MANAGEMENT'S DISCUSSION AND ANALYSIS

Introduction

The FY 2020 *Financial Report* provides the President, Congress, and the American people with a comprehensive view of the federal government's financial position and condition, and discusses important financial issues and significant conditions that may affect future operations, including the need to achieve fiscal sustainability over the long term.

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

The *Financial Report* is prepared from the financial information provided by 165 federal consolidation entities (see organizational chart on the next page and Appendix A). As it has for the past 22 years, GAO issued a disclaimer of opinion on the accrual-based, consolidated financial statements for the fiscal years ended September 30, 2020 and 2019. GAO also issued a disclaimer of opinion on the sustainability financial statements, which consist of the 2020 and 2019 SLTFP; the 2020, 2019, 2018, 2017, and 2016 SOSI; and the 2020 and 2019 SCSIA. A disclaimer of opinion indicates that sufficient information was not available for the auditors to determine whether the reported financial statements were fairly presented in accordance with GAAP. In FY 2020, 35[2] of the 40 most significant entities earned unmodified ("clean") opinions on their financial statements.

The FY 2020 *Financial Report* consists of:

- MD&A, which provides management's perspectives on and analysis of information presented in the *Financial Report*, such as financial and performance trends;
- Financial statements and the related notes to the financial statements;
- RSI and Other Information; and
- GAO's audit report.

This *Financial Report* addresses the government's financial activity and results as of and for the fiscal years ended September 30, 2020 and 2019. Note 29—Subsequent Events discusses events that occurred after the end of the fiscal year that may affect the government's financial position and condition.

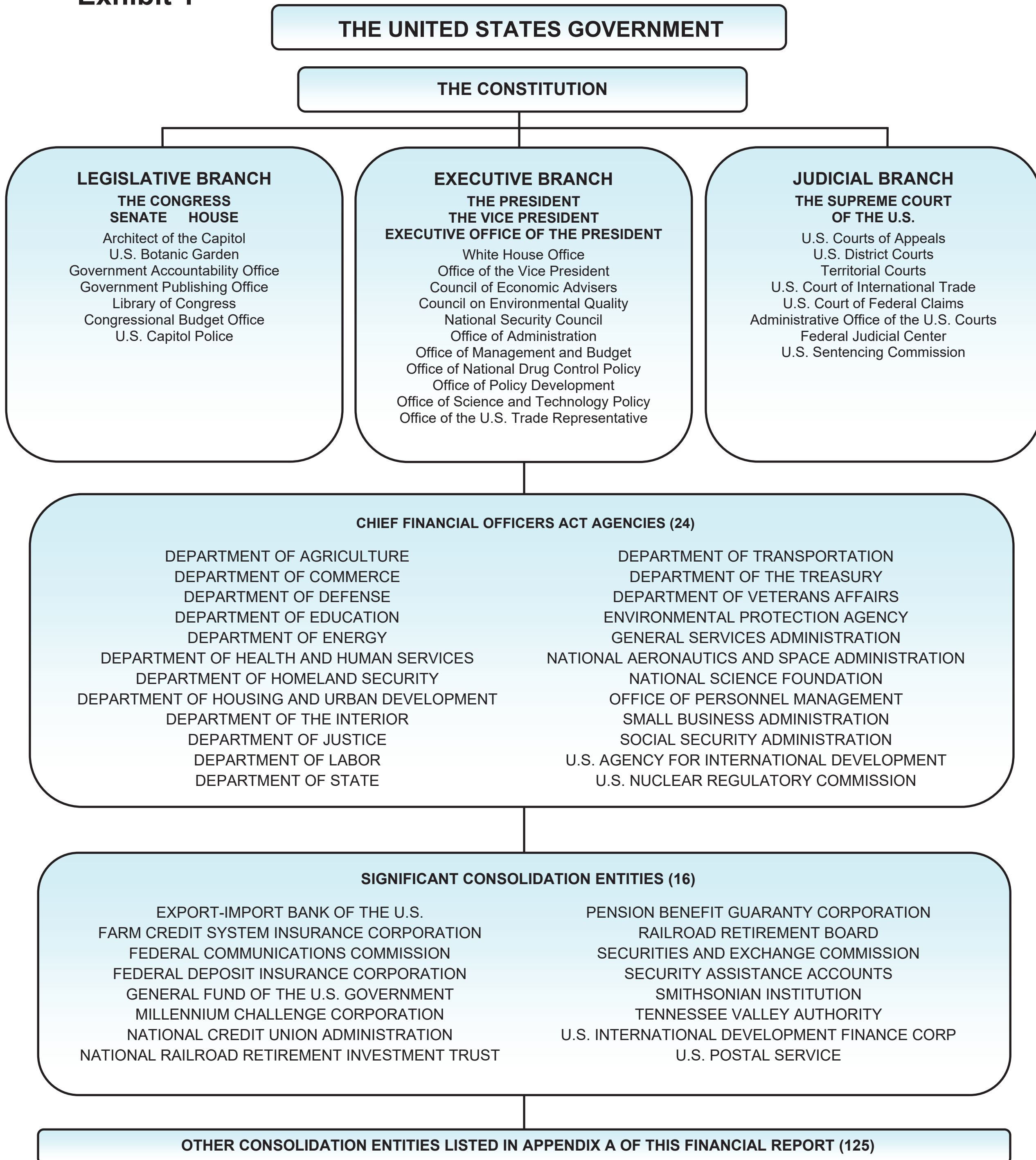
In addition, the Results in Brief and Executive Summary to this *Financial Report* provide a quick reference to the key issues in the *Financial Report* and an overview of the government's financial position and condition.

Mission & Organization

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

[1] The *Government Management Reform Act of 1994* has required such reporting, covering the executive branch of the government, beginning with financial statements prepared for FY 1997. The consolidated financial statements include the legislative and judicial branches.
[2] The 35 entities include the HHS, which received disclaimers of opinion on its 2020, 2019, 2018, 2017, and 2016 SOSI and on its 2020 and 2019 SCSIA.

Exhibit 1



The Government's Financial Position and Condition

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

Table 1
The Federal Government's Financial Position and Condition

		2020		2019*	Increase / (Decrease) $	%
FINANCIAL MEASURES (Dollars in Billions)						
Gross Cost	**$**	**(7,194.1)**	**$**	**(5,287.2)**	**$ 1,906.9**	**36.1%**
Less: Earned Revenue	$	461.6	$	418.4	$ 43.2	10.3%
Gain/(Loss) from Changes in Assumptions	$	(679.5)	$	(198.9)	$ 480.6	241.6%
Net Cost	**$**	**(7,412.0)**	**$**	**(5,067.7)**	**$ 2,344.3**	**46.3%**
Less: Tax and Other Revenues	**$**	**3,571.6**	**$**	**3,621.0**	**$ (49.4)**	**(1.4%)**
Unmatched Transactions & Balances	$	11.6	$	0.4	$ 11.2	2,800.0%
Net Operating Cost	**$**	**(3,828.8)**	**$**	**(1,446.3)**	**$ 2,382.5**	**164.7%**
Budget Deficit	**$**	**(3,131.9)**	**$**	**(984.4)**	**$ 2,147.5**	**218.2%**
Assets:						
Cash & Other Monetary Assets	$	1,926.9	$	524.6	$ 1,402.3	267.3%
Direct Loans and Loan Guarantees Receivable, Net	$	1,577.4	$	1,425.8	$ 151.6	10.6%
Inventories & Related Property, Net	$	379.7	$	355.7	$ 24.0	6.7%
General Property, Plant & Equipment, Net	$	1,145.0	$	1,106.9	$ 38.1	3.4%
Other	$	921.7	$	579.0	$ 342.7	59.2%
Total Assets	**$**	**5,950.7**	**$**	**3,992.0**	**$ 1,958.7**	**49.1%**
Liabilities:						
Federal Debt and Interest Payable	$	(21,082.9)	$	(16,861.0)	$ 4,221.9	25.0%
Federal Employee & Veteran Benefits Payable	$	(9,409.3)	$	(8,440.3)	$ 969.0	11.5%
Other	$	(2,251.7)	$	(1,643.5)	$ 608.2	37.0%
Total Liabilities	**$**	**(32,743.9)**	**$**	**(26,944.8)**	**$ 5,799.1**	**21.5%**
Unmatched Transactions and Balances	$	(3.1)	$	(14.7)	$ (11.6)	(78.9%)
Net Position	**$**	**(26,796.3)**	**$**	**(22,967.5)**	**$ 3,828.8**	**16.7%**
SUSTAINABILITY MEASURES (Dollars in Trillions)						
Social Insurance Net Expenditures:						
Social Security (OASDI)	$	(19.7)	$	(16.8)	$ 2.9	17.3%
Medicare (Parts A, B, & D)	$	(45.7)	$	(42.2)	$ 3.5	8.3%
Other	$	(0.1)	$	(0.1)	$ -	- %
Total Social Insurance Net Expenditures	**$**	**(65.5)**	**$**	**(59.1)**	**$ 6.4**	**10.8%**
Total Federal Non-Interest Net Expenditures	**$**	**(79.5)**	**$**	**(49.0)**	**$ 30.5**	**62.2%**
75-Year Fiscal Gap (Percent of Gross Domestic Product)[1]		**(5.4%)**		**(3.8%)**	**1.6%**	**42.1%**

*Restated (see Financial Statement Note 1.U)

[1]To prevent the debt-to-GDP ratio from rising over the next 75 years, a combination of non-interest spending reductions and receipts increases that amounts to 5.4 percent of GDP on average is needed (3.8 percent of GDP on average in 2019). See Financial Statement Note 24.

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

- This *Financial Report* includes discussion and analysis of the significant impact that the federal government's response to the COVID-19 pandemic had on the government's financial position during FY 2020.
- During FY 2020, the budget deficit increased by $2.1 trillion (218.2 percent) to $3.1 trillion and net operating cost increased by $2.4 trillion (164.7 percent) to $3.8 trillion.
- The government's gross costs of $7.2 trillion, less $461.6 billion in revenues earned for goods and services provided to the public (e.g., Medicare premiums, national park entry fees, and postal service fees), plus $679.5 billion in net losses from changes in assumptions (e.g., interest rates, inflation, disability claims rates) yields the government's net cost of $7.4 trillion, an increase of $2.3 trillion or 46.3 percent over FY 2019.
- Deducting $3.6 trillion in tax and other revenues, with some adjustment for unmatched transactions and balances, results in a "bottom line" net operating cost of $3.8 trillion for FY 2020, an increase of $2.4 trillion or 164.7 percent over FY 2019.
- Comparing total 2020 government assets of $6.0 trillion to total liabilities of $32.7 trillion (comprised mostly of $21.1 trillion in federal debt and interest payable[3], and $9.4 trillion of federal employee and veteran benefits payable) yields a negative net position of $26.8 trillion.
- The budget deficit is primarily financed through borrowing from the public. As of September 30, 2020, debt held by the public, excluding accrued interest, was $21.0 trillion. This amount, plus intra-governmental debt ($6.0 trillion) equals gross federal debt, which, with some adjustments, is subject to the statutory debt limit. As of September 30, 2020, the government's total debt subject to the debt limit was $26.9 trillion. The statutory debt limit was most recently suspended through July 31, 2021.

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

- The SLTFP shows that the PV[4] of total non-interest spending, including Social Security, Medicare, Medicaid, defense, and education, etc., over the next 75 years, under current policy, is projected to exceed the PV of total receipts by $79.5 trillion (total federal non-interest net expenditures from Table 1).
- The SOSI shows that the PV of the government's expenditures for Social Security and Medicare Parts A, B and D, and other social insurance programs over 75 years is projected to exceed social insurance revenues[5] by about $65.5 trillion, a $6.4 trillion increase over 2019 social insurance projections.
- The two sustainability measures in Table 1 differ primarily because total non-interest net expenditures from the SLTFP include the effects of general revenues and non-social insurance spending, neither of which is included in the SOSI.

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

- The budget deficit (i.e., including the consolidated receipts and outlays from federal funds and the Social Security Trust Fund) increased from $984.4 billion in FY 2019 to $3.1 trillion in FY 2020. The deficit-to-GDP ratio in 2020 was 14.9 percent, an increase from 4.6 percent in FY 2019.
- The budget deficit is primarily financed through borrowing from the public. As of September 30, 2020, the $21.0 trillion in debt held by the public, excluding accrued interest, equates to approximately 100 percent of GDP.
- The 2020 SOSI projection of $65.5 trillion net PV excess of expenditures over receipts over 75 years represents about 4.2 percent of the PV of GDP over 75 years. The excess of total projected non-interest spending over receipts of $79.5 trillion from the SLTFP represents 4.8 percent of GDP over 75 years. As discussed in this *Financial Report*, changes in these projections can, in turn, have a significant impact on projected debt as a percent of GDP.
- To prevent the debt-to-GDP ratio from rising over the next 75 years, a combination of non-interest spending reductions and receipts increases that amounts to 5.4 percent of GDP on average is needed (3.8 percent of GDP on average in the 2019 projections). The fiscal gap represents 30.2 percent of 75-year PV receipts and 23.8 percent of 75-year PV non-interest spending.

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

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

[5] Social Security is funded by the payroll taxes and revenue from taxation of benefits. Medicare Part A is funded by the payroll taxes, revenue from taxation of benefits, and premiums that support those programs. Medicare Parts B and D are primarily financed by transfers from the General Fund, which are presented, and by accounting convention, eliminated in the SOSI. For the FYs 2020 and 2019 SOSI, the amounts eliminated totaled $40.9 trillion and $36.8 trillion, respectively.

FY 2020 Financial Statement Audit Results

For FY 2020, GAO issued a disclaimer of audit opinion on the accrual-based, government-wide financial statements, as it has for the past 23 years, due to certain material weaknesses in internal control over financial reporting and other limitations on the scope of its work. In addition, GAO issued a disclaimer of opinion on the sustainability financial statements due to significant uncertainties primarily related to the achievement of projected reductions in Medicare cost growth and certain other limitations. GAO's audit report on page 226 of this *Financial Report*, discusses GAO's findings.

Twenty-two of the 24 entities required to issue audited financial statements under the CFO Act received unmodified audit opinions, as did 13 of 16 additional significant consolidation entities (see Table 11 and Appendix A).[6]

The Government-wide Reporting Entity

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

Fannie Mae and Freddie Mac meet the criteria for disclosure entities and, consequently, are not consolidated into the government's financial statements. However, the values of the investments in such entities, changes in value, and related activity with these entities are included in the consolidated financial statements. The FR System and the SPVs are disclosure entities and are not consolidated into the government's financial statements. See Note 1.A and Note 26—Disclosure Entities and Related Parties for additional information. In addition, per SFFAS No. 31, *Accounting for Fiduciary Activities*, fiduciary funds are not consolidated in the government financial statements.[7]

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

The following pages contain a more detailed discussion of the government's financial results for FY 2020, the budget, the economy, the debt, and a long-term perspective about fiscal sustainability, including the government's ability to meet its social insurance benefits obligations. The information in this *Financial Report*, when combined with the *Budget*, collectively presents information on the government's financial position and condition.

The Federal Government's Response to the Pandemic

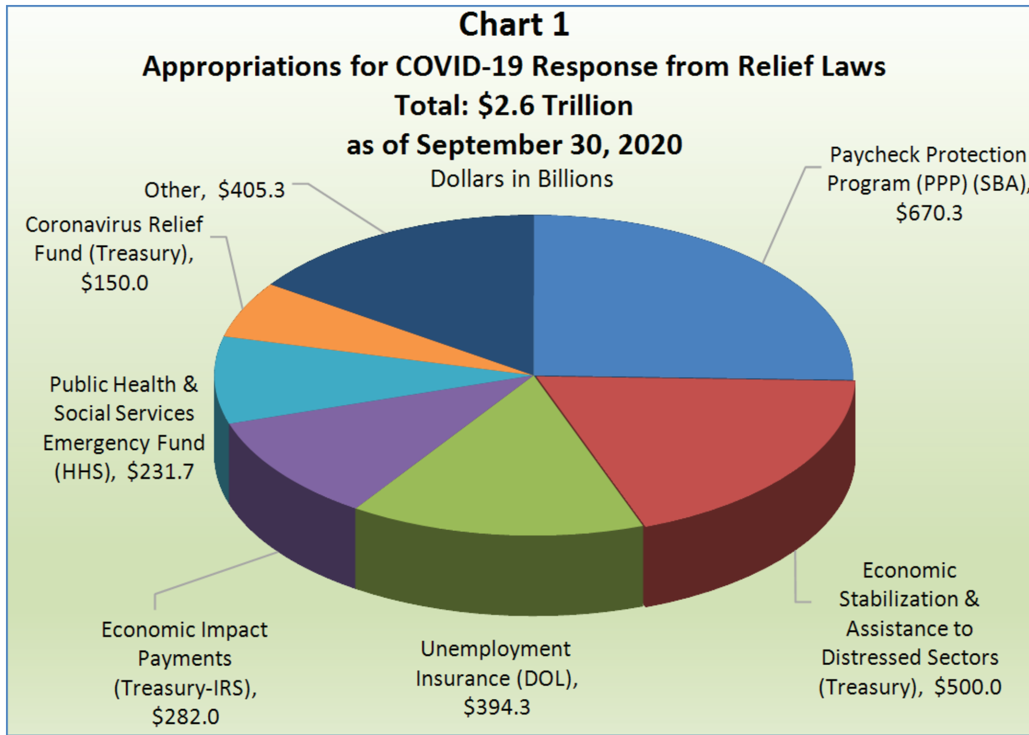
During FY 2020, the federal government took broad action to protect public health from the effects of the unprecedented pandemic, signing into law four major pieces of legislation:

- *Coronavirus Preparedness and Response Supplemental Appropriations Act of 2020* (P.L. 116-123)
- *Families First Coronavirus Response Act* (FFCRA, P.L. 116-127)
- *Coronavirus Aid, Relief, and Economic Security* (CARES Act, P.L. 116-136)
- *Paycheck Protection Program and Health Care Enhancement Act* (PPPHCE Act, P.L. 116-139)

These laws address the health and economic effects of COVID-19, providing assistance to American workers and families, small businesses, and state, local, tribal governments, and preserving jobs for American industry. As indicated here and in the *Financial Report*, these essential programs had significant effects on the federal government's budgetary and financial results.

[6] The 22 entities include the HHS, which received disclaimers of opinions on its 2020, 2019, 2018, 2017, and 2016 SOSI and its 2020 and 2019 SCSIA. The 13 entities include the FDIC, the NCUA, and the FCSIC, which operate on a calendar year basis (December 31 year-end). Statistic reflects 2019 audit results for these organizations if 2020 results are not available.

[7] See Note 22—Fiduciary Activities



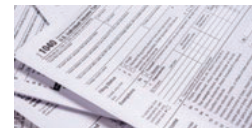
Source: Treasury – Central Accounting Reporting System (CARS)

Chart 1 summarizes the more than $2.6 trillion in appropriations enacted for key pandemic-related assistance programs during FY 2020, which include, but are not limited to:

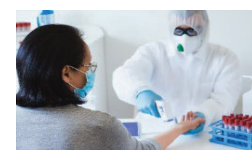
- The PPP, administered by the SBA, is a loan guaranty program designed to provide a direct incentive for small businesses to retain employees by providing loan forgiveness for amounts used for eligible expenses for payroll and benefit costs, interest on mortgages, rent, and utilities ($670.3 billion).

- Through its Economic Stabilization and Assistance to Severely Distressed Sectors of the U.S. Economy efforts (CARES Act Title IV), Treasury, including in collaboration with the Federal Reserve, provides funding through direct loans and loan guarantees or other support for various businesses and state and local governments ($500.0 billion).

- Through its UI Program, the DOL expands states' ability to provide UI for many workers impacted by the pandemic, including for workers who are not eligible for regular/traditional unemployment benefits ($394.3 billion).



- The IRS provided a refundable tax credit, the recovery rebate, of $1,200 per qualifying adult, and $500 per dependent child, and a deferral of payment of employer's share of Social Security taxes through December 2020 ($282.0 billion).



- Through the PHSSEF, the HHS provides broad support, including, but not limited to: reimbursements to health care providers for expenses or lost revenues attributable to the pandemic, and support for the development and purchase of vaccines, therapeutic treatment, testing, and medical supplies ($231.7 billion).

- Through Coronavirus Relief Fund efforts, Treasury provides for payments to states, local, and tribal governments for pandemic-related spending ($150.0 billion).

- Many other agencies and programs comprise the remaining $405.3 billion reported as "Other" in Chart 1, including, but not limited to funding for: transportation system assistance at the DOT, student loan deferrals provided by Education, and FEMA's Disaster Relief Fund.

- Note 29—Subsequent Events, discusses the financial effects of significant events that occurred following the end of the fiscal year, but prior to issuance of this *Financial Report*. Those subsequent events include additional appropriations as well as subsequent recissions (i.e., reductions) to appropriated amounts referenced above.[8] Additional subsequent events are referenced throughout the *Financial Report* as appropriate.

Three key components of the U.S. budget process are: 1) appropriations, 2) obligations, and 3) outlays. An appropriation is a provision of law authorizing the expenditure of funds for a given purpose. Once funds are appropriated by Congress, Treasury issues warrants that officially establish the amounts available to be obligated and spent (i.e., expended or outlayed) by each agency. An agency's obligation of funds is a binding agreement to outlay funds for a particular purpose immediately or in the future. Table 2 below compares the obligated and outlaid amounts to the appropriation amounts for each program summarized in Chart 1. Obligations and outlays provide an indication of how much appropriations have been used. Outlays for SBA's PPP and Treasury's Economic Stabilization & Assistance to Distressed Sectors programs detailed in Table 2 represent the subsidy cost reflected in the budget deficit for such programs. The PPP budget outlays primarily represent estimated subsidy cost for which cash payments have not yet been made to the lenders, resulting in a liability on the balance sheet as of September 30, 2020. Concerning Treasury's Economic Stabilization & Assistance to Distressed Sectors Program, the outlays primarily relate to estimated losses on Investments in Special Purpose Vehicles reported on the balance sheet.

Table 2: COVID-19 Response From Relief Laws

Dollars in Billions	Appropriatons*	Obligations Incurred **	Gross Outlays**
Paycheck Protection Program (PPP) (SBA)	$ 670.3	$ 532.3	$ 525.9
Economic Stabilization & Assistance to Distressed Sectors (Treasury)	$ 500.0	$ 31.8	$ 19.3
Unemployment Insurance (DOL)	$ 394.3	$ 358.0	$ 345.5
Economic Impact Payments (Treasury-IRS)	$ 282.0	$ 274.7	$ 274.7
Public Health & Social Services Emergency Fund (PHSSEF) (HHS)	$ 231.7	$ 141.7	$ 108.1
Coronavirus Relief Fund (Treasury)	$ 150.0	$ 150.0	$ 149.5
Other	$ 405.3	$ 301.9	$ 199.2
Total	**$ 2,633.6**	**$ 1,790.4**	**$ 1,622.2**

*Source: Treasury - Central Accounting Reporting System (CARS)

**Source: Treasury - Government-wide Treasury Account Symbol Adjusted Trial Balance System (GTAS)

Chart 1 and Table 2 above reflect only amounts appropriated, obligated, and outlaid as of September 30, 2020. The Treasury website, www.USAspending.gov provides more current information about amounts spent by the federal government for COVID-19 response and for other purposes.

Budgetary activity, such as appropriations, obligations, and outlays are different from, but related to financial activity, such as costs, assets, and liabilities. The following section provides a brief discussion of the relationship between budgetary and financial accounting in the federal government. As agencies implement programs, the appropriations, obligations, and outlays referenced in Table 2 precipitate a wide range of financial effects, including the incurrence of program costs, and the creation of or changes in assets such as advances or loans receivable, or liabilities such as loan guarantees. Table 3 in the following section, which summarizes the *Reconciliation of Net Operating Cost and Budget Deficit* statement, presents the significant differences between the two accounting perspectives utilized by the federal government. The corresponding financial effects are discussed later in the MD&A in the section entitled "The Government's Net Position: 'Where We Are'".

[8] On December 27, 2020, the President signed into law the *Consolidated Appropriations Act, 2021* (P.L. 116-120). This act included provisions for an additional $900.0 billion in stimulus relief related to the pandemic. In addition, as of the date of enactment, this act rescinded $478.8 billion of the $500.0 billion appropriation provided to Treasury under Section 4027 of the CARES Act. Effective January 9, 2021, the statute eliminates Treasury's ability to make new loans and investments under Section 4003 of the CARES Act. In addition, $146.5 billion that was appropriated to SBA under the SBA-Business Loans Program Account, CARES Act, was rescinded under the *Consolidated Appropriations Act, 2021*. In addition, on March 11, 2021, the President signed into law the *American Rescue Plan Act, 2021*, a $1.9 trillion economic relief package to address the continued impact of COVID-19 on the economy. See Note 29—Subsequent Events and Treasury's financial statements for more information.

Accounting Differences Between the Budget and the Financial Report

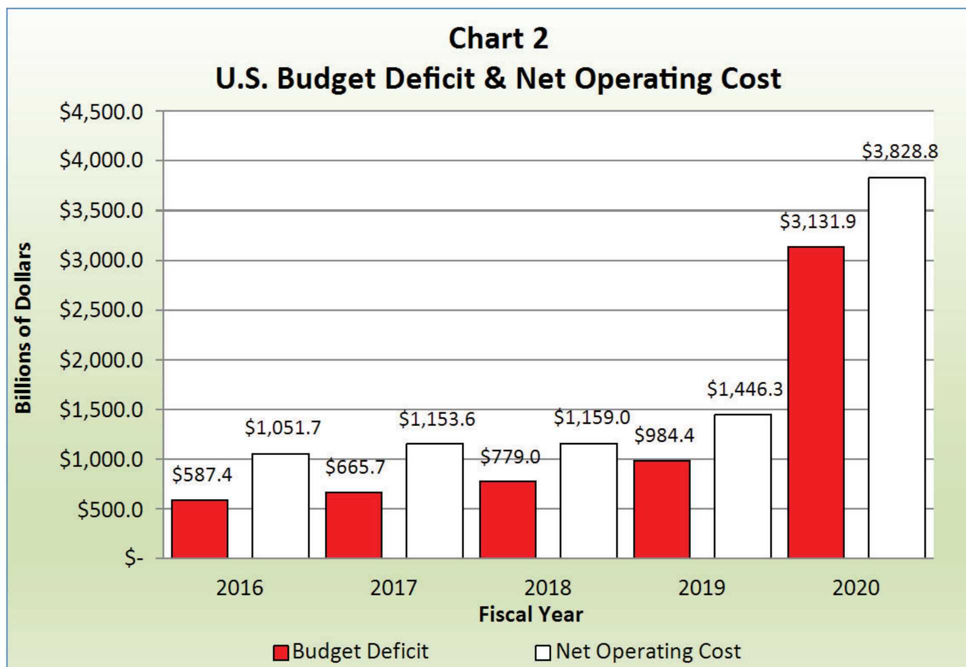
Each year, the Administration issues two reports that detail the government's financial results: the *Budget* and this *Financial Report*. The exhibit on the following page provides the key characteristics and differences between the two documents.

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

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

Budget Deficit vs. Net Operating Cost

The budget deficit is measured as the excess of outlays, or payments made by the government, over receipts, or cash received by the government. Net operating cost, on an accrual basis, is the excess of costs (what the government has incurred but has not necessarily paid) over revenues (what the government has collected and expects to collect but has not necessarily received). As shown in Chart 2, net operating cost typically exceeds the budget deficit due largely to the inclusion of cost accruals associated with increases in estimated liabilities for the government's postemployment benefit programs for its military and civilian employees and veterans as well as environmental liabilities.



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

The government's primarily cash-based[10] budget deficit increased by $2.1 trillion (about 218.2 percent) from approximately $984.4 billion in FY 2019 to about $3.1 trillion in FY 2020 due to a combined slight decrease in receipts and a significant increase in outlays in FY 2020. The $42.2 billion (1.2 percent) decrease in receipts can be attributed primarily to lower net individual and corporation income tax receipts and excise taxes, partially offset by higher social insurance and retirement receipts and deposits of earnings by the Federal Reserve. Outlays increased $2.1 trillion (47.3 percent). Contributing to the dollar increase over FY 2019 were higher outlays for Medicare, Defense, Medicaid, Social Security, Treasury and SBA.[11]

Treasury's September 2020 MTS is the source of receipts, spending, and deficit information for this Report. The MTS presents primarily cash-based spending, or outlays, for the fiscal year in a number of ways, including by month, by entity, and by budget function classification. The federal budget is divided into approximately 20 categories, or budget functions, as a means of organizing federal spending by primary purpose (e.g., National Defense, Transportation, and Health). Multiple entities may contribute to one or more budget functions, and a single budget function may be associated with only one entity. For example, DOD, DHS, DOE, and multiple other entities administer programs that are critical to the broader functional classification of National Defense. DOD, OPM, and many other entities also administer Income Security programs (e.g., retirement benefits, housing, financial assistance). By comparison, the Medicare program is a budget function category unto itself and is administered exclusively at the federal level by HHS. Federal spending information by budget function and other categorizations may be found in the September 2020 MTS.[12]

The government's largely accrual-based net operating cost increased by $2.4 trillion (164.7 percent) to $3.8 trillion during FY 2020. As explained below, net operating costs are affected by both changes in revenues and costs.

Table 3 provides a summary of the items reported in the *Reconciliation of Net Operating Cost and Budget Deficit,* which articulates the relationship between the government's accrual-based net operating cost and the primarily cash-based budget deficit. From Table 3, the $696.9 billion net difference between the government's budget deficit and net operating cost for FY 2020, is mostly attributable to: 1) a $969.0 billion net increase in liabilities for federal employee and veteran benefits payable; 2) a $91.1 billion increase in net taxes receivable; 3) a $44.9 billion timing difference between when credit reform costs are recorded in the budget versus net operating cost; and 4) a $150.7 billion net change in Other Assets, attributed mostly to advances and prepayments for certain COVID-19 related programs (see Note 10—Other Assets).

Table 3: Net Operating Cost vs. Budget Deficit

Dollars in Billions	2020	2019*
Net Operating Cost	**$ (3,828.8)**	**$ (1,446.3)**
Changes in:		
Federal Employee and Veteran Benefits Payable	$ 969.0	$ 458.0
Taxes Receivable, Net	$ (91.1)	$ (89.1)
Other Assets	$ (150.7)	$ 1.2
Timing Differences - Credit Reform Costs	$ 44.9	$ 45.3
Other, Net	$ (75.2)	$ 46.5
Subtotal - Net Difference:	$ 696.9	$ 461.9
Budget Deficit	**$ (3,131.9)**	**$ (984.4)**

*Restated (see Financial Statement Note 1.U)

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

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

[10] Interest outlays on Treasury debt held by the public are recorded in the budget when interest accrues, not when the interest payment is made. For federal credit programs, outlays are recorded when loans are disbursed, in an amount representing the PV cost to the government, commonly referred to as credit subsidy cost. Credit subsidy cost excludes administrative costs.
[11] 10/16/20 press release -- Joint Statement of Treasury Secretary Steven T. Mnuchin and OMB Director Russell Vought on Budget Results for FY 2020.
[12] Final MTS for FY 2020 through September 30, 2020 and Other Periods.

Financial Effects of the Federal Government's Pandemic Response

The financial effects of the government's response to the COVID-19 pandemic were broad, impacting many agencies in a variety of ways and to varying degrees. This section includes brief discussions of some of the more significant effects of the pandemic on the government's financial results for FY 2020. Please refer to Note 28—COVID-19 Activity and other disclosures in this *Financial Report*, as well as in the individual entities' financial statements for more information.

Costs and Revenues

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

Table 4: Gross Cost, Revenues, Net Cost, and Net Operating Cost

Dollars in Billions		2020		2019*	Increase / (Decrease) $	%
Gross Cost	**$**	**(7,194.1)**	**$**	**(5,287.2)**	**$ 1,906.9**	**36.1%**
Less: Earned Revenue	$	461.6	$	418.4	$ 43.2	10.3%
Gain/(Loss) from Changes in Assumptions	$	(679.5)	$	(198.9)	$ 480.6	241.6%
Net Cost	**$**	**(7,412.0)**	**$**	**(5,067.7)**	**$ 2,344.3**	**46.3%**
Less: Tax and Other Revenues	**$**	**3,571.6**	**$**	**3,621.0**	**$ (49.4)**	**(1.4%)**
Unmatched Transactions and Balances	$	11.6	$	0.4	$ 11.2	2,800.0%
Net Operating Cost	**$**	**(3,828.8)**	**$**	**(1,446.3)**	**$ 2,382.5**	**164.7%**

*Restated (see Financial Statement Note 1.U)

Table 4 shows that the government's "bottom line" net operating cost increased $2.4 trillion (164.7 percent) during 2020 from $1.4 trillion to $3.8 trillion. This increase is due mostly to a $2.3 trillion (46.3 percent) increase in entity net costs, combined with a $49.4 billion (1.4 percent) decrease in tax and other revenues over the past fiscal year as discussed in the following.

Gross Cost and Net Cost

The Statement of Net Cost starts with the government's total gross costs of $7.2 trillion, subtracts revenues earned for goods and services provided (e.g., Medicare premiums, national park entry fees, and postal service fees), and adjusts the balance for gains or losses from changes in actuarial assumptions used to estimate certain liabilities, including federal employee and veteran benefits to derive its net cost of $7.4 trillion (See Chart 3), a $2.3 trillion (46.3 percent) increase over FY 2019.

Typically, the annual change in the government's net cost is impacted by a variety of offsetting increases and decreases across entities. For example, offsetting changes in net cost during FY 2020 included:

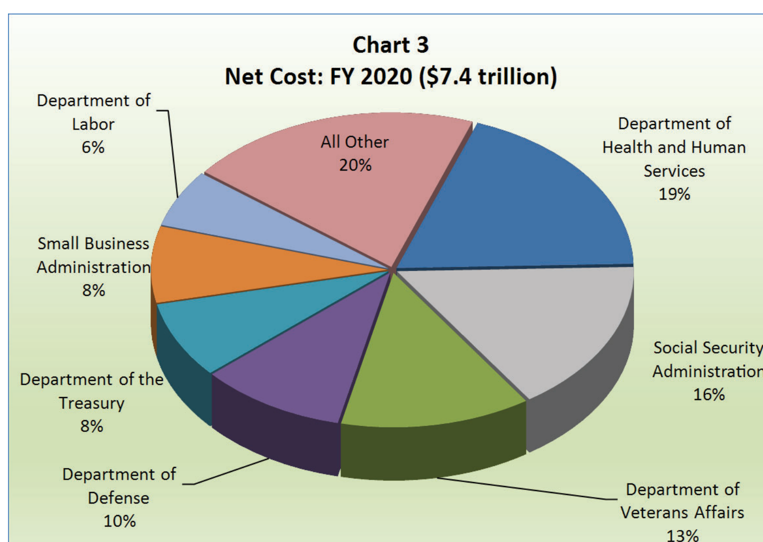
- As referenced earlier, the federal government's response to the COVID-19 pandemic had significant effects on agency and government-wide financial results. Congress appropriated $2.6 trillion as of September 30, 2020, which translated into substantial increases in costs across multiple agencies, including but not limited to:
    - The primary driver of a $559.1 billion increase in SBA net costs is a $527.8 billion increase in loan subsidy costs, including reestimates, attributable to the PPP and Debt Relief programs under the CARES Act. As noted earlier, the PPP provides loan forgiveness for amounts used for eligible expenses for payroll and benefit costs. Under the Debt Relief program, SBA pays six months of principal, interest, and any associated fees that borrowers owe for all current loans in regular servicing status in its 7(a), 504, and Microloan programs, as well as new 7(a), 504, and Microloans disbursed prior to September 27, 2020;
    - The $405.0 billion increase in Treasury net costs is largely due to payments issued to individuals pursuant to the CARES Act to help stimulate the economy through recovery rebates for individuals (also referred to

[13] As shown in Table 4, net operating cost includes an adjustment for unmatched transactions and balances, which represent unreconciled differences in intra-governmental activity and balances between federal entities. These amounts are described in greater detail in the Other Information section of this *Financial Report*.

as EIPs). In FY 2020, the IRS disbursed $274.7 billion of EIPs to eligible recipients in every state and territory and at foreign addresses. Treasury's net cost increase is also due in part from Coronavirus relief fund payments made to affected states, local, territorial, and tribal governments. $80.6 billion of the $149.5 billion of such payments made was recognized as net costs in FY 2020. Treasury costs also include $28.2 billion of financial assistance payments to passenger air carriers, air cargo carriers, and contractors to provide payroll support to aviation workers during the pandemic;

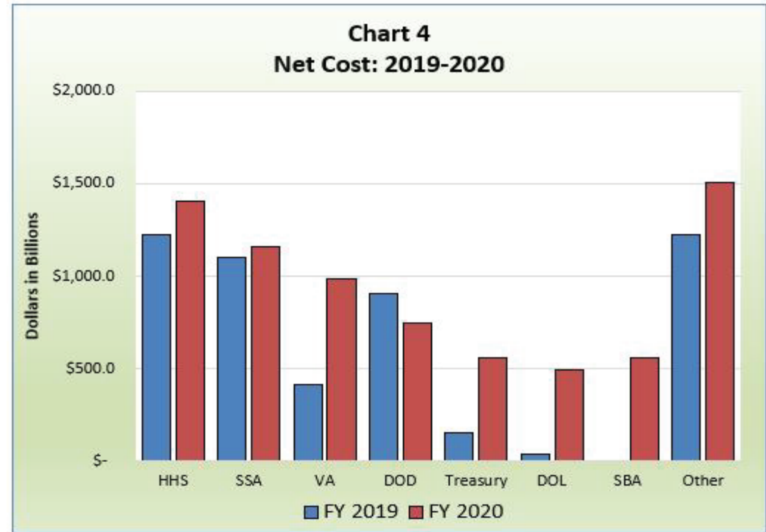
  - $115.2 billion out of a total $184.8 billion net cost increase at HHS is primarily due to increases to the PHSSEF, which, as noted earlier, funds a wide array of pandemic response efforts, including, but not limited to: 1) Provider Relief Fund, which provides payments to assist eligible health care providers for health care related expenses or lost revenues attributed to the pandemic, 2) SNS, and 3) vaccine, therapeutic and diagnostic research and development; and
  - A significant portion of the $452.7 billion increase at DOL is attributable to a $461.4 billion increase in Income Maintenance programs costs, primarily due to unemployment benefits authorized by the CARES Act. These programs include the FPUC program, which provided an additional $600 of weekly unemployment benefits and the PUA program, which provides temporary benefits for individuals who are not eligible for regular/traditional UI, respectively.

- Entities administering federal employee and veteran benefits programs employ a complex series of assumptions, including but not limited to interest rates, beneficiary eligibility, life expectancy, and medical cost levels, to make actuarial projections of their long-term benefits liabilities. Changes in these assumptions can result in either losses (net cost increases) or gains (net cost decreases). Across the government, these net losses from changes in assumptions amounted to $679.5 billion in FY 2020, a loss increase (and a corresponding net cost increase) of $480.6 billion compared to FY 2019. The primary entities that administer programs impacted by these assumptions – typically federal employee pension and benefit programs – are the OPM, VA, and DOD. These entities recorded losses and gains from changes in assumptions in the amounts of $89.9 billion loss, $602.7 billion loss, and $17.4 billion gain, respectively. These actuarial estimates and the resulting gains or losses from changes in assumptions can sometimes cause significant swings in total entity costs from year to year. For example, for FY 2020, changes in net cost at OPM ($67.3 billion increase), VA ($567.4 billion increase), and DOD ($163.4 billion decrease), were impacted by the corresponding changes in gains or losses from assumption changes at these entities.



- While most of the $163.4 billion decrease in DOD net costs is primarily due to a $156.4 billion loss decrease (net gain) from changes in assumptions as referenced above, the majority of DOD's net costs included military operations, readiness, and support; procurement; military personnel; and R&D, which collectively decreased slightly.

- $184.8 billion and $56.4 billion increases at HHS and SSA, respectively, were due to pandemic response at HHS as discussed above as well as to cost increases of the benefit programs that these entities administer (HHS – Medicare and Medicaid programs, SSA – OASDI programs).
- As referenced above, VA net costs increased $567.4 billion due largely to changes in benefits program experience and assumptions, including, but not limited to an increase in veterans who first became eligible for benefits during FY 2020.
- DHS costs increased by $49.7 billion due to costs associated with disaster responses to COVID-19, hurricanes, and wildfires.

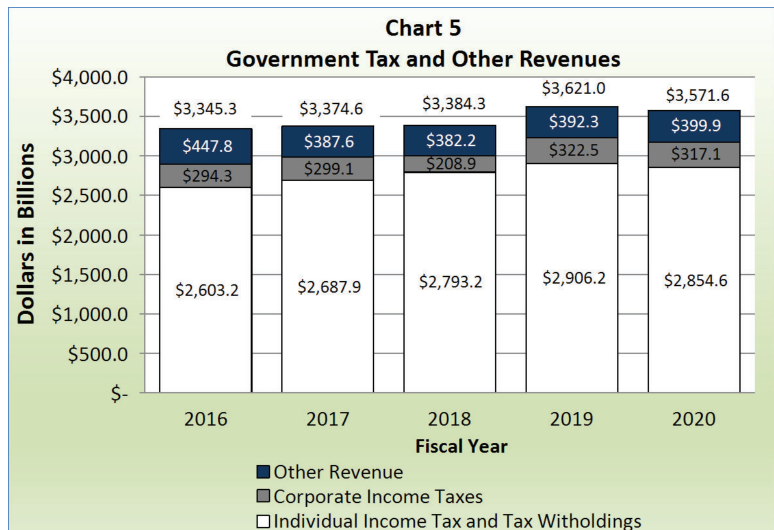


- A $32.5 billion decrease in interest on debt held by the public due largely to a decrease in average interest rates on outstanding debt held by the public.

Chart 3 shows the composition of the government's net cost. In FY 2020, 80 percent of the federal government's total net cost came from only seven agencies: HHS, SSA, VA, DOD, Treasury, DOL, and SBA. The other more than 150 entities included in the government's FY 2020 Statement of Net Cost accounted for a combined 20 percent of the government's total net cost for FY 2020. Chart 4 shows the two-year trend in these costs, illustrating the significant impact that the pandemic had on certain agency costs as summarized above. Aside from pandemic relief costs, as discussed above, HHS and SSA net costs for FY 2020 ($1.4 trillion and $1.2 trillion, respectively) are attributable to major social insurance programs administered by these entities. VA net costs of $985.0 billion support health, education and other benefits programs for our nation's Veterans. DOD net costs of $745.0 billion relate primarily to operations, readiness, and support; personnel; research; procurement; and retirement and health benefits. Treasury net costs of $560.7 billion support a broad array of programs that promote conditions for sustaining economic growth and stability, protecting the integrity of our Nation's financial system, and effectively managing the U.S. government's finances and resources. SBA net costs of $559.0 billion support agency programs and services that enable the establishment and vitality of small businesses and by providing assistance in the economic recovery of communities after disasters.

Tax and Other Revenues

As noted earlier, tax and other revenues from the Statement of Operations and Changes in Net Position are deducted from total net cost to derive the government's "bottom line" net operating cost. Chart 5 shows that total tax and other revenue decreased by $49.4 billion or 1.4 percent to $3.6 trillion for FY 2020. This net decrease was due to primarily to a $51.6 billion decrease in individual tax revenue, compared with an offsetting, comparatively smaller decreases and increases in corporate and other tax revenue, respectively.[14] Taxes receivable increased $91.1 billion during FY 2020 principally due to increased unpaid transition taxes on foreign earnings pursuant to the TCJA, coupled with a decrease in the related allowance for uncollectible taxes receivable due to a change in the methodology for estimating collectability, and the CARES Act Section 2302 provision allowing employers to defer payment of FICA Social Security taxes. Earned revenues from Table 4 are not considered "taxes and other revenue" and, thus, are not shown in Chart 5. Individual income tax and tax withholdings and corporate income taxes accounted for about 79.9 percent and 8.9 percent of total revenue, respectively in FY 2020; other revenues from Chart 5 include Federal Reserve earnings, excise taxes, unemployment taxes, and customs duties.



[14] FY 2020 Treasury's financial statements, p. 42

As previously shown in Table 4, the decrease in tax and other revenue combined with the increase in net cost, yielded a $2.4 trillion increase to the government's bottom line net operating cost to $3.8 trillion for FY 2020.

Tax Expenditures

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

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

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

Assets and Liabilities

The government's net position at the end of the fiscal year is derived by netting the government's assets against its liabilities, as presented in the Balance Sheet (summarized in Table 5). The Balance Sheet does not include the financial value of the government's sovereign powers to tax, regulate commerce, or set monetary policy or value of nonoperational resources of the government, such as national and natural resources, for which the government is a steward. In addition, as is the case with the Statement of Operations and Changes in Net Position, the Balance Sheet includes a separate presentation of the portion of net position related to funds from dedicated collections. Moreover, the government's exposures are broader than the liabilities presented on the Balance Sheet. The government's future social insurance exposures (e.g., Medicare and Social Security) as well as other fiscal projections, commitments and contingencies, are reported in separate statements and disclosures. This information is discussed later in this MD&A section, the financial statements, and RSI sections of this *Financial Report*.

Table 5: Assets and Liabilities

Dollars in Billions	2020	2019*	Increase / (Decrease) $	Increase / (Decrease) %
Assets				
Cash & Other Monetary Assets	$ 1,926.9	$ 524.6	$ 1,402.3	267.3%
Direct Loans and Loan Guarantees Receivable, Net	$ 1,577.4	$ 1,425.8	$ 151.6	10.6%
Inventories & Related Property, Net	$ 379.7	$ 355.7	$ 24.0	6.7%
General Property, Plant & Equipment, Net	$ 1,145.0	$ 1,106.9	$ 38.1	3.4%
Other	$ 921.7	$ 579.0	$ 342.7	59.2%
Total Assets	**$ 5,950.7**	**$ 3,992.0**	**$ 1,958.7**	**49.1%**
Less: Liabilities, comprised of:				
Federal Debt and Interest Payable	$ (21,082.9)	$ (16,861.0)	$ 4,221.9	25.0%
Federal Employee & Veteran Benefits Payable	$ (9,409.3)	$ (8,440.3)	$ 969.0	11.5%
Other	$ (2,251.7)	$ (1,643.5)	$ 608.2	37.0%
Total Liabilities	**$ (32,743.9)**	**$ (26,944.8)**	**$ 5,799.1**	**21.5%**
Unmatched Transactions and Balances	$ (3.1)	$ (14.7)	**$ (11.6)**	**(78.9%)**
Net Position	**$ (26,796.3)**	**$ (22,967.5)**	**$ 3,828.8**	**16.7%**

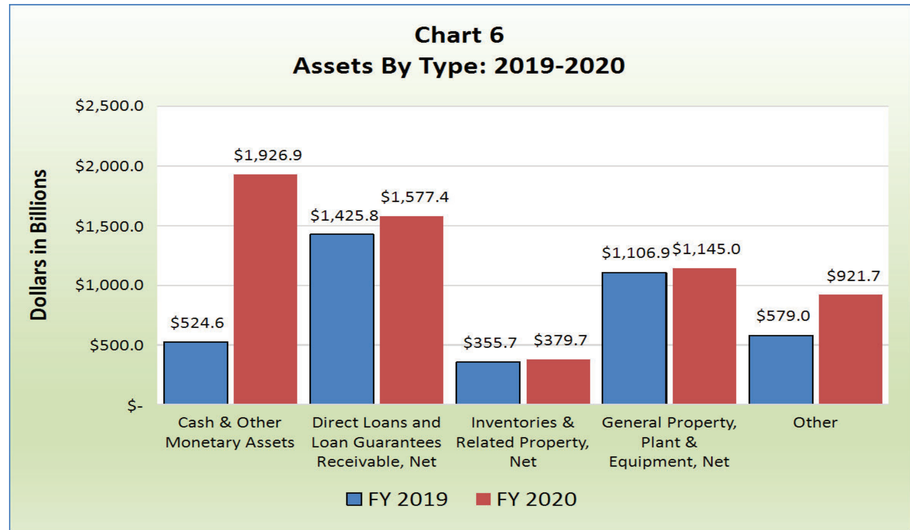
*Restated (see Financial Statement Note 1.U)

Assets

From Table 5, as of September 30, 2020, more than three-fourths of the government's $6.0 trillion in reported assets is comprised of: 1) cash and monetary assets ($1.9 trillion), 2) net loans receivable ($1.6 trillion), 3) and net PP&E ($1.1 trillion).[15] Chart 6 compares the balances of these and other balance sheet amounts as of September 30, 2020 and 2019, some of which were substantially impacted by the pandemic response.

Cash and monetary assets ($1.9 trillion) is comprised largely of the operating cash of the U.S. government. Operating cash held by Treasury increased $1.4 trillion (371 percent) to $1.8 trillion during FY 2020 largely due to Treasury maintaining an elevated cash balance to maintain prudent liquidity in light of the size and relative uncertainty of COVID-19--related outflows (see Note 2—Cash and Monetary Assets).

The federal government's direct loans and loan guarantee programs are used to promote the nation's welfare by making financing available to segments of the population not served adequately by non-federal institutions, or otherwise providing for certain activities or investments. For those unable to afford credit at the market rate, federal credit programs provide subsidies in the form of direct loans offered at an interest rate lower than the market rate. For those to whom non-federal financial institutions are reluctant to grant credit because of the high risk involved, federal credit programs guarantee the payment of these non-federal loans and absorb the cost of defaults. For example, Education supports individuals engaged in education programs through a variety of student loan, grant and other assistance programs. USDA administers loan programs to support the nation's farming and agriculture community. HUD loan programs support affordable homeownership, as well as the construction and rehabilitation of housing projects for the elderly and persons with disabilities. SBA loan programs enable the establishment and vitality of small businesses and assist in the economic recovery of communities after disasters. Significant changes to the federal government's direct loans and loan guarantees receivable and loan guarantees liability, as discussed in Note 4, include, but are not limited to:



- Education's Federal Direct Student Loan Program accounted for $1.1 trillion (69.8 percent) of total net direct loans and loan guarantees receivable. During FY 2020, Education's net loans receivable decreased by $32.4 billion, largely the result of net upward loan subsidy reestimates combined with loan modifications that increased the subsidy allowance by $97.7 billion, offset by increases in loans outstanding and accrued interest receivable. This change was due to a CARES Act provision and subsequently a Presidential Memorandum which provided support for student loan borrowers by temporarily suspending nearly all federal student loan payments, which increased costs to the government. In addition, all federal wage garnishments and collections actions for borrowers with federally held loans in default were halted.
- SBA's credit program receivables comprise business and disaster direct loans and defaulted business loans purchased per the terms of SBA's loan guaranty programs, offset by an allowance for related program subsidy costs. These receivables were valued at $182.9 billion as of FY 2020, stemming from a $173.2 billion increase in direct disaster loans primarily funded by the CARES Act. SBA's liability for loan guarantees increased $510.7 billion due to guarantees made under the PPP program.

Federal government PP&E includes many of the physical resources that are vital to the federal government's ongoing operations, including buildings, structures, facilities, equipment, internal use software, and general purpose land. DOD comprises approximately 69.0 percent of the government's reported PP&E of $1.1 trillion as of September 30, 2020.

"Other" Assets of $921.7 billion in Table 5 and Chart 6 includes: 1) $218.6 billion in "Advances and Prepayments" and 2) $108.4 billion of "Investments in SPVs". The $150.6 billion increase in this amount during FY 2020 is largely attributable to HHS and Treasury. HHS had an increase due to issuance of the COVID-19 AAP program and PHSSEF advances for personal protection equipment and test kits for COVID-19. Treasury provided Coronavirus Relief Fund financial assistance payments until such payments are either used by the recipients on or before December 31, 2021 (as extended – see Note 10) or returned unused to Treasury (see Note 10—Other Assets).

[15] For financial reporting purposes, other than multi-use heritage assets, stewardship assets of the government are not recorded as part of PP&E. Stewardship assets are comprised of stewardship land and heritage assets. Stewardship land consists of public domain land (e.g., national parks, wildlife refuges). Heritage assets include national monuments and historical sites that among other characteristics are of historical, natural, cultural, educational, or artistic significance. See Note 25—Stewardship Land and Heritage Assets.

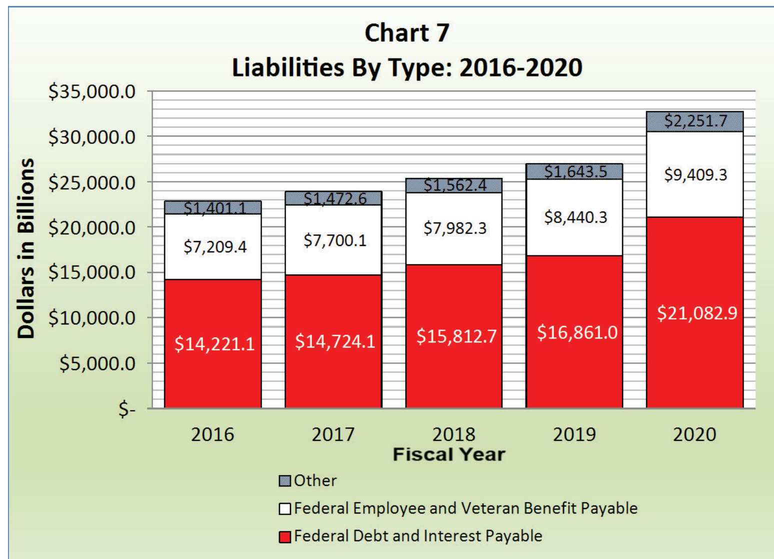
In addition, in response to the COVID-19 pandemic, under Section 4003 of the CARES Act, Treasury holds equity investments in SPVs established through the FRBNY and FRBB for the purpose of enhancing the liquidity of the U.S. financial system. These non-federal investment holdings are reported at their fair value on the Balance Sheet, and changes in the valuation of these investments are recorded on the Statement of Net Cost. See Note 8—Investments in Special Purpose Vehicles, and Note 28—COVID-19 Activity, as well as Treasury's FY 2020 financial statements for additional information.

Please refer to Note 28—COVID-19 Activity, as well as the FY 2020 entities financial statements for additional information about the pandemic's effects on the federal government's costs and revenues over the past fiscal year.

In addition, as indicated earlier, Note 29—Subsequent Events, discusses the financial effects of significant events that occurred following the end of the fiscal year, but prior to issuance of this *Financial Report*. For example, On December 27, 2020, the President signed into law the *Consolidated Appropriations Act, 2021* (P.L. 116-120). Effective January 9, 2021, this statue eliminates Treasury's ability to make new loans and investments under Section 4003 of the CARES Act (SPVs). These and other subsequent events and their effects are discussed in Note 29.

Liabilities

As indicated in Table 5 and Chart 7, of the government's $32.7 trillion in total liabilities, the largest liability is federal debt and interest payable, the balance of which increased by $4.2 trillion (25.0 percent) to $21.1 trillion as of September 30, 2020.



The other major component of the government's liabilities is federal employee and veteran benefits payable (i.e., the government's pension and other benefit plans for its military and civilian employees), which increased $969.0 billion (11.5 percent) during FY 2020, to about $9.4 trillion. This total amount is comprised of $2.7 trillion in benefits payable for the current and retired civilian workforce, and $6.7 trillion for the military and veterans. OPM administers the largest civilian pension plan, covering about 2.8 million current employees and 2.7 million annuitants and survivors. The military pension plan covers about 2.1 million current military personnel (including active service, reserve, and National Guard) and approximately 2.3 million retirees and survivors.

Federal Debt

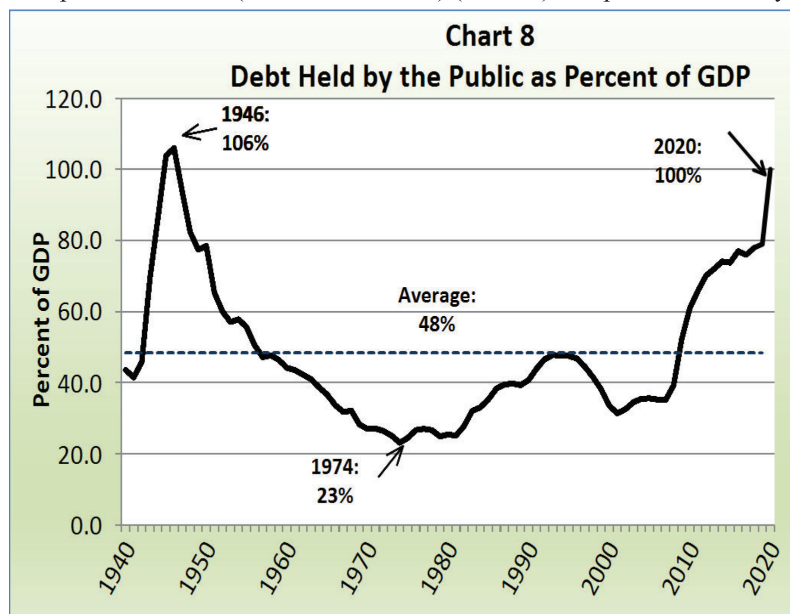
The budget surplus or deficit is the difference between total federal spending and receipts (e.g., taxes) in a given year. The government borrows from the public (increases federal debt levels) to finance deficits. During a budget surplus (i.e., when receipts exceed spending), the government typically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

The government's federal debt and interest payable (Balance Sheet liability), which is comprised of publicly-held debt and accrued interest payable, increased $4.2 trillion (25.0 percent) to $21.1 trillion as of September 30, 2020. It is comprised of Treasury securities, such as bills, notes, and bonds, net of unamortized discounts and premiums issued or sold to the public; and accrued interest payable. The "public" consists of individuals, corporations, state and local governments, FRBs, foreign governments, and other entities outside the federal government. As indicated above, budget surpluses have typically resulted in borrowing reductions, and budget deficits have conversely yielded borrowing increases. However, the government's debt operations are generally much more complex. Each year, trillions of dollars of debt mature and new debt is issued to take its place. In FY 2020, new borrowings were $19.0 trillion, and repayments of maturing debt held by the public were $14.8 trillion, both increases from FY 2019.

Prior to 1917, Congress approved each debt issuance. In 1917, to facilitate planning in World War I, Congress and the President established a dollar ceiling for federal borrowing. With the *Public Debt Act of 1941* (P.L. 77-7), Congress and the President set an overall limit of $65 billion on Treasury debt obligations that could be outstanding at any one time. Since then, Congress and the President have enacted a number of measures affecting the debt limit, including several in recent years. Congress and the President most recently suspended the debt limit from August 2, 2019 through July 31, 2021. It is important to note that increasing or suspending the debt limit does not increase spending or authorize new spending; rather, it permits the U.S. to continue to honor pre-existing commitments to its citizens, businesses, and investors domestically and around the world.

In addition to debt held by the public, the government has about $6.0 trillion in intra-governmental debt outstanding, which arises when one part of the government borrows from another. It represents debt issued by Treasury and held by government accounts, including the Social Security ($2.9 trillion) and Medicare ($221.2 billion) trust funds. Intra-governmental debt is primarily held in government trust funds in the form of special nonmarketable securities by various parts of the government. Laws establishing government trust funds generally require excess trust fund receipts (including interest earnings) over disbursements to be invested in these special securities. Because these amounts are both liabilities of Treasury and assets of the government trust funds, they are eliminated as part of the consolidation process for the government-wide financial statements (see Note 12). When those securities are redeemed, e.g., to pay Social Security benefits, the government must obtain the resources necessary to reimburse the trust funds. The sum of debt held by the public and intra-governmental debt equals gross federal debt, which (with some adjustments), is subject to a statutory ceiling (i.e., the debt limit). At the end of FY 2020, debt subject to the statutory limit was $26.9 trillion[16] (see sidebar).

The federal debt held by the public measured as a percent of GDP (debt-to-GDP ratio) (Chart 8) compares the country's debt to the size of its economy, making this measure sensitive to changes in both. Over time, the debt-to-GDP ratio has varied widely:



- For most of the nation's history, through the first half of the 20th century, the debt-to-GDP ratio has tended to increase during wartime and decline during peacetime.
- Chart 8 shows that wartime spending and borrowing pushed the debt-to-GDP ratio to an all-time high of 106 percent in 1946, soon after the end of World War II, but it decreased rapidly in the post-war years.
- The ratio grew rapidly from the mid-1970s until the early 1990s. Strong economic growth and fundamental fiscal decisions, including measures to reduce the federal deficit and implementation of binding PAYGO rules (which require that new tax or spending laws not add to the deficit), generated a significant decline in the debt-to-GDP ratio, from a peak of 48 percent in 1993-1995, to 31 percent in 2001.
- During the first decade of the 21st century, PAYGO rules were allowed to lapse, significant tax cuts were implemented, entitlements were expanded, and spending related to defense and homeland security increased. By September 2008, the debt-to-GDP ratio was 39 percent of GDP.
- PAYGO rules were reinstated in 2010, but the extraordinary demands of the last economic and fiscal crisis and the consequent actions taken by the federal government, combined with slower economic growth in the wake of the crisis, pushed the debt-to-GDP ratio up to 74 percent by the end of FY 2014.
- The debt was 100 percent of GDP at the end of FY 2020 (compared to 79 percent at the end of FY 2019 and as reported in the FY 2019 *Financial Report*).[17] From Chart 8, since 1940, the average debt-to-GDP ratio is 48 percent.

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[16] During FYs 2019 and 2018, Treasury faced two delays in raising the statutory debt limit that required it to depart from its normal debt management procedures and to invoke legal authorities to avoid exceeding the statutory debt limit. During these periods, extraordinary actions taken by Treasury have resulted in federal debt securities not being issued to certain federal government accounts with the securities being restored including lost interest to the affected federal government accounts subsequent to the end of the delay period. The first delay occurred beginning on December 9, 2017 and ending on February 9, 2018, with the enactment of the BBA of 2018 (P.L. 115-123) which suspended the statutory debt limit through March 1, 2019. The second delay in raising the statutory debt limit occurred beginning on March 2, 2019 and ending on August 2, 2019, with the enactment of the BBA of 2019 (P.L. 116-37) which suspended the statutory debt limit through July 31, 2021.

[17] Joint Statement of Treasury Secretary Steven T. Mnuchin and OMB Director Russell Vought on Budget Results for FY 2020.

The Economy in FY 2020

Table 6: National Economic Indicators*		
	FY 2020	FY 2019
Real GDP Growth	-2.8%	2.1%
Personal Consumption Expenditures	-2.8%	2.5%
Average monthly payroll job change (thousands)	-789	164
Unemployment rate (percent, end of period)	7.8%	3.5%
Consumer Price Index (CPI)	1.4%	1.7%
CPI, excluding food and energy	1.7%	2.4%
Real Disposable Personal Income	5.7%	2.0%
Real Average Hourly Earnings	3.2%	2.3%

* Some FY2019 data may differ from the FY2019 Financial Report due to updates and revisions.

A review of U.S. economic performance can help place the discussion of the government's financial statements in a broader context. Yet, in the latest fiscal year, further consideration of the effects of an external shock, the COVID-19 global pandemic, and the U.S. government's response, is also warranted.

The economy ended FY 2019 on a firm footing, with the unemployment rate at a half-century low, strong wage growth, and a pace of job creation more than sufficient to account for new entrants to the labor force. Through the first five months of FY 2020, the pace of payroll job growth accelerated to 219,000 per month, and the unemployment stood at 3.5 percent, the half-century low seen at the end of FY 2019. In addition, the labor force participation rate climbed to a six-year high in February 2020, and housing sector activity became increasingly buoyant. By February 2020, business and consumer sentiment had advanced to multi-year highs as well.

However, the spread of the COVID-19 virus ended the longest recovery in U.S. history in February 2020 at 128 months. The economy contracted sharply in the second and third quarters of FY 2020 as state and local governments implemented stay-at-home orders and mandated closures of non-essential businesses to mitigate the impact of the pandemic on health care resources. Meanwhile, the U.S. government responded quickly with unprecedentedly bold measures to support American households and small businesses during the pandemic. By March 27, 2020 – or roughly two weeks after stay-at-home orders were issued, three record-setting economic aid packages were passed totaling roughly $2.6 trillion. The administration rapidly implemented the various measures, including EIPs, expanded eligibility for UI payments, and the PPP, which provided forgivable loans to small businesses to encourage employee retention. These measures boosted household liquidity, contributed to a rapid reduction in unemployment, and allowed small businesses to maintain viability until their local economies reopened. Due to the relaxation of stay-at-home orders and this robust response, the economy expanded in the final quarter of FY 2020 at the fastest quarterly rate in seventy years, accompanied by a brisk pace of payroll job growth and strong growth in wages.

As summarized in Table 6, U.S. economic growth slowed markedly over FY 2020 as a whole compared with FY 2019. Real (i.e., inflation-adjusted) GDP declined by 2.8 percent over the four quarters of FY 2020, following growth of 2.1 percent during the previous fiscal year. A temporary collapse in personal consumption expenditures lead the overall contraction in the latest fiscal year, and business fixed investment also declined sharply. However, residential investment, government spending, net exports, and private inventory investment all supported growth. Over the four quarters of FY 2020, consumer spending contracted by 2.8 percent after growing by 2.5 percent the previous fiscal year. Early in the latest fiscal year, business fixed investment had been constrained by ongoing headwinds, including slowing global growth, policy uncertainty, low oil prices, and disruptions at specific domestic companies. The onset of the pandemic also put investment plans on hold, such that business fixed investment declined 4.5 percent in FY 2020, after growing 2.7 percent in FY 2019. Residential investment, despite a temporary setback in mid-2020, led growth in the latest fiscal year, with a gain of 7.2 percent following a 1.2 percent contraction in FY 2019. A smaller increase in government spending in the latest fiscal year (a 0.3 percent rise for FY 2020 as a whole, following a 2.2 percent advance in FY 2019), masked the significant increase in federal government expenditures in April 2020 to support the economy. Net exports made an essentially neutral contribution to growth while inventory investment contributed positively to real GDP growth in FY 2020; in the previous fiscal year, each of these components had posed a small drag on growth.

Although labor market strength was evident in the first five months of FY 2020, the imposition of stay-at-home orders and mandated business closures reduced economic activity severely, and the unemployment rate jumped to a post-World War II high of 14.8 percent in April 2020. More than 22 million payroll jobs were lost over March and April, but in May, job creation resumed, far earlier than expected. By the end of FY 2020, the unemployment rate had fallen by 6.8 percentage points to 7.8 percent, and a total of 11.5 million jobs had been recovered.

Continuing the trend seen over FY 2019, headline inflation slowed, during FY 2020, reflecting lower oil prices, but also weaker aggregate demand. Core inflation (excludes food and energy), which had accelerated modestly during FY 2019, also slowed in the latest fiscal year. The CPI rose 1.4 percent over the twelve months of FY 2020, decelerating from the 1.7 percent pace during the previous fiscal year. Core inflation was 1.7 percent over the FY ending September 2020, decelerating from the 2.4 percent pace during FY 2019.

Relatively low inflation and stronger nominal DPI growth helped to boost purchasing power in real terms in FY 2020. Real DPI grew 5.7 percent over the twelve months of FY 2020, after growing by 2.0 percent during the previous fiscal year.

Nominal average hourly earnings grew at a consistently strong pace during the first half of FY 2020, and grew faster during the second half, reflecting the temporary unemployment of lower-wage workers. Slower inflation helped boost wages in real terms. Real average hourly earnings increased 3.0 percent during FY 2020, after rising 2.3 percent during the previous fiscal year. Growth of non-farm labor productivity also accelerated over the four quarters of FY 2020, rising by 4.0 percent after growing 1.7 percent during FY 2019.

An Unsustainable Fiscal Path

An important purpose of the *Financial Report* is to help citizens understand current fiscal policy and the importance and magnitude of policy reforms necessary to make it sustainable. This *Financial Report* includes the SLTFP and a related Note Disclosure (Note 24). The Statements display the PV of 75-year projections of the federal government's receipts and non-interest spending[18] for FY 2020 and FY 2019.

Fiscal Sustainability

A sustainable fiscal policy is defined as one where the debt-to-GDP ratio is stable or declining over the long term. The projections based on the assumptions in this *Financial Report* indicate that current policy is not sustainable. This report presents data, including debt, as a percent of GDP to help readers assess whether current fiscal policy is sustainable. The debt-to-GDP ratio reached 100 percent at the end of FY 2020. The long-term fiscal projections in this report are based on the same economic and demographic assumptions that underlie the 2020 Social Security and Medicare Trustees' Reports, and those assumptions were developed prior to the COVID-19 pandemic and economic downturn. At this time, management cannot reasonably estimate the potential effects of COVID-19 on the projections or other sustainability measures (such as projected depletion dates for the Social Security and Medicare Hospital Insurance Trust Funds in Table 10 below), which could be significant. As discussed below, if current policy is left unchanged and based on this report's assumptions, the debt-to-GDP ratio is projected to rise to over 124 percent in 2030, and to 623 percent in 2095 and to even higher levels, thereafter. Preventing the debt-to-GDP ratio from rising over the next 75 years is estimated to require some combination of spending reductions and revenue increases that amount to 5.4 percent of GDP over the period. While this estimate of the "75-year fiscal gap" is highly uncertain, it is nevertheless nearly certain that current fiscal policies cannot be sustained indefinitely.

Delaying action to reduce the fiscal gap increases the magnitude of spending and/or revenue changes necessary to stabilize the debt-to-GDP ratio. For example, the magnitude of spending cuts and/or revenue increases necessary to close the gap rises about 18.5 percent if reforms are delayed ten years, and a further 21.9 percent if reform is delayed 20 years.

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

The projections discussed here assume current policy[19] remains unchanged, and hence, are neither forecasts nor predictions. Nevertheless, the projections demonstrate that policy changes must be enacted to move towards fiscal sustainability.

The Primary Deficit, Interest, and Debt

The primary deficit – the difference between non-interest spending and receipts – is the determinant of the debt-to-GDP ratio over which the government has the greatest control (the other determinants include interest rates and growth in GDP). Chart 9 shows receipts, non-interest spending, and the difference – the primary deficit – expressed as a share of GDP. The primary deficit-to-GDP ratio spiked during 2009 through 2012 due to the 2008-09 financial crisis and the ensuing severe recession, as well as the increased spending and temporary tax reductions enacted to stimulate the economy and support recovery. These elevated primary deficits resulted in a sharp increase in the ratio of debt to GDP, which rose from 39 percent at the end of 2008 to 70 percent at the end of 2012. As an economic recovery took hold, the primary deficit ratio fell, averaging 2.1 percent of GDP over 2013 through 2019, The primary deficit-to-GDP ratio again spiked in 2020, rising to 13.3 percent of GDP in 2020, due to increased spending to address the COVID-19 pandemic and lessen the economic impacts of stay-at-home and social distancing orders on individuals, hard-hit industries, and small businesses.

The primary deficit ratio is projected to fall to 6.0 percent in 2021 and then shrink to 2.9 percent in 2023 as the economy grows and spending due to legislation enacted in response to the COVID-19 pandemic decreases. After 2023, however, increased spending for Social Security and health programs due to the ongoing retirement of the baby boom generation and

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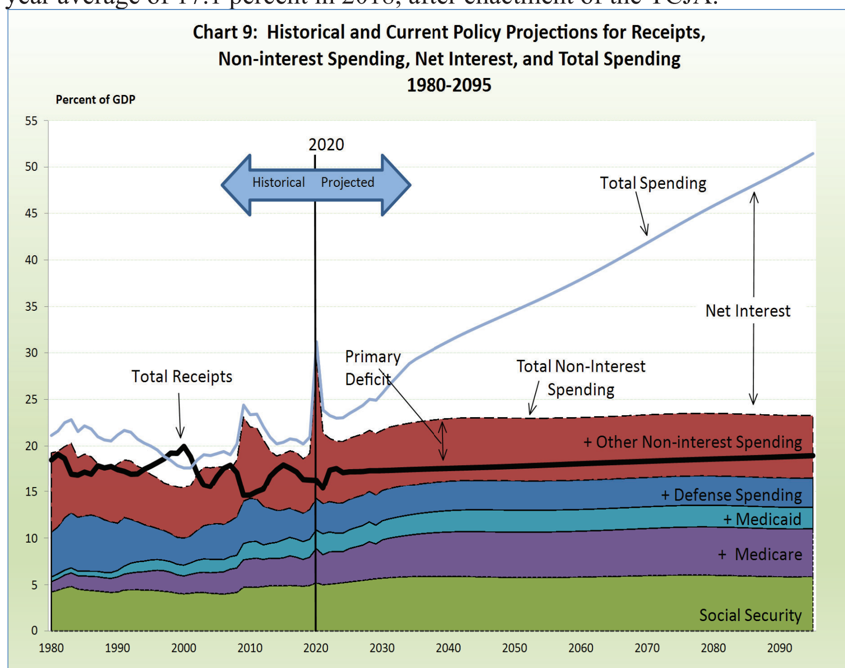
[18] For the purposes of the SLTFP and this analysis, spending is defined in terms of outlays. In the context of federal budgeting, spending can either refer to: 1) budget authority – the authority to commit the government to make a payment; 2) obligations – binding agreements that will result in either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

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

increases in the price of health care services is projected to result in increasing primary deficit ratios that reach 4.4 percent of GDP in 2030. The primary deficit ratio peaks at 5.4 percent in 2042, gradually decreases beyond that point as aging of the population continues at a slower pace, and reaches 4.3 percent of GDP in 2095.

Primary deficit trends are heavily influenced by tax receipts. Receipts as a share of GDP were markedly depressed in 2009 through 2012 because of the recession and tax reductions enacted as part of the ARRA and the *Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010*. The share subsequently increased to 18.0 percent of GDP by 2015, before falling below the 30-year average of 17.1 percent in 2018, after enactment of the TCJA.



Receipts were 16.3 percent of GDP in 2020. After 2024, receipts grow slightly more rapidly than GDP over the projection period as increases in real incomes cause more taxpayers and a larger share of income to fall into the higher individual income tax brackets.

On the spending side, the non-interest spending share of GDP, which was 29.6 percent in 2020, is projected to fall to 20.5 percent in 2024. After 2024, the non-interest spending share of GDP is projected to rise gradually from 20.8 percent in 2025 to 23.5 percent of GDP in 2078, and ends at 23.3 percent in 2095, the end of the projection period. Beginning in 2025, these increases are principally due to faster growth in Medicare, Medicaid, and Social Security spending (see Chart 9). Over the next 20 years, the spending shares of GDP of Social Security and Medicare are projected to increase by about 0.9 and 1.5 percentage points, respectively, from 2021 to 2040. The spending share of GDP for Medicaid stays roughly the same over that period. After 2040, the Social Security and Medicaid spending share of GDP remains relatively stable, while the Medicare spending share of GDP continues to increase through 2082, albeit at a slower rate, due to projected increases in health care costs and population aging.

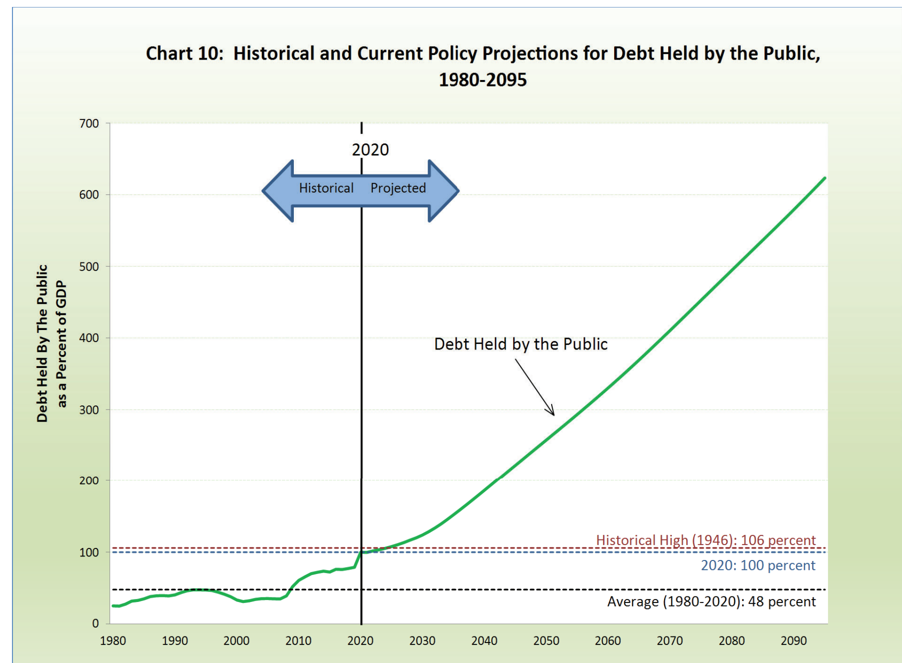
On a PV basis, deficit projections reported in the FY 2020 *Financial Report* increased in both present-value terms and as a percent of the current 75-year PV of GDP. As discussed in Note 24, the largest factors affecting the projections were actual budget results for FY 2020 and the budget estimates published in the FY 2021 President's Budget. This includes lower individual income tax receipts and higher spending for mandatory programs other than Social Security, Medicare, and Medicaid. Other factors affecting the change in these projections included updates of economic and demographic assumptions which increases the imbalance by 0.3 percent of the 75-year present value of GDP ($8.1 trillion), including lower population growth, which lowers wage projections and decreases individual income tax and social insurance receipts; the effect of new Social Security, Medicare, and Medicaid program-specific actuarial assumptions and the change in reporting period - the effect of shifting calculations from 2020 through 2094 to 2021 through 2095.

One of the most important assumptions underlying the projections is the future growth of health care costs. As discussed in Note 23, these future growth rates – both for health care costs in the economy generally and for federal health care programs such as Medicare, Medicaid, and PPACA exchange subsidies – are highly uncertain. In particular, enactment of the PPACA in 2010 and the MACRA in 2015 established cost controls for Medicare hospital and physician payments whose long-term effectiveness of which is not yet clear. The Medicare spending projections in the long-term fiscal projections are based on the projections in the 2020 Medicare Trustees' Report, which assume the PPACA and MACRA cost control measures will be effective in producing a substantial slowdown in Medicare cost growth. As discussed in Note 23, the Medicare projections are subject to much uncertainty about the ultimate effects of these provisions to reduce health care cost growth. For the long-term fiscal projections, that uncertainty also affects the projections for Medicaid and exchange subsidies, because the cost per beneficiary in these programs is assumed to grow at the same reduced rate as Medicare cost growth per beneficiary. The most recent Social Security and Medicare Trustees' Reports were released in April 2020, and the economic and demographic assumptions do not reflect the effects of the COVID-19 pandemic, increasing the uncertainty surrounding this year's long-term fiscal projections. At this time, management cannot reasonably estimate the potential effects of COVID-19 on the projections or other sustainability measures (such as projected depletion dates for the Social Security and Medicare Hospital Insurance Trust Funds in Table 10), which could be significant. See Note 24—Long-Term Fiscal Projections for additional information.

As discussed in Note 24 for the FY 2020 report, other key assumptions include, but are not limited to the following. For receipts, individual income taxes are based on the share of individual income taxes of salaries and wages in the FY 2021

President's Budget, and the salaries and wages projections in the Social Security 2020 Trustees' Report. That baseline accords with current policy as defined above, including the continuation of individual income and estate and gift tax provisions of the TCJA and the tendency of effective tax rates to increase as growth in income per capita outpaces inflation. Congressional action is required to make these changes. Similar to spending, the temporary receipt effects of legislation enacted in response to the COVID-19 pandemic are reflected through 2030 based on CBO estimates. Corporate income tax receipts are assumed to be the same share of GDP as projected in the President's Budget in the short term, which incorporates the expected effects of the TCJA, and then grow with GDP over the long term. For discretionary spending, the projections assume that discretionary spending stays within statutory caps that apply to 2021 under the 2019 BBA. Congressional action is required to fund this assumed discretionary spending. Similar to mandatory spending, discretionary spending from supplemental appropriations enacted in response to the COVID-19 pandemic is reflected through 2030, based on CBO estimates. GDP, interest, and other economic and demographic assumptions are the same as those that underlie the most recent Social Security and Medicare Trustees' Report projections, adjusted for historical revisions that occur annually. See Note 24—Long-Term Fiscal Projections for additional information about the assumptions used in this analysis.

The primary deficit-to-GDP projections in Chart 9, projections for interest rates, and projections for GDP together determine the debt-to-GDP ratio projections shown in Chart 10. That ratio was 100 percent at the end of FY 2020 and under current policy is projected to exceed the historic high of 106 percent in 2025, rise to 200 percent by 2042 and reach 623 percent by 2095. The change in debt held by the public from one year to the next generally represents the budget deficit, the difference between total spending and total receipts. The debt-to-GDP ratio rises continually in great part because primary deficits lead to higher levels of debt, which lead to higher net interest expenditures, and higher net interest expenditures lead to higher debt.[20] The continuous rise of the debt-to-GDP ratio indicates that current policy is unsustainable.



These debt-to-GDP projections are higher than the corresponding projections in both the 2019 and 2018 *Financial Reports*. For example, the last year of the 75-year projection period used in the FY 2018 *Financial Report* is 2093. In the FY 2020 *Financial Report*, the debt-to-GDP ratio for 2093 is projected to be 605 percent, which compares with 467 and 530 percent projected for that same year in the FY 2019 *Financial Report* and the FY 2018 *Financial Report,* respectively.[21]

The Fiscal Gap and the Cost of Delaying Policy Reform

The 75-year fiscal gap is one measure of the degree to which current policy is unsustainable. It is the amount by which primary surpluses over the next 75 years must, on average, rise above current-policy levels in order for the debt-to-GDP ratio in 2095 to remain at its level in 2020. The projections show that projected primary deficits average 4.8 percent of GDP over the next 75 years under current policy. If policies were adopted to eliminate the fiscal gap, the average primary surplus over the next 75 years would be 0.6 percent of GDP, 5.4 percentage points higher than the projected PV of receipts less non-interest spending shown in the basic financial statement. Hence, the 75-year fiscal gap is estimated to equal 5.4 percent of GDP. This amount is, in turn, equivalent to 30.2 percent of 75-year PV receipts and 23.8 percent of 75-year PV non-interest spending. The fiscal gap was estimated at 3.8 percent in the 2019 *Financial Report*.

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

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[20] The change in debt each year is also affected by certain transactions not included in the budget deficit, such as changes in Treasury's cash balances and the nonbudgetary activity of federal credit financing accounts. These transactions are assumed to hold constant at about 0.3 percent of GDP each year, with the same effect on debt as if the primary deficit was higher by that amount.

[21] See the Note 23 of the *FY 2019 Financial Report of the U.S. Government* for more information about changes in the long term fiscal projections between FYs 2018 and 2019.

Table 7	
Cost of Delaying Fiscal Reform	
Period of Delay	**Change in Average Primary Surplus**
Reform in 2021 (No Delay)	5.4 percent of GDP between 2021 and 2095
Reform in 2031 (Ten-Year Delay)	6.4 percent of GDP between 2031 and 2095
Reform in 2041 (Twenty-Year Delay)	7.8 percent of GDP between 2041 and 2095

Table 7 shows the cost of delaying policy reform to close the fiscal gap by comparing policy reforms that begin in three different years. Immediate reform would require increasing primary surpluses by 5.4 percent of GDP on average between 2021 and 2095 (i.e., some combination of reducing spending and increasing revenue by a combined 5.4 percent of GDP on average over the 75-year projection period). Table 7 shows that delaying policy reform forces larger and more abrupt policy reforms over shorter periods. For example, if policy reform is delayed by 10 years, closing the fiscal gap requires increasing the primary surpluses by 6.4 percent of GDP on average between 2031 and 2095. Similarly, delaying reform by 20 years requires primary surplus increases of 7.8 percent of GDP on average between 2041 and 2095. The differences between the required primary surplus increases that start in 2031 and 2041 (6.4 and 7.8 percent of GDP, respectively) and that which starts in 2021 (5.4 percent of GDP) is a measure of the additional burden that delay would impose on future generations. Future generations are harmed by policy reform delay, because the higher the primary surplus is during their lifetimes the greater the difference is between the taxes they pay and the programmatic spending from which they benefit.

Conclusion

The debt-to-GDP ratio is projected to rise over the 75-year projection period and beyond if current policy is unchanged, based on this report's assumptions, which implies that current policy is not sustainable and must ultimately change. If policy changes are not so abrupt as to slow economic growth, then the sooner policy changes are adopted to avert these trends, the smaller the changes to revenue and/or spending that would be required to achieve sustainability over the long term. While the estimated magnitude of the fiscal gap is subject to a substantial amount of uncertainty, it is nevertheless nearly certain that current fiscal policies cannot be sustained indefinitely.

These long-term fiscal projections and the topic of fiscal sustainability are discussed in further detail in Note 24 and the RSI section of this *Financial Report*.

Social Insurance

The long-term fiscal projections reflect government receipts and spending as a whole. The SOSI focuses on the government's "social insurance" programs: Social Security, Medicare, Railroad Retirement, and Black Lung.[22] For these programs, the SOSI reports: 1) the actuarial PV of all future program revenue (mainly taxes and premiums) - excluding interest - to be received from or on behalf of current and future participants; 2) the estimated future scheduled expenditures to be paid to or on behalf of current and future participants; and 3) the difference between 1) and 2). Amounts reported in the SOSI and in the RSI section in this *Financial Report* are based on each program's official actuarial calculations.

The SOSI projections are based on the same economic assumptions that underlie the Social Security Trustees' Report, and those assumptions were developed using data as of January 1, 2020, prior to the economic downturn. At this time, management cannot reasonably estimate the potential effects of COVID-19 on the SOSI or other sustainability measures (such as projected depletion dates for Social Security and Medicare Hospital Insurance Trust Fund in Table 10 below), which could be significant.

Table 8 summarizes amounts reported in the SOSI, showing that net social insurance expenditures are projected to be $65.5 trillion over 75 years as of January 1, 2020 for the "Open Group," an increase of $6.4 trillion over net expenditures of $59.1 trillion projected in the 2019 *Financial Report*.[23] The current-law 2020 amounts reported for Medicare reflect the physician payment levels expected under the MACRA payment rules and the PPACA-mandated reductions in other Medicare payment rates, but not the payment reductions and/or delays that would result from trust fund depletion.[24] Similarly, current-law projections for Social Security do not reflect benefit payment reductions and/or delays that would result from fund depletion. By accounting convention, the transfers from the General Fund to Medicare Parts B and D are eliminated in the

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

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

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

consolidation of the SOSI at the government-wide level and as such, the General Fund transfers that are used to finance Medicare Parts B and D are not included in table 8. For the FYs 2020 and 2019 SOSI, the amounts eliminated totaled $40.9 trillion and $36.8 trillion, respectively. SOSI programs and amounts are included in the broader fiscal sustainability analysis in the previous section, although on a slightly different basis (as described in Note 24).

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

Table 8: Social Insurance Future Expenditures in Excess of Future Revenues

Dollars in Trillions	2020	2019	Increase / (Decrease) $	Increase / (Decrease) %
Open Group (Net):				
Social Security (OASDI)	$ (19.7)	$ (16.8)	$ 2.9	17.3%
Medicare (Parts A, B, & D)	$ (45.7)	$ (42.2)	$ 3.5	8.3%
Other	$ (0.1)	$ (0.1)	$ -	0.0%
Total Social Insurance Expenditures, Net (Open Group)	**$ (65.5)**	**$ (59.1)**	$ 6.4	10.8%
Total Social Insurance Expenditures, Net (Closed Group)	**$ (87.0)**	**$ (80.4)**	$ 6.6	8.2%
Social Insurance Net Expenditures as a % of Gross Domestic Product (GDP)*				
Open Group				
Social Security (OASDI)	(1.2%)	(1.1%)		
Medicare (Parts A, B, & D)	(3.0%)	(3.0%)		
Total (Open Group)	**(4.2%)**	**(4.1%)**		
Total (Closed Group)	**(5.6%)**	**(5.6%)**		

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

* GDP values used are from the 2020 & 2019 Social Security and Medicare Trustees Reports and represent the present value of GDP over the 75-year projection period. As the GDP used for Social Security and Medicare differ slightly in the Trustees Reports, the two values are averaged to estimate the 'Other' and Total Net Social Insurance Expenditures as percent of GDP. As a result, totals may not equal the sum of components due to rounding.

Table 9 identifies the principal reasons for the changes in projected social insurance amounts during 2020 and 2019.

Table 9: Changes in Social Insurance Projections

Dollars in Trillions	2020	2019
Net Present Value (NPV) - Open Group (Beginning of the Year)	**$ (59.1)**	**$ (54.0)**
Changes In:		
Valuation Period	$ (2.2)	$ (1.9)
Demographic data, assumptions, and methods	$ 3.3	$ 0.8
Economic data, assumptions, and methods[1]	$ (1.8)	$ (1.0)
Law or policy	$ (0.6)	$ -
Methodology and programmatic data[1]	$ 0.2	$ 0.5
Economic and other healthcare assumptions[2]	$ (5.4)	$ (3.0)
Change in projection base[2]	$ 0.1	$ (0.5)
Net Change in Open Group measure	$ (6.4)	$ (5.1)
NPV - Open Group (End of the Year)	**$ (65.5)**	**$ (59.1)**

1 Relates to Social Security Program.

2 Relates to Medicare Program.

The following briefly summarizes the significant changes for the current valuation (as of January 1, 2020) as disclosed in Note 23 —Social Insurance. Note 23 is compiled from disclosures included in the financial reports of those entities administering these programs, including SSA and HHS. See Note 23 for additional information.

- Change in valuation period (affects both Social Security and Medicare): This change replaces a small negative net cash flow for 2019 with a much larger negative net cash flow for 2094. As a result, the PV of the estimated future net cash flows decreased (became more negative) by $2.2 trillion.
- Changes in demographic data, assumptions, and methods (affects both Social Security and Medicare): There were two changes to ultimate demographic assumptions compared to prior valuation: the ultimate total fertility rate was lowered; and the ultimate disability incidence rate was lowered, and the near-term assumed disability incidence rates are somewhat lower in the current valuation. In addition to this ultimate demographic assumption change, the starting demographic value and the way these value transition to the ultimate assumptions were changed. Overall, changes to these assumptions caused the PV of the estimated future net cash flows to increase (become less negative) by $3.3 trillion for Social Security and Medicare, respectively.
- Changes in economic data and assumptions (affects Social Security only): Several changes were made to the ultimate economic assumptions since the last valuation period. Lower assumed total-economy labor productivity growth and a lower assumed ultimate interest rate all contribute to lower projected cash flow while a change in projected ultimate inflation rates and an increase in the projected real wage differential partly offset the changes that have a negative effect. There was one notable change which was incorporating more recent projections of disability prevalence in the labor force participation model. Overall, changes to these assumptions caused the PV of the estimated future net cash flows to decrease (become more negative) by $1.8 trillion.
- Changes in law or policy (affects both Social Security and Medicare): For Social Security, between prior valuation and the current valuation one new law and one new regulation were enacted that are expected to have significant effects on the long-range cost. The ACA, which was enacted in 2010, specified an excise tax on employer-sponsored group health insurance premiums above a given level (commonly referred to as the "Cadillac" tax). On December 20, 2019, the ACA's excise tax provision was repealed. On February 25, 2020, SSA published a final rule in the Federal Register that eliminates the inability to communicate in English as an educational category in the disability determination and medical review process. Most of the provisions enacted as part of Medicare legislation since the prior valuation date had little or no impact on the program. Overall, the changes to these laws, regulations, and policies caused the PV of the estimated future net cash flows to decrease (become more negative) by $0.6 trillion for Social Security and Medicare.
- Changes in methodology and programmatic data (affects Social Security only). Several methodological improvements and updates of program-specific data are included in the current valuation, including, but not limited to: 1) the ultimate disability incidence rate was lowered from 5.2 per thousand exposed in the prior valuation to 5.0 in the current valuation; 2) as in the prior valuation, the current valuation uses a 10-percent sample of newly-entitled worker beneficiaries in a recent year to project average benefit levels of retired-worker and disabled-worker beneficiaries; and 3) The current valuation includes an improvement in the long-range model used for projecting the percentage of the population that has fully-insured status. Overall, changes in methodology and programmatic data caused the PV of the estimated future net cash flows to increase (become less negative) by $0.2 trillion.
- Changes in economic and other healthcare assumptions (affects Medicare only): The economic assumptions used in the Medicare projections are the same as those used for the OASDI (described above) and are prepared by the Office of the Chief Actuary at SSA. In addition to the economic assumptions changes described above, the healthcare assumptions are specific to the Medicare projections. Changes to these assumptions in the current valuation include: higher projected spending growth for Medicare Advantage beneficiaries; faster projected spending growth for physician-administered drugs under Part B; slower overall drug price increases and higher direct and indirect remuneration. The net impact of these changes caused the PV of the estimated future net cash flows to decrease (become more negative) by $5.4 trillion.

- Change in Projection Base (affects Medicare only): Actual income and expenditures in 2019 were different than what was anticipated when the 2019 Medicare Trustees' Report projections were prepared. Part A income and expenditures in 2019 were lower than anticipated based on actual experience. For both Part B and Part D, total income and expenditures were higher than estimated based on actual experience. The net impact of the Part A, B, and D projection base changes is an increase of $401 billion in the PV of the estimated future net cash flow, including combined trust fund assets. Actual experience of the Medicare Trust Funds between January 1, 2019 and January 1, 2020 is incorporated in the current valuation and is more than projected in the prior valuation. Overall, the net impact of the Part A, B, and D projection base change is an increase (become less negative) in the estimated future net cash flows by $0.1 trillion for Medicare.

As reported in Note 23, uncertainty remains about whether the projected cost savings and productivity improvements will be sustained in a manner consistent with the projected cost growth over time. Note 23 includes an alternative projection to illustrate the uncertainty of projected Medicare costs. As indicated earlier, GAO disclaimed opinions on the 2020, 2019, 2018, 2017 and 2016 SOSI because of these significant uncertainties.

Costs as a percent of GDP of both Medicare and Social Security, which are analyzed annually in the Medicare and Social Security Trustees' Reports, are projected to increase substantially through the mid-2030s because: 1) the number of beneficiaries rises rapidly as the baby-boom generation retires and 2) the lower birth rates that have persisted since the baby boom cause slower growth in the labor force and GDP.[25] According to the Medicare Trustees' Report, spending on Medicare is projected to rise from its current level of 3.7 percent of GDP to 6.0 percent in 2044 and to 6.5 percent in 2094.[26] As for Social Security, combined spending is projected to generally increase from its current level of 5.0 percent of GDP to about 5.9 percent by 2038, declining to 5.8 percent by 2053 and then generally increase to 5.9 percent by 2094. The government collects and maintains funds supporting the Social Security and Medicare programs in trust funds. A scenario in which projected funds expended exceed projected funds received, as reported in the SOSI, will cause the balances in those trust funds to deplete over time. Table 10 summarizes additional current status and projected trend information, including years of projected depletion, for the Medicare Hospital Insurance and Social Security Trust Funds.

Table 10: Trust Fund Status

Fund	Projected Depletion	Projected Post-Depletion Trend
Medicare Hospital Insurance (HI)*	2026 (unchanged from FY 2019 Report)	In 2026, trust fund income is projected to cover 90 percent of benefits, decreasing to 78 percent in 2044, then returning to 90 percent by 2094.
Combined Old-Age Survivors and Disability Insurance (OASDI)**	2035 (unchanged from FY 2019 Report)	In 2035, trust fund income is projected to cover 79 percent of scheduled benefits, decreasing to 73 percent by 2094.

* Source: 2020 Medicare Trustees Report ** Source: 2020 OASDI Trustees Report

Projections assume full Social Security and Medicare benefits are paid after fund depletion contrary to current law.
Projections do not include the effects of the pandemic.

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

[25] A Summary of the 2020 Annual Social Security and Medicare Trust Fund Reports, page 4.
[26] Percent of GDP amounts are expressed in gross terms (including amounts financed by premiums and state transfers).

Financial Management

Government Expenditures

Results-Oriented Accountability for Grants

Nearly $800 billion is spent annually on grants and cooperative agreements. Grants managers, both internal and external to the government, report that approximately 40 percent of their time is spent using antiquated processes to monitor compliance with grant requirements rather than using data analytics to monitor grant results. To address these challenges, OMB and the federal grant-making agencies[27] have developed a long-term improvement strategy. The strategy includes standardizing the grants management business process and data, building shared IT infrastructure, establishing a standard risk management framework across grant programs, and ensuring that new grant programs are designed to reflect measurable goals.

To support the standardization of the business process and data and the building of shared IT infrastructure, OMB issued M-18-24, "Strategies to Reduce Grant Recipient Reporting Burden," and published Version 1.0 of the Grants Management Standard Data Elements. In addition, in December 2019, the *Grant Reporting Efficiency and Agreement Transparency Act* was enacted and, in August 2020, OMB published final changes to 2 CFR to require future information collection requests to adhere to the Grants Management Standard Data Elements. Also, concurrent with the release of OMB memo M-19-16, "Centralized Mission Support Capabilities for the Federal Government," OMB predesignated HHS as the Grants Management QSMO and throughout FY 2020 HHS worked with the federal grants community to modernize grants technology, promote interoperability of systems, reduce the number of grants management systems, and promote a risk-based, data-driven approach to managing federal grants. In January 2021, OMB announced that HHS was formally designated as the Grants Management QSMO.

To assess a grant applicant's capabilities, agencies need performance data and the ability to include performance in risk modeling. Consistent with a risk-based approach, agencies are required to audit only seven, not all twelve, of the twelve management requirements (e.g., allowable costs, eligibility, cash management) applicable to grant programs. Specifically, they are required to audit the seven areas deemed to pose the greatest risk or that produced the greatest number of audit findings in the past, as specified in the Compliance Supplement.[28] OMB issued an Addendum to the 2020 Compliance Supplement for the major COVID-19 programs, which seeks to also ensure compliance with subaward reporting under the *Federal Funding Accountability and Transparency Act*.

In addition, in FY 2020, OMB published the performance "playbook," which promotes a common understanding of performance practices to improve grant recipient and program performance and OMB developed a change management strategy focused on listening sessions with federal stakeholders, including the grants community.

Also, in FY 2020, OMB issued COVID-19 related grants guidance, including: OMB Memorandum M-20-11, Administrative Relief for Recipients and Applicants of Federal Financial Assistance Directly Impacted by the Novel Coronavirus (COVID-19); OMB Memorandum M-20-17, Administrative Relief for Recipients and Applicants of Federal Financial Assistance Directly Impacted by the Novel Coronavirus (COVID-19) due to Loss of Operations; OMB Memorandum M-20-20, Repurposing Existing Federal Financial Assistance Programs and Awards to Support the Emergency Response to the Novel Coronavirus (COVID-19); and OMB Memorandum M-20-26, Extension of Administrative Relief for Recipients and Applicants of Federal Financial Assistance Directly Impacted by the Novel Coronavirus (COVID-19) due to Loss of Operations.

Getting Payments Right

Preventing improper payments in the federal government is a management priority. To be successful in preventing improper payments, there must be a focus on systemic enhancements intended to make payments correctly the first time with an emphasis on reducing monetary loss. The federal government, through the CFO community, has identified five strategies to reduce monetary loss and prevent improper payments, which are: 1) Clarify and Streamline Requirements, 2) Identify Monetary Loss Root Causes, 3) Strategic Data Use (using data to prevent improper payments), 4) Mitigation Strategies (using non-data methods to prevent improper payments), and 5) Strengthen State Partnerships.

Starting in FY 2018, agencies with programs reporting more than $100 million in monetary loss began providing a quarterly scorecard on PaymentAccuracy.gov. These scorecards provide information on the actions taken and progress made

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

[28]The Compliance Supplement is an annually updated authoritative source for auditors that identifies compliance requirements that the federal government expects to be considered as part of an audit. Auditors use it to understand the federal program's objectives, procedures, and compliance requirements, as well as audit objectives and suggested audit procedures for determining compliance with the relevant federal program.

on preventing improper payments that would result in monetary loss to the government. Additional details on the programs' FY 2020 improper payment data can be found at https://paymentaccuracy.gov/. Beginning in FY 2020, PaymentAccuracy.gov began providing payment integrity information that had previously been reported in agencies financial statements. Information about program compliance, corrective actions, and accountability mechanisms is now available in a consistent format across all programs.

In FY 2021, OMB will continue to work with agencies, the CFOC, and other stakeholders to improve the identification of the root causes of improper payments that result in monetary loss and to promote data analytic methods that take a comprehensive view of an agency's payment lifecycle.

Efficient Use of Real Property Assets

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

Land

The federal government owns roughly 640 million acres, which represents about 28 percent, of all U.S. land. Four major federal land management agencies administer 610.1 million acres, or 95 percent, of this land. They are the BLM, Fish and Wildlife Service, and National Park Service in DOI; and the Forest Service in USDA. These lands are managed for many purposes, primarily related to conservation, preservation, recreation, and the extraction of natural resources such as timber, minerals, oil, and gas. Much of the land managed by DOI and USDA is public domain land and is generally intended to be retained by the government for use by future generations. This and other land that qualifies as stewardship land is not valued on the government-wide Balance Sheet, but is discussed in Note 25 and in agencies financial statements. In addition, DOD (excluding the Army Corps of Engineers) uses stewardship land for military bases, training ranges, and other military related functions.

Structures

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

Buildings

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

The federal domestic building inventory is diverse and contains 272,000 owned and leased buildings totaling 2.7 billion square feet of space as of 2019. Several current real property initiatives being pursued are discussed below.

Transformation Efforts to Optimize the Use of Federal Real Property

OMB Memorandum M-18-21 requires all federal entities to designate senior real property officers to coordinate all aspects of their real property programs and to serve on the FRPC. The FRPC seeks to provide comprehensive government-wide strategic direction to help optimize the federal real property portfolio to achieve statutory missions while managing costs over the short, mid, and long-term. The FRPC is addressing current challenges such as the lack of a comprehensive strategic approach to asset management, funding challenges, poor data quality, and administratively burdensome and costly legislative disposal requirements. It seeks to revise the national strategy's policy framework, standardize the business processes and data, and diagnose and address root causes of current challenges.

On November 6, 2019, OMB issued Memorandum M-20-03, providing detailed guidance to agencies to implement the Capital Programming Guide in OMB Circular A-11 and to ensure that an agency's real property portfolio helps it efficiently achieve its mission. The Memo provides standards for agencies to use to develop a consistent methodology for allocating resources to real property. This resource allocation will occur as a part of the annual budget formulation process, with agencies systematically identifying their real property needs and assessing their existing real property assets. This process of reviewing real property holdings, acquisitions, and dispositions and linking clearly articulated long-term real property requirements to options that consider the life-cycle of real property is intended to allow agencies and policymakers to have the information necessary to optimize the federal real property portfolio. This should lead to the elimination of excess capacity, cost-effective long-term investments in real property, and annually updated information about the condition of existing property.

The strategic direction reflected in Memorandum M-20-03 builds on the results of the Reduce the Footprint policy, which was issued in 2015 and requires the CFO Act agencies to reduce the size of their federal real property portfolios by improving the use of government-owned buildings and by reducing the amount of leased space and the number of excess and underutilized properties. In March 2020, OMB issued Memorandum M-20-10 *Addendum to the National Strategy for the Efficient Use of Real Property* (Addendum), which goes beyond reducing office and warehouse space to optimizing the government's entire portfolio to achieve mission effectiveness and cost efficiency. The Addendum seeks to ensure that the federal government has the right type of property, in the right amount, at the right location, at the right cost, in the right condition, to support its diverse mission requirements. In addition, Implementation of the *Federal Assets Sale and Transfer Act of 2016* and the *Federal Property Management Reform Act of 2016* may result in a number of property disposals and aid in the efficient use of real property.

Leveraging Data as a Strategic Asset

DATA Act and USAspending.gov

The DATA Act amended the *Federal Funding Accountability and Transparency Act of 2006* by linking federal government contract, loan, and grant spending to federal programs and requiring that all federal spending be displayed on a website in searchable, downloadable, and machine-readable formats.

The USAspending.gov website, which Treasury launched in April 2018 in accordance with the DATA Act, allows users to examine more than $4 trillion in federal spending and identify communities, businesses and non-profit entities that have received federal funding. The data are provided by more than 100 federal agencies and is compiled by Treasury on a quarterly basis. The site allows users to explore the data and download reports that are tailored to their specific interests. The site also includes the Data Lab, which provides use cases, data visualizations, and analyses of federal spending and trends. The data are searchable in a machine-readable format and open application programming interface.

Under OMB Memorandum M-18-16, Management of Reporting Data Integrity Risk, Appendix A to OMB Circular A-123, agencies were required to develop and implement a data quality plan for FYs 2019 through 2021. The guidance also requires agencies to consider in their assurance statements all internal controls (including controls over DATA Act reporting). In November 2019, GAO noted (in GAO-20-75) that agencies had made significant progress in improving DATA Act data quality.

In April 2020, OMB issued Memorandum M-20-21 *Implementation Guidance for Supplemental Funding Provided in Response to the Coronavirus Disease 2019 (COVID-19),* which expanded the use of the DEFC for tracking disasters and emergencies to data provided for USAspending.gov. Additionally, in FY 2021, agencies are required to report program activities at the award level and, beginning in FY 2022 agencies are directed to begin monthly reporting, including outlays at the award level.

Program Inventory

In December 2020, OMB launched the Federal Program Inventory Exploratory Pilot as an interim step in a multi-year effort to create a coherent and comprehensive government-wide program inventory. The goal of the inventory, as articulated in the Government Performance and Results Modernization of 2010, is to provide policymakers and the public "a coherent picture of all Federal programs, and the performance of the Federal Government as well as individual agencies." This coherent picture has become known as the Federal Program Inventory.

Financial Management Framework

Sharing Quality Financial Management Services

The federal financial management infrastructure (which includes grants) exists in a complex environment of legacy systems, customized tools built to unique requirements, lack of harmonized standards, and business processes that no longer leverage modern technology. The sharing of financial technology and services has been successful for smaller agencies as well as a cabinet-level department, with much opportunity remaining to expand the use and effectiveness of these types of arrangements. Specifically, agencies that provide financial management services to other agencies have done so efficiently and effectively for agencies with more limited financial systems requirements. However, when the service providers have attempted to provide similar services and share technology with agencies that have more complex requirements, the result has

often been cost over-runs and the need for systems upgrades or customization. To address this, cross-agency work groups are exploring industry capabilities for optimal use of technology in federal financial management and coordinating the implementation of best practices across the government.

OMB issued M-19-16, "Centralized Mission Support Capabilities for the Federal Government," on April 26, 2019. In June of 2020, Treasury was officially designated as the QSMO for the financial management line of business and, along with OMB and GSA, will be working with agencies as they pursue the goals as outlined in M-19-16.

Financial Management Workforce

Federal agencies and OMB are committed to redefining the role of the federal government by prioritizing activities that advance the federal government financial workforce. The future workforce must enable senior leaders and front-line managers to align staff skills with evolving mission needs. This will require more nimble and agile management of the workforce, including reskilling and redeploying existing workers to keep pace with the current pace of change.

Under the CFOC, a cross-agency "Shape the Workforce" work group has been working to establish a systematic process for identifying and addressing gaps between the financial management workforce of today and the workforce needs of tomorrow. Through this process, CFO leadership will be able to identify the personnel required to meet organizational goals, conduct analyses to determine and close competency and skills gaps, develop strategies to address human capital needs, and assess the effectiveness of CFO office structures. In addition, the cross-agency work group is exploring options for consolidating recruitment efforts and streamlining the hiring process, leveraging technology to improve the financial management workforce, and developing new tools for retention and staff development.

Enterprise Risk Management

ERM is a tool used by agencies to systematically identify, assess, mitigate, manage, and prepare for risks that could interfere with an agency's ability to achieve its mission and goals. ERM promotes risk-informed decision making that allows resources to be prioritized and allocated based on risk and encourages agencies to target their limited resources to activities likely to produce the greatest improvement in program performance.

Using ERM techniques, federal agencies establish internal controls to address management challenges that cut across multiple agencies' functions and reduce associated risk to an acceptable level that aligns with the agency's risk appetite and tolerance. In this way, ERM integrates risk management and internal control processes. The 2016 update to OMB Circular A-123, Management's Responsibility for Enterprise Risk Management and Internal Control, stresses the importance of applying ERM to all financial management activities, including charge cards and payment integrity. In 2019, the updated OMB Circular A-11, Part 6, integrated ERM into agency strategic planning and performance measurement processes. In 2020, Circular A-11 (sections 31.1 and 31.8) was updated to integrate ERM into the budget formulation process. In response to COVID-19, OMB updated M-20-21, *Risk-Based Financial Audits and Reporting Activities in Response to COVID-19,* to encourage agencies to use risk-based frameworks to achieve financial, audit, and payment integrity objectives. Also in 2020, the CFOC established an ERM Executive Steering Committee to identify and share ERM best practices, develop a federal ERM maturity model (a self-assessment tool used to assist in ERM implementation), promote ERM integration with mission and mission support functions, and facilitate constructive coordination with oversight entities.

Agency Financial Report Results

Audits

Since the passage of the CFO Act, the federal financial community has made significant progress in financial accounting and reporting. As shown in Table 11, for FY 2020, 22 of the 24 CFO Act agencies obtained an unmodified opinion from the independent auditors on their financial statements.[29] In addition, 48 auditor-identified material weaknesses were reported at the end of FY 2020 compared to 41 for FY 2019. Twenty-six of these are associated with DOD. The other 22 material weaknesses are associated with non-DOD agencies, which represents an increase from 16 reported in 2019, primarily because of the increase in new material weaknesses at SBA associated with implementation of programs implemented under the CARES Act and related legislation. Although virtually all federal agencies have adopted and maintained disciplined financial reporting operations, implemented effective internal controls over financial reporting, and integrated transaction processing with accounting records, weaknesses in financial management practices still continue to prevent the government as a whole from achieving an audit opinion.

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

Table 11: Agency Audit Results: FY 2020						
	Audit	Auditor-Reported Material Weaknesses				
Agency	Opinion	Beginning	New	Resolved	Consolidated	Ending
Department of Agriculture (USDA)	Unmodified	2	0	0	0	2
Department of Commerce (DOC)	Unmodified	0	0	0	0	0
Department of Defense (DOD)	Disclaimer	25	4	2	1	26
Department of Education (Education)	Unmodified	1	1	1	0	1
Department of Energy (DOE)	Unmodified	0	0	0	0	0
Department of Health and Human Services (HHS)*	Unmodified	0	0	0	0	0
Department of Homeland Security (DHS)	Unmodified	2	0	0	0	2
Department of Housing & Urban Development (HUD)	Unmodified	1	0	0	0	1
Department of the Interior (DOI)	Unmodified	1	1	1	0	1
Department of Justice (DOJ)	Unmodified	1	0	1	0	0
Department of Labor (DOL)	Unmodified	0	0	0	0	0
Department of State (State)	Unmodified	0	0	0	0	0
Department of Transportation (DOT)	Unmodified	0	0	0	0	0
Department of the Treasury (Treasury)	Unmodified	0	0	0	0	0
Department of Veterans Affairs (VA)	Unmodified	5	0	0	0	5
Agency for International Development (USAID)	Unmodified	0	0	0	0	0
Environmental Protection Agency (EPA)	Unmodified	1	0	0	0	1
General Services Administration (GSA)	Unmodified	0	0	0	0	0
National Aeronautics & Space Administration (NASA)	Unmodified	0	0	0	0	0
National Science Foundation (NSF)	Unmodified	0	0	0	0	0
Nuclear Regulatory Commission (NRC)	Unmodified	0	1	0	0	1
Office of Personnel Management (OPM)	Unmodified	1	0	0	0	1
Small Business Administration (SBA)	Disclaimer	1	7	1	0	7
Social Security Administration (SSA)	Unmodified	0	0	0	0	0
Totals		**41**	**14**	**6**	**1**	**48**

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

Agency Financial Management Systems

Federal agencies improved, but continue to face challenges, in implementing financial management systems that meet federal requirements. The number of CFO Act agencies reporting lack of substantial compliance with one or more of the three Section 803(a) requirements of the FFMIA remained at seven in FY 2020, and the number of auditors reporting lack of substantial compliance with one or more of the three Section 803(a) FFMIA requirements increased to nine in FY 2020.

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

In 2020, Treasury was designated as the Financial Management systems QSMO and it is pursuing financial management improvement strategies that have government-wide implications. These strategies include standing up a financial management marketplace, developing system standards, and standardized processes, system requirements, and system interfaces. These efforts provide a path to the decommissioning of legacy systems and migration to updated systems, leveraging modernized technologies. Also, agencies are coordinating with Treasury QSMO to improve their financial management and financial reporting systems as described in their financial reports, budget requests, and performance plans. DOD continues to address its material weaknesses in financial reporting, and is bringing its financial systems into compliance with federal financial management systems requirements, including the FFMIA; these plans can be found in the agency financial statements. In addition, DOD's audit remediation efforts include issues related to real property, inventory and OM&S, government property in the possession of contractors, information technology access controls, reconciling DOD's fund balance with Treasury, internal controls over financial reporting, the Joint Strike Fighter program, and component audit support.

Agency Internal Controls

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

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

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

As noted above, the total number of reported material weaknesses for the CFO Act agencies as of the issuance of this *Financial Report* was 48 for FY 2020 and 41 for FY 2019. Effective internal controls are a challenge at the agency level and at the government-wide level, with GAO reporting that at the government-wide level, material weaknesses resulted in ineffective internal control over financial reporting. While progress is being made at many agencies and across the government in identifying and resolving internal control deficiencies, additional work is needed.

Legal Compliance

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

Conclusion

The federal government has seen significant progress in financial management since the passage of the CFO Act nearly 30 years ago, but significant challenges remain to realizing the intended financial management reforms of the act. The issues that the federal government faces today require financial managers to improve both the efficiency and effectiveness of financial management activities, which includes moving toward integrated government operations with standardized business processes, systems, and data. Together with Treasury and OMB, agencies are building on tools and capabilities to improve financial accountability and transparency.

Additional Information

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

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