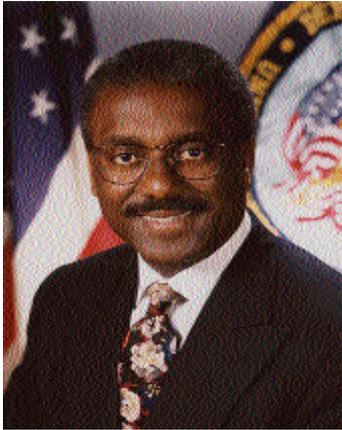


Message from the Secretary of Veterans Affairs



I am pleased to present the *Department of Veterans Affairs Fiscal Year 1996 Accountability Report*. The Report contains overviews of the performance of VA's mission, the audited financial statements, the status of management controls, and other items of interest to VA managers and customers.

The information in the Accountability Report comes from officially recognized financial and management systems. In accordance with the Federal Managers' Financial Integrity Act of 1982, I am providing reasonable assurance that my

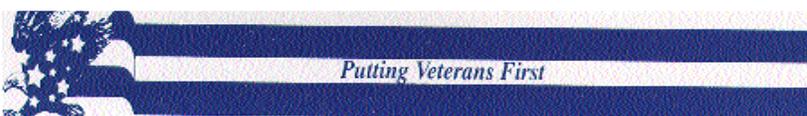
Department's management controls and financial systems comply with Governmentwide standards and requirements. Full compliance depends on the completion of the Veterans Benefits Administration's systems modernization efforts.

Our successes were highlighted a short while ago in the "Best Kept Secrets in Government" report sent to the President. Integrated healthcare networks have streamlined Veterans Health Administration management and focused resources on the needs of patients. All of our patients soon will have access to primary care teams and—thanks to the eligibility reform legislation recently signed into law—coordinated, comprehensive medical care.

Veterans Health Administration eliminated nearly 900 forms and increased sharing agreements to enhance timely access to health care. Veterans Benefits Administration reduced overhead costs by consolidating education and some compensation claims processing operations. Loan Guaranty Service improved communications so lenders now spend less time dealing with VA paperwork and more time making loans to veterans. The VA Insurance Center designed a policy statement that shows veterans the complete status of their policies which answers many of their concerns and questions before they have to write or call. National Cemetery System is developing new national cemeteries in under-served regions of the country.

President Lincoln once said, "*A nation that does not honor its heroes will not long endure.*" VA is dedicated to serving the needs of more than 26 million men and women and their dependents living today who have served in the nation's Armed Forces.

Jesse Brown





D. Mark Catlett
VA's Chief Financial Officer

Management Discussion and Analysis of Financial Condition and Results of Operations

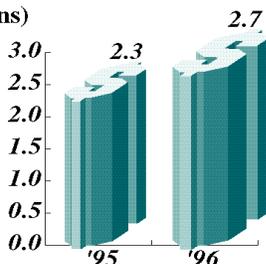
CFO Assessment

VA was the first Department of the Federal Government to produce audited consolidated financial statements, a feat accomplished in 1986. Ten years later, VA has achieved another significant milestone. It became the first Department to receive an unqualified or clean opinion on its Consolidated Statement of Financial Position as of September 30, 1996.

Reinventing how we spend our money, as well as being careful what we spend it on, is helping VA to control costs and maintain leadership in achieving National Performance Review goals. For example, innovative use of the IMPAC VISA card is helping VA realize substantial savings in rebates while providing better service to our customers. By the end of FY 1996, 64% of VA micro-purchases (those under \$2,500) were being made using purchase cards. Statistics for FY 1996 show 628,000 credit card purchases totaling \$273 million were made with this federal procurement card and VA earned rebates of \$795,404. With full VA implementation, we anticipate using purchase cards for 95% of micro-purchases and will earn rebates of approximately \$4.5 million during FY 1997. Daily credit card downloads spread VA's Austin Finance Center's workload over the month which resulted in a significant savings of resources. It also provided up to date information for our customers and eliminated one million pieces of paper last year.

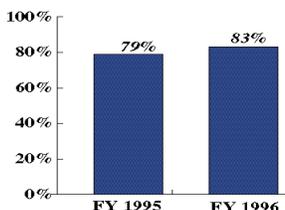


Electronic Payments
(in billions)



Electronic Commerce continuing to expand.

Prompt Pay
On-Time Percentage



4% increase over previous year.

Use of electronic commerce continued to expand. During FY 1996, vendors engaged with VA in electronic commerce increased by 31 percent. Electronic commerce accounted for 45% of the dollars and 28% of the invoices paid vendors. Eighty-three percent of these invoices were paid on time, based on the Prompt Payment Act. That represents a four percent improvement over the previous year, in spite of the government shut-down.

The Department achieved a 93 percent participation rate for Direct Deposit/Electronic Funds Transfer (DD/EFT) of salary payments in FY 1996, up from 90 percent in FY 1995.

1996 Accountability Report

VA financial policy manuals and reports, including this report, are available to our employees and constituents on the Internet. Veterans can contact us about benefits at our VA Home Page (<http://www.va.gov/>) or they can logon toll-free to the VAONLINE Bulletin Board Service at 1-800-US1-VETS. These on-line avenues of information mean quicker responses to veterans and reduced cost to VA in staff time.

Six service activities were converted from direct appropriation funding into entrepreneurial organizations within VA's Franchise Fund. These organizations now bill their customers for services rendered. They are: Information Technology-*Total Business Solutions*, Records Storage, Security Investigations, Police Officer Training, Payroll, and PC Training and Adaptive Technologies. The plan is that all centralized finance operations will be within the Franchise Fund in FY 1998.

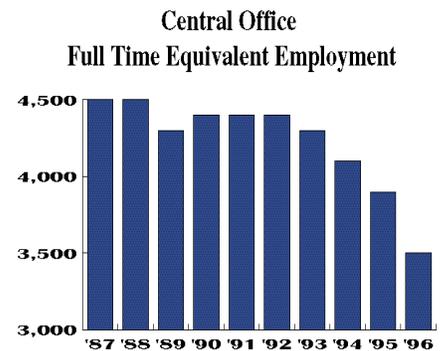
VA continues to reduce overhead costs, consolidate activities, and streamline processes. Establishment of a single shared service center was approved just recently. It will provide centralized human resources and payroll services to the Department and cross-service other agencies.

Departmentwide full time equivalent employment dropped by 6,623 during FY 1996, a reduction of three percent. In Central Office, the on-board strength dropped by 367, a reduction of ten percent during FY 1996.

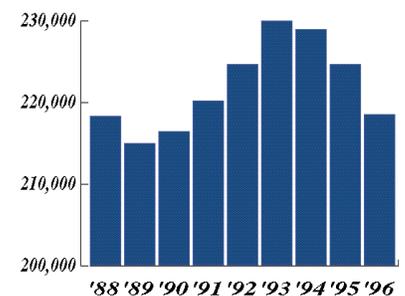
VA and Treasury combined forces to implement a Combo Printing System that allows for inclusion of an Explanation of Benefits (EOB) with a check payment. This is saving mailing costs of about \$438,000 annually.

VA's leadership in the field of Debt Management continued with collection rates for newly-established education (87%) and home loan debts (78%) again reaching all-time highs in FY 1996. The rate for compensation and pension (68%) fell slightly short of the record established the previous year. Almost 86,000 debts valued at over \$579 million were referred to consumer credit reporting agencies. Private Collection Agency referrals for FY 1996 totaled 11,000 accounts worth over \$165 million, with projected collections of approximately \$12 million. A decision was made to centralize collection of medical first party debts to Veterans Benefits Administration's (VBA) Debt Management Center to take advantage of debt management tools.

VA Home Page
<http://www.va.gov>



VA Field
Full Time Equivalent Employment





Analysis of Financial Statements

The assets on VA's Statement of Financial Position have remained very stable over the past ten years. The charts trend three of the major components of VA assets.

Investments are for the most part federal securities owned by Life Insurance programs. Accounts and Loans Receivable continue to be dominated by veterans benefit programs, principally home loans and veterans life insurance policy loans. However, since the early nineties, patient and third party insurers' medical debts have risen dramatically due to Medical Care Cost Recovery (MCCR) programs. During the same period, housing credit receivables decreased due to legislative changes. These changes relieved veterans of liability for VA losses on defaulted home loans, provided the veteran exercised good faith. Net Property, Plant, and Equipment reflect growth due to the capitalization of improvements over the years. The slight decrease in FY 1996 is attributable to the real and personal property records clean-up which occurred this year.

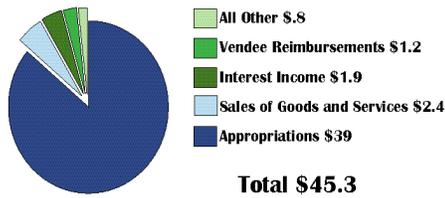
Funded liabilities have also remained stable over the years. The chart trends four of the major components of VA Funded Liabilities.

Liabilities for Loan Guaranties have grown since Credit Reform required up-front funding for all federal loan programs. The steady increase in Insurance Policy Reserves represents the maturing of the life insurance contracts. The funds borrowed from Treasury are directly related to the Housing Credit Assistance Program.

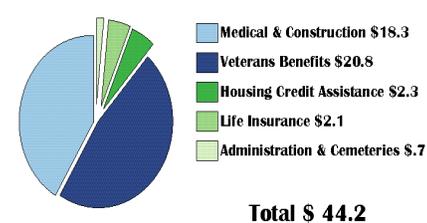
Unfunded liabilities have been very volatile in recent years. The chart trends four of the major components of VA Unfunded Liabilities.

Federal Employees Compensation Act (FECA) liability represents an actuarial estimate of future years' payments for VA cases currently on the rolls. After increasing for many years, the caseload has come down due to the diligent efforts of Veterans Health Administration (VHA) and Office of Human Resources and Administration to manage the costs of this program by returning employees to light duty and similar efforts. The unfunded liability Reserve for Losses on Guaranteed Loans has declined in recent years due to the Credit Reform requirement to fund guaranties up front. The big fluctuation in VA's Statement of Financial Position over the past five years is attributable to the unfunded liability for Veterans' Compensation and Pension Benefits. This actuarial esti-

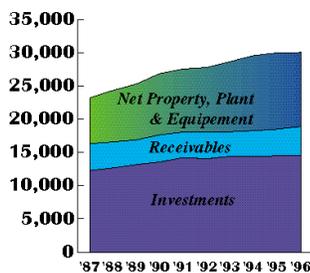
FY 1996 Revenue by Source
(in billions)



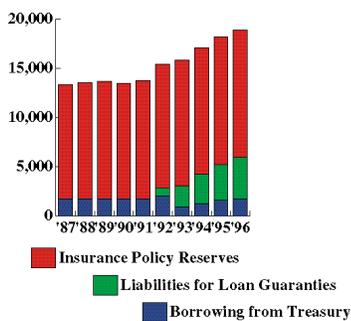
FY 1996 Expense by Activity
(in billions)



VA's Assets (in billions)



VA Funded Liabilities (in billions)



1996 Accountability Report

mate of future years' payments for cases currently on the rolls is very susceptible to changes in the discount rate used to make the present value computation. The liability was first reported after it became a federal accounting requirement enunciated in OMB's Form and Content Bulletin. It will change again with next year's statement (FY 1997) when VA implements Statement of Federal Financial Accounting Standards (SFFAS) No. 5 (Accounting for Liabilities of the Federal Government) which requires that veterans' pension liabilities be disclosed in a note to the financial statements but not shown as a liability. Veterans Compensation will continue to be reported as an unfunded liability.

The preparation of financial statements in conformity with generally accepted accounting principles for federal entities requires management to make estimates and assumptions that affect the amounts reported in the financial statements and footnotes thereto. This is particularly applicable to the amounts reported for unfunded liabilities. Actual results could differ from management's estimates.

Connecting Resources with Results

VA has made significant progress in integrating performance measures in the budget formulation and execution processes.

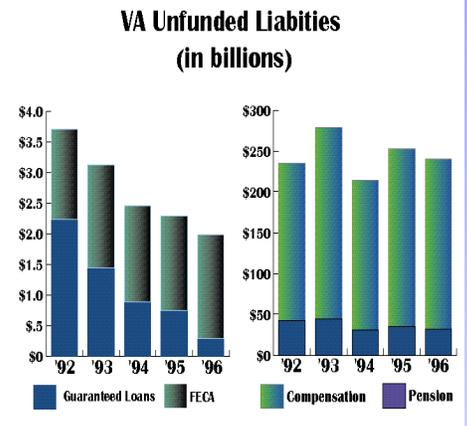
VA participated in the CFO Council's Governmentwide Cost Accounting Work Group to address costing issues and concerns common to all federal entities. One of four subgroups, the Budget/GPRA Subgroup, is tasked with developing methods for integrating government cost accounting, GPRA requirements, and the budget.

VA's FY 1998 Budget process is serving as a key stepping stone in our efforts to increase emphasis on connecting resources to results by both developing meaningful measures of performance and using this information to make better budget and management decisions. Management's focus has shifted from program inputs to program outcomes. Value judgments are being made concerning what veterans and the public are receiving in return for the funds devoted to VA programs.

Highlights of VA's Performance During FY 1996

Veterans Health Administration

- VHA is making great strides to transform itself into an organization where veterans and the public can expect to find a continuum of high quality healthcare in a convenient, responsive, caring manner—and at a reasonable cost. The overarching objective was to put in place

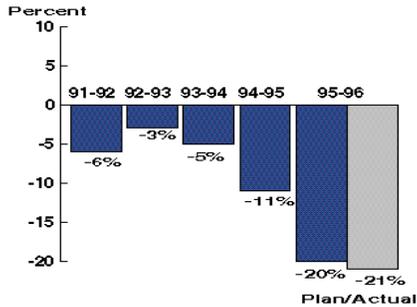


*GPRA/Budget
Subgroup
Integrating
Cost
Accounting...*

*“Healthcare
Value
Begins
with VA...”*



Percent Change in Bed Days of Care Per 1,000 Unique Users



structures that would shift VA from an inpatient-driven healthcare delivery system to one that is outpatient and primary care focused. As a result, major organizational and functional restructuring occurred which has flattened the organizational structure and moved decision making from headquarters to the field.

- Organizational goals were developed to articulate the Under Secretary's vision. In an effort to monitor and ensure achievement of goals, VHA developed a performance measurement system to monitor the organization's success and a performance management system to monitor senior managers' success. Both systems are linked to the organizational goals.
- For the first time, performance agreements with specific measures were made between the Under Secretary for Health and his senior managers. These measures included qualifying and incentive measures.
- VHA achieved: significant declines in the number of bed days of care per 1,000 unique users of the healthcare system; greater use of the ambulatory care setting for appropriate surgical and invasive diagnostic procedures; improved patient satisfaction with inpatient care and outpatient services; increased primary care enrollment; and decreases in waiting times for speciality care and primary appointments.

Veterans Benefits Administration

- VBA regional offices completed approximately 2.7 million claims for compensation and pension benefits during FY 1996. They improved their timeliness, and bettered their annual goals for completion of original compensation and pension claims. Original compensation claims were completed in an average of 144 days, an improvement of 17 days from FY 1995 and six days below their FY 1996 goal. Comparable achievements were accomplished for veterans pension, death pension, and dependency and indemnity compensation.
- The Compensation and Pension Service completed a business process reengineering study of claims processing and began to improve service, increase reliance on technology, and work closer with veterans, their representatives, and the Department of Defense. A business plan was prepared presenting a case manager approach to



Outreach Benefits Counseling.
Veterans Benefits Counselors Sherman Barton (right) and Leroy Saunders (center) solicit information from a homeless Vietnam veteran to assist him with a claim at Philadelphia's 69th Street Terminal.

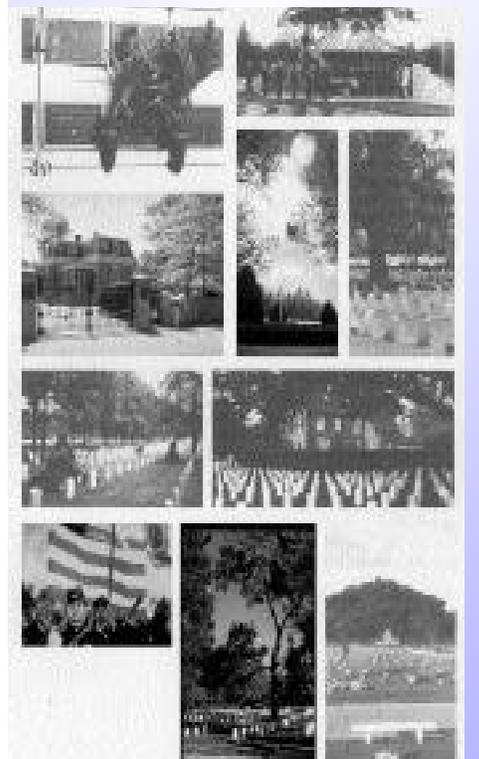
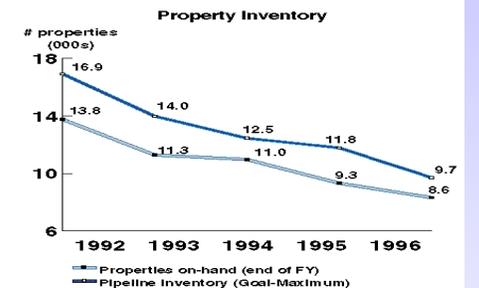
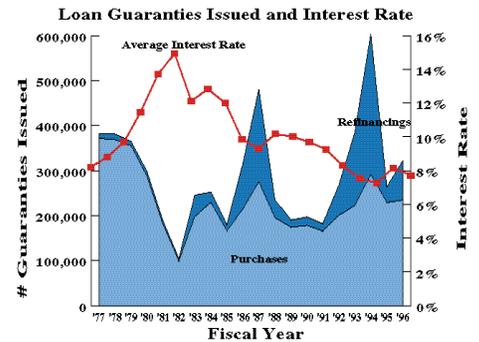
1996 Accountability Report

claims processing to eliminate the multiple hand-offs and diffusion of responsibility inherent in the functional specialization of traditional claims processing procedures.

- The consolidation of all education claims processing into four processing sites—Atlanta, Buffalo, Muskogee, and St. Louis—is now complete. This VBA reengineering initiative, started in FY 1993, allows work to be accomplished with fewer resources than if claims were processed in all regional offices.
- VA issued guaranties on 320,776 loans during FY 1996, of which over 86,000 were interest rate reduction loans, a significant increase from FY 1995. This increase was due to a temporary reduction in interest rates early in the calendar year, which resulted in a mini-refinancing wave. The property inventory decreased from 9,300 units at the end of FY 1995 to slightly over 8,600 at the end of FY 1996, a decrease of 8 percent. This is well below the six-month pipeline inventory of 10,000 properties which represents the maximum number of properties that were expected to be in the inventory.

National Cemetery System (NCS)

- NCS accomplished 71,786 interments, tended in excess of two million gravesites, and maintained over 5,000 acres of land developed for burial purposes. The Burial Operations Support System (BOSS) was fully activated to automate burial records, thereby reducing paper records, providing a centralized data base, and allowing cemeteries to redirect staff to provide direct service to veterans and their families.
- NCS's Memorial Programs Service provided 319,758 headstones and markers. To provide better service, NCS successfully initiated a program to accomplish the electronic ordering of markers for national cemeteries. An expansion of electronic ordering to state veterans' cemeteries and other Federal cemeteries will begin in FY 1997. Memorial Programs Service also provided 257,366 Presidential Memorial Certificates to the next of kin and other relatives of deceased veterans.
- NCS implemented initiatives that saved money and improved customer service. NCS's success in the area of customer service is evidenced by the presentation of the Robert W. Carey Quality Award to Calverton National Cemetery. The award recognizes the highest level



“Serving our veterans with compassion and dignity.”



of excellence in quality management among all VA facilities and offices. FY 1996 marks the first time the top award has gone to a national cemetery. Calverton was cited for its exceptionally strong leadership in quality performance and initiatives to improve customer service through self-directed work teams and focus groups involving both internal and external customers.

Management's Assertions

As VA's Chief Financial Officer, I conducted a thorough evaluation of the VA's management controls. Based upon the cumulative progress reported on material issues being monitored by VA's top management and the yearly assurance letters provided by all major VA element managers, I concluded that VA's management controls and financial systems generally comply with Governmentwide standards and requirements. I advised Secretary Brown that VA will be able to provide full assurance at the completion of Veterans Benefits Administration's systems modernization efforts.

<i>FMFIA Material Weaknesses</i>	Reported	Correction
Aging, Antiquated, and Proprietary Hardware and Software Systems	1983	1997
Lack of Adequate Contingency Plans	1984	1997
Insurance-Adaptability and Documentation	1985	1997
Controls Over Prescription Drugs	1990	1997
Education System - Chapter 1606	1993	1997
C&P-Adaptability and Documentation	1985	1998
Credit Reform	1990	1998
Loan Guaranty - Loan Service and Claims	1989	1999
Inadequate Controls Over Addictive Drugs	1991	1999
PAID-Mission Performance	1993	2000
LGY Financial Systems Modernization	1986	TBD
Loan Sale Program Management	1997	TBD

During FY 1996, VA closed four material weaknesses and continued to progressively implement important milestones affecting the remainder of VA's remaining eleven material weaknesses. Five are projected to be corrected by the end of FY 1997. One additional material weakness, Loan Sale Program Management, was disclosed in FY 1997.

1996 Accountability Report

Management is responsible for preparation of the Department's consolidated financial statements and related information appearing in this annual accountability report. Management believes that the consolidated statement of financial position fairly reflects the form and substance of transactions and that the financial statements reasonably present the Department's financial position and results of operations in conformity with generally accepted accounting principles for federal entities. Management has also included in the Department's financial statements amounts that are based on estimates and judgments which it believes are reasonable under the circumstances. It is the opinion of VA's management that the ultimate resolution of legal actions pending as of September 30, 1996, will not materially affect VA's operations and financial position, especially when consideration is given to the availability of the Judgment Fund appropriation to pay some court-settled legal cases.

D. Mark Catlett
Assistant Secretary for Management (CFO)



Lines of Business

