


BROWN & COMPANY CPAs, PLLC

CERTIFIED PUBLIC ACCOUNTANTS AND MANAGEMENT CONSULTANTS

INDEPENDENT AUDITOR'S REPORT ON FINANCIAL STATEMENTS

The Director
VA Enterprise Fund Office

We have audited the accompanying consolidated balance sheet of the Department of Veterans Affairs (VA) Franchise Fund as of September 30, 2006 and 2005, and the related consolidated statements of net cost, changes in net position, financing, and the combined statements of budgetary resources for the years then ended September 30, 2006 and 2005. These financial statements are the responsibility of the VA Franchise Fund's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in U.S. Government Auditing Standards, issued by the Comptroller General of the United States; and, Office of Management and Budget (OMB) Bulletin No. 06-03, *Audit Requirement for Federal Financial Statements, as amended*. Those standards and OMB Bulletin No. 06-03 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 audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the VA Franchise Fund as of September 30, 2006 and 2005, and its net costs, changes in net position, budgetary resources, and financing for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with U.S. Government Auditing Standards and OMB Bulletin No. 06-03, as amended, we have also issued a report dated November 17, 2006 on our consideration of the VA Franchise Fund's internal control over financial reporting and its compliance with provisions of laws and regulations. Those reports are an integral part of an audit performed in accordance with U.S. Government Auditing Standards and should be read in conjunction with this report in considering the results of our audit.

The information in "Management's Discussion and Analysis" is presented for the purpose of additional analysis and is required by OMB Circular No A-136, revised *Financial Reporting Requirements*. We have applied certain limited procedures, which consisted principally of inquiries of management, regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and, accordingly, express no opinion on it.

Largo, Maryland
November 17, 2006

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INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

The Director
VA Enterprise Fund Office

We have audited the financial statements of the Department of Veterans Affairs (VA) Franchise Fund as of and for the year ended September 30, 2006, and have issued our report thereon dated November 17, 2006. We conducted our audit in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in U.S. Government Auditing Standards, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 06-03, *Audit Requirements for Federal Financial Statements*.

In planning and performing our audit, we considered the VA Franchise Fund's internal control over financial reporting by obtaining an understanding of the VA Franchise Fund's internal control, determined whether internal controls had been placed in operation, assessed control risk, and performed tests of controls in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements. We limited our internal control testing to those controls necessary to achieve the objectives described in OMB Bulletin No. 06-03. We did not test all internal controls relevant to operating objectives as broadly defined by the Federal Managers' Financial Integrity Act of 1982, such as those controls relevant to ensuring efficient operations. The objective of our audit was not to provide an opinion on internal control and therefore, we do not express an opinion on internal control.

Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be reportable conditions. Under standards issued by the American Institute of Certified Public Accountants and OMB Bulletin No. 06-03, reportable conditions are matters coming to our attention that, in our judgment, should be communicated because they represent significant deficiencies in the design or operation of the internal control, which could adversely affect the VA Franchise Fund's ability to meet the objectives of internal control. Material weaknesses are reportable conditions in which the design or operation of the internal control does not reduce to a relatively low level the risk that errors, fraud or noncompliance in amounts that would be material in relation to the financial statements being audited, or material to a performance measure or aggregation of related performance measures, may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Because of inherent limitations in internal controls, misstatements, losses, or non-compliance may nevertheless occur and not be detected. However, we noted no matters involving the internal control and its operation that are considered to be reportable conditions or material weaknesses, except as stated in the following paragraphs.

In Fiscal Year (FY) 2006, the Department of Veterans Affairs (VA) Office of Inspector General (OIG) engaged an independent public accounting firm to perform the audit of VA's consolidated financial statements for the years ending 2006 and 2005. The VA's consolidated financial statements include the Franchise Fund. The accounting firm issued the *Independent Auditor's Report* and *Independent Auditors' Report on Internal Control over Financial Reporting and Compliance and Other Matters Based Upon the Audit Performed in Accordance with Government Auditing Standards* dated November 15, 2006, and identified three reportable conditions that include significant departures from certain requirements of OMB Circular A-127, Circular A-123, and Circular A-130: (1) Information Technology (IT) Security Controls – Material Weakness (Repeat Condition), (2) Integrated Financial Management System – Material Weakness (Repeat Condition); and (3) Operational Oversight – Material Weakness (Repeat Condition).

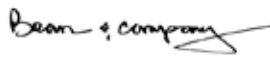
During the course of our audit we noted other matters involving internal control and its operation that we have reported to management of the VA Franchise Fund in a separate management letter dated December 1, 2006.

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In addition, with respect to internal control objective related to the performance measures included in the "Management's Discussion & Analysis," we obtained an understanding of the design of internal controls relating to the existence and completeness assertions, and determined whether they have been placed in operation as required by OMB Bulletin No. 06-03. Our procedures were not designed to provide an opinion on internal control over reported performance measures, and accordingly, we do not express an opinion on such controls.

This report is intended solely for the information and use of the management of the Department of Veterans Affairs Franchise Fund, the VA OIG, OMB, and Congress, and is not intended to be and should not be used by anyone other than these specified parties.



Largo, Maryland
November 17, 2006

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INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH LAWS AND REGULATIONS

The Director
VA Enterprise Fund Office

We have audited the consolidated financial statements of the Department of Veterans Affairs (VA) Franchise Fund as of and for the year ended September 30, 2006, and have issued our report thereon dated November 17, 2006. We conducted our audit in accordance with auditing standards generally accepted in the United States of America, and the standards applicable to financial audits contained in U.S. Government Auditing Standards, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 06-03, *Audit Requirements for Federal Financial Statement*.

The management of the VA Franchise Fund is responsible for complying with laws and regulations applicable to the VA Franchise Fund. As part of obtaining reasonable assurance about whether the VA Franchise Fund's financial statements are free of material misstatement, we performed tests of its 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. 06-03, including the requirements referred to in the Federal Financial Management Improvement Act (FFMIA) of 1996. We limited our tests of compliance to these provisions and we did not test compliance with all laws and regulations applicable to the VA Franchise Fund.

The results of our tests of compliance disclosed no instances of noncompliance with other laws and regulations discussed in the preceding paragraph exclusive of FFMIA that are required to be reported under U.S. Government Auditing Standards or OMB Bulletin No. 06-03.

Under FFMIA, we are required to report whether the VA Franchise Fund's financial management systems substantially comply with the Federal financial management systems requirements, applicable Federal accounting standards, and the United States Government Standard General Ledger at the transaction level. To meet this requirement, we performed tests of compliance with FFMIA section 803(a) requirements. The results of our tests disclosed no reportable instances in which the VA Franchise Fund financial management systems did not substantially comply with the three requirements.

However, in Fiscal Year (FY) 2006, the Department of Veterans Affairs (VA) Office of Inspector General (OIG) engaged an independent public accounting firm to perform the audit of VA's consolidated financial statements for the years ending 2006 and 2005. The VA's consolidated financial statements include the Franchise Fund. The accounting firm issued the *Independent Auditor's Report and Independent Auditors' Report on Internal Control over Financial Reporting and Compliance and Other Matters Based Upon the Audit Performed in Accordance with Government Auditing Standards* dated November 15, 2006, and identified three reportable conditions that include significant departures from certain requirements of OMB Circular A-127, Circular A-123, and Circular A-130: (1) Information Technology (IT) Security Controls – Material Weakness (Repeat Condition), (2) Integrated Financial Management System – Material Weakness (Repeat Condition); and (3) Operational Oversight – Material Weakness (Repeat Condition). These material weaknesses in internal control over financial reporting indicate that VA's financial management systems did not substantially comply with the Federal financial management systems requirements as required by FFMIA section 803(a).

Providing an opinion on compliance with certain provisions of laws and regulations was not an objective of our audit, and, accordingly, we do not express such an opinion.

This report is intended solely for the information and use of the management of the Department of Veterans Affairs Franchise Fund, the VA OIG, OMB, and Congress and is not intended to be and should not be used by anyone other than these specified parties.

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