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United States Government Accountability Office

Fiscal Stewardship:

A Critical Challenge Facing Our Nation

GAO-07-362SP

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Preface

The U.S. government is the largest, most diverse, most complex, and arguably the most important entity on earth today. The United States is also a great nation. It has much to be proud of and much to be thankful for. However, our nation is not well positioned to meet the challenges and capitalize on the opportunities of the 21st Century. We are also failing to properly discharge one of our biggest stewardship responsibilities to our children, grandchildren, and generations of unborn Americans: fiscal responsibility. The purpose of this publication is to assist both the Congress and American citizens in understanding and evaluating the federal government's current financial condition and long-term fiscal outlook.

The federal government's financial condition and fiscal outlook are worse than many may understand. Despite an increase in revenues in fiscal year 2006 of about $255 billion, the federal government reported that its costs exceeded its revenues by $450 billion (i.e., net operating cost) and that its cash outlays exceeded its cash receipts by $248 billion (i.e., unified budget deficit). Further, as of September 30, 2006, the U.S. government reported that it owed (i.e., liabilities) more than it owned (i.e., assets) by almost $9 trillion. In addition, the present value[1] of the federal government's major reported long-term "fiscal exposures"—liabilities (e.g., debt), contingencies (e.g., insurance), and social insurance and other commitments and promises (e.g., Social Security, Medicare)—rose from $20 trillion to about $50 trillion in the last 6 years.

The federal government faces large and growing structural deficits in the future due primarily to known demographic trends and rising health care costs. These structural deficits—which are virtually certain given the design of our current programs and policies—will mean escalating and ultimately unsustainable federal deficits and debt levels. Based on various measures—and using reasonable assumptions—the federal government's current fiscal policy is unsustainable. Continuing on this imprudent and unsustainable path will gradually erode, if not suddenly damage, our economy, our standard of living, and ultimately our domestic tranquility and national security.

This publication brings together selected financial statement information from the fiscal year 2006 *Financial Report of the United States Government (Financial Report)* and certain fiscal year 2006 budget information reported by the Department of the Treasury.[2] This budget information will also be included in the President's Budget proposal for fiscal year 2008, which will be released in February 2007. The Department of the Treasury, in coordination with the Office of Management and Budget, annually prepares the *Financial Report* and submits it to the President and the Congress. The *Financial Report* is the federal government's annual overall report of accountability to the American public and provides a comprehensive overview of the financial condition of the federal government, the cost of the federal government's operations, the revenue sources used to finance them, and the implications of various long-term federal obligations and commitments.[3] The President's Budget includes information on revenues and spending for previous fiscal years and presents the President's proposals for revenue and spending for the next fiscal year. It also contains additional analytical material.

GAO is responsible for auditing the financial statements included in the *Financial Report*, but we have been unable to express an opinion on them for the 10th year in a row because the federal government could not demonstrate the reliability of significant portions of the financial statements, especially in connection with major financial management challenges at the Department of Defense. Accordingly, amounts reported in this publication taken from the *Financial Report* may not be reliable. GAO also reported that the federal government did not maintain effective internal control over financial reporting (including safeguarding assets) and compliance with significant laws and regulations as of September 30, 2006. Further, GAO's audit report also included an emphasis paragraph for the 3rd consecutive year noting that the nation's current fiscal path is unsustainable and that tough choices by the President and the Congress are necessary to address the nation's large and growing long-term fiscal imbalance.

This publication was prepared under the direction of Gary T. Engel, Director, Financial Management and Assurance, who may be reached at (202) 512-3406 or engelg@gao.gov and Susan J. Irving, Director, Federal Budget Analysis, Strategic Issues, who may be reached at (202) 512-9142 or irvings@gao.gov if there are any questions. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this publication. Copies of this publication are available upon request. In addition, this document will be available at no charge on the GAO Web site at http://www.gao.gov.

David M. Walker
Comptroller General of the United States

Contents

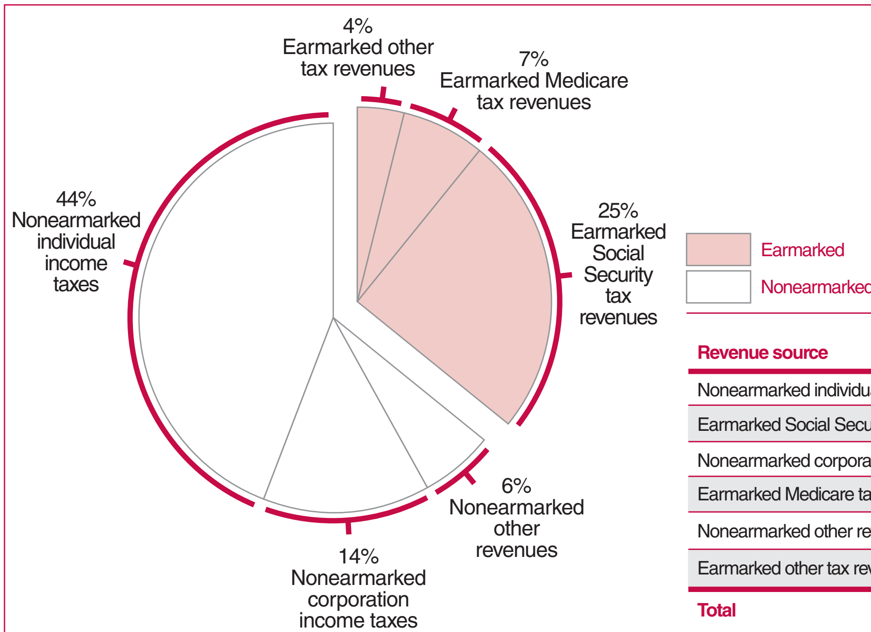
The Federal Government's Current Financial Condition—Fiscal Year 2006

The federal government's current financial condition as shown in the consolidated financial statements considers the results of the current fiscal year's activities including sources of federal revenue and where that money went, as well as the status of what the federal government owns and owes at the end of the fiscal year.

Where the Money Came From (i.e., Federal Revenue)

For the fiscal year ended September 30, 2006, the federal government reported total revenue[4]—principally tax receipts—of about $2,441 billion. Figure 1 provides a breakout of the various sources of this revenue. Certain revenues (e.g., Social Security and Medicare payroll taxes and unemployment taxes) are classified in the *Financial Report* as earmarked revenue, which are required to be used for designated activities, benefits, or purposes.[5]

Figure 1: Where the Money Came From in Fiscal Year 2006



Revenue source	Dollars in billions
Nonearmarked individual income taxes	$1,046
Earmarked Social Security tax revenues	$620
Nonearmarked corporation income taxes	$350
Earmarked Medicare tax revenues	$180
Nonearmarked other revenues	$137
Earmarked other tax revenues	$108
Total	**$2,441**

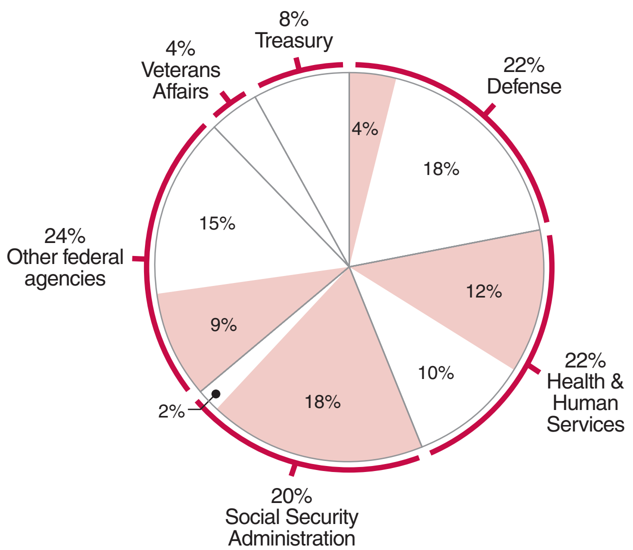
Source: The Department of the Treasury.

Note: Data are from the fiscal year 2006 *Financial Report*.

Where the Money Went (i.e., Federal Cost)

For the fiscal year ended September 30, 2006, the federal government reported total net cost of about $2,901 billion.[6] Figure 2 provides a breakout of the net cost.

Figure 2: Where the Money Went in Fiscal Year 2006



Dollars in billions

Federal agency	Earmarked	Nonearmarked	Total
Defense	$121	$513	$634
Health & Human Services	$337	$290[a]	$627
Social Security Administration	$543	$50	$593
Treasury - Interest on Treasury securities held by the public	-	$222	$222
Veterans Affairs	$1	$113	$114
Other federal agencies	$264	$447	$711
Total	**$1,266**	**$1,635**	**$2,901**

Source: The Department of the Treasury.

[a] Medicaid costs represent $180 billion or 62 percent of Health and Human Services's $290 billion of nonearmarked funds net costs.

Note: Data are from the fiscal year 2006 *Financial Report*.

The Federal Government's Financial and Budget Reporting

The federal government produces two types of measures—budget and financial—which further break down into three different numbers that can be seen as indicators of our current financial condition: the unified budget deficit, the on-budget deficit, and the net operating cost. Table 1 shows the reported amounts of these for the fiscal year ended September 30, 2006.

Table 1: Fiscal Year 2006 Budget Deficits and Net Operating Cost

	Dollars in billions
Unified budget deficit	($248)
On-budget deficit	($434)
Net operating cost[a]	($450)

Source: The Department of the Treasury.

[a] For fiscal year 2006, there was a significant decrease in certain actuarial costs primary due to changes in interest rates and other assumptions.

Note: Data are from the *Monthly Treasury Statement* as of the fiscal year end 2006 and the fiscal year 2006 *Financial Report*.

The most commonly reported measure is the unified budget deficit. This is a largely cash-based number that represents the difference between revenues and outlays—recorded in the period that cash is received or paid—for the government as a whole. It is an important measure since it is indicative of the government's draw on today's credit markets—and its claim on today's economy. The unified budget is a comprehensive measure of all federal activities, including those that are on-budget and off-budget. By law the Postal Service and Social Security trust funds are designated as off-budget. All other budget accounts are on-budget.

Net operating cost is the amount by which costs exceed revenue. Costs are recorded on an accrual basis—namely, in the period when goods are used or services are performed as opposed to when the resulting cash payments are made. Most revenues, on the other hand, are recorded on a modified cash basis—that is, they are essentially recorded when collected. For fiscal year 2006, the net operating cost of the federal government was comprised of earmarked funds net operating revenue[7] of approximately $172 billion (e.g., Social Security) and nonearmarked funds net operating cost of about $622 billion.[8]

Table 2 shows the relationship between these numbers.

Table 2: Relationship between Fiscal Year 2006 Budget Deficits and Net Operating Cost

	Dollars in billions
On-budget deficit	$ (434)
Add: Off-budget surplus[a]	186
Unified budget deficit	(248)
Add: Operating costs not in unified budget deficit (accrual basis)[b]	(318)
Less: Budget outlays not in net operating cost (cash basis)[c]	116
Net operating cost	$ (450)

Source: The Department of the Treasury.

[a] Comprised of $185 billion in Social Security surplus and $1 billion for Postal Service surplus.
[b] For example, increase in accrued Federal Employee and Veteran Benefits.
[c] For example, purchase of capital assets (e.g., property, plant, and equipment).

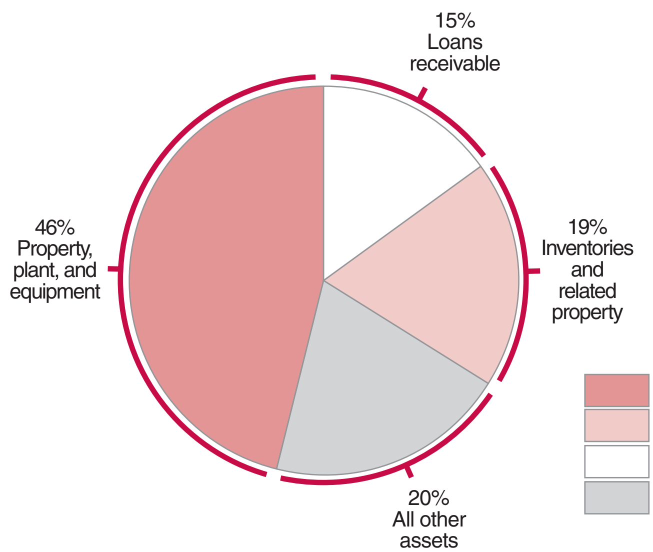
Note: Data are from the *Monthly Treasury Statement* as of the fiscal year end 2006 and the fiscal year 2006 *Financial Report*.

What We Own and What We Owe (i.e., the Balance Sheet)

What We Own (i.e., Federal Assets)

Assets represent items of economic value owned by the federal government. Figure 3 provides a breakout of the assets that are reported with dollar values in the Balance Sheet in the *Financial Report*. As of September 30, 2006, the federal government reported total federal assets of about $1,497 billion. In addition to these assets, certain federal assets are instead reported in physical quantities: stewardship land (e.g., national parks and forests) and heritage assets (e.g., national memorials, historic structures, and museum collections).[9]

Figure 3: Components of Total Federal Assets Reported as of September 30, 2006



Asset	Dollars in billions
Property, plant, and equipment	$689
Inventories and related property	$281
Loans receivable	$221
All other assets	$306
Total	**$1,497**

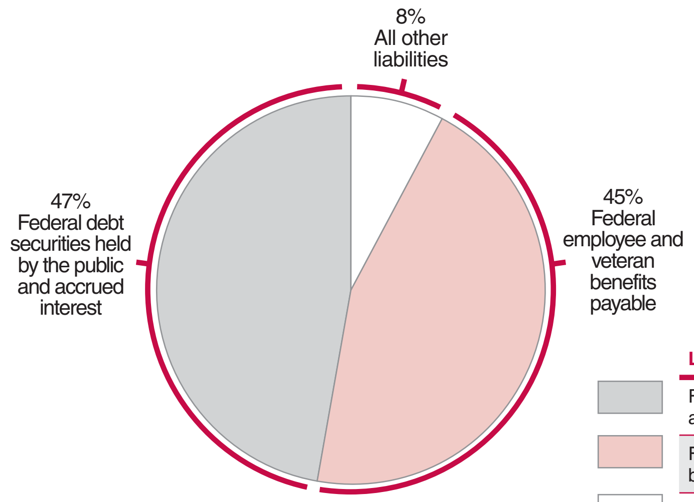
Source: The Department of the Treasury.

Note: Data are from the fiscal year 2006 *Financial Report*.

What We Owe (i.e., Federal Liabilities)

As of September 30, 2006, the federal government reported total federal liabilities of about $10,413 billion. These liabilities represent a financial obligation, debt, claim or probable potential loss that is reported in the Balance Sheet in the *Financial Report*. Figure 4 shows the components of these liabilities.

Figure 4: Components of Total Federal Liabilities Reported as of September 30, 2006



Liability	Dollars in billions
Federal debt securities held by the public and accrued interest[a]	$4,868
Federal employee and veteran benefits payable	$4,679
All other liabilities	$866
Total	**$10,413**

Source: The Department of the Treasury.

[a] This consists of $4,866 billion of gross federal debt minus $40 billion of net unamortized discounts plus $42 billion of accrued interest payable.

Note: Data are from the fiscal year 2006 *Financial Report*.

Gross Federal Debt

As shown in Figure 5, gross federal debt, which totaled about $8,530 billion as of September 30, 2006, consists of debt held by the public—$4,866 billion—and debt held by government accounts (referred to as intragovernmental debt holdings)—$3,664 billion.[10] The federal government borrows excess cash receipts from earmarked (e.g., Social Security) and certain other activities to finance general government operations and, in exchange, issues special U.S. Treasury securities. Of the $3,664 billion of intragovernmental debt holdings, $1,995 billion or 54 percent is held by the Social Security Trust Funds and $335 billion or 9 percent is held by the Medicare Trust Funds. Intragovernmental debt holdings are not reported in the federal government's Balance Sheet because under accounting principles they are treated as loans from one part of the federal government to another part of the federal government.[11]

Figure 5: Components of Gross Federal Debt as of September 30, 2006

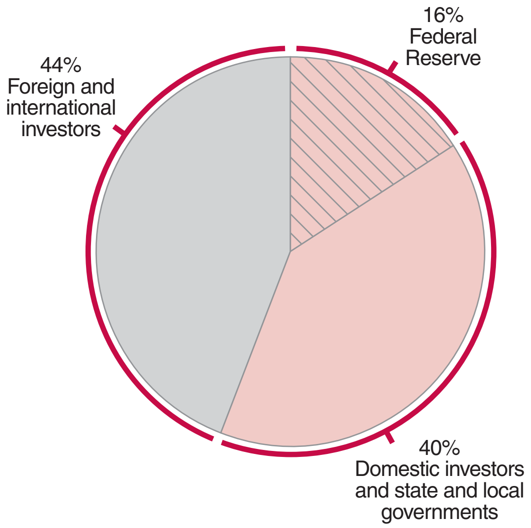
Debt held by the public — $4,866 billion	Intragovernmental debt holdings — $3,664 billion
Federal debt held by individual or institutional investors in the United States or abroad, state and local governments, and the Federal Reserve banking system.	Federal debt held by the federal government itself. Most of this debt is held by trust funds, such as Social Security and Medicare.

Source: The Department of the Treasury.

Note: Data are from the fiscal year 2006 *Financial Report*.

As shown in Figure 6, debt held by the public is composed of debt held by the Federal Reserve banking system (Federal Reserve), by state and local governments, by domestic investors in the United States and by foreign and international investors abroad. Over the last several years, there has been an upward trend in the amount of Treasury securities held by foreign and international investors. The United States benefits from purchases of Treasury securities by foreign investors because such investors fill part of the U.S. government's borrowing needs. However, the interest paid on this debt is sent abroad, which adds to the incomes of residents of other countries rather than to the incomes of U.S. residents. In addition, this increasing reliance on foreign investors to finance the deficits of the U.S. government presents potential risk to the U.S. economy, especially since the U.S. gross national saving rate is low by U.S. historical standards.

Figure 6: Components of Debt Held by the Public as of September 30, 2006



Debt component	Dollars in billions
Foreign and international investors[a]	$2,140
Domestic investors and state and local governments	$1,961
Federal Reserve	$765
Total	**$4,866**

Source: The Department of the Treasury.

[a] Excluding the $765 billion of debt held by the Federal Reserve, foreign and international investors hold 52 percent of the remaining $4,101 billion of debt held by the public.

Note: Data are from the fiscal year 2006 *Financial Report* and the December 2006 *Treasury Bulletin*.

Historically, the Congress and the President have enacted laws to establish a limit on the amount of public debt that can be outstanding—referred to as the debt ceiling.[12] The debt ceiling does not determine federal borrowing needs: these needs result from all of the revenue received and spending decisions the government makes as well as the performance of the economy. Whenever the federal government approaches the debt ceiling, the Congress and the President must eventually raise the ceiling to pay the government's bills as they come due. As of September 30, 2006, the debt ceiling was $8,965 billion and the debt subject to the ceiling was $8,420 billion.[13]

The Long-Term Fiscal Outlook

In addition to considering the federal government's current financial condition, it is critical to look at other measures of the long-term fiscal outlook of the federal government. An evaluation of the nation's long-term fiscal outlook should include not only liabilities included in the *Financial Report* but also the implicit promises embedded in current policy and the timing of these longer-term obligations and commitments in relation to the resources available under various assumptions.

Over the next few decades, the nation's fiscal outlook will be shaped largely by known demographic trends and rising health care costs. As the baby-boom generation retires, federal spending on current retirement and health care programs—Social Security, Medicare, and Medicaid—will grow dramatically. A range of other federal fiscal commitments, some explicit and some representing implicit public expectations, also bind the nation's fiscal future. Absent policy changes, a growing imbalance between expected federal spending and tax revenues will mean escalating and ultimately unsustainable federal deficits and debt levels.

There are various ways to consider and assess the long-term fiscal outlook. In this regard, information included in the *Financial Report*, and other information and analyses, can be used to more fully understand the nation's long-term fiscal outlook, including

- the Statement of Social Insurance,
- major reported long-term fiscal exposures, and
- long-term fiscal simulations.

Statement of Social Insurance

The Statement of Social Insurance in the *Financial Report* displays the present value of projected revenues and expenditures for scheduled benefits of certain benefit programs that are referred to as social insurance (e.g., Social Security, Medicare). For these programs, projected expenditures for scheduled benefits exceed earmarked revenues by approximately $39 trillion in present value terms over the next 75 years. Stated differently, one would need approximately $39 trillion invested today to deliver on the currently promised benefits for the next 75 years. Table 3 shows a simplified version of the Statement of Social Insurance by its primary components.

Table 3: Simplified Statement of Social Insurance as of January 1, 2006

Dollars in trillions

	Social Security	Medicare Hospital Insurance (Part A)	Medicare Supplementary Medical Insurance – Part B	Medicare Supplementary Medical Insurance – Part D	Total
Present value of future revenue (earmarked contributions, taxes, and premiums)	$32	$11	$5	$2	$50
Present value of expenditures for scheduled future benefits[a]	(39)	(22)	(18)	(10)	(89)
Present value of future expenditures in excess of future revenue[b]	($7)	($11)	($13)	($8)	($39)

Source: The Department of the Treasury.

[a] These amounts include administrative expenses for the programs.

[b] Under current law, Social Security and Federal Hospital Insurance (Medicare Part A) payments are limited to amounts available to the respective trust funds.

Note: Data are from the fiscal year 2006 *Financial Report*.

Major Reported Long-Term Fiscal Exposures

GAO developed the concept of "fiscal exposures" to provide a framework for considering the wide range of responsibilities, programs, and activities that explicitly or implicitly expose the federal government to future spending.

The concept of fiscal exposures is meant to provide a broader perspective on long-term costs. Major reported long-term fiscal exposures in fiscal year 2006 with a present value totaling about $50 trillion consisted of $10 trillion of liabilities reported on the Balance Sheet, $1 trillion of other commitments and contingencies, and the $39 trillion of social insurance responsibilities, the last two of which are reported elsewhere in the *Financial Report*. This $50 trillion compares to $20 trillion in fiscal year 2000.

These large numbers are difficult to comprehend. Table 4 seeks to translate them into several figures and ratios that are more understandable.

Table 4: Understanding the Size of Major Reported Fiscal Exposures

	2000	2006	Percentage increase
Major fiscal exposures	$20.4 trillion	$50.5 trillion	147%
Total household net worth	$42.0 trillion	$53.3 trillion	27%
Ratio of fiscal exposures to net worth	49 percent	95 percent	94%
Burden			
Per person	$70,000	$170,000	132%
Per full-time worker	$165,000	$400,000	143%
Per household	$190,000	$440,000	134%
Income			
Median household income	$41,990	$46,326	10%
Disposable personal income per capita	$25,127	$31,519	25%
Ratio of household burden to median income	4.5	9.5	112%

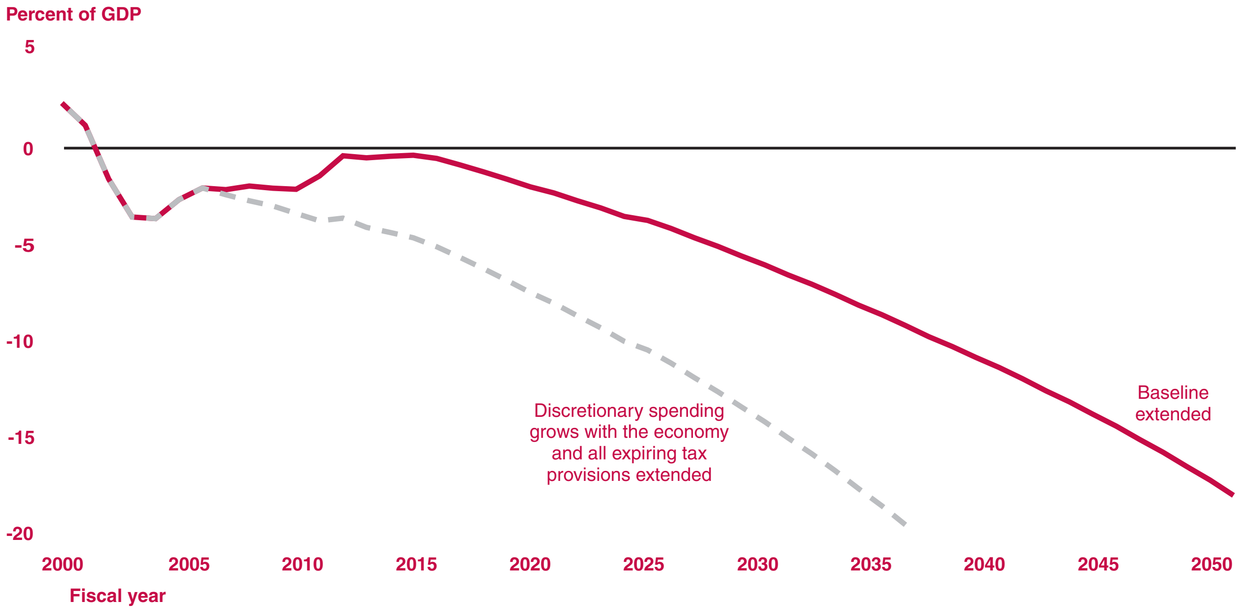
Sources: GAO analysis of data from the Department of the Treasury, Federal Reserve Board, U.S. Census Bureau, and Bureau of Economic Analysis.

Note: Percentage increases reflect actual data and may differ from calculation of rounded numbers presented in table.

Long-Term Fiscal Simulations

Another way to assess the U.S. government's long-term fiscal outlook and the sustainability of federal programs is to run simulations of future revenues and costs for all federal programs, based on a continuation of current or proposed policy. The simulations GAO has published since 1992 are designed to do that. As shown in Figure 7, GAO's long-term simulations—which are neither forecasts nor predictions—continue to show ever-increasing long-term deficits resulting in a federal debt level that ultimately spirals out of control. The timing of deficits and the resulting debt buildup varies depending on the assumptions used, but under either optimistic ("Baseline extended") or more realistic assumptions, the federal government's current fiscal policy is unsustainable.

Figure 7: Unified Surpluses and Deficits as a Share of Gross Domestic Product (GDP) under Alternative Fiscal Policy Simulations



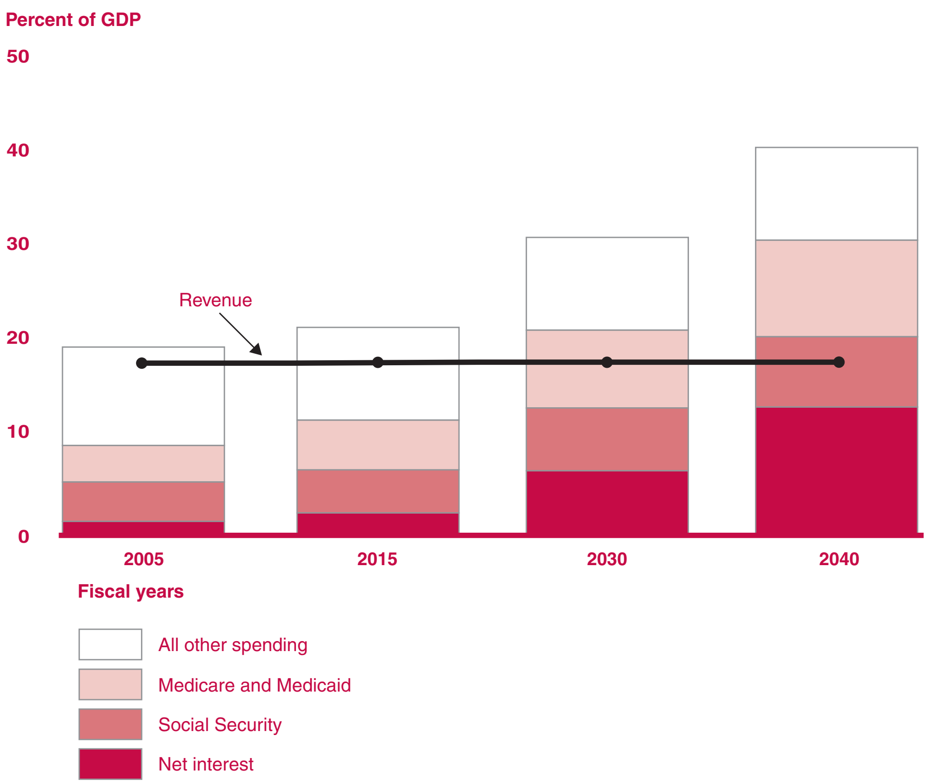
Source: GAO's August 2006 analysis.

Note: Assumes currently scheduled Social Security benefits are paid in full throughout the simulation period.

Over the long term, the nation's growing fiscal imbalance stems primarily from the aging of the population and rising health care costs. Absent significant changes on the spending or revenue sides of the budget or both, these long-term deficits will encumber a growing share of federal resources and test the capacity of current and future generations to afford both today's and tomorrow's commitments. Continuing on this unsustainable path will gradually erode, if not suddenly damage, our economy, our standard of living, and ultimately our domestic tranquility and national security.

If, for example, as shown in Figure 8, it is assumed that recent tax reductions are made permanent and discretionary spending keeps pace with the growth of our economy, our long-term simulations suggest that by 2040 federal revenues may be adequate to pay little more than interest on debt held by the public and some Social Security benefits. Neither slowing the growth in discretionary spending nor allowing the tax provisions, including the tax cuts enacted in 2001 and 2003, to expire—nor both together—would eliminate the imbalance.

Figure 8: Composition of Spending as a Share of GDP Assuming Discretionary Spending Grows with GDP after 2006 and All Expiring Tax Provisions Are Extended



Source: GAO's August 2006 analysis.

At some point, action will need to be taken to change the nation's fiscal course. The sooner appropriate actions are taken, the sooner the miracle of compounding will begin to work for the federal budget rather than against it. Conversely, the longer that action to deal with the nation's long-term fiscal outlook is delayed, the greater the risk that the eventual changes will be disruptive and destabilizing. Acting sooner rather than later will give us more time to phase in gradual changes, while also providing more time for those likely to be most affected to make compensatory changes.

The "fiscal gap" is a quantitative measure of long-term fiscal imbalance. Under GAO's more realistic simulation, even if the federal government continued to borrow money from the public at the current share of the economy (i.e., GDP), closing the fiscal gap would require spending cuts or tax increases equal to 8 percent of the entire economy each year over the next 75 years, or a total of about $61 trillion in present value terms. To put this in perspective, closing the gap would require an immediate and permanent increase in federal tax revenues of more than 40 percent or an equivalent reduction in federal program spending (i.e., in all spending except for interest on the debt held by the public, which cannot be directly controlled).

A Way Forward

Although the long-term fiscal outlook is driven by rising health care costs and known demographics, we cannot ignore other government programs and activities. There is a need to engage in a fundamental review, reprioritization, and reengineering of the base of government. Aligning the federal government to meet the challenges and capitalize on the opportunities of the 21st century will require a fundamental review of what the federal government does, how it does it, and how it is financed. Many of the federal government's current policies, programs, functions, and activities are based on conditions that existed decades ago, are not results-based, and are not well aligned with 21st century realities. We need to address the growing costs of the major entitlement programs and also review and reexamine all other major programs, policies, and activities on both the spending and the revenue side of the budget. Programs that run through the tax code—sometimes referred to as tax expenditures[14]—must be reexamined along with those that run through the spending side. As we move forward, the federal government needs to start making tough choices in setting priorities and linking resources and activities to results. Meeting our nation's large, growing, and structural fiscal imbalance will require a multipronged approach:

- increasing transparency in financial and budget reporting and in budget and legislative processes to highlight our long-term fiscal challenges;
- reinstituting and strengthening budget controls for both spending and tax policies to deal with both near-term and longer-term deficits;
- strengthening oversight of programs and activities including creating approaches to better facilitate the discussion of integrated solutions to crosscutting issues; and
- reengineering and reprioritizing the federal government's existing programs, policies, and activities to address 21st century challenges and capitalize on related opportunities.

In order to effectively address our long-term fiscal imbalance, fundamental reform of existing entitlement programs is essential. However, entitlement reform alone will not get the job done. We also need to reprioritize and constrain other federal government spending and generate more revenues—hopefully through a reformed tax system.

In November 2006, the Comptroller General of the United States provided the congressional leadership[15] with recommendations, based on the work of GAO, for consideration for the agenda of the 110th Congress. These recommendations focused on three areas: (1) targets for near-term oversight, (2) policies and programs that are in need of fundamental reform and reengineering, and (3) governance issues. In addition, GAO's *21st Century Challenges: Reexamining the Base of the Federal Government* contains a suggested list of specific federal activities for reexamination, illustrative reexamination questions, and perspectives on various strategies, processes, and approaches, for congressional consideration stemming from our audit and evaluation work that can be used in reexamining the federal base.[16] Answers to these questions may draw on the work of GAO and others; however, only elected officials can and should decide which issues to address as well as how and when to address them. Addressing these problems will require tough choices, and our fiscal clock is ticking. As a result, the time to start is now, to help save our future.

Endnotes

[1] Present value is the discounted value of a payment or stream of payments to be received or paid in the future, taking into consideration a specific interest or discount rate.

[2] The consolidated financial statements are prepared based on generally accepted accounting principles which differ from budgetary reporting. Generally accepted accounting principles are based on accrual accounting whereas the budget is primarily cash-based. These differences are discussed in the *Financial Report* and in GAO, *Understanding Similarities and Differences between Accrual and Cash Deficits*, GAO-07-117SP (Washington, D.C.: December 2006). The *Financial Report* can be found at www.fms.treas.gov/fr/index.html.

[3] For a guide to understanding the *Financial Report*, see GAO, *Understanding the Primary Components of the Annual Financial Report of the United States Government*, GAO-05-958SP (Washington, D.C.: September 2005).

[4] Revenues are reported in the *Statement of Operations and Changes in Net Position* in the *Financial Report*.

[5] As used in the *Financial Report*, earmarked funds are financed by specifically identified revenues and other financing sources (earmarked revenue) that remain available over time; are required by statute to be used for designated activities, benefits, or purposes (e.g., Social Security, Medicare, Unemployment, and Transportation trust funds); and must be accounted for separately from the federal government's nonearmarked funds (i.e., general revenues). Earmarked funds revenue in the *Financial Report* includes $185 billion of intragovernmental interest, that is eliminated for consolidated reporting purposes. Earmarked funds are different from the budget terms "earmarked collections" and "earmarking". Earmarked collections include trust fund receipts, special fund receipts, intragovernmental receipts, and offsetting collections credited to appropriation accounts. Earmarking refers to designating any portion of a lump-sum amount for particular purposes by means of legislative language or language included in congressional committee reports.

[6] Net Cost is reported in the *Statement of Net Cost* in the *Financial Report*. Nonearmarked funds net cost in the *Financial Report* includes $185 billion of intragovernmental interest, that is eliminated for consolidated reporting purposes.

[7] While the net operating cost and the unified budget deficit are based on the same underlying activities, in addition to the different bases of accounting, "Earmarked Funds Net Operating Revenue" includes programs (e.g., Medicare) in addition to those included in the "Off-budget surplus" (i.e., Social Security and Postal Service). Although earmarked funds in the aggregate run surpluses, some funds (e.g., Military Retirement Fund) run deficits.

[8] The Earmarked Funds Net Operating Revenue is the excess of revenues and of transfers from nonearmarked funds over net costs. The nonearmarked funds net operating cost is the excess of net costs and of transfers to earmarked funds over revenues.

[9] Stewardship land includes federally-owned land that is set aside for the use and enjoyment of current and future generations and land on which military bases are located. Heritage assets are federal government-owned assets that have one or more of the following characteristics—historical or natural significance, cultural, educational, or artistic importance, and significant architectural characteristics. Such assets are described in the *Financial Report* in Notes 24 and 25 to the Financial Statements.

[10] Approximately $3,555 billion or 97 percent of intragovernmental debt holdings is held by earmarked funds.

[11] For in-depth discussions on debt held by the public and intragovernmental debt holdings, see GAO, *Financial Audit: Bureau of the Public Debt's Fiscal Years 2006 and 2005 Schedules of Federal Debt*, GAO-07-127 (Washington, D.C.: Nov. 7, 2006) and GAO, *Federal Debt: Answers to Frequently Asked Questions, An Update*, GAO-04-485SP (Washington, D.C.: August 2004).

[12] The public debt limit is established by 31 U.S.C. § 3101 (2000) as amended by Pub. L. No. 107-199, § 1, 116 Stat. 734 (2002), Pub. L. No. 108-24, 117 Stat. 710 (2003), Pub. L. No. 108-415, § 1, 118 Stat. 2337 (2004), and Pub. L. No. 109-182, 120 Stat. 289 (2006).

[13] Not all of the obligations issued by federal government agencies are subject to the debt ceiling because either they are not issued under chapter 31 of title 31, U.S.C., or their principal and interest are not guaranteed by the U.S. government (e.g., obligations issued by the Tennessee Valley Authority (TVA) under authority of section 15d(a) of the TVA Act of 1933, 16 U.S.C. 831n-4(a) [2000]).

[14] In addition to the reported net cost, the federal government foregoes tax revenues as a result of preferential provisions, such as tax exclusions, credits, and deductions. These revenue losses are referred to as tax expenditures.

[15] GAO, *Suggested Areas for Oversight for the 110th Congress*, GAO-07-235R (Washington, D.C.: November 17, 2006).

[16] GAO, *21st Century Challenges: Reexamining the Base of the Federal Government*, GAO-05-325SP (Washington, D.C.: February 2005).

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