



June 7, 2013

Memorandum

To: Members of the Board
M.R. Valentine
From: Monica R. Valentine, Assistant Director
Wendy M. Payne
Through: Wendy M. Payne, Executive Director
Subject: Risk Assumed – Insurance and Guarantee Phase – **Tab A¹**

MEETING OBJECTIVES

To review the current measurement methodology in accounting for direct loans and loan guarantees to consider a similar approach for the accounting for insurance and guarantees. We will also review the scope of the insurance and guarantee phase of the overall risk assumed project.

BRIEFING MATERIAL

- ☐ Staff Memo
 - Staff Analysis and Board Questions – Insurance and Guarantee Phase
- ☐ Attachments –
 - I. Federal Insurance Programs -- Summary Factsheets
 - II. KPMG Government Institute Report – *Federal Credit Reform: Is it a sleeping giant?*

BACKGROUND

The risk assumed project is taking a broad look at all types of transactions and events that may result in future outflows as a result of the federal government's mission, operations, and current or past actions. During the summer of 2012 staff held two task force meetings on two explicit groupings of risk assumed: (1) commitments and

¹ The staff prepares Board meeting materials to facilitate discussion of issues at the Board meeting. This material is presented for discussion purposes only; it is not intended to reflect authoritative views of the FASAB or its staff. Official positions of the FASAB are determined only after extensive due process and deliberations.

obligations, including contracts, grants, and treaties, and (2) insurance and guarantees. As a result of those meetings and related research, staff recommended and the Board approved a three-phase approach. This sequences the areas to allow development of principles for measuring and reporting risk where risk is most clearly identifiable—insurance and guarantees providing explicit indemnification to identified parties. The first phase will allow us to develop a framework for use in later phases. Phase two will include entitlement programs; national defense, security and disaster response; and other potential effects on future outflows, such as regulatory actions, GSE's, etc. Phase three will include commitments and obligations and other risk areas.

At the April meeting the presentation by the FASB staff member on the proposed approach to account for insurance contracts highlighted the need for the Board to also re-examine its current standards on insurance and guarantee programs. Staff has continued its research on federal insurance programs and has developed summary factsheets on several programs to gain a better understanding of the types of federal insurance programs.

The primary objectives for this meeting's discussion are to further develop the scope of the insurance and guarantee phase and to get a clearer understanding of the credit reform standards and how that approach could assist in considering revisions to our current insurance and guarantee standards. In developing the scope, staff would like to address the following areas.

- Define federal insurance and guarantees by
 - developing a general definition of insurance and guarantees and
 - developing specific characteristics of insurance and guarantees.
- Evaluate the similarities and differences between loan guarantees and federal insurance and non-loan guarantees.
- Consider ways to evaluate the potential impact of the new FASB insurance contracts proposed standard on those federal entities that follow FASB GAAP.

Member feedback on the information presented will direct staff on the next steps to take in the project.

Staff Analysis and Questions for Board Consideration on the FASAB Risk Assumed Project: Insurance and Guarantee Phase

- ❖ **Insurance and Guarantee Program vs. Insurance and Guarantee Contract (Product)** – How should “insurance and guarantee” be defined in the federal environment? Should we use the proposed FASB/IASB definition of insurance contracts as a basis for identifying “insurance”? Is this differentiation a concern in the federal environment?

The current FASAB standards on insurance and guarantees frame the guidance based on a program and not a contract/product.

Insurance and guarantee **programs** are federal **programs** that provide protection to individuals or entities against specified risks. Many of these **programs** were established to assume risks that private sector entities are unable or unwilling to assume [at least at prices that beneficiaries of the **program** can afford (in some cases) or want to pay (in other cases)] or to subsidize the provision of insurance to achieve social objectives. **Program** participants pay fees or premiums for specific services. These funds are commonly held in revolving funds within the federal government; losses sustained by participants are paid from these funds. Many of these **programs** receive appropriations to pay excess claims and/or have authority to borrow from the Treasury. (SFFAS 5 par. 97)

The current FASAB standards on insurance and guarantees do not provide a definition of an insurance/guarantee program, but simply describe the many types of insurance/guarantee programs and in some instances program characteristics.

Excerpts from SFFAS 5:

Federal programs provide protection against many types of risk for individuals and entities. These include life insurance; medical insurance; and insurance against damage to property(homes, crops, and airplanes) or other assets (deposits and pension benefits) caused by perils such as flooding and other natural disasters, war-risk, and insolvency” (par. 100)

For federal insurance and guarantee programs, there **often is no explicit contract**. (par. 101)

Federal insurance programs also differ from private insurance in that they are **not subject to the same market forces** (e.g., competition for business and for capital) and regulatory requirements (e.g., for capitalization) that apply to privately owned insurers. In particular, federal insurance, unlike private insurance, is not extended with the intent of earning a profit. **Some programs operate deliberately at a loss**, as when disabled veterans are offered life insurance at premiums set for healthy participants. Other programs offer insurance covering **catastrophic or systemic risks**, where large losses can occur all at once, as in war risk or deposit insurance. At most, federal insurance

programs are **expected just to meet anticipated costs**, leaving them vulnerable to unfavorable surprises. (par. 102)

The *FASB/IASB* proposal² on the accounting for insurance **contracts** includes all insurance **contracts** (life and nonlife, and reinsurance) regardless of the type of entity issuing the **contract**, which differs from FASB's current standards.

The *FASB/IASB* proposal also defines an insurance contract as -- A **contract** under which one party (the insurer) accepts significant insurance risk from another party (the policyholder) by agreeing to compensate the policyholder if a specified uncertain future event (the insured event) adversely affects the policyholder. (*FASB Discussion Paper – Preliminary Views on Insurance Contracts*, 9/17/2010)

The FASB/IASB proposal also defines insurance and financial risk as follows.

Insurance risk – Risk, other than financial risk, transferred from the holder of a contract to the insurer.

Financial risk – The risk of a possible future change in one or more of a specified interest rate, financial instrument price, commodity price, foreign exchange rate, index of prices or rates, credit rating or credit index or other variable, provided in the case of a non-financial variable that the variable is not specific to a party to the contract.

➤ **Staff Analysis**

The overall risk assumed project is very broad and could encompass many different types of federal programs from deposit insurance to federal disaster relief. While this phase of the project is focusing on federal insurance and guarantees, use of the terms “program” vs. “contract” can significantly impact the scope of this phase of the project. For example, an insurance program approach may exclude insurance provisions embodied in individual agreements or contracts (such as treaties that include indemnification against losses).

Question 1a: How should “insurance and guarantee” be defined in the federal environment?

Question 1b: Should we use the proposed FASB/IASB definition of insurance contracts as a basis for identifying “insurance”?

Question 1c: Is the differentiation between “program” and “contract” a concern in the federal environment?

Staff Recommendation

Staff recommends scoping this phase of the project in the context of “federal insurance and guarantee **programs**” because it will allow us to more narrowly focus the development of the standard. Also, defining the scope in the context of a federal program aligns with how the federal government fulfills its missions and delivers its

² The anticipated 2013 proposal has not been published as of the writing of this memo. Discussion of the proposal is based on earlier proposals, Ms. Weiner's April briefing, and other sources.

services – by the use of **programs**. Although using “insurance contract” would be taking more of a principle-based approach, staff believes defining the Phase one scope in the context of a “contract” to describe federal activities would be more difficult to apply. “Contract” would have to be specifically defined in terms of its legal status (e.g., written, explicit, implied, enforceable, etc.). We believe this approach would lead to more confusion as to what federal activities are covered by the standard.

If the Board agrees with staff, we would develop a general definition of an “insurance and guarantee program” and identify the specific characteristics of the program, including identifying what are, in substance, insurance and guarantee terms or conditions. Certain exclusions would also have to be identified, such as loan guarantees.

Based on staff’s research on existing programs, the following is an initial list of possible characteristic of federal insurance and guarantee programs.

- The legislation establishing the program specifies the acceptance by the Federal government of certain risk(s) and the parameters of the program participants.
- The legislation explicitly establishes an agreement between the federal government and a program participant.
- Program participants pay fees or premiums in exchange of the government’s acceptance of the risk.
- The program provides protection to individuals or entities against a specific risk if a specified uncertain future event adversely affects the program participant.

❖ **Addressing “Non-Loan Guarantee Programs”** – Should non-loan guarantee programs be addressed in conjunction with insurance programs?

The current FASAB standards on insurance and guarantees do not specifically discuss any non-loan guarantee programs; whereas the FASB/IASB proposal would include many guarantee products that meet the definition of an insurance contract, such as loan guarantees and surety bonds.

➤ **Staff Analysis**

Staff has identified several federal non-loan guarantee programs, such as FDIC’s share loss program, NCUA’s guaranteed note program, and SBA’s surety bond program. The FDIC and NCUA programs guarantee the loss in the value of assets of failed or failing institutions and the SBA program guarantees performance on a contract.

Question 2: Should non-loan guarantee programs be addressed in conjunction with insurance programs?

Staff Recommendation

Staff would like to further research the underlying characteristics of non-loan guarantee programs to identify the similarities and differences between federal insurance programs and non-loan guarantee programs. This analysis will allow us to assess the development of the overall scope of this phase and ultimately determine whether different accounting should be proposed for non-loan guarantee programs.

- ❖ **Federal Insurance Programs that follow FASB GAAP** – Do members wish to know what, if any, comments federal insurance entities currently following FASB GAAP have on the FASB proposed standards for insurance and/or what, if any, changes in their financial reporting may result from the FASB standards?

The current FASAB standard on insurance and guarantees states the following:

When financial information pursuant to FASB's standards on federal insurance and guarantee programs conducted by government corporations is incorporated in general purpose financial reports of a larger federal reporting entity, the entity should report as RSI what amounts and periodic change in those amounts would be reported under the "risk assumed" approach referred to in this section (see par. 105). In other words, in addition to the liability for unpaid claims from insured events that have already occurred (including any contingent liability that meets criteria for recognition), such reporting entities should also report as RSI risk assumed information. [SFFAS 5 par. 106]

➤ **Staff Analysis**

Since certain federal insurance entities currently follow FASB GAAP, staff believes we can use those entities' analysis of the proposed FASB standards on insurance contract to assess the application of the FASB proposal to a federal program. In addition, while the individual entities apply FASB, FASAB will wish to consider any effect on the government-wide report. For example, whether concerns regarding comparability arise and whether additional disclosures or RSI would be needed upon consolidation.

Staff has identified the below federal insurance programs that follow FASB GAAP.

- Federal Deposit Insurance Corporation (FDIC)
- Pension Benefit Guaranty Corporation (PBGC)
- Farm Credit System Insurance Corporation (FCSIC)
- Overseas Private Investment Corporation (OPIC)

Question 3: Do members wish to know what, if any, comments these entities [federal insurance entities currently following FASB GAAP] have on the FASB proposed standards for insurance contracts and/or what, if any, changes in their financial reporting may result from the FASB standards?

Staff Recommendation

Staff recommends that the FASAB request that the four federal entities identified above respond to specific questions³ on FASB's insurance contracts proposal. Staff would use those responses to identify application concerns that would be unique to a federal entity.

³ The specific questions to pose would be provided to the Board for consideration after the FASB exposure draft is published.

- ❖ **Federal Insurance & Non-Loan Guarantee Programs vs. Credit Reform Programs** -- Should staff assess the conceptual similarities and differences between federal loan guarantee programs and federal insurance and non-loan guarantee programs to consider if they are similar enough to be accounted for similarly?

The current FASAB standards on insurance and guarantees exclude social insurance and loan guarantee programs.

“....., federal insurance programs are similar to federal credit programs. The federal government extends credit on terms and conditions designed to subsidize particular borrowers or encourage particular activities for social policy reasons. As soon as a federal direct loan or loan guarantee is obligated, the federal government is committed to bear whatever loss, through defaults or interest subsidies, is inherent in the terms and the conditions under which the credit is extended. The government is likewise committed when federal insurance is extended to additional policyholders, either for an additional fixed period, or to cover additional amounts of assets.” (SFFAS 5 par. 103)

Credit program is defined in SFFAS 19, *Technical Amendments to Accounting Standards For Direct Loans and Loan Guarantees in SFFAS 2*, as a federal program that makes loans and/or loan guarantees to nonfederal borrowers.

SFFAS 2, *Accounting for Direct Loans and Loan Guarantees* (as amended), provides accounting standards for federal direct loans and loan guarantees. The standards require that direct loans obligated and loan guarantees committed after September 30, 1991, be accounted for on a present value basis. The use of the present value accounting method is consistent with the intent of the Federal Credit Reform Act of 1990.

SFFAS 2 (as amended) contains the following essential requirements:

- Direct loans disbursed and outstanding are recognized as assets at the present value of their estimated net cash inflows. The difference between the outstanding principal of the loans and the present value of their net cash inflows is recognized as a subsidy cost allowance.
- For guaranteed loans outstanding, the present value of estimated net cash outflows of the loan guarantees is recognized as a liability. Disclosure is made of the face value of guaranteed loans outstanding and the amount guaranteed.
- For direct or guaranteed loans disbursed during a fiscal year, a subsidy expense is recognized. The amount of the subsidy expense equals the present value of estimated cash outflows over the life of the loans minus the present value of estimated cash inflows.
- The subsidy cost allowance for direct loans and the liability for loan guarantees are reestimated each year, taking into account all factors that may have affected the estimated cash flows. Any adjustment resulting

from the reestimates is recognized as a subsidy expense (or a reduction in subsidy expense).

- When direct loans or loan guarantees are modified, the cost of modifications is recognized at an amount equal to the decrease in the present value of the direct loans or the increase in the present value of the loan guarantee liabilities measured at the time of modification.
- Upon foreclosure of direct or guaranteed loans, the acquired property is recognized as an asset at the present value of its estimated future net cash inflows.

In the FASB proposal, “credit insurance” would be within the scope of the FASB/IASB insurance contracts project -- “credit insurance that provides for specified payments to be made to reimburse the holder for a loss it incurs because a specified debtor fail to make payment when due under the original or modified terms of a debt instrument.” [*IFRS Insurance Contracts Exposure Draft, July 2010, par. B18(g)*]

The President’s Budget specifically outlines the federal credit and insurance programs. This list can assist us with specifically scoping out credit programs from this project since they are covered by the existing credit reform standards. [See list from the Fiscal Year 2014 President’s Budget -- Analytical Perspectives on page 11 of this memo]

➤ **Staff Analysis**

Current FASAB standards on credit reform require direct loans disbursed and outstanding to be recognized as assets at the present value of their estimated net cash inflows. The difference between the outstanding principal of the loans and the present value of their net cash inflows is recognized as a subsidy cost allowance. For guaranteed loans outstanding, the present value of estimated net cash outflows of the loan guarantees is recognized as a loan guarantee liability.

FASB’s tentative accounting for insurance contracts would apply a building block measurement approach to long duration insurance contracts using the present value of the unbiased, probability-weighted estimate (i.e., the mean) of the future cash outflows less the future cash inflows (the expected value).

Given the measurement methodology similarities between the credit reform accounting and the FASB proposal, staff believes further analysis of both these methodologies could be useful in considering revisions to our current insurance and guarantee standards. (Note that staff is not implying that current standards for loans and loan guarantees be considered for amendment. Rather, that a better understanding of the similarities and differences between these types of activities may be helpful in selecting a methodology and explaining why it was selected.)

Question 4: Should staff assess the conceptual similarities and differences between federal loan guarantee programs and federal insurance and non-loan guarantee programs to consider if they are similar enough to be accounted for similarly?

Staff Recommendation

Staff recommends that we assess the conceptual similarities and differences between federal loan guarantee programs and federal insurance and non-loan guarantee programs to evaluate if the insurance and guarantee standards should mirror those of credit reform accounting for loan guarantees.



Questions for Board

- 1a. How should “insurance and guarantee” be defined in the federal environment?
- 1b. Should we use the proposed FASB/IASB definition of insurance contracts as a basis for identifying “insurance”?
- 1c. Is the differentiation between “program” and “contract” a concern in the federal environment?
2. Should non-loan guarantee programs be addressed in conjunction with insurance programs?
3. Do members wish to know what, if any, comments federal insurance entities currently following FASB GAAP have on the FASB proposed standards for insurance contracts and/or what, if any, changes in their financial reporting may result from the FASB standards?
4. Should staff assess the conceptual similarities and differences between federal loan guarantee programs and federal insurance and non-loan guarantee programs to consider if they are similar enough to be accounted for similarly?

The Analytical Perspectives Volume of the Fiscal Year 2014 President’s Budget of the United States Government specifically outlines the federal credit and insurance programs.

▪ **Insurance Programs:**

- Deposit Insurance – Federal Deposit Insurance Corporation (FDIC) through its Deposit Insurance Fund (DIF)
- Share Insurance – National Credit Union Administration (NCUA)
- Pension Guarantees – Pension Benefit Guaranty Corporation (PBGC)
- Flood Insurance – DHS/FEMA’s National Flood Insurance Program (NFIP)
- Crop Insurance – USDA’s Risk Management Agency (RMA)
- Insurance against Security-Related Risks
 - Treasury’s Terrorism Risk Insurance (TRIP)
 - Transportation’s Airline War Risk Insurance

▪ **Credit Programs**

- Housing Credit Programs:
 - Federal Housing Administration (FHA) – mortgage loan guarantees
 - Veterans Affairs (VA) – mortgage loan guarantees
 - USDA’s Rural Housing Service (RHS) – direct and guarantee loans
 - Government-Sponsored Enterprises (GSE) supporting the stability and liquidity of a secondary market for residential mortgage loans:
 - Federal National Mortgage Association (Fannie Mae)
 - Federal Home Loan Mortgage Corporation (Freddie Mac)
 - Federal Home Loan Bank (FHLB)
- Education Credit Programs – Dept. of Education’s Federal Family Education Loan (FFEL) and William D. Ford Federal Direct Student Loan (Direct Loan) programs
- Small Business Loan Farm Credit programs:
 - Small Business Administration (SBA) – loans to small businesses
 - USDA’s Farm Service Agency (FSA) – loans to farmers

- Farm Credit System (FCS) – a GSE providing credit to farmers, ranchers, etc.
 - Federal Agriculture Mortgage Corporation (Farmer Mac) – an institution of FCS to facilitate a secondary market for farm real estate and rural housing loans.
- Energy and Infrastructure Credit programs:
 - Dept. of Energy’s Title 17 loan guarantee program – loan guarantees for projects that employ innovative technologies to reduce pollutants.
 - Dept. of Energy’s Advanced Technology Vehicle Manufacturing (ATVM) direct loan program
- Electric and Telecommunication Loans—USDA’s Rural Utilities Service programs provide loans for rural electrification, telecommunications, distance learning, telemedicine, and broadband.
- USDA Rural Infrastructure and Business Development programs provide grants, loans, and loan guarantees to communities for constructing facilities.
- Transportation Infrastructure – Dept. of Transportation federal credit programs fund critical transportation infrastructure projects by providing supplemental and subordinate capital to projects of national or regional significance and provide direct loans and loan guarantees to railroads for facilities maintenance, rehabilitation, acquisitions, and refinancing.
- National Infrastructure Bank – Directs federal resources for infrastructure to projects that have a clear public benefit and that demonstrate the most merit and may be difficult to fund under current federal programs.
- International Credit Programs – Seven federal agencies -- the Department of Agriculture (USDA), the Department of Defense, the Department of State, the Department of the Treasury, the Agency for International Development (USAID), the Export-Import Bank, and the Overseas Private Investment Corporation (OPIC) -- provide direct loans, loan guarantees, and insurance to a variety of private and sovereign borrowers. These programs are intended to level the playing field for U.S. exporters, deliver robust support for U.S. goods and services, stabilize international financial markets, and promote sustainable development.

TAB A - ATTACHMENT I:
Federal Insurance and
Guarantee Programs --
Summary Factsheets

Federal Insurance and Guarantee Programs -- Summary Factsheets

Federal Insurance and Guarantee Programs	Page
Deposit Insurance – Federal Deposit Insurance Corporation	1
Share Insurance – National Credit Union Administration	8
Pension Guarantee – Pension Benefit Guaranty Corporation	14
Flood Insurance – DHS – Federal Emergency Management Agency	22
Crop Insurance – USDA – Risk Management Agency	27
Terrorism Risk Insurance – Department of the Treasury	33
Airline War Risk Insurance – Department of Transportation	39
Overseas Investment – Overseas Private Investment Corporation	46
Veterans Life Insurance – Department of Veterans Affairs	55
Export Credit Insurance – Export-Import Bank	66
Farm Credit System Insurance – Farm Credit System Corporation	86

DEPOSIT INSURANCE FUND

FEDERAL DEPOSIT INSURANCE CORPORATION

WWW.FDIC.GOV

BRIEF SUMMARY OF PROGRAM

The Federal Deposit Insurance Corporation (FDIC) is the independent deposit insurance agency created by Congress in 1933 to maintain stability and public confidence in the nation's banking system. Provisions that govern the operations of the FDIC are generally found in the Federal Deposit Insurance (FDI) Act, as amended (12 U.S.C. 1811, et seq). In carrying out the purposes of the FDI Act, the FDIC, as administrator of the Deposit Insurance Fund (DIF), insures the deposits of banks and savings associations (insured depository institutions).

"Deposit insurance is essentially about making people feel secure about putting their money into financial institutions." – 2011 FDIC Annual Report

FDIC's mission is to:

maintain stability and public confidence in the nation's financial system by insuring deposits, examining and supervising financial institutions for safety and soundness and consumer protection, and managing receiverships.

In cooperation with other federal and state agencies, the FDIC promotes the safety and soundness of insured depository institutions by identifying, monitoring and addressing risks to the DIF. Commercial banks, savings banks and savings associations (known as "thrifts") are supervised by either the FDIC, the Office of the Comptroller of the Currency, or the Federal Reserve Board. In addition, the FDIC, through administration of the Federal Savings and Loan Insurance Corporation (FSLIC) Resolution Fund (FRF), is responsible for the sale of remaining assets and satisfaction of liabilities associated with the former FSLIC and the former Resolution Trust Corporation (RTC). The DIF and the FRF are maintained separately by the FDIC to support their respective mandates.¹

RELATED LEGISLATION AND U.S. CODE (U.S.C.)

1. Banking Act of 1933
2. Banking Act of 1935
3. Federal Deposit Insurance Act of 1950
4. Depository Institutions Deregulation and Monetary Control Act of 1980
5. Financial Institution Reform, Recovery, and Enforcement Act (FIRREA) in 1989

¹ More information on the FDIC is available online at <http://fdic.gov/about/>; last accessed June 5, 2012.

6. Federal Deposit Insurance Corporation Improvement Act (FDICIA) in 1991
7. Omnibus Budget Reconciliation Act of 1993
8. Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994
9. Deposit Insurance Funds Act of 1996 (Funds Act)
10. The Federal Deposit Insurance Reform Act of 2005 and the Federal Deposit Insurance Reform Conforming Amendments Act of 2005 (collectively, "the Reform Act")
11. Dodd-Frank Wall Street Reform and Consumer Protection Act (2010)
12. 12 U.S.C. § 1811-1835a

SOURCES OF FINANCING

FDIC receives no Congressional appropriations. It is funded by insurance premiums on deposits held by insured banks and savings associations and from interest on the investment of those premiums in U.S. Government securities. FDIC has authority to borrow up to \$100 billion from the Treasury for insurance purposes.²

SOURCE OF GAAP

FDIC primarily applies generally accepted accounting principles (GAAP) issued by the Financial Accounting Standards Board (FASB). This practice is permitted by paragraph 9 of Statement of Federal Financial Accounting Standards 34, *The Hierarchy of Generally Accepted Accounting Principles, Including the Application of Standards Issued by the Financial Accounting Standards Board*.

² Source: 2012 U.S. Government Manual available online at <http://www.gpo.gov/fdsys/browse/collection.action?collectionCode=GOVMAN&browsePath=2012+Edition+%28December%29%3BGovMAN-2012-12-07%3Bthumbnails%5C%2Fgovman11-12.jpg&isCollapsed=false&leafLevelBrowse=false&ycord=0> ; last accessed June 5, 2013.

SIGNIFICANT FINANCIAL STATEMENT ELEMENTS³

Excerpt from FY 2012 FDIC Annual Report

DEPOSIT INSURANCE FUND (DIF)		
FEDERAL DEPOSIT INSURANCE CORPORATION DEPOSIT INSURANCE FUND BALANCE SHEET AT DECEMBER 31 Dollars in Thousands		
	2012	2011
Assets		
Cash and cash equivalents	\$3,100,361	\$3,277,839
Cash and investments - restricted - systemic risk (Note 16) (Includes cash/cash equivalents of \$0 at December 31, 2012 and \$1,627,073 at December 31, 2011)	0	4,827,319
Investment in U.S. Treasury obligations, net (Note 3)	34,868,688	33,863,245
Trust preferred securities (Note 5)	2,263,983	2,213,231
Assessments receivable, net (Note 9)	1,006,852	282,247
Receivables and other assets - systemic risk (Note 16)	0	1,948,151
Interest receivable on investments and other assets, net	433,592	488,179
Receivables from resolutions, net (Note 4)	23,119,554	28,548,396
Property and equipment, net (Note 6)	392,880	401,915
Total Assets	\$65,185,910	\$75,850,522
Liabilities		
Accounts payable and other liabilities	\$349,620	\$374,164
Unearned revenue - prepaid assessments (Note 9)	1,576,417	17,399,828
Refunds of prepaid assessments (Note 9)	5,675,199	0
Liabilities due to resolutions (Note 7)	21,173,785	32,790,512
Debt Guarantee Program liabilities - systemic risk (Note 16)	0	117,027
Deferred revenue - systemic risk (Note 16)	0	6,639,954
Postretirement benefit liability (Note 13)	224,225	187,968
Contingent liabilities for:		
Anticipated failure of insured institutions (Note 8)	3,220,697	6,511,321
Systemic risk (Note 16)	0	2,216
Litigation losses (Note 8)	8,200	1,000
Total Liabilities	32,228,143	64,023,990
Commitments and off-balance-sheet exposure (Note 14)		
Fund Balance		
Accumulated Net Income	32,682,237	11,560,990
Accumulated Other Comprehensive Income		
Unrealized gain on U.S. Treasury investments, net (Note 3)	33,819	47,697
Unrealized postretirement benefit loss (Note 13)	(60,448)	(33,562)
Unrealized gain on trust preferred securities (Note 5)	302,159	251,407
Total Accumulated Other Comprehensive Income	275,530	265,542
Total Fund Balance	32,957,767	11,826,532
Total Liabilities and Fund Balance	\$65,185,910	\$75,850,522

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

³ Source: FDIC website -- <http://www.fdic.gov/about/strategic/report/index.html> last accessed on June 5, 2013.

DEPOSIT INSURANCE FUND (DIF)

FEDERAL DEPOSIT INSURANCE CORPORATION
DEPOSIT INSURANCE FUND STATEMENT OF INCOME AND FUND BALANCE
FOR THE YEARS ENDED DECEMBER 31
Dollars in Thousands

	2012	2011
Revenue		
Assessments (Note 9)	\$12,397,022	\$13,498,587
Interest on U.S. Treasury obligations	159,214	127,621
Systemic risk revenue (Note 16)	(161,135)	(131,141)
Other revenue (Note 10)	6,127,211	2,846,929
Total Revenue	18,522,312	16,341,996
Expenses and Losses		
Operating expenses (Note 11)	1,777,513	1,625,351
Systemic risk expenses (Note 16)	(161,135)	(131,141)
Provision for insurance losses (Note 12)	(4,222,595)	(4,413,629)
Insurance and other expenses	7,282	3,996
Total Expenses and Losses	(2,598,935)	(2,915,423)
Net Income	21,121,247	19,257,419
Other Comprehensive Income		
Unrealized (loss) gain on U.S. Treasury investments, net	(13,878)	20,999
Unrealized postretirement benefit loss (Note 13)	(26,886)	(15,059)
Unrealized gain (loss) on trust preferred securities (Note 5)	50,752	(84,587)
Total Other Comprehensive Income (Loss)	9,988	(78,647)
Comprehensive Income	21,131,235	19,178,772
Fund Balance - Beginning	11,826,532	(7,352,240)
Fund Balance - Ending	\$32,957,767	\$11,826,532

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

RELEVANT GAO REPORTS (LAST 5 YEARS)

- Opportunities for Improvements in FDIC's Shared Loss Estimation Process ([GAO-12-752R](#), July 19, 2012)
- Federal Deposit Insurance Corporation Funds' 2011 and 2010 Financial Statements ([GAO-12-416](#), Apr 19, 2012)
- FEDERAL DEPOSIT INSURANCE ACT Regulators' Use of Systemic Risk Exception Raises Moral Hazard Concerns and Opportunities Exist to Clarify the Provision ([GAO-10-100](#), April 15, 2010)
- Assessment of Regulators' Use of Prompt Corrective Action Provisions and FDIC's New Deposit Insurance System ([GAO-07-242](#), February 15, 2007)

RELEVANT DISCLOSURES IN AFR

See attached disclosure excerpts

RELATED DISCLOSURES IN CFR

Excerpt from 2012 CFR Note 18: Insurance and Guarantee Program Liabilities
Note 18. Insurance and Guarantee Program Liabilities
Insurance and Guarantee Program Liabilities as of September 30, 2012, and 2011

(In billions of dollars)	2012	2011
Insurance and Guarantee Program Liabilities:		
Pension Benefit Guaranty Corporation - Benefit Pension Plans	105.6	93.0
Federal Deposit Insurance Corporation Funds	26.5	47.4
All other insurance and guarantee programs	24.3	21.3
Total insurance and guarantee program liabilities.....	<u>156.4</u>	<u>161.7</u>

PBGC insures pension benefits for participants in covered defined benefit pension plans. As a wholly-owned corporation of the U.S. Government, PBGC's financial activity and balances are included in the consolidated financial statements of the U.S. Government. However, under current law, PBGC's liabilities may be paid only from PBGC's assets and not from the General Fund of the Treasury or assets of the Government in general. As of September 30, 2012, and 2011, PBGC had total liabilities of \$119.2 billion and \$106.7 billion, and its total liabilities exceeded its total assets by \$34.4 billion and \$26.0 billion, respectively. In addition, as discussed in Note 22—Contingencies, PBGC reported reasonably possible contingent losses of about \$321.8 billion and \$250.2 billion as of September 30, 2012, and 2011, respectively. Of the total FDIC amount as of September 30, 2012, and 2011, \$3.6 billion and \$7.2 billion, respectively, represents the recorded contingent liability and loss provision for institutions insured by the Deposit Insurance Fund that are likely to fail. In addition, \$21.2 billion and \$31.5 billion pertain to liabilities due to resolutions of failed or failing institutions and to pending depositor claims as of September 30, 2012, and 2011 respectively. Another \$1.7 billion and \$8.2 billion as of September 30, 2012, and 2011 respectively, pertains to the Temporary Liquidity Guarantee Program, which guarantees certain newly issued debt and certain noninterest-bearing transaction accounts in an effort to counter the system-wide crisis in the nation's financial sector. The remaining amounts represent contingent liabilities for litigation.

Of the \$24.3 billion and \$21.3 billion under all other insurance and guarantee programs as of September 30, 2012, and 2011, respectively, \$20.0 billion and \$10.3 billion, respectively, pertain to the USDA's Federal Crop Insurance Program. The increase in the estimated indemnities is due to the most severe drought in the farm belt since 1988. The Federal Crop Insurance Program is administered by the Federal Crop Insurance Corporation, whose mission is to provide an actuarially sound risk management program to reduce agricultural producers' economic losses due to natural disasters. Also, \$3.4 billion and \$7.4 billion relates to the National Credit Union Administration's Temporary Corporate Credit Union Stabilization Fund as of September 30, 2012, and 2011, respectively. This Program guarantees the timely payment of principal and interest on certain unsecured debt of participating credit unions.

Excerpt from 2012 CFR Note 22: Contingencies

Insurance Contingencies

At the time an insurance policy is issued, a contingency arises. The contingency is the risk of loss assumed by the insurer, that is, the risk of loss from events that may occur during the term of the policy. The Government has insurance contingencies that are reasonably possible in the amount of \$329.0 billion as of September 30, 2012, and \$267.0 billion as of September 30, 2011. The major programs are identified below:

- PBGC reported \$321.8 billion and \$250.2 billion as of September 30, 2012, and 2011, respectively, for the estimated aggregate unfunded vested benefits exposure to the PBGC for private-sector single-employer and multiemployer defined benefit pension plans that are classified as a reasonably possible exposure to loss.
- FDIC reported \$6.9 billion and \$16.5 billion as of September 30, 2012, and 2011, respectively, for identified additional risk in the financial services industry that could result in additional loss to the Deposit Insurance Fund should potentially vulnerable insured institutions ultimately fail. Actual losses, if any, will largely depend on future economic and market conditions.

SHARE INSURANCE

NATIONAL CREDIT UNION ADMINISTRATION

www.NCUA.gov

BRIEF SUMMARY OF PROGRAM

The National Credit Union Administration (NCUA) is the independent federal agency that regulates, charters, and supervises federal credit unions (FCUs). Credit unions are privately owned, cooperative associations organized for the purpose of promoting thrift among their members and creating a source of credit for provident and productive purposes. A three-member board oversees NCUA's operations by setting policy, approving budgets, and adopting rules.

NCUA's mission is to:

facilitate the availability of credit union services to all eligible consumers, especially those of modest means, through an objective independent regulatory environment that protects credit union members.

NCUA protects the safety and soundness of the credit union system by identifying, monitoring, and combating risks to **the National Credit Union Share Insurance Fund (NCUSIF)**. Backed by the full faith and credit of the U.S. Government, the NCUSIF insures individual accounts up to \$250,000 and joint accounts up to \$250,000 per member. NCUA provides insurance to all federal credit unions and the overwhelming majority of state-chartered credit unions. Members have never lost a penny of insured savings at a federally insured credit union. Each insured credit union is required to deposit and maintain in the NCUSIF 1.0 percent of its insured shares. The NCUA Board may also assess premiums to all insured credit unions, as provided by the Federal Credit Union Act (FCU Act.)

In addition to the NCUSIF, NCUA operates the following four funds: **the NCUA Operating Fund (the Fund)** conduct the following activities prescribed by the FCU Act: (a) chartering new federal credit unions; (b) determining field of membership of federal credit unions; (c) promulgating rules and regulations; (d) performing regulatory and safety and soundness examinations; and (e) conducting administrative activities of the NCUSIF; **the Central Liquidity Facility (CLF)** improves the general financial stability of credit unions by meeting their emergency liquidity needs, primarily through borrowings from Treasury's Federal Financing Bank; **the Community Development Revolving Loan Fund (CDRLF)** provides low-interest loans and technical assistance to low-income credit unions to enable them to: (1) provide financial services to their communities, (2) stimulate economic activities in their communities, and (3) operate more efficiently; and **the Temporary Corporate Credit Union Stabilization Fund (TCCUSF)** accrues losses to the corporate credit union system, and recovers the losses over time through assessments to federally insured credit unions. While the other four NCUA funds are permanent funds, TCCUSF is a temporary fund that will sunset in the year 2021.

NCUSIF maintains a normal operating ratio of 1.30, set by the NCUA Board. If the equity ratio increases above the normal operating level, a distribution is normally paid to insured credit unions. However, when the TCCUSF has an outstanding loan from the U.S. Treasury, distributions are paid to the TCCUSF instead.

RELATED LEGISLATION AND U.S. CODE (U.S.C.)

1. Federal Credit Union Act (1934, amended 1959)
 2. National Credit Union Central Liquidity Facility Act (1978)
 3. Community Development Credit Union Transfer Act (1986)
 4. Credit Union Amendments of 1987
 5. Credit Union Membership Access Act (1998)
 6. Helping Families Act of 2009
 7. National Credit Union Authority Clarification Act (2011)
 8. Depository Institutions Deregulation and Monetary Control Act of 1980
 9. Financial Institution Reform, Recovery, and Enforcement Act (FIRREA) in 1989
 10. Dodd-Frank Wall Street Reform and Consumer Protection Act (2010)
 11. 12 U.S.C. § 1751-1795k
-

SOURCES OF FINANCING

Except for a small appropriation to the CDRLF to provide technical assistance to low-income credit unions (\$1.2 million in 2011), NCUA receives no Congressional appropriations. In addition to interest income on investments and loans, NCUA recognizes non-exchange revenue for capitalization deposits made by each insured credit union, as needed, to maintain a balance in the NCUSIF that is equivalent to 1.0 percent of its insured shares.

The NCUA Board has the statutory authority according to the FCU Act Section 202, *Administration of the Insurance Fund*, to assess premiums to insured credit unions. The NCUA Board may assess each insured credit union a premium charge for insurance in an amount stated as a percentage of insured shares outstanding as of the most recently ended reporting period if the NCUSIF's equity ratio, as defined, is less than 1.3 percent. When the NCUA Board projects that the equity ratio will, within six months, fall below 1.2 percent, the NCUA Board shall establish and implement a restoration plan within 90 days, which meets the statutory requirements and any further conditions that the NCUA Board determines appropriate. In order to meet statutory requirements, the plan must provide that the equity ratio will meet or exceed the minimum amount specified (1.2 percent) before the end of the 8-year period beginning upon the implementation of the plan (or such longer period as the NCUA Board may determine to be necessary due to extraordinary circumstances).

In addition, the NCUSIF has borrowing authority, shared with the TCCUSF, from the U.S. Treasury, and the ability to borrow from the NCUA's CLF.

SOURCE OF GAAP

NCUA reports on its five funds using two different primary sources of generally accepted accounting principles (GAAP):

Fund	Primary GAAP	
	FASAB	FASB
National Credit Union Share Insurance Fund (NCUSIF)	X	
NCUA Operating Fund (the Fund)		X
NCUA Central Liquidity Facility (CLF)		X
NCUA Community Development Revolving Loan Fund (CDRLF)		X
Temporary Corporate Credit Union Stabilization Fund (TCCUSF)	X	

SFFAS 34, *The Hierarchy of Generally Accepted Accounting Principles, Including the Application of Standards Issued by the Financial Accounting Standards Board*, recognizes that a limited number of federal entities prepare and publish financial reports pursuant to the accounting and reporting standards issued by the Financial Accounting Standards Board (FASB). SFFAS 34 provides that financial reports prepared in conformity with accounting standards issued by the FASB also may be regarded as in conformity with GAAP.

SIGNIFICANT FINANCIAL STATEMENT ELEMENTS¹

Excerpts from FY 2012 NCUA Annual Report

¹ Source: NCUA website --<http://www.ncua.gov/Legal/RptsPlans/AnnRpts/Pages/annualrpt.aspx> last accessed on June 5, 2013.

NATIONAL CREDIT UNION SHARE INSURANCE FUND

BALANCE SHEETS

As of December 31, 2012 and 2011

(Dollars in thousands)

	2012	2011
ASSETS		
INTRAGOVERNMENTAL		
Fund Balance with Treasury (Note 2)	\$ 2,479	\$ 423
Investments, Net U.S. Treasury Securities (Note 3)	11,293,087	11,392,576
Accounts Receivable Other	8	10
Accounts Receivable Note due from the National Credit Union Administration Operating Fund (Note 4)	14,415	15,756
Accrued Interest Receivable (Note 3)	63,154	81,707
Total Intragovernmental Assets	11,373,143	11,490,472
PUBLIC		
Accounts Receivable Capitalization Deposits from Insured Credit Unions, Net (Note 4)	38	30
Accounts Receivable Premium Assessments from Insured Credit Unions, Net (Note 4)		73
Accounts Receivable Other	25	
General Property, Plant, and Equipment, Net		18
Notes Receivable, Net (Note 5)	249,254	70,000
Accrued Interest Receivable Notes (Note 5)	202	150
Other Receivables from Asset Management Estates (AMEs), Net (Note 6)	252,029	114,741
Total Public Assets	501,548	185,012
TOTAL ASSETS	\$ 11,874,691	\$ 11,675,484
LIABILITIES		
INTRAGOVERNMENTAL		
Accounts Payable Due to the Temporary Corporate Credit Union Stabilization Fund	\$ 690	\$
Accounts Payable Due to the National Credit Union Administration Operating Fund (Note 9)	2,040	1,182
Other Distribution Payable to the Temporary Corporate Credit Union Stabilization Fund (Note 8)	88,090	278,641
Total Intragovernmental Liabilities	90,820	279,823
PUBLIC		
Accounts Payable	87,567	166
Other Insurance and Guarantee Program Liabilities (Note 7)	412,452	606,617
Total Public Liabilities	500,019	606,783
TOTAL LIABILITIES	590,839	886,606
Commitments and Contingencies (Note 7)		
NET POSITION		
Contributed Capital (Note 12)	8,315,011	7,805,718
Cumulative Result of Operations	2,968,841	2,983,160
Total Net Position	11,283,852	10,788,878
TOTAL LIABILITIES AND NET POSITION	\$ 11,874,691	\$ 11,675,484

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

NATIONAL CREDIT UNION SHARE INSURANCE FUND

STATEMENTS OF NET COST

For the Years Ended December 31, 2012 and 2011

(Dollars in thousands)

	2012	2011
GROSS COSTS		
Operating Expenses	\$ 141,237	\$ 132,358
Provision for Insurance Losses		
Reserve Expense (Reduction) (Note 7)	(74,874)	(525,678)
AME Receivable Bad Debt Expense (Reduction) (Note 6)	(2,910)	(6,730)
Total Gross Costs	63,453	(400,050)
LESS EARNED REVENUES		
Interest Revenue on Note Receivable from the National Credit Union Administration Operating Fund (Note 4)	(290)	(344)
Interest Revenue on Notes (Note 5)	(2,097)	(150)
Insurance and Guarantee Premium Revenue	(6,381)	(543)
Total Earned Revenues	(8,768)	(1,037)
TOTAL NET COST/(INCOME) OF OPERATIONS	\$ 54,685	\$ (401,087)

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

RELEVANT GAO REPORTS (LAST 5 YEARS)

NATIONAL CREDIT UNION ADMINISTRATION: Earlier Actions Are Needed to Better Address Troubled Credit Unions
GAO-12-247, Jan 4, 2012

RELEVANT DISCLOSURES IN AFR

See attached disclosure excerpts

RELATED DISCLOSURES IN CFR

Excerpt from 2012 CFR RSI: Risk Assumed

Risk Assumed

Risk assumed information is important for all Federal insurance and guarantee programs, except social insurance, life insurance, and loan guarantee programs. Risk assumed is generally measured by the present value of unpaid expected losses net of associated premiums, based on the risk inherent in the insurance or guarantee coverage in force. In addition to the liability for unpaid insurance claims included in Note 18—Insurance and Guarantee Program Liabilities, for events that have already occurred, the Government also is required to report as supplementary information risk assumed amounts and the periodic changes in those amounts.

The assessments of losses expected based on the risk assumed are based on actuarial or financial methods that include information and assumptions applicable to the economic, legal, and policy environment in force at the time the assessments are made. Management has estimated the loss amounts based on the risk assumed as well as the periodic changes.

Please refer to the individual financial statements of the PBGC, USDA, and NCUA for further detailed information, including information as to the indicators of the range of uncertainty around expected estimates and the indicators of the sensitivity of the estimates to changes in major assumptions. We note that this table does not include all federal insurance and guarantee programs.

Risk Assumed Information as of September 30, 2012, and 2011

(In billions of dollars)

	2012	2011
Present value of unpaid expected losses, net of associated premiums:		
Pension Benefit Guaranty Corporation	321.7	250.2
Department of Agriculture	18.3	8.8
National Credit Union Administration	3.4	7.4
All other	0.9	0.9
Total	344.3	267.3
Periodic changes in risk assumed amounts:		
Pension Benefit Guaranty Corporation	71.5	60.2
Department of Agriculture	9.5	1.3
National Credit Union Administration	(4.0)	(0.1)
All other	-	(1.1)
Total	77.0	60.3

PENSION BENEFIT INSURANCE

PENSION BENEFIT GUARANTY CORPORATION

www.PBGC.gov

BRIEF SUMMARY OF PROGRAM

The Pension Benefit Guaranty Corporation (PBGC) is a self-financing, wholly owned Government Corporation, established by title IV of the Employee Retirement Income Security Act of 1974. PBGC was created to encourage the growth of defined benefit pension plans, provide timely and uninterrupted payment of pension benefits, and keep pension insurance premiums at a minimum. Defined benefit pension plans promise to pay a specified monthly benefit at retirement, commonly based on salary and years on the job. PBGC protects the retirement incomes of more than 40 million American workers in more than 26,000 private-sector defined benefit pension plans. A defined benefit plan provides a specified monthly benefit at retirement, often based on a combination of salary and years of service. PBGC was created to encourage the continuation and maintenance of private-sector defined benefit pension plans, provide timely and uninterrupted payment of pension benefits, and keep pension insurance premiums at a minimum.

“Making the private pension system work well is vital to the retirement security of the millions of workers and retirees who depend on pension benefits and is a priority of this Administration. The Pension Benefit Guaranty Corporation has a key role in these efforts and in safeguarding the pension benefits of America's workers. The PBGC does this by paying guaranteed benefits earned by workers on time, and by working with employers to encourage them to maintain their pension plans and keep their pension promises.” – 2012 PBGC Annual Report

RELATED LEGISLATION AND U.S. CODE (U.S.C.)

1. The Employee Retirement Income Security Act of 1974
2. The Pension Protection Act of 2006

SOURCES OF FINANCING

PBGC is not funded by general tax revenues. PBGC collects insurance premiums from employers that sponsor insured pension plans, earns money from investments and receives funds from pension plans it takes over.

SOURCE OF GAAP

PBGC primarily applies generally accepted accounting principles (GAAP) issued by the Financial Accounting Standards Board (FASB). This practice is permitted by paragraph 9 of Statement of Federal Financial Accounting Standards 34, *The Hierarchy of Generally Accepted Accounting Principles, Including the Application of Standards Issued by the Financial Accounting Standards Board*.

SIGNIFICANT FINANCIAL STATEMENT ELEMENTS¹

Excerpts from FY 2012 PBGC Annual Report

PENSION BENEFIT GUARANTY CORPORATION STATEMENTS OF FINANCIAL CONDITION

	Single-Employer Program		Multiemployer Program		Memorandum Total	
	September 30,		September 30,		September 30,	
<i>(Dollars in Millions)</i>	2012	2011	2012	2011	2012	2011
ASSETS						
Cash and cash equivalents	\$ 3,767	\$ 5,021	\$ 25	\$ 5	\$ 3,792	\$ 5,026
Securities lending collateral (Notes 3 and 5)	3,425	4,587	0	0	3,425	4,587
Investments, at market (Notes 3 and 5):						
Fixed maturity securities	48,176	46,257	1,767	1,720	49,943	47,977
Equity securities	22,619	17,997	0	0	22,619	17,997
Private equity	1,339	1,459	0	0	1,339	1,459
Real estate and real estate investment trusts	511	536	0	0	511	536
Other	77	22	0	0	77	22
Total investments	72,722	66,271	1,767	1,720	74,489	67,991
Receivables, net:						
Sponsors of terminated plans	41	31	0	0	41	31
Premiums (Note 11)	1,086	561	1	1	1,087	562
Sale of securities	1,353	1,807	0	0	1,353	1,807
Derivative contracts (Note 4)	83	178	0	0	83	178
Investment income	452	469	12	12	464	481
Other	4	3	0	0	4	3
Total receivables	3,019	3,049	13	13	3,032	3,062
Capitalized assets, net	40	32	2	1	42	33
Total assets	\$ 82,973	\$ 78,960	\$ 1,807	\$ 1,739	\$ 84,780	\$ 80,699

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

¹ Source: PBGC website -- <http://www.pbtc.gov/res/reports/ar2012.html>, last accessed on June 5, 2013.

PENSION BENEFIT GUARANTY CORPORATION
STATEMENTS OF FINANCIAL CONDITION

	Single-Employer Program		Multiemployer Program		Memorandum Total	
	September 30,		September 30,		September 30,	
<i>(Dollars in Millions)</i>	2012	2011	2012	2011	2012	2011
LIABILITIES						
Present value of future benefits, net (Note 6):						
Trusteed plans	\$103,126	\$ 91,718	\$1	\$ 1	\$103,127	\$ 91,719
Plans pending termination and trusteeship	418	346	0	0	418	346
Settlements and judgments	56	56	0	0	56	56
Claims for probable terminations	2,035	833	0	0	2,035	833
Total present value of future benefits, net	105,635	92,953	1	1	105,636	92,954
Present value of nonrecoverable future financial assistance (Note 7)						
Insolvent plans	0	0	1,388	1,232	1,388	1,232
Probable insolvent plans	0	0	5,622	3,243	5,622	3,243
Total present value of nonrecoverable future financial assistance	0	0	7,010	4,475	7,010	4,475
Payables, net:						
Derivative contracts (Note 4)	94	173	0	0	94	173
Due for purchases of securities	2,557	4,079	0	0	2,557	4,079
Payable upon return of securities loaned	3,425	4,587	0	0	3,425	4,587
Unearned premiums	328	366	30	31	358	397
Accounts payable and accrued expenses (Note 8)	76	68	3	2	79	70
Total payables	6,480	9,273	33	33	6,513	9,306
Total liabilities	112,115	102,226	7,044	4,509	119,159	106,735
Net position	(29,142)	(23,266)	(5,237)	(2,770)	(34,379)	(26,036)
Total liabilities and net position	\$82,973	\$ 78,960	\$1,807	\$1,739	\$84,780	\$ 80,699

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

PENSION BENEFIT GUARANTY CORPORATION
STATEMENTS OF OPERATIONS AND CHANGES IN NET POSITION

	Single-Employer Program		Multiemployer Program		Memorandum Total	
	For the Years Ended September 30,		For the Years Ended September 30,		For the Years Ended September 30,	
(Dollars in Millions)	2012	2011	2012	2011	2012	2011
UNDERWRITING						
Income:						
Premium, net (Note 11)	\$ 2,642	\$ 2,072	\$ 92	\$ 92	\$ 2,734	\$ 2,164
Other	13	17	-	0	13	17
Total	2,655	2,089	92	92	2,747	2,181
Expense:						
Administrative	360	353	20	14	380	367
Other	-	21	-	0	-	21
Total	360	374	20	14	380	388
Other underwriting activity:						
Losses from completed and probable terminations (Note 12)	2,006	201	-	0	2,006	201
Losses from insolvent and probable plans- financial assistance (Note 7)			2,466	1,461	2,466	1,461
Actuarial adjustments (credits) (Note 6)	229	1,672	(6)	37	223	1,709
Total	2,235	1,873	2,460	1,498	4,695	3,371
Underwriting gain (loss)	60	(158)	(2,388)	(1,420)	(2,328)	(1,578)
FINANCIAL:						
Investment income (loss) (Note 13):						
Fixed	4,699	3,502	91	148	4,790	3,650
Equity	4,073	(276)	-	0	4,073	(276)
Private equity	42	144	-	0	42	144
Other	(22)	76	-	0	(22)	76
Total	8,792	3,446	91	148	8,983	3,594
Expense:						
Interest	83	71	-	0	83	71
Actuarial charges (Note 6):						
Due to expected interest	3,927	3,880	54	52	3,981	3,932
Due to change in interest rates	10,718	1,009	116	10	10,834	1,019
Total	14,728	4,960	170	62	14,898	5,022
Financial income (loss)	(5,936)	(1,514)	(79)	86	(6,015)	(1,428)
Net loss	(5,876)	(1,672)	(2,467)	(1,334)	(8,343)	(3,006)
Net position, beginning of year						
	(23,266)	(21,594)	(2,770)	(1,436)	(26,036)	(23,030)
Net position, end of year						
	\$ (29,142)	\$ (23,266)	\$ (5,237)	\$ (2,770)	\$ (34,379)	\$ (26,036)

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

RELEVANT GAO REPORTS (LAST 5 YEARS)

PRIVATE PENSIONS: Multiemployer Plans and PBGC Face Urgent Challenges
GAO-13-428T, Mar 5, 2013

PENSION BENEFIT GUARANTY CORPORATION: Redesigned Premium Structure Could Better Align Rates with Risk from Plan Sponsors
GAO-13-58, Nov 7, 2012

PENSION BENEFIT GUARANTY CORPORATION: Asset Management Needs Better Stewardship
GAO-11-271, Jun 30, 2011

PENSION BENEFIT GUARANTY CORPORATION: More Strategic Approach to Contracting Still Needed
GAO-11-588, Jun 29, 2011

PENSION BENEFIT GUARANTY CORPORATION: Improvements Needed to Strengthen Governance Structure and Strategic Management
GAO-11-182T, Dec 1, 2010

PENSION BENEFIT GUARANTY CORPORATION : Workers and Retirees Experience Delays and Uncertainty when Underfunded Plans Are Terminated
GAO-10-181T, Oct 29, 2009

PENSION BENEFIT GUARANTY CORPORATION: More Strategic Approach Needed for Processing Complex Plans Prone to Delays and Overpayments
GAO-09-716, Aug 17, 2009

PENSION BENEFIT GUARANTY CORPORATION: Financial Challenges Highlight Need for Improved Governance and Management
GAO-09-702T, May 20, 2009

RELEVANT DISCLOSURES IN AFR

See attached disclosure excerpts

RELATED DISCLOSURES IN CFR

Excerpt from 2012 CFR Note 18: Insurance and Guarantee Program Liabilities

Note 18. Insurance and Guarantee Program Liabilities

Insurance and Guarantee Program Liabilities as of September 30, 2012, and 2011

(In billions of dollars)	2012	2011
Insurance and Guarantee Program Liabilities:		
Pension Benefit Guaranty Corporation - Benefit Pension Plans	105.6	93.0
Federal Deposit Insurance Corporation Funds	26.5	47.4
All other insurance and guarantee programs	24.3	21.3
Total insurance and guarantee program liabilities	156.4	161.7

PBGC insures pension benefits for participants in covered defined benefit pension plans. As a wholly-owned corporation of the U.S. Government, PBGC's financial activity and balances are included in the consolidated financial statements of the U.S. Government. However, under current law, PBGC's liabilities may be paid only from PBGC's assets and not from the General Fund of the Treasury or assets of the Government in general. As of September 30, 2012, and 2011, PBGC had total liabilities of \$119.2 billion and \$106.7 billion, and its total liabilities exceeded its total assets by \$34.4 billion and \$26.0 billion, respectively. In addition, as discussed in Note 22—Contingencies, PBGC reported reasonably possible contingent losses of about \$321.8 billion and \$250.2 billion as of September 30, 2012, and 2011, respectively. Of the total FDIC amount as of September 30, 2012, and 2011, \$3.6 billion and \$7.2 billion, respectively, represents the recorded contingent liability and loss provision for institutions insured by the Deposit Insurance Fund that are likely to fail. In addition, \$21.2 billion and \$31.5 billion pertain to liabilities due to resolutions of failed or failing institutions and to pending depositor claims as of September 30, 2012, and 2011 respectively. Another \$1.7 billion and \$8.2 billion as of September 30, 2012, and 2011 respectively, pertains to the Temporary Liquidity Guarantee Program, which guarantees certain newly issued debt and certain noninterest-bearing transaction accounts in an effort to counter the system-wide crisis in the nation's financial sector. The remaining amounts represent contingent liabilities for litigation.

Of the \$24.3 billion and \$21.3 billion under all other insurance and guarantee programs as of September 30, 2012, and 2011, respectively, \$20.0 billion and \$10.3 billion, respectively, pertain to the USDA's Federal Crop Insurance Program. The increase in the estimated indemnities is due to the most severe drought in the farm belt since 1988. The Federal Crop Insurance Program is administered by the Federal Crop Insurance Corporation, whose mission is to provide an actuarially sound risk management program to reduce agricultural producers' economic losses due to natural disasters. Also, \$3.4 billion and \$7.4 billion relates to the National Credit Union Administration's Temporary Corporate Credit Union Stabilization Fund as of September 30, 2012, and 2011, respectively. This Program guarantees the timely payment of principal and interest on certain unsecured debt of participating credit unions.

Excerpt from 2012 CFR Note 22: Contingencies

Insurance Contingencies

At the time an insurance policy is issued, a contingency arises. The contingency is the risk of loss assumed by the insurer, that is, the risk of loss from events that may occur during the term of the policy. The Government has insurance contingencies that are reasonably possible in the amount of \$329.0 billion as of September 30, 2012, and \$267.0 billion as of September 30, 2011. The major programs are identified below:

- PBGC reported \$321.8 billion and \$250.2 billion as of September 30, 2012, and 2011, respectively, for the estimated aggregate unfunded vested benefits exposure to the PBGC for private-sector single-employer and multiemployer defined benefit pension plans that are classified as a reasonably possible exposure to loss.
- FDIC reported \$6.9 billion and \$16.5 billion as of September 30, 2012, and 2011, respectively, for identified additional risk in the financial services industry that could result in additional loss to the Deposit Insurance Fund should potentially vulnerable insured institutions ultimately fail. Actual losses, if any, will largely depend on future economic and market conditions.

Excerpt from 2012 CFR RSI: Risk Assumed

Risk Assumed

Risk assumed information is important for all Federal insurance and guarantee programs, except social insurance, life insurance, and loan guarantee programs. Risk assumed is generally measured by the present value of unpaid expected losses net of associated premiums, based on the risk inherent in the insurance or guarantee coverage in force. In addition to the liability for unpaid insurance claims included in Note 18—Insurance and Guarantee Program Liabilities, for events that have already occurred, the Government also is required to report as supplementary information risk assumed amounts and the periodic changes in those amounts.

The assessments of losses expected based on the risk assumed are based on actuarial or financial methods that include information and assumptions applicable to the economic, legal, and policy environment in force at the time the assessments are made. Management has estimated the loss amounts based on the risk assumed as well as the periodic changes.

Please refer to the individual financial statements of the PBGC, USDA, and NCUA for further detailed information, including information as to the indicators of the range of uncertainty around expected estimates and the indicators of the sensitivity of the estimates to changes in major assumptions. We note that this table does not include all federal insurance and guarantee programs.

Risk Assumed Information as of September 30, 2012, and 2011		
(In billions of dollars)	2012	2011
Present value of unpaid expected losses, net of associated premiums:		
Pension Benefit Guaranty Corporation	321.7	250.2
Department of Agriculture	18.3	8.8
National Credit Union Administration	3.4	7.4
All other	0.9	0.9
Total	344.3	267.3
Periodic changes in risk assumed amounts:		
Pension Benefit Guaranty Corporation	71.5	60.2
Department of Agriculture	9.5	1.3
National Credit Union Administration	(4.0)	(0.1)
All other	-	(1.1)
Total	77.0	60.3

NATIONAL FLOOD INSURANCE

FEDERAL EMERGENCY MANAGEMENT AGENCY
(DEPARTMENT OF HOMELAND SECURITY)

WWW.FEMA.GOV

BRIEF SUMMARY OF PROGRAM

The Federal Emergency Management Agency (FEMA) was originally founded in 1979 as an independent Federal agency reporting to the President. In March 2003, FEMA joined 22 other federal agencies, programs and offices in becoming the Department of Homeland Security (DHS).

FEMA's mission is to:

Support our citizens and first responders to ensure that as a nation we work together to build, sustain and improve our capability to prepare for, protect against, respond to, recover from and mitigate all hazards.

.FEMA is responsible for coordinating the Federal response to floods, earthquakes, hurricanes, and other natural or man-made disasters and providing disaster assistance to States, communities and individuals. Disasters are declared by the President at the request of the Governor of the impacted State if the impacts of the disaster exceed the ability of the State and the affected communities to respond.

The Federal Insurance and Mitigation Administration (FIMA) within FEMA is responsible for administering the National Flood Insurance Program (NFIP) and administering programs that provide assistance for mitigating future damages from natural hazards. The NFIP is a Federal program created by Congress to mitigate future flood losses nationwide through sound, community-enforced building and zoning ordinances and to provide access to affordable, federally backed flood insurance protection for property owners. The NFIP is designed to provide an insurance alternative to disaster assistance to meet the escalating costs of repairing damage to buildings and their contents caused by floods.

"The NFIP is not simply an insurance program. It works to reduce the cost of flood damage through identifying, analyzing, and reducing flood risk." – 2013 FEMA NFIP Budget Justification

RELATED LEGISLATION AND U.S. CODE (U.S.C.)

1. National Flood Insurance Act of 1968 (42 U.S.C. § 4001 et seq.)
 2. Flood Disaster Protection Act of 1973
 3. National Flood Insurance Reform Act of 1994
 4. Bunning-Bereuter-Blumenauer Flood Insurance Reform Act (FIRA) of 2004
 5. Biggert-Waters Flood Insurance Reform Act of 2012
-

SOURCES OF FINANCING

Until 1986, the NFIP was funded, in part, by congressional appropriations. The NFIP was self-supporting from 1986 until 2005 as policy premiums and fees covered all expenses and claim payments. Funding for the National Flood Insurance Program is currently derived from offsetting collections two primary sources:

- Flood insurance premiums, which are used to pay claims and flood-related grants, and to provide funding to support the operating and administrative costs associated with maintaining the program. FEMA estimates mandatory premium collections of \$3.38 billion in FY 2013.
- Policy fee income, also paid by flood insurance policy holders, which supports floodplain management, flood mapping, insurance operations, and NFIP management. For FY 2013, FEMA projects fee collections of \$171 million, which reflects no change in funding from FY 2012.

In 2005, the NFIP incurred approximately \$17 billion in flood claims caused by Hurricanes Katrina, Rita, and Wilma (KRW). FEMA paid \$19.28 billion in KRW-related claims as a result of the 2005 Gulf Coast hurricanes. This amount exceeded its premiums earned annually and its \$1.5 billion borrowing authority from the U.S. Treasury. As a result of the catastrophic property losses under the NFIP from KRW, in September 2005, the Congress passed and the President signed into law legislation to increase NFIP borrowing authority first to \$3.5 billion (P.L. 109-65) and then to \$18.5 billion (P.L. 109-106) in November 21, 2005, and finally to \$20.775 billion (P.L. 109-208) on March 23, 2006, to allow the agency to continue to pay claims. On September 27, 2007, the House approved H.R. 3121, the Flood Insurance Reform and Modernization Act of 2007, to reform the program while retaining its original intent to keep rates affordable for people to buy the insurance. H.R. 3121 would also increase the NFIP's Treasury borrowing authority from \$20.775 to \$21.5 billion. Under current law, funds borrowed from the Treasury must be repaid with interest.

SOURCES OF GAAP

DHS's financial statements are prepared from the accounting records of the Department based on guidance in U.S. generally accepted accounting principles (GAAP) and OMB Circular A-136, *Financial Reporting Requirements*, as amended. GAAP for federal

entities are the standards prescribed by the Federal Accounting Standards Advisory Board, the official accounting standards-setting body of the Federal Government.

SIGNIFICANT FINANCIAL STATEMENT ELEMENTS¹

Excerpts from FY 2012 DHS Annual Financial Report

Department of Homeland Security FY 2012 Annual Financial Report

	Customs User Fees	Sport Fish Restoration Boating Trust Fund	Immigration Examination Fees	National Flood Insurance Program	Oil Spill Liability Trust Fund	Aviation Security Capital Fund	All Other Earmarked Funds	Total Earmarked Funds
Balance Sheet as of September 30, 2012								
ASSETS								
Fund Balance with Treasury	\$ 67	\$ 34	\$ 1,939	\$ 1,026	\$ 6	\$ 1,239	\$ 921	\$ 5,232
Investments, Net	-	1,949	-	-	2,599	-	3	4,551
Accounts Receivable	135	124	10	3	501	-	66	839
Taxes Receivable	123	-	-	-	-	-	-	123
Other	-	-	278	627	-	-	2	907
Total Assets	\$ 325	\$ 2,107	\$ 2,227	\$ 1,656	\$ 3,106	\$ 1,239	\$ 992	\$ 11,652
LIABILITIES								
Other Liabilities	\$ 144	\$ 1,302	\$ 1,144	\$ 20,730	\$ 329	\$ 26	\$ 32	\$ 23,707
Total Liabilities	\$ 144	\$ 1,302	\$ 1,144	\$ 20,730	\$ 329	\$ 26	\$ 32	\$ 23,707
NET POSITION								
Cumulative Results of Operations	\$ 181	\$ 805	\$ 1,083	\$ (19,074)	\$ 2,777	\$ 1,213	\$ 960	\$ (12,055)
Total Liabilities and Net Position	\$ 325	\$ 2,107	\$ 2,227	\$ 1,656	\$ 3,106	\$ 1,239	\$ 992	\$ 11,652
Statement of Net Cost for the Year Ended September 30, 2012								
Gross Program Costs	\$ 472	\$ 118	\$ 2,517	\$ 988	\$ 431	\$ 51	\$ 1,003	\$ 5,580
Less: Earned Revenue	-	-	(2,629)	(3,494)	(237)	(250)	(631)	(7,281)
Net Cost of Operations	\$ 472	\$ 118	\$ (112)	\$ (2,506)	\$ 174	\$ (199)	\$ 352	\$ (1,701)
Statement of Changes in Net Position for the Year Ended September 30, 2012								
Net Position Beginning of Period	\$ 796	\$ 773	\$ 848	\$ (21,568)	\$ 2,469	\$ 1,014	\$ 828	\$ (14,840)
Prior-Period Adjustment Due to Changes in Accounting Principle	(640)	-	-	-	-	-	-	(640)
Net Position Beginning of Period, as Adjusted	156	773	848	(21,568)	2,469	1,014	828	(15,480)
Net Cost of Operations	(472)	(118)	112	2,506	(174)	199	(352)	1,701
Non-exchange Revenue	463	663	-	1	517	-	173	1,817
Other	34	(513)	123	(13)	(35)	-	311	(93)
Change in Net Position	25	32	235	2,494	308	199	132	3,425
Net Position, End of Period	\$ 181	\$ 805	\$ 1,083	\$ (19,074)	\$ 2,777	\$ 1,213	\$ 960	\$ (12,055)

¹ Source: DHS website -- <http://www.dhs.gov/performance-accountability>, last accessed on June 5, 2013.

Department of Homeland Security FY 2012 Annual Financial Report

	Customs User Fees	Sport Fish Restoration Boating Trust Fund	Immigration Examination Fees	National Flood Insurance Program	Oil Spill Liability Trust Fund	Aviation Security Capital Fund	All Other Earmarked Funds	Total Earmarked Funds
Balance Sheet as of September 30, 2011								
ASSETS								
Fund Balance with Treasury	\$ 717	\$ 9	\$ 1,743	\$ 1,211	\$ 200	\$ 1,030	\$ 832	\$ 5,742
Investments, Net	-	1,895	-	-	2,263	-	1	4,159
Accounts Receivable	98	132	7	2	309	-	42	590
Taxes Receivables	86	-	-	-	-	-	-	86
Other	-	-	187	567	-	-	8	762
Total Assets	\$ 901	\$ 2,036	\$ 1,937	\$ 1,780	\$ 2,772	\$ 1,030	\$ 883	\$ 11,339
LIABILITIES								
Other Liabilities	\$ 105	\$ 1,263	\$ 1,089	\$ 23,348	\$ 303	\$ 16	\$ 55	\$ 26,179
Total Liabilities	\$ 105	\$ 1,263	\$ 1,089	\$ 23,348	\$ 303	\$ 16	\$ 55	\$ 26,179
NET POSITION								
Cumulative Results of Operations	\$ 796	\$ 773	\$ 848	\$ (21,568)	\$ 2,469	\$ 1,014	\$ 828	\$ (14,840)
Total Liabilities and Net Position	\$ 901	\$ 2,036	\$ 1,937	\$ 1,780	\$ 2,772	\$ 1,030	\$ 883	\$ 11,339
Statement of Net Cost for the Year Ended September 30, 2011 (unaudited)								
Gross Program Costs	\$ 407	\$ 126	\$ 2,433	\$ 5,312	\$ 319	\$ 38	\$ 859	\$ 9,494
Less: Earned Revenue	-	-	(2,578)	(3,313)	(330)	(250)	(558)	(7,029)
Net Cost of Operations	\$ 407	\$ 126	\$ (145)	\$ 1,999	\$ (11)	\$ (212)	\$ 301	\$ 2,465
Statement of Changes in Net Position for the Year Ended September 30, 2011 (unaudited)								
Net Position, Beginning of Period	\$ 789	\$ 794	\$ 640	\$ (19,563)	\$ 2,005	\$ 807	\$ 712	\$ (13,816)
Net Cost of Operations	(407)	(126)	145	(1,999)	11	212	(301)	(2,465)
Non-exchange Revenue	406	638	-	1	547	-	143	1,735
Other	8	(533)	63	(7)	(94)	(5)	274	(294)
Change in Net Position	7	(21)	208	(2,005)	464	207	116	(1,024)
Net Position, End of Period	\$ 796	\$ 773	\$ 848	\$ (21,568)	\$ 2,469	\$ 1,014	\$ 828	\$ (14,840)

Financial Information

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RELEVANT GAO REPORTS (LAST 5 YEARS)

FLOOD INSURANCE: Public Policy Goals Provide a Framework for Reform
GAO-11-670T, Jun 23, 2011

FLOOD INSURANCE: FEMA's Rate-Setting Process Warrants Attention
GAO-09-12, Oct 31, 2008

FLOOD INSURANCE: Options for Addressing the Financial Impact of Subsidized Premium Rates on the National Flood Insurance Program
GAO-09-20, Nov 14, 2008

FLOOD INSURANCE: Opportunities Exist to Improve Oversight of the WYO Program
GAO-09-455, Aug 21, 2009

ECONOMIC DEVELOPMENT: Information on Proposed Changes to the National Flood Insurance Program
GAO-09-420R, Feb 27, 2009

FEMA: Action Needed to Improve Administration of the National Flood Insurance Program
GAO-11-297, Jun 9, 2011

NATIONAL FLOOD INSURANCE PROGRAM: Continued Actions Needed to Address Financial and Operational Issues
GAO-10-1063T, Sep 22, 2010

FINANCIAL MANAGEMENT: Improvements Needed in National Flood Insurance Program's Financial Controls and Oversight
GAO-10-66, Dec 22, 2009

NATIONAL FLOOD INSURANCE PROGRAM: Financial Challenges Underscore Need for Improved Oversight of Mitigation Programs and Key Contracts
GAO-08-437, Jun 16, 2008

NATURAL CATASTROPHE INSURANCE: Analysis of a Proposed Combined Federal Flood and Wind Insurance Program
GAO-08-504, Apr 25, 2008

RELEVANT DISCLOSURE IN THE AFR

See attached disclosure excerpts

RELEVANT DISCLOSURES IN CFR

None

FEDERAL CROP INSURANCE

USDA RISK MANAGEMENT AGENCY FEDERAL CROP INSURANCE CORPORATION

WWW.RMA.USDA.GOV/FCIC/

BRIEF SUMMARY OF PROGRAM

The role of USDA's Risk Management Agency (RMA) is to help producers manage their business risks through effective, market-based risk management solutions. RMA's mission is to promote, support, and regulate sound risk management solutions to preserve and strengthen the economic stability of America's agricultural producers. As part of this mission, RMA operates and manages the Federal Crop Insurance Corporation (FCIC).

The Federal Crop Insurance Program is administered by the Federal Crop Insurance Corporation, whose mission is to provide an actuarially sound risk management program to reduce agricultural producers' economic losses due to natural disasters. The Federal Crop Insurance Corporation (FCIC) promotes the economic stability of agriculture through a sound system of crop insurance and providing the means for the research and experience helpful in devising and establishing such insurance. Management is vested in a Board of Directors, subject to the general supervision of the Secretary of Agriculture.¹

"It's a public private-insurance system that is frankly working very well," Senate Agriculture committee Chairwoman Debbie Stabenow, D-Mich., said on the Senate floor while debating a bill that would expand government-subsidized crop insurance.²

RELATED LEGISLATION AND U.S. CODE (U.S.C.)

1. Administrative Regulations 7 CFR Part 400
2. 2008 Farm Bill
3. Federal Crop Insurance Act
4. Federal Crop Insurance Statute: Outline | Full Text

¹ Source: USDA Federal Crop Insurance Corporation (FCIC) at <http://www.rma.usda.gov/fcic/> last accessed May 22, 2013.

² Source: "Senate debating federal dollars for crop insurance" at <http://news.yahoo.com/senate-debating-federal-dollars-crop-insurance-162851157.html> last accessed May 22, 2013.

5. Text of H.R. 2559 - Agricultural Risk Protection Act of 2000

SOURCES OF FINANCING

The U.S. crop insurance program is funded by taxpayers, regulated by USDA's Risk Management Agency (RMA), but sold and serviced by private business. (There are economic and historical reasons why the program is neither all public nor all private.)

USDA Risk Management Agency Federal Crop Insurance Corporation receives annual appropriations and is listed in the Budget. However, farmers must pay for crop insurance, but they pay only a portion of the amount needed to cover insured losses. Throughout the 1980s and 1990s, farmers were reluctant to buy enough crop insurance to satisfy Congress. So to get farmers to buy more insurance, ARPA dramatically decreased the portion that farmers must pay. Currently, farmers pay about 41 percent of the amount needed to cover insured losses. This large subsidy means that most farmers will get substantially more back from the program than they pay into it.

SOURCE OF GAAP

USDA primarily applies generally accepted accounting principles (GAAP) issued by the FASAB.

SIGNIFICANT FINANCIAL STATEMENT ELEMENTS

Cash consists of Federal crop escrow amounts

Other Liabilities for losses on crop insurance claims

RELEVANT GAO REPORTS (LAST 5 YEARS)

- Crop Insurance: Savings Would Result from Program Changes and Greater Use of Data Mining, GAO-12-256, Mar 13, 2012.** The U.S. Department of Agriculture (USDA) administers the federal crop insurance program with private insurance companies. In 2011, the program provided about \$113 billion in insurance coverage for over 1 million policies. Program costs include subsidies to pay for part of farmers' premiums. According to the Congressional Budget Office, for fiscal years 2013 through 2022, the program costs—primarily premium subsidies—will average \$8.9 billion annually. GAO determined the (1) effect on program costs of applying limits on farmers' premium subsidies, as payment limits are set for other farm programs, and (2) extent to which USDA uses key data mining tools to prevent and detect fraud, waste, and abuse in the program. GAO analyzed USDA data, reviewed economic studies, and interviewed USDA officials. To reduce crop insurance program costs, Congress should consider limiting premium subsidies for individual farmers, reducing subsidies for all farmers, or both. GAO also recommends, in part, that USDA encourage the completion of field inspections. In commenting on a report draft, USDA did not agree that Congress should consider limiting premium subsidies, but GAO believes that when farm income is at a record high and the nation faces

severe fiscal problems, limiting premium subsidies is an appropriate area for consideration. USDA agreed with encouraging the completion of field inspections.

- Crop Insurance: Opportunities Exist to Reduce the Costs of Administering the Program, GAO-09-445, Apr 29, 2009.** The U.S. Department of Agriculture (USDA) administers the federal crop insurance program with private insurance companies, which, in turn, work with insurance agencies that sell crop insurance. In 2008, according to USDA, the program cost \$6.5 billion, including about \$2.0 billion in allowances to insurance companies to cover their administrative and operating (A&O) expenses, such as salaries and sales commissions to agencies. GAO was asked to examine (1) the reasons for recent substantial increases in A&O allowances, and the purposes for which insurance companies use these allowances, and (2) insurance agencies' expenses for selling federal crop insurance policies, and questionable practices, if any, that agencies use to compete for business among farmers. GAO analyzed USDA and private insurers' data, among other things. Companies reported to USDA that their expenses to administer the program in 2007 exceeded their allowances. However, GAO determined that these expenses exceeded allowances largely because of the higher commissions paid to insurance agencies. USDA and state insurance regulators are working to reduce the potential for this practice.

DISCLOSURES IN AFR

Excerpts from FY 2012 USDA Agency Financial Report³

Note 4. Cash and Other Monetary Assets

In FY 2012 and FY 2011, cash mostly consists of Federal crop insurance escrow amounts of \$183 million and \$247 million respectively.

	FY 2012	FY 2011
Cash	\$ 183	\$ 248

³ Source: USDA website -- <http://www.ocfo.usda.gov/> last accessed June 6, 2013.

Note 12. Liabilities Not Covered By Budgetary Resources

In FY 2012 and FY 2011, other intragovernmental liabilities not covered by budgetary resources include accruals for Federal Employee Compensation Act (FECA) of \$167 million and \$167 million, contract disputes claims payable to Treasury's Judgment Fund of \$23 million and \$20 million, unemployment compensation of \$25 million and \$24 million, and custodial of \$3 million and \$5 million, respectively. In FY 2011, deposit funds and clearing accounts was \$41 million.

In FY 2012 and FY 2011, other liabilities with the public not covered by budgetary resources include, Tobacco Transition Payment Program of \$1,906 million and \$2,857 million, future funded indemnity costs of \$18,193 million and \$9,284 million, unfunded leave of \$615 million and \$640 million, Payments to States \$346 million and \$357 million, contingent liabilities of \$74 million and \$1,162 million, and estimated program delivery costs to reinsurer of \$92 million and \$54 million, respectively. In FY 2012, Black Farmer Discrimination Lawsuit, also known as Pigford II was \$50 million, and unapplied collections were \$16 million. In FY 2011, underwriting gain on crop insurance was \$1,007 million and deposit funds and clearing accounts was \$16 million.

	FY 2012	FY 2011
Intragovernmental:		
Other	\$ 218	\$ 257
Subtotal Intragovernmental	218	257
With the Public:		
Accounts Payable	-	2
Federal employee and veterans' benefits	944	904
Environmental and disposal liabilities	8	8
Other	21,291	15,376
Subtotal With the Public	22,243	16,290
Total liabilities not covered by budgetary resources	22,461	16,547
Total liabilities covered by budgetary resources	130,673	119,705
Total Liabilities	\$ 153,134	\$ 136,252

Note 15. Other Liabilities

In FY 2012, other liabilities with the public include estimated losses on crop insurance claims of \$17,068 million, estimated underwriting gains on crop insurance of \$1,666 million, crop insurance premium subsidy deficiency reserve of \$1,126 million, *Pigford II* of \$1,200 million, Payments to States of \$346 million, estimated program delivery cost to reinsurer of \$92 million, credit reform programs of \$18 million, unapplied collections of \$16 million, loans paid in advance for multi-family housing of \$12 million, and purchaser road credits of \$1 million.

In FY 2011, other liabilities with the public include estimated losses on crop insurance claims of \$8,034 million, estimated underwriting gains on crop insurance of \$1,007 million, crop insurance premium subsidy deficiency reserve of \$1,250 million, Payments to States of \$357 million, Brazilian Cotton Industry of \$146 million, estimated program delivery cost to reinsurer of \$54 million, credit reform programs of \$14 million, loans paid in advance for multi-family housing of \$11 million, and purchaser road credits of \$1 million.

Note 25. Permanent Indefinite Appropriations

USDA has permanent indefinite appropriations available to fund 1) subsidy costs incurred under credit reform programs, 2) certain costs of the crop insurance program, 3) certain commodity program costs and 4) certain costs associated with FS programs.

The permanent indefinite appropriations for credit reform are mainly available to finance any disbursements incurred under the liquidating accounts. These appropriations become available pursuant to standing provisions of law without further action by Congress after transmittal of the Budget for the year involved. They are treated as permanent the first year they become available, as well as in succeeding years. However, they are not stated as specific amounts but are determined by specified variable factors, such as cash needs for liquidating accounts, and information about the actual performance of a cohort or estimated changes in future cash flows of the cohort in the program accounts.

The permanent indefinite appropriation for the crop insurance program is used to cover premium subsidy, delivery expenses, losses in excess of premiums and research and delivery costs.

The permanent indefinite appropriation for commodity program costs is used to encourage the exportation of agricultural commodities and products, to encourage domestic consumption of agricultural products by diverting them, and to reestablish farmers' purchasing power by making payments in connection with the normal production of any agricultural commodity for domestic consumption.

The permanent indefinite appropriation for FS programs is used to fund Recreation Fee Collection Costs, Brush Disposal, License programs, Smokey Bear and Woodsy Owl, Restoration of Forest Lands and Improvements, Roads and Trails for States, National Forest Fund, Timber Roads, Purchaser Elections, Timber Salvage Sales and Operations, and Maintenance of Quarters. Each of these permanent indefinite appropriations is funded by receipts made available by law, and is available until expended.

RELATED DISCLOSURES IN CFR

Excerpt from 2012 CFR Note 18: Insurance and Guarantee Program Liabilities

Note 18. Insurance and Guarantee Program Liabilities

Insurance and Guarantee Program Liabilities as of September 30, 2012, and 2011

(In billions of dollars)	2012	2011
Insurance and Guarantee Program Liabilities:		
Pension Benefit Guaranty Corporation - Benefit Pension Plans	105.6	93.0
Federal Deposit Insurance Corporation Funds	26.5	47.4
All other insurance and guarantee programs	24.3	21.3
Total insurance and guarantee program liabilities	156.4	161.7

PBGC insures pension benefits for participants in covered defined benefit pension plans. As a wholly-owned corporation of the U.S. Government, PBGC's financial activity and balances are included in the consolidated financial statements of the U.S. Government. However, under current law, PBGC's liabilities may be paid only from PBGC's assets and not from the General Fund of the Treasury or assets of the Government in general. As of September 30, 2012, and 2011, PBGC had total liabilities of \$119.2 billion and \$106.7 billion, and its total liabilities exceeded its total assets by \$34.4 billion and \$26.0 billion, respectively. In addition, as discussed in Note 22—Contingencies, PBGC reported reasonably possible contingent losses of about \$321.8 billion and \$250.2 billion as of September 30, 2012, and 2011, respectively. Of the total FDIC amount as of September 30, 2012, and 2011, \$3.6 billion and \$7.2 billion, respectively, represents the recorded contingent liability and loss provision for institutions insured by the Deposit Insurance Fund that are likely to fail. In addition, \$21.2 billion and \$31.5 billion pertain to liabilities due to resolutions of failed or failing institutions and to pending depositor claims as of September 30, 2012, and 2011 respectively. Another \$1.7 billion and \$8.2 billion as of September 30, 2012, and 2011 respectively, pertains to the Temporary Liquidity Guarantee Program, which guarantees certain newly issued debt and certain noninterest-bearing transaction accounts in an effort to counter the system-wide crisis in the nation's financial sector. The remaining amounts represent contingent liabilities for litigation.

Of the \$24.3 billion and \$21.3 billion under all other insurance and guarantee programs as of September 30, 2012, and 2011, respectively, \$20.0 billion and \$10.3 billion, respectively, pertain to the USDA's Federal Crop Insurance Program. The increase in the estimated indemnities is due to the most severe drought in the farm belt since 1988. The Federal Crop Insurance Program is administered by the Federal Crop Insurance Corporation, whose mission is to provide an actuarially sound risk management program to reduce agricultural producers' economic losses due to natural disasters. Also, \$3.4 billion and \$7.4 billion relates to the National Credit Union Administration's Temporary Corporate Credit Union Stabilization Fund as of September 30, 2012, and 2011, respectively. This Program guarantees the timely payment of principal and interest on certain unsecured debt of participating credit unions.

TERRORISM RISK INSURANCE

U.S. DEPARTMENT OF THE TREASURY

<http://www.treasury.gov/resource-center/fin-mkts/Pages/program.aspx>

BRIEF SUMMARY OF PROGRAM

Congress enacted the Terrorism Risk Insurance Act (TRIA) in 2002 to increase the availability of terrorism risk insurance to at-risk American businesses by guaranteeing that the government would share some of the losses with private insurers should a terrorist attack occur. This was in response to the attacks of 9/11 - when private reinsurers exited the U.S. market and commercial insurance insurers began excluding terrorism coverage from policies provided to businesses.

On December 26, 2007, the President signed into law the Terrorism Risk Insurance Program Reauthorization Act of 2007 which extends the Terrorism Risk Insurance Act through December 31, 2014. The law extends the temporary federal Program that provides for a transparent system of shared public and private compensation for insured losses resulting from acts of terrorism. The Treasury Department implements the Program.¹

Recently Rep. Bennie G. Thompson (D-MS), Ranking Member of the Committee on Homeland Security, introduced the "Fostering Resilience to Terrorism Act of 2013" to extend and enhance the Terrorism Risk Insurance Program for 10 years - which is set to expire next year.²

Insurers' Retention of Losses under TRIA

The Program involves shared public and private compensation for privately-insured commercial property and casualty losses resulting from acts of terrorism. The private sector insurers' share of the losses has several components: (1) the insurer deductible; (2) the insurer share of insured losses above the deductible; (3) a floor loss threshold before the Federal Government shares in the losses; (4) a ceiling loss threshold through an annual cap on aggregate insured losses paid under the Program; and (5) an insurance marketplace aggregate retention which establishes a minimum amount of aggregate insured losses that will be borne by private industry, both commercial insurance policyholders and insurance companies.

Under the Program, insured losses above the insurer deductible amount are shared between the insurance company and the Federal Government. As TRIA was originally enacted, the insurer share was fixed at 10 percent of the insured losses, and the Federal Government's share equal to 90 percent of the losses above the deductible. When the

¹ Source: U.S. Department of Treasury, Resource Center- Terrorism Risk Insurance Program <http://www.treasury.gov/resource-center/fin-mkts/Pages/program.aspx> last accessed on May 22, 2013.

² Source: Article *Thompson Introduces Legislation to Extend Terrorism Risk Insurance Program* internet <http://insurancenewsnet.com/article.aspx?id=381093&type=financial> last accessed on May 22, 2013.

Program was extended in 2005, the insurer share was raised to 15 percent in 2007, reducing the Federal share slightly to 85 percent. Under current law, the public and private shares remain at these levels through 2014.

TRIA mandates certain limitations on Federal payments under the Program. The Terrorism Risk Insurance Extension Act of 2005 amended TRIA so the Federal Government would not share in the losses of relatively small-scale acts of terrorism. TRIA prohibits the Program from making Federal payments until the aggregate industry insured losses resulting from a certified act of terrorism exceed the "Program Trigger," which was first set at \$50 million in 2006 and increased to \$100 million in 2007, where it is set to remain for the duration of the Program. Acts of terrorism above \$5 million in aggregate insured losses remain eligible for certification under the Program, and any certification will trigger coverage under terrorism risk insurance policies. However, the Federal Government does not share in any losses until the Program Trigger is reached. The Program Trigger, therefore, serves as a floor on Federal payments under the Program. Below that floor, the private sector retains all of the losses.³ (Additional detail regarding different scenarios and market can be found in the report referenced in the footnote.)

"The Boston Marathon bombings last month serve as a stark reminder that terrorism and mass violence remain both a homeland security and economic threat. If TRIA is allowed to expire next year, there may be fewer insurers offering terrorism insurance and prices potentially could increase. By extending this program for 10 years, we will ensure much-needed stability and predictability for the business community." Congressman Thompson statement introducing bill to extend TRIA⁴

In calling for the reauthorization of TRIA, Mr. Lundberg stated, "While private insurance capacity apparently has grown slightly in the past decade, these years have also taught us that a continuing federal role in this unique risk remains vital. The terrorism peril is simply too intrinsically linked to government policy and intelligence to be solely handled by the private sector alone."⁵

³ Source: <http://www.treasury.gov/resource-center/fin-mkts/Pages/resources.aspx> Report of the President's Working Group on Financial Markets Market Condition for Terrorism Risk Insurance

⁴ Ibid

⁵ Source: September 11, 2012: Coalition to Insure Against Terrorism (CIAT) testifies before Insurance, Housing and Community Opportunity Subcommittee of the House Financial Services Committee. Rolf Lundberg, Senior Vice President, Congressional and Public Affairs, U.S. Chamber of Commerce, testified on behalf of the Coalition to Insure Against Terrorism at a hearing entitled "TRIA at Ten Years: The Future of the Terrorism Risk Insurance Program." The hearing was called to assess conditions in the insurance market and the private sector's capacity to offer insurance and reinsurance coverage for losses resulting from acts of international and domestic terrorism.

RELATED LEGISLATION AND U.S. CODE (U.S.C.)

1. Terrorism Risk Insurance Act of 2002 (Pub. L. 107–297, 116 Stat. 2322)
 2. Terrorism Risk Insurance Extension Act of 2005
 3. Terrorism Risk Insurance Program Reauthorization Act of 2007
-

SOURCES OF FINANCING

The Department of the Treasury Terrorism Insurance Program Corporation receives annual appropriations and is listed in the Budget. Under the Program, insured losses above the insurer deductible amount are shared between the insurance company and the Federal Government.

SOURCE OF GAAP

Dept. of the Treasury primarily applies generally accepted accounting principles (GAAP) issued by the FASAB.

SIGNIFICANT FINANCIAL STATEMENT ELEMENTS

No claims under TRIA in 2011 or 2012.

RELEVANT GAO REPORTS (*LAST 5 YEARS*)

None

DISCLOSURES IN AFR

Excerpts from FY 2012 Dept. of Treasury Agency Financial Report⁶

Footnote 1X: Summary of Significant Accounting Policies

X. CREDIT, MARKET AND FOREIGN CURRENCY RISK

Credit risk is the potential, no matter how remote, for financial loss from a failure of a borrower or counterparty to perform in accordance with underlying contractual obligations. The 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 10). The following programs of the Department entail credit risk: monetary assets held; committed but undisbursed direct loans; liquidity commitment to the GSEs; GSE obligations obtained under the HFA Initiative (the NIBP and TCLP); investments, loans, and other credit programs of the TARP; programs including the CDFI Fund, SBLF, and certain portions of the Department's participation in the IMF; and the Terrorism Risk Insurance Program.

Except for the Terrorism Risk Insurance Program, the Department's activities focus on the underlying problems in the credit markets, and the ongoing instability in those markets exposes the Department to potential costs and losses. The extent of the risk assumed by the 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 7, 8, and 11). Given the history of the 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 Department's expectation of credit losses is nominal.

For Emergency Economic Stabilization Act (EESA) programs, the statute requires that budgetary costs of the troubled assets and guarantees of troubled assets be calculated by adjusting the discount rate for market risks. Within the TARP programs, the Department has invested in many assets that would traditionally be held by private investors and their valuation would inherently include market risk. Accordingly, for all TARP direct loans, equity investments, and other credit programs, the Department calculates a Market Risk Adjusted Discount Rate (MRADR). Therefore, the Department's 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 being valued. The inclusion of the MRADR is the mechanism for deriving a fair value of the assets. As directed by Congress, a MRADR is also used in the credit reform model for certain portions of the Department's participation in the IMF.

The Department faces certain risks and uncertainties as a result of holding securities denominated in foreign currency. The price of holdings of such securities may widely fluctuate as a result of volatility in foreign currency markets and changes in real and perceived credit of the Department's counterparties.

⁶ Source: Treasury website -- <http://www.treasury.gov/about/organizational-structure/ig/Audit%20Reports%20and%20Testimonies/OIG13012.pdf> last accessed on June 6, 2013.

Footnote 28: Commitments and Contingencies

Terrorism Risk Insurance Program

The *Terrorism Risk Insurance Act* (TRIA), signed into law in November 2002, was enacted to address market disruptions resulting from terrorist attacks on September 11, 2001. TRIA helps to ensure available and affordable commercial property and casualty insurance for terrorism risk, and simultaneously allows private markets to stabilize. The authority to pay claims under the Terrorism Risk Insurance Program (TRIA Program) is activated upon the certification of an “act of terrorism” by the Secretary 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. TRIA also gives the Department authority to recoup federal payments made under the TRIA Program through policyholder surcharges under certain circumstances, and contains provisions designed to manage litigation arising from or relating to a certified act of terrorism. There were no claims under TRIA as of September 30, 2012 or 2011.

RELATED DISCLOSURES IN CFR

Excerpt from 2012 CFR Note 1Y: Summary of Significant Accounting Policies

Y. 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 Government takes on 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.

The Government also takes on credit risk related to committed but undisbursed direct loans, liquidity commitment to GSEs, the MBS portfolio, investments, loans, and asset guarantees of the TARP, guarantee of money market funds, and the 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 Government to potential unknown costs and losses. The extent of the risk assumed is described in more detail in the notes to the financial statements, and where applicable, is factored into credit reform models and reflected in fair value measurements.

Terrorism Risk Insurance Program

The U. S. Government has entered into agreements that could potentially require claims on Government resources in the future. For example, The Terrorism Risk Insurance Act of 2002 (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. 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 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 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 Government for insured losses above a designated deductible amount. Insured losses above this amount will be shared between insurance companies and the Government. The Act also gives Treasury 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. There were no claims under TRIA as of September 30, 2012, or September 30, 2011.

AVIATION INSURANCE PROGRAM

MARINE WAR RISK INSURANCE PROGRAM

DEPARTMENT OF TRANSPORTATION

WWW.DOT.GOV

BRIEF SUMMARY OF PROGRAM

The Secretary of Transportation under 49 U.S.C. § 44301, et seq., may provide insurance and reinsurance against loss or damage arising out of any risk from the operation of an American aircraft or foreign-flag aircraft. Insurance can be provided on the condition (1) the President determines it is necessary for the continuation of U.S. commercial air service in the interest of air commerce, national defense, or foreign policy, and (2) the Secretary determines insurance is not readily available from insurance companies on reasonable terms. Program authority is effective until December 31, 2013.

The Federal Aviation Administration (FAA) Aviation Insurance Program provides products that address the insurance needs of the U.S. domestic air transportation industry not adequately met by the commercial insurance market.

The FAA currently is providing war risk insurance under two separate programs; 1) Premium War Risk Insurance, and 2) Non Premium War Risk Insurance.¹ After the terrorist events of September 11, 2001, the FAA began issuing premium third party liability war risk insurance to U.S. air carriers. The Homeland Security Act of 2002 (HSA), Public Law 112-7 and subsequent legislation mandated the expansion of war risk insurance coverage to include hull loss and passenger liability and required continued provision of this insurance.

The Secretary of Transportation may provide insurance without premium, if the Secretary of Defense or the head of a Department, Agency, or instrumentality of the U.S. Government agrees to indemnify the Secretary of Transportation against all losses covered by the insurance. FAA insurance is available to CRAF participants and other air carriers flying under U.S. Government contracts.

Insurance may be provided for a period of not more than one year. Presidential approval of the standing interagency indemnification agreement constitutes the necessary Presidential determination to issue non-premium insurance for additional periods of not more than one year.

¹ More information on the program is available online at http://www.faa.gov/about/office_org/headquarters_offices/apl/aviation_insurance/; last accessed June 3, 2013.

The Department of Transportation's (DOT) authority to provide aviation war risk insurance expires on December 31, 2013. With the goal of building private capacity to manage aviation war risk, the Administration proposes to transform the program into a co-insurance arrangement in which DOT and a private insurer would jointly underwrite a common policy. In the case of a claim, DOT would pay an established fraction of the losses, and the private partner would pay the remainder. The Federal share would be slightly reduced each year as private capacity expands. The proposal would extend the existing program through 2014, during which time DOT would propose changes to its underlying statutory authority and work with the private insurance industry to develop co-insurance policies. The Budget proposes that a co-insurance arrangement would begin to reduce the government's share of any losses, starting in 2015.²

The Maritime provide war risk insurance whenever it appears to the Secretary of Transportation that adequate insurance for waterborne commerce cannot be obtained on reasonable terms and conditions from licensed insurance companies in the United States.

Hull insurance usually does not cover the risk of a vessel sailing into a war zone, but such insurance can be purchased separately as "war risk insurance." War risk insurance is special coverage on cargo in transcontinental ships that protects against the risk of confiscation by a government in wartime. War risk insurance coverage protects, at an additional premium, against the danger of loss in a war zone. The war risk zones are established by the London-based Lloyd's Market Association's Joint War Committee (JWC), which has recently included the Gulf of Aden as a war risk area due to piracy.²⁰ (About a decade ago, the Malacca Straits were similarly designated a war risk area due to piracy.) The JWC represents the interests of underwriters writing war and related risks within the London ocean marine insurance market.³

The U.S. Department of Transportation's Maritime Administration's (MARAD) marine war risk insurance program under Title XII, Merchant Marine Act, 1936, as amended, includes a provision of vessel war risk insurance, as follows.⁴

The Secretary (of Transportation), with the approval of the President, and after such consultation with interested agencies of the Government as the President may require, may provide insurance and reinsurance against loss or damage by war risks in the manner and to the extent provided in this subchapter, whenever it appears to the Secretary that such insurance adequate for the needs of the water-borne commerce of the United States cannot be obtained on reasonable terms and conditions from companies authorized to do an insurance business in a State of the United States.⁵

During times of national emergency, at the request of the Department of Defense, the MARAD underwrites marine insurance risk insurance for DOD-chartered vessels during national emergency. Commercial shippers can obtain war risk insurance coverage from MARAD.

² Source: The Analytical Perspectives Volume of the Fiscal Year 2014 President's Budget of the United States Government -- http://www.whitehouse.gov/omb/budget/Analytical_Perspectives

³ Source: CRS Report R40081 Ocean Piracy and Its Impact on Insurance.

⁴ Merchant Marine Act, 1936, 46 U.S.C. App. 1282, 64 Stat. 773.

⁵ The White House, "Presidential Memo on Marine War Risk Insurance Coverage," December 12, 2001, located at <http://www.whitehouse.gov/news/releases/2001/12/print/20011214-9.html>.

Federal policy (Title XII of the Merchant Marine Act of 1936, as amended) authorizes the federal government to administer a maritime war risk insurance program that insures or reinsures, as a last resort, ocean-going commerce should private ocean marine insurance markets prove insufficient. Available statistics suggest that industry resources are adequate, given the property and casualty insurance industry surplus and the relatively low cost of insurance premiums. As a result, despite the increased activity of pirates, some may contend that Congress does not need to amend the existing federal insurance statutory construct. Others, however, may urge increased levels of oversight and investigation into the situation in an effort to ensure that international commerce remains stabilized, particularly at a time of global economic crisis.⁶

NEW CONSIDERATIONS—PIRACY

Standard hull and machinery insurance policies are not specifically designed to address security-related risks such as piracy. War Risk insurance provides this special coverage for ships exposed to piracy risks on a per transit basis. Federal law (Title XII of the Merchant Marine Act of 1936, as amended) authorizes the federal government to administer a maritime war risk insurance program that insures or reinsures, as a last resort, ocean-going commerce in high-risk areas should private ocean marine insurance markets prove insufficient. Available statistics suggest that the insurance industry's financial resources are adequate, given policyholder surplus levels (an insurance term that refers to the claims-paying capacity or capital available to the insurer), and there is ample supply of coverage for ocean-going vessels. Therefore, some may contend that Congress does not need to amend the existing federal insurance statutory construct. Some have urged the arming of ship crews or bringing onboard armed security as a risk mitigation option. Despite the persistence of pirate attacks, though, many ship owners and their underwriters are reluctant to employ armed security onboard their vessels. The use of armed security may create third-party liabilities if security officers harm innocent mariners or vessels.⁷

RELATED LEGISLATION AND U.S. CODE (U.S.C.)

1. 49 U.S.C. § 44301
2. Homeland Security Act of 2002 (HSA)
3. Public Law 112-7
4. Merchant Marine Act of 1936
5. Title XII, as amended

SOURCES OF FINANCING

DOT Aviation receives Congressional appropriations and is listed in the Budget. The program offers both premium and non-premium insurance.

⁶ Source: CRS Report R40081 Ocean Piracy and Its Impact on Insurance.

⁷ Source: CRS Report, R40528 Piracy off the Horn of Africa

SOURCE OF GAAP

DOT primarily applies generally accepted accounting principles (GAAP) issued by the FASAB.

SIGNIFICANT FINANCIAL STATEMENT ELEMENTS

Commitments and Contingencies

RELEVANT GAO REPORTS (*LAST 5 YEARS*)

No recent GAO reports identified.

RELEVANT DISCLOSURES IN AFR

Excerpt from FY 2012 Dept. of Transportation Agency Financial Report⁸

⁸ Source: DOT website -- <http://www.dot.gov/mission/budget/fy-2012-agency-financial-report>
(footnote continued)

NOTE 17. COMMITMENTS AND CONTINGENCIES

AVIATION INSURANCE PROGRAM

FAA is authorized to issue hull and liability insurance under the Aviation Insurance Program for air carrier operations for which commercial insurance is not available on reasonable terms and when continuation of U.S. flag commercial air service is necessary in the interest of air commerce, national security, and the foreign policy of the United States. FAA may issue non-premium insurance and premium insurance for which a risk-based premium is charged to the air carrier, to the extent practical.

During FY 2012, FAA provided premium war-risk insurance to 53 airlines. For these airlines, combined hull and liability per occurrence coverage limits range from \$100 million to \$4 billion. FAA also provided non-premium war-risk insurance to 37 carriers with 2,387 aircraft for Department of Defense charter operations for Central Command.

As of September 30, 2012, there are pending aviation insurance claims in the amount of \$10 million. There is approximately \$1.8 billion available in the Aviation Insurance Revolving Fund to pay claims to carriers covered by premium insurance. If premium insurance claims should exceed that amount, additional funding could be appropriated from the General Fund. The Department of Defense and State Department have agreed to pay claims to the carriers covered by non-premium insurance.

MARINE WAR RISK INSURANCE PROGRAM

MARAD is authorized to issue hull and liability insurance under the Marine War Risk Insurance Program for vessel operations for which commercial insurance is not available on reasonable terms and conditions, when the vessel is considered to be in the interest of national defense or national economy of the United States. MARAD may issue (1) premium based insurance for which a risk based premium is charged and (2) non-premium insurance for vessels under charter operations for the Military Sealift Command.

During FY 2012, MARAD wrote non-premium war risk insurance with a total coverage of \$448.5 million for six companies on six vessels and the coverage ranges from \$64 million to \$83 million to cover hull liability and vessel's crew. During FY 2011, MARAD wrote non-premium war risk insurance with a total coverage of \$448.5 million for six companies on six vessels and the coverage ranges from \$52 million to \$84.5 million to cover hull

last accessed on June 6, 2013.

liability and vessel's crew. The Department of Defense has fully indemnified MARAD for any losses arising out of the non-premium insurance. There have been no losses and no claims are outstanding for this non-premium insurance. There is approximately \$47 million in the Marine War Risk Insurance fund to reimburse operators that may be covered by premium insurance in future periods. MARAD has not issued premium War Risk Insurance in approximately 20 years. MARAD would have to request Presidential authority to write any premium insurance, and no such request is pending at this time.

Excerpt from FY 2012 FAA Performance and Accountability Report⁹

U. S. Department of Transportation FEDERAL AVIATION ADMINISTRATION SCHEDULE OF BUDGETARY RESOURCES BY MAJOR FUND TYPE As of September 30, 2012 Unaudited								
	Trust Fund Grants-in-Aid to Airports	Trust Fund Facilities & Equipment	Trust Fund Research, Eng. & Development	Aviation Insurance Revolving	Franchise Fund	Operations	Other Funds	Combined Total
BUDGETARY RESOURCES								
Unobligated balance brought forward, transfers and other	\$ 12,531	\$ 1,479,618	\$ 82,707	\$ 1,671,936	\$ 127,892	\$ 162,187	\$ 19,640	\$ 3,556,211
Recoveries of prior year obligations	145,952	122,692	6,676	53	18,660	112,754	6,913	413,890
Other changes in unobligated balance	—	(70,177)	(1,966)	—	—	(60,234)	15,536	(116,841)
Appropriations	—	2,730,732	167,572	—	—	4,592,701	5,061,365	12,552,370
Contract Authority	3,360,000	—	—	—	—	—	—	3,360,000
Spending authority from offsetting collections	230	66,548	6,154	161,763	451,454	5,293,517	213	5,969,679
Total Budgetary Resources	\$ 3,508,713	\$ 4,319,413	\$ 261,143	\$ 1,833,752	\$ 597,696	\$ 10,100,925	\$ 5,103,667	\$ 25,725,509
STATUS OF BUDGETARY RESOURCES								
Obligations incurred	\$ 3,494,492	\$ 3,053,596	\$ 180,374	\$ (58.7)	\$ 488,819	\$ 9,928,070	\$ 5,061,067	\$ 22,205,831
Apportioned	2,473	1,172,189	49,167	43,634	98,125	65,325	1	1,430,914
Unapportioned	11,748	93,628	31,602	1,790,705	10,952	107,530	42,599	2,088,764
Total Status of Budgetary Resources	\$ 3,508,713	\$ 4,319,413	\$ 261,143	\$ 1,833,752	\$ 597,696	\$ 10,100,925	\$ 5,103,667	\$ 25,725,509
CHANGE IN OBLIGATED BALANCES								
Obligated balance, net, beginning of period	\$ 5,223,111	\$ 1,905,142	\$ 152,462	\$ 5,546	\$ 129,561	\$ 1,491,126	\$ 48,089	\$ 8,955,069
Obligations incurred	3,494,492	3,053,596	180,374	(58.7)	488,819	9,928,070	5,061,067	22,205,831
Gross Outlays	(3,143,869)	(2,968,584)	(187,866)	(3,159)	(443,427)	(9,922,552)	(5,096,844)	(21,766,301)
Recoveries of prior year obligations	(145,952)	(122,692)	(6,676)	(53)	(18,660)	(112,754)	(6,913)	(413,890)
Change in uncollected customer payments from Federal sources	—	(6,166)	(1,890)	—	6,340	(40,870)	(66)	(42,652)
Obligated balance, net, end of period	\$ 5,427,782	\$ 1,861,296	\$ 136,424	\$ 1,747	\$ 162,443	\$ 1,343,022	\$ 5,333	\$ 8,938,047
BUDGET AUTHORITY AND OUTLAYS								
Budget authority, gross	\$ 3,360,230	\$ 2,787,280	\$ 173,726	\$ 161,763	\$ 451,454	\$ 9,886,218	\$ 5,061,578	\$ 21,872,249
Actual offsetting collections	(230)	(60,362)	(4,264)	(161,763)	(457,794)	(5,252,647)	(147)	(5,927,227)
Change in uncollected customer payments from Federal sources	—	(6,166)	(1,890)	—	6,340	(40,870)	(66)	(42,652)
Budget authority, net	\$ 3,360,000	\$ 2,730,732	\$ 167,572	\$ —	\$ —	\$ 4,592,701	\$ 5,061,365	\$ 15,902,370
NET OUTLAYS								
Gross outlays	\$ 3,143,869	\$ 2,968,584	\$ 187,866	\$ 3,159	\$ 443,427	\$ 9,922,552	\$ 5,096,844	\$ 21,766,301
Offsetting collections	(230)	(60,362)	(4,264)	(161,763)	(457,794)	(5,252,647)	(147)	(5,927,227)
Distributed offsetting receipts	—	—	—	—	—	—	(11,560)	(11,560)
Net Outlays	\$ 3,143,639	\$ 2,918,222	\$ 183,602	\$ (158,604)	\$ (14,367)	\$ 4,669,905	\$ 5,085,137	\$ 15,827,514

⁹ Source: FAA website -- http://www.faa.gov/about/plans_reports/#performance
last accessed on June 6, 2013.

RELATED DISCLOSURES IN CFR

None

OVERSEAS PRIVATE INVESTMENT

OVERSEAS PRIVATE INVESTMENT CORPORATION (OPIC)

WWW.OPIC.GOV

BRIEF SUMMARY OF PROGRAM

OPIC mobilizes private capital to help solve critical development challenges and in doing so, advances U.S. foreign policy. Because OPIC works with the U.S. private sector, it helps U.S. businesses gain footholds in emerging markets, catalyzing revenues, jobs and growth opportunities both at home and abroad. OPIC achieves its mission by providing investors with financing, guarantees, political risk insurance, and support for private equity investment funds.

Established as an agency of the U.S. Government in 1971, OPIC operates on a self-sustaining basis at no net cost to American taxpayers. OPIC services are available for new and expanding business enterprises in more than 150 countries worldwide. To date, OPIC has supported more than \$200 billion of investment in over 4,000 projects, generated an estimated \$75 billion in U.S. exports and supported more than 277,000 American jobs.¹

Political Risk Insurance

Investing in emerging markets can be unpredictable, even for the most sophisticated investors. While developing markets can offer great opportunity, they can also present a variety of political risks beyond an investor's control. Among them:

- War, civil strife, coups and other acts of politically-motivated violence including terrorism
- Expropriation, including abrogation, repudiation and/or impairment of contract and other improper host government interference
- Restrictions on the conversion and transfer of local-currency earnings

OPIC offers several types of political risk coverage: Currency Inconvertibility, Expropriation, Political Violence and more targeted specialty products.

OPIC political risk insurance is available to U.S. citizens, U.S. firms, or to the foreign subsidiaries of U.S. firms as long as the foreign subsidiary is at least 95%-owned by a U.S. citizen. According to OPIC, such insurance is available for investments in new ventures or in expansions of existing enterprises, and can cover equity investments, parent company and third party loans and loan guarantees, technical assistance agreements, cross-border leases, assigned inventory or equipment, and other forms of

¹ More information on the OPIC is available online at <http://www.opic.gov/> ; last accessed May 29, 2013.

investment. This insurance covers three broad areas of political risk: currency inconvertibility, expropriation, and political violence. Currency inconvertibility coverage compensates investors if new currency restrictions are imposed which prevent the conversion and transfer of remittances from insured investments, but it does not protect against currency devaluation.

Expropriation coverage protects U.S. firms against the nationalization, confiscation, or expropriation of an enterprise, including actions by foreign governments that deprive an investor of fundamental rights or financial interests in a project for a period of at least six months. This coverage excludes losses that may arise from lawful regulatory or revenue actions by a foreign government and actions instigated or provoked by the investor or foreign firm.

Political violence coverage compensates U.S. citizens and firms for property and income losses directly caused by various kinds of violence, including declared or undeclared wars, hostile actions by national or international forces, civil war, revolution, insurrection, and civil strife (including politically motivated terrorism and sabotage). Income loss insurance protects the investor's share of income from losses that result from damage to the insured property caused by political violence. Assets coverage compensates U.S. citizens and firms for losses of or damage to tangible property caused by political violence. OPIC also has a number of special programs that protect U.S. banks from political violence. This type of insurance reduces risks for banks and other institutional investors, which allows them to play a more active role in financing projects in developing countries. Specialized types of insurance coverage also is available for U.S. investors involved with certain contracting, exporting, licensing, or leasing transactions that are undertaken in a developing country.²

Coverage & Extent of Coverage

Coverage elections for most equity and shareholder debt investments are based on a coverage ceiling and an active amount. The coverage ceiling represents the maximum insurance available for the insured investment and future earnings under an insurance contract. Premiums are calculated based on the active amount, which represents the insurance actually in force during any contract period.

The active amount under all coverages must equal at least the book value of the insured investment unless a lower coverage ceiling is elected. There is no charge for the difference between the coverage ceiling and the active amount.

For most other investment types, premiums are computed based on a maximum insured amount (MIA), a current insured amount (CIA) and a standby amount. The MIA represents the maximum insurance available for the insured investment under an insurance contract. The CIA represents the insurance actually in force during any contract period. The difference between the MIA and CIA is the standby amount. Separate premiums are charged for CIA and standby amounts. For loans, premiums are charged on the "covered amount," the amount of disbursed principal plus accrued

² Source: CRS Report for Congress, 98-567 The Overseas Private Investment Corporation: Background and Legislative Issues

interest less principal paid to date, and a standby fee is charged for undisbursed principal.

OPIC insurance contracts generally require that premiums be paid annually in advance. Insurance policies for equity coverage are available for up to 20-year terms. For loans, leases and transactions covered by the contractors and exporters insurance product, the term is generally equal to the duration of the underlying contract or agreement.

OPIC can insure up to 90 percent of an eligible investment. OPIC's statute generally requires that the investor bear at least 10 percent of the risk of loss. However, loans and capital leases from financial institutions to unrelated third parties may be insured for 100 percent of principal and interest.

For equity investments, OPIC typically issues insurance commitments equal to 270 percent of the initial investment — 90 percent representing the original investment and 180 percent to cover future earnings. Coverage amounts may be limited for investments in countries where OPIC has a high portfolio concentration.

“OPIC’s insurance – combined with our financing options -- allows U.S. businesses to take advantage of commercially attractive opportunities in emerging markets, mitigating risk and helping them compete in a global marketplace. OPIC insurance provides innovative, comprehensive, and cost-effective risk-mitigation products to cover losses to tangible assets, investment value, and earnings that result from political perils.” OPIC’s Website www.opic.gov

RELATED LEGISLATION AND U.S. CODE (U.S.C.)

1. Foreign Assistance Act of 1961 (P.L. 87-195) as amended

SOURCES OF FINANCING

Established as an agency of the U.S. Government in 1971, OPIC operates on a self-sustaining basis at no net cost to American taxpayers. While OPIC is fully self-sustaining from its own revenues, Congress annually provides OPIC with the authority to cover its administrative expenses and credit subsidy funding from its offsetting collections, which include user fees and interest from U.S. Treasury securities. OPIC's budget is composed of noncredit and credit accounts, in conformity with the standards set out in the Federal Credit Reform Act of 1990. The noncredit portion of OPIC's budget relates to OPIC's political risk insurance program, while the credit portion is comprised of OPIC's direct and guaranteed loans. OPIC uses premium income and the interest it accrues from the assets in its noncredit account to fund the direct and indirect expenses

in its noncredit and credit accounts. OPIC has a net negative budget authority, as its offsets to budget authority have been greater than its appropriations. For more than thirty years, OPIC has regularly returned “surplus” funds to the U.S. Treasury. Strictly speaking, OPIC’s net negative budget authority is not necessarily a “surplus” for the agency. These funds represent a reserve fund against losses that OPIC may accrue through its financing and insurance programs. The surplus may reflect revenues which OPIC has earned (such as through the premiums, interest, and fees generated from OPIC’s services), but for which OPIC has not received payment yet. The surplus also may reflect expenses (such as financing, insurance, or investment commitments) that OPIC has incurred but for which OPIC has not yet disbursed payment. The transfer of these funds to the Treasury essentially is a transaction in the accounting ledger between the Treasury and OPIC, rather than a cash transfer of funds.³

SOURCE OF GAAP

OPIC primarily applies generally accepted accounting principles (GAAP) issued by the Financial Accounting Standards Board (FASB). This practice is permitted by paragraph 9 of Statement of Federal Financial Accounting Standards 34, *The Hierarchy of Generally Accepted Accounting Principles, Including the Application of Standards Issued by the Financial Accounting Standards Board*.

³ Source: CRS Report for Congress, 98-567 The Overseas Private Investment Corporation: Background and Legislative Issues

SIGNIFICANT FINANCIAL STATEMENT ELEMENTS

Excerpt from FY 2012 OPIC Annual Report⁴

BALANCE SHEETS

Overseas Private Investment Corporation—Years ended September 30, 2012 and 2011 (\$ in thousands)

Assets	2012	2011
Fund Balance with U.S. Treasury (notes 2 and 4)	\$1,076,559	\$ 707,257
U.S. Treasury securities, at amortized cost plus related receivables (notes 2 and 7)	5,320,325	5,188,527
Direct loans outstanding, net (notes 2 and 10)	1,363,216	1,326,292
Accounts receivable resulting from investment guaranties, net (notes 2 and 11)	42,394	59,602
Assets acquired in insurance claims settlements, net (notes 2 and 11)	1,507	1,507
Guaranty receivable (notes 2 and 19)	692,000	456,130
Accrued interest and fees and other, net (notes 2 and 10)	32,843	29,481
Furniture, equipment and leasehold improvements at cost less accumulated depreciation and amortization of \$17,255 in FY2012 and \$15,742 in FY2011 (note 2)	6,223	6,649
Total assets	<u>\$8,535,067</u>	<u>\$7,775,445</u>
Liabilities, Capital, and Retained Earnings		
Liabilities:		
Reserve for political risk insurance (note 9)	\$278,000	\$275,000
Reserve for investment guaranties (notes 10)	489,320	573,331
Accounts payable and accrued expenses	5,515	4,984
Guaranty liability (notes 2 and 19)	692,000	456,130
Customer deposits and deferred income	52,196	47,465
Borrowings from U.S. Treasury, and related interest (note 6)	2,241,224	1,827,691
Unearned premiums	26,382	8,144
Deferred rent & rent incentives from lessor of \$6,413 and \$5,779 net of accumulated amortization of \$2,660 and \$2,421 in FY2012 and FY2011 (note 14)	3,753	3,358
Total liabilities	<u>3,788,390</u>	<u>3,196,103</u>
Contingent liabilities (notes 2 and 17)		
Capital and retained earnings:		
Contributed capital	50,000	50,000
Credit funding (note 5)	107,484	105,788
Interagency transfers (Note 2)	16,312	16,354
Retained earnings and reserves:		
Insurance (notes 9 and 12)	858,251	790,887
Guaranty (notes 10 and 12)	3,714,630	3,616,313
Total capital and retained earnings	<u>4,746,677</u>	<u>4,579,342</u>
Total liabilities, capital, and retained earnings	<u>\$8,535,067</u>	<u>\$7,775,445</u>

⁴ Source: OPIC website -- <http://www.opic.gov/media-connections/annual-reports> last accessed on June 6, 2013.

STATEMENTS OF INCOME

Overseas Private Investment Corporation—Years ended September 30, 2012 and 2011 (\$ in thousands)

Revenues	2012	2011
Political risk insurance premiums and fees (note 9)	\$ 15,452	\$ 14,281
Investment financing interest and fees	198,699	218,164
Interest on finance program deposits	36,124	31,059
Interest on U.S. Treasury securities	162,113	170,364
Total revenues	<u>412,388</u>	<u>433,868</u>
Expenses		
Provisions for reserves:		
Political risk insurance (notes 2 and 9)	(23,021)	(9,750)
Investment financing (notes 2, 10 and 11)	4,721	34,720
Salaries and benefits (note 15)	33,320	31,608
Rent, communications and utilities (note 14)	7,005	6,953
Contractual services	19,146	13,596
Travel	4,739	3,949
Interest on borrowings from U.S. Treasury (note 6)	90,547	80,824
Depreciation and amortization (note 2)	1,513	885
Other general and administrative expenses	1,848	1,627
Total expenses	<u>139,818</u>	<u>164,412</u>
Net income	<u>\$272,570</u>	<u>\$269,456</u>

RELEVANT GAO REPORTS (LAST 5 YEARS)

No recent or relevant reports.

DISCLOSURES IN AFR

Excerpt from FY 2012 OPIC Annual Report⁵

(2) Summary of Significant Accounting Policies

Reserves for Political Risk Insurance and Investment Guaranties:

The reserves for political risk insurance and investment guaranties provide for losses inherent in those operations using the straight-line method. These reserves are general reserves, available to absorb losses related to the total insurance and guaranties outstanding, which are off-balance-sheet commitments. The reserves are increased by provisions charged to expense and decreased for claims settlements. The provisions for political risk insurance and investment guaranties are based on management's evaluation of the adequacy of the related reserves. This evaluation encompasses consideration of past loss experience, changes in the composition and volume of the insurance and guaranties outstanding, worldwide economic and political conditions, and project-specific risk factors. Also, in the political risk insurance reserve evaluation, OPIC takes into consideration losses incurred but not yet reported.

FASB Accounting Standards Codification Topic 460 for the Guarantee Topic (FASB ASC 460):

FASB ASC 460 requires that upon issuance of a guaranty, the guarantor must disclose and recognize a liability for the fair value of the obligation it assumes under that guaranty. The initial recognition and measurement requirement of FASB ASC 460 applies only to guaranties issued or modified after December 31, 2002. OPIC's initial guarantee obligation reported, represents the fair value of the investment guaranties. This obligation is reduced over the term of the investment guarantee agreements, as OPIC is released from its obligation.

⁵ Source: OPIC website -- <http://www.opic.gov/media-connections/annual-reports> last accessed on June 6, 2013.

(9) Political Risk Insurance

Insurance revenues include the following components for the years ended September 30 (dollars in thousands):

	2012	2011
Political risk insurance premiums	\$15,452	14,281
Miscellaneous insurance income	—	—
Total insurance revenue	<u>\$15,452</u>	<u>14,281</u>

OPIC's capital, allowance, retained earnings, and reserves available for insurance totaled \$1.1 billion at both September 30, 2012 and 2011. Charges against retained earnings could arise from (A) outstanding political risk insurance contracts, (B) pending claims under insurance contracts, and guaranties issued in settlement of claims arising under insurance contracts.

single highest coverage amount. Claim payments are limited by the value of the investment and the amount of current coverage in force at the time of the loss and may be reduced by the insured's recoveries from other sources. In addition, in certain contracts, OPIC's requirement to pay up to the single highest coverage amount is further reduced by stop-loss and risk-sharing agreements. Finally, losses on insurance claims may be reduced by recoveries by OPIC as subrogee of the insured's claim against the host government. Payments made under insurance contracts that result in recoverable assets are reported as assets acquired in insurance settlements.

OPIC's Maximum Contingent Liability at September 30, 2012 and 2011 was \$3.1 billion and \$2.6 billion, respectively. This amount is OPIC's estimate of maximum exposure to insurance claims, which includes standby coverage for which OPIC is committed but not currently at risk. A more realistic measure of OPIC's actual exposure to insurance claims is the sum of each single highest "current" coverage for all contracts in force, or Current Exposure to Claims (CEC). OPIC's CEC at September 30, 2012 and 2011 was \$2.4 billion and \$1.7 billion, respectively.

(a) Political Risk Insurance

OPIC insures investments for up to 20 years against three different risks: inconvertibility of currency, expropriation, and political violence. Insurance coverage against inconvertibility protects the investor from increased restrictions on the investor's ability to convert local currency into U.S. dollars. Inconvertibility insurance does not protect against devaluation of a country's currency.

Expropriation coverage provides compensation for losses due to confiscation, nationalization, or other governmental actions that deprive investors of their fundamental rights in the investment.

Insurance against political violence insures investors against losses caused by politically motivated acts of violence (war, revolution, insurrection, or civil strife, including terrorism and sabotage).

Under most OPIC insurance contracts, investors may obtain all three coverages, but claim payments may not exceed the

(b) Pending Claims

At both September 30, 2012 and 2011 OPIC had no material pending insurance claims. In addition to requiring formal applications for claimed compensation, OPIC's contracts generally require investors to notify OPIC promptly of host government action that the investor has reason to believe is or may become a claim. Compliance with this notice provision sometimes results in the filing of notices of events that do not mature into claims.

OPIC does not record a specific liability related to such notices in its financial statements, due to the highly speculative nature of such notices, both as to the likelihood that the events referred to will ripen into any claims, and the amounts of compensation, if any, that may become due. Any claims that might arise from these situations are factored into the reserves for political risk insurance.

Changes in the reserve for political risk insurance during fiscal years 2012 and 2011 were as follows (dollars in thousands):

	2012	2011
Beginning balance	\$275,000	275,000
Amounts charged off	—	—
Increase/(Decrease) in provisions	3,000	29
Transfers (to)/from other reserves	—	(29)
Ending balance	<u>\$278,000</u>	<u>275,000</u>

(16) Concentration of Risk

OPIC is subject to certain risks associated with financial instruments not reflected in its balance sheet. These financial instruments include political risk insurance, loan guaranties, and committed-but-undisbursed direct loans.

With respect to political risk insurance, OPIC insures against currency inconvertibility, expropriation of assets, and political violence. Additionally, OPIC provides investment financing through direct loans and investment guaranties.

OPIC's credit policy is to take a senior security position in the assets of the projects or transactions it guaranties. The nature and recoverable value of the collateral pledged to OPIC varies from transaction to transaction and may include tangible assets, cash collateral or equivalents, and/or a pledge of shares in the project company as well as personal and corporate guaranties. OPIC takes all necessary steps to protect its position in such collateral and retains the ability to enforce its rights as a secured lender if such action becomes necessary.

The following is a summary of OPIC's off-balance-sheet risk at September 30, 2012 and 2011 (dollars in thousands):

	2012		
	Total	Outstanding	Unused Commitments
Guaranties	\$10,022,667	5,437,500	4,585,167
Undisbursed			
direct loans	1,806,812	—	1,806,812
Insurance	3,134,483	2,353,720	780,763

	2011		
	Total	Outstanding	Unused Commitments
Guaranties	\$8,096,076	4,867,358	3,228,718
Undisbursed			
direct loans	2,119,809	—	2,119,809
Insurance	2,595,376	1,662,057	933,319

OPIC's off-balance-sheet finance and insurance exposure involves coverage outside of the United States. The following is a breakdown of such total commitments at September 30, 2012 by major geographical area (dollars in thousands):

	Loan Guaranties	Undisbursed Portion on Direct Loans	Insurance
Africa	\$ 1,969,363	275,813	1,301,259
Asia	1,222,502	291,327	627,815
Europe	1,443,842	37,699	4,027
Latin America	2,533,029	220,099	329,518
Middle East	1,806,158	518,527	868,136
NIS (New Independent States)	625,549	143,397	366,746
Worldwide	422,224	319,950	—
Insurance stop loss adjustment	—	—	(363,018)
	<u>\$10,022,667</u>	<u>1,806,812</u>	<u>3,134,483</u>

OPIC has several client-specific contracts with stop-loss limits that are less than the aggregate coverage amounts. The insurance stop-loss adjustment represents the difference between the aggregate coverage amount and OPIC's actual exposure under these contracts.

At September 30, 2012, OPIC's largest finance and insurance exposure was in the following countries and sectors (dollars in thousands):

Country	
Turkey	\$1,119,229
Jordan	1,077,717
Ghana	834,668
India	728,946
South Africa	628,967
Sector	
Financial services	\$8,143,930
Energy - Power	3,368,243
Services	1,335,353
Energy - Oil and Gas	909,591
Manufacturing	722,594

DISCLOSURES IN CFR

None

VETERANS LIFE INSURANCE

U.S. DEPARTMENT OF VETERANS AFFAIRS

WWW.VA.GOV , WWW.BENEFITS.VA.GOV/INSURANCE/

BRIEF SUMMARY OF PROGRAM

Veterans' Group Life Insurance (VGLI) provides for the conversion of Service members' Group Life Insurance (SGLI) to a renewable term life insurance policy. This policy is renewable every five years, regardless of health, and can be retained for life.

Service members are eligible to apply for VGLI if they were insured under full-time SGLI and

- are being released from active duty or the Ready Reserves or were released within the last year and 120 days.
- are a member of the Individual Ready Reserve (IRR) or Inactive National Guard (ING).
- are a reservist who suffered an injury or disability during active duty or inactive duty for training for a period of less than 31 days and became uninsurable at standard premium rates.¹

VGLI provides a maximum amount of coverage equal to the amount of SGLI coverage a member had in force at the time of separation from active duty or the Reserves. VGLI is issued in multiples of \$10,000, up to the current legal maximum of \$400,000. VGLI can be converted at any time to an individual permanent (i.e., whole life or endowment) plan with one of 20 participating commercial insurance companies.

Effective April 11, 2011, Veterans already covered by VGLI who are under age 60 and have less than \$400,000 in coverage can purchase up to \$25,000 of additional coverage on each five-year anniversary of their coverage, up to the current maximum of \$400,000. No medical underwriting is required for the additional coverage.

The SGLI Disability Extension allows Veterans who are totally disabled at the time of discharge to retain the SGLI coverage they had in service for up to two years from the date of discharge, at no cost. At the end of that two-year period, they will automatically be issued VGLI provided they begin paying premiums.

¹ Source: Office of Public and Intergovernmental Affairs Fact sheets on the Office of Public and Intergovernmental Affairs <http://www.va.gov/opa/publications/factsheets.asp> website last accessed May 28, 2013.

Servicemembers' Group Life Insurance (SGLI) is a low-cost group term life insurance program for Servicemembers. Coverage can be extended for up to two years if the Servicemember is totally disabled at separation.

Veterans' Group Life Insurance (VGLI) allows Veterans to convert your SGLI to a civilian program of lifetime renewable term coverage after separation from service.

Family Servicemembers' Group Life Insurance (FSGLI) insures spouses and children of Servicemembers with SGLI coverage. Spousal coverage may not exceed the Servicemember's coverage. Dependent children are automatically covered at no charge.

Servicemembers' Group Life Insurance Traumatic Injury Protection (TSGLI) is an automatic feature of SGLI that provides payments to Servicemembers who suffer losses, such as amputations, blindness, and paraplegia, due to traumatic injuries that occur in service.

Service-Disabled Veterans' Life Insurance (S-DVI) provides life insurance coverage to Veterans who have been given a VA rating for a new service-connected disability in the last two years. Totally disabled Veterans are eligible for free coverage and have the opportunity to purchase additional life insurance.

Veterans' Mortgage Life Insurance (VMLI) provides mortgage life insurance protection to disabled Veterans who have been approved for a VA Specially Adapted Housing (SAH) grant.

The Insurance Actuarial Staff is located at the Insurance Center in Philadelphia. They are responsible for the financial management and actuarial soundness of the life insurance programs that are administered and supervised by the Department of Veterans Affairs Insurance Center.

The Staff's responsibilities include the determination of premiums and dividends, determining policy values, developing mortality and insurance experience studies, setting appropriate reserve levels and financial reporting. The Actuarial Staff is also responsible for the evaluation of the financial impact of legislative proposals that will affect the life insurance programs. The Actuarial Staff prepares the financial statements for each of the VA life insurance programs. These statements present the financial position of each program. Each year, independent auditors audit these statements to ensure that the statements accurately reflect the financial position of the programs. This is important because a favorable audit opinion means that the life insurance programs are able to meet their obligations to policyholders and that all policyholders are being treated equitably. For every fiscal year since 1992, the VA Insurance program has received an unqualified audit opinion. This means that the independent auditors have determined that the financial statements accurately reflect the financial position of the insurance programs.

The Department of Veterans Affairs Insurance Center (VAIC) in Philadelphia manages the government life insurance programs. For the six insurance programs that are administered directly by VA (USGLI, NSLI, VSLI, VRI, S-DVI and VMLI) the Insurance Center is responsible for:

- Issuing new policies

- Collecting premiums
- Processing policy actions (change of address, loans, cash surrenders, etc.)
- Paying death and disability claims
- Providing toll-free telephone service
- Performing all actuarial functions
- Formulating policy, plans and procedures and
- Evaluating performance of the insurance programs

Note: Designing, developing, installing and maintaining application software, which supports the life insurance programs, is performed by the Insurance Products Division of the Office of Information and Technology, which is co-located with the Philadelphia VAIC. The Insurance Center also supervises the SGLI and VGLI programs. The SGLI/VGLI group life insurance policy is issued by Prudential Insurance Company of America. SGLI and VGLI provide coverage for members of the uniformed services (including family members), reservists and post-Vietnam Veterans. The Office of Servicemembers' Group Life Insurance (OSGLI) in Roseland, New Jersey, is an administrative office created by Prudential to administer the day-to-day operations of SGLI and VGLI.

Size of VA Insurance Programs

According to the most recent data available (calendar year 2011), VA was the 9th largest insurer in the country with 7.0 million individuals insured for \$1.34 trillion. This figure includes the coverage provided under all of the Insurance programs for which VA is responsible.²

"As part of our mission to serve Servicemembers, Veterans, and their families, VA provides valuable life insurance benefits to give you the peace of mind that comes with knowing your family is protected. VA's life insurance programs were developed to provide financial security for your family given the extraordinary risks involved in military service." VA Website³

² Source: 2013 VA Life Book accessed at http://www.benefits.va.gov/INSURANCE/ins_publications.asp last accessed on May 28, 2013.

³ Source: Life Insurance: Protect You and Your Family with VA Life Insurance VA website <http://www.benefits.va.gov/insurance/> last accessed May 29, 2013

RELATED LEGISLATION AND U.S. CODE (U.S.C.)

1. War Risk Insurance Act, Public Law 65-90, 38 U.S.C 1903-1941
 2. United States Government Life Insurance (1919-1951)
 3. National Service Life Insurance Act, Public Law 76-801
 4. Servicemen's Indemnity and Insurance Act, Public Law 82-23
 5. Veterans' Special Life Insurance (1951-1956)
 6. Service-Disabled Veterans Insurance (1951-Present)
 7. Veterans' Reopened Insurance (1965-1966)
 8. Servicemembers' Group Life Insurance (1965-Present)
 9. World War Veterans Act, Public Law 68-242
 10. Veterans' Group Life Insurance (1974-Present)
 11. Veterans' Mortgage Life Insurance (1971-Present)
 12. The Veterans' Benefit Act of 2010 (Public Law 111-275)
-

SOURCES OF FINANCING

VA receives Congressional appropriations and is listed in the Budget. However, serviceman pay for their insurance policy—whether to the Insurance Center or Prudential Insurance Company of America.

The law specifies that NSLI be operated as a Trust Fund. Its revenues are used exclusively for the benefit of its policyholders and may not be used for any other government program. Any excess revenues resulting from favorable experience are returned to NSLI policyholders in the form of dividends.

NOTE: Much more additional analysis could be done of the various programs. Additional information about each insurance program including eligibility, coverage amounts and premiums can be found in the publication Veterans Life Insurance Publications & Handbooks at http://www.benefits.va.gov/INSURANCE/ins_publications.asp.

SOURCE OF GAAP

VA primarily applies generally accepted accounting principles (GAAP) issued by the FASAB.

SIGNIFICANT FINANCIAL STATEMENT ELEMENTS

Insurance Liabilities

RELEVANT GAO REPORTS (*LAST 5 YEARS*)

No recent GAO reports identified.

DISCLOSURES IN AFR

Excerpts from FY 2012 VA Performance and Accountability Report⁴

⁴ Source: VA website -- <http://www.va.gov/budget/report/> last accessed June 6, 2013.

Insurance Liabilities

Insurance Liabilities for VA's life insurance programs include: policy reserves; unearned premiums; insurance dividends left on deposit and related interest payable; accrued interest payable on insurance policies and dividends payable to policyholders.

Actuarial reserve liabilities for VA's insurance programs for 2012 and 2011 are based on mortality and interest rate assumptions that vary by fund, type of policy, and type of benefit. The interest rate assumptions range from 2.25 to 5.0 percent. The mortality assumptions include the American Experience Table, the X-18 Table, the 1941 Commissioners Standard Ordinary (CSO) Table, the 1958 CSO Basic Table, the 1980 CSO Basic Table, and the 2001 Valuation Basic Male (VBM) Table.

National Service Life Insurance (NSLI) basic policy reserves for permanent plans are based on the American Experience Table with 3 percent interest, except for the Modified Life plans, which are based on the 1958 CSO Basic Table with 3 percent interest, and paid-up additions purchased by dividends, which are based on the 2001 VBM Table with 4 percent interest. The reserve for Term policies is based on the 2001 VBM Table with 4 percent interest and the age 70 rate (the capped premium) of \$6.18 per month per \$1,000 face amount.

United States Government Life Insurance (USGLI) permanent plan policy reserves are based on the American Experience Table with 3.5 percent interest and are held on a net single premium basis.

Veterans Special Life Insurance (VSLI) permanent plan policy reserves are based on the X-18 Table at 2.5 percent interest, except for paid-up additions, which are based on the 1980 CSO Basic Table with 5 percent interest. The reserve for Term policies is based on the

1980 CSO Basic Table with 5 percent interest and the age 70 rate (the capped premium) of \$5.87 per month per \$1,000 face amount.

Service-Disabled Veterans Insurance (S-DVI) permanent plan policy reserves are based on the 1941 CSO Table at 3.5 percent interest using rate book premiums. The reserve for 5-Year Term policies is based on varying ratios of the 1941 CSO Table at 3.5 percent interest using rate book premiums and is computed on a complete contract basis. The mortality ratios start at 250 percent for ages 50 and below and grade down to 100 percent of the table for ages 65 and older. The reserve for Term policies renewed at age 70 and over is based on the 1941 CSO Table with 3.5 percent interest and the age 70 Term capped premium of \$5.87 per month per \$1,000 face amount.

Veterans Reopened Insurance (VRI) basic policy reserves are based on an interest rate of 3.5 percent and a mortality basis that varies by segment ("J", "JR" or "JS") and by rating code within the "JR" segment. For "J", the basis is 100 percent of the 1958 CSO Basic Table. For "JR", the basis is the same as the rating code (150, 175, 200, 250, 300, 400 or 500 percent) of the Basic Table. For "JS", the basis is the American Experience Table, and the reserve is a single premium. Reserves for paid-up additions are based on the 2001 VBM Table and 4 percent interest for "J", the 1958 CSO Basic Table and 4 percent interest for "JR", and 150 percent of the 1958 CSO Basic Table and 4 percent interest for "JS".

The Veterans' Mortgage Life Insurance (VMLI) program is operated through the Veterans' Insurance & Indemnities (VI&I) fund. The reserve for VMLI policies is based on 500 percent of the 1958 CSO Basic Table at 2.5 percent interest.

A reserve for unearned premiums is held for premiums paid for coverage past the date of

the statement. It is comprised of an estimate for premiums paid less than one month in advance that are unearned at the end of the reporting period, and a reserve for premiums paid one month or more in advance computed from in-force master records.

the discount rate was 5 percent for all funds, except USGLI, which was 4.5 percent. The methodology employed by VA to estimate the dividend liability reflects expected dividends to be paid by quarter using percentages that are based on the actual distribution of dividend anniversaries at the end of the prior year.

Insurance dividends that are left on credit or deposit with VA accrue interest at a rate that varies by fund relative to the fund's investment portfolio earnings. For 2012 and 2011, the interest rates ranged from 4.25 percent to 5.5 percent

The Secretary of VA determines annually the excess funds available for dividend payment. Policyholders can elect to: (1) receive a cash payment; (2) prepay premiums; (3) repay loans; (4) purchase paid-up insurance; or (5) deposit the amount in an interest-bearing account. Policies in four of the administered programs are eligible for dividends: NSLI, USGLI, VSLI and VRI. The dividend authorization is based on an actuarial analysis of each program's claims and investment experience, compared to the mortality and interest assumptions utilized in that program, at the end of the preceding calendar year. Dividends are declared on a calendar year basis and paid on policy anniversary dates. A provision for dividends is charged to operations and an insurance dividend is established when gains to operations are realized in excess of those essential to maintain solvency of the insurance programs.

The reserve for Dividends Payable is an estimate of the present value of dividends accrued as of the valuation date. In accordance with GAAP requirements, VA records only that portion of the estimated policy dividend that applies to the current reporting period as a dividend liability. For 2012, a discount rate of 4 percent (5 percent VSLI), along with the appropriate accrual factor, was used. For 2011,

17. Insurance Programs

Through VA, the Government administers six life insurance programs: the United States Government Life Insurance (USGLI) program, the National Service Life Insurance (NSLI) program, the Veterans Special Life Insurance (VSLI) program, and the Veterans Reopened Insurance (VRI) program, which cover Veterans who served during World War I, World War II, and the Korean Conflict eras, and also the Service-Disabled Veterans Insurance (S-DVI) program and the Veterans Mortgage Life Insurance (VMLI) program, which cover severely disabled Veterans and are open to new issues. VMLI is part of the Veterans Insurance & Indemnities (VI&I) fund.

In addition, VA supervises the Servicemembers Group Life Insurance (SGLI) and the Veterans Group Life Insurance (VGLI) programs, which provide coverage to members of the uniformed armed services, reservists, and post-Vietnam Veterans and their families. All SGLI insureds are automatically covered under the Traumatic Injury Protection (TSGLI) program, which provides for insurance payments to members who suffer a serious traumatic injury in service. VA has entered into a group policy with the Prudential Insurance Company of America to administer these programs.

Premiums for the SGLI and VGLI programs are set by mutual agreement between VA and Prudential. SGLI premiums for active duty personnel and their spouses are deducted from the Servicemember's pay by the Armed Services components through the DoD. DoD, through the Defense Finance and Accounting Service (DFAS), remits collected premiums to VA, which are then transmitted to Prudential. Prudential records the premiums and maintains investments in their accounting records separate and independent from the VA reporting entity. VA monitors Prudential's insurance reserve balances to determine their

adequacy and may increase or decrease the amounts retained by Prudential for contingency purposes. The reserves for the contingent liabilities are recorded in Prudential's accounting records and are not reflected in the VA reporting entity because the risk of loss on these programs is assumed by Prudential and its reinsurers through the terms and conditions of the group policy. Prudential administers the TSGLI program under an Administrative Services Only agreement with VA. Under the law, DoD pays for any claim costs for this program in excess of premiums collected.

The Secretary of VA determines the claim costs that are traceable to the extra hazards of duty in the uniformed services, on the basis of the excess mortality incurred by members and former members of the uniformed armed services insured under SGLI, above what their mortality would have been under peacetime conditions. The costs so identified by the Secretary are paid by the uniformed services, not from the Servicemembers' premiums, as are all other programs costs.

The insurance reserves for the administered programs are reported as liabilities covered by budgetary resources, while part of the S-DVI and VI&I reserves are reported as liabilities not covered by budgetary resources. Reserves for SGLI and VGLI are maintained in Prudential's financial records since the risk of loss is assumed by Prudential and its reinsurers. United States Code, Title 38, requires that the Life Insurance programs invest in Treasury securities.

Actuarial reserve liabilities for the administered life insurance programs are based on the mortality and interest assumptions that vary by fund, type of policy, and type of benefit. The interest assumptions range from 2.25 to 5 percent. The mortality assumptions include the

American Experience Table, the 1941
Commissioners Standard Ordinary (CSO)
Table, the 1958 CSO Basic Table, the 1980 CSO

Basic Table, the 2001 CSO Table and the 2001
Valuation Basic Male (VBM) Table.

**Insurance Liability (Reserve) Balances
as of September 30, 2012**

Program	Insurance Death Benefits	Death Benefit Annuities	Disability Income & Waiver	Reserve Totals
NSLI	\$ 5,661	\$ 75	\$ 41	\$ 5,777
USGLI	5	2	-	7
VSLI	1,497	6	13	1,516
S-DVI	510	6	693	1,209
VRI	203	1	2	206
VI&I	201	-	-	201
Subtotal	\$ 8,077	\$ 90	\$ 749	\$ 8,916
Unearned Premiums				59
Insurance Dividends Left on Deposit and Related Interest Payable				1,521
Dividends Payable to Policyholders				84
Unpaid Policy Claims				1
Insurance Liabilities reported on the Consolidated Balance Sheet				10,581
Less Liability not Covered by Budgetary Resources				(1,293)
Liability Covered by Budgetary Resources				\$ 9,288

as of September 30, 2011

Program	Insurance Death Benefits	Death Benefit Annuities	Disability Income & Waiver	Reserve Totals
NSLI	\$ 6,187	\$ 84	\$ 47	\$ 6,318
USGLI	8	2	-	10
VSLI	1,528	7	15	1,550
S-DVI	484	6	646	1,136
VRI	227	1	2	230
VI&I	114	-	-	114
Subtotal	\$ 8,548	\$ 100	\$ 710	\$ 9,358
Unearned Premiums				65
Insurance Dividends Left on Deposit and Related Interest Payable				1,587
Dividends Payable to Policyholders				101
Unpaid Policy Claims				2
Insurance Liabilities reported on the Consolidated Balance Sheet				11,113
Less Liability not Covered by Budgetary Resources				(1,161)
Liability Covered by Budgetary Resources				\$ 9,952

Insurance In-Force

The amount of insurance in-force is the total face amount of life insurance coverage provided by each administered and supervised program as of the end of the fiscal year. It includes any paid-up additional coverage provided under these policies. The supervised programs' policies and face value are not reflected in the VA reporting entity because the risk of loss on these programs is assumed by Prudential and its reinsurers through the terms and conditions of the group policy. As a result, the information provided below under the Supervised Programs

is for informational purposes only and is unaudited. Prudential and its reinsurers provided coverage to 6,009,819 and 6,103,250 policy holders with a face value of \$1.3 trillion and \$1.3 trillion for the years ended September 30, 2012, and 2011, respectively. The face value of the insurance provided by Prudential and its reinsurers represents 99 percent and 99 percent of the total insurance in-force as of September 30, 2012, and 2011, respectively. The number of policies represents the number of active policies remaining in the program as of the end of each fiscal year.

	2012 Policies	2011 Policies	2012 Face Value	2011 Face Value
Supervised Programs (UNAUDITED)				
SGLI Active Duty	1,525,000	1,560,000	\$ 588,489	\$ 604,138
SGLI Ready Reservists	771,500	774,500	268,153	271,826
SGLI Post Separation	93,000	88,000	34,812	33,097
SGLI Family - Spouse	1,095,000	1,128,000	108,012	111,320
SGLI Family - Children	2,098,000	2,126,000	20,980	21,260
TSGLI*	-	-	229,650	233,450
VGLI	427,319	426,750	62,700	60,694
Total Supervised	6,009,819	6,103,250	\$ 1,312,796	\$ 1,335,785
Administered Programs				
NSLI	586,450	665,394	\$ 7,174	\$ 8,040
VSLI	149,947	158,765	2,055	2,141
S-DVI	241,224	227,887	2,499	2,340
VRI	23,983	27,605	249	283
USGLI	2,165	2,958	6	8
VMLI	2,466	2,395	299	179
Total Administered	1,006,235	1,085,004	\$ 12,282	\$ 12,991
Total Supervised and Administered Programs	7,016,054	7,188,254	\$ 1,325,078	\$ 1,348,776

*TSGLI coverage is a rider attached to SGLI coverage, so policies under SGLI also have TSGLI.

Policy Dividends

The Secretary of VA determines annually the excess funds available for dividend payment.

Policy dividends for 2012 and 2011 were \$189 million and \$229 million, respectively.

RELATED DISCLOSURES IN CFR

Excerpt from 2012 CFR Note 15: Federal Employees and Veteran Benefit Payable
Life Insurance Benefits

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

- National Service Life Insurance (NSLI) covers policyholders who served during World War II.
- Veterans' Special Life Insurance (VSLI) was established in 1951 to meet the insurance needs of veterans who served during the Korean Conflict and through the period ending January 1, 1957.
- Veterans' Reopened Insurance (VRI), which provided a 1-year reopening for insurance coverage in 1965 for those eligible to have obtained NSLI or VSLI and were disabled.

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

Veterans Life Insurance Liability as of September 30, 2012, and 2011		
(In billions of dollars)	2012	2011
Insurance death benefits:		
NSLI	5.7	6.2
VSLI	1.5	1.5
VRI	0.2	0.2
Other	0.7	0.6
Total death benefits	<u>8.1</u>	<u>8.5</u>
Death benefit annuities	0.1	0.1
Disability income and waiver	0.7	0.7
Insurance dividends payable	1.6	1.7
Unearned premiums	0.1	0.1
Total veterans life insurance liability	<u>10.6</u>	<u>11.1</u>

Insurance dividends payable consists of dividends left on a deposit with VA, related interest payable, and dividends payable to policyholders.

The VA supervises Servicemembers Group Life Insurance and Veterans Group Life Insurance programs that provide life insurance coverage to members of the uniformed armed services and veterans who served during the Vietnam era or thereafter. The VA also provides certain veterans and/or their dependents with pension benefits, based on annual eligibility reviews, if the veteran died or was disabled for nonservice-related causes. The actuarial present value of the future liability for pension benefits is a non-exchange transaction and is not required to be recorded on the Balance Sheet. The projected amounts of future payments for pension benefits (presented for informational purposes only) as of September 30, 2012, and 2011, were \$92.8 billion and \$89.2 billion, respectively.

EXPORT CREDIT INSURANCE

EXPORT-IMPORT BANK

<http://export.gov>

BRIEF SUMMARY OF PROGRAM

The Export-Import (Ex-Im) Bank of the United States is the official export credit agency of the United States. Ex-Im Bank's mission is to assist in financing the export of U.S. goods and services to international markets. The Ex-Im Bank is an independent federal government agency and operates at no cost to U.S. taxpayers.

Ex-Im Bank offers U.S. companies insurance for both export transactions and for the political risk associated with overseas investments. Ex-Im Bank's export credit insurance policies enables U.S. exporters to both finance their export activities and mitigate the risk of non-payment. Ex-Im Bank enables U.S. companies — large and small — to turn export opportunities into real sales that help to maintain and create U.S. jobs and contribute to a stronger national economy. Ex-Im Bank does not compete with private sector lenders but provides export financing products that fill gaps in trade financing. Ex-Im Bank assumes credit and country risks that the private sector is unable or unwilling to accept. They also help to level the playing field for U.S. exporters by matching the financing that other governments provide to their exporters.¹

About Export Credit Insurance: Making international sales is challenging enough without worrying about getting paid. Ex-Im Bank's export credit insurance policy provides payment coverage for both commercial risks (such as buyer default) and political risks (such as war). The Bank protects sales to a single buyer or an entire export portfolio.

The **Express Insurance Program** is a "named buyer" policy that simplifies small business access to export credit risk insurance on their foreign accounts receivable. It also has a streamlined online application provides a policy quote and credit decisions up to \$300,000 on foreign buyers within five workdays (buyer credit requests exceeding \$300,000 will require additional processing time).

The **Small Business Export Credit Insurance Policy** is specifically designed for small, financially viable businesses that are new to exporting, or have only occasionally exported. It can help increase an exporter's international sales by extending competitive credit terms while minimizing risks.

The **Multi-Buyer Export Credit Insurance Policy** enables U.S. exporters to reduce their risk of selling on credit terms by insuring their export accounts receivable against default or non-payment. The policy can help increase international sales by extending competitive credit terms to foreign buyers while minimizing risks.

¹ Source <http://www.exim.gov/> last accessed June 4, 2013

The **Short-Term Single-Buyer Export Credit Insurance Policy** allows exporters to insure specific, short-term foreign receivables against loss due to commercial and specified political risks on a selective basis.

Ex-Im Bank offers U.S. leasers the opportunity to expand their overseas leasing programs by providing **comprehensive insurance** for both the stream of lease payments and the fair market value of the leased products.²

Export credit insurance is another major product offered by the Ex-Im Bank. The Ex-Im Bank issues the insurance policy to a U.S. exporter, that provides credit to the foreign buyer of the exporter's products. If the foreign borrower defaults for political or commercial reasons, the Bank will pay the exporter the outstanding balance owed by the foreign borrower. Insurance coverage carries various conditions that must be met by the insured before the Bank will pay off a claim.

The Ex-Im Bank charges the exporter an insurance premium in a variable amount based on duration, amount, and risk characteristics of transactions. The Ex-Im Bank's export credit insurance includes both short-term and medium-term insurance. Small businesses are a significant user of the Ex-Im Bank's export credit insurance program.

Like loan guarantees, export credit insurance reduces some of the risks involved in exporting by protecting against commercial or political uncertainty. There is an important distinction, however, between the two programs. Insurance coverage is more conditional than a guarantee. In contrast, a guarantee is a commitment made to a commercial bank by the Ex-Im Bank that promises full repayment with few, if any, conditions attached.³

With each transaction, the Bank is fulfilling its congressional charter, which states, "The Bank's objective in authorizing loans, guarantees, insurance and credits shall be to contribute to maintaining or increasing employment of United States workers." Export – Import 2012 Annual Report

RELATED LEGISLATION AND U.S. CODE (U.S.C.)

1. Export-Import Bank Act of 1945, as amended
2. P.L. 112-74 (reauthorization) Consolidated Appropriations Act of 2012
3. 12 USC § 635a–3 - Export-Import Bank

² Source: http://export.gov/finance/eg_main_018098.asp June 4, 2013.

³ Source: Congressional Research Service Report, R42472 Export-Import Bank: Background and Legislative Issues

SOURCES OF FINANCING

Although the Bank may on occasion receive appropriations when it is determined that additional funds are needed through the credit loss re-estimate of the Bank's existing portfolio, the Bank no longer receives appropriations from Congress to cover administrative costs and program costs for new loan, guarantee and insurance authorizations. Instead, the Bank covers these costs from the fees collected on a cash basis (offsetting collections) from the Bank's credit program customers. Fees collected are first used to cover the costs of the Bank's loan, guarantee and insurance programs by setting aside prudent reserves for credit losses. Fees collected in excess of those set aside for reserves are then used to cover administrative costs up to limits set by Congress. The disposition of fees collected in excess of amounts set aside for credit loss reserves and administrative costs are determined by the Bank's annual appropriation act passed by Congress.⁴

SOURCE OF GAAP

Export-Import Bank primarily applies generally accepted accounting principles (GAAP) issued by the FASAB.

⁴ FY 2012 Annual Report <http://www.exim.gov/about/library/reports/annualreports/2012/> last accessed June 4, 2013.

SIGNIFICANT FINANCIAL STATEMENT ELEMENTS

Excerpts from FY 2012 Ex-Im Annual Report⁵

Exhibit 14: Significant Financial Data

(in millions)	FY 2012	FY 2011
Fund Balance With the U.S. Treasury	\$2,477.3	\$3,842.3
Receivables from the Program Account	—	789.3
Loans Receivable, Net	10,865.4	6,701.0
Receivables from Subrogated Claims, Net	303.7	367.2
Other Assets	22.8	11.2
Borrowings from the U.S. Treasury	11,301.3	8,279.3
Accounts Payable to the U.S. Treasury	704.0	939.6
Payable to the Financing Account	—	789.3
Payment Certificates	47.5	64.3
Guaranteed Loan Liability	1,814.0	1,219.5
Other Liabilities	563.0	876.7
Cumulative Results of Operations	(1,975.9)	(1,675.5)
Interest Expense	523.9	439.0
Provision for Credit Losses	1,022.9	482.1
Fees and Other Income	366.4	305.7

Guaranteed Loan Liability: Guaranteed Loan Liability increased by \$594.5 million from \$1,219.5 million at September 30, 2011, to \$1,814.0 million at September 30, 2012. The change is attributed to increased guarantee and insurance exposure and changes to the risk profile of the portfolio.

Fees & Other Income: Fees and Other Income increased \$60.7 million from \$305.7 million for the year ended September 30, 2011, to \$366.4 million for the year ended September 30, 2012. The change represents activity resulting from increased levels of loan, guarantee and insurance authorizations.

⁵ Source: Ex-Im website -- <http://www.exim.gov/about/library/reports/annualreports/2012/> last accessed June 4, 2013.

RELEVANT GAO REPORTS (LAST 5 YEARS)

Recent GAO reports pertain to loan and loan guarantee programs

RELEVANT DISCLOSURES IN AFR

Excerpts from FY 2012 Ex-Im Annual Report⁶

Products

From a portfolio perspective, guarantees made up the largest portion (62.7 percent and 68.8 percent) of Ex-Im Bank's exposure at September 30, 2012, and September 30, 2011, respectively.

(in millions)	FY 2012		FY 2011	
Outstanding Guarantees	\$54,133.5	50.8%	\$47,844.0	53.7%
Outstanding Loans	12,354.1	11.6%	8,109.7	9.1%
Outstanding Insurance	2,689.4	2.5%	2,444.8	2.7%
Outstanding Claims	1,499.2	1.4%	1,677.6	1.9%
Total Outstanding	70,676.2	66.3%	60,076.1	67.4%
Undisbursed Loans	16,404.2	15.4%	8,622.7	9.7%
Undisbursed Guarantees	12,726.7	11.9%	13,585.1	15.2%
Undisbursed Insurance	6,839.3	6.4%	6,868.1	7.7%
Total Undisbursed	35,970.2	33.7%	29,075.9	32.6%
Total Exposure	\$106,646.4	100.0%	\$89,152.0	100.0%

⁶ Source: Ex-Im website -- <http://www.exim.gov/about/library/reports/annualreports/2012/> last accessed June 4, 2013.

Express Insurance, which provides small-businesses with payment-risk protection, allows the extension of competitive credit terms to foreign buyers and enables small businesses to obtain lender financing of receivables through the assignment of policy proceeds. It also delivers a five-day turnaround on policy quotation and two buyer-credit decisions on a simple, streamlined application platform. The Express Insurance program has been recognized with a "Bright Idea in Government" award from the Ash Center for Democratic Governance and Innovation at Harvard University's John F. Kennedy School of Government.

Also in FY 2012 the Bank began a multiyear project to modernize IT systems infrastructure. The Total Enterprise Modernization (TEM) project will make long-deferred technology investments and focus on transforming business processes to grow the Bank's capacity to meet customer needs and enhance long-term capabilities of the Bank.

Results: FY 2012 Authorizations

The Bank has responded to a record level of financing requests this year to provide export financing on behalf of U.S. companies expanding foreign sales and sustaining and creating jobs. In FY 2012, Ex-Im Bank approved \$35,784.3 million in authorizations. This is a 9.3 percent increase over authorizations of \$32,727.1 million in FY 2011.

The authorizations supported an estimated U.S. export value of \$49,988.9 million for FY 2012 and \$41,305.1 million in FY 2011 and an estimated 255,000 and 288,000 U.S. jobs in FY 2012 and FY 2011, respectively. The increasing level of authorizations is due primarily to the lack of available private-sector liquidity, the overall growth in U.S. exports, which since the announcement of the National Export Initiative in 2010 has grown nearly 38 percent, the Bank's ability to respond to the resulting financing gaps and continued implementation of the Bank's five-year strategic plan. Full-year authorizations increased from \$14,398.9 million to \$35,784.3 million during the past five fiscal years as shown in Exhibit 1B.

Exhibit 1B: Authorizations by Fiscal Year

(in millions)

Authorizations	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012
Long Term					
Loans	\$356.0	\$3,025.5	\$4,255.5	\$6,315.0	\$11,751.7
Guarantees	8,101.5	9,628.5	10,225.0	15,479.4	14,879.6
Subtotal, Long-Term	8,457.5	12,654.0	14,480.5	21,794.4	26,631.3
Medium Term					
Loans	—	—	5.1	79	12.8
Guarantees	697.0	315.2	702.5	693.0	186.8
Insurance	228.0	237.3	312.9	238.8	165.0
Subtotal, Medium-Term	925.0	552.5	1,020.5	939.7	364.6
Short Term					
Working Capital	1,380.9	1,531.0	2,178.5	3,228.0	3,254.1
Insurance	3,635.5	6,275.8	6,788.3	6,765.0	5,534.3
Subtotal, Short-Term	5,016.4	7,806.8	8,966.8	9,993.0	8,788.4
Tied Aid	—	7.8	—	—	—
Total Authorizations	\$14,398.9	\$21,021.1	\$24,467.8	\$32,727.1	\$35,784.3

Ex-Im Bank loan guarantees cover the repayment risks on the foreign buyer's debt obligations incurred to purchase U.S. exports. Ex-Im Bank guarantees to a lender that, in the event of a payment default by the borrower, it will pay to the lender the outstanding principal and interest on the loan. Ex-Im Bank's comprehensive guarantee covers commercial and political risks for up to 85 percent of the U.S. contract value.

When needed, Ex-Im Bank offers fixed-rate loans directly to foreign buyers of U.S. goods and services. Ex-Im Bank extends to a company's foreign customer a fixed-rate loan covering up to 85 percent of the U.S. contract value. Ex-Im Bank's direct loans generally carry fixed-interest rates permitted for the importing country and term under the Arrangement on Guidelines for Officially Supported Export Credits negotiated among members of the Organisation for Economic Co-operation and Development (OECD).

Loans and guarantees extended under the medium-term loan program typically have repayment terms of one to seven years, while loans and guarantees extended under the long-term loan program usually have repayment terms in excess of seven years.

Under the Working Capital Guarantee Program, Ex-Im Bank provides repayment guarantees to lenders on secured, short-term working capital loans made to qualified exporters. The working capital guarantee may be approved for a single loan or a revolving line of credit. Ex-Im Bank's working capital guarantee protects the lender from default by the exporter for 90 percent of the loan principal and interest.

Ex-Im Bank's Export Credit Insurance Program helps U.S. exporters sell their goods overseas by protecting them against the risk of foreign-buyer or other foreign-debtor default for political or commercial reasons, allowing them to extend credit to their international customers. Insurance policies may apply to shipments to one buyer or many buyers, insure comprehensive (commercial and political) credit risks or only political risks, and cover short-term or medium-term sales.

Significant Factors Influencing Financial Results

The most significant factor that determines Ex-Im Bank's financial results and condition is a change in the risk level of Ex-Im Bank's loan, guarantee and insurance portfolio, and the adjustment to the allowance for credit losses that must be made to reflect the change in risk. The level of risk of individual credits or groups of credits may change in an unexpected manner as a result of international financial, economic and political events. Consequently, significant and unanticipated changes in Ex-Im Bank's allowance for credit losses may occur in any year.

The major risks to the Bank in its credit portfolio are repayment risk and concentration risk. Other risks the Bank must assess and attempt to minimize are foreign-currency risk, operational risk, organizational risk and interest-rate risk.

4. Direct Loan, Loan Guarantees and Export-Credit Insurance Programs, Nonfederal Borrowers

Ex-Im Bank offers fixed-rate loans directly to foreign buyers of U.S. goods and services. Ex-Im Bank extends to a company's foreign customer a fixed-rate loan covering up to 85 percent of the U.S. contract value. The buyer must make a cash payment to the U.S. exporter of at least 15 percent of the U.S. contract value. Ex-Im Bank's direct loans generally carry the lowest fixed-interest rate permitted for the importing country and term under the "Arrangement on Guidelines for Officially Supported Export Credits" negotiated among members of the OECD.

Ex-Im Bank loan guarantees cover the repayment risks on the foreign buyer's debt obligations incurred to purchase U.S. exports. Ex-Im Bank guarantees to a lender that, in the event of a payment default by the borrower, it will pay to the lender the outstanding principal and interest on the loan. Ex-Im Bank's comprehensive guarantee covers all of the commercial and political risks for 85 percent of the U.S. contract value.

Ex-Im Bank's export-credit insurance helps U.S. exporters sell their goods overseas by protecting them against the risk of foreign-buyer or other foreign-debtor default for political or commercial reasons, allowing them to extend credit to their international customers. Insurance policies may apply to shipments to one buyer or many buyers, insure comprehensive (commercial and political) credit risks or only political risks, and cover short-term or medium-term sales.

Credit Reform

The primary purpose of the FCRA is to measure more accurately the cost of federal credit programs and to place the cost of such credit programs on a basis equivalent with other federal spending.

OMB established The Interagency Country Risk Assessment System (ICRAS) to provide a framework for uniformly measuring country risk for the U.S. government's international credit programs across the various agencies that administer them. The ICRAS methodology determines the risk levels for lending to both sovereign governments and nonsovereign borrowers.

ICRAS rates every country to which U.S. government agencies have outstanding loans or loan guarantees or are anticipating making new credits available. ICRAS rates countries on the basis of economic and political and/or social variables. There are 11 sovereign and nine nonsovereign risk categories and each country receives two ratings: a sovereign-risk rating and a private-risk rating. ICRAS currently has risk ratings for 198 sovereign and 200 nonsovereign markets.

FY 2012 and FY 2011 Activity

Ex-Im Bank received a \$4.0 million appropriation in FY 2012 and \$2.5 million in FY 2011 for the Inspector General administrative costs.

Beginning in FY 2008, fees collected in excess of expected credit losses (offsetting collections) are used to cover the Bank's credit program needs for providing new direct loans, guarantees and insurance and for administrative costs.

The following table summarizes offsetting collections and appropriations received and used in FY 2012 and in FY 2011:

(in millions)	FY 2012	FY 2011
RECEIVED AND AVAILABLE		
Appropriation for Inspector General Administrative Costs	\$4.0	\$2.5
Offsetting Collections	197.9	701.1
Total Received	201.9	703.6
Unobligated Balance Carried Over From Prior Year	950.2	676.5
Rescission of Unobligated Balances	(400.0)	(275.0)
Cancellations of Prior-Year Obligations	9.7	4.5
Total Available	560.9	406.0

OBLIGATED

Of the remaining balance of \$595.9 million at September 30, 2012, \$92.5 million is available until September 30, 2013; \$217.0 million is available until September 30, 2014; \$108.0 million is available until September 30, 2015; and \$178.4 million is available until expended and may be used for tied-aid programs.

New loans, guarantees and insurance result in a program cost (or subsidy cost) when the net present value of expected cash disbursements exceeds expected cash receipts. Cash receipts typically include fees or premia, loan principal and interest, and cash disbursements typically include claim payments and loan disbursements. For new authorizations, Ex-Im uses both its own historical default and recovery rates in its cash flow models to calculate program cost.

When the present value of expected cash receipts exceeds the present value of expected cash disbursements, a "negative" credit subsidy (or program revenue) arises.

Starting in FY 2008, Ex-Im Bank has operated on a self-sustaining basis using program revenue to fund current year administrative expenses and program costs. During FY 2012, Ex-Im Bank collected \$1,001.6 million of receipts in excess of estimated credit losses. Of these offsetting collections, \$89.9 million was used to fund administrative expenses, \$803.7 million was sent to the U.S Treasury and \$108.0 million was retained and is available for obligation until September 30, 2015. During FY 2011, Ex-Im Bank collected \$701.1 million of receipts in excess of estimated credit losses. Of these offsetting collections, \$83.9 million was used to fund administrative expenses, \$0.2 million was used to fund subsidy expense, and \$617.0 million was retained. In FY 2012, \$400.0 million of the FY 2011 offsetting collections were rescinded, leaving \$217.0 million available for obligation until September 30, 2014.

Administrative costs are the costs to administer and service Ex-Im Bank's entire credit portfolio. The program costs are obligated to cover the estimated subsidy costs at the time loans, guarantees and insurance are committed. As the loans are disbursed, or when the insured or guaranteed event has taken place (generally when the related goods are shipped), the obligated amounts are used to cover the estimated subsidy costs related to the disbursements and shipments. The portion of the obligated amounts related to Ex-Im Bank's lending programs is used to partially fund the loan disbursements, while the portions related to Ex-Im Bank's guarantee and insurance programs are invested in an interest-bearing account with the U.S. Treasury. Prior to loan disbursement or the insured or guaranteed event, all of the appropriated funds and offsetting collections are held in a

F. Guaranteed Loans and Insurance

Ex-Im Bank is exposed to credit loss with respect to the amount of outstanding guaranteed loans and insurance policies in the event of nonpayment by obligors under the agreements. The commitments shown below are agreements to lend monies and issue guarantees and insurance as long as there is no violation of the conditions established in the credit agreement.

(in millions)	FY 2012	FY 2011
Gross Outstanding Principal of Guaranteed Loans and Insurance, Face Value	\$56,822.9	\$50,288.8
Gross Undisbursed Principal of Guaranteed Loans and Insurance, Face Value	19,566.0	20,453.2
Total Gross Principal of Guaranteed Loans and Insurance, Face Value	\$76,388.9	\$70,742.0
Amount of Principal That is Guaranteed and Insured by Ex-Im Bank	\$76,388.9	\$70,742.0
Gross Amount of Guaranteed Loans and Insurance Disbursed During Year, Face Value	\$21,879.7	\$17,892.9
Amount of Guaranteed Loans and Insurance Disbursed During Year That is Guaranteed and Insured by Ex-Im Bank	\$21,879.7	\$17,892.9

G. Liability for Loan Guarantees and Insurance

The Liability for Loan Guarantees and Insurance of \$1,814.0 million at September 30, 2012, and \$1,219.5 million at September 30, 2011 represents the liability for Post FY 1991 guarantees and insurance credits. Since FY 2011, Ex-Im no longer has pre-FY 1992 liabilities for loan guarantees and insurance.

H. Program Cost and Re-Estimate Expense for Loan Guarantees and Insurance by Component

The table below discloses defaults, fees and re-estimate amounts associated with the program cost disbursed in the current year on loan guarantee and insurance authorizations made in the current and prior fiscal years and the current year loss re-estimate. The total program cost also includes modifications made on these authorizations.

(in millions)	FY 2012	FY 2011
Defaults	\$829.0	\$549.8
Fees and Other Collections	(1,195.5)	(792.3)
Total	(366.5)	(242.5)
Net Re-estimate – Principal	290.8	(312.5)
Net Re-estimate – Interest	(570)	(104.6)
Total Net Re-estimate	233.8	(417.1)
Total Loan Guarantee and Insurance Program Cost and Re-Estimate Expense	(\$132.7)	(\$659.6)

I. Program Cost Rates for Loan Guarantees and Insurance by Component

The program cost rates disclosed below relate to the percent of program costs on loan guarantee and insurance authorizations made in the reporting fiscal year. Because these rates only pertain to authorizations from the reporting fiscal year, these rates cannot be applied to the guarantees of loans disbursed during the reporting fiscal year to yield the program cost, which could result from disbursements of loans from both current and prior years.

	FY 2012	FY 2011
Defaults	2.2%	2.1%
Fees and Other Collections	(4.8)%	(4.5)%
Total	(2.6)%	(2.4)%

K. Administrative Costs

(in millions)	FY 2012	FY 2011
Total Administrative Costs	\$98.7	\$91.1

All of the Bank's administrative costs are attributed to the support of the Bank's loan, guarantee and insurance programs. Administrative costs are not allocated to individual programs.

L. Allowance and Exposure Summary

(in millions)	FY 2012	FY 2011
Pre - Credit-Reform Allowance		
Allowance for Loan Losses	\$379.8	\$388.8
Allowance for Defaulted Guarantees	60.8	73.8
Total Pre - Credit-Reform Allowance	440.6	462.6
Credit-Reform Allowance		
Allowance for Loan Losses	1,205.8	1,149.4
Allowance for Defaulted Guarantees and Insurance	1,136.1	1,237.7
Liability for Loan Guarantees and Insurance	1,814.0	1,219.5
Total Credit-Reform Allowance	4,155.9	3,606.6
Total Allowance for Loan Loss	1,585.6	1,538.2
Total Allowance for Guarantees and Insurance	3,010.9	2,531.0
Total Allowance	\$4,596.5	\$4,069.2
Total Outstanding Balance of Loans, Guarantees and Insurance	\$70,676.2	\$60,076.1
Percent Allowance to Outstanding Balance	6.5%	6.8%
Total Exposure	\$106,646.4	\$89,152.0
Percent Allowance to Exposure	4.3%	4.6%

7. Statutory Limitations on Lending Authority

Under provisions of the Export-Import Bank Act, as amended in FY 2012, Ex-Im Bank's statutory authority was increased from \$100.0 billion to \$120.0 billion of loans, guarantees and insurance outstanding at any one time. At September 30, 2012, and September 30, 2011, Ex-Im Bank's statutory authority used was as follows:

(in millions)	FY 2012	FY 2011
Outstanding Guarantees	\$54,133.5	\$47,844.0
Outstanding Loans	12,354.1	8,109.7
Outstanding Insurance	2,689.4	2,444.8
Outstanding Claims	1,499.2	1,677.6
Total Outstanding	70,676.2	60,076.1
Undisbursed Loans	16,404.2	8,622.7
Undisbursed Guarantees	12,726.7	13,585.1
Undisbursed Insurance	6,839.3	6,868.1
Total Undisbursed	35,970.2	29,075.9
Total Exposure	\$106,646.4	\$89,152.0

Transactions can be committed only to the extent that budget authority is available to cover program costs. For FY 2012 and FY 2011, Congress placed no limit on the total amount of loans, guarantees and insurance that could be committed in those years, provided that the statutory authority established by the Export-Import Bank Act was not exceeded.

During FY 2012, Ex-Im Bank committed \$11,764.5 million for direct loans, \$24,019.8 million for guarantees and insurance, using \$72.1 million of budget authority and no tied-aid funds. During FY 2011, Ex-Im Bank committed \$6,322.9 million for direct loans, \$26,404.2 million for guarantees and insurance, using \$68.1 million of budget authority and no tied-aid funds.

Ex-Im Bank has authorized guarantee transactions denominated in a foreign currency during FY 2012 totaling \$1,721.2 million, and authorized \$1,896.3 million during FY 2011, as calculated at the exchange rate at the time of authorization. Ex-Im Bank adjusts the allowance for all transactions denominated in a foreign currency using the various foreign-currency exchange rates at the end of the fiscal year.

For financial statement purposes, Ex-Im Bank defines exposure as the authorized outstanding and undisbursed principal balance of loans, guarantees, and insurance. It also includes the unrecovered balance of payments made on claims that were submitted to Ex-Im in its capacity as guarantor or insurer under the export guarantee and insurance programs. Exposure does not include accrued interest or transactions pending final approval. This corresponds to the way activity is charged against the Bank's overall \$120 billion lending limit imposed by Section 6(a)(2) of Ex-Im Bank's charter.

Working capital guarantees may be approved for a single loan or a revolving line of credit, with an availability generally of one year. Guaranteed lenders do not report activity to Ex-Im Bank; the entire credit is assumed to be "disbursed" when the fee is paid to the Bank. The credit is recorded as repaid in one installment six months after the expiry date of the credit unless the Controller's office is notified before that time that a claim has been paid. Under the assumption that the exporter is using the credit up to the

end of the expiry period, six months provides sufficient time for the guaranteed lender to report defaults to Ex-Im Bank in the event that the exporter does not repay the credit. If a claim is paid, the remaining outstanding balance of the credit associated with the claim is reduced to zero. Exposure is then reflected as an unrecovered claim.

Since there is typically a delay in reporting shipments under the insurance program, undisbursed balances remain on the books for 120 days after the expiry date to allow for the posting of shipments that took place within the period covered by the policy but were reported after the expiry date. These unreported shipments pose some liability in the form of claims that have been incurred but not yet reported (IBNR). Leaving the policy open past the expiry date provides a reserve for IBNR.

8. Concentration of Risk

Ex-Im Bank support is available to U.S. businesses exporting to countries around the world. The Bank's portfolio is concentrated more heavily in some regions, industries and obligors than others. In reviewing each transaction, Ex-Im Bank considers the option of using various credit enhancements to support its standard for a reasonable assurance of repayment. Various types of collateral, including liens on commercial aircraft, may or may not be appropriate or available in support of a credit.

The volatility in commodity prices, the fluctuation in currency exchange rates, and the tightening of credits markets may have an impact on borrowers' ability to service their obligations. Ex-Im Bank closely monitors the portfolio and makes appropriate rating adjustments and loss reserve adjustments as necessary.

The following tables summarize total exposure by geographic region as of September 30, 2012, and September 30, 2011:

2012 (in millions)		
Region	Amount	Percentage
Asia	\$42,345.3	39.7%
Latin America and Caribbean	22,104.6	20.7%
Europe	11,303.8	10.6%
North America	10,579.3	9.9%
Oceania	8,305.0	7.8%
Africa	5,770.8	5.4%
All Other	6,237.6	5.9%
Total	\$106,646.4	100.0%
2011 (in millions)		
Region	Amount	Percentage
Asia	\$32,832.3	36.9%
Latin America and Caribbean	19,728.3	22.1%
Europe	10,772.7	12.1%
North America	9,382.9	10.5%
Oceania	5,372.5	6.0%
Africa	4,832.5	5.4%
All Other	6,260.8	7.0%
Total	\$89,152.0	100.0%

The following tables summarize total exposure by industry as of September 30, 2012 and September 30, 2011:

2012 (in millions) Industry	Amount	Percentage
Air Transportation	\$49,419.6	46.3%
Manufacturing	18,091.0	17.0%
Oil and Gas	13,938.7	13.1%
Power Projects	8,649.2	8.1%
All Other	16,547.9	15.5%
Total	\$106,646.4	100.0%

2011 (in millions) Industry	Amount	Percentage
Air Transportation	\$43,014.5	48.2%
Manufacturing	12,499.8	14.0%
Oil and Gas	10,916.6	12.2%
Power Projects	6,818.8	7.6%
All Other	15,902.3	18.0%
Total	\$89,152.0	100.0%

Guarantees and Insurance:

2012 (in millions) Country	Amount	Percentage
Mexico	\$7,076.8	9.3%
India	4,968.8	6.5%
Ireland	4,756.3	6.2%
United Arab Emirates	4,240.5	5.6%
All Other	55,346.5	72.4%
Total	\$76,388.9	100.0%

12. Other Liabilities

(in millions)	FY 2012	FY 2011
Current		
Funds Held Pending Application	\$470	\$33.1
Administrative Expenses Payable	10.4	8.6
Miscellaneous Accrued Payables	1.5	1.9
Non-Current		
Deferred Revenue	504.1	833.1
Total Other Liabilities	\$563.0	\$876.7

As of September 30, 2012, and September 30, 2011, \$504.1 million and \$833.1 million, respectively represent deferred revenue in the form of offsetting collections which are available to cover administrative expenses and program costs.

14. Commitments and Contingencies

Pending Litigation

As of September 30, 2012, Ex-Im Bank was named in several legal actions, virtually all of which involved claims under the guarantee and insurance programs. It is not possible to predict the eventual outcome of the various actions; however, it is management's opinion that these claims will not result in liabilities to such an extent that they would materially affect the financial position or results of operations of Ex-Im Bank.

RELATED DISCLOSURES IN CFR

None

FARM CREDIT SYSTEM INSURANCE

FARM CREDIT SYSTEM INSURANCE CORPORATION

WWW.FCSIC.GOV

BRIEF SUMMARY OF PROGRAM

The Farm Credit System Insurance Corporation was established by the Agricultural Credit Act of 1987 as an independent U.S. Government controlled corporation. The Corporation's primary purpose is to ensure the timely payment of principal and interest on insured notes, bonds, and other obligations issued on behalf of Farm Credit System banks.¹ The mission is to: protect investors in insured Farm Credit System obligations and taxpayers through sound administration of the Farm Credit Insurance Fund, exercise its authorities to minimize Insurance Fund loss, and help ensure the future of a permanent system for delivery of credit to agricultural borrowers.

The Farm Credit System Insurance Corporation (FCSIC) insures the timely payment of principal and interest on the debt securities issued jointly by the five Farm Credit System Banks (Systemwide Debt Securities). The Federal Farm Credit Banks Funding Corporation acts as agent for the five banks in issuing and marketing the Systemwide Debt Securities to the public. The Insurance Fund represents the Corporation's equity, the difference between total assets and total liabilities, including insurance obligations. The Insurance Fund is comprised of an unallocated Insurance Fund, assets for which no specific use has been identified or designated, and six allocated Insurance Reserves Accounts (AIRAs). There is one AIRA for each of the five system banks and one account for the Financial Assistance Corporation (FAC) stockholders.

Insurance premiums are assessed with the objective of maintaining the Secure Base Amount (SBA), defined in the Farm Credit Act as 2 percent of aggregate insured obligations reduced by 90 percent of Federally guaranteed loans and investments and 80 percent of State guaranteed loans and investments, assuming the loans are in accrual status and the investments are not permanently impaired. At yearend, any excess funds above the SBA are transferred to the AIRAs and may be subsequently paid to the account holders. The current AIRAs balance is recorded as part of the Insurance Fund and is available to satisfy insurance obligations until the Corporation disburses payments to the account holders.

The Farm Credit Administration is the safety and soundness regulator responsible for the examination, supervision, and regulation of each FCS institution. FCA is an independent agency in the executive branch of the U.S. Government and derives its broad authorities from the Farm Credit Act. These authorities include examination and enforcement authorities similar to those of commercial bank regulators. The U.S. Senate

¹ More information on the FCIC is available online at <http://www.fcsic.gov/index.html>; last accessed May 21, 2013.

Committee on Agriculture, Nutrition, and Forestry and the U.S. House of Representatives Committee on Agriculture oversee FCSIC, FCA, and the FCS.

“Protecting Investors in Agriculture and Rural America” 2011 Annual Report

RELATED LEGISLATION AND U.S. CODE (U.S.C.)

1. Agricultural Credit Act of 1987
2. Farm Credit Act
3. 55 FR 36610

SOURCES OF FINANCING

The Corporation operates with no appropriated funds. It collects insurance premiums from each System bank that issues insured obligations. These premiums and the income from the Corporation’s investment portfolio provide the funds necessary to fulfill its mission. Investors provide the funds the System lends to agriculture and rural America.²

SOURCE OF GAAP

FCSIC primarily applies generally accepted accounting principles (GAAP) issued by the Financial Accounting Standards Board (FASB). This practice is permitted by paragraph 9 of Statement of Federal Financial Accounting Standards 34, *The Hierarchy of Generally Accepted Accounting Principles, Including the Application of Standards Issued by the Financial Accounting Standards Board*.

² Source: 2011 FCSIC Annual Report <http://www.fcsic.gov/FCSIC%20Annual%20Reports.html> last accessed May 21, 2013.

SIGNIFICANT FINANCIAL STATEMENT ELEMENTS

Excerpts from FY 2012 FCSIC Annual Report³

Farm Credit System Insurance Corporation
Statements of Financial Condition
As of December 31, 2012 and 2011
(Dollars in thousands)

	<u>2012</u>	<u>2011</u>
Assets		
Cash and cash equivalents	\$ 5,079	\$ 1,101
Investments in U.S. Treasury Obligations (Note 3)	3,196,211	3,266,285
Accrued interest receivable	12,667	26,264
Premiums receivable (Note 4)	<u>84,266</u>	<u>98,699</u>
Total assets	<u>\$ 3,298,223</u>	<u>\$ 3,392,349</u>
Liabilities and Insurance Fund		
Accounts payable and accrued expenses (Note 6)	<u>\$ 287</u>	<u>\$ 385</u>
Total liabilities	<u>287</u>	<u>385</u>
Farm Credit Insurance Fund		
Allocated Insurance Reserves Accounts Allocated in 2012	0	221,851
Unallocated Insurance Fund Balance	<u>3,297,936</u>	<u>3,170,113</u>
Total Insurance Fund	<u>3,297,936</u>	<u>3,391,964</u>
Total liabilities and Insurance Fund	<u>\$ 3,298,223</u>	<u>\$ 3,392,349</u>

³ Source: FCSIC website -- <http://www.fcsic.gov/index.html> last accessed June 6, 2013.

Farm Credit System Insurance Corporation
Statements of Income and Expenses and Changes in Insurance Fund
For the years ended December 31, 2012 and 2011
(Dollars in thousands)

	<u>2012</u>	<u>2011</u>
Income		
Premiums (Note 4)	\$ 84,298	\$ 97,257
Interest income	46,842	72,616
Total income	<u>131,140</u>	<u>169,873</u>
Expenses		
Administrative operating expenses (Note 6)	3,317	3,255
Total Expenses	<u>3,317</u>	<u>3,255</u>
Net Income	<u>127,823</u>	<u>166,618</u>
Farm Credit Insurance Fund – beginning of year	<u>3,391,964</u>	<u>3,225,346</u>
Payments to AIRAs Accountholders	<u>221,851</u>	<u>0</u>
Farm Credit Insurance Fund – end of year	<u><u>\$ 3,297,936</u></u>	<u><u>\$ 3,391,964</u></u>

RELEVANT GAO REPORTS (LAST 5 YEARS)

None

RELEVANT DISCLOSURES IN AFR

Excerpts from FY 2012 FCSIC Annual Report⁴

Liability for Estimated Insurance Obligations—The liability for estimated insurance obligations is the present value of estimated probable insurance payments to be made in the future based on the Corporation's analysis of economic conditions of insured System banks.

The insured System banks' primary lending markets are borrowers engaged in farming, ranching, and producing or harvesting of aquatic products, and their cooperatives. Financial weaknesses in these market segments and the effect of general market conditions on the System's borrowers could adversely affect the banks' financial condition and profitability. Insured System banks also face risks from changing interest rate environments and the need to maintain ongoing access to financial markets. Adverse changes in the financial condition and profitability of insured System banks resulting from increased levels of credit, financial, or other risks could occur in the future which would have a material effect on the liability for estimated insurance obligations.

The Corporation actively monitors the creditworthiness and financial position of the insured System banks. Management is not aware of any events or circumstances at this time which would require a liability for estimated insurance obligations to be recorded.

⁴ Source: FCSIC website -- <http://www.fcsic.gov/index.html> last accessed June 6, 2013.

The Farm Credit System

Structure and Funding

The Farm Credit System (System or FCS) is a federally chartered network of cooperative lending institutions owned by the agricultural and rural customers it serves, including farmers, ranchers, producers or harvesters of aquatic products, agricultural cooperatives, and farm-related businesses. As of December 31, 2012, the System had four banks and 82 associations. Each of the associations has its own chartered territory and is affiliated with one of the four banks.

Each association receives wholesale funding from its affiliated bank and lends directly to its owner-borrowers, providing a consistent and reliable source of agricultural and rural credit throughout the United States and the Commonwealth of Puerto Rico. CoBank also has nationwide authority to make retail loans to cooperatives and other eligible entities.

The banks obtain funds for their operations primarily through the sale of Federal Farm Credit Banks Consolidated Systemwide debt securities. The banks own and utilize the Federal Farm Credit Banks Funding Corporation to issue Systemwide debt securities in the capital markets. As the fiscal agent for the banks, the Funding Corporation partners with a select group of dealers to market and distribute the securities to investors throughout the world to finance the System's operations.

Combined Farm Credit System Statistics

(Dollars in Billions)

	2012	2011	2010
Insured Debt Outstanding ¹	\$ 197.5	\$ 184.2	\$ 188.3
Production Agriculture:			
Real Estate Mortgage Loans	88.3	80.7	78.0
Production and Intermediate-term Loans	43.9	41.3	40.6
Agribusiness Loans ²	27.1	24.7	29.6
Communication Loans	4.2	3.8	3.6
Energy, Water and Waste Disposal Loans	14.5	11.8	11.5
Rural Residential Real Estate Loans	6.2	5.8	5.5
International Loans	4.7	3.8	4.0
Lease Receivables	2.4	2.1	2.0
Loans to Other Financial Institutions	0.7	0.6	0.5
Cash and Investments	46.9	47.3	46.3
Net Income	4.1	3.9	3.5
Nonperforming Loans as a Percentage of Total Loans	1.4%	1.7%	1.9%

1. Insured debt outstanding is based on System institution Call Report information and reflects the book value of insured debt outstanding, excluding fair value adjustments, plus accrued interest as of December 31, 2012.
2. As of December 31, 2012, agribusiness loans consisted of loans to cooperatives of \$12.8 billion, processing and marketing loans of \$11.5 billion, and farm-related business loans of \$2.8 billion.

Insured and Other Obligations

FCSIC insures Systemwide and consolidated bonds, notes, and other obligations issued by System banks through the Federal Farm Credit Banks Funding Corporation under section 4.2 (c) or (d) of the Farm Credit Act. Figure 1 shows that insured debt outstanding increased by 7.2 percent in 2012 to \$197.5 billion. This is in contrast to a 2.2 percent decrease in insured debt outstanding in 2011.

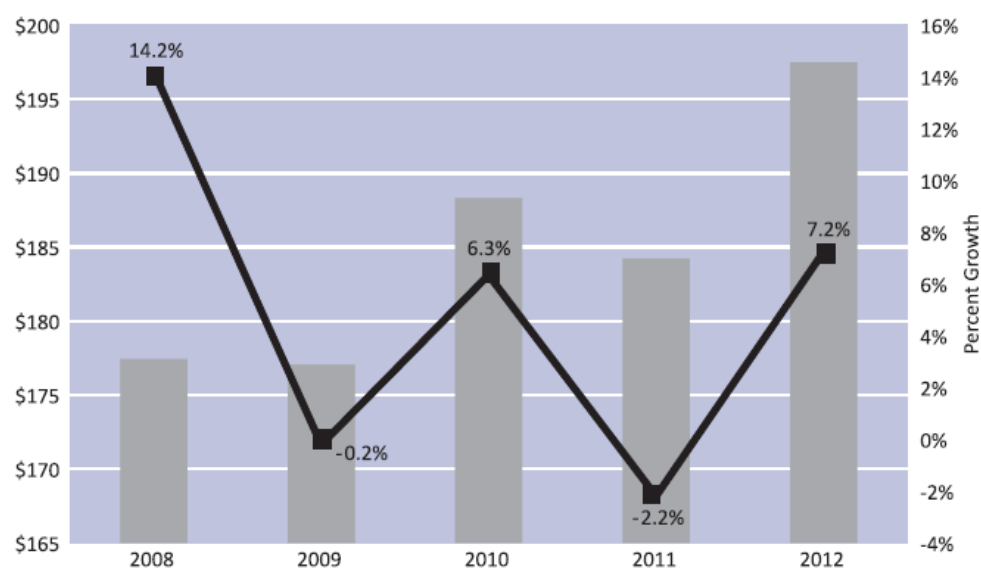
FCSIC must also ensure the retirement of eligible borrower stock at par value, as required by section 4.9A of the Farm Credit Act. This stock, also known as protected borrower stock, was outstanding prior to October 6, 1988. At year-end 2012, protected borrower stock outstanding at System institutions totaled \$2 million, down from \$5 million at year-end 2011.

Figure 1

Insured Debt Outstanding

Growth Averaged 5.1 Percent Over the Past 5 Years

(Dollars in Billions)



Note: Insured debt outstanding is based on System institution Call Report information and reflects the book value of insured debt outstanding, excluding fair value adjustments, plus accrued interest as of December 31, 2012.

Farm Credit System Capital

The primary source of funds to repay insured Systemwide debt securities is the System's borrowers. Each borrower must have a minimum net worth and, in most cases, collateral posted in connection with his or her loan. The borrower makes payments on the loan to the lending bank or association.

The lending association in turn makes payments on its loan to the lending bank. Both the banks, which ultimately repay Systemwide debt securities, and the associations exceed their minimum regulatory capital requirements as protection and support for the repayment of the outstanding insured debt.

If a bank were unable to repay its portion of an insured Systemwide debt obligation, the Corporation would use the Insurance Fund to make that payment. Since the repayment of Systemwide debt securities is the joint and several obligation of the banks, in the event the assets of the Insurance Fund were exhausted, the provisions of joint and several liability of all banks would be triggered, which means the financial resources of the other banks would be used to repay the defaulting bank's portion of the debt issuance.

As figure 2 shows, the amount of FCS bank capital and the balance in the Insurance Fund together increased 41 percent, from \$12.4 billion at year-end 2008 to \$17.5 billion at year-end 2012. Bank capital plus the amount in the Insurance Fund as a percentage of insured debt outstanding decreased from 9.1 percent in 2011 to 8.9 percent in 2012 (see figure 3). Over the past several years, the System banks have reported strong earnings primarily from their ability to re-price debt at favorable rates in the low-interest rate environment. Between 2009 and 2011, the banks retained a significant portion of their earnings to boost capital levels. In 2012, the System's loan growth outpaced its capital growth, causing a slight decline in bank capital as a percentage of insured debt.

Overall, the financial performance and condition of the System on a consolidated basis remains strong, though some individual institutions continue to experience stress from credit deterioration in certain agricultural sectors and from continued stress in the general economy. (See trends in the Financial Institution Rating System in the "Risk Management" section beginning on page 23.)

System associations have boosted capital levels through the net income they have earned and retained. Association capital helps reduce the credit exposure of the association's direct loan with its affiliated bank. As figure 4 shows, from 2008 to 2012, combined association capital increased \$7.4 billion or 38.7 percent, with an annual average increase of approximately 8.6 percent. Since 2008, the associations have collectively achieved solid earnings and preserved capital, causing association capital as a percentage of total assets to steadily increase to 17.8 percent in 2011 and 2012 (see figure 5).

Figure 3

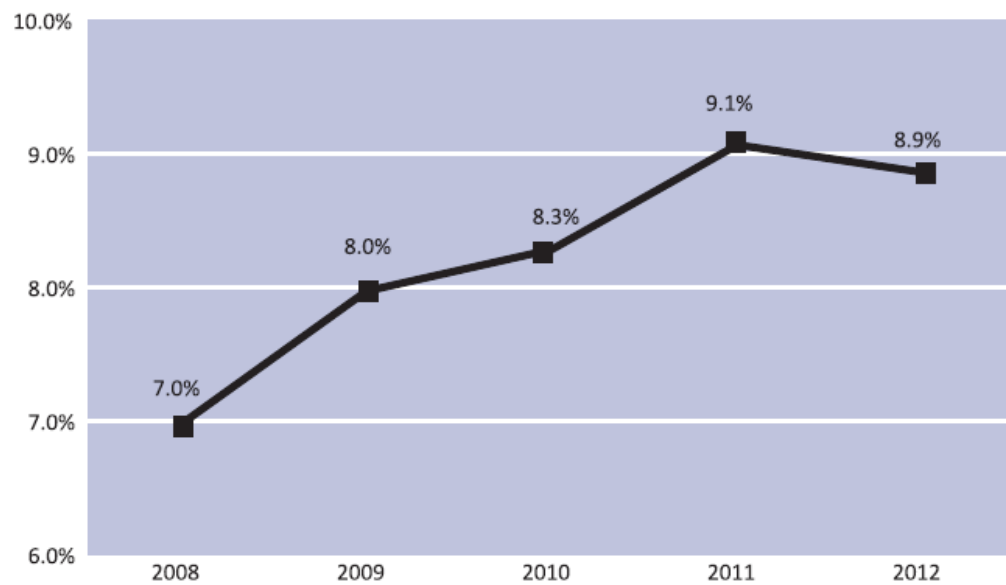
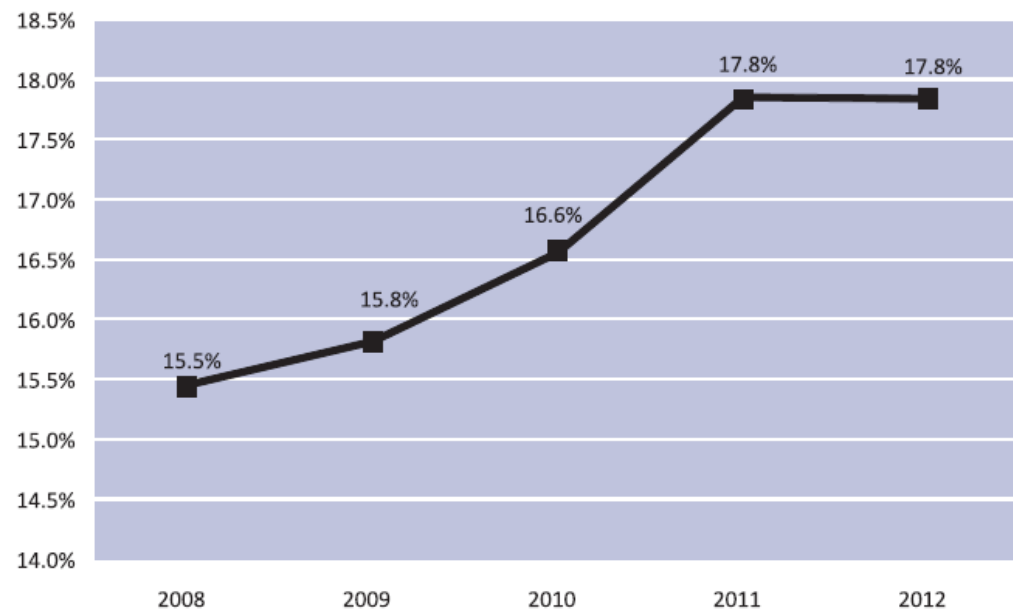
Bank Capital Plus Insurance Fund as Percentage of Insured Debt

Figure 5

Combined Association Capital as a Percentage of Total Assets

Additional Protections

Farm Credit System banks have additional risk management tools to protect investors. One such tool is the Contractual Interbank Performance Agreement (CIPA). All System banks have entered into this agreement, which measures the financial condition and performance of each bank by using ratios that consider bank capital, asset quality, earnings, interest rate risk, and liquidity. The CIPA financially penalizes banks that do not meet performance standards.

The System and the Federal Farm Credit Banks Funding Corporation have also entered into the Market Access Agreement, which establishes conditions for each bank's continued participation in the debt market. If a bank fails to meet agreed-upon performance measures, including capital and collateral ratios, the bank may be restricted from issuing debt. The criteria used under the Market Access Agreement are the CIPA scores and the net collateral and permanent capital ratios.

The System entered into a common minimum liquidity standard in 2010 to improve the quality and quantity of bank liquidity reserves. This standard is designed to maintain and ensure adequate liquidity to meet the business and financial needs of each bank and the System in the event access to the debt market is temporarily impeded.

In April 2013, the Farm Credit Administration issued a final liquidity rule that strengthens the banks' liquidity reserve requirement, promotes liquidity risk management best practices, and better prepares the banks to withstand a liquidity crisis. For additional information on bank liquidity, see the discussion in the "Risk Management" section of this report.

Insurance Fund Management

The Insurance Fund and the Secure Base Amount

The Farm Credit Insurance Fund represents FCSIC's equity, the difference between total assets and total liabilities, including insurance obligations. The Insurance Fund is composed of an unallocated Insurance Fund (the assets in the Insurance Fund for which no specific use has been identified or designated) and an allocated Insurance Fund (assets transferred to the AIRAs). Premiums are due until the unallocated portion of the Insurance Fund reaches the secure base amount.

The secure base amount established by the Farm Credit Act of 1971, as amended, is 2 percent of the aggregate outstanding insured obligations (adjusted to exclude 90 percent of Federal Government-guaranteed loans and investments and 80 percent of State Government-guaranteed loans and investments), or another percentage that FCSIC determines to be actuarially sound to maintain in the Insurance Fund, taking into account the risk of insuring outstanding insured obligations.

In 2012, both the total Insurance Fund and total assets declined by 2.8 percent to \$3.30 billion as a result of AIRA payments of \$221.9 million. Insured debt outstanding grew \$13.4 billion in 2012 (7.2 percent). The Insurance Fund finished 2012 at 1.93 percent, which was \$119.1 million below the secure base amount (see figure 6). Consequently, no excess funds were available for allocation to the AIRAs at year-end.

At year-end 2011, \$221.9 million, the calculated excess amount in the Insurance Fund, was transferred to the AIRAs. In April 2012, after completion of our year-end audit, the Board of Directors authorized the payment of the \$221.9 million to the account holders. Payments were made in May 2012. (See Note 4 to the Financial Statements for additional details.)

Over the past five years, the total Insurance Fund and total assets each grew at an annual rate of 5.1 percent. We did not accrue a provision for insurance obligations in 2012.

Risk Management

FCSIC monitors and manages insurance risk to minimize the Farm Credit Insurance Fund's exposure to potential losses. Our staff analyzes and evaluates the financial performance and condition of System institutions, maintains continual dialogue with Farm Credit Administration examiners, and reviews reports of examination. When necessary, we request special examinations at System institutions of concern. On a quarterly basis, we screen all System institutions against key performance criteria to identify those institutions that may pose increasing insurance risk.

We also assess risk to the Insurance Fund by

- reviewing corporate actions (such as mergers, restructurings, and other corporate changes) approved by FCA for System institutions;
- monitoring legislative, judicial, regulatory, and economic trends that could adversely affect the agricultural or financial services industries;
- using analytical models; and
- participating as a nonvoting member on FCA's Regulatory Enforcement Committee.

During 2012, risk management staff monitored and evaluated trends and other information affecting agriculture and System institutions, including

- conditions in the global and domestic economy, capital markets, and the agricultural and financial sectors;
- trade policy and Government programs that support U.S. agriculture;
- the effects of commodity price volatility on agricultural operations and farmland values in the Midwest;
- the prolonged effects of the housing crisis on agricultural real estate values in certain regions of the country;
- stress in several farm sectors affecting the quality of System institutions' loan portfolios, including the dairy, swine, poultry, forestry, nursery, and biofuels industries;
- negative trends at specific System institutions with declining Financial Institution Rating System ratings; and
- the performance and condition of the four System banks.

RELATED DISCLOSURES IN CFR

None.

TAB A - ATTACHMENT II:
KPMG Government Institute
Report – *Federal Credit
Reform: Is it a sleeping
giant?*



KPMG GOVERNMENT INSTITUTE

Federal Credit Reform: Is it a sleeping giant?

AUDIT





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Federal Credit Reform: Is it a sleeping giant?

Introduction

The Federal Credit Reform Act of 1990 (FCRA) was passed into legislation in 1990 as part of the Omnibus Budget Reconciliation Act of 1990. This law was established consistent with the Chief Financial Officers Act of 1990 (CFO Act) legislation that provided the foundation for comprehensive reform of Federal financial management and reporting. The CFO Act created the Chief Financial Officer position in the Federal government and financial reporting requirements for Federal agencies. Given these initiatives, the FCRA set out to prescribe the requirements to address accounting and reporting requirements of Federal credit programs so that the long-term costs were adequately captured and reported in the Federal budget and government-wide financial statements.

These pieces of legislation, coupled with additional laws and other requirements in the immediate years that followed, ushered in an era of government accountability through financial reporting, which continues to evolve to this day.

Fundamentally, the purpose of the FCRA is to measure more accurately the cost of Federal credit programs. The intention of the FCRA was for Federal agencies to be able to more accurately measure the long-term costs of Federal credit programs and, as a result, allow the Federal government to better budget for future outlays and allocate resources among credit and other programs.¹

The KPMG Government Institute sponsored the development of this white paper for the purpose of providing a historical perspective of the FCRA, including how its programs have evolved since 1990, a discussion of some of the key credit reform concepts, and importantly, the issues and audit challenges for federal financial professionals in the future.

¹ Specifically, Sec. 501 of the FCRA states that the purpose of the Act is to: (1) Measure more accurately the costs of Federal credit programs; (2) Place the cost of credit programs on a budgetary basis equivalent to other Federal spending; (3) Encourage the delivery of benefits in the form most appropriate to the needs of beneficiaries; and (4) Improve the allocation of resources among credit programs and between credit and other spending programs.

About the KPMG Government Institute: The KPMG Government Institute was established to serve as a strategic resource for government chief financial officers seeking to achieve high standards of accountability, transparency, and performance. The Institute is a forum for ideas, a place to share leading practices, and a source of thought leadership as a catalyst to help governments address difficult challenges.

Background: The Federal Credit Reform Act of 1990

Since its inception, the FCRA substantially changed the financing, accounting, and reporting for Federal loans and loan guarantees and, as a result, allowed Federal financial managers to make informed budgetary decisions concerning the cost and programmatic aspects of these programs. In a sense, these measures provided a better allocation of budgetary resources for Federal government credit programs, that enabled major business segments in the United States to gain access to credit that was not easily accessible through non-Federal financial institutions. Federal credit programs are essential for our economy because they directly support the housing, small business, educational, agricultural, and financial banking sectors as noted by the recent events affecting our nation's economy. Over the years since passage of the FCRA, Federal credit programs have steadily grown in popularity and size, and in recent years have been one of the main tools used by the Federal government to provide economic stimulus to the American economy. The use of these programs generally since the FCRA was passed, and more recently to spur economic growth, is not widely known to the citizenry or to those who benefit from them. However, Federal credit reform programs continue to be a growing component of the Federal budget. Given the slow, steady, and silent growth of Federal credit programs, could this be a sleeping giant?

Prior to the passage of the FCRA, Congress and Federal agencies accounted for direct loans and loan guarantee programs using the

"Cash Basis of Accounting." A loan was recognized when disbursed and no accrual was recorded for the long-term cost. Similarly, in the case of loan guarantees, the cost of these programs was not recognized until a borrower loan default occurred. In many cases, loan defaults for both direct loans and loan guarantees occurred many years after origination. Since anticipated defaults were not recognized when the loans and loan guarantees were initially recorded, it resulted in billions of dollars in losses for which no budgetary resources were allocated, creating a deficit that future generations of taxpayers were required to finance. In addition, the Federal government had no effective and reliable means to determine whether these programs were in fact serving the purpose for which they were created. Given these shortcomings, it is not surprising that reform over Federal loans and loan guarantees was necessary.²

Another element of the FCRA was the implicit subsidy created by these programs to assist borrowers by enabling them to acquire loans at below-market rates. The Federal government was able to finance the credit program operations by issuing Treasury notes, bonds, or other securities while paying the prevailing market interest rates. The borrowings represent an additional cost to the Federal government, as the government will in turn loan monies through Federal credit programs to the borrowers at a much lower interest rate (this is typically considered an interest rate differential). This interest subsidy—the difference

between lower loan interest rate and the higher market interest rates—is another layer of cost to the government. Given the obvious problems associated with using the Cash Basis of accounting to record these Federal credit program transactions, the FCRA brought about the requirement for the Federal credit agencies to recognize the up-front, full cost of a direct loan or loan guarantee, which includes, among other costs, estimated defaults and the interest rate differential.³ The reason for this accounting and budgetary treatment is that fundamentally the true cost of the loan instrument should be recognized in the year the loan is disbursed or the guarantee issued, even though the life of the loans extends over many years, thereby providing for a better matching of benefits and resources used. It also provides Federal credit agencies a means of measuring the budgetary costs of these programs, thereby providing the means to better manage budgetary resources.

The FCRA gives authority to the Office of Management and Budget (OMB), to provide oversight over FCRA programs. OMB Circular A-11, *Preparation, Submission, and Execution of Budget, Section 185, Federal Credit*, requires that Federal agencies' accounting and budgeting activities be recorded in accordance with the FCRA. OMB Circular A-11 is one of the most critical pieces of Federal credit program guidance, as it defines the requirements to formulate and annually reestimate subsidy rates used to measure the long-term cost of these programs to the government.

² The Federal government still carries pre-credit reform loans, or "liquidating loans" as they are commonly termed. These loans precede loans issued after October 1, 1991. The balances diminish each year as more collections are received. By their nature, there are no additional loan or guarantee disbursements/issuances.

³ Source: *Federal Accounting Handbook*, by Cornelius E. Tierney, and published by John Wiley and Sons Inc., Chapter 1, "Financial Management Legislation and Policy, Federal Credit Reform Act of 1990."

Evolution of Federal Credit Programs

Federal credit programs have evolved significantly over time. Changes to program requirements have added complexities to the accounting operations of many Federal agencies and in turn has increased the complexities of financial reporting and the related agency audits.

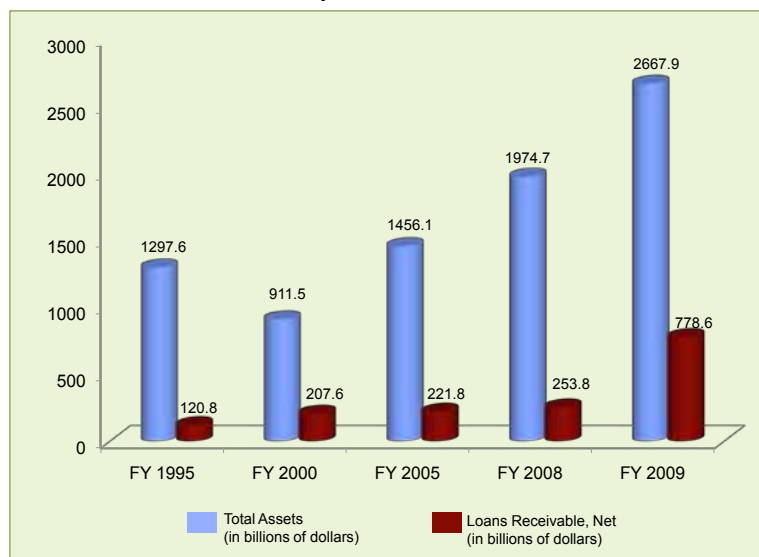
Direct Loans

The Federal government has in past years committed significant financial resources to credit programs aimed at assisting homeowners, students, small businesses, disaster victims, and farmers, among others. If we look at the government-wide financial statements at various points in time, the increase in relative significance of credit programs to other government-wide assets becomes evident. For instance, Chart 1 below, *Government-wide Comparison of Loans Receivable to Total Assets*, shows that net direct loan receivables have steadily increased since 1995, with the most dramatic increase between fiscal

year 2008 and 2009.⁴ If we consider the trajectory of the loan portfolio over time, the increments from 1995 to 2008 illustrate the general relevance of Federal credit programs in housing, education, small business, and other sectors of our economy. The increment from 2008 to 2009 can be explained by the impact on our economy of the recession that began at the end of 2007 and the financial crisis that ensued near the end of fiscal year 2008. It was due to these economic events that the Federal government supplied significant amounts of budgetary resources to help improve the financial credit market liquidity and the nation's overall economy.

⁴ The largest component of the Government-wide Loans Receivable is direct loans. The FCRA defines direct loans as a disbursement of funds by the government to a non-Federal borrower under a contract that requires the repayment of such funds with or without interest. The term includes the purchase of, or participation in, a loan made by another lender and financing arrangements that defer payment for more than 90 days, including the sale of a government asset on credit terms. The term does not include the acquisition of a Federally guaranteed loan in satisfaction of default claims or the price support loans of the Commodity Credit Corporation.

Chart 1: Government-wide Comparison of Loans Receivable to Total Assets

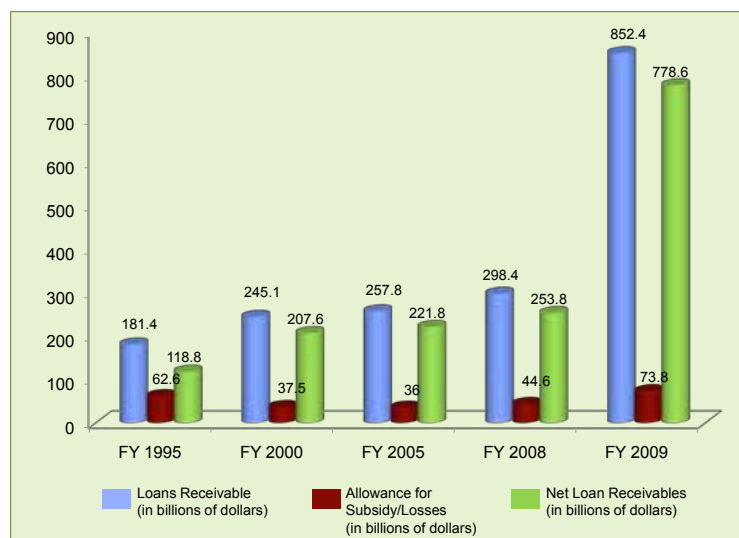


(Source: FY 1995, 2000, 2005 and 2009 Government-wide Financial Statements.)

A more detailed comparison showing the trend in the government-wide direct loans receivable portfolio since 1995 is illustrated below in Chart 2, *Government-Wide Comparison of Direct Loans Receivable and Allowance for Subsidy/Losses*. In Chart 2, the allowance for subsidy/losses stayed relatively unchanged from 1995 to 2008. The allowance increased nominally in 2009 relative to prior years while the direct loan receivable amounts almost tripled during that same time. The increment in fiscal year 2009 is attributed to the purchases by the U.S. Department of Treasury of various investments (e.g., mortgage backed securities) as part of the Housing and Economic Recovery Act of 2008 (HERA) and the Economic Emergency Stabilization Act of 2008 (EESA), that created the Troubled Asset Relief Program (TARP), allowing the Federal government to acquire the so-called “toxic assets” from the financial sector to increase liquidity in the credit

markets. In accordance with the HERA and EESA, the loans purchased were accounted for as direct loans under the FCRA. The relatively small increment in the related allowance for subsidy may be attributed to the expected long-term value of these assets from which the Federal government expects to collect a substantial portion of the face value of these investments, including interest. The fact that the Federal government has the capability to hold these investments indefinitely represents an important distinction between the Federal government and banking institutions. The expediency with which investments flow in the financial markets and the immediate liquidity requirements of financial institutions make it impossible for financial institutions to hold investments for long periods. The ability for banks to “move the paper” is crucial for their survival and overall financial market liquidity.

Chart 2: Government-wide Comparison of Direct Loans Receivable and Allowance for Subsidy/Losses



(Source: FY 1995, 2000, 2005 and 2009 Government-wide Financial Statements.)

Loan Guarantees

The Federal government permits borrowers to obtain loans from private lenders in which the latter, for a fee, receive a guarantee against borrower default from the Federal government. The guarantee can either be a certain percentage or the full face amount of the loan disbursed by the lender.⁵ The budgetary cost of the loan guarantee to the government (or the Federal government's obligation to provide the guarantee) must be recognized before the loan is disbursed by the lender. At the time the loan is disbursed by the lender, the Federal government recognizes the cost (subsidy expense). One of the most important aspects related to cost for

⁵ According to the FCRA, loan guarantees are defined as any guarantee, insurance, or other pledge with respect to the payment of all or a part of the principal or interest on any debt obligation of a non-Federal borrower to a non-Federal lender, but does not include the insurance of deposits, shares, or other withdrawal accounts in financial institutions.

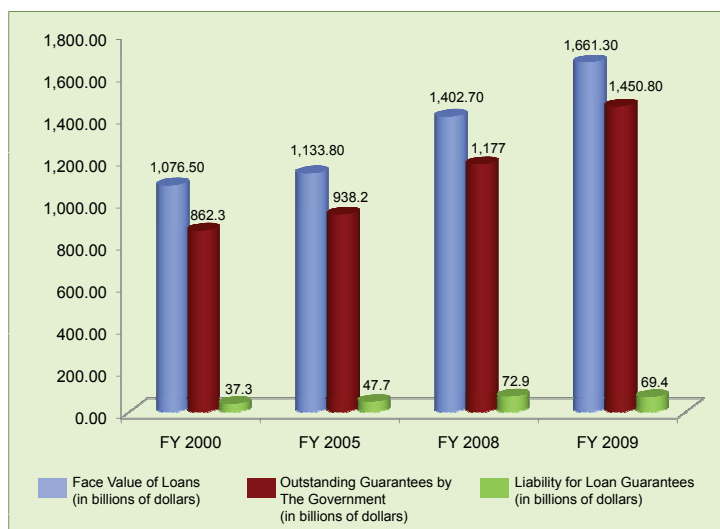
this type of program is the estimated exposure to the Federal government as a result of future loan defaults. This estimated future cost is recognized as a liability for loan guarantees in the Federal government-wide balance sheet.

Although the balance sheet of the Federal government does not carry a substantial liability for loan guarantees, \$69.4 billion as of September 30, 2009, the outstanding value of loans guaranteed as of September 30, 2009 was \$1,450.8 billion, a figure that is almost twice the amount of the government-wide portfolio of direct loans (\$778.6 billion as of the same date). A comparison of Chart 2, on page 8, and Chart 3 below, *Government-wide Comparison of Liability for Loan Guarantees, Face Value of Guarantees, and Outstanding Loan Guarantees*, illustrates this difference.

The ability to assess the Federal government's exposure on the loan guarantee portfolio is one of the key challenges financial managers at Federal agencies

and independent auditors must face every year during the financial statement audit and budget submission process. This is necessary to ensure that program activities are accounted for under the provisions of the FCRA, and that these liabilities are properly valued in the financial statements and represented in the President's budget. For instance, at the individual agency level, the challenge is to assess the reasonableness of the liability for loan guarantees in the financial statements relative to the total guarantees outstanding. As noted in the Federal government-wide financial statements, the liability in the balance sheet in the amount of \$69.4 billion is nominal compared to the \$1,450.8 billion of total guaranteed loans outstanding. Therefore, it is critical for both financial managers and auditors to determine if the liability in the financial statements adequately represents the level of exposure based on the total guarantee portfolio.

Chart 3: Government-wide Comparison of Liability for Loan Guarantees, Face Value of Guarantees, and Outstanding Loan Guarantees



(Source: FY 2000, 2005 and 2009 Government-wide Financial Statements.)



Given the range of values presented in the previous charts, it is evident that Federal credit programs play a significant role in Federal government operations both in prosperous and diminished economic times. Consider the following question, taking into consideration the unprecedented increase in direct loans and loan guarantees during the past two years as the country headed into the recession: *Would the U.S. economy and financial markets be able to survive without the unprecedented help from the Federal government in recent times?* Evidently, the role of the Federal government has been crucial in rescuing the nation during this time of crisis, as noted by the level of financial resources committed since the end of fiscal year

2008 and the fact that in some sectors there are signs of recovery. The government implications go far beyond the dollars funneled to struggling organizations and the financial markets. The Federal government's actions have increased the Federal deficit and created widespread discussions among the citizenry and the media concerning the fiscal well-being of the nation. There are concerns regarding the deficit pressure resulting from the financial bailout, especially at a time when entitlement program obligations—Social Security, Medicare, and Medicaid—represent significant unfunded obligations that by the end of this decade will most certainly cause the Federal deficit to exponentially increase.



Impact on the Federal Government and the Economy

In several recent speeches about how to reduce the unemployment rate, currently close to 10%, President Obama emphasized the importance of small businesses having access to credit, as small businesses, including restaurants, manufacturing companies, and service organizations are the driving force of the economy. For example, with a series of loan guarantee programs, the U.S. Small Business Administration (SBA) has been at the forefront of the Administration's initiatives to jumpstart the economy by assisting small-business owners to achieve their business goals. In the past, many small businesses have benefited from SBA's programs and over time have evolved into large companies and household names, including: Hewlett Packard, Federal Express, Staples, Under Armour, Intel, and Sun Microsystems. Furthermore, some SBA loan guarantees are pooled, securitized, and sold in the secondary market, providing additional liquidity to banks and enabling them to make additional loans directly contributing to American small

businesses. Also, through the SBA Disaster Loan Program, SBA assists thousands of disaster victims through a series of loan products with favorable terms, allowing families and businesses alike to recover from natural disasters. For instance, as a result of Hurricane Katrina, SBA provided an unprecedented level of aid to disaster victims. While SBA's numbers do not represent a substantial portion of the loans receivable and loan guarantee portfolios at the government-wide level, its role in our economy and society is nonetheless significant.

The Federal Student Direct Loan Program (Direct Loan) and Federal Family Education Loan Guarantee Program (FFELP), administered by the U.S. Department of Education, help thousands of students across the country to pursue higher education, which is at the heart of developing our nations' future leaders and professionals. The commitment of the Federal government to these programs is impressive. As of September 30, 2009, the Direct Loan and FFELP represented \$234.2 billion, or 30%, and \$20.6 billion, or 30%, of the total net loans receivable and loan guarantees, respectively.

The U.S. Department of Agriculture (USDA), through its various direct loan and loan guarantee programs for rural development, water and environment, food aid, telecommunications, and farm aid, help improve the quality of life in Rural America. In addition, through substantial subsidies provided to the agriculture industry, the Federal government, through these various programs, has significant influence on the pricing of agriculture commodities in global markets. The total portfolio of USDA direct loans represents \$84.1 billion or 11% of the total government-wide net loan receivable portfolio, and the guarantee program represents \$1.7 billion or 2.4% of the total government-wide loan guarantee portfolio. Other well established major Federal credit program agencies include the U.S. Department of Housing and Urban Development, U.S. Veterans Administration, and the U.S. Export and Import Bank. In addition to these long-standing programs, there are now a host of newly created Federal credit programs. For instance, as part of the American Recovery and Reinvestment Act of 2009 (ARRA), the U.S. Department of Energy is currently in the beginning stages of developing

and implementing new Federal credit programs to create incentives for the development of alternative sources of energy. According to the U.S. Department of Energy Web site, approximately \$4 billion of ARRA funds were provided to support up to \$32 billion in loans and loan guarantees for clean energy projects.

However, in the past two years, the most innovative credit programs, developed out of the necessity to alleviate the financial crisis and improve the nation's economy, were the result of legislative efforts that created HERA, EESA, TARP, and the ARRA.

Federal Government's Role during the Financial Crisis

The financial crisis started with the collapse of the real estate property values toward the end of 2007. This was also the period most economists identified as the starting point of the market contraction that led to the beginning of the recession in 2008. The downturn in the real estate market triggered a series of events during fiscal year 2008 that exposed significant vulnerabilities in our financial sector. Essentially, the financial sector was negatively impacted due to what appears to be overvalued investments linked to subprime mortgages during the housing boom (years 2000 to 2006). Also, innovative investment products introduced into the financial markets, particularly in the United States during the housing boom years, produced a series of complex investments that spread throughout the global economy. However, the regulation necessary to provide oversight to these markets did not evolve at the same time and at the same rate. In a sense, the global

nature of the financial market crisis made the problem more difficult to manage. The U.S. regulatory system of controls was not fully prepared to provide the oversight necessary to monitor a new and significantly more complex financial market. When it became evident that investment values in the primary and secondary markets were considered inflated, relative to what the market would bear, it negatively impacted the entire global financial sector by substantially limiting the availability of credit. Interbank lending and the availability of credit to finance capital and business operations were brought to a halt and, as a result, worsened the recession.

Toward the end of fiscal year 2008, the financial crisis approached dangerous levels for the U.S. economy as Fannie Mae and Freddie Mac were put into conservatorship, Lehman Brothers failed, and American International Group (AIG), among other financial institutions, suffered severe financial distress, giving rise to the need for Federal government bailouts. The downward spiraling economy required Federal government action in order to establish confidence, help stabilize financial markets, and to rescue our nation's financial system from what appeared to be imminent collapse.

Housing Economic Recovery Act of 2008

HERA was enacted in July 2008, for the purpose of establishing a new regulatory agency, the Federal Housing Finance Agency (FHFA), authorized to regulate the housing Government Sponsored Enterprises (GSEs), Fannie Mae, Freddie Mac, and the Federal Home Loan Banks (FHLB). The regulatory authority placed on the FHFA allowed it to impose

minimum capital requirements and to monitor and guide the business activities of the GSEs. In addition, HERA provided authority to the U.S. Department of Treasury (Treasury) Secretary to purchase obligations and other securities issued by the GSEs. This authority to purchase expired on December 31, 2009.

As a result of actions taken by the FHFA, two of the GSEs were placed in conservatorship in September 2008 to preserve the GSEs assets and restore these organizations to a healthy and solvent financial condition. Under the authority granted the Treasury Secretary, the Treasury purchased a substantial number of securities from the GSEs. The securities were fundamentally Mortgage Backed Securities (MBS) of the best branches, or classes, held by the GSEs. The MBS purchased were accounted for under FCRA. At September 30, 2009, the balance of MBS, including a positive allowance for subsidy of \$11.1 billion was \$184 billion. This indicates that as of September 30, 2009, on a long-term basis, Treasury estimates the MBS purchase program under HERA will generate a positive cash flow, i.e., there will be no net cost to the government.

Emergency Economic Stabilization Act of 2008

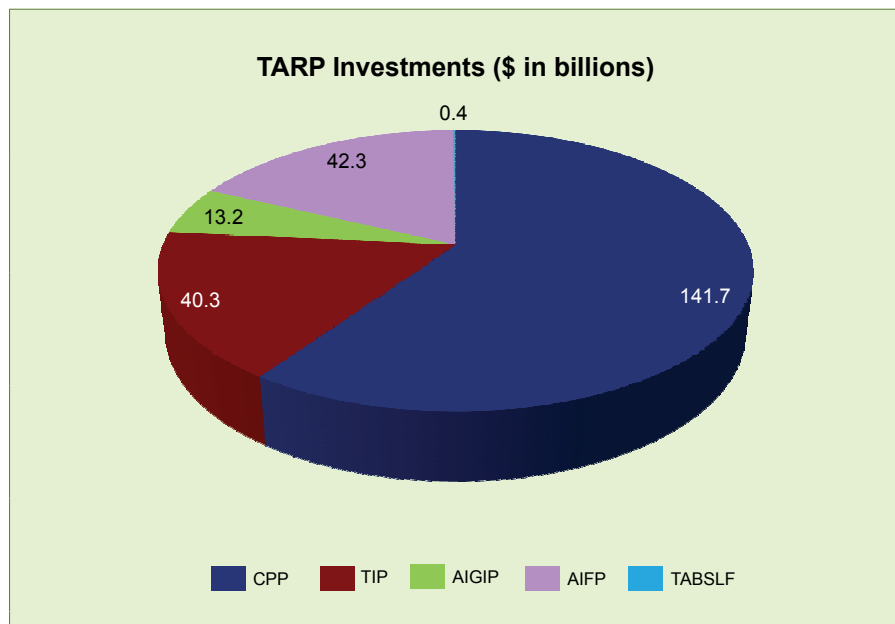
As a result of the failure of Lehman Brothers and the significant liquidity problems at AIG and other financial institutions, investor confidence quickly diminished to the lowest levels in recent history, bringing the entire financial system to near collapse. As a result, EESA was enacted. The most significant provision of this legislation was the creation of the

TARP. This program granted authority to the Treasury Secretary to provide liquidity and stability to the U.S. financial system. It also created the Office of Financial Stability (OFS) within Treasury to oversee and manage the TARP programs. At the heart of the TARP was the belief that this program would provide the quickest path to restoring market confidence.

The EESA provided budget authority for the TARP to purchase or guarantee troubled assets up to \$700 billion. According to the OFS, Agency Financial Report for fiscal year 2009, through these purchases and guarantees, OFS intended to free up credit in the financial system by funneling billions of dollars through its investment purchases and guarantees. Through this capital infusion, it expected to create the liquidity needed to stabilize the financial markets. OFS expects the investment purchases and guarantees to be substantially repaid over time.

As of September 30, 2009, the OFS disbursed approximately \$364 billion of the \$700 billion authorized. Of the \$364 billion, approximately \$73 billion was repaid during fiscal year 2009. The estimated value of the investments, including the related subsidy allowance of \$53.1 billion, was \$237.9 billion, as of September 30, 2009. The investments held at September 30, 2009 were related to the following programs: Capital Purchase Program (CPP), Targeted Investment Program (TIP), AIG Investment Program (AIGIP), Automotive Industry Financing Program (AIFP), and the Term Asset-Backed Securities Loan Facility (TABSLF). Chart 4 below, *Composition of TARP Investments*, depicts TARP Investments as of September 30, 2009.

Chart 4: Composition of TARP Investments



(Source: Office of Financial Stability FY 2009 Agency Financial Report)

The EESA required that the investment purchases and guarantees be valued for budget purposes in accordance with the FCRA. This accounting treatment, coupled with the FCRA requirements in HERA, resulted in the largest increase of credit reform activity in a single year since the enactment of the FCRA in 1990.

American Recovery and Reinvestment Act

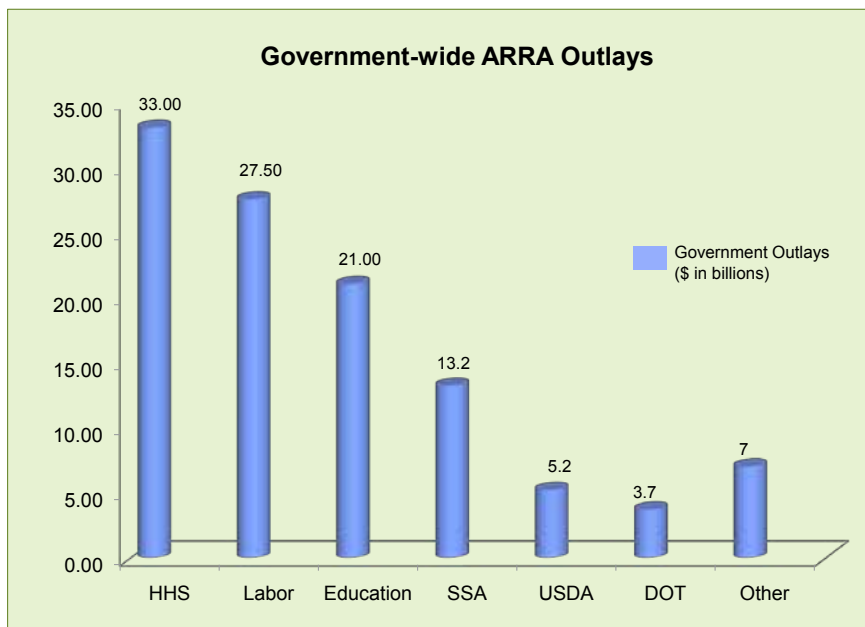
While the combined impact of the HERA and TARP was showing signs of stabilizing the credit markets, there were other areas of the economy that still needed to be restored. During most of fiscal year 2009, the recession continued to negatively impact many sectors of the economy, as evidenced by the steep increase in home foreclosures

and unemployment. The ARRA was enacted on February 17, 2009 as an additional Federal government initiative to restore our economy and save jobs. The ARRA provided a package of \$787 billion to be spread among Federal, state and local government agencies. The ARRA created new credit programs or increased the funding to existing credit programs. The ARRA was considered an unprecedented, and to some extent controversial, piece of legislation that imposed strict accountability and transparency reporting requirements on agencies administering ARRA funds.

Chart 5 below, *Government-wide ARRA Outlays*, illustrates the agencies with the largest ARRA-related outlays during fiscal year 2009.

While all funds related to ARRA shown in Chart 5 were not designated for Federal credit programs, in the case of the Department of Education, USDA, and the Small Business Administration (included in the "Other" column in the chart), most of the funds provided to these agencies under the legislation were related to new and existing Federal credit programs.

Chart 5: Government-wide ARRA Outlays



(Source: Recovery.org)



Debt and Cost of the Federal Credit Programs

The budget authority to finance Federal credit programs comes from two sources: borrowings from Treasury, and appropriations. In the case of direct loans, the borrowings, or the debt ultimately payable back to the Treasury, fund the portion of the loans that the Federal government expects to be repaid by borrowers. The portion that has a potential for default is subsidized by appropriations from Congress. The subsidy required from appropriated dollars is determined, or “estimated” at the time of loan origination in conformance with the requirements of the FCRA. The government subsidizes guarantee programs through appropriated dollars that reflect the probability of default and other costs at the time the guarantees are issued. The appropriated dollars for the loan guarantees are expensed and recognized as a liability in the balance sheet of Federal agencies. At the time of loan default, the government will use a combination of reserves created by appropriations received and borrowings to pay the default claims from private lenders. Also at the time of default, Federal agencies typically purchase the defaulted loan. These defaulted loans receivable (offset by an allowance) become assets of the Federal agency until they are either collected from borrowers or written off.

There is an important distinction to be made between the direct loan and loan guarantee programs. In the case of a direct loan program, there is an immediate outlay requiring borrowings from the government as loans are disbursed to the borrowers. In the case of a loan guarantee program, the borrowing and loan disbursement transactions are between private lenders and borrowers. The Federal government receives subsidy appropriations for potential future defaults, but the appropriations are not considered outlays until there is an actual default claim requiring the Federal agency to honor the guarantee commitment. However, the subsidy expense is recognized when the guarantee is issued, thus recognizing the probability of potential future defaults. Charts 2 and 3, presented in Section II illustrate this concept. The government-wide net loans receivable are significantly higher relative to the government-wide liability for loan guarantees. When considering this difference, it becomes evident that the deferment of outlays until default that occurs in the loan guarantee programs substantially reduces the need for Federal government resources.

The ability to properly estimate the cost of direct loan and loan guarantee programs is essential to determine if the programs will receive the required cash inflows to pay the debt to Treasury. This is the essence of the FCRA: the capability of agencies to properly estimate the risk of default and to properly budget for the resource requirements to operate Federal credit programs. During the past couple of years, borrowings substantially increased to fund the recently passed legislation. According to the government-wide financial statements for fiscal year 2009, Congress raised the debt limit twice in FY 2009—from \$10.6 trillion to \$11.3 trillion—in October 2008 with the passage of the EESA, and then again to \$12.1 trillion in February 2009 with the passage of the ARRA. In December 2009 and February 2010, the debt limit was raised again to \$12.4 trillion and \$14.3 trillion, respectively, in part to provide sufficient funding for credit program activities. However, it is important to note that at this time the Federal government has not yet used all the borrowing authority associated with EESA and ARRA. It is possible that this authority will be reprogrammed into other initiatives if the remaining borrowing authority is not used, as some of the provisions associated with these legislative actions expired on September 30, 2009.

The cost associated with Federal credit programs is estimated over long periods of time, requiring complex estimation procedures to ensure that the estimated



long-term cost of the Federal credit programs is properly budgeted and reported each fiscal year. These estimates form part of the budget requests embedded in the President's Budget (PB) each year, and eventually become an integral part of agency annual appropriations bills. As estimates extend into the outer years, it becomes increasingly difficult to predict the relative accuracy of those estimates. This has become very clear in the past decade. For instance, the government-wide financial statements as of September 30, 2000 anticipated a unified budget surplus in the amount of \$5.4 trillion (under fiscal year 2000 service baselines, which did not consider changes to taxes or spending) over the following 10 years. As of September 30, 2009, the Federal government reported a unified budget deficit of \$1.4 trillion. Situations like the September 11, 2001 attacks, the wars in Iraq and Afghanistan, and the recent recession and financial market crisis during 2008 and 2009 were not contemplated in fiscal year 2000. Similarly, it becomes increasingly difficult to estimate Federal credit program costs 10 or 20 years in the future because of unforeseen changes in the economy and the impact those changes will have on the direct loan and loan guarantee portfolios.

Estimating the Long-Term Costs of Federal Credit Programs

As noted earlier, the responsibility to provide guidance and oversight of Federal credit programs was delegated to OMB in the FCRA legislation. OMB in turn assigned the responsibility to individual Federal agencies to determine the long-term costs of these programs. The process undertaken by Federal credit agencies can be separated into two main activities: formulation

of initial subsidies represented by a formulation subsidy rate, and an annual reestimate of the formulation subsidy rate at the end of the fiscal year. The results of reestimate calculations are used by financial managers to adjust the allowance for subsidies related to direct loans receivable and the liability for loan guarantees for financial statement purposes, and to prepare the formulation subsidies for submission in the next PB.

The process that Federal credit agencies use to estimate the long-term costs of credit programs has evolved and improved since the creation of the FCRA, and the Federal credit agencies—in coordination with OMB—have created sophisticated models to project and discount cash flows in accordance with the FCRA. Still, the process of estimating the long-term cost continues to be very complex and is further complicated by unknown economic events that could render the estimated costs overly optimistic or pessimistic, moving the pendulum drastically between the two extremes. Therefore, the process to calculate reasonable reestimates depends on the sophistication and reliability of the cash flow models, which are tools used by Federal credit agencies to discount future cash flows, and the availability of data to estimate cash flow projections.

If we consider the recent financial crisis, trillions of dollars in asset values that many companies were reporting in their financial statements were revalued downward in a very short period of time. At the same time, the Federal government provided unprecedented levels of support to the markets—to the tune of approximately \$2 trillion dollars—resulting in the largest increase

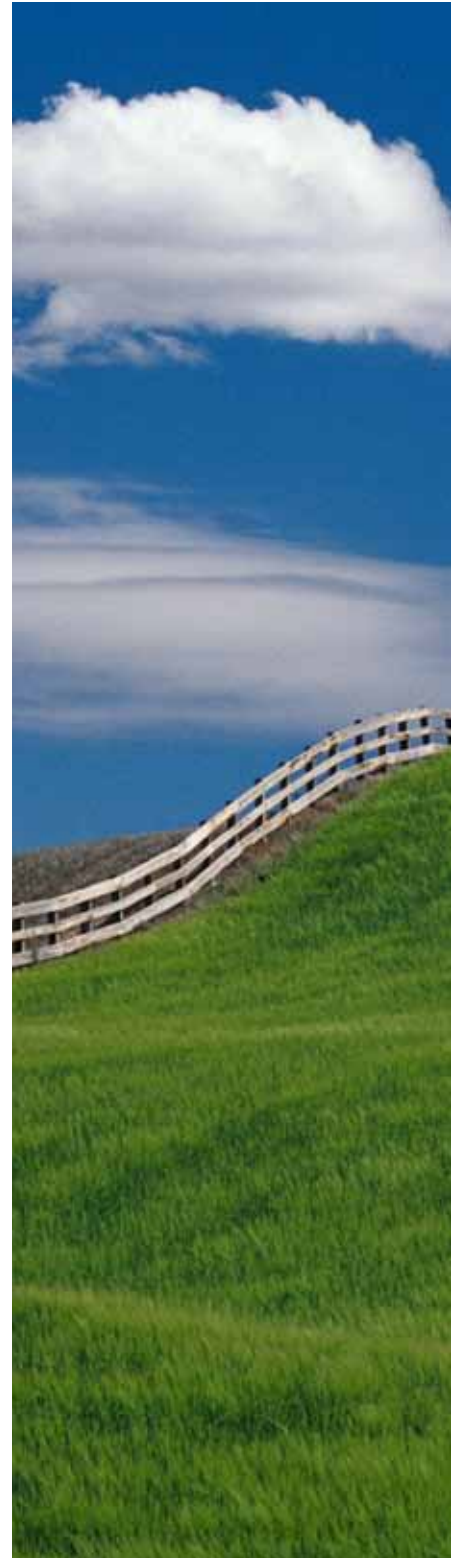
in Federal credit program activity since the FCRA was enacted. This situation creates great challenges for Federal agencies and auditors in trying to determine the reasonableness, or sufficiency of the credit program reserve estimates. Hence, it is important that Federal agencies evaluate, revise, and enhance, as necessary, their cash flow projection tools, and to analyze the loan and loan guarantee portfolios' historical performance data in order to adequately calculate the credit program reestimates. These considerations should be part of the periodic communications between Federal agency financial managers and their auditors.

The complexity of financial markets, globalization, and current political and economic conditions in foreign countries play an important role in the U.S. economy by influencing our financial markets and the health of our domestic businesses of all sizes. Further, as noted earlier, the impending outlays required for health care spending are expected to continue to grow and will have a negative impact on the Federal deficit and our economy toward the end of the decade. In addition, other situations such as environmental disasters are impossible to predict and place additional pressure on the Federal government's ability to consistently provide necessary funding to satisfy competing priorities.

The current budget deficit deteriorates the economic outlook further. In a recent article in *The Washington Post* titled "The welfare state death spiral," about the economic crisis in Greece and why it matters to the United States, economist Robert J. Samuelson wrote: "Almost anything governments might do with their budgets threatens to make

matters worse by slowing the economy or triggering a recession. By allowing deficits to balloon, they risk a financial crisis as investors one day—no one knows when—doubt governments' ability to service their debts and, as with Greece, refuse to lend except at exorbitant rates." Although the U.S. economy is distanced from the current Greek financial crisis and from other economies facing similar difficulties, the trend of increased budget deficits could trigger another economic crisis in the United States. The potential economic outcomes are the subject of much debate, and current efforts and initiatives are being discussed at all levels of government to try to address the fiscal well-being of the nation. For instance, the passage of the EESA and ARRA was controversial because the related spending added to the Federal deficit. As a result, there continues to be discussions about the growing U.S. deficit, what needs to be done about it, and how the nation can continue on the road to economic recovery, while at the same time avoid compromising U.S. competitiveness in global markets.

Certainly, there are competing priorities facing our Federal government leaders, and many in and outside the Federal government believe that government spending will need to be reduced in the near future, with an increased emphasis placed on properly assessing and prioritizing the costs allocated to Federal government programs. Federal credit programs are some of the more complex Federal program cost estimates, and it will be essential for these program cost estimates to be as accurate as possible if the Federal government is to properly manage its budgetary resources.



Audit Challenges Financial Managers Should Consider

In his recent book, *The Black Swan*, author Nassim Nicholas Taleb defines “Black Swans” as highly consequential but unlikely events that are easily explainable—but only identifiable in retrospect. In addition, Mr. Taleb suggests that some of the most destructive biases result in misuse of standard statistical tools such as the bell curve, which ignores black swans, and that, as the forecasting period lengthens, the prediction errors grow exponentially. He also suggests that as the world becomes more interconnected, the probability of black swans becomes more consequential. Although accounting standards require financial managers to calculate estimates that are measurable and, in doing so, inherently ignore the incorporation of black swans, the views presented by Mr. Taleb highlight one of the main dilemmas financial managers and auditors face, which is to determine

what is measurable and reasonable when performing asset and liability valuation assessments, and what are the proper tools and considerations to determine relevancy and accuracy of financial information. This becomes increasingly difficult when you consider that financial managers don’t have the capability to forecast black swans or extraordinary events that, on a long-term basis, have a probability to occur. This dilemma increases the exposure of organizations to financial instability. In the case of Federal credit programs, the government uses macro-economic and management assumptions, driven by known historical portfolio performance, to estimate the long-term cost of these programs, in most cases, over a 20- or 30-year term. However, the current pressures put on the deficit by Federal government spending affect our economy and credit markets, which in turn affect the way loan portfolios perform. It is the costs associated with these economic factors that are the most difficult to measure. As Federal credit agencies continue to improve their modeling methodologies,

it may become easier to more accurately reflect these underlying economic impacts in management’s future cost projections, thereby reducing this inherent risk of financial instability.

Currently, the guiding principles to account for the long-term cost of federal credit programs are founded in accounting standards promulgated by the Federal Accounting Standard Advisory Board (FASAB), and other FASAB prescribed guidance to calculate credit program estimates. Generally, financial auditors follow generally accepted auditing standards issued by the American Institute of Certified Public Accountants (AICPA) to perform audits of estimates. These standards are also used in audits of Federal agencies. However, in addition to the AICPA standards, auditors in the Federal sector must also perform audits in accordance with *Government Auditing Standards*, issued by the Comptroller of the United States, as well as other guidance listed in Table 1 on the following page.



Table 1: Federal Credit Reform Audit and Accounting Guidance

Standard/Authoritative Guidance	Agency/ Regulatory Body	Description	Users
Statement of Auditing Standards No. 57, Auditing Accounting Estimates	AICPA	Provides guidance and considerations that auditors must follow when auditing estimates	Audit Organizations
Financial Audit Manual	Government Accountability Office (GAO)	Provides guidance and considerations that auditors must follow when performing audits of Federal agencies	Audit Organizations
OMB Bulletin 07-04, <i>Audit Requirements for Federal Financial Statements</i>	OMB	Provides minimum requirements and considerations that auditors must follow when performing audits of Federal agencies	Audit Organizations
Statement of Federal Financial Accounting Standards 2, <i>Accounting for Direct Loans and Loan Guarantees</i>	FASAB	Provides accounting and reporting requirements for direct loans and loan guarantees in accordance with FCRA	Agency financial staff and managers, audit organizations
SFFAS 18, <i>Amendments to Accounting Standards for Direct Loans and Loan Guarantees</i>	FASAB	Amends SFFAS 2, and provides additional reporting requirements for direct loans and loan guarantees in accordance with FCRA	Agency financial staff and managers, auditors
SFFAS 19, <i>Technical Amendments to Accounting Standards for Direct Loans and Loan Guarantees</i>	FASAB	Amends SFFAS 2, and provides additional reporting requirements and clarifications for direct loans and loan guarantees in accordance with FCRA	Agency financial staff and managers, audit organizations
Office of Management Budget Circular A-11, <i>Preparation, Submission, and Execution of Budget, Section 185, Federal Credit</i>	OMB	Provides guidance and requirements concerning computing the subsidy rates of Federal credit programs as well as budgetary reporting requirements	Agency financial staff and managers, audit organizations
Technical Release No. 3, <i>Auditing Estimates for Direct Loan and Loan Guarantee Subsidies under the Federal Credit Reform Act</i>	FASAB	Provides guidance for auditors when auditing Federal credit programs	Audit organizations (recommended reading for agency financial managers and staff)
Technical Release No. 6, <i>Preparing Estimates for Direct Loan and Loan Guarantee Subsidies under the Federal Credit Reform Act</i>	FASAB	Provides guidance for financial managers when calculating subsidy reestimates	Agency financial staff and managers, audit organizations

The audit of Federal credit programs requires thorough planning during the early stages to the audit. This involves a well-rounded understanding of the Federal credit programs, the industry, and the market influences affecting these programs. Financial auditors must be aware of existing legislation, budgetary authority, knowledge of prior year audit results—including audit adjustments—prior year audit findings, and corrective

actions financial managers have implemented to address those findings. Further, it is essential that the auditors understand the financial systems used by agencies to account for Federal credit program transactions, and the cash flow models and other tools used by management to perform the estimate calculations.

Agency financial managers should be aware that the primary objective of the audit of Federal credit programs is to ensure that the financial statement assertions are satisfied, and compliance with laws and regulations—including FCRA—are met. Table 2 below illustrates a suggested approach that auditors might use when conducting the audit. The approach considers three audit objectives, as indicated.

Table 2: Suggested Audit Approach

Audit Objectives for Financial Statements and Related Credit Reform Disclosures		
Audit Objective 1:	Audit Objective 2:	Audit Objective 3:
<ul style="list-style-type: none">• Related to routine transactions, e.g., loan disbursements• Determines:<ul style="list-style-type: none">– If financial assertions (CEAO)* are supported– The effectiveness of internal controls	<ul style="list-style-type: none">• Relates to nonroutine transactions, e.g., reestimates• Determines:<ul style="list-style-type: none">– If financial statement assertions (VP)** are supported– The effectiveness of internal controls	<ul style="list-style-type: none">• Relates to compliance with direct and material laws and regulations at year-end• Normally performed in tandem with Objectives 1 and 2 (multipurpose tests)

* Completeness, Existence, Accuracy, Obligations

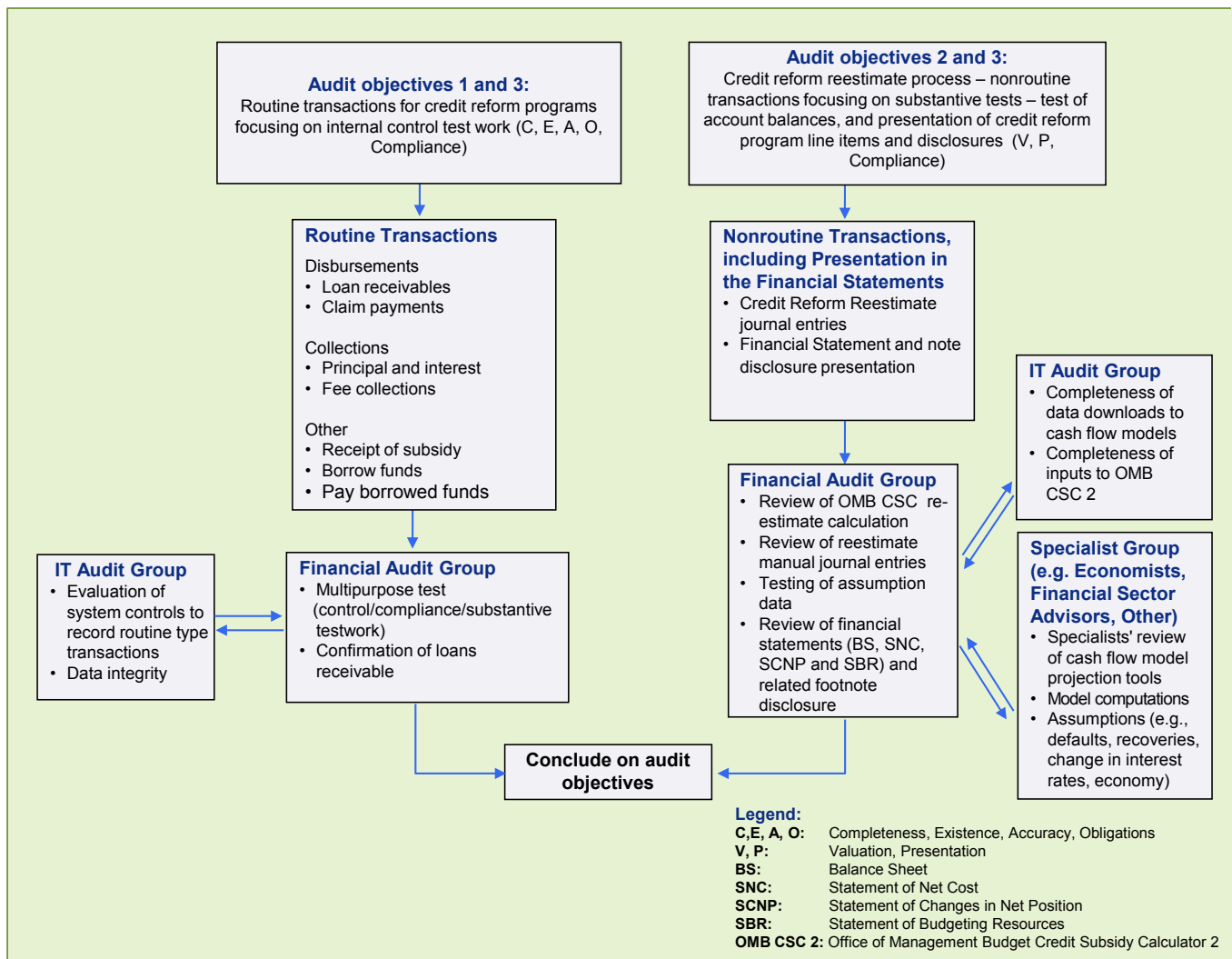
** Valuation and Presentation



The previous table illustrates a typical approach to audit Federal credit programs. The logic for this approach follows the most common process for auditing estimates in which the transactions that are considered “routine” type transactions (e.g., disbursements, collections, transfers or subsidy, issuance of guarantee) are separate from the “nonroutine” type transactions (e.g., reestimate calculation) for purposes of the audit. In essence, these are distinct

processes with separate risks and internal control processes that require different audit procedures. However, the credit program estimates, or the nonroutine transactions, are impossible to audit without reliance on the routine transactions that form the basis for the historical data management uses to project future cash flows, ultimately leading to the final reserve valuation. This Federal Credit Reform Audit Work Flow concept is illustrated below in Chart 6.

Chart 6: Credit Reform Audit Work flow



Fundamentally, the main goal of the audit of credit programs is to determine whether the balances of the direct loan and loan guarantee programs are properly reported in the agency's financial statements and footnotes.

Once all relevant audit test work concerning the routine transactions is completed, the focus of the audit shifts to the reestimate calculations. After management completes its projection of future program cash flows, the agency discounts back to the present value of the future cash flows, using an OMB discounting tool, OMB Credit Subsidy Calculator 2, or OMB CSC2. However, the actual cash flow projections, using macro-economic and management assumptions, is the most complex and sensitive area of the audit. During this portion of the audit, the cash flow models and underlying cash flow assumptions are reviewed by the auditor to determine if the cash flow models are

functioning properly and the assumptions are reasonable. In preparation for the audit of the reestimate calculations, Federal financial managers should focus on the importance of properly documenting management assumptions, which in most cases are based on auditable historical data as well as forward-looking econometric assumptions. It is important to note that many of the auditor's findings relate to a lack of proper or auditable documentation. Therefore, it is advisable that Federal financial managers adhere to the guidance presented in TR 6 concerning the process for preparing credit program estimate calculations. In addition, Federal financial managers must also consider the agency's ability to properly disclose what events throughout the year impacted the various credit programs, and what effect those events had on the final amounts reported.



Summary and Conclusion

The FCRA has substantially contributed to our nation's economy and to society since the passage of the legislation in 1990. The FCRA ensures that the long-term costs of the Federal credit programs are determined at the time of loan and loan guarantee origination. In doing this, the Federal government is able to better manage its budgetary resources. Over time, the direct loan and loan guarantee programs have significantly increased in popularity and use, providing much needed financing to many sectors of our economy, including housing, small business, education, and agriculture. During the recent financial crisis, the Federal government devoted approximately \$2 trillion dollars to assist our nation's economy and financial credit markets, most of it related to Federal credit programs, and in turn recorded the largest increase in Federal credit program activity since the inception of the FCRA. This activity was the result of unprecedented market forces that led to the creation of the HERA of 2008, EESA of 2008, and the ARRA of 2009, and in turn established the Federal government's stake in the U.S. financial sector. At this point, we are still evaluating the full ramifications of these Federal government actions. As a result, concerns about the rising budget deficit and the fiscal sustainability of the nation are at the forefront of American political discourse as well as on the minds of many Federal government and private business financial managers.

The ability of Federal agencies to properly manage and allocate scarce resources in the future will significantly impact the country's ability to manage the Federal deficit. Given the steady rise in popularity of Federal credit program offerings to a point now where these program costs make up a significant portion of the Federal government's discretionary spending, effective future Federal credit program cost allocations become even more important. Cost allocations are based on the use of very complex accounting estimates, and the ability of Federal credit agencies to properly account for Federal credit program transactions will be essential in this new environment. To successfully accomplish this, Federal managers must work with their independent auditors in order to ensure agreement regarding the reasonableness of Federal credit program costs reported. As a result, understanding the audit process—and what Federal financial managers must expect in preparation for it—should be a priority for every Federal agency with FCRA programs.

Is there perhaps a sleeping giant lurking in the halls of Federal credit program agencies? Will we continue to see a rise in direct loans and loan guarantee portfolios? Given the steady rise in Federal credit program offerings since the inception of the FCRA and the steep rise in the use of these programs to stimulate our economy during the recent economic downturn, it appears these programs will continue to grow over time and become an even larger component of the Federal budget.



A photograph of a wind turbine in a field of yellow flowers under a blue sky. The turbine is white and stands tall on the left side of the image. The field is a vibrant yellow, and the sky is a clear, bright blue. In the background, other wind turbines are visible, slightly out of focus.

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Mike Lippert's audit and advisory services experience includes nine years managing Federal audit engagements under the CFO Act and its successors. He is the engagement partner for many of our clients that report in accordance with the Credit Reform Act of 1990, including FY2004 through FY2008 audits of the USDA Commodity Credit Corporation and the FY2006 through FY2009 audits of the Small Business Administration. Mike also served the USDA RD by providing an independent review of the processes, methodologies, and assumptions used by RD to develop the subsidy rates for its Direct Loan Single Family Housing program—Model A. He is also the engagement partner on the FY2005 through FY2009 audits of the Overseas Private Investment Corporation, an organization that reports under commercial accounting standards. He is responsible for the audit work performed at the Department of Commerce's Bureau of the Census and the National Institute of Standards and Technology for FY2005 to FY2009. Mike has been a national and local instructor for KPMG for the last seven years, instructing all professional levels—partners, managers, and staff—on technical topics, including federal credit reform concepts; internal control; general federal, state, and local government topics; and a wide variety of other matters.

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Armando is an Audit senior manager in KPMG's Federal Audit practice in the Washington, DC office. His 14 years of experience include 12 years focused on performing Chief Financial Officers Act financial statements audits, and advisory services to federal agencies. He also has experience in providing auditing services to state and local governments. Armando has provided professional audit services to several federal agencies in accordance with FASAB, OMB and GAO promulgated standards and regulations. His main area of specialization is the Federal Credit Reform Act of 1990 (FCRA) accounting and auditing. He has substantial experience auditing federal loan and loan guarantee portfolios, which requires the examination of complex cash flow models and other estimation tools, management, and economic assumptions. Armando has also developed an in-depth knowledge of internal controls, risk assessments, and compliance with laws and regulations affecting the Federal industry. He has performed advisory services to federal agencies in the areas of audit readiness and review of credit reform cash flow models and control processes. Armando is a local office training developer and instructor in the areas of federal accounting and auditing to include: Accounting and Auditing Credit Reform Programs; Budgetary and Proprietary Accounting; and Financial Reporting. He is a national instructor and has participated in many national trainings teaching audit methodology and Federal industry related topics.

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