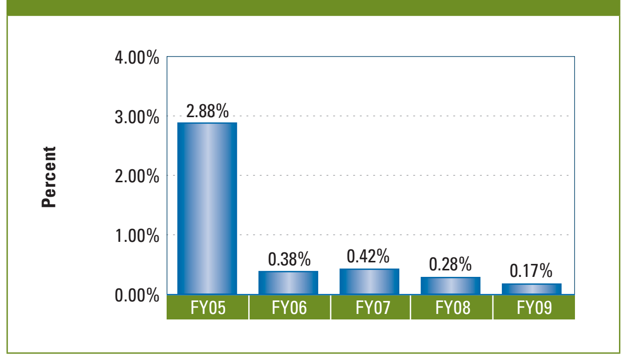
Percentage of Dollar Amount of Interest Penalties Paid



Total Number of Invoices Paid (in thousands)



Percentage of Number of Interest Penalties Paid



TAX GAP

Reducing the tax gap is at the heart of IRS' enforcement programs. The tax gap is the difference between what taxpayers should pay and what they actually pay due to not filing tax returns, not paying their reported tax liability on time, or failing to report their correct tax liability. The tax gap, about $345 billion based on updated fiscal year 2001 estimates, represents the amount of noncompliance with the tax laws. Underreporting tax liability accounts for 82 percent of the gap, with the remainder almost evenly divided between non-filing (8 percent) and underpaying (10 percent). 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.

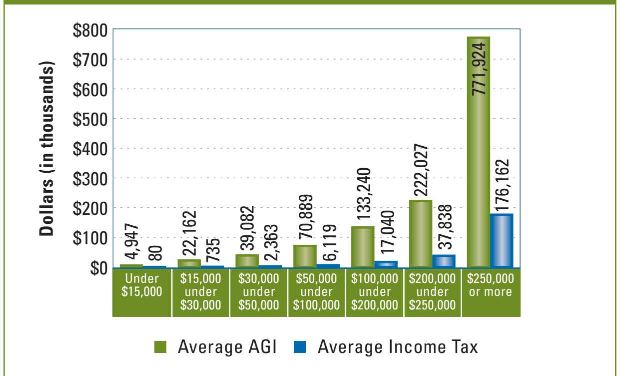
The tax gap is the aggregate amount of tax (i.e., excluding interest and penalties) that is imposed by the tax laws for any given tax year but is not paid voluntarily and timely. The tax gap arises from the three types of noncompliance: not filing required tax returns on time or at all (the non-filing 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). Of these three components, only the underpayment gap is observed; the non-filing gap and the underreporting gap must be estimated. 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. Obviously, 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 tax, penalties, and interest that has been assessed over many years, but has not been paid by a certain point in time, and which the IRS expects to remain uncollectible. In essence, it represents the difference between the total balance of unpaid assessments and the net taxes receivable reported on the IRS' balance sheet. The tax gap and the collection gap are related and overlapping concepts, but they have significant differences. The collection gap is a cumulative balance sheet concept for a particular point in time, while the tax gap is like an income statement item for a single year. Moreover, the tax gap estimates include all noncompliance, while the collection gap includes only amounts that have been assessed (a small portion of all noncompliance).

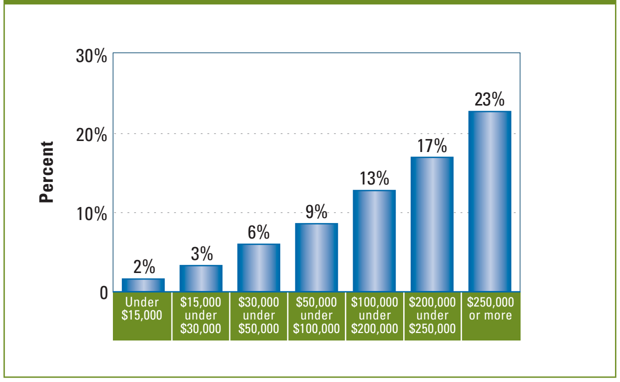
TAX BURDEN

The Internal Revenue Code provides for progressive rates of tax, whereby higher incomes are generally subject to higher rates of tax. The graphs below present the latest available information on income tax and adjusted gross income (AGI) for individuals by AGI level and for corporations by size of assets. For individuals, the information illustrates, in percentage terms, the tax burden borne by varying AGI levels. For corporations, the information illustrates, in percentage terms, the tax burden borne by these entities by various sizes of their total assets. The graphs are only representative of more detailed data and analysis available from the Statistics of Income (SOI) office.

Average Individual Income Tax Liability and Average Adjusted Gross Income (AGI) Tax Year 2007



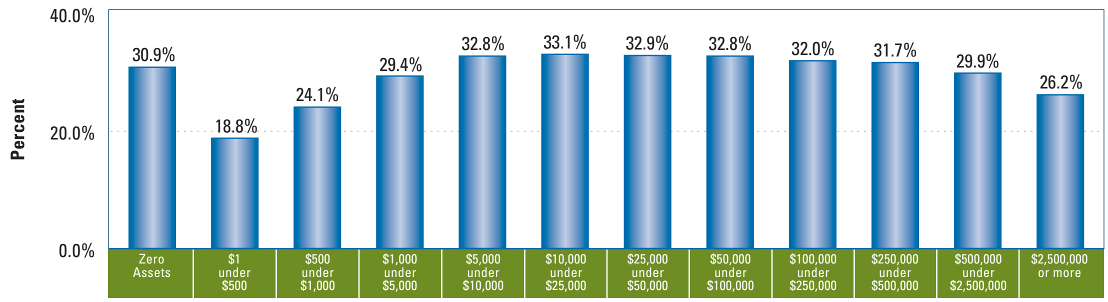
Individual Income Tax Liability as a Percentage of AGI Tax Year 2007



INDIVIDUAL INCOME TAX LIABILITY TAX YEAR 2007

Adjusted Gross Income (AGI)	Number of taxable returns (in thousands)	AGI (in millions)	Total income tax (in millions)	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	37,597	$186,000	$3,022	$4,947	$80	1.6%
$15,000 under $30,000	30,229	669,932	22,211	22,162	735	3.3%
$30,000 under $50,000	25,978	1,015,283	61,396	39,082	2,363	6.0%
$50,000 under $100,000	31,260	2,216,021	191,293	70,890	6,119	8.6%
$100,000 under $200,000	13,463	1,793,835	229,415	133,242	17,040	12.8%
$200,000 under $250,000	1,501	333,309	56,802	222,058	37,843	17.0%
$250,000 or more	3,002	2,317,016	528,770	771,824	176,139	22.8%
Total	143,030	8,531,396	1,092,909			

Corporation Tax Liability as a Percentage of Taxable Income Tax Year 2006 Data



CORPORATION TAX LIABILITY TAX YEAR 2006

Total Assets (in thousands)	Income subject to tax (in millions)	Total income tax after credits (in millions)	Percentage of income tax after credits to taxable income
Zero Assets	$17,500	$5,399	30.9%
$1 under $500	9,519	1,787	18.8%
$500 under $1,000	4,659	1,123	24.1%
$1,000 under $5,000	16,790	4,933	29.4%
$5,000 under $10,000	10,019	3,286	32.8%
$10,000 under $25,000	16,070	5,321	33.1%
$25,000 under $50,000	14,181	4,661	32.9%
$50,000 under $100,000	16,626	5,457	32.8%
$100,000 under $250,000	32,623	10,431	32.0%
$250,000 under $500,000	36,396	11,531	31.7%
$500,000 under $2,500,000	181,767	54,367	29.9%
$2,500,000 or more	935,281	244,788	26.2%
Total	$1,291,431	$353,084	27.3%

Appendix B: Improper Payments Information Act and Recovery Auditing Act

The *Improper Payments Information Act of 2002* (IPIA) requires agencies to review their programs and activities annually to identify those susceptible to significant improper payments. According to the Office of Management and Budget (OMB) Circular A-123, *Management's Responsibility for Internal Control*, Appendix C, Requirements for Effective Measurement and Remediation of Improper Payments (A-123, Appendix C), "significant" means that an estimated error rate and a dollar amount exceed the threshold of 2.5 percent and $10 million of total program funding. A-123, Appendix C also requires the agency to implement a corrective action plan that includes improper payment reduction targets.

The government-wide Chief Financial Officers Council developed an alternative for meeting IPIA requirements for federal programs that are so complex that developing an annual error rate is not feasible. Agencies may establish an annual estimate for a high-risk component of a complex program (e.g., a specific program population) with OMB approval. Agencies must also perform trend analyses to update the program's baseline error rate in the interim years between detailed program studies. When development of a statistically valid error rate is possible, the reduction targets are revised and become the basis for future trend analyses.

I. DESCRIPTION OF THE DEPARTMENT'S RISK ASSESSMENT(S) PERFORMED SUBSEQUENT TO COMPILING ITS FULL PROGRAM INVENTORY AND RISK-SUSCEPTIBLE PROGRAMS.

Each year, the Department develops a comprehensive inventory of the funding sources for all programs and activities and distributes it to the Treasury bureaus and offices. If program or activity funding is at least $10 million, Risk Assessments are required at the payment type level (e.g., payroll, contracts, vendors, travel, etc.). For those payment types resulting in high risk assessments that comprise at least 2.5 percent and $10 million of a total funding source, (1) statistical sampling must be performed to determine the actual improper payment rate, and (2) a corrective action plan must be developed and submitted to the Department and OMB for approval.

Responses to the Risk Assessments produce a score that falls into pre-determined categories of risk. The following table describes the actions required to be taken at each risk level:

RISK LEVEL	REQUIRED ACTION(S)
High Risk > 2.5% Error Rate & > $10 Million	Corrective Action Plan
Medium Risk	Review Payment Controls for Improvement
Low Risk	No Further Action Required

The Risk Assessments performed across the Department in fiscal year 2009 resulted in all programs and activities as low and medium risk susceptibility for improper payments except for the Internal Revenue Service's (IRS)

Earned Income Tax Credit (EITC) program. The EITC's high-risk status is well-documented, having been previously identified in the former Section 57 of OMB Circular A-11, *Preparation, Submission, and Execution of the Budget,* and has been deemed a complex program for the purposes of the IPIA.

II. DESCRIBE THE STATISTICAL SAMPLING PROCESS CONDUCTED TO ESTIMATE THE IMPROPER PAYMENT RATE FOR EACH PROGRAM IDENTIFIED.

EARNED INCOME TAX CREDIT

The EITC is a refundable federal tax credit that offsets income taxes owed by low income workers and, if the credit exceeds the amount of taxes owed, provides a lump-sum payment to those who qualify.

The next section explains how the IRS currently develops its erroneous payment projections. The most recent projection is based on a tax year 2001 reporting compliance study that estimated the level of improper overclaims for fiscal year 2009 to range between $11.2 - $13.3 billion and 23 percent (lower bound) to 28 percent (upper bound) of approximately $48.1 billion in total program payments.

NATIONAL RESEARCH PROGRAM (NRP) ANALYSIS

The complexity of the EITC program, the nature of tax processing, and the expense of compliance studies preclude statistical sampling on an annual basis to develop error rates for comparison to reduction targets. The estimates are based primarily on information from the National Research Program (NRP) reporting compliance study of individual income tax returns for tax year 2001—the most recent year for which compliance information from a statistically valid, random sample of individual tax returns is available. The approach is nearly identical to that used for earlier years. The difference is that the estimates make use of more recent EITC payment data from the President's fiscal year 2010 Budget.

Under the tax year 2001 NRP reporting compliance study, individual income tax returns filed during calendar year 2002 for tax year 2001 were randomly selected for examination.[1] This selection method allows the measures for the individual income tax return filing population to be estimated from the results of the NRP sample returns. Because one of the objectives of the NRP is to provide data for compliance measurement, NRP procedures and data collection differed from those followed in standard examination programs. NRP classification and examination procedures were more comprehensive in scope and depth than those for standard examination programs. These expanded procedures were designed to provide a more thorough determination of what taxpayers should have reported on their returns.

The tax year 2001 NRP individual income tax return study covered filers of all types of individual income tax returns. About 6,400 of the approximately 44,400 returns in the regular NRP sample were EITC claimants.[2] The NRP study results for this EITC claimant subset of NRP returns were the primary source of data for the improper payments estimates. Other data and information sources used for the estimates included the IRS Enforcement Revenue Information System (ERIS), which tracks assessments and collections from IRS enforcement-related activities; Treasury Department estimates of the effect of the EITC provisions in the Economic Growth and Tax

1 The NRP used a stratified, random sample design. Returns are grouped into predefined categories or "strata" and selected randomly within each stratum.

2 About 1,600 other returns (the "calibration sample") were included in the tax year 2001 NRP Individual Income Tax Study. These returns went through a somewhat different examination process and they were not used for these calculations.

Relief Reconciliation Act of 2001 (EGTRRA) on erroneous EITC claims, and Treasury Department fiscal year 2010 EITC budget estimates.

Enacted in 2001, EGTRRA contains several provisions related to the EITC that became effective for tax year 2002. These provisions are believed to influence taxpayer behavior in a number of ways, among them increased claims and improved compliance for EITC claimants.[3] Since the improper payment rate is derived from pre-EGTRRA taxpayer behavior (tax year 2001), it must be adjusted to reflect the estimated impact of the EITC-related EGTRRA provisions. Treasury Department economists conducted an analysis of the EITC-related EGTRRA provisions, concluding that the provisions reduced EITC erroneous claims by about 13 percent and increased claims by about 5 percent.[4] To account for these effects, the NRP-based estimate of the improper payment rate for tax year 2001 was adjusted by reducing the of the *Amount of EITC Overclaimed* by 13 percent and increasing the *Amount of EITC Claimed on all Returns* by 5 percent.

The general approach for developing the fiscal year 2009 set of EITC improper payments estimates involved the following steps: (1) estimating an improper payment rate for tax year 2001 using the NRP data, (2) adjusting the tax year 2001 rate to reflect the estimated impact of the EITC-related EGTRRA provisions, (3) estimating EITC claims for fiscal year 2009 through fiscal year 2012 by projecting tax year 2001 claims forward using the growth rates implicit in Treasury Department budget outlay estimates, and (4) multiplying the adjusted improper payment rate by the estimated claims to calculate estimated improper payments for each fiscal year.

The error rate estimate from the EITC component of the tax year 2006 NRP study will be completed during fiscal year 2010. The updated error estimate will help inform business decisions about program administration and meets IPIA standards for measuring and reporting on improper payments.

III. DESCRIBE THE CORRECTIVE ACTION PLANS FOR REDUCING THE ESTIMATED RATE OF IMPROPER PAYMENTS FOR THE EITC PROGRAM.

The IRS uses a two-pronged approach to reduce erroneous EITC payments:

1. Continually seek opportunities to increase program efficiency within existing resources – in other words, make the base program better; and
2. Test potential business process enhancements to reduce error and then request implementation funding if the tests prove successful.

BASE PROGRAM

In 2009, the IRS prevented more than $3.0 billion from being paid in error. The prevention activity is primarily focused in three areas:

- **Examinations** – the IRS identifies tax returns for examination and holds the EITC portion of the refund until an audit can be conducted. This is the only ongoing IRS audit program where exams are

3 For example, EGTRRA implemented a uniform definition of a "qualifying child" and simplified the rule for determining which taxpayer was eligible to claim the qualifying child in potentially ambiguous cases (the AGI tiebreaker rule). The simpler rules were expected to enhance compliance by reducing the number of claims arising from misinterpretation of the tax law and to increase the number of claims by those who were deterred by its complexity.

4 The estimates were in 1999 dollars.

conducted before a refund is released. The examination closures and enforcement revenue protected in the charts below do not include test initiatives.

- **Math Error** – this refers to an automated process in which the IRS identifies math or other statistical irregularities and automatically prepares an adjusted return for a taxpayer. Congressional approval is required for math error use.
- **Document Matching** – involves comparing income information provided by the taxpayer with matching information (e.g., W-2s, 1099s) from employers to identify discrepancies.

The chart below shows significant results from fiscal year 2004 through fiscal year 2010. In fiscal year 2009 alone, the IRS conducted over 500,000 examinations, issued 350,000 math error notices, and closed over 300,000 document matching reviews.

COMPLIANCE ACTIVITIES (THOUSANDS)

	FY04*	FY05*	FY06*	FY07	FY08*	FY09**	FY10***	FY04-FY10 Total
Examinations	472,022	527,969	517,617	503,267	503,755	508,398	500,000	3,533,028
Math Error Notices**	624,590	515,890	460,316	393,263	432,797	350,000	350,000	3,126,856
Document Matching	300,000	324,419	364,020	394,217	377,327	314,469	325,000	2,399,452
Amended Returns					32,473	25,395	25,000	82,868

*Restated actual
**Preliminary estimates
***Estimate based on fiscal year 2009 preliminary data

These activities had a significant effect. Treasury projects that continued enforcement efforts will protect a total of $19 billion in revenue through fiscal year 2010.

ENFORCEMENT REVENUE PROTECTED ($ BILLIONS)

	FY04	FY05*	FY06*	FY07*	FY08*	FY09**	FY10***	FY04-FY10 Total
Examinations	1.12	1.35	1.50	1.49	2.00	2.15	2.15	11.76
Math Error Notices**	0.62	0.52	0.46	0.41	0.44	0.38	0.38	3.21
Document Matching	0.25	0.53	0.60	0.73	0.74	0.63	0.65	4.13
Amended Returns					0.07	0.07	0.07	0.21
TOTAL	1.99	2.40	2.56	2.63	3.25	3.23	3.25	19.31

*Restated actual
**Preliminary estimates
***Estimate based on fiscal year 2009 preliminary data

TESTING NEW BUSINESS PROCESSES

The IRS continues to build new solutions for existing business processes and to use other activities to combat program error including:

- Continuing the partnership with members from two key tax software associations to identify software enhancements and collaborative efforts that can help reduce EITC errors and assist preparers in meeting their EITC due diligence requirements
- Implementing an on-line training module for paid preparers on EITC preparer due diligence requirements and standards
- Further refining and completing activities associated with a suite of EITC paid preparer treatments, based on risk-based selections, including due diligence audits, visits by revenue and criminal investigation agents, streamlined injunctions, first-time paid preparer treatments to influence the accuracy of EITC returns filed, and analyzing short-term outcomes, including penalties and accuracy of returns.

IV. EITC IMPROPER PAYMENT REDUCTION OUTLOOK

The reduction outlook for EITC improper payments is as follows:

IMPROPER PAYMENT (IP) REDUCTION OUTLOOK ($ IN BILLIONS)

Program	PY Outlays	PY %	PY $	CY Outlays	CY IP%	CY IP$	CY+1 Est Outlays	CY+1 IP%	CY+1 IP$	CY+2 Est Outlays	CY+2 IP%	CY+2 IP$	CY+3 Est Outlays	CY+3 IP%	CY+3 IP$
EITC Upper Bound Estimate	$47.6	28%	$13.1	$48.1	28%	$13.3	$60.7	28%	$16.8	$58.5	28%	$16.2	$49.4	28%	$13.7
EITC Lower Bound Estimate	$47.6	23%	$11.1	$48.1	23%	$11.2	$60.7	23%	$14.2	$58.5	23%	$13.6	$49.4	23%	$11.5

Outlays: The amounts shown are projections of total payments for the EITC, estimated by the Office of Tax Analysis within the Department of the Treasury. Following prior methodology, the amount shown is the total EITC claimed.

IP % and IP $: These estimates follow the prior approach which provided a range for improper payments.

Note: The Improper Payment percentage and Estimated Outlay columns reflect a constant error rate pending the development of an annual error rate measurement.

CY+1 and CY+2 estimates include ARRA EITC provisions which expand EITC for families with three children and increase the beginning of the phaseout range for couples filing a joint return.

CY: Current year; PY: Prior year

RECOVERY AUDITING ACT

V. TREASURY'S RECOVERY AUDITING PROGRAM

Section 831 of the *Defense Authorization Act* for fiscal year 2002 added a new subchapter to the U.S. Code (31 U.S.C 3561-3567), also known as the Recovery Auditing Act, that requires agencies that enter into contracts with a total value in excess of $500 million in a fiscal year to carry out a cost-effective program for identifying errors made in paying contractors and for recovering amounts erroneously paid to the contractors. A required element of such a program is the use of recovery audits and recovery activities. In accordance with OMB Circular A-123, *Management's Responsibility for Internal Control,* Appendix C, reporting on recovery auditing is required annually.

In fiscal year 2009, Treasury issued contracts totaling $5.0 billion. The annual Improper Payments Information Act Risk Assessment process includes a review of pre-payment controls that minimize the likelihood and occurrence of improper payments. For Recovery Auditing Act compliance, Treasury requires each bureau and office to review their post-payment controls and report on recovery auditing activities, contracts issued, improper payments made, and recoveries achieved. Bureaus and offices may use recovery auditing firms to perform many of the steps in their recovery auditing program and identify candidates for recovery action.

Treasury considers both pre-payment and post-payment reviews to identify payment errors a good management practice that should be included among basic payment controls. All of Treasury's bureaus use some form of recovery auditing techniques to identify improper payments during post-payment reviews. At times, bureaus may use the services of recovery auditors to help them identify payment anomalies and target areas for improvement. However, Treasury has extensive contract payment controls that are applied at the time each payment is processed, making recovery activity minimal. The low level of improper payments in 2009 did not require any Treasury bureau to develop a management improvement program under *Recovery Auditing Act* guidance.

RECOVERY AUDITING INFORMATION FISCAL YEAR 2004 - FISCAL YEAR 2009

Agency	Amount Subject to Review for CY Reporting	Actual Amount Reviewed and Reported CY	Amount Identified for Recovery CY	Amount Recovered CY*	Amount Identified for Recovery PY	Amount Recovered PY	Cumulative Amts. Identified for Recovery (CY+PYs)	Cumulative Amts. Recovered (CY+PYs)
Treasury	$5,254,751,759	$4,661,539,275	$1,475,232	$1,357,672	$825,279	$839,818	$6,733,805	$5,500,579

Note: CY: Current year; PY: Prior year

* Includes amounts identified for recovery in prior years.

For fiscal year 2009, the total number of contracts subject to review was 34,855; the total number reviewed was 32,311, for a total program cost of approximately $1.2 million dollars.

VI. MANAGEMENT ACCOUNTABILITY

The Secretary of the Treasury has delegated responsibility for improper payments to the Assistant Secretary for Management/Chief Financial Officer (ASM/CFO). Improper payments fall under the Department's management and internal control program. A major component of the internal control program is risk assessments, which are an extension of each bureau's annual improper payment review process. Under Treasury Directive 40-04, *Treasury Internal (Management) Control Program*, executives and other managers are required to have management control responsibilities as part of their annual performance plans. With oversight mechanisms such as the Treasury CFO Council and the IRS's Financial and Management Controls Executive Steering Committee, managerial responsibility and accountability in all management and internal control areas are visible and well documented.

Improper payments also have been monitored for improvement as a significant deficiency under the Federal Managers' Financial Integrity Act. Executives who are responsible and accountable for reducing the level of EITC overclaims have been identified, while other senior and mid-level officials have responsibility for monitoring progress in this area as bureau and program internal control officers.

VII. RESOURCES REQUESTED IN THE FISCAL YEAR 2010 BUDGET SUBMISSION TO CONGRESS

The IRS fiscal year 2010 President's Budget submission included no new initiatives related directly to the EITC program.

VIII. LIMITING STATUTORY AND REGULATORY BARRIERS

A number of factors serve as barriers to reducing overclaims in the EITC program. These include:

- Complexity of the tax law
- Structure of the Earned Income Tax Credit
- Confusion among eligible claimants
- High turnover of eligible claimants
- Unscrupulous return preparers
- Fraud

No one of these factors can be considered the primary driver of program error. Furthermore, the interaction among the factors makes addressing the credit's erroneous claims rate, while balancing the need to ensure the credit makes its way to taxpayers who are eligible, extremely difficult.

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Appendix C: Management and Performance Challenges and Responses

In accordance with the *Reports Consolidation Act of 2000*, the Inspectors General issue Semiannual Reports to Congress that identify specific management and performance challenges facing the Department. At the end of each fiscal year, the Treasury Office of Inspector General (OIG) and the Treasury Inspector General for Tax Administration (TIGTA) send an update of these management challenges to the Secretary and cite any new challenges for the upcoming fiscal year.

This Appendix contains the incoming management and performance challenges letters from OIG and TIGTA and the Secretary's responses describing actions taken and planned to address the challenges.

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DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

OFFICE OF
INSPECTOR GENERAL

October 29, 2009

INFORMATION MEMORANDUM FOR SECRETARY GEITHNER

FROM: Eric M. Thorson
Inspector General

SUBJECT: Management and Performance Challenges Facing the Department of the Treasury (OIG-CA-10-001)

In accordance with the Reports Consolidation Act of 2000, we are providing you with our perspective on the most serious management and performance challenges facing the Department of the Treasury.

This year, we are reporting one new challenge:

- Management of Recovery Act Programs

This challenge relates to the significant additional responsibilities and funding received by Treasury through the American Recovery and Reinvestment Act of 2009 (Recovery Act) for a variety of programs.

We also continue to report four challenges from last year:

- Management of Treasury's New Authorities Related to Distressed Financial Markets
- Regulation of National Banks and Thrifts
- Management of Capital Investments
- Anti-Money Laundering and Terrorist Financing/Bank Secrecy Act Enforcement

We removed two previously reported challenges:

- Corporate Management
- Information Security

Challenge 1: Management of Treasury's New Authorities Related to Distressed Financial Markets

As we reported last year, Treasury, along with the Federal Reserve, the Federal Deposit Insurance Corporation (FDIC), and the Federal Housing Finance Agency, has taken unprecedented actions to address the current financial crisis. To assist in those efforts, Congress passed the Housing and Economic Recovery Act in July 2008, which gave Treasury broad new authorities to address the distressed financial condition of Fannie Mae and Freddie Mac. Less than 6 weeks later, the Federal Housing Finance Agency put both entities into conservatorship.

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Treasury agreed to purchase senior preferred stock in Fannie Mae and Freddie Mac, established a new secured line of credit available to them, and initiated a temporary program to purchase new mortgage-backed securities issued by them. According to Treasury data, as of June 30, 2009, Treasury had purchased $86.5 billion in preferred stock of the two entities to cover their continuing losses and maintain a positive net worth. Treasury also purchased $154.2 billion of mortgage-backed securities issued by Fannie Mae and Freddie Mac. Even with this assistance, both entities remain in a weakened financial condition and may require more assistance.

As the turmoil in the financial markets increased, Treasury and the Federal Reserve took additional actions to deal with the situation, including rescuing Bear Stearns and American International Group. Treasury also sought and obtained additional authorities through passage of the Emergency Economic Stabilization Act (EESA) in October 2008. EESA, commonly known as the Troubled Assets Relief Program (TARP), gave the Treasury Secretary $700 billion to, among other things, (1) purchase capital in qualifying U.S.-controlled financial institutions and (2) buy, maintain, and sell toxic mortgage-related assets from financial institutions. These authorities were intended to bolster credit availability and address other serious problems in U.S. and world financial markets.

After EESA was enacted, the Department aggressively moved forward to loosen the credit market by purchasing senior preferred stock in nine of the nation's largest financial institutions. Since then, hundreds of other financial institutions have also participated in the Capital Purchase Program (CPP). To date, some CPP participants have repurchased preferred shares and warrants totaling more than $70 billion. However, a small but growing number of CPP recipients are failing to make their 5 percent dividend payments due to Treasury.

The Department implemented a number of other mechanisms to carry out its other authorities and responsibilities under TARP, including the Public-Private Investment Program and the Home Affordable Modification Program. To administer TARP, Treasury established the Office of Financial Stability.

EESA established a special inspector general for TARP and imposed oversight and periodic reporting requirements on both the special inspector general and the Government Accountability Office (GAO). Under EESA, GAO is also responsible for performing the annual financial statement audit of TARP. Recently, GAO reported that at the 1-year mark, TARP in general and CPP in particular, along with other efforts by the Federal Reserve and FDIC, had made important contributions to help stabilize credit markets. However, GAO also reported that many challenges and uncertainties remain—for example, whether Treasury will fully recoup TARP assistance to the automobile industry and AIG, among others. GAO further noted that other programs, such as the Public-Private Investment Program and the Home Affordable Modification Program, still face implementation or operational challenges. GAO recommended that as Treasury considers further action under TARP, including whether to extend the program beyond December 31, 2009, the Department should evaluate the program in the broader context of efforts by the Federal Reserve and FDIC to stabilize the financial system.

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At the time of this writing, it should also be noted that the Department is working through several significant accounting issues involving some very complex TARP transactions. As a result, the Department, in consultation with our office and GAO, has requested an extension from the Office of Management and Budget for its fiscal year 2009 annual financial reporting submission.

As conditions improve, Treasury will need to work with its partners to disassemble the structure established to support recovery efforts and ensure that federal funds no longer needed for those efforts are returned in an orderly manner to the Treasury general fund.

Challenge 2: Regulation of National Banks and Thrifts

Since September 2007, 39 Treasury-regulated financial institutions have failed, with estimated losses to the deposit insurance fund exceeding $27 billion. Even more financial institutions are expected to fail over the next 2 years.

Although many factors have contributed to the turmoil in the financial markets, Treasury's Office of the Comptroller of the Currency (OCC) and Office of Thrift Supervision (OTS) did not identify early or force timely correction of unsafe and unsound practices by institutions under their supervision. The irresponsible lending practices of many institutions are now well-recognized—including reliance on risky products, such as option adjustable rate mortgages, and degradation of underwriting standards. At the same time, financial institutions engaged in other high-risk activities, including high asset concentrations in commercial real estate and overreliance on unpredictable brokered deposits to fund rapid growth. There have also been instances of certain ailing thrifts backdating capital contributions.

The banking industry will continue to be stressed over the next several years. In their 2009 interagency Shared National Credits (SNC) review, OCC, OTS, and the other federal banking regulators found that credit quality had deteriorated to record levels with respect to the $2.9 trillion in large ($20 million or more) loans and loan commitments held by U.S. bank organizations, foreign bank organizations, and nonbank entities such as securitization pools, hedge funds, insurance companies, and pension funds. The review, which covered $1.2 trillion of the $2.9 trillion SNC portfolio, identified total losses of $53 billion. That amount exceeded the combined losses reported in the previous eight SNC reviews and was nearly triple the amount of the previous high, identified in 2002. The next substantial stresses to financial markets may result from troubled credit card debt and further deterioration in commercial real estate loans and could significantly affect financial institutions that had limited exposure to the housing crisis.

Our office is mandated to review failures of Treasury-regulated financial institutions that result in material losses to the deposit insurance fund. Since 2007, we have completed 12 such reviews and are engaged in 19 others. These reviews identify the causes of the failures and assess supervision exercised over failed institutions. Both OCC and OTS have been responsive to our recommendations for improving supervision. For example, OTS has issued guidance addressing concentration issues and the appropriate accounting treatment for capital contributions. However, these reviews do not address the broader supervisory effectiveness of the federal banking regulators as a whole or the effectiveness of the supervisory structure. It is therefore essential that OCC and OTS continue to take a critical look at their supervisory processes to identify why those processes did not prevent or mitigate the practices that led to the current crisis and what can be done to better protect the financial health of the banking industry and consumers going forward.

Recognizing that the focus of EESA and the Recovery Act is on the current crisis, another consideration is the need to identify, monitor, and manage emerging domestic and global systemic economic risks. Moreover, these emerging risks may go beyond the current U.S. regulatory structure. As we reported last year, Treasury and its regulatory partners must continue to diligently monitor both regulated and unregulated products and markets for new systemic risks that may require action.

Finally, in response to the current crisis, both the administration and Congress are considering proposals for regulatory reform, ranging from the creation of a single financial regulator to a more limited approach calling for oversight councils composed of the existing regulators and consolidating OTS and OCC. (Consolidating OTS and OCC is a common feature of the proposals and has been advocated by the Department.) Also under consideration is transferring responsibility for consumer financial protection functions to a new regulatory agency. Although it is too soon to know which direction regulatory reform will take, Treasury, OCC, and OTS will need to work in concert with the other affected federal bank regulators to ensure a smooth and effective transition to the new regulatory structure that emerges.

Challenge 3: Management of Recovery Act Programs

Treasury is responsible for overseeing an estimated $150 billion of Recovery Act funding and tax relief. Treasury's oversight responsibilities include grants for specified energy property in lieu of tax credits, grants to states for low-income housing projects in lieu of tax credits, increased Community Development Financial Institutions Fund grants and tax credits, economic recovery payments to social security beneficiaries and others, and payments to U.S. territories for distribution to their citizens. Many of these programs are new to Treasury and involve very large dollar amounts. As a result, Treasury faces immense challenges in ensuring that the programs achieve their intended purposes, provide for accountability and transparency, and are free from fraud and abuse.

It is estimated that Treasury's Recovery Act grants in lieu of tax credit programs—for specified energy property and to states for low-income housing projects—will cost almost $20 billion over their lives. Treasury has dedicated only a small number of staff to award and monitor these funds. We have concerns that the current staffing level is not commensurate with the size of these programs.

To date, we have issued two audit reports on Treasury's Recovery Act programs. The first, issued in August 2009, discussed progress made and additional steps necessary to operate the specified energy property program more effectively. The second, issued in October 2009, discussed our concerns with a survey the Department completed for the Recovery Accountability and Transparency Board on Recovery Act staffing levels, qualifications, and training. We concluded that the information provided in the survey response was unreliable. Although these two early audits identified problems, the Deputy Secretary and the Senior Accountability Officer (the Assistant Secretary for Management, Chief Financial Officer, and Chief Performance Officer) have shown a strong commitment to implementing an effective control structure over Recovery Act activities and strong support for our oversight effort. We will work with the Department and the Treasury Inspector General for Tax Administration to help ensure that appropriate controls are in place.

Challenge 4: Management of Capital Investments

Managing large capital investments, particularly information technology investments, is a difficult challenge for any organization, whether public or private. In prior years, we have reported on a number of capital investment projects that either failed or had serious problems. Treasury is now making the transition to a new, mission-critical telecommunications system, TNet. The overall value of the TNet contract is estimated at $270 million. Treasury was originally to have begun the transition in February 2008. It is now expected to begin in December 2009, nearly 2 years late. In light of this delay, previously reported problems with large capital investments, and hundreds of millions of procurement dollars at risk, Treasury must exercise continuous vigilance in managing such investments.

Challenge 5: Anti-Money Laundering and Terrorist Financing/Bank Secrecy Act Enforcement

Treasury faces unique challenges in carrying out its responsibilities under the Bank Secrecy Act (BSA) and USA Patriot Act to prevent and detect money laundering and terrorist financing. The Financial Crimes Enforcement Network (FinCEN) is the Treasury bureau responsible for administering BSA. However, a large number of other federal and state entities participate in efforts to ensure compliance with BSA, including the five federal banking regulators, the Internal Revenue Service, the Securities and Exchange Commission, the Department of Justice, and state regulators. Many of these entities also participate in efforts to ensure compliance with U.S. foreign sanction programs administered by Treasury's Office of Foreign Assets Control (OFAC).

Treasury faces significant challenges in coordinating the efforts of these multiple entities, many external to Treasury. FinCEN and OFAC have entered into memoranda of understanding with many federal and state regulators in an attempt to build a consistent and effective process. However, these instruments are nonbinding and carry no penalties for violations, and their overall effectiveness has not been independently assessed. Furthermore, the USA Patriot Act has increased the types of financial institutions required to file BSA reports. In fiscal year 2008, financial institutions filed approximately 18 million BSA reports.

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Although BSA reports are critical to law enforcement, past audits have shown that many contain incomplete or erroneous data and that examination coverage by financial institution regulators of BSA compliance has been limited. In a response to our 2008 management challenges letter, Secretary Paulson said that FinCEN had published interpretive guidance in fiscal year 2008 to address many issues, including common errors noted in suspicious activity reports. The response also stated that FinCEN, OCC, OTS, and other federal banking regulators had studied and made adjustments to the risk-based examination process. We have not had the opportunity to assess these or other recent changes.

Given the criticality of this management challenge to the Department's mission, we continue to consider BSA and OFAC programs as inherently high-risk. Adding to this risk in the current environment is the risk that financial institutions and their regulators may decrease their attention to BSA and OFAC program compliance as they address safety and soundness concerns. As the administration and Congress consider what could be sweeping changes to the financial regulatory structure, those changes must ensure that BSA and OFAC compliance examination coverage is sufficient. Mandatory work, particularly material loss reviews of failed banks and thrifts, prevented us from performing any audits in this area in fiscal year 2009 and we do not expect to provide significant audit coverage in this area in fiscal year 2010.

Challenges Removed

We removed corporate management as an overarching management challenge, first identified as a challenge in 2004, because the Department has made significant progress in building up a sustainable corporate control structure. This progress was evident in the relatively smooth transition that occurred with the change in administrations this year. Treasury nevertheless remains a highly decentralized organization, and recent economic events have increased the number and complexity of its missions. Possible regulatory reforms could subject the Department's missions and structure to further change. In addition, Treasury has yet to fill many key leadership positions. Given these matters, senior leadership will need to ensure that the Department's corporate control structure remains strong and in place.

We removed information security as a management and performance challenge because Treasury has made significant strides in improving and institutionalizing its information security controls. We noted this progress in our two most recent annual Federal Information Security Management Act independent evaluations. Information security requires continued and strong management attention, however, so that policies remain current and practices do not deteriorate.

We would be pleased to discuss our views on these management and performance challenges in more detail.

cc: Daniel Tangherlini, Assistant Secretary for Management, Chief Financial Officer, and
Chief Performance Officer

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C.

SECRETARY OF THE TREASURY

December 11, 2009

MEMORANDUM FOR ERIC M. THORSON
INSPECTOR GENERAL

FROM: Timothy F. Geithner TFG

SUBJECT: Management and Performance Challenges Facing the Department of the Treasury

I am responding to your memorandum of October 29, 2009, describing your perspective on the most serious management and performance challenges facing the Department of the Treasury. The Department appreciates your independent assessment of progress in addressing these challenges.

Fiscal year (FY) 2009 brought a new management challenge, *Management of Recovery Act Programs*. The Department has established effective control structures to monitor the implementation of our Recovery Act programs to ensure they achieve their intended purposes, as well as to provide unprecedented accountability and transparency.

I want to thank you for recognizing our efforts in resolving *Corporate Management and Information Security* issues and for removing them from your listing of the Department's management challenges. We have taken, and will continue to take, appropriate actions to address those and remaining management challenges.

The Department is committed to remain vigilant about the risks associated with all of our programs and to adjust our strategies based on changing circumstances to achieve financial stability, economic security, and protection of the taxpayer. We look forward to working with you to further address these challenges.

Challenge 1 – Treasury's New Authorities Related to Distressed Financial Markets

The financial system and the economy are showing signs of stability. The cost of borrowing has declined to pre-crisis levels for many businesses, states and local governments, the government sponsored enterprises (GSEs), and the banks. Housing markets have shown signs of stabilization, and home prices have ticked up in recent months, after three straight years of declines. The economy grew in the third quarter, and most private economists predict it will grow for the remainder of this year and next. That improvement in the economic and financial outlook since the spring reflects a broad and aggressive policy response that included the financial stability policies implemented under the Troubled Asset Relief Program (TARP), efforts to bolster confidence in the housing and mortgage markets under the Housing and Economic Reform Act (HERA), other financial stability policies implemented by the Federal Deposit Insurance Corporation and the Board of Governors of the Federal Reserve System (Federal Reserve), accommodative monetary policy, and the Obama Administration's fiscal stimulus package implemented under the American Recovery and Reinvestment Act of 2009.

Despite TARP's positive record to date, and the improving financial and economic outlook, significant challenges remain for the financial sector and our economy. While the economy is growing again, jobs are still being lost and credit losses in some parts of the financial system are still accelerating. The pace of bank failures, which tends to lag economic cycles, remains elevated. Foreclosure rates also remain high. Bank lending continues to contract, with credit standards tight and demand still down. Small businesses rely heavily on such lending, as they do not have the ability to raise capital through debt issuance in securities markets. Further, commercial real estate losses weigh heavily on many banks, especially those that are small, impairing their ability to extend new loans. While a number of TARP initiatives have begun to wind down, Treasury continues to focus on stabilizing the housing markets as well as improving access to credit for small businesses. Based on the need for continuing work in these areas and also the need to ensure an orderly close out of the TARP Program, we have extended TARP authority to October 3, 2010. Following is additional information on actions we have taken and continue to take in addressing this challenge.

The Department of the Treasury's Office of Debt Management (ODM) has purchased over $200 billion in Mortgage Backed Securities (MBS) guaranteed by Fannie Mae and Freddie Mac through two expert asset managers, Barclays Global Investors and State Street Global Advisors. The Housing and Economic Recovery Act of 2008 granted Treasury the authority to make these purchases. That authority expires December 31, 2009. For increased transparency, the Department publishes aggregate information on its holdings of Agency MBS on FinancialStability.gov (***http://www.financialstability.gov/roadtostability/homeowner.html***). Treasury holds monthly executive committee meetings chaired by the Acting Under Secretary for Domestic Finance to discuss program implementation, and is actively seeking advanced risk management tools beyond those provided by the asset managers for the maintenance stage of the program. These tools will be in place by January 1, 2010.

We have tested the Government Sponsored Enterprises Credit Facility (GSECF) in a development environment and the Office of the Fiscal Assistant Secretary has established robust procedures for its use. The GSECF has not been used to date, nor do we expect it to be before its December 31, 2009 expiration date.

In October 2008, the Emergency Economic Stabilization Act authorized a total of $700 billion for Treasury to purchase or to insure troubled assets. Treasury used this authority to implement the Troubled Asset Relief Program (TARP) to strengthen the U.S. financial system, restore credit markets for businesses and consumers, and address foreclosures in the housing market. In fiscal year 2009, the Department rolled out eight programs: Capital Purchase Program; Targeted Investment Program; American International Group Investment Program (formerly known as the Systemically Significant Failing Institution Program); Automotive Industry Financing Program (including the Auto Suppliers Support Program and the Auto Warranty Program); Asset Guarantee Program; Term Asset-Backed Securities Loan Facility, as part of the Consumer and Business Lending Initiative; Public-Private Investment Program; and the Home Affordable Modification Program. As of September 30, 2009, over $521 billion had been designated for particular TARP programs. Of that amount, over $444 billion had been obligated to specific institutions under signed agreements, with over $365 billion of those funds already disbursed.

Treasury Departmental Offices and bureaus played a critical role in establishing a well-functioning Office of Financial Stability (OFS) to implement these programs. Over the past year, while aggressively implementing the programs listed above, OFS has grown into an organization of 212 full-time employees who support the TARP. Initially, several key Office of the Comptroller of the Currency (OCC) and Office of Thrift Supervision (OTS) personnel were detailed to OFS positions to provide assistance in setting up accounting, finance, and reporting systems. They also assisted in developing information technology, procurement, and risk management processes. The infrastructure put in place to support the TARP mitigates risk for the taxpayer. For each TARP operational program, sound controls and oversight have been properly designed, planned, and implemented for the longer term.

TARP was designed as an emergency response to a major financial crisis. Because financial conditions have begun to improve, Treasury has already started the process of exiting from some emergency programs. Although Treasury and other government institutions have accomplished a great deal in a relatively short time, more work lies ahead. As necessary, TARP will maintain capacity to address new developments until financial stability and economic health have been fully restored.

Challenge 2 - Regulation of National Banks and Thrifts

Both the Administration and Congress are in the midst of reviewing numerous proposals for financial regulatory reform. Treasury Departmental Offices, OCC, and OTS are working closely with other federal financial regulators to ensure a smooth transition to a new regulatory structure. The Department also expects to devote resources in 2010 toward implementing the recommendations of its working groups on the conduct of financial supervision and regulation and on the regulatory capital regime.

Regulation of National Banks

In fiscal year 2009, 13 OCC-supervised and regulated national banks failed, with estimated losses to the deposit insurance fund totaling approximately $3.7 billion. All 13 are community banks and the majority of these failures were the result of high concentrations in acquisition, development, and construction lending to the residential construction industry. In addition to taking actions to address the recommendations contained in the four Material Loss Review reports issued by your office during fiscal year 2009, the OCC conducted its own reviews of the national bank failures. Lessons learned included the need to reinforce adherence to OCC's policy on the timely use of and follow through on "Matters Requiring Attention," and the need to ensure that bank management and boards of directors provide effective oversight and adequate controls over risk. The OCC reports that the results of these critical reviews were used to communicate areas of concern to examiners and to adjust supervisory processes to better protect the safety and soundness of the national banking system.

During fiscal year 2009, the OCC introduced a program for its large national bank population that emphasized more intensive, ongoing monitoring of bank liquidity, standardization of liquidity measures across institutions, and evaluation of banks' liquidity cushions and contingency plans in the regular course of their OCC supervision.

In June the federal banking agencies released for comment the proposed *Interagency Guidance on Funding and Liquidity Risk Management*, which would effectively extend the features of the OCC's program to all domestic financial institutions. In September the federal banking agencies also released for comment proposed *Interagency Guidance on Correspondent Concentration Risks*. More broadly, the OCC worked with other financial supervisors, both domestically and internationally, to identify areas where risk management practices at financial institutions and supervisory expectations or requirements need to be strengthened. In this regard, the OCC is actively involved in efforts underway by the Basel Committee on Banking Supervision to strengthen and enhance international capital standards and liquidity risk management. The Comptroller continued to serve as co-chairman of the Financial Stability Board's working group on provisioning.

In the area of consumer regulation and protection, the OCC issued guidance to national banks on the Credit Card Accountability Responsibility and Disclosure (CARD) Act of 2009; Final Rules and Guidelines to Promote

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Accurate Reports about Consumers; and Final Rules and Guidelines Implementing Accuracy and Integrity Provisions of the Fair and Accurate Credit Transactions Act. The OCC also issued Consumer Advisories.

The OCC's Bank Supervision Operating Plan describes several key objectives for 2010. Effective credit risk and liquidity risk management, as well as the quality of capital and level of regulatory capital to absorb unexpected losses are areas of focus. Supervisory attention will also focus on corporate governance and compliance functions, the capability of bank management to manage risk, and the effective resolution of problem banks. The OCC will also encourage banks to continue to meet the needs of credit worthy borrowers and comply with consumer compliance laws and regulations.

Regulation of Thrifts

During fiscal year 2009, 14 OTS-regulated thrifts were placed in receivership with estimated losses to the deposit insurance fund of approximately $11 billion. Many of these failures were the result of poor risk management practices and excessive concentrations in high risk assets.

In addition to responding to Material Loss Review recommendations from your office, the OTS conducts internal reviews following the receivership of failed thrifts. The objective of the internal assessment is to review the chronology of events leading to the failure, identify the causes of the failure, evaluate OTS supervision and enforcement activities, and provide recommendations for addressing the findings of the review. The OTS completed seven such reviews in fiscal year 2009, and has made significant progress implementing the recommendations from these reviews.

During 2009, the OTS supplemented and improved staff guidance to address concentration risks, enforcement actions, capital contributions, downgraded securities, examination follow-up, and other key supervisory issues. The OTS also emphasized the importance of comprehensive loan modification programs to provide solutions for borrowers who cannot afford their current mortgage payments. In August, the OTS released Thrift Bulletin 85, *Regulatory and Accounting Issues Related to Modifications and Troubled Debt Restructurings of 1-4 Residential Mortgage Loans*, to update thrift management on accounting and regulatory issues associated with loan modification programs.

Also in 2009, the OTS issued a final rule prohibiting a series of unfair credit card practices under the Agency's authority to issue regulations under Section Five of the Federal Trade Commission Act banning unfair and deceptive acts and practices. The economic downturn will continue to have a significant affect on the performance of the thrift industry over the next several years.

To meet the challenges that will arise during fiscal year 2010, OTS has emphasized the following priorities in thrift supervision. During each regular examination OTS staff will review each thrift's operations to ensure it is properly managing any concentration risk in its portfolio, has sufficient capital commensurate with its operations, has appropriate and effective risk management controls, and has sufficient liquidity levels and contingency liquidity plans. The OTS will continue to work on an inter-agency basis with the other federal banking regulators to ensure fair and balanced regulation that includes appropriate counter-cyclical and systemic risk measures.

Reform efforts

As part of a comprehensive package of financial regulatory reform, Treasury has proposed legislation to overhaul the structure of federal supervision and regulation, including consolidating the OCC and OTS into one agency. Treasury's proposals would also make sure that all financial firms that own banks are subject to robust consolidated supervision by closing gaps and loopholes in the Bank Holding Company Act and requiring thrift holding companies to become bank holding companies. Other elements of the comprehensive reform include requiring all firms whose failure could threaten financial stability to submit to strong prudential supervision regardless of whether they own a bank; creating a Financial Services Oversight Council (FSOC) to monitor emerging threats; establishing a new Consumer Financial Protection Agency; and creating a resolution regime for large, highly interconnected financial firms to allow these firms to fail while protecting taxpayers and the economy.

Treasury also continues to work with the OCC, OTS, and other federal financial agencies to analyze lessons learned from the financial crisis and pursue appropriate reforms that do not require legislative action. Following on the release of the Treasury's regulatory reform legislative proposals, Treasury is leading working groups on regulatory capital and on the future of financial supervision and regulation. These working groups will make further proposals for strengthening the conduct of supervision and addressing shortcomings in rules and regulations. The Treasury expects that implementing their recommendations will require the commitment of all of these agencies in the next two years.

Challenge 3 – Management of Recovery Act Programs

Under the American Recovery and Reinvestment Act of 2009 (ARRA, or Recovery Act), Treasury administers grants, cash assistance in lieu of tax credits, economic recovery payments, and some 60 tax relief provisions which will deliver over $300 billion in relief to American families and businesses.

Treasury recognizes the immense challenges in managing its Recovery Act programs in a manner that ensures the programs achieve their intended purpose, provide for unprecedented accountability and transparency, and are free from fraud and abuse.

In implementing ARRA, the Department must ensure that we balance and meet the objectives of speed, quality and accountability. To achieve these objectives, Treasury established a Recovery Act implementation team responsible for working with the program offices across the Department. The Recovery Act team facilitates all Recovery Act implementation Department-wide and interfaces with the broader Recovery Act community. As part of this broad responsibility, the team establishes internal processes, addresses external data requirements, manages risk inherent in Recovery Act implementation, and coordinates Treasury Recovery Act audits. The team works closely with the Office of Management and Budget (OMB) and the Recovery Implementation Office to document progress on Recovery Act implementation and assists in implementing OIG/TIGTA/GAO recommendations.

Internally, the Recovery Act team developed detailed spend plans for its major programs and documents reporting responsibility for executing those initiatives. Treasury monitors and reviews those spend plans with bureau and Senior-accountable officials. This review focuses on items such as percent on-time performance for project activities, obligations and outlays versus plan, acquisition competition and contract types, performance measure actual values versus targets, and accountability metrics. Corrective and preventive actions, established as a result of the reviews, are tracked for implementation. We also review risk assessments and the implementation of mitigation plans to minimize the probability of fraud and abuse.

Treasury keeps the public informed through both agency and bureau websites and press releases, and monitors timely submissions to both the Recovery.gov and Treas.gov Recovery Act web pages.

ARRA established a number of innovative new programs to ease the impact of the credit crunch on state and local government budgets. One such program, which has been implemented very successfully by the Department of the Treasury, is the Build America Bond program (BAB). BABs are taxable bonds issued by state and local governments with a 35 percent interest subsidy paid directly to the issuer by the federal government. This bond program has allowed states to raise capital needed for crucial infrastructure projects by attracting new investors to the municipal bond market and reducing the issuer's debt cost. $47 billion in Build America Bonds were issued from the program's inception in April 2009 through the end of October, representing 21 percent of all municipal issuances in that time frame. A total of 42 states have participated in the program with over 500 separate issues. In addition to giving issuers access to much needed capital, the program has succeeded in making municipal debt attractive to new investors such as pension funds and foreign investors. By bringing in new investors, BABs have relieved supply pressure and have helped reduce borrowing costs on traditional tax-exempt municipal debt.

You expressed concern that Treasury staffing for two of our Recovery Act programs (cash assistance to states for low-income housing projects in lieu of tax credits and cash assistance for specified energy property in lieu of tax credits) is not commensurate with the size of these programs. The Office of the Fiscal Assistant Secretary assembled a core staff of five full-time employees to manage these programs. Although this is a small staff in relation to the size of the programs, we are achieving success by ensuring that this staff has appropriate skill sets and by leveraging the skills and expertise of others, both within and outside the Department. Staff members from several other offices within Treasury, including the IRS, are devoting time to these two programs. Additionally, we entered into an Interagency Agreement with the Department of Energy to provide necessary technical expertise in implementing the energy cash assistance program. We successfully implemented both of these programs in five months and have made awards to date in excess of $4 billion.

We recognize that staffing needs may change over the life of the programs, particularly as we move into the post-award monitoring phase. We therefore will continue to evaluate workforce needs and make adjustments as necessary.

Challenge 4 - Management of Capital Investments

The Department takes investment management very seriously and remains committed to improving the management of Information Technology (IT). In support of this commitment, the Department-level Executive Investment Review Board (E-Board), chaired by the Deputy Secretary and the Assistant Secretary for Management and Chief Financial Officer (ASM/CFO), met twice in fiscal year 2009. In support of the E-Board's efforts and to fulfill its IT Governance role, the Office of the Chief Information Officer (CIO) is actively engaged in the following activities:

Infrastructure Optimization – In July 2009, the Treasury E-Board endorsed a multi-faceted strategy for reducing the Department's IT infrastructure costs. To support this strategy, the Treasury CIO Council is developing a proposal of specific initiatives which will achieve cost savings by maximizing all infrastructure optimization and consolidation opportunities.

Monthly Evaluation of IT Investments – In July 2009, the Treasury CIO began monthly evaluations on the degree to which major IT investments met cost, schedule, and other performance goals. This information is made possible via a website hosted by OMB. The public transparency and increased frequency of assessments have resulted in increased executive attention to IT investment management, which in turn results in more consistent management of the Treasury IT budget.

Oversight of the Treasury Network (TNet) Transition – Recognizing the challenges associated with critical infrastructure investments, the Office of the CIO is actively overseeing the transition to Treasury's new consolidated wide area network project, TNet, and making a concerted effort to stay on schedule.

Challenge 5 - Anti-Money Laundering and Terrorist Financing/Bank Secrecy Act Enforcement

The Department does face unique challenges in carrying out its responsibilities under the Bank Secrecy Act (BSA) and the USA PATRIOT Act to prevent and to detect money laundering and terrorist financing, and we are focused on executing our mission as effectively as possible to protect the integrity of the financial system. The Financial Crimes Enforcement Network (FinCEN) has overall authority for BSA enforcement and compliance.

In the last several years, FinCEN has focused on effective and efficient administration, outreach, and engagement of existing industries covered by the BSA. The subsequent paragraphs highlight the actions FinCEN, in coordination with other federal and state authorities, completed in fiscal year 2009 with regard to existing industries. However, new payment systems and industries vulnerable to money laundering continually evolve, such as stored value cards, non-bank mortgage lenders, and hedge funds. In fiscal year 2010 and beyond, FinCEN will expand BSA regulations to new industry sectors, consistent with the Administration's priorities.

In fiscal year 2009, FinCEN published a proposal simplifying the organizational structure of BSA requirements. In addition, OCC, OTS, and FinCEN worked with other federal banking agencies to continue to enhance the Federal Financial Institutions Examination Council's *Bank Secrecy Act/Anti-Money Laundering Examination Manual*, first issued in 2005, with revisions to be issued in fiscal year 2010. Following up on the success of this manual, FinCEN worked with the IRS and state regulators to develop a Money Services Business (MSB) examination manual, released in fiscal year 2009. FinCEN facilitated the development of training materials on this manual, and fostered training for state examiners in fiscal year 2009, with further training scheduled in fiscal year 2010. Additionally, FinCEN issued a final rule in fiscal year 2009 simplifying the appropriate exemption of customers from currency transaction reporting requirements.

To enhance the efficiency and effectiveness of the BSA regulatory framework, FinCEN also initiated several rulemaking proposals in fiscal year 2009, including issuing notices of proposed rulemaking to accomplish the following:

- help ensure suspicious activity reports (SARs) are subject to appropriate protection and simultaneously issued proposed guidance to expand the ability of financial institution to share SAR information within their organizational structures;
- revise the regulatory definition of MSBs to make the determination of which businesses qualify as MSBs more straightforward; and
- move to streamline mutual fund BSA requirements by allowing mutual funds to file currency transaction reports.

FinCEN also sought comment on a wide range of questions pertaining to the possible application of anti-money laundering (AML) program and SAR rules to non-bank residential mortgage lenders and originators. In fiscal year 2010, FinCEN will continue working on these proposals, as well as regulations regarding stored value, as mandated by the CARD Act.

Outreach plays an important role in effectively administering the BSA. The Bank Secrecy Act Advisory Group (BSAAG) serves as the principal forum to discuss BSA issues among regulators, law enforcement, and the industry. FinCEN's Data Management Council enables government users of the BSA database to have a more direct role in providing advice about their information needs and helping FinCEN prioritize adjustments to the database. In fiscal year 2009, FinCEN continued outreach to specific financial institutions, visiting several large MSBs. We plan to conduct further outreach to additional industry segments in fiscal year 2010.

Active engagement with other regulators is also critical to meet our challenges. FinCEN established 55 memoranda of understanding (MOU) with federal and state regulators to enhance the sharing of information derived from compliance examinations, and by signing a MOU with the Commodity Futures Trading Commission (CFTC) in fiscal year 2009, FinCEN has now finalized MOUs with all federal functional regulators. FinCEN shared analytic reports in the form of BSA data profiles with these federal and state regulators, and surveyed its MOU partners to determine the impact of the information exchanged; 82 percent of respondents indicated the information shared with them was valuable. As these MOUs mature, the information exchanged will help FinCEN improve BSA examination consistency and compliance. In fiscal year 2010, FinCEN will pursue MOUs with additional state regulators.

To enhance regulated financial industry understanding of and compliance with BSA requirements, in fiscal year 2009 FinCEN published a range of interpretive guidance, including guidance to financial institutions on filing SARs regarding loan modification and foreclosure rescue scams; guidance on the scope of permissible information sharing covered by Section 314(b) safe harbor of the USA PATRIOT Act, and an educational pamphlet on the currency transaction reporting requirements. In fiscal year 2010, FinCEN will conduct strategic analytical studies and publish reports promoting both greater awareness of emerging money laundering trends, vulnerabilities, and avoidance of compliance expenditures that are not commensurate with actual risks. These initiatives will include additional analysis on mortgage loan and loan modification fraud.

A primary strategy for meeting the goal of a safer, more transparent financial system includes effective examination for any potential money laundering, terrorist financing, and BSA issues in OTS and OCC-supervised institutions. OTS and OCC continue to examine compliance with BSA, USA PATRIOT Act, and other anti-money laundering provisions through a process which consists of on-site examinations conducted every 12-18 months, supplemented by off-site monitoring and follow-up to address identified supervisory issues. Additionally, in fiscal year 2009 FinCEN and the IRS continued implementing a strategy for developing and implementing a more effective BSA examination regime for non-bank financial institutions that the IRS examines. Implementation of this strategy and other efforts, including enhancements to the non-compliance referral process, will continue through fiscal year 2010.

Challenge 5 also refers to Office of Foreign Assets Control (OFAC) programs and discusses OFAC MOUs with state and federal regulators. It is true that financial institutions' OFAC compliance programs are critical to the implementation of sanctions, and OFAC will continue to work with regulators and the regulated community to ensure attention to OFAC compliance is not lessened in the current environment. Substantively, the MOUs with Federal and State regulators are working as intended. OFAC keeps a financial institution's regulator fully informed about any apparent violation of OFAC regulations by that institution. This information is used to help the regulators develop the scope of the OFAC examination to which the institution should be subject. OFAC also requests and receives information from the regulators about the sufficiency of a financial institution's OFAC compliance program. This information is used as a factor in determining what level of enforcement action to take against a financial institution for an apparent violation of OFAC regulations. In addition to these formal requests, the regulators may contact OFAC if they have particular concerns about an institution.

cc: The Deputy Secretary
Assistant Secretary for Management and Chief Financial Officer

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INSPECTOR GENERAL for TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

October 15, 2009

MEMORANDUM FOR SECRETARY GEITHNER

FROM: J. Russell George J. Russell George
Inspector General

SUBJECT: Management and Performance Challenges Facing the Internal Revenue Service for Fiscal Year 2010

The Reports Consolidation Act of 2000[1] requires that the Treasury Inspector General for Tax Administration (TIGTA) summarize, for inclusion in the *Department of the Treasury Accountability Report for Fiscal Year 2009,* its perspective on the most serious management and performance challenges confronting the Internal Revenue Service (IRS or Service). The top 10 challenges in order of priority are:

1. Modernization;
2. Security;
3. Tax Compliance Initiatives;
4. Implementing Tax Law Changes;
5. Providing Quality Taxpayer Service Operations;
6. Human Capital;
7. Erroneous and Improper Payments and Credits;
8. Globalization;
9. Taxpayer Protection and Rights; and
10. Leveraging Data to Improve Program Effectiveness and Reduce Costs.

TIGTA's assessment of the major IRS management challenge areas for Fiscal Year 2010 has changed from the prior year. The changes include reorganizing the priority of challenges four through nine, revising the titles of three challenges to better reflect their current emphasis, and adding a new challenge entitled "Globalization."

Although not listed as challenges, two issues – tax law complexity and proposed healthcare reform legislation – warrant additional consideration. While "Complexity of the Tax Law" does not appear on this year's list of challenges because it has been overtaken by other concerns, it remains a serious, underlying issue with wide-ranging implications for both the IRS and taxpayers. Tax law complexity and frequent revisions to the Internal Revenue Code make it more difficult for the IRS to explain and enforce

[1] 31 U.S.C. § 3516(d).

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the tax laws and more costly for taxpayers who want to comply. However, as the IRS lacks the authority to enact changes to the tax law, it can do little but continue to react to the frequently changing Internal Revenue Code while the debate over many significant issues continues.

Similarly, numerous tax law changes are contained in the healthcare reform legislation presently working its way through Congress. The proposals include a number of provisions that could have a significant effect on the IRS in the coming year. As policies under consideration continue to look toward the Internal Revenue Code to effect changes, the IRS potentially faces the challenge of responding quickly by shifting resources and altering established plans. However, in doing so, there is some risk to the IRS's overall mission if the actions taken cause a decline in the quality and effectiveness of service or taxpayer perception.

The following is a discussion of each of the most serious management and performance challenges facing the IRS during Fiscal Year 2010.

Modernization

The Business Systems Modernization Program (Modernization Program or Program) is a complex effort to modernize IRS technology and related business processes. It involves integrating thousands of hardware and software components while replacing outdated technology and maintaining the current tax system. The IRS originally estimated that the Modernization Program would last up to 15 years and incur contractor costs of approximately $8 billion.[2] The Program is now in its 11th year and has received approximately $2.7 billion for contractor services, plus an additional $353 million for internal IRS costs.

TIGTA reviews have identified weaknesses in program management processes throughout the life of the Modernization Program. While the IRS has improved its controls over these processes as the Program has continued to mature, several weaknesses continue to exist. Recent TIGTA audits have identified continued problems in requirements development and management, program management, contract management and security controls.

Although the Modernization Program has continued to help improve IRS operations, project development activities have not always implemented planned processes effectively or delivered all planned system capabilities. The past year's Program performance did not continue the trend of improvement it demonstrated in the prior three years. For example, from May 2008 to May 2009, five of the 17 project milestones scheduled for completion were significantly over budget, and three of 17 milestones were significantly behind schedule.

The Modernization Program has experienced significant and frequent turnover of high-level IRS and Program executives. Since the Program began in 1999, three

[2] Treasury Inspector General for Tax Administration, Ref. No. 2009-20-136, *Annual Assessment of the Business Systems Modernization Program* (2009).

Commissioners, five Chief Information Officers, and, recently, a Chief Technology Officer have overseen the Program. Many of these executives have made major changes to the Program's direction and strategies during their tenure. These changes in direction and strategy have made it challenging to achieve continuity and long-term success.

The IRS has recognized that it faces challenges in meeting the requirements of the next phase of project development and system integration. As a result, the IRS has stated that a strategy correction is needed to meet changing business needs, have a more agile information technology environment, and reduce risks with associated costs to build and maintain systems.

The immediate challenge recognized by the IRS is the future of the Customer Account Data Engine,[3] the acknowledged centerpiece of the Modernization Program. Since the IRS initiated the Customer Account Data Engine project in 1999, after spending $335 million in development costs, it has been able to process only about 30 percent of the individual income tax returns filed. Limitations in Customer Account Data Engine capabilities, including those reported by TIGTA and the Government Accountability Office (GAO) in previous years, have resulted in the IRS's effort to reengineer processing of individual taxpayer accounts and the ability to use downstream systems to improve customer service. With the pending changes and the yet to be determined implementation of a reengineered process, the risks to the success of the Modernization Program are significant.

Since 1995, the IRS has identified and reported the Modernization Program as a material weakness. The Program and processes have not progressed enough to eliminate the material weakness designation. Until the IRS is able to show consistent progress and improvement in the management of its Modernization Program and adequately addresses past TIGTA and GAO recommendations, the Program will remain a high risk for the IRS and will continue to be considered a material weakness.

Security

Millions of taxpayers entrust the IRS with sensitive financial, personal, and other data that are processed by and stored on IRS computer systems. Reports of identity theft from both the private and public sectors have heightened awareness of the need to protect these data. The risk that taxpayers' identities could be stolen by exploiting security weaknesses in the IRS's computer systems continues to increase, as does the risk that IRS computer operations could be disrupted. Internal factors (such as the increased connectivity of computer systems and increased use of portable laptop

[3] The Customer Account Data Engine is the foundation for managing taxpayer accounts in the IRS Modernization plan. When completed, it will consist of databases and related applications that will replace the existing IRS Master File processing systems and will include applications for daily posting, settlement, maintenance, refund processing, and issue detection for taxpayer tax account and return data.

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computers) and external factors (such as the volatile threat environment resulting from increased terrorist and hacker activity) require strong security controls.

Homeland Security Presidential Directive-20[4] requires Federal Government agencies to develop business continuity plans[5] to enable the recovery of critical functions after a disaster or emergency. To comply with the Directive, the IRS must develop and continually update its business continuity plans to protect employees and recover critical business processes, data, and information technology systems. The IRS must protect large amounts of sensitive taxpayer data in addition to more than 100,000 employees and contractors in more than 660 facilities throughout the country. In reviews of these plans,[6] we determined that the IRS's business continuity planning efforts have not been sufficient to ensure that critical business processes and systems may be efficiently restored in the event of a disaster. We also found a majority of the incident management, business resumption, and disaster recovery plans lacked detailed planning information and recovery strategies.

The Federal Information Security Management Act (FISMA)[7] requires each Federal Government agency to report annually to the Office of Management and Budget and to Congress on the effectiveness of its security programs and to perform an annual independent evaluation of its information security program and practices. The number of incidents reported by Federal agencies has increased dramatically over the past three fiscal years, from 5,503 incidents in 2006 to 16,843 incidents in 2008.[8] The IRS has made steady progress in complying with FISMA requirements since the law's enactment in 2002 and continues to place a high priority on efforts to improve its security program. However, the IRS needs to do more to adequately secure its systems and data. Past audits have shown that the most significant areas of concern are compliance with mandated security configurations, implementation of access controls for computer systems, and use of audit trails to detect computer intrusions and misuse.

The introduction of malware,[9] also known as malicious code or malicious software, into the IRS network continues to present a growing security concern. Although the IRS has

[4] *National Continuity Policy*, dated May 4, 2007 (also known as National Security Presidential Directive-51). This Directive establishes a comprehensive national policy on the continuity of Federal Government structures and operations.
[5] IRS business continuity plans include an Occupant Emergency Plan, which provides instructions to safely evacuate employees and visitors from a facility or shelter them in place; an Incident Management Plan, which addresses the overall command structure that would be implemented in an emergency; a Business Resumption Plan, which provides instructions for recovering and restoring disrupted business processes; and a Disaster Recovery Plan, which addresses recovery and restoration of information technology systems and data.
[6] Treasury Inspector General for Tax Administration, Ref. No. 2009-20-038, *Better Emergency Preparedness Planning Could Improve Business Continuity Efforts* (2009).
[7] Federal Information Security Management Act of 2002, 44 U.S.C. §§ 3541–3549.
[8] U.S. Government Accountability Office, GAO-09-701T, *Information Security: Agencies Make Progress in Implementation of Requirements, but Significant Weaknesses Persist* (2009).
[9] Malware refers to a program inserted into a computer with the intent of compromising the confidentiality, integrity, or availability of an organization's data, applications, or operating systems.

had success in preventing serious infections, the number of malware incidents within the IRS continues to rise. Malware is difficult to combat because it is delivered through commonly used applications and devices, such as e-mail, the Internet, and portable media devices. Without sufficient controls to prevent the introduction of malware, IRS computers and the sensitive taxpayer data stored on them are at risk of compromise that could result in identity theft and fraud.

Identity theft and phishing[10] schemes are also growing security concerns. TIGTA works closely with the IRS to identify and investigate these schemes. Attempts at identity theft and phishing related to Federal income taxes continue to rise with incidents growing more than seven times in 2008.[11] In its 2009-2013 Strategic Plan, the IRS identifies the explosion in electronic data, online interactions, and related security risks as a major trend expected to affect the Service over the next five years.

Tax Compliance Initiatives

Another compelling challenge confronting the IRS is tax compliance. Tax compliance initiatives include the administration of tax regulations, collection of the correct amount of tax from businesses and individuals, and oversight of tax-exempt and government entities. Increasing voluntary compliance and reducing the Tax Gap[12] are currently the focus of many IRS initiatives. Nevertheless, the IRS is facing significant challenges in obtaining more complete and timely data, and developing the methods necessary to interpret the data.

Businesses and Individuals

The IRS estimated the gross Tax Gap for Tax Year (TY) 2001 to be approximately $345 billion. Underreporting of taxes, which is comprised of four major components (individual income tax, employment tax, corporate income tax, and estate and excise taxes), is estimated at $285 billion and accounts for the largest portion of the Tax Gap. Overall, the underreporting of individual income tax and employment tax constitute over 70 percent of the gross Tax Gap.

In August 2007, the Department of the Treasury and the IRS issued a report entitled *Reducing the Federal Tax Gap: A Report on Improving Voluntary Compliance*, which details the strategy being taken to address the Tax Gap by increasing voluntary compliance.[13] TIGTA provided an evaluation of this strategy in 2008 and reported that the long-term success of the strategy will, in large part, be dependent

[10] Phishing is the act of sending an e-mail to a user falsely claiming to be an established, legitimate enterprise in an attempt to scam the user into surrendering private information that could be used for identity theft.
[11] Internal Revenue Service Strategic Plan 2009-2013.
[12] The IRS defines the Tax Gap as the difference between the estimated amount taxpayers owe and the amount they voluntarily and timely paid for a tax year.
[13] An updated report providing an overview of efforts to close the Tax Gap was issued in July 2009.

on addressing several risk factors, including some that are beyond the control of the IRS.[14]

The IRS's Fiscal Year 2010 budget submission requests $603 million above its Fiscal Year 2009 enacted budget. More than half of this amount, $332 million, is intended for additional compliance initiatives that will target the Tax Gap. The IRS must continue to seek accurate measures for the various components of the Tax Gap and the effectiveness of the actions taken to reduce it. Broader strategies and better research are needed to determine what actions are most effective in addressing noncompliance.

Tax-Exempt Entities

The IRS continues to face challenges in administering programs focused on ensuring that tax-exempt organizations comply with applicable laws and regulations to qualify for tax-exempt status. The number of organizations granted tax-exempt status each year continues to increase. With more than $15 trillion in assets currently controlled by tax-exempt organizations or held in tax-exempt retirement programs and financial instruments, the IRS recognized in its 2009-2013 Strategic Plan that it must provide more careful oversight and advisory support than ever before. In addition, the IRS's Fiscal Year 2010 budget submission recognizes the importance of maintaining a strong enforcement presence in the tax-exempt sector to ensure charitable organizations are not used for non-charitable or illegal purposes, including financing terrorist activities.

In a report issued in Fiscal Year 2009, we determined that the Federal Government is at risk of losing future tax revenue because the IRS has not developed or implemented the processes necessary to identify and address noncompliance with State volume cap limits for tax-exempt private activity bonds. Without these processes, tax-exempt private activity bonds could be issued in excess of federally mandated yearly State dollar limits without the IRS detecting and addressing the noncompliance.[15]

<u>Implementing Tax Law Changes</u>

Each filing season tests the IRS's ability to implement tax law changes made by Congress. It is during the filing season that most individuals file their income tax returns and contact the IRS with questions about specific tax laws or filing procedures. Correctly implementing tax law changes is a continuing challenge because the IRS must identify the tax law changes; revise the various tax forms, instructions, and publications; and reprogram the computer systems used for processing returns. Changes to the tax laws have a major effect on how the IRS conducts its activities, what resources are required, and how much progress can be made on strategic goals.

[14] Treasury Inspector General for Tax Administration, Ref. No. 2008-30-094, *Additional Actions Are Needed to Effectively Address the Tax Gap* (2008).
[15] Treasury Inspector General for Tax Administration, Ref. No. 2009-10-097, *Future Tax Revenues Are at Risk Because Certain Tax-Exempt Bonds May Exceed Annual Dollar Limits Without Detection* (2009).

Congress frequently changes the tax laws, so some level of change is a normal part of the IRS environment. However, certain types of changes and the timing of those changes can significantly affect the IRS in terms of the quality and effectiveness of its service and how taxpayers perceive the IRS. In its 2009-2013 Strategic Plan, the IRS identifies the increasing complexity of tax administration, which includes responding to new tax provisions and adjusting to expiring ones, as a major trend expected to affect the Service over the next five years.

American Recovery and Reinvestment Act

The American Recovery and Reinvestment Act of 2009[16] (Recovery Act) was signed into law on February 17, 2009. The Recovery Act presents significant challenges to all Federal agencies as they move to implement provisions quickly while attempting to minimize risk and meet increased standards for transparency and accountability. With its numerous tax provisions, the Recovery Act poses significant challenges to the IRS as the Nation's tax collection agency and administrator of the tax laws. These provisions, which impact both individual and business taxpayers, will challenge the IRS as it attempts to implement the required changes over multiple filing seasons.

Other Tax Law Changes

Other recent legislation that has affected the IRS includes the Housing and Economic Recovery Act of 2008,[17] the Emergency Economic Stabilization Act of 2008,[18] and the Economic Stimulus Act of 2008.[19] These three Acts contained numerous tax law changes that challenged the IRS during the 2009 Filing Season. Despite these challenges, the 2009 Filing Season was generally successful, although the Recovery Rebate Credit, part of the Economic Stimulus Act of 2008, did cause significant taxpayer confusion. Although the IRS initiated a number of efforts to educate and assist individuals in computing the Recovery Rebate Credit, the Credit still resulted in millions of taxpayer errors. Two significant issues that could affect the IRS's 2010 Filing Season include Alternative Minimum Tax relief and the proposed healthcare legislation.

Providing Quality Taxpayer Service Operations

Since the late 1990's, the IRS has increased its delivery of quality customer service to taxpayers. In July 2005, Congress requested that the IRS develop a five-year plan, including an outline of which services the IRS should provide and how it will improve services for taxpayers. The IRS developed the plan – the Taxpayer Assistance Blueprint – which focuses on services that support the needs of individual filers who file

[16] Pub. L. No. 111-5, 123 Stat. 115.
[17] Pub. L. No. 110-289, 122 Stat. 2654.
[18] Pub. L. No. 110-343, 122 Stat. 3765.
[19] Pub. L. No. 110-185, 122 Stat. 613.

or should file the Form 1040 series tax returns.[20] The Blueprint includes performance measures, service improvement initiatives, and an implementation strategy for improving future service investment decisions. The IRS has begun implementing the initiatives, but many are dependent on future funding.

Despite having a plan in place to improve service, providing quality service to taxpayers remains a significant challenge for the IRS. For example, the Toll-Free Telephone Program only achieved a 58.8 percent Level of Service[21] during the 2009 Filing Season (through March 7, 2009) because of increased call demand for prior year Adjusted Gross Income and the Recovery Rebate Credit. Furthermore, the average speed to answer taxpayers' calls was 586 seconds (9.8 minutes), and the number of blocked calls during the 2009 Filing Season increased more than seven times over the 2008 Filing Season.[22] Taxpayer Assistance Centers[23] answered only 67 percent of tax law questions accurately and 82 percent of tax account[24] questions accurately.[25] Additionally, the Volunteer Program, which plays an increasingly important role in the IRS's efforts to improve taxpayer service and facilitate participation in the tax system, accurately prepared only 59 percent of TIGTA's test tax returns.

The Department of the Treasury and the IRS recognize that effective taxpayer service has a significant impact on voluntary tax compliance. Assisting taxpayers in preparing their returns by answering tax questions reduces the burden of notices and correspondence that taxpayers might have received if they made errors on their returns. Taxpayer service also reduces overall unintentional noncompliance and the need for compliance activity in the future. The IRS continues to focus on the importance of improving service by emphasizing it as one of the two main goals in its 2009-2013 Strategic Plan.

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[20] The Form 1040 series tax returns include any IRS tax forms that begin with "1040" such as the U.S. Individual Income Tax Return (Form 1040), U.S. Individual Income Tax Return (Form 1040-A), and Income Tax Return for Single and Joint Filers With No Dependents (Form 1040EZ).

[21] Level of Service is the IRS's primary measure of providing taxpayers with access to an assistor. Level of Service reflects the relative success rate of taxpayers who call the 20 Customer Account Services toll-free telephone lines seeking assistance from an assistor. It measures the success rate of access to the telephone system using the number of calls answered by IRS assistors.

[22] A blocked call is one that cannot be connected immediately because either: 1) no circuit is available at the time the call arrives (i.e., the taxpayer receives a busy signal); or 2) the system is programmed to block calls from entering the queue when the queue backs up beyond a defined threshold (i.e., the taxpayer receives a recorded announcement to call back at a later time). The IRS refers to the latter type of blocked call as a courtesy disconnect. The IRS blocked more calls during the filing season rather than allow more callers to wait on hold.

[23] Taxpayer Assistance Centers are walk-in sites where taxpayers can obtain answers to both account and tax law questions, as well as receive assistance in preparing their tax returns.

[24] A tax account is a record of a taxpayer's tax and tax-related data recorded on the IRS's Master File database.

[25] Treasury Inspector General for Tax Administration, Ref. No. 2009-40-058, *Interim Results of the 2009 Filing Season* (2009).

Human Capital

Since 2001, the GAO has designated strategic human capital management as a high-risk area within the Federal Government. In its 2009 update, the GAO reported that despite significant progress over the last few years the area remains a high risk because of a continuing need for a government-wide framework to advance human capital reform.[26]

The Commissioner of Internal Revenue (Commissioner) indicated his recognition of the need for greater attention to human capital. The Commissioner established the Workforce of Tomorrow Task Force to address recruitment and retention issues so that the IRS has the necessary leadership and workforce in place to address future challenges. Beginning in Fiscal Year 2008, TIGTA developed a broad audit strategy for addressing human capital at an IRS agency-wide level using the Human Capital Assessment and Accountability Framework[27] as a guide.

Like many other Federal Government agencies, the IRS has experienced workforce challenges over the past few years, including recruiting, training, and retaining employees, as well as an increasing number of employees who are eligible to retire. More than half of the IRS's employees and managers have reached age 50, and 39 percent of IRS executives are currently eligible for retirement. To fill the projected shortage in leadership, the IRS has stated that it must recruit one manager a day for the next 10 years. Furthermore, the rate at which new recruits in mission critical occupations are leaving the IRS during the first and second year of employment has increased since Fiscal Year 2005. The pending loss of institutional knowledge and expertise at all levels and the challenge of retaining a highly skilled workforce increase the risk that the IRS may not be able to achieve its mission.

The IRS's challenge of having the right people in the right place at the right time is made more difficult by many complex internal and external factors. The work performed by IRS employees continually requires greater expertise as tax laws become more complex, manual systems used to support tax administration become computer based, and attempts by taxpayers and tax practitioners to evade compliance with the tax laws become more sophisticated. The IRS must also compete with other Government agencies and private industry for the same human resources, complicated by the fact that younger generations of employees move between jobs more frequently than employees in the past. Furthermore, budget constraints, legislative changes, and economic shifts can create unforeseen challenges for the IRS in addressing its long-term human capital issues. In its 2009-2013 Strategic Plan, the IRS identifies human capital challenges as a major trend expected to affect the Service over the next five years.

[26] U.S. Government Accountability Office, GAO-09-271, *High Risk Series: An Update* (2009).
[27] The Framework was established by the United States Office of Personnel Management. It provides consolidated guidance for agencies to transform human capital management and understand what is to be done, how it can be done, and how to gauge progress and results. It also presents the expectations that guide the agency's assessment of human capital efforts.

Erroneous and Improper Payments and Credits

As defined by the Improper Payments Information Act of 2002,[28] an improper payment is 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 service, any duplicate payment, payments for services not received, and any payment that does not account for credit for applicable discounts. For the IRS, improper and erroneous payments generally involve improperly paid refunds, tax return filing fraud, or overpayments to vendors or contractors.

Refundable Credits

The IRS administers numerous refundable tax credits. These refundable credits allow individual taxpayers to reduce their tax liability below zero and, thus, receive a tax refund even if no income tax was withheld or paid. Two significant refundable credits are the Earned Income Tax Credit (EITC) and the Additional Child Tax Credit. The recently enacted American Recovery and Reinvestment Act of 2009 also authorized several new refundable credits, examples of which include the Making Work Pay Credit and First-Time Homebuyer Credit.

The EITC remains the main refundable credit and continues to be vulnerable to a high rate of noncompliance, including incorrect or erroneous claims caused by taxpayer error and resulting from fraud. The IRS has successfully developed a number of processes to identify erroneous EITC payments prior to issuance. However, because compliance resources are limited and alternatives to traditional compliance methods have not been developed, the majority of the potentially erroneous EITC claims identified continue to be paid in error. The IRS reports $10 billion to $12 billion annually in erroneous EITC payments.[29]

Contract and Other Payments

Each year, the Federal Government spends billions of dollars to acquire goods and services. In Fiscal Year 2008, Federal contracting outlays were more than $500 billion. Similarly, contract spending by the IRS represents a significant outlay of Service funds. Numerous past TIGTA audits have identified millions of dollars in questioned costs and several instances of contractor fraud. A summary of our work in this area over a period of approximately four years concluded that an incomplete invoice verification process resulted in the IRS paying approximately $7.5 million in questionable contract charges. In addition, an analysis of Defense Contract Audit

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[28] Pub. L. No. 107-300, 116 Stat. 2350.

[29] Treasury Inspector General for Tax Administration, Ref. No. 2009-40-024, *The Earned Income Tax Credit Program Has Made Advances; However, Alternatives to Traditional Compliance Methods Are Needed to Stop Billions of Dollars in Erroneous Payments* (2008).

Agency reports issued in Fiscal Years 2006 and 2007 identified approximately $167 million in questionable charges directly related to IRS contracts.[30]

Globalization

The scope, complexity, and magnitude of the international financial system present significant enforcement challenges for the IRS. As technology continues to advance and cross-border transactions rise, the IRS faces the growing challenge created by economic globalization. Technological advances have provided opportunities for offshore investments that were once only possible for large corporations and wealthy individuals.

Taxpayers with international activities – individuals, businesses, and tax-exempt organizations – continue to grow in number and variety. Examples of this trend include: 1) United States-based corporations more than tripled their foreign profits between 1994 and 2004, from $89 billion to $298 billion, with 58 percent of those profits earned in low-tax or no-tax jurisdictions; 2) the number of multinational corporations worldwide has grown from an estimated 3,000 in 1990 to over 63,000 in 2007; 3) the total income reported for 2005 from active foreign corporations owned by United States taxpayers exceeded $1.8 trillion; and 4) the percentage of Americans' income originating from foreign sources doubled between 2001 and 2006.

The IRS is challenged by a lack of information reporting on many cross-border transactions. In addition, the varying legal requirements imposed by different jurisdictions result in the formation of complex business structures that make it difficult to determine the full scope and effect of cross-border transactions. However, over the past few years, the IRS has taken actions to better coordinate international tax compliance issues. In September 2007, the IRS announced a Service-wide Approach to International Tax Administration highlighted by three strategic goals: 1) improving taxpayer service; 2) enhancing enforcement and modernizing the IRS for improving voluntary compliance with international tax provisions; and 3) reducing the Tax Gap attributable to international transactions. In addition, the Commissioner has emphasized that international issues will be a top priority during his tenure. The IRS has also made other changes to its structure and processes, including increasing cooperation and outreach efforts to foreign governments. In its 2009-2013 Strategic Plan, the IRS identifies accelerating globalization as a major trend expected to affect the Service over the next five years.

Taxpayer Protection and Rights

The IRS must ensure that tax compliance activities are balanced against the rights of taxpayers to receive fair and equitable treatment. The IRS continues to dedicate significant resources and attention to implementing the taxpayer rights provisions of the

[30] Treasury Inspector General for Tax Administration, Ref. No. 2008-10-092, *Procurement's Control Environment Was Ineffective and Did Not Prevent Overpayments to Contractors* (2008).

IRS Restructuring and Reform Act of 1998 (RRA 98).[31] Annual audit reports are mandated for the following taxpayer rights provisions:

- Notice of Levy;
- Restrictions on the Use of Enforcement Statistics to Evaluate Employees;
- Fair Debt Collection Practices Act Violations;
- Notice of Lien;
- Seizures;
- Illegal Protestor Designations;
- Assessment Statute of Limitations;
- Restrictions on Directly Contacting Taxpayers Instead of Authorized Representatives; and
- Separated or Divorced Joint Filer Requests.

In general, the IRS has improved its compliance with these statutory taxpayer rights provisions. The IRS has shown improvement over prior years when documenting that taxpayers were informed of their rights. However, there were still instances in which there was no documentation in the related case files to show that taxpayers were advised of their rights regarding assessment statute extensions,[32] and the IRS did not always follow procedures for mailing notices to taxpayers or their representatives in Federal Tax Lien cases.[33]

Some IRS management information systems do not track cases that require mandatory annual audit coverage.[34] Thus, neither TIGTA nor the IRS could evaluate the Service's compliance with certain RRA 98 provisions.

Leveraging Data to Improve Program Effectiveness and Reduce Costs

While the IRS has made some progress in using its data to improve program effectiveness and reduce costs, this area continues to be a major challenge. The IRS lacks a comprehensive, integrated system that provides accurate, relevant, and timely financial and operating data that describes performance measures, productivity, and associated costs of IRS programs. In addition, the IRS cannot produce timely, accurate, and useful information needed for day-to-day decisions, which hinders its

[31] Pub. L. No. 105-206, 112 Stat. 685 (codified as amended in scattered sections of 2 U.S.C., 5 U.S.C. app., 16 U.S.C., 19 U.S.C., 22 U.S.C., 23 U.S.C., 26 U.S.C., 31 U.S.C., 38 U.S.C., and 49 U.S.C.).
[32] Treasury Inspector General for Tax Administration, Ref. No. 2009-30-113, *Fiscal Year 2009 Statutory Audit of Compliance With Notifying Taxpayers of Their Rights When Requested to Extend the Assessment Statute* (2009).
[33] Treasury Inspector General for Tax Administration, Ref. No. 2009-30-089, *Additional Actions Are Needed to Protect Taxpayers' Rights During the Lien Due Process* (2009).
[34] Treasury Inspector General for Tax Administration, Ref. No. 2009-30-046, *Fiscal Year 2009 Statutory Review of Disclosure of Collection Activity With Respect to Joint Returns* (2009) and Treasury Inspector General for Tax Administration, Ref. No. 2009-30-054, *Fiscal Year 2009 Statutory Review of Restrictions on Directly Contacting Taxpayers* (2009).

ability to address financial management and operational issues to fulfill its responsibilities.

TIGTA and the GAO have continued to report that various IRS management information systems are insufficient to enable IRS management to measure costs, determine if performance goals have been achieved, or monitor progress in achieving program goals. In its most recent financial statement audit, the GAO noted that the IRS continues to face several key issues that represent material weaknesses in internal control, including not having current and reliable ongoing cost information to support management decision making and to prepare cost-based performance measures.[35] In addition, our analysis of the IRS's December 31, 2008, Federal Financial Management Improvement Act of 1996 (FFMIA)[36] remediation plan found that the IRS did not include remediation actions to address certain GAO findings and recommendations related to the IRS's noncompliance with the FFMIA. These findings and recommendations related to the IRS's Integrated Financial System, which provides the Service with an integrated accounting system to account for and control resources.[37]

Conclusion

The above are the ten major management and performance challenges for the IRS in Fiscal Year 2010. TIGTA's Fiscal Year 2010 Annual Audit Plan contains our planned reviews and is organized by these challenges. If you have questions or wish to discuss TIGTA's views on the IRS's challenges in greater detail, please contact me at (202) 622-6500.

cc: Deputy Secretary
Assistant Secretary for Management and Chief Financial Officer
Commissioner of Internal Revenue

[35] U.S. Government Accountability Office, GAO-09-119, *Financial Audit: IRS's Fiscal Years 2008 and 2007 Financial Statements* (2009).
[36] Pub. L. No. 104-208, 110 Stat. 3009.
[37] Treasury Inspector General for Tax Administration, Ref. No. 2009-10-094, *The Internal Revenue Service's Federal Financial Management Improvement Act Remediation Plan As of December 31, 2008* (2009).

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DEPARTMENT OF THE TREASURY
WASHINGTON, D.C.

SECRETARY OF THE TREASURY

December 11, 2009

MEMORANDUM FOR J. RUSSELL GEORGE
TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION

FROM: Timothy F. Geithner

SUBJECT: Response to Management and Performance Challenges Facing the Internal Revenue Service

I am responding to your October 15, 2009, memorandum describing the most serious management and performance challenges facing the Internal Revenue Service (IRS). The Department appreciates your independent assessment of progress in addressing these challenges. This memorandum provides information on the actions completed in Fiscal Year (FY) 2009 and the actions planned for fiscal year 2010 to address these challenges.

Challenge 1 - Modernization

In fiscal year 2009, IRS continued to execute on its long-term plan to modernize the technological underpinnings of the nation's tax system. The Customer Account Data Engine (CADE), Modernized e-File (MeF), and Account Management Services (AMS) modernization projects delivered the changes necessary for a successful tax filing season, supported implementation of the American Reinvestment and Recovery Act (ARRA) provisions, and provided audit trails to enhance the security posture of IRS systems.

Also in fiscal year 2009, the IRS enhanced its strategy to accelerate completion of a consolidated taxpayer account database, in part based on feedback from TIGTA. Contingent upon funding, the IRS plans to implement the new taxpayer account database for the 2012 filing season. The new database will support daily processing and result in faster refunds for all individual refund filers. Daily updating of individual taxpayer accounts by 2012 also will improve taxpayer service and accuracy, reduce interest paid on late refunds, improve data security, and create new tools to combat fraud and improve enforcement activities. Completion of the taxpayer account database is the prerequisite for other major initiatives, including significant expansion of online services and transactions and next generation of enforcement technologies.

Challenge 2 - Security

In fiscal year 2009, the IRS expanded its efforts to detect and prevent security threats. By securing infrastructure, data, and applications, the IRS protected access to taxpayer information. For example, every laptop at the IRS is equipped with sophisticated disk encryption software to protect against unauthorized use of sensitive data.

The IRS also maintained an agency-wide information security program and made major enhancements to its Disaster Recovery Program to ensure the continuity and resiliency of IRS critical business processing systems. An Emergency Management and Preparedness Executive Steering Committee was established to direct an IRS-wide emergency management program, and the Physical Security and Emergency Preparedness office focuses on management of the IRS continuity planning program.

The IRS takes the issue of Identity Theft very seriously. In fiscal year 2009, to preserve and enhance public confidence, the IRS established specialized units and dedicated toll-free telephone lines to provide guidance and assistance to taxpayers affected by identify theft. In the first year, the IRS responded to more than 120,000 calls and opened nearly 34,000 cases of suspected identity theft for further investigation. The IRS also placed markers on more than 231,300 taxpayer accounts to alert employees the account belongs to a substantiated identity theft victim. In fiscal year 2009, the IRS sent nearly 79,600 letters to individuals to inform them their personal information was used by another individual to file a return or may have been compromised through phishing scams. The IRS also eliminated the use of Social Security Numbers (SSNs) on more than 8 million forms, notices, and letters issued. This is the first large-scale effort to eliminate and reduce the use of SSNs on taxpayer correspondence. Over the next two to five years IRS will eliminate the use of SSNs on more than 90 million notices and forms sent to individual and business taxpayers.

To address the challenges of malicious code or software into the network, the Computer Security Incident Response Center (CSIRC) provides the IRS with a team of capable "first responders" organized, trained, and equipped to identify, contain, and eradicate cyber threats targeting IRS computing assets. In fiscal year 2009, the IRS repelled more than 35 million unauthorized access attempts, with about one-third of this malicious activity originating from outside the United States.

In fiscal year 2010, the IRS will continue to develop and update its business and continuity plans to protect employees and to recover the critical business processes, data, and information technology systems. A test and exercise program is in development that integrates all four business continuity plans used to prepare for, respond to, and recover from a disaster or emergency incident.

Challenge 3 - Tax Compliance Initiatives

During fiscal year 2009, the IRS focused on targeting its enforcement efforts on high-risk categories of non-compliance to support the overall goal of reducing the tax gap. In addition to the specific programs outlined below, the IRS continued work on a reporting compliance study for individual taxpayers that will provide updated and more accurate audit selection tools as the first of an ongoing series of individual studies using a rolling multi-year methodology. Studies in subsequent tax years will allow the IRS to make more frequent updates to its voluntary compliance estimates.

The IRS has a seven-part, multi-year strategy to address the Tax Gap as presented in the July 2009 Tax Gap Report. The strategy outlines a series of initiatives designed to reduce opportunities for tax evasion by implementing more stringent reporting requirements, making a commitment to providing more useful, up-to-date estimates of the tax gap, and continuing to make improvements in information technology to help make early detection and intervention efforts more effective. Additional strategies include supporting a sustained focus in the areas of greatest risk including international enforcement, improved compliance programs for business and high-income individuals, and providing innovative on-line services and streamlined written communication to enhance taxpayer services. Reform and simplification of the tax law includes the continuing effort to simplify tax forms and publications and taxpayer burden reduction actions. The multi-pronged strategy also includes ensuring ethical standards of conduct for tax preparers to improve taxpayer compliance.

IRS actions to address compliance by businesses and individuals in fiscal year 2009 included expanded enforcement presence in the international field and continued pursuit of high net-worth noncompliant taxpayers.

The IRS also developed a tax preparer strategy to identify recommendations to ensure consistent standards for tax preparer qualifications, ethics and service. The recommendations will be developed from information obtained from a large and diverse constituent community that included those licensed by state and federal authorities, unlicensed tax preparers, software vendors, consumer groups and taxpayers. Over 450 taxpayers and tax professionals along with 600 employees responded to the IRS request for comments to help better leverage the tax return preparer community with the twin goals of increasing taxpayer compliance and ensuring uniform and high ethical standards of conduct for tax preparers.

In fiscal year 2010 the IRS will significantly expand international enforcement, implement significant new information reporting authorities into compliance programs, and move toward higher standards in the tax practitioner community.

Challenge 4 – Implementing Tax Law Changes

The IRS is faced with implementing tax law changes each filing season. In response to recent revisions to the tax laws, the IRS helped taxpayers file correct tax returns by providing education and outreach through automation, face-to-face contact, and the media. In fiscal year 2009, taxpayers continued to use the IRS website, IRS.gov, in record numbers to get current information. Passage of the First-Time Homebuyer Credit and ARRA, as well as questions on the Recovery Rebate Credit resulted in the IRS providing real-time, updated information to taxpayers as they filed their returns.

The IRS also delivered outreach and education to the tax professional community, industry partners, and small business and self-employed taxpayers through a wide range of strategies, outreach products and communication vehicles such as Webinars, tax practitioner institutes, and National Tax Forums. In addition, the IRS website was expanded to include an online version of the Small Business Resource Guide and Small Business Tax Center; an interactive Spanish application for "How much was my Stimulus Payment?"; and a Spanish Tax Practitioner Tool Kit.

American Recovery and Reinvestment Act

The IRS expedited completion of tax products to address ARRA provisions. Before enactment, the IRS initiated work on the tax-related provisions to ensure timely implementation, including releasing forms, schedules and guidance three days after enactment; developing new publications to explain the tax provisions to individual and business filers; and informing taxpayers of the tax credits they may be entitled to using multiple communication channels including press releases, television commercials, and updated information on the irs.gov website. For the first time, the IRS launched a YouTube video site and an ITunes podcast site to provide information on ARRA, tax tips, and how-to videos. This comprehensive approach to administering the provisions of ARRA allowed the IRS to meet taxpayer and stakeholder expectations for these important tax law changes.

Other Tax Law Changes

Other recent legislation contained tax law changes, including the Housing and Economic Recovery Act of 2008; the Emergency Economic Stabilization Act of 2008; the Economic Stimulus Act of 2008; and the Worker, Retiree, and Employer Recovery Act of 2008. The IRS delivered a successful 2009 filing season despite the substantial number of legislative actions (500 actions affecting 203 tax products) required from these Acts.

Although resources were strained, 95 percent of the critical individual filing season products and over 96 percent of the tax-exempt and business tax products were delivered timely.

The IRS provided taxpayers with online access to tax law information, including tax law changes, in an easily understandable format on IRS.gov. In fiscal year 2009, taxpayers used the site to find out about the Rebate Recovery Credit. More than 54 million taxpayers used the "Where's My Refund?" calculator to check on the status of their tax refund, an increase of 38 percent, and over 430,000 taxpayers used the Spanish version. Over 650,000 taxpayers who did not receive a stimulus payment in 2008 used the new Recovery Rebate Credit calculator to help them determine if they were eligible for the credit, and if so, how much they could claim.

In fiscal year 2010, the IRS will continue to monitor proposed changes to the tax laws, including Alternative Minimum Tax relief and the proposed health-care legislation, and prepare accordingly to ensure taxpayers have the necessary forms and information for the filing season.

Challenge 5 - Providing Quality Taxpayer Service Operations

In fiscal year 2009, the IRS continued the implementation of Taxpayer Assistance Blueprint (TAB) service improvements. A new group was created to identify and coordinate enterprise-wide service improvements from the taxpayer's perspective. The initiatives included the implementation of an online tool which provides taxpayers with tax- law information in an easily navigable format, the creation of 332 "talking Tax Forms" for visually impaired taxpayers, and the launch of Spanish versions of the Free File Program.

The IRS provided extensive media coverage and expanded electronic outreach activities to make taxpayers aware of new credits, deductions, and exclusions for which they qualified. A second "Super Saturday" event was held in fiscal year 2009, and the IRS provided over 11,000 taxpayers with tax assistance and return preparation. The event was the largest one-day outreach service event in IRS history.

The IRS also provided assistance to millions of taxpayers by expanding partnerships with nonprofit and community organizations, opening more than 12,100 free tax preparation sites nationwide. Volunteers at these sites prepared over 3.0 million returns for low-income and elderly taxpayers. The IRS also served 6.2 million taxpayers at the Taxpayer Assistance Centers (TACs).

In fiscal year 2010, the IRS will continue to provide quality taxpayer service by implementing additional improvements outlined in the TAB, including greater access to available services on non-workdays through events like "Super Saturday." The IRS also will improve the taxpayer's filing experience by implementing new quality standards at the TACs and volunteer return preparation sites through reviews of selected prepared returns to determine accuracy.

Challenge 6 - Human Capital

In fiscal year 2009, the IRS engaged in an extensive enforcement hiring initiative, resulting in an enforcement staffing increase of more than 3,000 employees. To ensure coordination at all levels, the IRS established a governance structure to provide oversight of the hiring initiative and created a centralized office to coordinate all recruiting efforts. For the first time, candidates who applied for multiple jobs in different locations were ranked and interviewed only once, and competing organizations collaborated on selections to ensure the best-skilled individual was hired for each position. The IRS also increased its veteran hiring by 85 percent from 901 in fiscal year 2006 to 1,669 in fiscal year 2009 with targeted recruitment efforts.

The report of the IRS Workforce of Tomorrow (WOT) Task Force was released in August 2009. The report included initiatives to improve the hiring process to ensure continued success in filling critical enforcement positions. Highlights included creation of a detailed workforce planning model that can be embedded into the existing planning processes, a centralized recruiting organization and corporate recruiting strategy that ensures consistent brand messaging and engagement of local leaders, an enhanced hiring process implemented in phases that can cut hiring time by 50 percent, reduction of managerial burden initiatives, enhanced training and support for managers, and a leadership development process to identify and develop leaders across the IRS.

In fiscal year 2010, the IRS will implement additional WOT recommendations, implement streamlined hiring, and pilot an accelerated leadership program for high potential candidates.

Challenge 7 - Erroneous and Improper Credits and Payments

The IRS has a balanced and comprehensive plan, including compliance activities and systemic changes, to reduce improper payments.

Refundable Credits

In fiscal year 2009, the IRS protected over $3.2 billion in revenue through EITC enforcement efforts, including examination of over 500,000 returns and 25,000 amended returns claiming EITC, 314,000 document matching reviews, and 300,000 math error process corrections. The IRS also identified more than 123,000 fraudulent returns claiming over $361 million in refunds and stopped over $90 million in fraudulent claims using the Electronic Fraud Detection System (EFDS).

The IRS also completed activities associated with the EITC Return Preparer Study, including analyzing short-term outcomes from due diligence visits, developing new education and compliance notices, making phone calls to first-time EITC preparers to make sure they understand the program guidelines, and adjusting the timing of EITC paid preparer due diligence visits to clarify procedures. These improvements resulted in a 5 percent increase in due diligence visits over 2008 and proposed penalties of $462,500. Additionally, the IRS continued to identify and investigate high-impact EITC fraud and tax scheme promoters and identified research-based approaches to improve EITC participation and minimize taxpayer errors.

The manner and means by which individuals deploy fraudulent refund schemes are constantly evolving and are becoming more complex and sophisticated. The Questionable Refund Program (QRP), a nationwide multifunctional program designed to identify fraudulent returns and to stop payment of fraudulent refunds, continued to show positive results. In fiscal year 2009, the IRS identified over 414,000 potentially fraudulent returns claiming over $2.7 billion in total refunds and initiated 418 investigations with an 86.6 percent conviction rate, a 78.8 percent incarceration rate, and an 87.2 percent publicity rate on adjudicated cases.

In fiscal year 2010, the IRS will continue to identify and investigate EITC tax scheme promoters and preparers through improved data matching, while utilizing automated under-reporter data to identify outreach and education opportunities for identified patterns of noncompliance. In addition, the IRS will improve the accuracy of EITC returns by refining the due diligence audit process, conducting visits by revenue and criminal investigation agents, streamlined injunctions, and notice and phone contact treatments.

Contract and Other Payments

To properly account for contract spending, the IRS developed templates for documenting contract type decisions and rationale when Performance-Based Acquisition methods are not used. In addition, a module entitled, "Types of Work Statements, Appropriate Contract Types and Risk," will be included in the annual Advance Acquisition Planning conference to emphasize the importance of the acquisition team selecting the appropriate contract type. The IRS will continue to utilize the Contract Review Board established in fiscal year 2008 to review all information technology acquisitions meeting established dollar thresholds.

Challenge 8 - Globalization

International compliance is a key challenge as reflected by its recent enforcement initiatives, as well as its prominence in the IRS Strategic Plan.

The IRS has placed unprecedented focus on detecting and bringing to justice those who hide assets overseas to avoid paying tax. As part of an overall IRS strategy to improve offshore compliance, new initiatives were implemented to identify US taxpayers that engaged in offshore tax evasion schemes.

The IRS established an Offshore Voluntary Disclosures/Penalty Framework for taxpayers to voluntarily disclose their offshore activities. The framework provides taxpayers the opportunity to calculate the total cost of resolving all offshore tax issues; become compliant with U.S. tax laws; make voluntary disclosures that will be used to further the IRS understanding of how foreign accounts and foreign entities are promoted to U.S. taxpayers as ways to avoid or evade tax; and provide data to be used in developing additional IRS strategies to inhibit promoters and facilitators from soliciting new clients. Thousands of taxpayers with offshore accounts voluntarily came forward to disclose information as a result of this initiative.

In fiscal year 2010, the IRS will continue its focus on international tax enforcement. In addition, the IRS will use audit results and intelligence from ongoing offshore initiatives to refine case identification and selection methods and to identify promoters, facilitators and participants in abusive offshore arrangements. The IRS will also improve the way compliance risks are identified and addressed in large, complex global businesses and high wealth individuals.

Challenge 9 - Taxpayer Protection and Rights

Taxpayer protection is a top priority for the IRS. In fiscal year 2009, the IRS continued to monitor compliance with the taxpayer rights provisions of the IRS Restructuring and Reform Act of 1998 (RRA 98), including quarterly managerial certifications and annual independent reviews of the RRA 98 Section 1204 provisions. The certification process serves to ensure management does not use enforcement statistics to evaluate employees and drive behavior in conflict with taxpayer rights. As TIGTA indicated in its report, the IRS has shown improvement over prior years that taxpayers were informed of their rights.

In fiscal year 2009, the IRS also completed an oversight review/approval process for preparer penalties to ensure uniform and consistent application of penalties; continued efforts to remove or redact Social Security Numbers from outgoing correspondence; and completed an analysis of excluding all Social Security Administration (SSA) recipients below certain income levels from the Federal Payment Levy Program.

Actions planned for fiscal year 2010 and beyond include the implementation of a low-income filter that will exclude taxpayers that are more likely to experience a hardship if included in the Federal Payment Levy Program. The IRS also will identify parameters for contractors regarding the protection of taxpayer Personally Identifiable Information (PII) for inclusion in all publishing contracts. Additionally, adoption of a broad set of recommendations around regulation of tax preparers will be at the forefront of IRS efforts.

Challenge 10 – Leveraging Data to Improve Program Effectiveness and Reduce Costs

In fiscal year 2009, the IRS continued to make significant progress in financial management, particularly in the development and provision of cost information across multiple business units. As a result, in its audit of the fiscal year 2009 IRS financial statements, GAO determined that the remaining issues regarding Financial Reporting no longer constituted a material weakness and that the remaining issues regarding Tax Revenue and Refunds no longer constituted a significant deficiency.

In fiscal year 2010, the IRS will continue its use of the managerial cost accounting system to conduct cost-benefit analyses that provide timely, accurate, and useful data for decision making by the major business units.

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Appendix D: Material Weaknesses, Audit Follow-Up, Financial Systems, and Recovery Act Risk Management

This section consists of detailed descriptions of Treasury's material weakness inventory, including a summary of actions taken and planned to resolve the weaknesses; tracking and follow-up activities related to Treasury's GAO, OIG, TIGTA, and the Special Inspector General for the Troubled Asset Relief Program audit inventory; an analysis of potential monetary benefits arising from audits performed by Treasury's Inspectors General; an update on Treasury's financial systems framework; and an overview of Treasury's risk management activities for the implementation of the *American Recovery and Reinvestment Act of 2009* (Recovery Act or ARRA).

TREASURY'S MATERIAL WEAKNESSES

Management may declare audit findings or internal situations as a material weakness whenever a condition exists that may jeopardize the Treasury mission or continued operations. Reporting on material weaknesses is required in these instances by the *Federal Managers' Financial Integrity Act of 1982* (FMFIA) and the *Federal Financial Management Improvement Act of 1996* (FFMIA).

FEDERAL MANAGERS' FINANCIAL INTEGRITY ACT OF 1982 (FMFIA)

The FMFIA requires agencies to establish and maintain internal control. The Secretary must annually evaluate and report on the controls (FMFIA Section 2) and financial systems (FMFIA Section 4 and FFMIA) that protect the integrity of federal programs. The requirements of the FMFIA serve as an umbrella under which other reviews, evaluations, and audits should be coordinated and considered to support management's assertion about the effectiveness of internal control over operations, financial reporting, and compliance with laws and regulations.

As of September 30, 2009, Treasury has five material weaknesses under Section 2 of the FMFIA, summarized as follows:

SUMMARY OF FMFIA AND FFMIA MATERIAL WEAKNESSES	SECTION 2	SECTION 4	TOTAL
Balance at the Beginning of FY 2009	4	0	4
Closures/Downgrades during FY 2009	0	0	0
Reassessed during FY 2009	0	0	0
New MW declared during FY 2009	1	0	1
Balance at the End of FY 2009	5	0	5

Below are detailed descriptions of Treasury's five material weaknesses:

MATERIAL WEAKNESS DESCRIPTION	
Internal Revenue Service - Improve Modernization Management Controls and Processes	
The IRS needs to improve its Business Systems Modernization program. Key elements: • Assess the recommendations from the Special Studies and Reviews of the Business Modernization program and projects • Implement and institutionalize procedures for validating contractor-developed costs and schedules • Establish effective contract management practices • Complete a human capital strategy • Improve configuration management practices	
Actions Completed	**What Remains to be Done**
✓ Deployed Release 4.2 of the Customer Account Data Engine (CADE) in January 2009. CADE added capabilities to process prior-year and decedent returns, remittances, estimated tax payments, requests for extensions, and surname changes ✓ Deployed Modernized e-File (MeF) release 5.5 that included the redesigned Form 990 (Return of Organization Exempt from Income Tax) in time for the filing season ✓ Completed the 2009 releases of Account Management Services (AMS) providing additional real-time changes to CADE	❍ Allow assessment time to observe long-term effect of actions completed and demonstrate sustained improved performance ❍ Targeted Downgrade/Closure: FY 2011

MATERIAL WEAKNESS DESCRIPTION	
Internal Revenue Service - Computer Security	
The IRS has various computer security controls that need improvement. Key elements: • Adequately restrict electronic access to and within computer network operational components • Adequately ensure that access to key computer application and systems is limited to authorized persons for authorized purposes • Adequately configure system software to ensure the security and integrity of system programs, files, and data • Appropriately delineate security roles and responsibilities within functional business operating and program units, as required by the Federal Information Security Management Act • Appropriately segregate system administration and security administration responsibilities • Sufficiently plan or test the activities required to restore certain critical business systems where unexpected events occur • Effectively monitor key networks and systems to identify unauthorized activities and inappropriate system configurations • Provide sufficient technical, security-related training to key personnel • Certify and accredit 90 percent of all systems	
Actions Completed	**What Remains to be Done**
✓ Security roles and responsibilities ✓ Security/System Administration segregation of duties ✓ Security training ✓ Certification and Accreditation	❍ Network access controls ❍ Systems/Application controls ❍ Systems software configuration access controls ❍ Contingency planning ❍ Audit trails ❍ Targeted Downgrade/Closure: FY 2012

MATERIAL WEAKNESS DESCRIPTION	
Internal Revenue Service - Financial Accounting of Revenue – Custodial The IRS needs to have detail data to support custodial financial reporting of revenue. Key elements: • Inability to provide detailed support for large types of revenue for employment and excise taxes • Lack of effective custodial supporting systems/subsidiary detail • Subsidiary ledger does not track and report one Trust Fund Recovery Penalty (TFRP) balance • Untimely posting of TFRP assessments and untimely review of TFRP accounts • Lack of a single, integrated general ledger to account for tax collection activities and the costs of conducting those activities • IRS's general ledger for its custodial activities does not use the standard federal accounting classification structure	
Actions Completed	**What Remains to be Done**
✓ Masterfile Custodial Detail Database (CDDB) Trace ID in production and the production of mismatch reports for the reconciliation process put in place ✓ Completion of CDDB release to load frozen credits ✓ Proper crediting of payments to all associated parties on TFRP accounts created since October 2001	❍ Completion of CDDB Releases to provide a single, integrated subsidiary ledger using standard federal accounting classification structure ❍ Targeted Downgrade/Closure: FY 2010

MATERIAL WEAKNESS DESCRIPTION	
Financial Management Service - Consolidated Government-wide Financial Statements The Federal Government does not have adequate systems, controls, and procedures to properly prepare the Consolidated Government-wide Financial Statements. Key elements: • The government lacks a process to obtain information to effectively reconcile the reported excess of net costs over revenue with the budget deficit, and when applicable, a reported excess of revenue over net costs with a budget surplus • Weaknesses in financial reporting procedures in internal control over the process for preparing the Consolidated Financial Statements	
Actions Completed	**What Remains to be Done**
✓ Partially reconciled FY 2008 operating revenues with budget receipts ✓ Developed a model to provide analysis of unreconciled transactions that affect the change in net position. ✓ Accounted for intra-governmental differences through formal consolidating and elimination accounting entries using all reciprocal fund categories including the General Fund ✓ Federal agencies submit complete closing packages to GAO ✓ Established traceability from agency footnotes to the Consolidated Financial Statements for completeness	❍ Complete reconciliation of operating revenues to budget receipts ❍ Complete reciprocal category for the Treasury General Fund ❍ Implement changes identified by the Office of the Fiscal Assistant Secretary as a result of its review of the Reporting Entity definitions per the Financial Accounting Standards ❍ Include all disclosures as appropriate ❍ Include all loss contingencies as appropriate ❍ Targeted Downgrade/Closure: FY 2012

MATERIAL WEAKNESS DESCRIPTION	
Treasury Departmental Offices - Financial Management Practices The Office of Accounting and Internal Control (AIC) has not fully developed sufficient internal control over the underlying financial data included in the consolidated balance sheet to ensure it is complete and accurate. This is due in part because the financial infrastructure for the financial reporting responsibilities of the Treasury Department is inadequately staffed for such a large and complex Executive Agency. Key elements: • AIC has not developed clear, step-by-step procedures for performance of the financial statements analyses or clearly explained and presented the methodogy used for preparation of these analyses. • AIC has not clearly documented procedure manuals or process flow documentation. • Key senior financial management and budget staff positions were vacant during critical time periods • Lack of continuity with historical knowledge and experience caused significant delays in audit deliverables as well as in addressing accounting issues.	
Actions Completed	**What Remains to be Done**
✓ Initiated development of standard operating procedures and cross-training of staff on financial statement process ✓ Filled AIC credit reform accountant and two senior accounting positions ✓ Obtained authorization for two additional staff accountant positions in AIC ✓ Filled three staff positions in the Office of Financial Management ✓ Filled two Budget Execution positions ✓ Brought contractors aboard to assist with GSE transactions	❍ Study existing analytical and review processes, then develop/revise policy and procedures ❍ Fill two new AIC accountant positions ❍ Review current funding, staffing, skill competencies, contract support, and training, and determine proper levels needed to fully perform daily operations ❍ Based on results of review, hire additional staff, establish additional contract service support, and/or establish agreements with Treasury bureaus for detailees ❍ Provide additional training and guidance to staff ❍ Targeted Downgrade/Closure: FY 2010

AUDIT FOLLOW-UP ACTIVITIES

During fiscal year 2009, Treasury placed renewed emphasis on both the general administration of internal control issues throughout the Department and the timely resolution of findings and recommendations identified by the Office of the Inspector General (OIG), the Treasury Inspector General for Tax Administration (TIGTA), the Special Inspector General for the Troubled Asset Relief Program (SIG TARP), the Government Accountability Office, and external auditors. During the year, Treasury continued to implement enhancements to the tracking system called the "Joint Audit Management Enterprise System" (JAMES). JAMES is a Department-wide, interactive, web-based system accessible to the OIG, TIGTA, SIG TARP, bureau management, Departmental management, and others. The system tracks information on audit reports from issuance through completion of all corrective actions required to address findings and recommendations contained in an audit report. JAMES is the official system of record for Treasury's internal control program.

POTENTIAL MONETARY BENEFITS

The *Inspector General Act Amendments of 1988*, Public Law 101-504, require the Inspectors General and the Secretaries of Executive Agencies and Departments to submit semiannual reports to the Congress on actions taken on audit reports issued that identify potential monetary benefits. The Department consolidates and analyzes all relevant information for inclusion in this report. The information contained in this section represents a consolidation of information provided separately by the OIG, TIGTA, and Department management.

In the course of their audits, the Inspectors General periodically identify questioned costs, make recommendations that funds be put to better use, and identify measures that demonstrate the value of audit recommendations to tax administration and business operations. "Questioned costs" include:

- a cost that is questioned because of an alleged violation of a provision of a law, regulation, contract, or other requirement governing the expenditure of funds
- a finding, at the time of the audit, that such costs are not supported by adequate documentation (i.e., an unsupported cost)
- a finding that expenditure of funds for the intended purpose is unnecessary or unreasonable

The Department regularly reviews progress made by the bureaus in realizing potential monetary benefits identified in audit reports, and coordinates with the auditors as necessary to ensure the consistency and integrity of information on monetary benefit recommendations being tracked.

The statistical data in the following summary table and charts represent audit report activity for the period from October 1, 2008 through September 30, 2009. The data reflect information on reports that identified potential monetary benefits issued by the OIG and TIGTA.

AUDIT REPORT ACTIVITY WITH POTENTIAL MONETARY BENEFITS FOR WHICH MANAGEMENT HAS IDENTIFIED CORRECTIVE ACTIONS (OIG AND TIGTA)
OCTOBER 1, 2008 THROUGH SEPTEMBER 30, 2009
(DOLLARS IN MILLIONS)

	Disallowed Costs		Better Used Funds		Revenue Enhancements		Totals	
	Reports	Dollars	Reports	Dollars	Reports	Dollars	Report Total	Total Dollars
Beginning Balance	11	$ 35.1	4[1]	$ 17.2[1]	10	$ 753.2	25	$ 805.5
New Reports	9	2.9	5	9,058.9	11	2,766.2	25	11,828
Total	20	38.0	9	9,076.1	21	3,519.4	50	12,633.5
Reports Closed	10	1.1	3	8,917.0	10	983.1	23	9,901.2
a. Realized or Actual	6	.7	1	.1	3	12.2	10	13.0
b. Unrealized - Written off	5	.4	2	8,916.9[2]	7	970.9[3]	14	9,888.2
Ending Balance	**10**	**$ 36.9**	**6**	**$ 159.1**	**11**	**$ 2,536.3**	**27**	**$ 2,732.3**

1 The beginning balances for better used funds were adjusted to reflect TIGTA's removal of one report for $3.7 million.
2 This category includes two reports, with $8,916.9 million written off, for which IRS management did not concur with TIGTA's projected benefits.
3 This category includes four reports, with $939.3 million written off, for which IRS management was undecided or did not concur with TIGTA's projected benefits.

The following table provides a snapshot of OIG and TIGTA audit reports with significant recommendations reported in previous semiannual reports for which corrective actions had not been completed as of September 30, 2008, and September 30, 2009, respectively. OIG and TIGTA define as "significant" any recommendation open for more then one year. There were no "Undecided Audit Recommendations" during the same periods.

SIGNIFICANT UNIMPLEMENTED RECOMMENDATIONS

	9/30/2008		9/30/2009	
	OIG	TIGTA	OIG	TIGTA
	No. of Reports	No. of Reports	No. of Reports	No. of Reports
Unimplemented	6	40	8	26

The following table presents a summary of OIG and TIGTA audit reports that were open for more than a year with potential monetary benefits at the end of fiscal years 2007, 2008, and 2009.

NUMBER OF REPORTS WITH POTENTIAL MONETARY BENEFITS OPEN FOR MORE THAN ONE YEAR

	AFR Report Year	9/30/2007	9/30/2008	9/30/2009
OIG	No. of Reports	1	1	0
	$ Projected Benefits	$29.4 million	$29.4 million	$0 million
TIGTA	No. of Reports	10	12	10
	$ Projected Benefits	$ 66.5 million	$661.5 million	$673.8 million

The following tables present a summary of TIGTA audit reports, broken out by year of report issuance, on which management decisions were made on or before September 30, 2008, but the final actions had not been taken as of September 30, 2009. (Note: There are no OIG audit reports for this category.)

DETAILS OF THE AUDIT REPORTS WITH POTENTIAL MONETARY BENEFITS ON WHICH MANAGEMENT DECISIONS WERE MADE ON OR BEFORE SEPTEMBER 30, 2008, BUT FINAL ACTIONS HAVE NOT BEEN TAKEN AS OF SEPTEMBER 30, 2009 (DOLLARS IN THOUSANDS)

Bureau	Report Number	Report Issue Date	Brief Description	Disallowed Costs	Funds Put to Better Use	Revenue Enhancement	Total	Due Date
IRS	2004-20-142	8/26/2004	The IRS should ensure the Storage Strategy Study addresses the data storage capacity deficiency and recommends a cost-effective virtual tape system solution to reduce maintenance and tape shipping costs.		200.0		200.0	Due 12/31/2010
FY 2004	**1**				**200.0**		**200.0**	
IRS	2006-1c-142	9/25/2006	The IRS Contracting Officer (CO) should use the results of the Defense Contract Auditing Agency (DCAA) report to fulfill his/her duties in awarding and administering contracts.	32,373.8			32,373.8	Delayed to 9/30/2010
FY 2006	**1**			**32,373.8**			**32,373.8**	
IRS	2007-1c-040	3/8/2007	The IRS CO will work with DCAA and the contractor to resolve the questioned costs applicable to IRS contracts.	103.6			103.6	Due 2/15/2010
IRS	2007-1c-041	3/8/2007	The IRS CO will work with DCAA and the contractor to resolve the questioned costs applicable to IRS contracts.	2,247.0			2,247.0	Due 3/15/2010
IRS	2007-30-062	3/30/2007	Ensure the revised Form 4137 is used effectively to identify and assess the employer's share of Social Security and Medicare taxes on unreported tip income.			541,124.0	541,124.0	Delayed to 1/15/2010
IRS	2007-1c-149	9/24/2007	The IRS CO will work with DCAA and the contractor to resolve the questioned costs applicable to IRS contracts.	62.2			62.2	Due 9/15/2010
IRS	2007-1c-154	9/24/2007	The IRS CO will work with DCAA and the contractor to resolve the questioned costs applicable to IRS contracts.	1.2			1.2	Due 9/15/2010
FY 2007	**5**			**2,414.0**		**541,124.0**	**543,538.0**	
IRS	2008-30-155	8/22/2008	The IRS should revise computer programming to automatically reissue an undelivered refund check when an address change is reflected on a taxpayer's account.		36.2		36.2	Due 1/15/2010

Continued on next page

DETAILS OF THE AUDIT REPORTS WITH POTENTIAL MONETARY BENEFITS ON WHICH MANAGEMENT DECISIONS WERE MADE ON OR BEFORE SEPTEMBER 30, 2008, BUT FINAL ACTIONS HAVE NOT BEEN TAKEN AS OF SEPTEMBER 30, 2009 (DOLLARS IN THOUSANDS)

Bureau	Report Number	Report Issue Date	Brief Description	Disallowed Costs	Funds Put to Better Use	Revenue Enhancement	Total	Due Date
IRS	2008-40-087	3/28/2008	The IRS should develop and implement strategies to bring noncompliant taxpayers back into compliance.			52,100.0	52,100.0	Due 1/15/2010
			The IRS should consider using the indicator shown on Form 5498 to identify taxpayers who are subject to required minimum distributions.			94.4	94.4	Due 1/15/2010
IRS	2008-40-167	8/29/2008	The IRS should develop a process to identify those employers that do not adequately withhold taxes from their employees after receiving a lock-in letter.			45,500.0	45,500.0	Due 12/15/2009
FY 2008	3				36.2	97,694.4	97,730.6	
TOTAL	10			34,787.8	236.2	638,818.4	673,842.4	

FINANCIAL MANAGEMENT SYSTEMS FRAMEWORK

Overview

The Department of the Treasury's financial management systems structure consists of financial and mixed systems maintained by the Treasury bureaus and the Department-wide Financial Analysis and Reporting System (FARS). The bureau systems process and record the detailed financial transactions and submit summary-level data to FARS on a scheduled basis. FARS maintains the key financial data necessary for consolidated financial reporting. In addition, the FARS modules maintain data on performance management and the status of audit-based corrective actions. Under this systems structure, the bureaus are able to maintain financial management systems that meet their specific business requirements. On a scheduled basis, the required financial and performance data are submitted to FARS to meet Departmental analysis and reporting requirements. The Department uses FARS to produce its periodic financial and performance reports as well as the annual Agency Financial Report (AFR) and the Annual Performance Report (APR). This structured financial systems environment enables Treasury to receive an unqualified audit opinion and supports its required financial management reporting and analysis requirements.

The FARS structure consists of the following components:

- Bureau core and financial management systems - process and record detailed financial transactions
- Treasury Information Executive Repository (TIER) - consolidates bureau financial data
- CFO Vision - produces monthly financial statements and performs financial analysis
- Joint Audit Management Enterprise System (JAMES) - tracks information on audit findings, recommendations, and planned corrective actions
- Performance Reporting System (PRS) - tracks the status of key performance measures

Bureaus submit summary-level financial data to TIER on a monthly basis, within three business days of the month-end. These data are then used by CFO Vision to generate financial statements and reports on both a Department-wide and bureau-level basis. This structure enables the Department to produce its audited annual financial statements and monthly management reports. During fiscal year 2009, Treasury continued to upgrade its FARS applications to take advantage of improvements in system technology. This included completing the roll-out of CFO Vision to Treasury bureaus. CFO Vision provides the bureaus with direct system access for enhanced reporting capabilities and financial analysis.

The Department continues to eliminate redundant and outdated financial management systems with the goal of consolidating financial management activities to improve productivity. As of September 30, 2009, the number of financial management systems decreased to 55, down from 60 at the end of fiscal year 2008. This reduction is due in part to bureaus migrating to the Bureau of the Public Debt Administrative Resource Center (BPD ARC) for these services.

As part of the Department's enhancement effort, 14 Treasury bureaus and reporting entities are cross-serviced for core financial systems by BPD ARC. Cross-servicing enables these bureaus to have access to core financial systems without having to maintain the necessary technical and systems architectures. In an effort to continue to streamline its financial systems environment, Treasury will work with the remaining bureaus to develop plans to migrate to Treasury's Shared Service Provider for core financial systems in accordance with the Financial Management

Line of Business requirements. In addition, as part of the Department's implementation of the e-Travel initiative, bureaus have eliminated their legacy travel systems.

In fiscal year 2009, to improve management's decision making process concerning the FARS applications projects, Treasury enhanced its risk management controls. Treasury identifies and monitors the risks and the potential threats to the FARS applications, surveys FARS customers to measure application satisfaction, and identifies areas needing improvement. The Department continues to modernize the capabilities of the FARS applications by implementing solutions to provide timely and useful financial and program data. FARS applications have been expanded to support new organizations and new functionality as the Department has assumed new responsibilities resulting from the recent economic conditions. For example, Treasury expanded the JAMES to support the initiatives of the Office of the Special Inspector General for Trouble Asset Relief Program (SIGTARP), the Internal Revenue Service/Taxpayer Advocate Service, and the Office of Financial Stability (OFS). To support OFS's financial reporting needs, the FARS application CFO Vision was modified to produce stand-alone financial statements for OFS. This expanded use of CFO Vision, combined with OFS's use of a cross-serviced core financial system provided by BPD ARC, reduces the need for OFS to develop or purchase its own core financial system.

Continued Improvement

Treasury's target financial management systems structure continues to build upon the current FARS foundation. Over the years, FARS has been enhanced to support new financial and performance requirements. FARS continues to provide management with the appropriate tools needed to align with the Department's goals and objectives.

Treasury completed the rollout of CFO Vision to the bureaus, modified FARS to support the requirements of the new Troubled Asset Relief Program (TARP), enhanced TIER to support the month-end financial close and preparation of the monthly financial statements and reports, and established a disaster recovery site for the FARS applications to provide business continuity in case of an emergency or disaster.

The Internal Revenue Service (IRS) continued work on the Integrated Financial System (IFS). IFS is the IRS's administrative financial management system. It accounts for $11.5 billion in IRS funding and provides timely financial statements for budgeting, analysis, and government-wide reporting. Fiscal year 2009 IFS accomplishments include:

- Interfaced with GovTrip, the Department's automated travel system
- Significantly reduced user access to the mainframe by migrating legacy system reports to the business warehouse, retired legacy processes, and trained users on reporting capabilities
- Implemented automated tax withholding for employee tuition assistance, created employee invoices, and automatically posted all payments received through ***pay.gov*** (Treasury's secure electronic payments system to federal agencies)
- Updated contingency plans, and completed penetration and disaster recovery testing
- Exceeded the average system uptime target of 97 percent.

The IRS successfully deployed the Customer Account Data Engine (CADE), Release 4.2 in January 2009. CADE is used to electronically process tax returns. With the implementation of Release 4.2, capabilities were added to process prior year and decedent returns, remittances, estimated tax payments, requests for extensions, and surname changes. In fiscal year 2009, CADE processed over 40 million returns, issued more than 34.9 million refunds using a modernized account database, and processed over 7 million payments totaling $58.6 billion. The IRS developed a comprehensive Audit Trail Plan and requirements for CADE, which are necessary to account for assets and processes across the IRS.

As previously indicated, BPD ARC cross-services 14 Treasury bureaus and reporting entities for core financial systems. In addition to the cross-servicing for core financial systems, Treasury bureaus are also cross-serviced for other financial management services, such as electronic travel and human resource processing. This cross-servicing has resulted in a reduction in the number of financial management systems maintained by the Department. In fiscal year 2009, BPD ARC's accomplishments include:

- Selected by OMB as one of four government Shared Service Centers to perform information technology system Certification and Accreditation work under the Information Systems Security Line of Business (ISSLOB) initiative
- Provided system and processing support to 14 of Treasury's bureaus for human resource management and travel management
- Utilized information technology services to implement best practices for managing IT operations and improving quality and support in a cost effective manner
- Conducted a customer satisfaction survey - two-thirds of the customer agencies responded and the results showed an overall customer satisfaction score of 89 percent
- Enhanced GovTrip, Treasury's electronic travel system, to improve audit and expense descriptions and added new functionality to support user needs and improve security
- Participated in the Department of the Treasury's annual continuity exercise to assess BPD ARC's ability to perform essential functions during various emergency scenarios, and identified areas for improvement

FEDERAL FINANCIAL MANAGEMENT IMPROVEMENT ACT (FFMIA) COMPLIANCE

As of September 30, 2009, the Department of the Treasury's financial management systems were not in substantial compliance with FFMIA due to deficiencies with the IRS's financial management systems. The IRS has a remediation plan in place to correct the deficiencies. For each FFMIA recommendation, the remediation plan identifies specific remedies, target dates, responsible officials, and resource estimates required for completion. This plan is reviewed and updated quarterly.

The IRS made significant progress in fiscal year 2009 toward the financial management systems being in FFMIA compliance by implementing the final release of the Custodial Detail Database (CDDB). CDDB contains detailed records of IRS revenue, refunds, and unpaid assessments. It addresses an IRS material weakness by providing detail data to support custodial financial reporting and was used by GAO during the fiscal year 2009 financial statements audit.

The IRS developed and tested a replacement revenue accounting system that is planned for implementation in fiscal year 2010. This system was designed to incorporate the United States Standard General Ledger (USSGL); and add traceability between the revenue, refunds, and unpaid assessments summary record and the IRS processing system's detail records.

RECOVERY ACT RISK MANAGEMENT ACTIVITIES

Upon the enactment of the Recovery Act in February 2009, just weeks after the new Administration took office, Treasury quickly designed and implemented a robust risk management program to support the Department's implementation of the Act. Following OMB's Recovery Act implementation guidance, Treasury required the programs' senior accountable officials in the bureaus to certify that they had taken the following actions for each Recovery Act program:

- Identified and documented program-specific risks
- Identified and documented applicable current process internal controls
- Determined the risk level (high, medium, or low) by using Treasury's Recovery Act risk and impact assessment questionnaire
- Determined additional controls needed, if any
- Developed (or updated existing) and implemented a risk mitigation plan for each program with a risk level of medium or high
- Performed ongoing monitoring and testing

Treasury created a Recovery Act Risk Management Council that meets monthly to discuss the progress and status of each bureau's Recovery Act risk management activities.

Appendix E
Glossary of Acronyms

GLOSSARY OF ACRONYMS	
ABS	Asset-Backed Securities
AFR	Agency Financial Report
AGP	Asset Guarantee Program
AIFP	Automotive Industry Financing Program
AIG	American International Group
AIIP	Automotive Industry Investment Program
APR	Annual Performance Report
ARC	Administrative Resource Center
ASC	Accounting Standards Codification
ASM/CFO	Assistant Secretary for Management & Chief Financial Officer
BEP	Bureau of Engraving and Printing
BPD	Bureau of the Public Debt
BSA	Bank Secrecy Act
BSM	Business Systems Modernization
CADE	Customer Account Data Engine
CAP	Competitiveness Assessment Process
CAP	Capital Assessment Program
CBLI	Consumer and Business Lending Initiative
CDDB	Custodial Detail Database
CDE	Community Development Entities
CDFI	Community Development Financial Institutions
CDS	Credit Default Swaps
CFPA	Consumer Financial Protection Agency
CFO	Chief Financial Officer
CFS	Consolidated Financial Statements
CFTC	Commodities Futures Trading Commission
CMBS	Commercial Mortgage Backed Securities
CO	Contracting Officer
COP	Congressional Oversight Panel
CPP	Capital Purchase Program
CSRS	Civil Service Retirement System
CTF	Clean Technology Fund

(continued)

GLOSSARY OF ACRONYMS	
DASHR/CHCO	Office of the Deputy Assistant Secretary for Human Resources/Chief Human Capital Officer
DCAA	Defense Contract Auditing Agency
DCP	Office of D.C. Pensions
DIP	Debtor-in-Possession
DO	Departmental Offices
DHS	Department of Homeland Security
EESA	Emergency Economic Stability Act of 2008
EFTPS	Electronic Federal Tax Payment System
EGTRRA	Economic Growth and Tax Relief Reconciliation Act
EITC	Earned Income Tax Credit
ESF	Exchange Stabilization Fund
Fannie Mae	Federal National Mortgage Association
FARS	Financial Analysis and Reporting System
FASAB	Federal Accounting Standards Advisory Board
FATF	Financial Action Task Force
FCDA	Foreign Currency Denominated Assets
FCRA	Federal Credit Reform Act
FDIC	Federal Deposit Insurance Corporation
FECA	Federal Employees' Compensation Act
FERS	Federal Employees' Retirement System
FEGLI	Federal Employees Group Life Insurance
FEHBP	Federal Employees Health Benefits Program
FFB	Federal Financing Bank
FFMIA	Federal Financial Management Improvement Act
FHFA	Federal Housing Finance Agency
FHLB	Federal Home Loan Bank
FinCEN	Financial Crimes Enforcement Network
FMFIA	Federal Managers' Financial Integrity Act
FMIS	Financial Management Information System
FMS	Financial Management Service
FRB	Federal Reserve Bank
FRBNY	Federal Reserve Bank of New York
Freddie Mac	Federal Home Loan Mortgage Corporation
FTO	Fine Troy Ounce
FY	Fiscal Year
G-7	Group of Seven

(continued)

GLOSSARY OF ACRONYMS	
G-20	Group of Twenty
GAAP	Generally Accepted Accounting Principles
GAB	General Arrangement to Borrow
GAO	Government Accountability Office
GFRA	General Fund Receipt Account
GM	General Motors
GMAC	General Motors Acceptance Corporation
GSA	General Services Administration
GSE	Government Sponsored Enterprises
GSECF	Government Sponsored Enterprise Credit Facility
HAMP	Home Affordable Modification Program
HCTC	Health Coverage Tax Credit
HERA	Housing and Economic Recovery Act
HUD	Department of Housing and Urban Development
IAP	International Assistance Programs
IFS	Integrated Financial System
IMF	International Monetary Fund
IPIA	Improper Payments Information Act
IRACS	Interim Revenue Accounting Control System
IRS	Internal Revenue Service
IT	Information Technology
JAMES	Joint Audit Management Enterprise System
LIBOR-OIS	London Inter-Bank Offered Rate-Overnight Index Swap
MBS	Mortgage-Backed Securities
MDB	Multilateral Development Banks
MeF	Modernized Electronic File
MINT	U.S. Mint
MRADR	Market Risk Adjusted Discount Rate
MV&S	Modernization, Vision, and Strategy
NAB	New Arrangement to Borrow
NACA	Native American CDFI Assistance
NMTC	New Markets Tax Credit
NRC	National Revenue Center
NRP	National Research Program
OCC	Office of the Comptroller of the Currency
OFS	Office of Financial Stability

(continued)

GLOSSARY OF ACRONYMS	
OIG	Office of Inspector General
OMB	Office of Management and Budget
ONI	Office of National Insurance
OPEB	Other Post Employment Benefits
OPM	Office of Personnel Management
ORB	Other Retirement Benefits
OTC	Over-the-Counter
OTS	Office of Thrift Supervision
PB	President's Budget
PCA	Planned Corrective Actions
PP&E	Property, Plant, and Equipment
PPIF	Public-Private Investment Fund
PPIP	Public-Private Investment Program
PSPA	Preferred Stock Purchase Agreements
QEO	Qualified Equity Offering
QFI	Qualified Financial Institution
RRACS	Redesign Revenue Accounting Control System
SAR	Suspicious Activity Report
SBA	Small Business Administration
SBR	Statement of Budgetary Resources
SCAP	Supervisory Capital Assessment Program
SDR	Special Drawing Rights
SEC	Securities and Exchange Commission
SED	Strategic Economic Dialogue
SFFAS	Statement of Federal Financial Accounting Standards
SFP	Supplementary Financing Program
SIGTARP	Special Inspector General for TARP
SOMA	System Open Market Account
SPSPA	Senior Preferred Stock Purchase Agreements
SPV	Special Purpose Vehicle
SSP	Shared Service Provider
SSP	Stable Share Price
TAIFF	Troubled Assets Insurance Financing Fund
TALF	Term Asset-Backed Securities Loan Facilities
TARP	Troubled Asset Relief Program
TFF	Treasury Forfeiture Fund

(continued)

GLOSSARY OF ACRONYMS	
TIER	Treasury Information Executive Repository
TIGTA	Treasury Inspector General for Tax Administration
TIP	Targeted Investment Program
TIPS	Treasury Inflation-Protected Securities
TRES	Treasury Retail E-Services
TRIA	Terrorism Risk Insurance Act
TTB	Alcohol and Tobacco Tax and Trade Bureau
USSGL	United States Standard General Ledger
VITA	Volunteer Income Tax Assistance

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Website Information

Treasury On-line	**www.treas.gov**
Alcohol and Tobacco Tax and Trade Bureau	**www.ttb.gov**
Community Development Financial Institutions Fund	**www.treas.gov/cdfi**
Comptroller of the Currency	**www.occ.treas.gov**
Bureau of Engraving & Printing	**www.bep.treas.gov**
Financial Crimes Enforcement Network	**www.treas.gov/fincen**
Financial Management Service	**www.fms.treas.gov**
Internal Revenue Service	**www.irs.gov**
U.S. Mint	**www.usmint.gov**
Bureau of the Public Debt	**www.publicdebt.treas.gov**
Office of Thrift Supervision	**www.ots.treas.gov**
The Financial Stability Plan	**www.financialstability.gov**
Help for America's Homeowners	**www.makinghomeaffordable.gov**
Recovery Act Spending	**www.recovery.gov**

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