Part B

FINANCIAL SECTION

Message From the Chief Financial Officer

The Forest Service, an agency of the Department of Agriculture (USDA), strives to increase transparency of financial information that promotes the Open Government initiative and accountability and demonstrates results to the American people. As Chief Financial Officer, I am especially pleased to note that for the 10th consecutive year, the Forest Service received an unqualified ("clean") audit opinion on its principal FY 2011 financial statements. Additionally, for the 4th consecutive year, the independent auditors reported no area of material weakness.

As outlined in Chief Tidwell's message at the beginning of this report, we have worked aggressively in FY 2011 to complete recommended actions and close all open financial statement audits and a record number of program audits. These results demonstrate the agency's continued commitment to financial management excellence.

The agency's continued achievements in financial management are due in part to its focus on collaboration between the finance, budget, and program areas, as well as the various partnerships within each of these areas. Collaboration efforts advance good communication, transparency, integration, and efficiency in delivery of services. The joint efforts of Forest Service managers, employees, and partners are key as the Forest Service sustains quality financial management.

In keeping with USDA's commitment to deploy an enhanced financial system, the Forest Service is moving forward to prepare for the significant changes that come with the Financial Management Modernization Initiative (FMMI). In FY 2012, the Forest Service will continue to devote resources to ensure a successful implementation of FMMI in early FY 2013.

While we celebrate our successes, we also realize we have areas in which we can improve and strive to promote efficiency and continuous improvement.

Chief Tidwell addressed the daunting conservation challenges in his message. As such, we continue to address the inherent logistical challenges of managing vast natural resources that are becoming more complicated and expensive. It is key that we provide timely and accurate financial data to assist managers in making decisions as they manage these important resources.

Donna M. Carmical

DONNA M. CARMICAL
Chief Financial Officer

United States Department of Agriculture
Office of Inspector General
Washington, D.C. 20250

NOV 10 2011

REPLY TO
ATTN OF: 08401-0001-11

TO: Thomas Tidwell
Chief
Forest Service

ATTN: Donna Carmical
Chief Financial Officer

Jennifer McGuire
Director, Audit and Assurance

Sandy Coleman
Agency Liaison Officer

FROM: Gil H. Harden
Assistant Inspector General
for Audit

SUBJECT: Forest Service's Financial Statements for Fiscal Years 2011 and 2010

This report presents the results of the audit of Forest Service's (FS) financial statements for the fiscal years ending September 30, 2011 and 2010. The report contains an unqualified opinion on the financial statements, as well as an assessment of FS' internal controls over financial reporting and compliance with laws and regulations.

Kearney & Company, P.C. (Kearney), an independent certified public accounting firm, conducted the fiscal year 2011 audit. In connection with the contract, we reviewed Kearney's report and related documentation and inquired of its representatives. Our review, as differentiated from an audit in accordance with *Government Auditing Standards* (issued by the Comptroller General of the United States), was not intended to enable us to express, and we do not express, opinions on FS' financial statements, internal control, or on whether FS' financial management systems substantially complied with the Federal Financial Management Improvement Act; or conclusions on compliance with laws and regulations. Kearney is responsible for the attached auditor's report, dated November 8, 2011, and the conclusions expressed in the report. However, our review disclosed no instances where Kearney did not comply, in all material respects, with *Government Auditing Standards*, and the Office of Management and Budget Bulletin 07-04, *Audit Requirements for Federal Financial Statements*, as amended.

It is the opinion of Kearney, that the financial statements present fairly, in all material aspects, FS' financial position as of September 30, 2011, and its net costs, changes in net position, and budgetary resources for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

The Kearney report identified two significant deficiencies. Specifically, Kearney identified weaknesses in FS's internal controls over:

- information technology; and
- property, plant, and equipment.

Kearney did not consider either of the above significant deficiencies to be material weaknesses. Kearney reported that FS substantially complied with FFMIA, and did not report any noncompliances with laws and regulations exclusive of FFMIA.

The financial statements of FS as of and for the year ended September 30, 2010, were audited by KPMG LLP whose report dated November 5, 2010, expressed an unqualified opinion on those financial statements.

In accordance with Departmental Regulation 1720-1, please furnish a reply within 60 days describing the corrective actions taken or planned, including the timeframes to address the report recommendations. Please note the regulation requires a management decision to be reached on all findings and recommendations within a maximum of 6 months from report issuance.

Independent Auditor’s Report

KEARNEY& COMPANY

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REPORT OF INDEPENDENT AUDITORS

To the Chief of the United States Forest Service
The Inspector General, United States Department of Agriculture

We have audited the accompanying consolidated balance sheet of the United States Forest Service (Forest Service), an agency of the United States Department of Agriculture (USDA), as of September 30, 2011, and the related consolidated statements of net cost, changes in net position, and combined statement of budgetary resources (hereinafter referred to as "the financial statements") for the year then ended. The financial statements are the responsibility of the Forest Service's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of the Forest Service as of September 30, 2010 were audited by other auditors whose report, dated November 5, 2010, expressed an unqualified opinion on those statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America; standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements*, as amended. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above, including the accompanying notes, present fairly, in all material respects, the financial position of the Forest Service as of September 30, 2011, and its net cost of operations, changes in net position, and changes in budgetary resources for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The information in the Management's Discussion and Analysis, Required Supplementary Stewardship Information, Required Supplementary Information, and Other Accompanying Information sections is not a required part of the basic financial statements. Rather, they are considered supplementary information required by OMB Circular A-136, *Financial Reporting Requirements*, and the Federal Accounting Standards Advisory Board. This supplementary information is the responsibility of the Forest Service's management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit. However, such

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information was not subjected to the procedures applied in our audit of the basic financial statements. Accordingly, we do not express an opinion on this information.

In accordance with *Government Auditing Standards* and OMB Bulletin No. 07-04, as amended, we have also issued reports, dated November 8, 2011, on our consideration of the Forest Service's internal control over financial reporting and compliance, and on our tests of the Forest Service's compliance with certain provisions of laws, regulations, and other matters for the year ended September 30, 2011. The purpose of those reports is to describe the scope of our testing of internal control over financial reporting and compliance and the Forest Service's compliance with certain provisions of laws and regulations as well as the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance and other matters. Those reports are an integral part of an audit performed in accordance with *Government Auditing Standards* and OMB Bulletin No. 07-04, as amended, and should be considered in assessing the results of our audit.

Alexandria, Virginia
November 8, 2011

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INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL

To the Chief of the United States Forest Service
The Inspector General, United States Department of Agriculture

We have audited the financial statements of the United States Forest Service (Forest Service) as of and for the year ended September 30, 2011, and have issued our report dated November 8, 2011. We conducted our audit in accordance with auditing standards generally accepted in the United States of America; standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements*, as amended. The management of the Forest Service is responsible for establishing, maintaining, and assessing internal control related to financial reporting and compliance and assessing internal control to provide reasonable assurance that the broad control objectives of the Federal Managers' Financial Integrity Act of 1982 (FMFIA) are met.

In planning and performing our work, we considered the Forest Service's internal control over financial reporting and compliance by obtaining an understanding of the design effectiveness of the Forest Service's internal control, determining whether controls had been placed in operation, assessing control risk, and performing tests of the Forest Service's controls as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal controls. Accordingly, we do not express an opinion on the effectiveness of the Forest Service's internal control over financial reporting and compliance or on management's assertion on internal control included in Management's Discussion and Analysis.

We limited our internal control testing to those controls necessary to achieve the OMB Bulletin No. 07-04, as amended, control objectives that provide reasonable, but not absolute assurance, that: (1) transactions are properly recorded, processed, and summarized to permit the preparation of the financial statements in accordance with accounting principles generally accepted in the United States of America (GAAP), and assets are safeguarded against loss from unauthorized acquisition, use, or disposition; and (2) transactions are executed in compliance with laws governing the use of budget authority, Government-wide policies and laws identified in Appendix E of OMB Bulletin No. 07-04, as amended, and other laws and regulations that could have a direct and material effect on the financial statements. We did not test all internal controls relevant to operating objectives, as broadly defined by FMFIA, such as those controls relevant to ensuring efficient operations.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable

possibility that a material misstatement of the entity's financial statements will not be prevented or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraphs and was not designed to identify all deficiencies in internal control that might be significant deficiencies or material weaknesses; therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. We did not identify any deficiencies in internal control that we consider to be material weaknesses, as defined above.

A significant deficiency is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness yet important enough to merit attention by those charged with governance. We consider the following deficiencies in the Forest Service's internal control to be significant deficiencies.

Significant Deficiencies

I. Information Technology (IT)

The Forest Service's IT internal control structure, both for the general support systems and critical financial reporting applications, did not include a comprehensive risk analysis, effective monitoring of design and performance, and an ability to identify and respond to changing risk profiles. The National Institute of Standards and Technology (NIST) and Government Accountability Office (GAO) (in its Federal Information System Controls Audit Manual [FISCAM]) provide control objectives and evaluation techniques for IT internal control structures, which we utilized during the course of our audit.

The Forest Service's IT control environment included design and operation weaknesses that, when combined, are considered to be a significant deficiency, as summarized below.

- The Forest Service's control structure contains two weaknesses related to segregation of duties. In one instance, three users of one application had access to the application's development and production environments. The Forest Service's control structure relies on a manual control to mitigate this weakness; however, Kearney & Company, P.C.'s (Kearney) audit procedures indicated that this manual control does not mitigate the weakness. In the second instance, eight users of another application were able to perform incompatible functions. The Forest Service's control structure contains an automated review control for these functions at the Albuquerque Service Center (ASC); however, Kearney's audit procedures did not indicate that the Forest Service mitigates the risk related to this segregation of duties weakness to an acceptable level.

  Recommendation Number 1: Kearney recommends that the Forest Service monitor access to systems in order to prevent users from having incompatible functions, and document any instances of conflicting roles and provision of access based on risk

analysis. Kearney also recommends that the Forest Service augment and improve the identified mitigating controls to specifically address the weaknesses identified.

- The Forest Service did not deactivate employee accounts within one business day of an employee's separation, as required by Forest Service policy. Kearney's audit procedures identified approximately 600 separated employees in four applications. If their accounts are not deactivated timely, employees who have been separated may be able to access information systems after their separation from the Forest Service, which could result in waste, fraud, or abuse. Failure to limit user access and processing capabilities to authorized employees may result in system vulnerabilities, possible defalcations, and errors in accounting records.

  Recommendation Number 2: Kearney recommends that the Forest Service implement a process to ensure that inactive accounts and accounts for separated employees are disabled or removed from Forest Service information systems in a timely manner.

- The Forest Service does not currently maintain a comprehensive IT inventory of hardware and software for one General Support System (GSS), nor does it currently document and maintain hardware and software configuration baselines for two GSSs. Without a process for managing configuration baselines, the Forest Service increases the risk that information systems and their supporting IT infrastructures are not configured in a manner to maximize security. Weak security could lead to the compromise of information systems, and ultimately, sensitive financial data. Weak security could also negatively impact the confidentiality, integrity, and availability of financial system data. Additionally, the Forest Service cannot develop a comprehensive and effective IT Contingency Plan (CP) without baseline configurations. Failure to develop and test an IT CP may result in the loss of system access, data, and automated controls, which could lead to errors and defalcations.

  Recommendation Number 3: Kearney recommends that the Forest Service implement a process to ensure that information system inventories and configuration baselines are documented and updated in accordance with policy. This may require the Forest Service to document, back up, and protect a current and comprehensive baseline inventory of hardware, software, and firmware. This may also require the Forest Service to map hardware, software, and firmware to the applications they support. Kearney also recommends that the Forest Service select mandatory configuration settings based off of a NIST-approved baseline, and document any deviations from the baseline. This may require the Forest Service to ensure that changes to existing baselines follow the change management process, whereby changes are authorized, tested, approved, and documented according to policy.

- The Forest Service did not update documentation authorizing two information systems to operate in a timely manner. Specifically, the Forest Service did not fully implement all recommended steps within the risk management framework, including ongoing monitoring of the control environment and updating of System Security Plans (SSP) on

an annual basis, as required per United States Department of Agriculture (USDA) policy. By not monitoring the control environments for information systems and updating SSPs, the Forest Service increases the likelihood that risks to information systems will not be adequately mitigated in a timely and consistent manner, which may ultimately lead to errors in accounting records.

Recommendation Number 4: Kearney recommends that the Forest Service implement a process to ensure that the risk management framework is fully implemented. This may require the Forest Service to update SSPs at least annually, or whenever there is a significant change to the control environment. Kearney also recommends that the Forest Service certify and accredit all information systems before they are placed into operation or at least every three years, or more frequently if major system changes occur.

- The Forest Service does not have a formal and documented service provider management monitoring function in place. The Forest Service has not assigned responsibility for monitoring contracts, Service Level Agreements (SLA), and Statements on Standards for Attestation Engagement (SSAE) No. 16 reports. The Forest Service has not mitigated the risks associated with the use of service providers, and may not be able to identify ineffective or inefficient services provided by service providers, or failures in the service providers' control environments.

  Recommendation Number 5: Kearney recommends that the Forest Service implement a process to ensure that third party SLAs are executed, and that SSAE No. 16 reports are received from all service providers and evaluated. This may require the Forest Service to implement a service provider management process to identify parties responsible for monitoring contracts, agreements, SLAs, and SSAE No. 16 reports.

- The Forest Service was not able provide documentation supporting the status of any background re-investigations, as required by Office of Personnel Management (OPM) and USDA policy. The Forest Service did not provide documentation required by policy to support the status of three out of 45 initial background investigations. Employees and contractors who have not been screened by the background investigation process prior to gaining access to Forest Service information system(s) and/or have not been re-investigated according to OPM guidance may have access to Forest Service information systems that exceeds their need-to-know. This may lead to users compromising sensitive financial data or introducing unauthorized transactions.

  Recommendation Number 6: Kearney recommends that the Forest Service improve its process for background investigations and re-investigations to ensure that necessary investigations are performed in accordance with Forest Service policy. This may require the Forest Service to ensure that databases used to track contractors' and employees' background investigations and re-investigations are continually updated with contractors joining and leaving the Forest Service. This may also require the Forest Service to ensure that contractors and employees have background investigations commensurate with their position descriptions, and that re-investigations are completed in a timely manner.

- The Forest Service uses single factor authentication for remote access (i.e., user name and password), which is insufficient for a moderate to high-sensitivity system, according to Federal Information Processing Standard 199. Although the Forest Service has installed the software necessary to support multi-factor authentication for remote access users, it has not completed the implementation. The Forest Service has not fully complied with Homeland Security Presidential Directive 12, in that Personal Identity Verification cards have not been issued to approximately half of the 15,000 Forest Service employees and 2,500 contractors with Virtual Private Network access. Lack of multi-factor authentication over remote access could cause financial systems to be vulnerable to fraudulent access. Multi-factor authentication should be designed to be a more secure control to ensure that only approved and appropriate access to sensitive financial data is allowed.

  Recommendation Number 7: Kearney recommends that the Forest Service implement a process to ensure that the selection of authentication methods is appropriate based on risk. Kearney also recommends that the Forest Service implement multi-factor authentication for remote access. Since the Forest Service network can be accessed remotely, it is imperative that multi-factor authentication, rather than single factor authentication, be used to protect sensitive financial data.

II. Property, Plant, and Equipment (PP&E)

The Forest Service reported approximately $1.4 billion in net PP&E on its fiscal year (FY) 2011 Balance Sheet, which is about 23% of its total assets. Kearney's audit procedures identified several internal control deficiencies that negatively impact the Forest Service's ability to record real and personal property transactions in a complete, accurate, and timely manner. These deficiencies are discussed below.

- The Forest Service's internal control structure was not sufficient to ensure that projects were transferred from Work in Process (WIP) to PP&E as the project was substantially completed and placed into service. Specifically, field personnel do not submit project completion forms timely. Property personnel do not review WIP projects for indications of substantial completion. Forest Service policy produces at least a three-month delay in transferring substantially completed projects to PP&E.

  Kearney's audit procedures identified eight current year untimely WIP transfers, a 40% error rate, and 106 WIP projects that had no financial activity in the last four months. Additional procedures revealed that 18 projects, a 90% error rate, were substantially complete and should have been placed into service. Delays in the WIP transfer caused an understatement of depreciation by approximately $1.2 million.

  Recommendation Number 8: Kearney recommends that the Forest Service perform an annual evaluation of WIP projects to timely identify the need for WIP project closure. This may require the Forest Service to monitor the potential impact of understating depreciation expense related to untimely WIP transfers. Kearney also recommends that

the Forest Service improve escalation procedures to ensure appropriate monitoring and communication with field personnel.

- The Forest Service reported approximately $24 million of repairs and maintenance expenses. Kearney's audit procedures identified approximately $10 million of expenses that should have been capitalized in 26 transactions—a 42% error rate. The Forest Service's internal control structure did not ensure that only expenditures related to ordinary repairs and maintenance were expensed; the Forest Service expensed asset improvements, which included assets that were being remodeled, renovated, upgraded, or replaced. These improperly expensed transactions resulted in an understatement of depreciation by approximately $100,000.

  Recommendation Number 9: Kearney recommends that the Forest Service revise its existing desk procedures related to acquisition and capitalization of property that highlight the need to include capitalized costs when acquiring assets, and include direction stressing the need for periodic notifications and communication between field personnel and the ASC. Kearney also recommends that the Forest Service review its current capitalization procedures to assess an acceptable level of risk for not accurately capturing all capital improvement projects. This may require the Forest Service to identify and implement preventative and detective controls as necessary.

- The Forest Service's internal control structure did not ensure that capitalized personal property costs were complete and accurate. Kearney's audit procedures identified four transactions, a 3% error rate, in which approximately $5,000 of costs were not capitalized, projecting approximately $1 million in understated PP&E. These costs were related to transportation and modifications, and the errors resulted from the improper coding of transactions. In addition to an understatement of PP&E, these errors produced an understatement of current year depreciation expense.

  Recommendation Number 10: Kearney recommends that the Forest Service revise its existing desk procedures related to acquisition and capitalization of property highlighting the need to include capitalized costs when acquiring assets, and include direction stressing the need for periodic notifications and communication between field personnel and the ASC. Kearney also recommends that the Forest Service perform a review over all personal property additions for FY 2011 (in both personal property sub-ledger systems), and analyze and assess all capitalized costs associated with placing personal property into service. In addition, Kearney recommends that the Forest Service implement a detective control that analyzes costs associated with placing an asset into service at the Budget Object Code (BOC) level and comparing these costs to the job codes used for capitalized property.

- The Forest Service's internal control structure did not ensure that leases were accounted for properly. Kearney's audit procedures identified that 20 of the 47 capital leases, a 43% error rate, did not qualify for capital lease treatment when the option periods were removed from the analysis. In addition, the Forest Service did not update future

minimum operating lease payment schedules for subsequent changes to payment terms. Assets under capital leases were overstated by approximately $6 million, obligations under capital leases were understated by approximately $1 million, and the future minimum operating lease payment disclosure was originally and cumulatively overstated by $180 million.

Recommendation Number 11: Kearney recommends that the Forest Service refine and reassess its processes and internal controls related to lease accounting to ensure that leased assets are recorded accurately and completely. Kearney also recommends that the Forest Service implement a procedure to ensure that changes to operating leases are reflected in the future minimum payment schedule.

- The Forest Service's internal control structure does not ensure that property disposals are recorded timely. Kearney's audit procedures identified 23 property disposals recorded in the current year that occurred in a prior FY.

  Recommendation Number 12: Kearney recommends that the Forest Service strengthen its monitoring controls over property disposals at the field level in order to more accurately align the physical disposal of the asset in question and the receipt of the field supporting documentation.

During the audit, we noted certain other matters that we will report to the Forest Service's management in a separate letter. Additionally, the Forest Service's management has indicated in a separate response that it concurs with the findings presented in our report. We did not audit the Forest Service's response, and accordingly, we do not express an opinion on it.

* * * * * * * * *

This report is intended solely for the information and use of Forest Service management, those charged with governance and others within the Forest Service, the USDA Office of Inspector General, OMB, GAO, Department of the Treasury, and Congress, and is not intended to be and should not be used by anyone other than these specified parties.

Alexandria, Virginia
November 8, 2011

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APPENDIX A: Status of Prior Year Deficiencies

In the Independent Auditor's Report on Internal Control included in the audit report of the Forest Service's FY 2010 financial statements,[1] several issues were noted related to internal control over financial reporting. The table below presents a summary of the current year status of these issues.

Prior Year Internal Control Significant Deficiencies

Control Deficiency	2010 Status	2011 Status
IT Internal Control Environment	Significant Deficiency	Significant Deficiency
Accounts Payable Accruals	Significant Deficiency	N/A
Financial Reporting Requirements	Significant Deficiency	N/A
Credit Card Transactions	Significant Deficiency	Management Letter
Revenue Related Transactions	Significant Deficiency	N/A
Third Party Transactions Review	Significant Deficiency	Modified Repeat Condition (included in the IT Significant Deficiency)

* * * * * * * * *

This report is intended solely for the information and use of Forest Service management, those charged with governance and others within the Forest Service, the United States Department of Agriculture's Office of Inspector General, Office of Management and Budget, Government Accountability Office, Department of the Treasury, and Congress, and is not intended to be and should not be used by anyone other than these specified parties.

[1] *Independent Auditor's Report on the U.S. Forest Service 2010 and 2009 Financial Statements.*

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INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE AND OTHER MATTERS

To the Chief of the United States Forest Service
The Inspector General, United States Department of Agriculture

We have audited the financial statements of the United States Forest Service (Forest Service) as of and for the year ended September 30, 2011, and have issued our report dated November 8, 2011. We conducted our audit in accordance with auditing standards generally accepted in the United States of America; standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements*, as amended. The management of the Forest Service is responsible for compliance with laws and regulations.

As part of obtaining reasonable assurance about whether the Forest Service's financial statements are free of material misstatement, we performed tests of the Forest Service's compliance with certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of financial statement amounts, and certain other laws and regulations specified in OMB Bulletin No. 07-04, as amended. As part of our work, we performed tests of compliance with the Federal Financial Management Improvement Act of 1996 (FFMIA) Section 803(a) requirements. We limited our tests of compliance to these provisions; we did not test compliance with all laws and regulations applicable to the Forest Service. Providing an opinion on compliance with certain provisions was not an objective of our audit and accordingly, we do not express such an opinion.

Under FFMIA, we are required to report whether the Forest Service's financial management systems substantially comply with Federal financial management systems requirements, applicable Federal accounting standards, and the U.S. Standard General Ledger (USSGL) at the transaction level. Our audit procedures indicated that the Forest Service substantially complies with FFMIA; however, we noted two instances in which the Forest Service's financial management systems did not substantially comply with certain Federal financial management systems requirements, applicable Federal accounting standards, and the USSGL at the transaction level. The Forest Service did not maintain adequate segregation of duties in two financial systems. Additionally, the Forest Service did not terminate approximately 600 user access accounts upon employee separation.

Except as noted above, the results of our tests of compliance with the provisions of selected laws and regulations disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards* and OMB Bulletin No. 07-04, as amended.

KEARNEY& COMPANY

During the audit, we noted certain other matters that we will report to the Forest Service's management in a separate letter. Additionally, the Forest Service's management provided a separate response to our report. We did not audit the Forest Service's response, and accordingly, we do not express an opinion on it.

* * * * * * * * *

This report is intended solely for the information and use of the Forest Service management, those charged with governance and others within the Forest Service, the U.S. Department of Agriculture Office of Inspector General, OMB, the Government Accountability Office, the Department of the Treasury, and Congress, and is not intended to be and should not be used by anyone other than these specified parties.

Alexandria, Virginia
November 8, 2011

USDA United States Department of Agriculture | Forest Service | Washington Office | 1400 Independence Avenue, SW Washington, DC 20250

File Code: 1430
Date: NOV 08 2011

Mr. Bill Kubistal
Partner
Kearney & Company
1701 Duke Street, Suite 500
Alexandria, VA 22314

Dear Mr. Kubistal,

We have reviewed the Kearney & Company Independent Auditors Report dated the day of this letter, and generally agree with its contents. The Forest Service will develop an implementation plan to address the findings and recommendations identified during the audit. As we consider the required corrective actions, we will continue to work with the Office of the Inspector General in identifying the specific actions that will assist us in successfully addressing the recommendations.

If you have questions or require additional information, please contact me at (202) 205-1321.

Sincerely,

Donna M. Carmical

DONNA M. CARMICAL
Chief Financial Officer

cc: Steve Boozell OIG, Jennifer McGuire, Kandice Cotner, Dianna Capshaw, Erica Y Banegas, Sandy T Coleman

U.S. Department of Agriculture
Forest Service
CONSOLIDATED BALANCE SHEETS
As of September 30, 2011 and 2010
(in millions)

	2011	2010
Assets:		
Intragovernmental:		
Fund Balance with Treasury (Note 2)	$ 4,379	$ 5,252
Investments (Note 3)	-	6
Accounts Receivable, net (Note 4)	20	24
Total Intragovernmental	4,399	5,282
Cash and Other Monetary Assets	1	1
Accounts Receivable, net (Note 4)	256	115
General Property, Plant, and Equipment (PP&E), net (Note 5)	1,400	1,383
Other (Note 1D)	23	44
Total Assets	$ 6,079	$ 6,825
Stewardship PP&E (Note 6)		
Liabilities:		
Intragovernmental:		
Federal Employee Benefits (Notes 7 & 8)	$ 73	$ 74
Other (Note 10)	188	132
Total Intragovernmental	261	206
Accounts Payable	36	47
Federal Employee Benefits (Notes 7 & 8)	381	369
Environmental and Disposal Liabilities (Notes 7 & 9)	1	1
Other (Note 10)	1,583	1,514
Total Liabilities (Note 7)	2,262	2,137
Commitments and Contingencies (Note 10)		
Net Position:		
Unexpended Appropriations - other funds	2,056	2,991
Cumulative Results of Operations - earmarked funds (Note 12)	1,002	933
Cumulative Results of Operations - other funds	759	764
Total Net Position	3,817	4,688
Total Liabilities and Net Position	$ 6,079	$ 6,825

The accompanying notes are an integral part of these statements.

U.S. Department of Agriculture
Forest Service
CONSOLIDATED STATEMENTS OF NET COST
For the years ended September 30, 2011 and 2010
(in millions)

	2011	2010
Program Costs (Note 13):		
Total Gross Costs	$ 7,160	$ 6,702
Less: Total Earned Revenue	833	623
Net Cost of Operations	$ 6,327	$ 6,079

The accompanying notes are an integral part of these statements.

U.S. Department of Agriculture
Forest Service
CONSOLIDATED STATEMENTS OF CHANGES IN NET POSITION
For the years ended September 30, 2011 and 2010
(in millions)

	FY 2011			FY 2010		
	Earmarked Funds (Note 12)	**All Other Funds**	**Consolidated Total**	**Earmarked Funds (Note 12)**	**All Other Funds**	**Consolidated Total**
Cumulative Results of Operations:						
Beginning Balance	$ 933	$ 764	$ 1,697	$ 907	$ 751	$ 1,658
Budgetary Financing Sources:						
Appropriations Used	-	5,849	5,849	-	5,531	5,531
Non-Exchange Revenue	-	2	2	-	2	2
Donations and Forfeitures of Cash	1	-	1	1	-	1
Transfers - In/Out without Reimbursement	116	-	116	170	-	170
Other Financing Sources (Non-Exchange):						
Transfers without Reimbursement	(68)	68	-	(60)	63	3
Imputed Financing	-	425	425	-	426	426
Other	66	(68)	(2)	43	(58)	(15)
Total Financing Sources	115	6,276	6,391	154	5,964	6,118
Net Cost of Operations	(46)	(6,281)	(6,327)	(128)	(5,951)	(6,079)
Net Change	69	(5)	64	26	13	39
Cumulative Results of Operations	**1,002**	**759**	**1,761**	**933**	**764**	**1,697**
Unexpended Appropriations:						
Beginning Balance	-	2,991	2,991	-	2,966	2,966
Budgetary Financing Sources:						
Appropriations Received	-	5,327	5,327	-	5,557	5,557
Appropriation Transfers - In/Out	-	(3)	(3)	-	(1)	(1)
Other Adjustments	-	(410)	(410)	-	-	-
Appropriations Used	-	(5,849)	(5,849)	-	(5,531)	(5,531)
Total Budgetary Financing Sources	-	(935)	(935)	-	25	25
Total Unexpended Appropriations	**-**	**2,056**	**2,056**	**-**	**2,991**	**2,991**
Net Position	**$ 1,002**	**$ 2,815**	**$ 3,817**	**$ 933**	**$ 3,755**	**$ 4,688**

The accompanying notes are an integral part of these statements.

U.S. Department of Agriculture
Forest Service
COMBINED STATEMENTS OF BUDGETARY RESOURCES
For the years ended September 30, 2011 and 2010
(in millions)

	2011	2010
Budgetary Resources:		
Unobligated Balance, Brought Forward, October 1	$ 2,359	$ 2,745
Recoveries of Prior Year Unpaid Obligations	94	40
Budget Authority:		
Appropriations	5,824	6,094
Spending Authority from Offsetting Collections:		
Earned:		
Collected	496	495
Change in Receivables from Federal Sources	137	(50)
Change in Unfilled Customer Orders:		
Advance Received	49	7
Without Advance from Federal Sources	38	9
Subtotal	6,544	6,555
Nonexpenditure Transfers, net	(2)	(1)
Permanently Not Available	(410)	-
Total Budgetary Resources (Note 16)	$ 8,585	$ 9,339
Status of Budgetary Resources:		
Obligations Incurred (Note 15):		
Direct	$ 6,064	$ 6,571
Reimbursable	614	$ 409
Subtotal	6,678	6,980
Unobligated Balance-Apportioned (Note 2)	1,194	1,361
Unobligated Balance Not Available (Note 2)	713	998
Total Status of Budgetary Resources (Note 16)	$ 8,585	$ 9,339
Change in Obligated Balance:		
Obligated Balance, net		
Unpaid Obligations, Brought Forward, October 1	$ 3,072	$ 2,641
Less: Uncollected Customer Payments from Federal Sources, Brought Forward, October 1	(310)	(351)
Total Unpaid Obligated Balance, net	2,762	2,290
Obligations Incurred, net	6,678	6,980
Less: Gross Outlays	(6,885)	(6,509)
Less: Recoveries of Prior Year Unpaid Obligations, actual	(94)	(40)
Change in Uncollected Customer Payments from Federal Sources	(175)	41
Obligated Balance, net, End of Period		
Unpaid Obligations (Note 17)	2,771	3,072
Less: Uncollected Customer Payments from Federal Sources	(485)	(310)
Total, Unpaid Obligated Balance, net, End of Period (Note 2)	$ 2,286	$ 2,762
Net Outlays:		
Gross Outlays	$ 6,885	$ 6,509
Less: Offsetting Collections	(545)	(503)
Less: Distributed Offsetting Receipts	(467)	(429)
Net Outlays	$ 5,873	$ 5,577

The accompanying notes are an integral part of these statements.

NOTE 1: SIGNIFICANT ACCOUNTING POLICIES

A: REPORTING ENTITY

The U.S. Department of Agriculture (USDA) Forest Service (Forest Service) was established on February 1, 1905, as an agency of the United States Federal Government within the USDA, for the purpose of maintaining and managing the Nation's forest reserves. It operates under the guidance of the Under Secretary for Natural Resources and Environment. Forest Service policy is implemented through nine regional National Forest System (NFS) offices, one State and Private Forestry (S&PF) area office, five Research and Development (R&D) stations, the Forest Products Laboratory (FPL) and the International Institute of Tropical Forestry (IITF), functioning in nearly all States, Puerto Rico, and the U.S. Virgin Islands.

The Forest Service's mission includes the following four major segments:

National Forests and Grasslands – Protection and management of an estimated 193 million acres (unaudited) of NFS land that includes 36.6 million acres (unaudited) of designated wilderness areas. In addition, the Forest Service partners with other nations and organizations to foster global natural resource conservation and sustainable development of the world's forest resources.

Forest and Rangeland Research – Research and development of forest and rangeland management practices to provide scientific and technical knowledge for enhancing and protecting the economic productivity and environmental quality of the 1.3 billion acres (unaudited) of forests and associated rangelands in the United States.

State and Private Forestry – Cooperation with and assistance to State and Local governments, Tribal governments, forest industries, and private landowners to help protect and manage non-Federal forests and associated rangeland and watershed areas.

Wildland Fire Management – Protection of life, property, and natural resources on NFS lands, extending to an estimated additional 20 million acres (unaudited) of adjacent State and private lands.

The accompanying consolidated and combined financial statements of the Forest Service account for all funds under the Forest Service's control. Substantially all assets are considered "entity assets" and are available for use in the Forest Service's operations.

B: BASIS OF PRESENTATION AND ACCOUNTING

The Consolidated Balance Sheets (BS), Consolidated Statements of Net Cost (SNC), Consolidated Statements of Changes in Net Position (SCNP), and the Combined Statements of Budgetary Resources (SBR) (hereinafter referred to as the "financial statements") were prepared to report the financial position, net costs, changes in net position, and budgetary resources of the Forest Service. The financial statements have been prepared from the books and records of the Forest Service in accordance with accounting principles generally accepted in the United States of America as promulgated by the Federal Accounting Standards Advisory Board (U.S. GAAP) and in accordance with the Office of Management and Budget (OMB) Circular A-136, *Financial Reporting Requirements*, revised September 29, 2010. All material intra-agency transactions and balances have been eliminated for presentation on a consolidated basis. However, the SBR is presented on a combined basis in accordance with OMB Circular A-136.

These financial statements present proprietary and budgetary information. The accounting structure of Federal agencies is designed to reflect both accrual and budgetary accounting transactions. Under the accrual method of accounting, revenues are recognized when earned and expenses are recognized when incurred without regard to receipt or payment of cash. The budgetary accounting principles, on the other hand, are designed to recognize the obligation of funds according to legal requirements, which in many cases is prior to the occurrence of an

accrual-based transaction. The recognition of budgetary accounting transactions is essential for compliance with legal constraints and controls over the use of Federal funds.

The Forest Service recognizes budgetary resources as assets when cash funds held by U.S. Department of Treasury (Treasury) is made available through the Treasury General Fund warrants and other transfers. In addition to appropriated funds, the Forest Service is authorized by law to retain specific earned revenues primarily from sales of forest products and services and to spend these monies on resource management activities identified in the governing legislation. Some examples of the Forest Service's earned revenues are monies collected from timber sales or recreation fees.

C: FUND BALANCE WITH TREASURY

Treasury processes cash receipts and disbursements on behalf of the Forest Service. Funds on deposit with Treasury are primarily appropriated, trust and other fund types such as special funds that are available to pay current liabilities and finance authorized purchase commitments.

D: OTHER ASSETS

Payments made by the Forest Service in advance of the receipt of goods and services are recorded as advances at the time of payment and recognized as expenditures/expenses when the related goods and services are received.

E: GENERAL PROPERTY, PLANT, AND EQUIPMENT

General property, plant, and equipment (PP&E) includes real and personal property used in normal business operations. Real and personal property is recorded at cost or estimated fair value and must have an estimated useful life of 2 years or more. The Forest Service capitalization threshold for real and personal property is $25 thousand or more. Internal use software is capitalized in accordance with U.S. GAAP if the fair value meets or exceeds $100,000. The Forest Service recognizes liabilities for capital leases in accordance with U.S. GAAP. Under U.S. GAAP the cost of general PP&E acquired under a capital lease is equal to the amount recognized as a liability for the capital lease at its inception (net present value of the lease payments) unless the net present value exceeds the fair value of the asset. There are no restrictions on the use or convertibility of general PP&E.

See Note 6 for specific disclosures related to multi-use Heritage Assets.

F: STEWARDSHIP PP&E

Stewardship PP&E includes assets such as heritage assets and stewardship land, which due to their unique nature would be difficult to value. In accordance with U.S. GAAP, all heritage assets and stewardship land information has been reclassified as basic, except for condition information, which is reclassified as required supplementary information (RSI).

See Note 6 for specific disclosures related to Stewardship PP&E.

G: LIABILITIES

Liabilities represent the amount of monies or other resources that are likely to be paid by the Forest Service as a result of a transaction or event that has occurred. However, the Forest Service cannot satisfy a liability without an appropriation. Liabilities for which there is no appropriation and for which there is no certainty that an appropriation will be enacted, are classified as unfunded liabilities. The U.S. Government, acting in its sovereign capacity, can abrogate liabilities.

H: ENVIRONMENTAL AND DISPOSAL LIABILITIES

The Forest Service's estimated Government-related and Government-acknowledged environmental liabilities are principally associated with the future remediation of certain landfills, buildings, and other related sites in accordance with all applicable Federal, State and local laws.

See Note 9 for specific disclosures related to cleanup costs for ongoing operations.

I: COMMITMENTS AND CONTINGENCIES

The Forest Service is a party in various administrative proceedings, legal actions, environmental lawsuits, and claims. In the opinion of the Forest Service management and its legal counsel, the ultimate resolution of most of these proceedings is remote. Where probable and reasonably estimable, the full value of amounts related to unsettled litigation and other claims against the Forest Service is recognized as a liability and expense. Expected amounts related to litigation and other claims include amounts to be paid by Treasury on behalf of the Forest Service from a permanent appropriation for judgments and from other appropriations.

J: WORKERS' COMPENSATION LIABILITY

The Federal Employees' Compensation Act (FECA) provides income and medical cost protection to Federal civilian employees injured on the job, employees who have incurred a work related occupational disease and beneficiaries of employees whose death is attributable to a job-related injury or occupational disease. Benefit claims incurred for the Forest Service's employees under FECA are administered by the U.S. Department of Labor (DOL). The USDA uses Forest Service funds to reimburse the DOL for FECA claims. Consequently, the Forest Service recognizes a liability for this compensation comprised of: (1) an accrued liability that represents money owed for claims paid by the DOL through the current fiscal year and (2) an actuarial liability that represents the expected liability for Forest Service approved compensation cases to be paid beyond the current fiscal year.

K: EMPLOYEE ANNUAL, SICK, AND OTHER LEAVE

Annual and other vested leave such as compensatory, credit hours, and restored leave is accrued as it is earned, and the accrual is reduced as leave is taken. Each quarter, the balance in the accrued annual leave account is adjusted to reflect the latest pay rates and unused hours of leave. Sick leave is generally non-vested. Funding will be obtained from future financing sources to the extent that current or prior year appropriations are not available to fund annual and other types of vested leave earned but not taken. Sick leave and other types of non-vested leave are expensed when used.

L: PENSION AND OTHER RETIREMENT BENEFITS

Forest Service employees participate in either the Civil Service Retirement System (CSRS) or the Federal Employees Retirement System (FERS). The employees who participate in CSRS are beneficiaries of the Forest Service's matching contribution, equal to 7.0 percent of pay, distributed to their annuity account in the Civil Service Retirement and Disability Fund.

FERS went into effect on January 1, 1987, pursuant to Public Law 99-335. FERS and Social Security automatically cover most employees hired after December 31, 1983. Employees hired prior to January 1, 1984 could elect to join FERS and Social Security, or choose to remain in CSRS. FERS offers a savings plan to which the Forest Service automatically contributes 1.0 percent of pay and matches any employee contribution up to an additional 4.0 percent of pay. For FERS participants, the Forest Service also contributes the employer's matching share for Social Security.

The Forest Service recognizes the imputed cost of pension and other health and life insurance retirement benefits during the employees' active years of service. Office of Personnel Management (OPM) actuaries determine

pension cost factors by calculating the value of pension benefits expected to be paid in the future and communicate these factors and information regarding the full cost of health and life insurance benefits to the Forest Service for current period expense reporting.

M: REVENUES AND OTHER FINANCING SOURCES

The Forest Service is funded principally through Congressional appropriations and other authorizations in the Budget of the United States. The Forest Service receives annual, multi-year, and no-year appropriations that are used, within statutory limits, for operating and capital expenditures. Other funding sources are derived through reimbursements for services performed for other Federal and non-Federal entities, sale of goods to the public, gifts from donors, cost-share contributions and interest on invested amounts.

Appropriations are used at the time the related program or administrative expenses are incurred or when the appropriations are expended for capital property and equipment. Other revenues are recognized as earned when goods have been delivered or services rendered.

In accordance with U.S. GAAP, the Forest Service classifies revenue as either “exchange revenue” or “non-exchange revenue.” Exchange revenue arises from transactions that occur when each party to the transaction sacrifices value and receives value in return. An example of exchange revenue is the income from the sale of forest products. In some cases, the Forest Service is required to remit exchange revenue receipts to Treasury. In other instances, the Forest Service is authorized to use all, or a portion of its exchange revenues for specific purposes. Non-exchange revenue is revenue the Federal Government is able to demand or receive because of its sovereign powers. Penalties and cash donations received from private citizens and organizations are examples of non-exchange revenue.

The Forest Service reports the full cost of products and services generated from the consumption of resources. Full cost is the total amount of resources used to produce a product or provide a service unless otherwise noted. In accordance with U.S. GAAP, the Forest Service’s pricing policies are set to recover full cost except where mandated by law or for the public good, such as in the case of grazing fees. Also, costs and exchange revenue are disclosed in Note 13 as intragovernmental or with the public based on the related source or customer, respectively.

N: IMPUTED FINANCING

The Forest Service recognizes as imputed financing the amount of accrued pension and post-retirement benefit expenses for current employees. The assets and liabilities associated with such benefits are the responsibility of the administering agency, OPM. Amounts paid from the Treasury Judgment Fund in settlement of claims or court assessments against the Forest Service are also recognized as imputed financing. Imputed financing for the years ended September 30, 2011 and 2010 was $425 million and $426 million, respectively.

O: PARENT/CHILD REPORTING REQUIREMENTS

The Forest Service is a party to allocation transfers with other federal agencies as both a transferring (parent) entity and/or a receiving (child) entity. Allocation transfers are legal delegations by one department of its authority to obligate budget authority and outlay funds to another department. A separate fund account (allocation account) is created in the Treasury as a subset of the parent fund account for tracking and reporting purposes. All allocation transfers of balances are credited to this account, and subsequent obligations and outlays incurred by the child entity are charged to this allocation account as they execute the delegated activity on behalf of the parent entity. In accordance with OMB Circular A-136, all financial activity related to these allocation transfers (e.g., budget authority, obligations, and outlays) is reported in the financial statements of the parent entity, from which the underlying legislative authority, appropriations and budget apportionments are derived. The Forest Service allocates funds as the parent to the Department of Transportation (DOT), Department of Interior (DOI), Department of the Army, Department of the Navy, Department of the Air Force, and the Corps of Engineers, Civil.

The Forest Service receives allocation transfers, as the child, from the DOL, DOT, and DOI.

P: USE OF ESTIMATES

Management has made certain estimates and assumptions when reporting assets, liabilities, revenue, and expenses. Actual results could differ from these estimates. Significant estimates underlying the accompanying financial statements include the majority of accrued liabilities and federal employee benefits liabilities.

Q: EARMARKED FUNDS

The Forest Service reports the earmarked funds for which it has program management responsibility, using the following three criteria:

- A statute committing the Federal Government to use specifically identified revenues and other financing sources only for designated activities, benefits, or purposes.
- Explicit authority for the earmarked fund to retain revenues and other financing sources not used in the current period for future use to finance the designated activities, benefits, or purposes.
- A requirement to account for and report on the receipt, use, and retention of the revenues and other financing sources that distinguishes the earmarked fund from the Federal Government's general revenues.

R: INTER-ENTITY COST IMPLEMENTATION

In accordance with U.S. GAAP, each entity's full cost should incorporate the full cost of goods and services that it receives from other entities. The entity providing the goods and services has the responsibility to provide the receiving entity with information on the full cost of such goods or services either through billing or other advice.

Recognition of inter-entity costs that are not fully reimbursed is limited to material items that (1) are significant to the receiving entity, (2) form an integral or necessary part of the receiving entity's output, and (3) can be identified or matched to the receiving entity with reasonable precision. Broad and general support services provided by an entity to all or most other entities should not be recognized unless such services form a vital and integral part of the operations or output of the receiving entity.

NOTE 2: FUND BALANCE WITH TREASURY

Funds with Treasury are primarily appropriated (general and special funds), revolving (working capital fund), and trust funds that are available to pay current liabilities and finance authorized purchase commitments. The category of other fund types includes deposit and suspense accounts. It is the Forest Service's policy to ensure the Fund Balance with Treasury (FBWT) reported on the balance sheets is consistent with the records of the Treasury.

The Forest Service has a known discrepancy with Treasury in FBWT, suspense account 12F3885, as of September 30, 2011. These suspense accounts were discontinued effective July 31, 2008. USDA elected not to obtain a waiver, which would have permitted the Forest Service to continue using suspense accounts. In addition, Treasury has stopped accepting new activity in these suspense accounts from entities without the required waiver, but certain intragovernmental activity is still mapped to 12F3875 and 12F3885. Although there is continuing activity in 12F3875, as of September 30, 2011, the balance is zero and therefore did not result in a discrepancy with Treasury. Per Treasury guidance, the balances are not reported to Treasury. The difference between the FBWT balance and Treasury as of September 30, 2011, is $222,169.

Fund Balance with Treasury as of September 30, 2011 and 2010 consisted of the following:

	(in millions)	
A. Fund Balances:	**2011**	**2010**
(1) Trust Funds	$ 397	$ 374
(2) Special Funds	964	943
(3) Revolving Funds	178	167
(4) General Funds	2,726	3,686
(5) Other Fund Types	114	82
Total	$ 4,379	$ 5,252
B. Status of Funds:		
(1) Unobligated Balance		
(a) Available	$ 1,194	$ 1,361
(b) Unavailable	713	998
(2) Obligated Balance not yet Disbursed	2,286	2,762
(3) Non-Budgetary FBWT Accounts	186	131
Total	$ 4,379	$ 5,252

NOTE 3: INVESTMENTS

Investments are associated with earmarked funds. The Federal Government does not set aside assets to pay future expenditures associated with earmarked funds. Instead, the cash generated from earmarked funds is used by Treasury for general Government purposes. Treasury securities are issued to the earmarked fund as evidence of earmarked receipts and provide the fund with the authority to draw upon Treasury for future authorized expenditures. These securities are an asset to the earmarked fund and are presented as Investments in Note 12 – Earmarked Funds. Treasury securities are a liability of Treasury and are eliminated in the consolidation of the U.S. Government-wide financial statements. Treasury will finance any future redemption of the securities by an earmarked fund in the same manner that all other Government expenditures are financed. Forest Service earmarked fund investments reported in FY 2010 were redeemed in 1st Quarter FY 2011.

Investments
As of and for the year ended September 30, 2011
(in millions)

	Amortization Method	Cost	Net Amortized (Premium)	Investments, Net	Market Value Disclosure
(3) Non-Marketable:					
Market-Based	Straight-Line	$ -	$ -	$ -	$ -
Total	**N/A**	**$ -**	**$ -**	**$ -**	**$ -**

Investments
As of and for the year ended September 30, 2010
(in millions)

	Amortization Method	Cost	Net Amortized (Premium) Discount	Investments, Net	Market Value Disclosure
(3) Non-Marketable:					
Market-Based	Straight-Line	$ 6	$ -	$ 6	$ 6
Total	**N/A**	**$ 6**	**$ -**	**$ 6**	**$ 6**

NOTE 4: ACCOUNTS RECEIVABLE, NET

Intragovernmental Accounts Receivable represent amounts due under reimbursable and cooperative agreements with Federal entities for services provided by the Forest Service. An Allowance for Uncollectible Accounts is not established for these amounts because monies due from other Federal entities are considered fully collectible. As of September 30, 2011 and 2010, the Intragovernmental Accounts Receivable balances were $20 million and $24 million, respectively.

Non-Intragovernmental Accounts Receivable is comprised primarily of timber harvest and reimbursements and refunds owed to the Forest Service for fire prevention and suppression activities. An Allowance for Uncollectible Accounts is established against outstanding non-Federal accounts receivable based on historical experience. The historical percentage is calculated by comparing the ending fiscal year balance in the write-off account against the previous ending fiscal year balance of open accounts receivable. The historical percentage is then applied to the ending balance of open accounts receivable. This approach is used to estimate the allowance for uncollectible accounts and recording receivables at net realizable value.

Non-Intragovernmental Accounts Receivable as of September 30, 2011 and 2010 consisted of the following:

	(in millions)	
	2011	2010
Accounts Receivable	$ 264	$ 121
Allowance for Uncollectible Accounts	(8)	(6)
Accounts Receivable, Net	$ 256	$ 115

NOTE 5: GENERAL PROPERTY, PLANT, AND EQUIPMENT, NET

Depreciation of General PP&E for the Forest Service is recorded on the straight-line method based on the estimated useful lives listed below. Capitalization thresholds are provided in Note 1, Section E.

As of September 30, 2011 and 2010 the Forest Service's General PP&E consisted of the following:

September 30, 2011
(in millions)

Property Class	Estimated Useful Life (Years)	Cost	Accumulated Depreciation	Book Value
Personal Property				
Equipment	5 - 20	$ 702	$ (462)	$ 240
Internal Use Software	5	94	(84)	10
Internal Use Software in Development	n/a	73	-	73
Total Personal Property		**869**	**(546)**	**323**
Real Property				
Land and Land Rights	n/a	52	-	52
Improvements to Land	10	732	(644)	88
Construction in Progress	n/a	187	-	187
Buildings, Improvements, and Renovations	15 - 30	993	(615)	378
Other Structures and Facilities	15 - 50	1,692	(1,346)	346
Assets Under Capital Lease	5 - 30	61	(39)	22
Leasehold Improvements	10	11	(7)	4
Total Real Property		**3,728**	**(2,651)**	**1,077**
Total		**$ 4,597**	**$ (3,197)**	**$ 1,400**

September 30, 2010
(in millions)

Property Class	Estimated Useful Life (Years)	Cost	Accumulated Depreciation	Book Value
Personal Property				
Equipment	5 - 20	$ 688	$ (467)	$ 221
Internal Use Software	5	95	(76)	19
Internal Use Software in Development	n/a	46	-	46
Total Personal Property		**829**	**(543)**	**286**
Real Property				
Land and Land Rights	n/a	51	-	51
Improvements to Land	10	715	(624)	91
Construction in Progress	n/a	139	-	139
Buildings, Improvements, and Renovations	15 - 30	977	(591)	386
Other Structures and Facilities	15 - 50	1,698	(1,301)	397
Assets Under Capital Lease	5 - 30	61	(36)	25
Leasehold Improvements	10	14	(6)	8
Total Real Property		**3,655**	**(2,558)**	**1,097**
Total		**$ 4,484**	**$ (3,101)**	**$ 1,383**

NOTE 6: STEWARDSHIP PROPERTY, PLANT, AND EQUIPMENT

This note provides information on certain resources entrusted to and stewardship responsibilities assumed by the Forest Service. These resources and responsibilities are referenced in accordance with U.S. GAAP on the Forest Service's Balance Sheets.

Stewardship PP&E

Stewardship PP&E are assets whose physical properties resemble those of the General PP&E that are traditionally capitalized in the financial statements. Due to the nature of these assets, however, valuation would be difficult and matching costs with specific periods would not be meaningful. Stewardship PP&E includes heritage assets and stewardship land. The Forest Service reports Stewardship PP&E by site. Sites include National Forests, National Grasslands, other Forest Service-managed sites, and non Forest Service-managed sites such as museums and university laboratories. The protection of these lands and resources is a fundamental Forest Service responsibility.

The mission of the Forest Service is to sustain the health, diversity, and productivity of the Nation's forests and grasslands to meet the needs of present and future generations. The Forest Service strives to achieve quality land management under the sustainable multiple-use management concept to deliver the necessary products and services that are essential for enhancing natural resource stewardship and to meet the diverse needs of people.

The preservation and management of heritage assets is guided through the enactment of many laws and regulations including the Organic Administration Act of 1897 (16 U.S.C. 473-478, 479-482, 551), the Antiquities Act of 1906 (16 U.S.C. 431), the National Historic Preservation Act of 1966 (16 U.S.C. 470), the Archaeological Resources Protection Act of 1979 (16 U.S.C. 470aa *et seq*.), the Native American Graves Protection and Repatriation Act of 1990 (25 U.S.C. 3001), Executive Order 13287 – Preserve America, issued March 3, 2003, National Register of Historic Places (36 CFR, part 60), Protection of Archaeological Resources Uniform Regulations (36 CFR part 296), and the Curation of Federally-owned and Administered Archaeological Collections (36 CFR part 79), as well as many others.

The predominant laws governing the management of stewardship land are the Transfer Act of 1905 (16 U.S.C. 472, 478, 495, 551, 554a, 615b, 554, 524), the Multiple Use-Sustained Yield Act of 1960 (16 U.S.C. 528-531, 528 note), the Forest and Rangeland Renewable Resources Planning Act of 1974 (16 U.S.C. 1600 note, 1600-1614), and the National Forest Management Act of 1976 (16 U.S.C. 472a).

These laws and regulations are implemented through Forest Service policy and guidance. Program management evaluations and technical reviews are performed to ensure compliance.

Heritage Assets

Heritage assets, as defined by U.S. GAAP, are PP&E that are unique for one or more of the following reasons:

- Historical or natural significance
- Cultural, educational, or artistic (e.g. aesthetic) importance
- Significant architectural characteristics

Heritage assets can include non-collection type assets, such as historic or prehistoric sites, monuments, and buildings, or collection type assets, such as objects gathered and maintained for exhibition.

Some heritage assets may also be classified as multi-use heritage assets if they serve two purposes—a heritage function and a general government operations function, such as a forest guard station building. The building may be listed on the National Register of Historic Places, but it serves primarily as an administrative site, hence, it is considered a "multi-use" heritage asset. Multi-use heritage assets are capitalized as General PP&E. Multi-use heritage assets are reported as Stewardship PP&E.

Heritage Asset categories can include the following:

Priority Heritage Assets: Heritage assets of distinct public value that are, or should be, actively maintained, and meet one or more of the following criteria:

- The property is recognized through an official designation, such as a listing on the National Register of Historic Places, State register, etc.
- The property is recognized through prior investment in preservation, interpretation, and use. Any improvement to a PHA that meets real property designation criteria is considered real property.
- The property is recognized in an agency-approved management plan.
- The property exhibits critical deferred maintenance needs and those needs have been documented.

Other Heritage Assets: Assets that may have potential important historical or cultural significance, but lack formal listing and the demonstrated need for active maintenance.

Assemblage Assets: Any grouping of artifacts or archival materials aggregated through donation, agency events, site-specific or other field collection, other acquisition method, or combination therein. Assemblage assets include materials donated to the Forest Service, artifact or archival materials collected from a single site, Forest Service administrative unit or event, or any combination thereof.

Addition and Deletion of Heritage Assets

The Forest Service generally does not construct heritage assets, although in some circumstances important site-structural components may be rehabilitated or reconstructed into viable historic properties to provide forest visitors with use and interpretation. Heritage assets may be added through the procurement process, but this rarely occurs. Normally, heritage assets are part of the land acquisition and inventory process. Deletion occurs through land exchange or natural disasters. Most additions occur through inventory activities where previously undocumented sites are discovered and added to the total.

The Heritage Asset Sites reported by management area as of September 30, 2011, are as follows:

HERITAGE ASSET SITES BY MANAGEMENT AREA	FY 2010 Final Sites	Additions	Deletions	FY 2011 Final Sites
National Forests				
Region 1 - Northern Region	15	-	-	15
Region 2 - Rocky Mountain Region	17	-	-	17
Region 3 - Southwestern Region	12	-	-	12
Region 4 - Intermountain Region	18	-	-	18
Region 5 - Pacific Southwest Region	18	-	-	18
Region 6 - Pacific Northwest Region	21	-	-	21
Region 8 - Southern Region	35	-	-	35
Region 9 - Eastern Region	17	-	-	17
Region 10 - Alaska Region	2	-	-	2
Subtotal	155			155
National Grasslands				
Region 1 - Northern Region	4	-	-	4
Region 2 - Rocky Mountain Region	7	-	-	7
Region 3 - Southwestern Region	4	-	-	4
Region 4 - Intermountain Region	1	-	-	1
Region 5 - Pacific Southwest Region	1	-	-	1
Region 6 - Pacific Northwest Region	1	-	-	1
Region 8 - Southern Region	2	-	-	2
Subtotal	20			20
Non Forest Service Sites	155	18	(6)	167
TOTAL SITES	**330**	**18**	**(6)**	**342**

Region 1 - Montana, North Dakota, Northern Idaho, and Northwestern South Dakota
Region 2 - Colorado, Kansas, Nebraska, South Dakota, and Wyoming
Region 3 - Arizona and New Mexico
Region 4 - Southern Idaho, Nevada, Utah, and Western Wyoming
Region 5 - California, Hawaii, Guam, and Trust Territories of the Pacific Islands
Region 6 - Oregon and Washington
Region 8 - Alabama, Arkansas, Florida, Georgia, Kentucky, Louisiana, Mississippi, North Carolina, Oklahoma, Puerto Rico, South Carolina, Tennessee, Texas, Virgin Islands, and Virginia
Region 9 - Delaware, Illinois, Indiana, Iowa, Maine, Maryland, Massachusetts, Michigan, Minnesota, Missouri, New Hampshire, New Jersey, New York, Ohio, Pennsylvania, Rhode Island, Vermont, West Virginia, and Wisconsin
Region 10 - Alaska

Stewardship Land

Stewardship land consists primarily of the national forests and grasslands owned by the Forest Service. Stewardship land is valued for its environmental resources, recreational and scenic value, cultural and paleontological resources, vast open spaces, and resource commodities and revenue provided to the Federal Government, States, and counties.

National Forests
The national forests are formally established and permanently set aside and reserved for national forest purposes. The following categories of NFS lands have been set aside for specific purposes in designated areas:

- **National Wilderness Areas** - Areas designated by Congress as part of the National Wilderness Preservation System.
- **National Primitive Areas** - Areas designated by the Chief of the Forest Service as primitive areas. They are administered in the same manner as wilderness areas, pending studies to determine sustainability as a component of the National Wilderness Preservation System.
- **National Wild and Scenic River Areas** - Areas designated by Congress as part of the National Wild and Scenic River System.
- **National Recreation Areas** - Areas established by Congress for the purpose of assuring and implementing the protection and management of public outdoor recreation opportunities.
- **National Scenic Research Areas** - Areas established by Congress to provide use and enjoyment of certain ocean headlands and to ensure protection and encourage the study of the areas for research and scientific purposes.
- **National Game Refuges and Wildlife Preserve Areas** - Areas designated by Presidential proclamation or Congress for the protection of wildlife.
- **National Monument Areas** - Areas including historic landmarks, historic and prehistoric structures, and other objects for historic or scientific interest, declared by Presidential proclamation or Congress.

National Grasslands
National grasslands are designated by the Secretary of Agriculture and permanently held by the USDA under Title III of the Bankhead-Jones Farm Tenant Act.

Research and Experimental Areas
Research and experimental areas are reserved and dedicated by the Secretary of Agriculture for forest and range research experimentation. Areas reported are located outside the exterior boundaries of a national forest or grassland.

National Preserves and Other Areas
National preserves is established to protect and preserve scientific, scenic, geologic, watershed, fish, wildlife, historic, cultural, and recreational values; and provide for multiple use and sustained yield of its renewable resources. Other areas include areas administered by the Forest Service that are not included in one of the above groups.

Addition and Deletion of Stewardship Lands

The Land and Water Conservation Fund (L&WCF) Land Acquisition Program acquires land for the Forest Service NFS. The program coordinates with a variety of partners, including State, local, and Tribal governments, and private landowners through statewide planning for development of a land-adjustment strategy.

The Land Acquisition Program preserves, develops, and maintains access to NFS lands and waters for the public and provides permanent access to public lands for recreation, commodity production, resource management, public safety, and community economic viability.

The L&WCF statutory authority specifically defines the purpose to also include protecting the quality of scientific, scenic, historical, ecological, environmental, air and atmospheric, water resource, archeological values, as well as food and habitat for fish and wildlife, and managing the public lands for minerals, food, timber and fiber.

From these several allowable uses of program funding, the program concentrates on protecting habitat for priority species identified in the national forest and grassland's Land Management Plans and enhancing recreational opportunities for areas with high demand for recreation. The program focuses acquisitions on inholdings and areas adjacent to existing NFS lands.

The NFS sites reported by major category as of September 30, 2011, are as follows:

STEWARDSHIP LAND ASSET SITES	FY 2010 Final Sites	Additions	Deletions	FY 2011 Final Sites
National Forests	155	-	-	155
National Grasslands	20	-	-	20
Research and Experiment Areas	3	-	-	3
National Preserves and Other Areas	3	-	-	3
TOTAL SITES	**181**	**-**	**-**	**181**

NOTE 7: LIABILITIES NOT COVERED BY BUDGETARY RESOURCES

Liabilities not covered by budgetary resources are liabilities for which Congressional action is needed before budgetary resources can be provided. Liabilities not covered by budgetary resources as of September 30, 2011 and 2010 consisted of the following:

	(in millions)	
	2011	2010
Intragovernmental:		
Treasury Judgment Fund	$ 20	$ 18
Other Unfunded Employment Related Liability	21	14
Federal Employee Benefits (Note 8)	73	74
Total Intragovernmental Not Covered by Budgetary Resources	114	106
Federal Employee Benefits (Note 8)	381	369
Annual Leave Liability	214	214
Contingent Liabilities (Note 10)	12	-
Accrued Liability for Payments to States	357	409
Total Liabilities Not Covered by Budgetary Resources	1,078	1,098
Total Liabilities Covered by Budgetary Resources	1,184	1,039
Total Liabilities	$ 2,262	$ 2,137

Other Unfunded Employment Related Liability consists of the Forest Service portion of the unemployment compensation unfunded liability as established in § 909 of the Social Security Act, approved, August 14, 1935.

NOTE 8: FEDERAL EMPLOYEE BENEFITS

Liabilities under the Federal Employees' Compensation Act (FECA) are incurred as a result of accrued workers' compensation benefits not yet paid by the Forest Service.

Workers' compensation benefits include the current and expected future liability for death, disability, medical, and other approved costs. The U.S. Department of Labor (DOL) actuarially determines the expected future liability for the USDA as a whole, including the Forest Service. The Forest Service is billed annually as its claims are paid by the DOL. Payments to the DOL are deferred for two years so that the bills may be funded through the budget. The amounts of unpaid FECA billings constitute the accrued FECA payable.

The total components of accrued FECA payable as of September 30, 2011 and 2010 consisted of the following:

	(in millions)	
	2011	2010
Intragovernmental Federal Employee Benefits (Note 7)	$ 73	$ 74
Federal Employee Benefits (Note 7)	381	369
Total	$ 454	$ 443

NOTE 9: ENVIRONMENTAL AND DISPOSAL LIABILITIES

Forest Service discloses information related to cleanup costs for environmental hazards, in accordance with U.S. GAAP, which addresses liabilities associated with Government-related events and Government-acknowledged events.

Government-related events are non-transaction based events that involve interaction between the Forest Service and the environment; damages caused by such factors as ongoing operations or natural forces. The resulting liability is considered probable based on Forest Service's responsibility for cleanup of Government-related events and is recognized in the period the event occurs or as soon as it becomes measurable.

Government-acknowledged events are non-transaction events that are of financial consequence to the Forest Service because it chooses to respond to the event, and the primary responsible party cannot be located. Cleanup costs associated with events such as toxic waste damage caused by non-Federal entities or natural disasters, may ultimately become the responsibility of the Forest Service. However these costs do not meet the definition of a "liability" until, and to the extent that financial responsibility is acknowledged by the Forest Service, Congress has appropriated resources, and an exchange or non-exchange transaction has occurred.

The Forest Service is subject to environmental laws and regulations regarding air, water, and land use, the storage and disposal of hazardous materials, and the operation and closure of facilities at which environmental contamination may be present. Forest Service project managers confer with the appropriate States, the Office of General Counsel (OGC), and occasionally, Environmental Protection Agency (EPA) and local governments. The agency follows cleanup requirements from the legislative sources in Appendix I of Federal Financial Accounting and Auditing, Technical Release No. 2, including the Comprehensive Environmental Response Compensation and Liability Act of 1980 (CERCLA), the Resource Conservation and Recovery Act (RCRA), other Federal or State regulations and USDA or Forest Service policy, as necessary. Estimated environmental and disposal liabilities include expected future cleanup costs, and the cost of studies necessary to evaluate response requirements for those sites where future liability is unknown.

PP&E cleanup cost estimates—usually immaterial to the total project cost for the majority of demolitions, deconstructions, or renovations—are included in PP&E operations and maintenance costs (O&M). When contamination occurs that is not addressed under regular O&M, the agency develops a cost estimate for the total cleanup and, to the extent it is probable and reasonable to estimate, records the cost to cleanup any contaminated PP&E. Professional judgment and prior experience is often the basis for cost estimates. If the agency has no previous similar experience, the staff performs other comparable technical reviews or derives estimates using standard cost estimating guides.

Exceptions occur when a *previous* activity results in release or potential release of a hazardous substance, and if contamination migrates offsite from a *current* operation. In these instances, the total reasonably estimable costs are recognized when the exception is discovered.

Forest Service cleanup cost estimates are based on the current total cost for a contaminated site according to laws, technology, and inflation/deflation. Forest Service updates cost estimates, including changes relating to prior period operations, for Government-related liabilities at least annually, to reflect changes in laws or regulations, technology, and inflation or deflation.

The Forest Service has recognized an estimated liability for government related events of $1 million for the years ended September 30, 2011 and 2010.

NOTE 10: OTHER LIABILITIES

	(in millions)					
	2011			2010		
	Non-Current	Current	Total	Non-Current	Current	Total
Intragovernmental						
Employer Contributions & Payroll Tax	$ -	36	$ 36	$ -	30	$ 30
Accrued Liabilities	20	67	87	18	43	61
Advances from Others	-	42	42	-	26	26
Deposit Liabilities	-	2	2	-	1	1
Other (Note 7)	-	21	21	-	14	14
Total Intragovernmental	$ 20	168	$ 188	$ 18	114	$ 132
Other						
Accrued Liabilities	-	782	782	-	734	734
Advances from Others	-	83	83	-	49	49
Deposit Liabilities	-	108	108	-	77	77
Purchaser Road Credits	-	1	1	-	1	1
Accrued Liability for Payments to States & Counties	-	357	357	-	409	409
Annual Leave Liability	-	214	214	-	214	214
Contingent Liabilities	-	12	12	-	-	-
Custodial Liabilities	-	1	1	-	3	3
Capital Leases (Note 11)	19	3	22	22	3	25
Other	-	3	3	-	2	2
Total Other	$ 19	1,564	$ 1,583	$ 22	1,492	$ 1,514
Total Other and Intragovernmental Liabilities	$ 39	1,732	$ 1,771	$ 40	1,606	$ 1,646

As of September 30, 2011 and 2010, the Forest Service's major components of other liabilities are as follows:

Accrued Liabilities: Accrued liabilities consist primarily of accruals for payroll and for receipt of goods and services. Accrued liabilities for occupancy agreements between U.S. General Services Administration (GSA) and the Forest Service are also included. A portion of the accrued liabilities total is calculated by a mathematical model based on a regression between open obligation balances and subsequent payments.

Accrued Liability for Payments to States and Counties: The Twenty-Five Percent Fund Act of May 23, 1908, as amended (16 U.S.C. 500), authorized the Payments to States Program. This program requires revenue generated by the sale of goods and services on the national forests to be shared with the States for public schools and public roads in the county or counties in which the national forests are located. The Secure Rural School and Community Self Determination Act of 2000, (P.L. 106-393) as amended by § 601 of The Emergency Economic Stabilization Act of 2008, (H.R. 1424) (P.L. 110-343) also provides for roads and schools, Forest Service projects and emergency services. Legislation mandates a declining scale in payment calculation of approximately 90 percent of the full funding amount for the preceding fiscal year. In addition, the Payments to Counties, Bankhead-Jones Farm Tenant Act of 1937 requires 25 percent of the net revenues from each national grassland or land utilization project to be paid to the counties in which such lands are located.

Annual Leave Liability: Annual and other vested leave such as compensatory, credit hours, and restored leave is accrued as it is earned, and the accrual is reduced as leave is taken. Each quarter, the balance in the accrued

annual leave account is adjusted to reflect the latest pay rates and unused hours of leave. Funding will be obtained from future financing sources to the extent that current or prior year appropriations are not available to fund annual and other types of vested leave earned but not taken.

Contingent Liabilities and Commitments: As of September 30, 2011 the Forest Service contingent liabilities and commitments increased by $12 million from cases that are now reported as probable (Refer to Note 1I) from OGC. Based on information provided by legal counsel, management accrues liabilities for some adverse actions determined to be probable in occurrence and reasonably estimable. The Forest Service discloses potential liabilities related to claims where the probability of occurrence is at least reasonably possible. There are no estimated obligations related to cancelled appropriations for which there is a contractual commitment for payment. In addition, there are no contractual arrangements which may require future financial obligations.

The accrued and potential contingent liabilities as of September 30, 2011 and 2010 are summarized as follows:

(in millions)

FY 2011		**Estimated Range of Loss**	
(in millions)	**Accrued Liabilities**	**Lower End**	**Upper End**
Contingent Liabilities			
Probable	$ 12	$ 12	$ 199
Reasonably Possible		$ 33	$ 125

FY 2010		**Estimated Range of Loss**	
(in millions)	**Accrued Liabilities**	**Lower End**	**Upper End**
Contingent Liabilities			
Probable	$ -	$ -	$ 17
Reasonably Possible		$ 1	$ 198

NOTE 11: LEASE LIABILITIES

The Forest Service enters into leasing agreements through leasing authority delegated by GSA for general facilities (buildings and office space), equipment, and land. Leases may include renewal options for periods of one or more years. Most leases are subject to cancellation upon certain funding conditions. The Forest Service's assets under capital leases as of September 30, 2011 and 2010 and future capital and operating lease agreement payments as of September 30, 2011 consisted of the following:

	(in millions)	
Capital Leases:	**2011**	**2010**
Summary of Assets Under Capital Leases		
Land, Buildings, Machinery, and Equipment	$ 61	$ 61
Accumulated Amortization	(39)	(36)
Total	$ 22	$ 25

Future Payments Due:

		Land & Buildings, Machinery, and Equipment
	Year 1 (2012)	9
	Year 2 (2013)	9
	Year 3 (2014)	8
	Year 4 (2015)	8
	Year 5 (2016)	7
	After 5 Years	26
Total Future Lease Payments		$ 67
Less: Imputed Interest		(33)
Less: Executory Costs		(12)
Subtotal		22
Lease Liabilities Covered by Budgetary Resources		$ 22

Operating Leases:		(in millions)
Future Payments Due:		
	Fiscal Year	Land & Buildings, Machinery, and Equipment
	Year 1 (2012)	$ 48
	Year 2 (2013)	40
	Year 3 (2014)	35
	Year 4 (2015)	31
	Year 5 (2016)	27
	After 5 Years	155
Total Future Lease Payments		$ 336

NOTE 12: EARMARKED FUNDS

In accordance with U.S. GAAP, the Forest Service administers certain earmarked funds, which are specifically identified revenues, often supplemented by other financing sources that remain available over time. These funds predominately finance the enhancement and maintenance of NFS lands, including reforestation. Donations are handled on a cash basis and all other collections are accounted for on an accrual basis. The following is a list of earmarked funds and their base Treasury symbols for which the Forest Service has program management responsibility. Those with an asterisk are authorized by specific legislative acts as permanent indefinite appropriations.

Treasury Account Symbols and Titles

5004 Land Acquisition
5008 National Forest Fund Receipts
5010 Recreation Fees for Collection Costs
5072 Fees, Operation and Maintenance of Recreation Facilities
5201 Payments to States, National Forest Fund
*5202 Timber Roads Purchaser Election
*5203 Roads and Trails for States, National Forest Funds
*5204 Timber Salvage Sales
*5206 Expenses, Brush Disposal
5207 Range Betterment Fund
5208 Acquisition of Lands for National Forests, Special Acts
5212 Construction of Facilities or Land Acquisition
*5213 Payments to Minnesota (Cook, Lake and St. Louis Counties), National Forest Funds
*5214 Licensee Program
*5215 Restoration of Forest Lands and Improvements
5216 Acquisition of Lands to Complete Land Exchanges (Funds EXSL and EXSC)
5217 Tongass Timber Supply Fund
*5219 Operation and Maintenance of Quarters
*5220 Resource Management Timber Receipts
*5223 Quinault Special Management Area
*5264 Timber Sales Pipeline Restoration Fund
*5268 Recreation Fee Demonstration Program
*5277 MNP Rental Fee Account
*5278 Midewin National Tallgrass Prairie Restoration Fund
*5360 Land Between the Lakes Management Fund
*5361 Administration of Rights-of-Way and Other Land Uses Fund
*5363 Valles Caldera Fund
5367 State, Private and International Forestry Land and Water Conservation Fund
*5462 Hardwood Technology Transfer and Applied Research Fund
*5540 Stewardship Contracting Product Sales, Funds Retained
*5896 Payments to Counties, National Grasslands
*8028 Cooperative Work, Forest Service
8029 Mount Saint Helens Highway
8034 Gifts, Donations, and Bequests for Forest and Rangeland Research
8039 Land Between the Lakes Trust Fund
8046 Reforestation Trust Fund
*8203 Gifts and Bequests, Department of Agriculture

Financial information for all earmarked funds is included, and significant funds are specifically identified as shown below:

Earmarked Funds
As of and for the year ended September 30, 2011
(in millions)

	Cooperative Work	Payments to States National Forests Fund	Restoration of Forest Lands and Improvements	State, Private, & International Forestry Land & Water Conservation Fund	Other Funds	Total
ASSETS						
Fund Balance with Treasury	$ 376	$ 206	$ 170	$ 123	$ 487	$ 1,362
Investments	-	-	-	-	-	-
Accounts Receivable, Net	2	-	2	-	13	17
Advances To Others	-	1	-	-	-	1
General Property, Plant & Equipment, Net	16	3	-	-	99	118
TOTAL ASSETS	$ 394	$ 210	$ 172	$ 123	$ 599	$ 1,498
LIABILITIES						
Accounts Payable	$ 1	$ 1	$ -	$ -	$ 2	$ 4
Other Liabilities	80	332	2	29	49	492
TOTAL LIABILITIES	81	333	2	29	51	496
Total Net Position	313	(123)	170	94	548	1,002
TOTAL LIABILITIES AND NET POSITION	$ 394	$ 210	$ 172	$ 123	$ 599	$ 1,498
CHANGE IN NET POSITION						
Beginning Balances, as adjusted	$ 326	$ (191)	$ 170	$ 83	$ 545	$ 933
Budgetary Financing Sources:						
Donations and Forfeitures of Cash	-	-	-	-	1	1
Transfers -in/out without Reimbursemer	-	-	-	53	63	116
Other Financing Sources:						
Transfers-in/out without Reimbursemen	-	-	-	-	(68)	(68)
Other	-	-	-	-	66	66
Total Financing Sources	-	-	-	53	62	115
Revenue	88	116	19	-	212	435
Expenses	(101)	(48)	(19)	(42)	(271)	(481)
Net Cost of Operations	(13)	68	-	(42)	(59)	(46)
ENDING BALANCES	$ 313	$ (123)	$ 170	$ 94	$ 548	$ 1,002

Earmarked Funds
As of and for the year ended September 30, 2010
(in millions)

	Cooperative Work	Payments to States National Forest Fund	Restoration of Forest Lands and Improvements	State, Private, & International Forestry Land & Water Conservation Fund	Recreation Fee Demonstration Program	Other Funds	Total
ASSETS							
Fund Balance with Treasury	$ 357	$ 197	$ 169	$ 124	$ 98	$ 372	$ 1,317
Investments	-	-	-	-	-	6	6
Accounts Receivable, Net	2	-	2	-	1	11	16
Advances To Others	-	1	-	9	-	-	10
General Property, Plant & Equipment, Net	19	2	-	-	3	97	121
TOTAL ASSETS	$ 378	$ 200	$ 171	$ 133	$ 102	$ 486	$ 1,470
LIABILITIES							
Accounts Payable	$ 2	$ -	$ -	$ -	$ 1	$ 2	$ 5
Other Liabilities	50	391	1	50	4	36	532
TOTAL LIABILITIES	52	391	1	50	5	38	537
Total Net Position	326	(191)	170	83	97	448	933
TOTAL LIABILITIES AND NET POSITION	$ 378	$ 200	$ 171	$ 133	$ 102	$ 486	$ 1,470
CHANGE IN NET POSITION							
Beginning Balances, as adjusted	$ 359	$ (272)	$ 175	$ 80	$ 128	$ 437	$ 907
Budgetary Financing Sources:							
Donations and Forfeitures of Cash	1	-	-	-	-	-	1
Transfers -in/out without Reimbursement	-	-	-	76	-	94	170
Other Financing Sources:							
Transfers-in/out without Reimbursement	(1)	-	-	-	-	(59)	(60)
Other	-	-	-	-	-	43	43
Total Financing Sources	-	-	-	76	-	78	154
Revenue	79	118	33	-	65	120	415
Expenses	(112)	(37)	(38)	(73)	(96)	(187)	(543)
Net Cost of Operations	(33)	81	(5)	(73)	(31)	(67)	(128)
ENDING BALANCES	$ 326	$ (191)	$ 170	$ 83	$ 97	$ 448	$ 933

Descriptions of the significant earmarked funds are as follows:

Cooperative Work
Cooperative contributions are deposited into Treasury account 12X8028 for disbursement in compliance with the terms and provisions of the agreement between the cooperator and the Forest Service. Cooperators include timber purchasers, not-for-profit organizations, and local hunting and fishing clubs. The governing authorities are the Cooperative Funds Act of June 30, 1914 (16 U.S.C. 498), and the Knutson-Vandenberg Act.

Payments to States, National Forests Fund
The Act of May 23, 1908, as amended (16 U.S.C. 500), commonly known as “Payments to States”, requires with a few exceptions, that 25 percent of all monies received from the national forests and deposited into the National Forest Fund (Treasury Symbol 125008) during a fiscal year from timber, grazing, special-use permits, power and mineral leases, and admission and user fees be paid to the States in which the national forests are located, for public schools and public roads in the county or counties in which the national forests are situated. The Secure

Rural Schools and Community Self-Determination Act of 2000 (P.L. 106-393) as amended by § 601 of The Emergency Economic Stabilization Act of 2008, (H.R. 1424) (P.L. 110-343), provides stabilized education and road maintenance funding through predictable payments to counties, job creation in those counties, and other opportunities associated with the restoration, maintenance, and stewardship of Federal lands.

Restoration of Forest Lands and Improvements
The Restoration of Forest Lands and Improvements Acts (16 U.S.C. 579c) states any monies received by the United States with respect to lands under the administration of the Forest Service (a) as a result of the forfeiture of a bond or deposit by a permittee or timber purchaser for failure to complete performance of improvement, protection, or rehabilitation work required under the permit or timber sale contract or (b) as a result of a judgment, compromise, or settlement of any claim, involving present or potential damage to lands or improvements, shall be deposited into the Restoration of Forest Lands and Improvements Account – 12X5215 and made available until expended to cover the cost of any improvement, protection, or rehabilitation work on lands under the administration of the Forest Service rendered necessary by the action which led to the forfeiture, judgment, compromise, or settlement, provided that any portion of the monies so received in excess of the amount expended in performing the work necessitated by the action which led to their receipt shall be transferred to miscellaneous receipts.

State, Private, and International Forestry, Land and Water Conservation Fund
The Fiscal Year 2004 Department of Interior and Related Agencies Appropriation Act (Public Law 108-108) authorizes the Forest Service to receive a transfer of receipts from Department of Interior's Land and Water Conservation Fund to finance the existing Forest Legacy Program, funded previously by State and Private Forestry general appropriation, 12X1105. To accommodate the new financing arrangement and at OMB's request, the Department of Treasury established a new special fund, 12X5367, "State, Private and International Forestry Land and Water Conservation Fund". The program expenditures include grants and an occasional land purchase but no real property will be procured or constructed.

Recreation Fee Demonstration Program
The Recreation Fee Demonstration Program Treasury account 12X5268 receives deposits of recreation fees collected from projects that are part of the Recreation Fee Demonstration program. These monies are retained and used for backlog repair and maintenance of recreation areas, sites or projects. These funds are also used for interpretation, signage, habitat or facility enhancement, resource preservation, annual operation, maintenance, and law enforcement related to public use of recreation areas and sites. The Recreation Fee Demonstration Program is authorized by § 315 of Title III General Provisions of Public Law 104-134: Recreation Fee Demonstration Program 16 U.S.C. 4601-6a.

NOTE 13: SUBORGANIZATION PROGRAM COSTS/PROGRAM COSTS BY SEGMENT

The Forest Service reflects costs through four primary responsibility segments: National Forests and Grasslands, Forest and Rangeland Research, State and Private Forestry, and Wildland Fire Management. National Forests and Grasslands is a principle contributor to accomplishing Forest Service Strategic Goals 2, 4, and 5; Forest and Rangeland Research is a principle contributor to accomplishing Goal 7; State and Private Forestry is a principle contributor to accomplishing Goals 3 and 6; and Wildland Fire Management is a principle contributor to accomplishing Goal 1.

The following tables illustrate program costs by segment for the years ended September 30, 2011 and 2010.

Program Costs by Segment
For the year ended September 30, 2011
(in millions)

	National Forests and Grasslands	Forest and Rangeland Research	State and Private Forestry	Wildland Fire Management	Total
Intragovernmental Gross Costs:					
Benefit Program Costs	$ 345	$ 43	$ 15	$ 240	$ 643
Imputed Costs	425	-	-	-	425
Reimbursable Costs	146	19	13	194	372
Total Intragovernmental Gross Costs	916	62	28	434	1,440
Less: Intragovernmental Earned Revenue	53	19	42	9	123
Intragovernmental Net Costs	863	43	(14)	425	1,317
Gross Costs With the Public:					
Grants and Indemnities	381	10	233	162	786
Stewardship Land Acquisition (Note 14)	44	-	-	-	44
Other:					
Operating Costs	1,988	255	104	1,929	4,276
Depreciation Expense	119	2	-	24	145
Reimbursable Costs	155	21	25	268	469
Total Other	2,262	278	129	2,221	4,890
Total Gross Costs with the Public	2,687	288	362	2,383	5,720
Less: Earned Revenues from the Public	503	4	-	203	710
Net Costs with the Public	2,184	284	362	2,180	5,010
Net Cost of Operations	$ 3,047	$ 327	$ 348	$ 2,605	$ 6,327

Program Costs by Segment
For the year ended September 30, 2010
(in millions)

	National Forests and Grasslands	Forest and Rangeland Research	State and Private Forestry	Wildland Fire Management	Total
Intragovernmental Gross Costs:					
Benefit Program Costs	$ 305	$ 42	$ 15	$ 224	$ 586
Imputed Costs	426	-	-	-	426
Reimbursable Costs	147	19	12	135	313
Total Intragovernmental Gross Costs	878	61	27	359	1,325
Less: Intragovernmental Earned Revenue	77	28	28	(1)	132
Intragovernmental Net Costs	801	33	(1)	360	1,193
Gross Costs With the Public:					
Grants and Indemnities	421	16	287	75	799
Stewardship Land Acquisition (Note 14)	57	-	-	-	57
Other:					
Operating Costs	2,185	259	117	1,513	4,074
Depreciation Expense	118	2	-	28	148
Reimbursable Costs	149	30	17	103	299
Total Other	2,452	291	134	1,644	4,521
Total Gross Costs with the Public	2,930	307	421	1,719	5,377
Less: Earned Revenues from the Public	448	4	-	39	491
Net Costs with the Public	2,482	303	421	1,680	4,886
Net Cost of Operations	$ 3,283	$ 336	$ 420	$ 2,040	$ 6,079

NOTE 14: COST OF STEWARDSHIP PP&E

Stewardship PP&E acquired in FYs 2011 and 2010 amounted to $44 and $57 million, respectively. Cost of Stewardship PP&E includes purchases of lands, easements, and rights-of-way. Stewardship land is land and land rights owned by the Federal Government and are excluded from General PP&E. Examples of stewardship land includes land used for forests, grazing, and wildlife.

Costs for stewardship land include all costs to acquire and prepare the land for its intended use. The acquired land was adjacent to existing forest/grassland sites, thus the number of sites reported in Note 6 remains unchanged.

NOTE 15: APPORTIONMENT CATEGORIES OF OBLIGATIONS INCURRED

The Office of Management and Budget (OMB) usually distributes budgetary resources in an account or fund by specific time periods, activities, projects, objects or a combination of these categories by a process called apportionments. Apportionments by fiscal quarters are classified as category A and all other apportionments are classified as category B. The funds on quarterly apportionment are National Forest System (12X1106) and Wildland Fire Management (12X1115). Presented below are the amounts of direct and reimbursable obligations incurred by apportionment category for FY 2011 and 2010.

For the year ended September 30, 2011
(in millions)

	Apportionment Category A	Apportionment Category B	Total
Obligations Incurred - Direct	$ 4,014	$ 2,050	$ 6,064
Obligations Incurred - Reimbursable	260	354	614
Total Obligations Incurred	**$ 4,274**	**$ 2,404**	**$ 6,678**

For the year ended September 30, 2010
(in millions)

	Apportionment Category A	Apportionment Category B	Total
Obligations Incurred - Direct	$ 3,537	$ 3,034	$ 6,571
Obligations Incurred - Reimbursable	93	316	409
Total Obligations Incurred	**$ 3,630**	**$ 3,350**	**$ 6,980**

NOTE 16: EXPLANATION OF DIFFERENCES BETWEEN THE STATEMENT OF BUDGETARY RESOURCES AND THE BUDGET OF THE UNITED STATES GOVERNMENT

The differences between the FY 2010 Statement of Budgetary Resources (SBR) and the FY 2010 actual numbers presented in the FY 2012 Budget of the United States Government (Budget) are summarized in the table below. The President's Budget with actual numbers for 2011 has not yet been published, and is expected to be published in February of 2012, and to be made available at www.whitehouse.gov. OMB Circular A-136 states that the note should "identify and explain material differences between amounts reported in the SBR and actual amounts reported in the Budget of the United States Government as required by U.S. GAAP." The Department's threshold for explaining material variances is $25 million and 10%. No variances meet this threshold.

	(in millions)			
SBR Line Description	SBR Amount	Budget Amount	Dollar Variance	Percentage Variance
Total Budgetary Resources/Status of Resources	9,339	9,334	5	0%
Total Status of Resources	9,339	9,334	5	0%
Unobligated Balance-Beginning of Year	2,745	2,741	4	0%
Recoveries of Prior Year Obligations	40	41	(1)	-2%
New Budget Authority	6,094	6,094	-	0%
Spending Authority from Offsetting Collections	461	460	1	0%
Non Expenditure Transfers	(1)	(2)	1	-50%
Total New Obligations	6,980	6,980	-	0%
Unobligated Balance & Unobligated Balance not Available	2,359	2,354	5	0%
Obligated Balance - Beginning of Year	2,290	2,290	-	0%
Obligated Balance - End of Year	2,762	2,763	(1)	0%
Gross Outlays	6,509	6,508	1	0%
Less: Offsetting Collections	(503)	(502)	(1)	0%
Less: Distributed Offsetting Receipts	(429)	(426)	(3)	-1%
Net Outlays	5,577	6,006	(429)	-7%

NOTE 17: UNDELIVERED ORDERS AT THE END OF THE PERIOD

Undelivered orders included in unpaid obligations as of September 30, 2011 and 2010 were as follows:

	(in millions)	
	2011	2010
Unpaid Obligations	2,771	3,072
Undelivered Orders	1,860	2,243

NOTE 18: SEIZED PROPERTY

A seizure is the act of taking possession of goods in consequence of a violation of public law. Seized property may consist of monetary instruments, real property, tangible personal property and evidence. Until judicially or administratively forfeited, the Forest Service does not legally own such property. Seized evidence includes cash, weapons, illegal drugs and non-monetary valuables.

Pursuant to Federal Financial Accounting and Auditing Technical Release No. 4, *Reporting on Non-Valued Seized and Forfeited Property* (Release No. 4), property that is seized but not forfeited (e.g., weapons, chemicals, drug paraphernalia, gambling devices) is not included on the balance sheet.

The Forest Service has custody of illegal drugs and weapons seized as evidence for legal proceedings. Illegal drugs and weapons have no saleable value to the Federal Government and are destroyed upon resolution of legal proceedings. Marijuana represents the most significant seized drug for the Forest Service. As of September 30, 2011 and 2010, the amount of marijuana on hand was 28,205 (kg) and 32,046 (kg), respectively. Since the amount of seized property is deemed to be immaterial, a schedule of brought forward balances, additions, deletions and adjustments is not presented.

NOTE 19: RECONCILIATION OF NET COST OF OPERATIONS (PROPRIETARY) TO BUDGET (FORMERLY THE STATEMENT OF FINANCING)

	(in millions)	
	2011	2010
Resources Used to Finance Activities:		
Budgetary Resources Obligated:		
Obligations Incurred	$ 6,678	$ 6,980
Less: Spending Authority from Offsetting Collections and Recoveries	814	501
Obligations Net of Offsetting Collections and Recoveries	5,864	6,479
Less: Offsetting Receipts	467	429
Net Obligations	5,397	6,050
Other Resources:		
Transfers in/out Without Reimbursement	-	3
Imputed Financing from Costs Absorbed by Others	425	426
Other	(2)	(15)
Net Other Resources Used to Finance Activities	423	414
Total resources used to finance activities	**5,820**	**6,464**
Resources Used to Finance Items not Part of the Net Cost of Operations:		
Change in Budgetary Resources Obligated for Goods, Services, and Benefits Ordered But not Yet Provided	380	(421)
Resources that Fund Expenses Recognized in Prior Periods	(20)	(27)
Budgetary Offsetting Collections and Receipts that do not Affect Net Cost of Operations		
Change in Unfilled Orders	89	16
Other	(1)	-
Resources that Finance the Acquisition of Assets	(184)	(163)
Other Resources or Adjustments to Net Obligated Resources that do not Affect the Net Cost of Operations	66	60
Total Resources Used to Finance Items not Part of the Net Cost of Operations	330	(535)
Total Resources Used to Finance the Net Cost of Operations	**6,150**	**5,929**
Components of the Net Cost of Operations that will not Require or Generate Resources in the Current Period:		
Components Requiring or Generating Resources in Future Periods:		
Increase in Annual Leave Liability	-	8
Increase in Exchange Revenue Receivable from the Public	(7)	(3)
Total Components of Net Cost of Operations that will Require or Generate Resources in Future Periods	(7)	5
Components not Requiring or Generating Resources:		
Depreciation and Amortization	145	148
Revaluation of Assets or Liabilities	34	2
Other Components not Requiring or Generating Resources:		
Bad Debt Expense	6	(1)
Other	(1)	(4)
Total Components of Net Cost of Operations that will not Require or Generate Resources	184	145
Total Components of Net Cost of Operations that will not Require or Generate Resources in the Current Period	177	150
Net Cost of Operations	**$ 6,327**	**$ 6,079**

This note is intended to be a bridge between the entity's budgetary and financial (proprietary) accounting. This reconciliation first identifies total resources used by an entity during the period (budgetary and other) and then makes adjustments to the resources based upon how they were used to finance net obligations or cost. The budgetary information used to calculate net obligations (the first four lines) must be presented on a combined basis to enable a direct tie to the Statement of Budgetary Resources. The reconciliation then explains the difference between the budgetary net obligations and the proprietary net cost of operations by setting forth the items that reconcile the two amounts. The budgetary net obligations and the proprietary net cost of operations are different in that (1) the net cost of operations may be financed by non-budgetary resources; (2) the budgetary and non-budgetary resources used by an agency may finance activities which are not components of the net cost of operations; and (3) the net cost of operations may contain components which do not use or generate resources in the period.