

Consolidated Financial Statements

**DEPARTMENT OF VETERANS AFFAIRS FRANCHISE FUND
CONSOLIDATED BALANCE SHEET
AS OF SEPTEMBER 30, 2006 and 2005
(Dollars in Thousands)**

	<u>2006</u>	<u>2005</u>
ASSETS		
Intragovernmental		
Fund Balance with Treasury (Note 2)	\$ 147,785	\$ 110,805
Accounts Receivable	48,387	54,620
Other Assets (Note 3)	2,318	7,189
Total Intragovernmental	<u>198,489</u>	<u>172,614</u>
Accounts Receivable	28	145
Property, Plant and Equipment, Net (Note 4)	24,039	21,247
Other Assets (Note 3)	<u>8</u>	<u>8</u>
Total Assets	<u>\$ 222,564</u>	<u>\$ 194,014</u>
LIABILITIES		
Intragovernmental Liabilities		
Accounts Payable	\$ 0	\$ 7
Other Liabilities (Note 6)	24,179	31,789
Total Intragovernmental	<u>24,179</u>	<u>31,796</u>
Accounts Payable	10,565	3,140
Other Liabilities (Note 6)	<u>77,932</u>	<u>59,702</u>
Total Liabilities	<u>112,676</u>	<u>94,638</u>
NET POSITION	<u>\$ 109,888</u>	<u>\$ 99,376</u>
TOTAL LIABILITIES AND NET POSITION	<u>\$ 222,564</u>	<u>\$ 194,014</u>

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

**DEPARTMENT OF VETERANS AFFAIRS FRANCHISE FUND
CONSOLIDATED STATEMENT OF NET COST
FOR THE YEARS ENDED SEPTEMBER 30, 2006 and 2005
(Dollars in Thousands)**

	<u>2006</u>	<u>2005</u>
PROGRAM COSTS:		
Program A:		
Gross Costs Intragovernmental	\$ 23,374	\$ 51,306
Less: Earned Revenue-Intragovernmental	(297,715)	(251,457)
Net Program Costs - Intragovernmental	<u>(274,340)</u>	<u>(200,151)</u>
Costs Not Assigned to Programs	270,390	196,223
Less: Earned Revenues Not Attributed to Programs (Note 7)	<u>0</u>	<u>(200)</u>
NET COST OF OPERATIONS	<u><u>\$ (3,950)</u></u>	<u><u>\$ (4,128)</u></u>

**DEPARTMENT OF VETERANS AFFAIRS FRANCHISE FUND
CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION
FOR THE YEARS ENDED SEPTEMBER 30, 2006 and 2005
(Dollars in Thousands)**

	<u>2006</u>	<u>2005</u>
CUMULATIVE RESULTS OF OPERATIONS		
Beginning Balance	\$ 99,376	\$ 90,693
OTHER FINANCING SOURCES (NON-EXCHANGE):		
Transfers-In	2,183	277
Imputed Financing	4,379	4,278
Total Financing Sources	<u>6,562</u>	<u>4,555</u>
Net Cost of Operations	<u>3,950</u>	<u>4,128</u>
Net Change	<u><u>10,512</u></u>	<u><u>8,683</u></u>
TOTAL NET POSITION	<u><u>\$ 109,888</u></u>	<u><u>\$ 99,376</u></u>

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

**DEPARTMENT OF VETERANS AFFAIRS FRANCHISE FUND
COMBINED STATEMENT OF BUDGETARY RESOURCES
FOR THE YEARS ENDED SEPTEMBER 30, 2006 and 2005
(Dollars in Thousands)**

	<u>2006</u>	<u>2005</u>
BUDGETARY RESOURCES		
Unobligated Balance at the Beginning of the Period	\$ 88,930	\$ 75,722
Spending Authority from Offsetting Collections		
Earned		
Collected	311,095	239,659
Receivable from Federal sources	(6,233)	26,709
Change in unfilled customer orders		
Advance Received	(20)	6,182
Without Advance from Federal Sources	47,452	
Total Budgetary Resources	<u><u>441,223</u></u>	<u><u>348,272</u></u>
STATUS OF BUDGETARY RESOURCES		
Obligations Incurred	290,872	259,343
Unobligated Balance Available (Note 2)	150,351	88,929
Unobligated Balance Not Available (Note 2)	0	0
Total Status of Budgetary Resources	<u><u>441,223</u></u>	<u><u>348,272</u></u>
CHANGE IN OBLIGATED BALANCE		
Obligated Balance, Net - Beginning of the Period	21,875	20,202
Obligations Incurred	290,872	259,343
Less Gross Outlays	(274,095)	(230,960)
Less Recoveries of Prior Year Unpaid Obligations, Actual	-	-
Change in Uncollected Customer Payments from Federal Sources	(41,219)	(26,709)
Obligated Balance, Net End of Period	<u><u>\$ (2,566)</u></u>	<u><u>\$ 21,875</u></u>
NET OUTLAYS		
Gross Outlays - Disbursements	274,095	230,960
Less: Offsetting Collections	(311,075)	(245,841)
Net Outlays	<u><u>\$ (36,980)</u></u>	<u><u>\$ (14,881)</u></u>

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

**DEPARTMENT OF VETERANS AFFAIRS FRANCHISE FUND
CONSOLIDATED STATEMENT OF FINANCING
FOR THE YEARS ENDED SEPTEMBER 30, 2006 and 2005
(Dollars in Thousands)**

	<u>2006</u>	<u>2005</u>
RESOURCES USED TO FINANCE ACTIVITIES		
Budgetary Resources Obligated		
Obligations Incurred	\$ 290,872	\$ 259,343
Less: Spending Authority from Offsetting Collections and Adjustments	(352,294)	(272,550)
Net Obligations	<u>(61,421)</u>	<u>(13,207)</u>
Other Resources		
Transfers-In	2,183	277
Financing Imputed for Cost Subsidies	4,379	4,277
Net Other Resources Used to Finance Activities	<u>6,562</u>	<u>4,554</u>
Total Resources Used to Finance Activities	<u>(54,859)</u>	<u>(8,653)</u>
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	53,694	4,120
Resources that Finance the Acquisition of Assets Property, Plant and Equipment	(9,433)	(7,956)
Resources that Fund Expenses Recognized in Prior Periods	117	(127)
Total Resources Used to Finance Items Not Part of Net Cost of Operations	<u>44,378</u>	<u>(3,963)</u>
Total Resources Used to Finance the Net Cost of Operations	<u>(10,481)</u>	<u>(12,616)</u>
COMPONENTS NOT REQUIRING OR GENERATING RESOURCES		
Depreciation and Amortization	6,901	8,406
Bad Debts	1	0
Gain/Loss on Disposition of Assets	(260)	82
Other	(111)	0
	<u>6,531</u>	<u>8,488</u>
NET COST OF OPERATIONS	<u><u>\$ (3,950)</u></u>	<u><u>\$ (4,128)</u></u>

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

Notes to the Consolidated Financial Statements

Department of Veterans Affairs Franchise Fund

Notes to the Consolidated Financial Statements
For the Years Ended September 30, 2006 and 2005
(Dollars in Thousands)

Note 1. Summary of Significant Accounting Policies

A. Reporting Entity

Created by Congress in 1996, as one of six Franchise Fund pilots operating within the Executive Branch of Government, the Department of Veterans Affairs' (VA) Franchise Fund supports VA's mission by supplying common administrative services at competitive prices. By law, the business lines within the Fund can only sell to Federal entities. This organization accounted for its funds in six activity centers (VA Enterprise Centers) and in one administrative organization: Austin Automation Center, Debt Management Center, Financial Services Center, Law Enforcement Training Center, Security and Investigations Center, VA Records Center and Vault and the Enterprise Fund Office. The consolidated financial statements include the six individual activity centers of the Fund. All material intrafund transactions have been eliminated.

B. Basis of Presentation

The VA Franchise Fund consolidated financial statements report all activities of Franchise Fund components. The consolidated financial statements differ from the financial reports used to monitor and control budgetary resources, but are prepared from the same books and records. The statements should be read with the understanding that the VA Franchise Fund is a component unit of the U.S. Government. The Franchise Fund's fiscal year (FY) 2006 and 2005 financial statements are presented in conformity with the Office of Management and Budget's (OMB) Bulletin 01-09, "Form and Content of Agency Financial Statements," as amended.

C. Basis of Accounting

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

D. Fund Balance with Treasury

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

Department of Veterans Affairs Franchise Fund

Notes to the Consolidated Financial Statements For the Years Ended September 30, 2006 and 2005 (Dollars in Thousands)

E. Accounts Receivable

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

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

F. Property, Plant and Equipment

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

G. Other Liabilities

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

H. Revenues and Financing Sources

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

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

I. Accounting for Intragovernmental Activities

In order to prepare reliable financial statements, transactions occurring among VA components must be eliminated. All significant intra-entity transactions were eliminated from Franchise Fund's consolidated financial statements.

Department of Veterans Affairs Franchise Fund

Notes to the Consolidated Financial Statements
For the Years Ended September 30, 2006 and 2005
(Dollars in Thousands)

J. Annual, Sick and Other Types of Leave

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

K. Imputed Financing

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

L. Litigation

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

Note 2. Fund Balance with Treasury

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

	<u>2006</u>	<u>2005</u>
Fund Balance with Treasury	\$147,785	\$110,805

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

	<u>2006</u>	<u>2005</u>
Unobligated Apportionment		
Available	\$150,351	\$ 88,929
Unavailable		
Obligated balance not yet Disbursed	(2,566)	21,875
Total Unexpended Apportionment	<u>\$147,785</u>	<u>\$110,805</u>

Department of Veterans Affairs Franchise Fund

Notes to the Consolidated Financial Statements
For the Years Ended September 30, 2006 and 2005
(Dollars in Thousands)

Note 3. Other Assets

Other assets are generally made up of advances. There are two types of advances handled by the Franchise Fund. The first is when Treasury processes charges from other agencies to the Franchise Fund via the IPAC system. Charges are recorded as an advance until the applicable obligation is located and the charges can be transferred. These charges are for GSA rent, GPO printing services, FTS, and motor pool.

One of the product lines available to other government agencies is the handling of the purchase card activity. When the purchase credit card payments are scheduled, an advance is set up. Charges are then IPACed to the applicable agency to offset the advances.

Note 4. Property, Plant and Equipment

Property, Plant and Equipment (PP&E), including transfers from other federal agencies, are recorded at cost. Expenditures for major additions, replacements, and alterations are capitalized. Routine maintenance is expensed when incurred. Items costing over \$100,000 with a useful life of 2 years or more are capitalized. All capitalized purchases are depreciated using the straight-line method over the estimated useful life, usually 3 to 5 years.

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

PP&E as of September 30, 2006:

	<u>Acquisition Cost</u>	<u>Accumulated Depreciation</u>	<u>Net Book Value</u>
Furniture & Equipment	\$ 1,054	\$ (746)	\$ 308
Capital Leases	0	0	0
ADP Equipment	27,065	(17,483)	9,582
Software	11,073	(9,204)	1,868
Software - In Development	413	0	413
Leasehold Improvements	<u>22,814</u>	<u>(10,947)</u>	<u>11,867</u>
Total PP&E	\$ <u>62,419</u>	\$ <u>(38,380)</u>	\$ <u>24,039</u>

Department of Veterans Affairs Franchise Fund

Notes to the Consolidated Financial Statements
For the Years Ended September 30, 2006 and 2005
(Dollars in Thousands)

Note 4. Property, Plant and Equipment (Continued)

PP&E as of September 30, 2005:

	<u>Acquisition Cost</u>	<u>Accumulated Depreciation</u>	<u>Net Book Value</u>
Furniture & Equipment	\$ 1,054	\$ (652)	\$ 402
Capital Leases	0	0	0
ADP Equipment	29,562	(20,908)	8,654
Software	10,913	(8,563)	2,350
Software - In Development	124	0	124
Leasehold Improvements	19,463	(9,746)	9,717
Total PP&E	<u>\$ 61,116</u>	<u>\$ (39,869)</u>	<u>\$ 21,247</u>

Note 5. Leases

The Franchise Fund has operating leases. Due to the number of operating leases, the future commitment for operating leases is not known. The Franchise Fund's FY 2006 operating lease costs were \$1,420,809 for real property rentals and \$48,672 for equipment rentals. The Franchise Fund's FY 2005 operating lease costs were \$1,355,599 for real property rentals and \$37,009 for equipment rentals. The following chart represents the Franchise Fund's estimate for operating lease costs for the next 5 years, assuming a range of 4.2 to 4.7 percent annual increases in cost.

OPERATING LEASES

<u>Fiscal Year</u>	<u>Percentage Increase</u>	<u>Real Property</u>	<u>Equipment</u>
2007	4.7	\$ 1,488	\$ 51
2008	4.3	1,552	53
2009	4.2	1,617	55
2010	4.2	1,685	58
2011	4.2	1,755	60

Department of Veterans Affairs Franchise Fund

Notes to the Consolidated Financial Statements
For the Years Ended September 30, 2006 and 2005
(Dollars in Thousands)

Note 6. Other Liabilities

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

	<u>2006</u>	<u>2005</u>
Intragovernmental		
Accrued Payables – Federal	\$ 4,603	\$ 12,193
Advances – Federal	<u>19,576</u>	<u>19,596</u>
Total Intragovernmental Liabilities	<u>\$ 24,179</u>	<u>\$ 31,789</u>
Public		
Accrued Payables	\$ 72,489	\$ 54,128
Accrued Salaries & Wages	1,878	2,162
Accrued Funded Annual Leave	<u>3,564</u>	<u>3,412</u>
Total Public Liabilities	<u>\$ 77,932</u>	<u>\$ 59,702</u>

Note 7. Public Earned Revenue

In 1987, the General Services Administration (GSA) issued regulations providing guidelines for the establishment and installation of physical fitness facilities in government-owned space. GSA coordinates the Cooperative Administrative Support Unit (CASU) program. This program establishes the legal and administrative framework for agencies in multi-tenant buildings to share common services, including health and fitness centers. The Financial Services Center is the sponsor agency for the Mid-Atlantic CASU. The Mid-Atlantic CASU manages a health and fitness center in a Federal building in New York City. Federal employees are members and the revenue for their fees is considered public revenue.