FY 2018

DELIVERING
REMARKABLE VALUE
AND EXCEPTIONAL
SERVICES TO OUR
FEDERAL CUSTOMERS

DEPARTMENT OF VETERANS AFFAIRS

FRANCHISE FUND
ANNUAL REPORT

DEPARTMENT OF VETERANS AFFAIRS
FRANCHISE FUND FY 2018 ANNUAL REPORT

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VA's Mission

To fulfill President Lincoln's promise — "To care for him who shall have borne the battle, and for his widow, and his orphan"—by serving and honoring the men and women who are America's Veterans.

VA Franchise Fund's Mission

To deliver best-in-class services and capabilities to VA's Administrations and Staff Offices so that they can focus on delivering world-class benefits and services to Veterans and eligible beneficiaries.

VA Franchise Fund's Vision

To transform enterprise transactional services and capabilities to best-in-class levels, enabling VA to focus on improving the Veterans' experience and empower VA employees.

VA Franchise Fund's Values

To guide us in fulfilling our mission, our employees strive to uphold core values that are consistent and closely aligned with those of VA. These values include integrity, commitment, advocacy, respect, and excellence.

"To care for him who shall have borne the battle, and for his widow, and his orphan."

VA CORE VALUES

Integrity

Act with high moral principle. Adhere to the highest professional standards. Maintain the trust and confidence of all with whom I engage.

Commitment

Work diligently to serve Veterans and other beneficiaries. Be driven by an earnest belief in VA's mission. Fulfill my individual responsibilities and organizational responsibilities.

Advocacy

Be truly Veteran-centric by identifying, fully considering, and appropriately advancing the interests of Veterans and other beneficiaries.

Respect

Treat all those I serve and with whom I work with dignity and respect. Show respect to earn it.

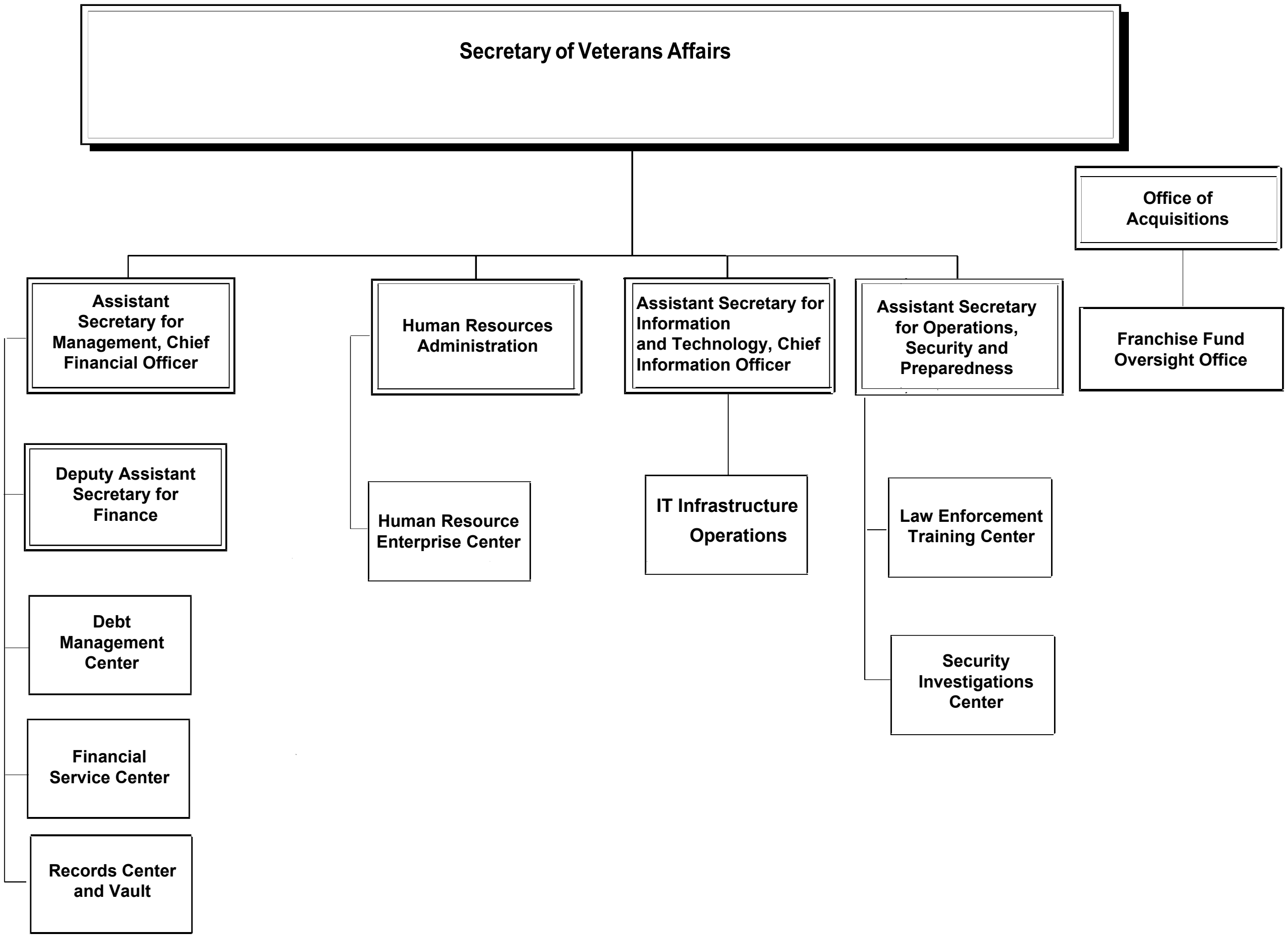
Excellence

Strive for the highest quality and continuous improvement. Be thoughtful and decisive in leadership, accountable for my actions, willing to admit mistakes, and rigorous in correcting them.

MEMBERS OF THE VA FRANCHISE FUND NETWORK

Origin of the VA Franchise Fund

The VA Franchise Fund was established under the authority of the Government Management Reform Act of 1994 and the VA and Housing and Urban Development and Independent Agencies Appropriations Act of 1997. VA was selected by the Office of Management and Budget (OMB) in 1996 as one of six Executive branch agencies to establish a franchise fund pilot program. Created as a revolving fund, the VA Franchise Fund began providing common administrative support services to VA and other government agencies in 1997 on a fee-for-service basis. In 2006, under the Military Quality of Life and Veterans Affairs Appropriations Act, Public Law 109-114, permanent status was conferred upon the VA Franchise Fund.



Organizational Structure

The VA Franchise Fund consists of an administrative office (Franchise Fund Oversight Office) and seven self-supporting lines of business (Enterprise Centers). The Revolving Fund Chief Financial Officer along with the Directors of the individual Enterprise Centers and their staffs are responsible for customer liaison and coordination, business planning and development, staffing, and execution of day-to-day business activities consistent with their annual business plans. The Support Services Governance Board (SSGB) was subsumed by the Revolving Fund Board (RFB) in March 2018 and is composed of representatives from the five VA organizations that manage the Enterprise Centers (the Office of Management; the Office of Human Resources; the Office of Operations, Security, and Preparedness; Office of Acquisitions and the Office of Information and Technology), major organizations within VA, Veterans Health Administration (VHA), Veterans Benefits Administration (VBA), and National Cemetery Administration (NCA), and pertinent VA staff offices.

Members of the VA Franchise Fund Network

Entrepreneurial Network

We are one of the leading fee-for-service operations in government. By employing people nationwide to execute our day-to-day business activities, we provide our customers with services that save resources and allow them to concentrate on mission-critical functions within their organizations. We have positioned ourselves to meet the needs of any Federal agency at competitive prices.

Business Segments

The VA Franchise Fund consists of four major segments: Information Technology (IT), Financial Management (FM), Personnel Security and Law Enforcement (PS&LE) and Enterprise Support Services (ESS). The chart below shows the revenue among our segments for FY 2016 through FY 2018.

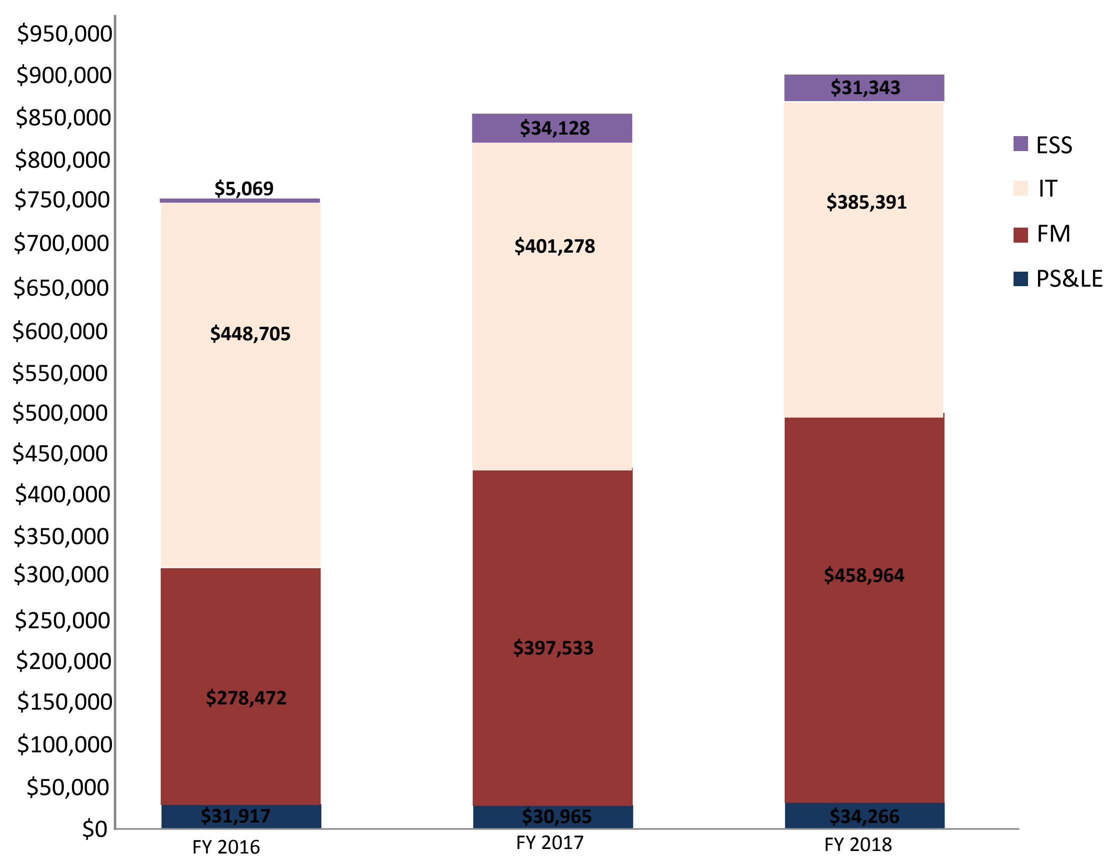
The IT segment generated $385 million in revenue in FY 2018, which is a notable decrease from $401 million in FY 2017. This decrease was due to an overall reduction in business volume. The FM segment generated $459 million in FY 2018, which is a significant increase from $397 million in FY2017.

The PS&LE segment ended FY 2018 with over $34 million in revenue which is a slight increase from the $31 million in revenue reported at the end of FY 2017.

The ESS segment ended FY 2018 with $31 million in revenue. This is a slight decrease from $34 million in revenue reported during FY 2017.

During FY 2018, the ESS Segment was dissolved due to the disestablishment of Office of Enterprise Support Services. Consequently, HREC was reorganized under the Human Resource Administration (HRA). FY 2019 reporting will reflect this reorganization which will present HREC under the new HR segment. RCV, which was also part of the now dissolved ESS segment, will henceforth be presented under the FM segment.

VA Franchise Fund
Revenue Trend by Major Segments (Dollars in Thousands)



Financial Management (FM)

Financial Services Center (Austin, TX)

- Financial Reports and Accounting
- Construction Accounting
- Credit Card Payments
- Vendor File Maintenance
- Customer Care Center
- Rejects and Adjustments
- Prime Vendor Subsistence
- Electronic Commerce/Electronic Data Interchange
- Document Management System
- Payroll Support Services
- Travel Services
- Common Administrative Services
- Financial Systems Oversight
- FMS Service Requests
- Audit Services
- Purchased Care Claims Services
- Combo II Services
- Consulting
- VA Conference Tracking and Reporting

Financial Management (FM)

Debt Management Center (St. Paul, MN)

- Account Maintenance
- Administrative Offset/Expanded Tools
- Enhancement of VHA Debt Management Services
- Expanded VHA Debt Management Tools
- Business Process Optimization
- Employee Salary Offset Hearings
- Grant Waivers

Enterprise Support Services (ESS)

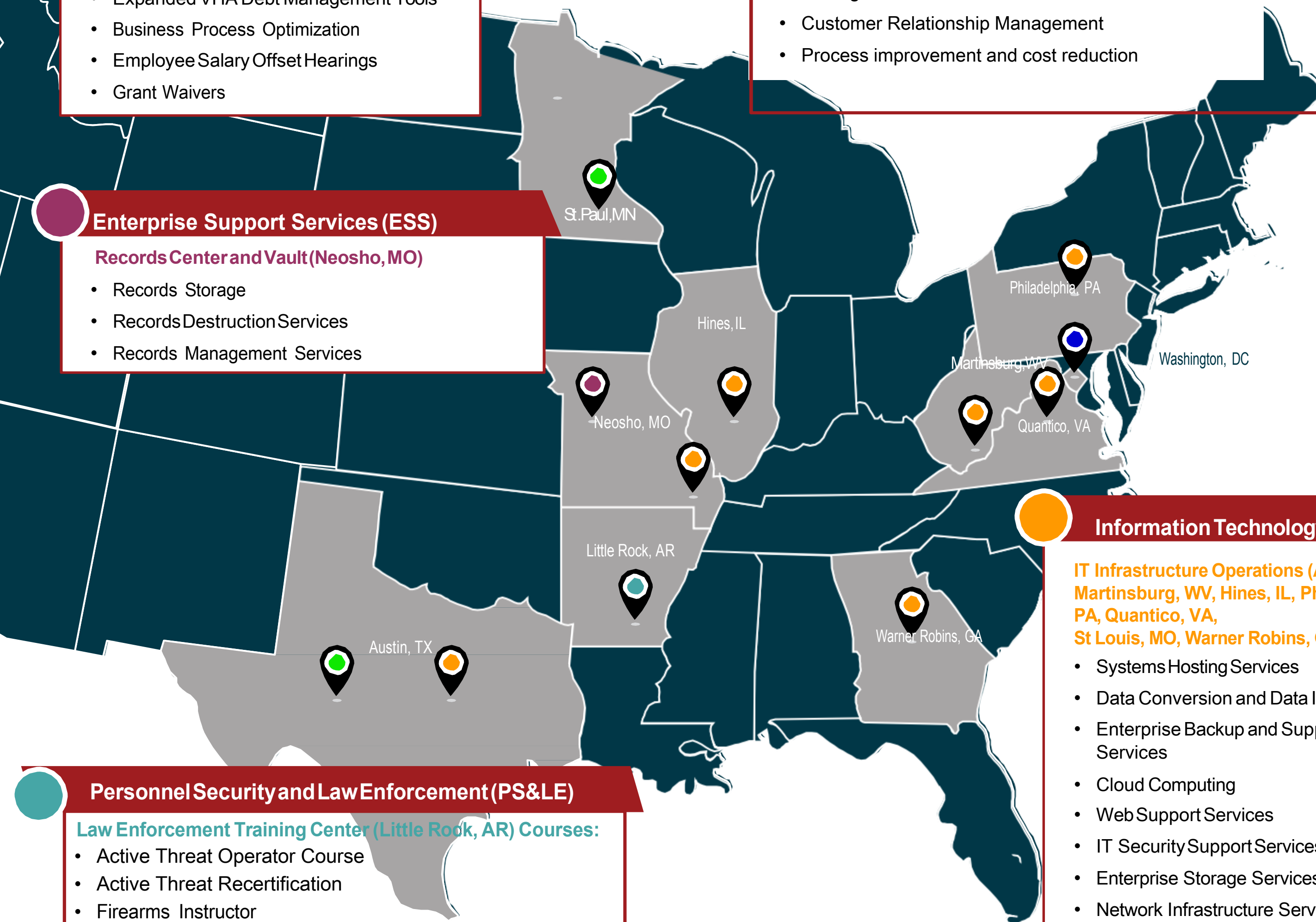
Franchise Fund Oversight Office / Enterprise Support Services (Washington, DC)

- Administrative Support to the Enterprise Centers
- Budget Formulation and Execution Analysis
- Financial and Business Planning Oversight
- Audit of Consolidated Financial Statements
- Annual Report Coordination
- Marketing Strategies
- Strategic Plan Coordination
- Customer Relationship Management
- Process improvement and cost reduction

Enterprise Support Services (ESS)

Records Center and Vault (Neosho, MO)

- Records Storage
- Records Destruction Services
- Records Management Services



Information Technology (IT)

IT Infrastructure Operations (Austin, TX, Martinsburg, WV, Hines, IL, Philadelphia, PA, Quantico, VA, St Louis, MO, Warner Robins, GA)

- Systems Hosting Services
- Data Conversion and Data Interfacing
- Enterprise Backup and Support Services
- Cloud Computing
- Web Support Services
- IT Security Support Services
- Enterprise Storage Services
- Network Infrastructure Services
- Mainframe Support Services
- Database Support Services
- Web Hosting Services
- Data Center Operations and Logistics

Personnel Security and Law Enforcement (PS&LE)

Law Enforcement Training Center (Little Rock, AR) Courses:

- Active Threat Operator Course
- Active Threat Recertification
- Firearms Instructor
- Firearms Recertification
- Ground Defense and Recovery Recertification
- Instructor Development
- Long Gun
- Physical Security
- Police Service Program Compliance
- USAF Basic Police Officer
- Verbal Defense Training

Personnel Security and Law Enforcement (PS&LE)

Security and Investigations Center (Little Rock, AR)

- National Security Background Investigations and Adjudications
- Public Trust Background Investigations and Adjudications
- Low Risk Background Investigations and Adjudications
- Reciprocation of a Prior Adjudication from other Federal Agency
- Security Check for Candidate Requiring Approval of the Secretary
- Special Agreement Check (Fingerprint) Adjudication
- Fingerprint Submission
- Reissuance/Copy of Certificate of Investigation/Eligibility

Enterprise Support Services (ESS)

Human Resource Enterprise Center (Washington, DC)

- Consolidated Internship Programs
- Competency Course Offerings
- Competency Modeling and Mapping
- VA Talent Management System Administration
- Learning Management Systems Training
- Electronic Course Content Management
- OESS Website and SharePoint Management
- VA Personnel Notification and Accountability
- OESS HR Management

Members of the VA Franchise Fund Network

Joe Schmitt, Director, Debt Management Center

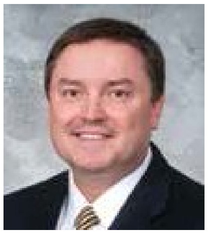
Eddie Pool, Executive Director, IT Infrastructure Operations

Jared Martin Interim Director, Financial Services Center and Records Center and Vault

Christian Poole, Chief Financial Officer, Revolving Fund

James Ward, Director Law Enforcement Training Center

Catherine Biggs-Silvers, Acting Director, Human Resource Enterprise Center



Joshua Blockburger, Director, Security and Investigations Center

Information Technology

IT Infrastructure Operations (ITIO).

Composed of data centers in Austin, TX; Martinsburg, WV; Hines, IL; Philadelphia, PA; Quantico, VA and St Louis, MO; ITIO provides hosting and Tier 3 technical support services for VA IT systems in core VA data centers and customer facilities across the enterprise. ITIO fosters standardization, consolidation, and faster adoption of new technologies and support for systems requiring specialized knowledge of the business and technical application needs. Key services include IT security, storage, network infrastructure, unified communications, operating systems, mainframe, database, middleware, web hosting services, and data center operations and logistics.

Financial Management

Debt Management Center (DMC).

Located in St. Paul, Minnesota, the DMC is a centralized facility that provides direct collection of delinquent consumer debt owed to VA. DMC provides high quality customer-responsive receivables management services. DMC balances the charter to collect debts on behalf of the American taxpayers and VA with a Veteran-centric, compassionate approach; helping Veterans and families understand their rights, meet their obligations and develop solutions to resolve their debts. DMC provides a full spectrum of administrative services to properly handle their customers' accounts receivable needs; from establishment through disposition of the receivables. DMC provides debt notification and counseling to Veterans and payment options for amounts owed to VBA and VHA for compensation, pension, education benefits, home loan guarantees, and co-payments. DMC also manages the administrative offset process for both internal benefits offsets and those referred to the Department of Treasury (Treasury) for offset under the Treasury Offset Program (TOP).

Financial Services Center (FSC).

Located in Austin, TX, Waco, TX and Washington, DC, the FSC provides a full range of financial and accounting services. These services include financial reports and accounting, invoice payments, credit card payments, medical claims adjudication and payment processing, vendor file maintenance, discount subsistence purchases, payroll processing, and VA conference tracking and reporting. The FSC also provides customer support for payroll, travel and payment processing, electronic commerce/ electronic data interchange, automated document management, audit recovery, permanent change of station and temporary duty travel pay processing, common administrative services, accounting training, and consulting.

Records Center and Vault (RCV).

Located in a subterranean, climate-controlled facility in a remote Midwestern part of the country, the RCV provides records storage, protection, and management services for official Federal records. The 403,160 square foot facility is certified by the National Archives and Records Administration to operate as an agency records center. General, vital, and unscheduled records, as well as records pending litigation freezes are safely and securely stored in paper or film format for Federal customers.

Acquisitions and Logistics

Franchise Fund Oversight Office (FFO).

Located in Washington, DC, the FFO functions as the business office for the VA Franchise Fund. As such, the FFO is responsible for providing administrative support to the Enterprise Centers by directing and analyzing budget formulation and execution processes, administering financial resources, overseeing business planning activities, managing the annual financial statement audit for the Fund, preparing the annual reports and strategic plans, coordinating marketing activities, and serving as the liaison between the Enterprise Centers, their customers, and the Revolving Fund Board.

Personnel Security and Law Enforcement

Law Enforcement Training Center (LETC).

The LETC, located in Little Rock, AR, provides special training for police officers working in a health care or service-oriented environment. Emphasizing training in health care or limited jurisdiction environments, the LETC is available to approximately 4,500 law enforcement personnel working at VA health care facilities and to law enforcement professionals at other Federal agencies.

Security and Investigations Center (SIC).

Located in North Little Rock, AR, the SIC provides quality background investigations and timely adjudications for VA employees in national security and public trust positions and all risk levels for VA contractors nationwide. Additionally, the SIC provides security checks for appointees, high-level award recipients centralized to the Secretary of VA, and supports the Personal Identification Verification (PIV) process for employees, contractors, and affiliates of the Department.

Human Resources Administration

Human Resource Enterprise Center (HREC).

The HREC, located in Washington, D.C. established in January 2017 provides Department-wide limited HR support services to improve support services capability, performance and to optimize existing support service delivery processes. HREC supports continuing and emerging VA customer requirements while delivering best-in-class human resource (HR services and capabilities to VA's Administrations and Staff Offices, allowing them to focus on delivering world-class benefits and services to Veterans and eligible beneficiaries. HREC provides products and services to nearly 600,000 VA employees, contractors, volunteers and academic affiliates.

LETTER TO STAKEHOLDERS

J.Christian Poole

Chief Financial Officer, Revolving Fund

On behalf of the Franchise Fund, I invite you to examine our FY 2018 Annual Report, outlining the VA Enterprise Centers' accomplishments and plans for next year, and the Franchise Fund's audited financial statements. This report documents the Franchise Fund's progress in the delivery of exceptional support services to VA and other government agencies (OGA). We ended FY 2018 with total revenue of $910 million, which is a significant increase from FY 2017 revenue of $864 million.

The Franchise Fund's progress resulted in some noteworthy accomplishments. They include:

- Attaining an unqualified audit opinion of our financial statements for the 21st consecutive year.
- Utilizing $34 million of financial reserves during FY 2018 to execute technical refreshes required as systems reach end-of-life status and can no longer function in a sustainable manner. These technical refreshes ensured the increased speed, stability and capacity of critical systems which support the VA's mission while maintaining price consistency for customers. (ITIO)
- Supporting the VA's Financial Management Business Transformation (FMBT) initiative by performing extensive data cleansing related to cost of living adjustments and unapplied proceeds which will consequently increase collections and preparedness for FMBT. (DMC)
- Providing business process re engineering Leadership to VA's Financial Management Business Transformation (FMBT), and extensive Subject Matter Expert (SME) support for Accounting Classification Structure, Budget Formulation and Execution as well as piloting the interface of the Invoice Payment Processing System (IPPS) with the Integrated Financial and Acquisition Management System (iFAMS). (FSC)
- Continuing to expand capacity and variety of course offerings, LETC trained 3,338 VA police officers during FY 2018 which is a 5 percent increase from prior year. LETC currently has the ability to accommodate approximately 4,500 law enforcement personnel working at VHA health care facilities as well as other Federal agencies. (LETC)
- Processing 29,851 requests for background investigation case files for National Background Investigations Bureau (NBIB) during FY 2018 which represents a 6 percent increase from the 28,060 background investigation processed during FY 2017. (SIC)
- Reducing the labor required to search for records while simultaneously decreasing the physical storage space needed to to maintain paper logs. During FY 2018, RCV facilitated the development of an electronic indexing system. RCV outlined specifications for a secure portal to catalog the contents of the 1.7 million cubic feet of paper Veteran medical records stored on behalf of VHA . (RCV)
- Deploying the upgraded Talent Management System (TMS 2.0) and retiring the legacy application and hosting environment in August 2018. TMS 2.0 will continue to support leadership and employee development while tracking more than 10 million instances of said development throughout the VA. (HREC)

These successful endeavors are examples of the Franchise Fund delivering remarkable value and exceptional services to its Federal customers. The success of the Franchise Fund would not have been possible without the support of its customers. We thank all of our customers for their continuing support.

I am pleased to submit the VA Franchise Fund FY 2018 Annual Report. As the Franchise Fund looks forward to this coming year, I am confident it will continue to demonstrate sound business practices under the current governance structure.

J. Christian Poole

Our Stakeholders

Our ultimate stakeholders are Veterans and their families who directly benefit from the services VA provides, and those who carefully monitor the delivery of these services, including OMB, Congressional authorization and appropriations committees and subcommittees, and Veterans Service Organizations. Other stakeholders include VA and other government agencies (OGA).

As knowledgeable government professionals, we provide our stakeholders with creative, cost-effective, and practical solutions to help them accomplish their primary mission. Although Federal agencies have unique missions, our collective experience enables us to give expert advice from an insider's point of view, as we understand unique requirements and financial constraints. We realize that we must compete for business every day to retain our customers' trust and confidence.

The American public holds us accountable to high standards as we spend their tax dollars to administer government programs. Expensive and wasteful practices are not acceptable. We embrace resilience and resourcefulness as we adopt business practices that enable us to become more efficient and responsive.

External Stakeholders

- Veterans and their families
- Congressional authorization and appropriations committees and subcommittees
- Department of Air Force
- Department of Commerce
- Department of Defense (DOD)
- Department of Health and Human Services (HHS)
- Department of Homeland Security (DHS)
- Department of Interior (Interior) Environmental
- Protection Agency (EPA)
- General Accounting Office (GAO)
- Office of Management and Budget
- Postal Regulatory Commission
- Private Sector Vendors
- Surface Transportation Board
- Veterans Service Organizations (VSO)

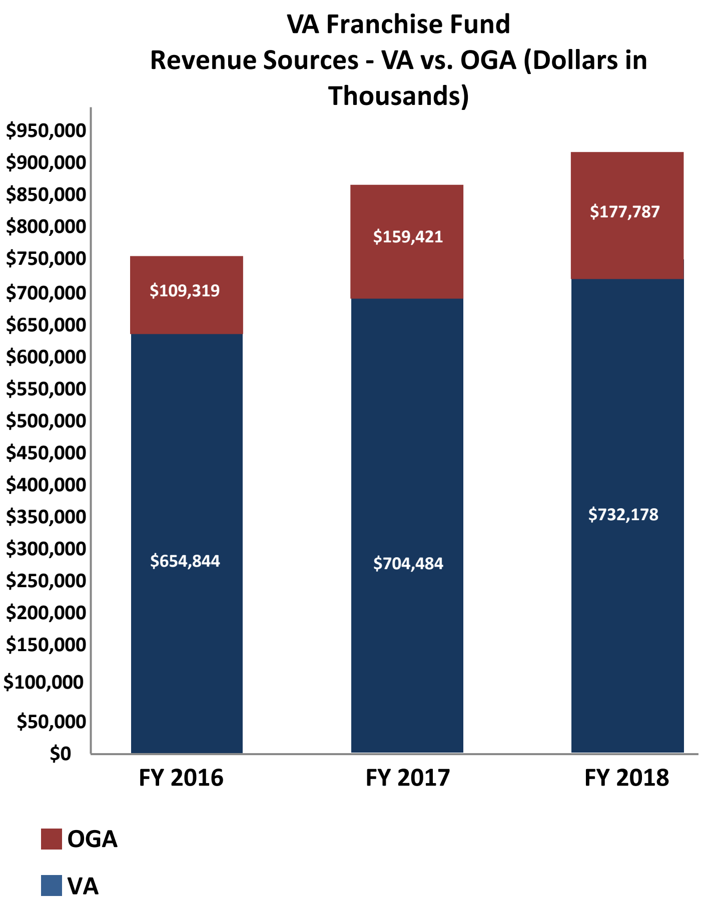
Internal Stakeholders

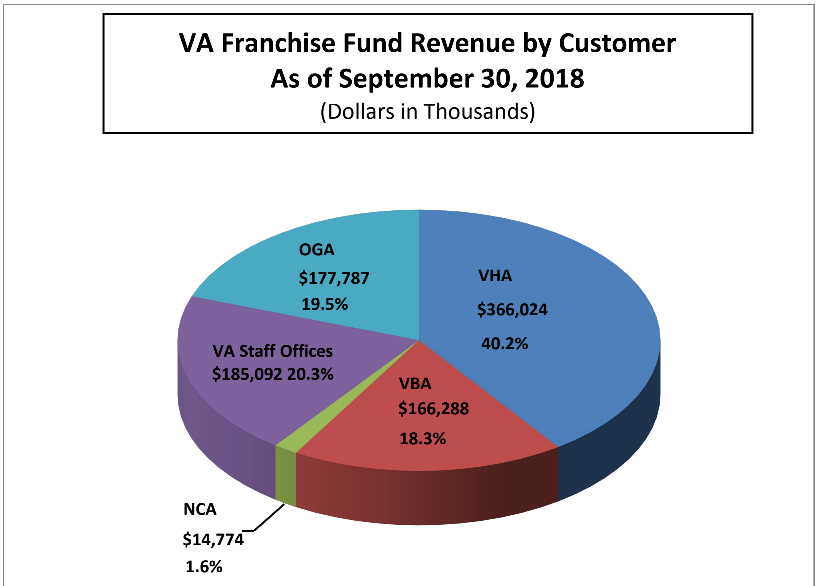
- Veterans Health Administration (VHA)
- Veterans Benefits Administration (VBA)
- National Cemetery Administration (NCA)
- VA Staff Offices
- Board of Veterans' Appeals
- Franchise Fund Enterprise Centers
- Internal Control Service
- Office of Acquisition and Logistics
- Office of Construction and Facilities Management
- Office of Business Oversight – Management
- Quality Assurance Service
- Office of Financial Systems and Operations – Fiscal Applications
- Office of Information & Technology
- Office of the Inspector General

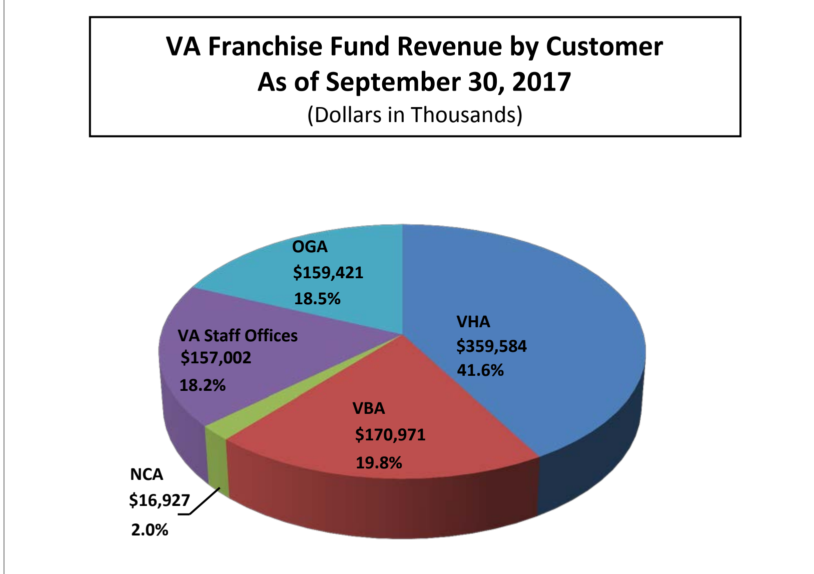
Comparison of Customer Revenue from FY 2017–2018

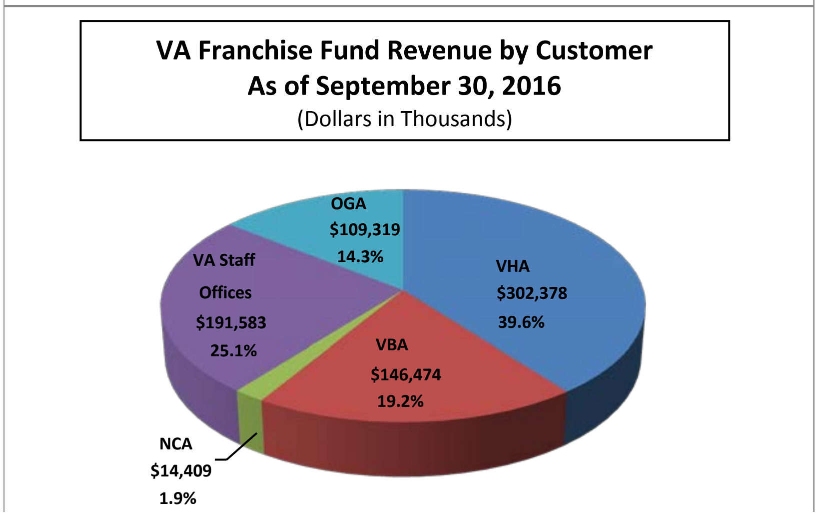
Approximately 80 percent of Franchise Fund revenue comes from VA customers. Within VA, VHA programs provide the most revenue to the Enterprise Centers. The remaining 20 percent comes from several different OGA customers. During FY 2018, revenue from VHA customers increased by $6 million while revenue from VBA customers decreased by $4 million.

Revenue from OGA customers increased notably between FY 2017 and FY 2018. The Franchise Fund ended FY 2018 with $177 million in revenue, an increase from FY 2017 levels of $159 million. This revenue increase was due to the growing business needs of FSC's OGA customers. FSC received increased OGA revenue from all OGA customers including the Department of Homeland Security (DHS), Department of Health and Human Services (HHS) as well as the Surface Transportation Board (STB) in the amount of $18 million.









Meeting VA Franchise Fund Objectives

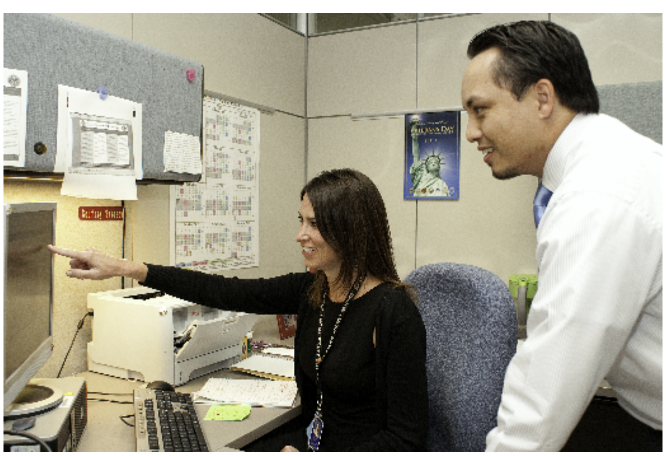
Information Technology Segment – ITIO

Cloud Architecture and Operations

During FY 2018, the ITIO Cloud Architecture and Operations team supported over 23 VA Enterprise Cloud (VAEC) early adopters and the operations of designated production applications. Additionally, this team established a Cloud operational structure which ensures 24-hour coverage and incident response.

Property Management

During FY 2018, the ITIO Property Management team supported the move of over 5,000 National Cemetery Administration (NCA) desktop assets to the area of responsibility, updated the Austin IT Center's warehouse storage racks with an Automotive Rail System, and updated the shipping preparation area at the Hines IT Center in order to efficiently prepare more than 200 pallets annually for shipment and support operations.



Technology Business Management Framework

During FY 2018, in order to facilitate transparency and decision making, ITIO implemented the Technology Business Management (TBM) framework. TBM allows for the categorization and allocation of expenses to TBM taxonomy elements. TBM taxonomy defines the 3 perspectives (languages) of finance, IT and business; this structure allows ITIO to benchmark against other IT organizations. Additionally, ITIO began the implementation of Apptio, an IT financial management tool, which further supports the TBM methodology.

VistA Migration

During FY 2018, ITIO completed a multi-year project to migrate 97 VistA systems serving regions 02, 03 and 04 from their respective medical centers to fully tiered VA core data centers, moving them from a legacy operating system to a more modern Linux operating system. During the VistA migrations, ITIO installed Next-Generation, Converged Virtual Infrastructure technology architecture that has and will continue to achieve significant infrastructure advancements.

Process Streamlining

During FY 2018, ITIO drafted a charter with the purpose of unifying two current ITIO hosting request processes for handling standard ITIO products and services. A single request procedure will ensure process optimization activities to receive, validate, adjudicate, assign, and close requests. Upon formal charter approval, a benchmarking and process integration strategy will begin with support from a Continual Service Improvement (CSI) team.

Financial ManagementSegment – FSC

Invoice Payment Processing

During FY 2018, FSC set a record for the processing of vendor payments through the Invoice Payment Processing System (IPPS). IPPS processed over 1.5 million invoices valued at $21 million. Additionally, IPPS achieved both timeliness of payments and accuracy of payments in excess of 99 percent. Interest penalties were reduced 40 percent below performance targets, saving the VA over $300 thousand and achieving a prompt pay discount rate of 94.7 percent which further saved the VA over $4.5 million. IPPS is also the first VA system to establish a two-way connection with the new VA Integrated Financial and Acquisition Management System (iFAMS), utilizing the iFAMS Web services to send transactions and receive data extracts.

Choice Claims Processing

During FY 2018, FSC procured a new modern commercial off-the-shelf (COTS) medical claims adjudication system, eCAMS. After this procurement, a new project to support Community Care Non-Network Claims (CCNNC) using the COTS package was established. Three development builds were completed in FY 2018 to support the implementation of eCAMS by the initial operational capability date of January 17, 2019 and full operational capability date no later than the end of November 2019. The development builds focused on interfacing vital VA subsystems with the procured COTS package. eCAMS utilizes auto-adjudication of claims, replacing the legacy Fee Basis Claims System (FBCS) that relies heavily on manual processing. eCAMS is projected to significantly improve the timeliness and accuracy of CCNNC claims processing at a reduced cost.

Improper Payments

During FY 2018, the ICARD IPERA team took great strides in stopping disbursements of improper payments that should not have been made or that were made in an incorrect amount, including both over payments and under payments. The team identified $1.5 million in Franchise Fund improper payments, recovering $1.4 million during FY 2018.

Data Analytics

Utilizing an agile framework that embraces collaboration and responsiveness, FSC's Data Analytics Service has developed over 400 data visualizations; assessed and integrated data from over 185 data sources; and developed 8 unique data products, ranging from the basic description tool to complex advanced predictive models. Three of the major dashboards includes:

1) Fee Basis Claims System (FBCS) reconciliation dashboard which addresses audit concerns by reconciling variances between the FBCS and Financial Management System (FMS). This has reduced the unobligated funds by nearly $300 million and created a method to reconcile healthcare claims paid, authorizations, and financial statements, enabling CFOs across the VA to obligate funds more accurately.

2) The Purchase Card Fraud Detection initiative which identifies improper uses of purchase cards in violation of VA policy. Armed with these results, Inspector General (IG) audit staff have stated that their time spent identifying fraud, waste, and abuse transactions has been reduced by 80 percent.

3) The Veterans Health Administration (VHA) Supply Chain Common Operating Picture (SCCOP) which provides a comprehensive supply chain management performance view through a series of metric-based dashboards. These dashboards promote the facilities' efficient utilization of medical supplies to ensure that each medical facility has the right equipment on hand at the right time.

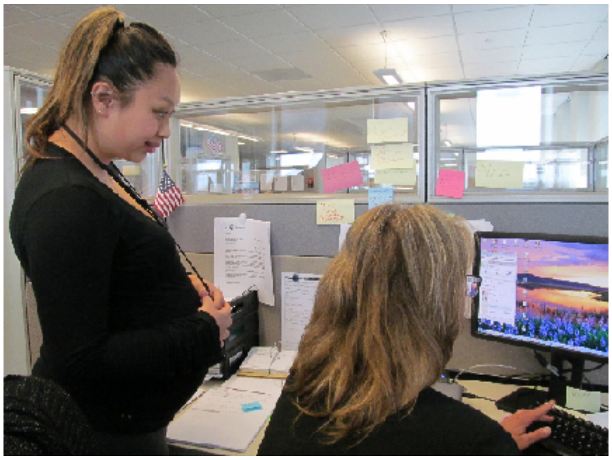
Financial Management Segment – DMC

Improving Veterans' Experience

In FY 2018, DMC continued to lead process changes to improve the Veterans' experience and provide quality customer-focused receivables management services for the VA. DMC balances the charter to collect overpayments on behalf of the American taxpayers and VA with a Veteran-centric, compassionate approach; helping Veterans and families understand their rights, meet their financial obligations and provide solutions to resolve their debts/ overpayments.

Repayment Plan Deployment

In FY 2018, DMC continued to successfully deploy the automated twelve-month auto-repayment plans for Compensation and Pension (C&P) debts. This Veteran-centric program reduced the number of hardship refunds, contributing to the 37 percent reduction in total calls to DMC and the 62 percent reduction in repeat calls. DMC also initiated extended repayment plans up to 5 years for C&P non-rating debts. These initiatives result in increased Veteran satisfaction.



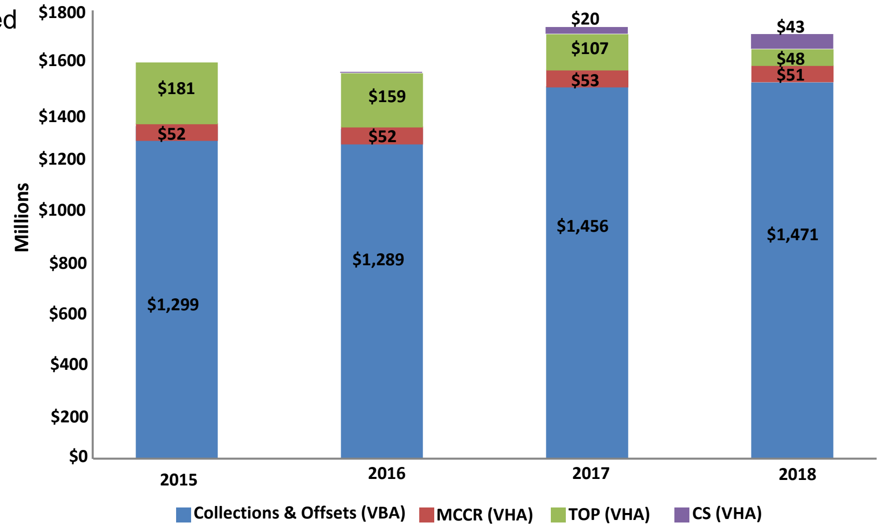
Document Scanning and Storage

During FY 2018, DMC partnered with FSC to deploy front-end scanning of documents and conversion of document storage from the Synergy legacy system to a new document management system called PEGA. The phased implementation of this digital transformation began in April 2018. This new front-end scanning system reduced document availability lead time from 10 days to 2 days for a total volume of 850 thousand documents annually. This process improvement project will transform DMC's former paper dependency and manual work flow to a completely digital work flow process which will enhance quality, timeliness, and productivity while eliminating past redundancies.

Contact Center Process Improvement

During FY 2018, DMC took significant steps to improve Veterans' experience. DMC upgraded its phone system to provide enhanced call features such as virtual call-back, advanced routing, and 100 percent call recording. These enhancements allowed the DMC Contact Center to answer 621,224 Veterans' calls; which represents a 15 percent increase over the prior year. DMC also reduced average call wait times to less than 5 minutes; which was a 74 percent improvement over the prior year. Additionally, DMC experienced a 62 percent reduction in repeat calls compared to the prior year. These improvements allow DMC to offer a more Veteran-centric experience which ultimately lead to higher overall customer satisfaction.

Total Collections and Offsets



Debt Collection Process Improvement

During FY 2018, DMC worked closely with Treasury to implement and test a new accounts receivable system called Cross-Servicing Next Generation (CSNG). This system ensures data processing accuracy and efficiency of referrals, updates, rejects and reconciliations. Initially, processing errors occurred between agencies with numerous error codes on reject files. To resolve this issue, DMC temporarily halted all file processing to Treasury and suspended collection on Veterans' accounts until said errors were reconciled. When CSNG referrals resumed, all the Treasury collection tools were turned off; some of which are still turned off which degrades collection efforts. However, DMC will continue to work with Treasury to ensure that all Treasury collection tools will be turned on in FY 2019. This will ensure improved collections on behalf of the Veterans Health Administration (VHA).

Personnel Security and Law Enforcement Segment – SIC

Background Investigation Process Automation

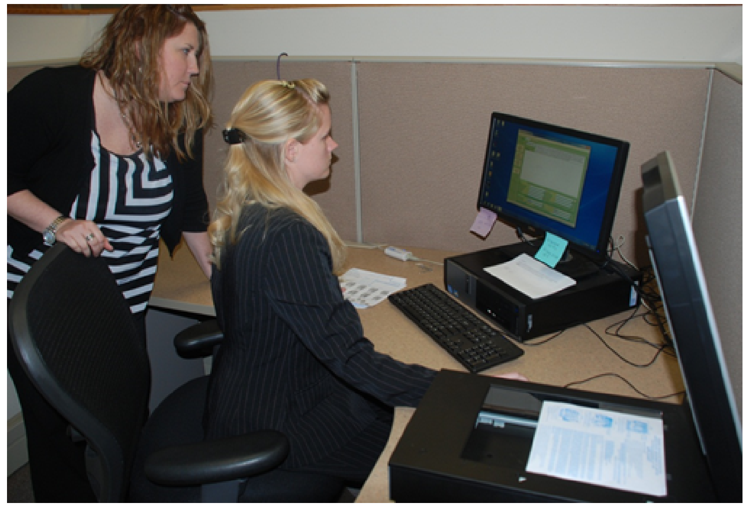
During FY 2018, SIC continued to deploy automated features to enhance the processing of its investigative products. SIC continues to use a SharePoint portal to upload and archive PDF applications for background investigations. However, during FY 2018, SIC worked diligently to finalize the requirements for a commercial off-the-shelf (COTS) application that would replace SharePoint in FY 2019. The replacement system is designed to manage and archive all SIC background investigation requests and supporting documents, providing total transparency to the customer with regards to the current status of a pending background investigation all the way to the point it is scheduled at the National Background Investigation Bureau (NBIB). This system will provide systematic and automated rejection and acceptance parameters and processes for each type of request and document submitted to SIC.

Cost-effective Business Practice

During FY 2018, SIC credited its customers over $1.3 million in refunds for unneeded Enhanced Subject Interviews. These refunds were issued due to policy changes enacted by the National Background Investigation Bureau (NBIB) as well as SIC's readjustment of its billing processes. These cost saving opportunities provided by SIC for its customers, allows the VA to better meet the needs of our Veterans.

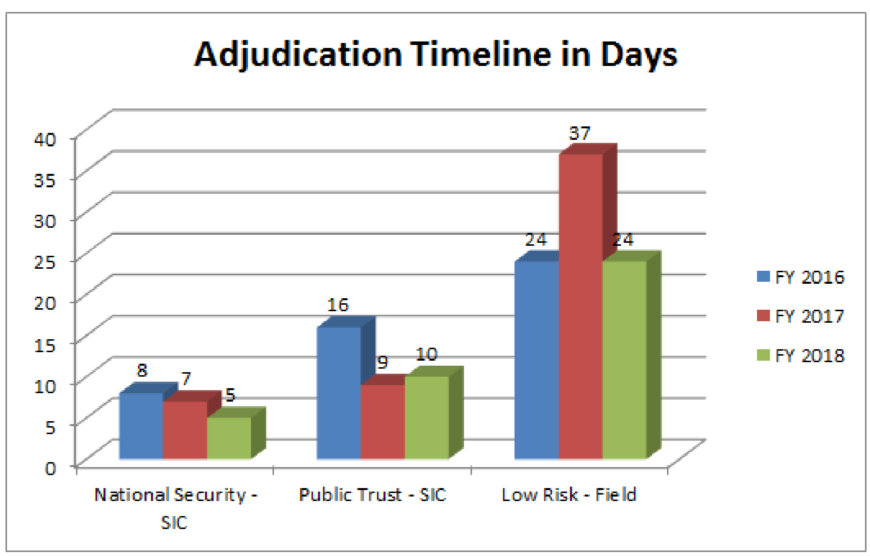
Workforce Training and Development

During FY 2018, SIC continued to invest in the development of its employees. All adjudicators must be trained and certified by the appropriate oversight Federal agency for the type of adjudications they perform. Suitability adjudicators are required to complete the NBIB's Essentials of Suitability Adjudication Program course and pass the certification exam. National Security adjudicators are required to complete the Defense Security Service Academy's Personnel Security Adjudication course and pass the certification exam. The SIC's goal is for all senior adjudicators to obtain both certifications.



Reduced Adjudication Timeline

During FY 2018, SIC continued to make sufficient progress in reducing the number of days to adjudicate closed case files from the Office of Personnel Management (OPM) which pertained to national security and public trust background investigations. Additionally, SIC processed 1,791 more cases in FY 2018 as compared to prior year despite having eight less employees. Furthermore, SIC experienced a 17 percent increase in the use of the "adjudication only" product line primarily due to a few stations that elected to utilize the SIC as their sole source for adjudications. This allowed these stations to redistribute their manpower, in order to fulfill other staffing requirements at their particular station.



Personnel Security and Law Enforcement Segment–LETC

Verbal Defense Training

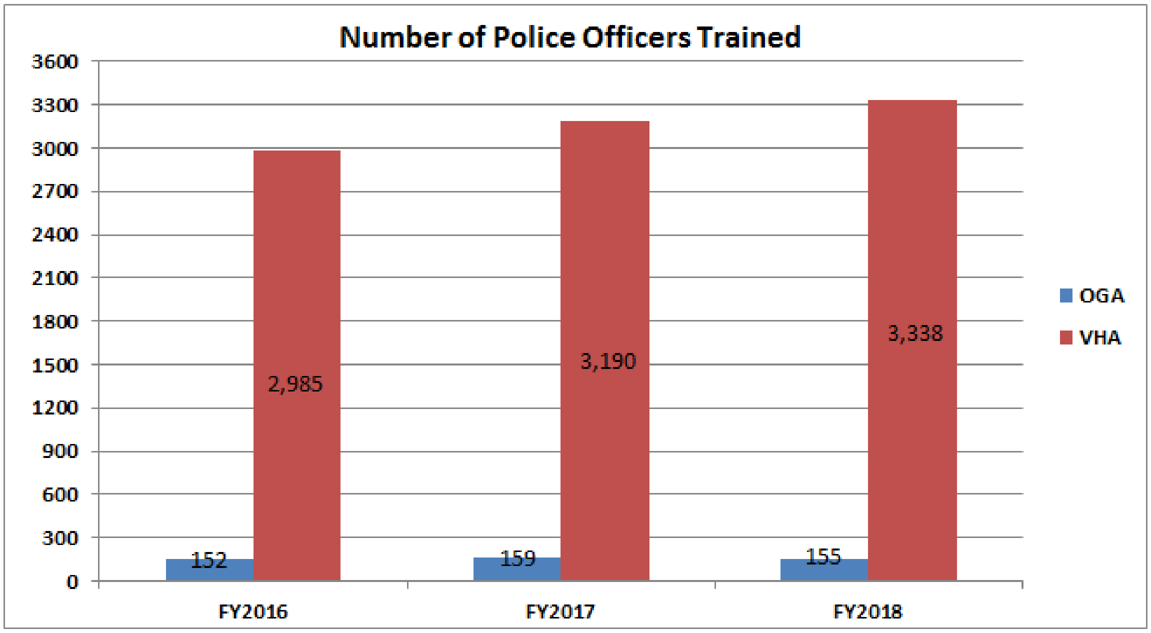
During FY 2018, LETC's Verbal Defense in Healthcare (VDH) training was in great demand for VA Medical Centers nationwide. Due to this demand, LETC has traveled to 24 VA Medical Centers throughout the nation and provided 112 VDH training courses to approximately 3,000 non-law enforcement personnel, many of whom were VA hospital personnel. VHA has requested LETC continue the VDH training series; consequently, LETC is scheduled to visit 31 VA Medical Centers during FY 2019.

New LETC Courses

In FY 2018, LETC significantly expanded its course offerings. These courses include Outside Law Enforcement - First Responder (Suicide Prevention); Advance Ground Defense and Recovery Course I and United States Air Force (USAF) Physical Assessment tests. Additionally, the Police Officer Standardized Training (POST) course was increased from eight weeks to ten weeks and the Department of Air Force Civilian Police Academy (DAF CPA) was increased from five weeks to six weeks. These courses either provided new training or extended training opportunity to approximately 2,000 personnel.

VA Training Facility

During FY 2018, LETC completed the construction of its new Firing Range building. This facility has expanded LETC's footprint, hence allowing its students access to a second training campus while allowing LETC to continue expanding its course offerings.



Support Services Excellence Segment - RCV

Records Destruction

During FY 2018, the RCV Business Office and Operations management team worked closely with the Office of Acquisition Operations to award a large-scale destruction contract. All VA records approved for destruction are securely transported to a commercial incineration facility, and RCV staff witness the full destruction process. In the last two months of FY 2018, RCV safely destroyed approximately 10,000 cubic feet of VA records, which were approved by customers for destruction. In addition to awarding a multi-year contract to handle current and future destruction, RCV ensured that the selected vendor is 'green' and generates clean energy. The facility servicing RCV processes 1,125 tons of solid waste daily, creating enough clean energy to power approximately 20,000 homes in the surrounding area.

Electronic Records Indexing

Throughout FY 2018, the RCV Operations team has made great strides in scanning older, paper inventories to electronic, PDF documents. This aids the team in locating Veteran records when the requesting VA office no longer has accurate copies of their inventory. This project will continue as needed, with RCV focused on the most requested accessions.

Records Retrieval Process Improvement

In FY 2018, RCV continued its commitment to process improvement through its focus on key performance measures such as the speed and accuracy of returning requested files. RCV strives to return the right record(s) within 1 business day at least 99.5 percent of the time. To continuously meet and exceed this rate, RCV constantly reviews its retrieval process to identify areas for improvement. The Operations group is cross-trained so that each person can perform multiple duties. This ensures continuity of operations if staff are temporarily out of the office.

Support Services Excellence Segment - HREC

Cloud-Based VA Notification System

During FY 2018, HREC initiated the deployment of a comprehensive VA-wide accountability and notification method to send critical safety and emergency alert notifications and to rapidly and accurately gain cognizance of the safety and work status of its employees, contractors, affiliates, and associate workforce. This cloud-based Emergency Accountability and Alerting System (EAAS), which will replace the legacy VA Notification System (VANS) and VA Personnel Accountability System (VAPAS), is scheduled for completion in April, 2019.

Lean Six Sigma

During FY 2018, an HREC led Lean Six Sigma team developed and implemented a contract review process that delivered improved products and services for its customers. The process improvement saved VA $36 million in contract reductions and cost avoidance.

VA Digital Learning Initiatives

In FY 2018, HREC conducted more than 20 informational e-Learning and Digital Book Webinars for VA employees. The webinars focus on various ways VA employees can utilize online training and educational resources, for their personal and professional development. Additionally, HREC upgraded the VA Learning Content Management System (LCMS) to version 11.2, providing support for the xAPI communication standard and updated content viewers for over 250 content developers working on more than 500 courses throughout the Department.

National Diversity Internship Program

During FY 2018, HREC managed the Department of Veterans Affairs (VA) National Diversity Internship Program (NDIP) to provide internship opportunities and invaluable work experience in various career fields. These internships were available to undergraduate and graduate students enrolled full-time or part-time, in degree-seeking programs at accredited post-secondary institutions. These institutions include Minority Serving Institutions such as Historically Black Colleges and Universities, Hispanic Serving Institutions, Asian American Colleges, Pacific Islander Serving Institutions, and Tribal Colleges and Universities. In FY 2018, VA hosted 54 students throughout various VA staff offices and Administrations.

Talent Management System (TMS)

In FY 2018, after recording 100 million completions in the Talent Management System (TMS), VA retired the legacy system and delivered a solution upgrade to the TMS 2.0 platform on August 13, 2018. TMS 2.0 ensures VA has a sustainable, extended official system of record for VA employee development and training. From September 2017 to present, over 2,500 TMS administrators across VA were trained to support the TMS program at the local, facility, Veterans Integrated Service Networks (VISN), Regional and national level. Through the newly released TMS 2.0, VA will rack and report more than 10 million instances of employee development and training throughout the enterprise.

The performance information presented below accurately represents the Enterprise Centers' performance during fiscal years 2016 – 2018. We are committed to ensuring that reported performance information is accurate and based on reliable information, and we continually seek to improve our data collection and monitoring techniques.

Each component of the VA Franchise Fund is committed to achieving its performance goals to ensure that we remain a performance-based organization.

Performance Summary Table

	Actuals			Plan	Were 2018 Goals Achieved or Exceeded?	
Performance Measure	2016	2017	2018	2018	Yes	No
Percent of Veterans and/or beneficiaries who contacted the DMC without receiving a busy signal (DMC)	100.0%	100.0%	100.0%	100.0%	✓	
Payment processing accuracy rate (FSC)**	99.6%	99.7%	99.0%	99.0%	✓	
Class graduation rate (LETC)	95.3%	96.1%	95.0%	95.0%	✓	
Percent of adjudications that are completed within the established time frames (SIC)	99.0%	99.0%	100.0%	99.0%	✓	
Percent of recalled records that are shipped securely and accurately to requesting facilities within established timeframes (RCV)	99.9%	99.9%	99.9%	99.9%	✓	
Number of audit qualifications for the VA Enterprise Centers (FF)	0	0	0	0	✓	
Claim processing time (percent paid within 30 days)* (FSC) *	N/A	N/A	100.0%	98.0%	✓	
Invoices paid in accordance with Prompt Payment Act* (FSC)*	N/A	N/A	99.4%	95.0%	✓	
First call resolution* (FSC)*	N/A	N/A	97.6%	90.0%	✓	
Average wait time until caller speak to a live person (minutes:seconds)* (FSC)*	N/A	N/A	2 minutes 39 seconds	< 3 minutes	✓	

*New performance measures established during FY 2017
**Performance goal was replaced by invoice paid in accordance with the Prompt Payment Act goal in FY 2018

Performance Highlights During FY 2018

- During FY 2018, 77 data centers were consolidated and 7 data centers were closed by ITIO. Consequently, 299 data centers remain active in the Office of Management and Budget (OMB) inventory list. This is a reduction from 362 data centers during FY 2017 and is in conducive with the Federal Data Center Consolidation Initiative (FDCCI) and the Data Center Optimization Initiative (DCOI). (ITIO)
- During FY 2018, National Archives and Records Administration (NARA) auditors visited the RCV operations facility in Neosho, MO, to observe the staff and ensure all measures were in place to safely and securely manage all records storage services. RCV met and exceeded all NARA requirements and is well positioned to continue providing support for the next two years. RCV is the only VA facility accredited by NARA to provide secure, long-term storage of records for VA and other government agencies. Recertification is required every ten years. (RCV)
- During FY 2018, FSC completed deployment of VA Time and Attendance System (VATAS). The system was rolled out to all VA employees (approximately 400,000 users). VATAS provides a Web-based, centralized timekeeping system enforcing pay regulations and policies for both Title 5 and Title 38 employees. VATAS enables VA's transformation to a high performing, 21st century organization and provides value through increased accountability, risk reduction, and transparency. (FSC)
- OPM requires the adjudication of National Security background investigations within 20 days of the OPM closing date of the investigation at least 90 percent of the time as illustrated in the Performance Summary table. However, the adjudication of suitability background investigations are not required by OPM to be adjudicated within the same 20 day time period as National Security cases. The SIC's goal is to adjudicate all suitability background investigations within 30 days of the OPM's closing date 90 percent of the time. OPM reported that the SIC average suitability adjudication timeline was 10 days in FY 2018, exceeding the self-imposed goal of 30 days. (SIC)
- During FY 2018, VHA Medical Center recognized the positive outcomes associated with staff having the requisite skill-sets to verbally de-escalate inappropriate behavior as a means to enhance both Veteran and employee satisfaction. To meet those demands, LETC increased the number of Verbal Defense in Healthcare (VDH) courses progressing from teaching 42 classes in 11 VA Medical Centers in FY 2017 to teaching 115 classes in 22 VA Medical Centers during FY 2018. Employee critiques have rated the course at over 98 percent excellent. (LETC)

Performance Highlights During FY 2018

- During FY 2018, DMC made significant improvements designed to provide the best possible customer service experience for its customers. These improvements included a 12-month auto-repayment plan which significantly reduces hardship experienced by customers as a result of debt collection. Additionally, contact center improvements and staffing increases resulted in a 15 percent increase in calls answered, a 62 percent reduction in repeat callers and a reduction in call wait times to under 5 minutes, which is a 74 percent improvement from prior year. (DMC)
- For the 21st consecutive year, the audited financial statements of the VA Franchise Fund received an unqualified "clean" opinion.

Limitation Statement

The principal financial statements have been prepared to report the financial position and results of operations of the entity, pursuant to the requirements of 31 U.S.C. 3515(b).

While the statements have been prepared from the books and records of the entity in accordance with generally accepted accounting principles for Federal entities and the formats prescribed by OMB, the statements are in addition to the financial reports used to monitor and control budgetary resources which are prepared from the same books and records.

The statements should be read with the realization that they are for a component of the U.S. Government, a sovereign entity.

Audit Opinion

For the 21st consecutive year (1998 - 2018), the VA Franchise Fund has received an unmodified "clean" audit opinion.

Financial Statement Analysis

The consolidated financial statements present the Franchise Fund's financial position, cumulative results of operations, changes in net position, and information on budgetary resources for FY 2018 and FY 2017. Highlights of the information contained in the consolidated financial statements are summarized in this section.

Overview of Financial Position

Assets

The Consolidated Balance Sheets reflect the Fund's asset balances of $458 million as of September 30, 2018. This is an increase of $34 million, or 8 percent, over the previous year's total assets of $424 million. An increase to Accounts Receivable was primarily due to an increase in volume of services provided to OIT, VHA, VBA by ITIO, FSC and DMC. Additionally, the purchase of Oracle super cluster servers/racks/switches by ITIO and Health Claims Processing software cost for FSC contributed to the increase of property, plant and equipment.

The Fund's assets as presented in the Consolidated Balance Sheets are summarized in the following table:

(Dollars in Thousands)	2018	2017
Fund Balance with Treasury	$ 254,294	$ 269,498
Property, Plant and Equipment, Net	83,444	65,230
Accounts Receivable, Net	118,816	88,881
Other Assets	1,117	
Total Assets	$457,671	$ 423,609

Liabilities

The Fund had total liabilities of $123 million as of September 30, 2018. This represents a decrease of $7 million, or 5 percent, over the previous year's total liabilities of $130 million. The decrease in Accounts Payable is primarily due to a large increase in scheduled payments processed by ITIO. Additionally, the decrease in other liabilities is primarily due to a decrease in FY 2018 accrued salaries.

The Fund's liabilities as presented in the Consolidated Balance Sheets are summarized in the following table:

(Dollars in Thousands)	2018	2017
Accounts Payable	$ 84,864	$ 90,225
Other Liabilities	37,790	39,316
Total Liabilities	$ 122,654	$ 129,541

Net Position

The Fund's net position increased by $41 million in FY 2018 on the Consolidated Balance Sheets and the Consolidated Statement of Changes in Net Position. The net position for the Fund was $335 million; a 14 percent increase over the prior year's ending net position of $294 million. Net position is the sum of unexpended funds and cumulative results of operations.

Net Cost

The Fund's net cost of operations incurred a net gain of $25 million in FY 2018, as reflected in the Consolidated Statement of Net Cost.

Budgetary Resources

The Combined Statement of Budgetary Resources presents budgetary resources made available to the Fund during the year and the resulting status of budgetary resources at year-end. The Fund does not receive an annual appropriation from Congress. The Fund is fully self-sustained by recovering all costs through reimbursements for services provided. The Fund has total budgetary resources of $1.09 billion, a $3 million increase from the FY 2017 level of $1.06 billion.

The Fund's Budgetary Resources as presented in the Combined Statement of Budgetary Resources are summarized in the following table:

(Dollars in Thousands)	2018	2017
Beginning Unobligated Balance	$ 115,002	$ 156,116
Unpaid Obligations	37,643	40,945
Other Changes in Unobligated Balance	1	38
Spending Authority from Offsetting Collection	933,161	867,699
	---------------	------------
Total Budgetary Resources	$ 1,085,807	1,064,798

Management Assurances

The financial and performance data presented in this report are complete and reliable. Throughout the year, VA Franchise Fund senior managers assess the efficiency and effectiveness of their organizations by analyzing financial and performance data. Management relies on this data to identify material inadequacies in the financial and program performance areas and to identify corrective tasks needed to resolve them.

The Department of Veterans Affairs management is responsible for (1) evaluating the effectiveness of internal control over financial reporting based on criteria established under the Federal Managers' Financial Integrity Act (FMFIA), (2) providing a statement of assurance on the overall effectiveness on internal control over financial reporting, (3) ensuring VA's financial management systems are in substantial compliance with FFMIA requirements, and (4) complying with other applicable laws, regulations, contracts, and grant agreements. With respect to internal control, CliftonLarsonAllen LLP identified six material weaknesses. (1) Compensation, pension, burial and education actuarial estimates; (2) Community care obligations, reconciliations, and accrued expenses; (3) Financial reporting; (4) Loan guarantee liability; (5) Chief Financial Officer organizational structure; (6) Information technology security controls.

In addition, CliftonLarsonAllen LLP identified one significant deficiency: procurement, undelivered orders, accrued expenses, and reconciliations.

CliftonLarsonAllen LLP identified (1) Substantial noncompliance with Federal financial management systems requirements and the United States Standard General Ledger at the transaction level under the Federal Financial Management Improvement Act (FFMIA) of 1996; (2) Improvements needed in complying with the Federal Managers' Financial Integrity Act; (3) Instances of noncompliance with Title 38 United States Code §5315 pertaining to the charging of interest and administrative costs, (4) Noncompliance with Title 38 United States Code §3733 pertaining to the vendee loan program (5) One violation of the Antideficiency Act, as reported to CliftonLarsonAllen LLP by VA, which has been reported to Congress and 6 (Noncompliance with the Improper Payments Elimination and Recovery Act for FY 2016.

http://www.va.gov/finance/docs/afr/2017VAafrFullWeb.pdf

OLLIE GREEN & COMPANY
CERTIFIED PUBLIC ACCOUNTANTS AND MANAGEMENT CONSULTANTS

INDEPENDENT AUDITOR'S REPORT

To the Director of
Department of Veterans Affairs Franchise Fund Oversight Office

In our audits of the fiscal years 2018 and 2017 financial statements of the Department of Veterans Affairs (VA) Franchise Fund we found

- VA Franchise Fund's financial statements as of and for the fiscal years ended September 30, 2018, and 2017, are presented fairly, in all material respects, in accordance with U.S. generally accepted accounting principles;

- no material weaknesses in internal control over financial reporting based on the limited procedures we performed; and

- no reportable noncompliance for fiscal year 2018 with provisions of applicable laws, regulations, contracts, and grant agreements we tested.

The following sections discuss in more detail (1) our report on the financial statements, which includes required supplementary information (RSI) included with the financial statements; (2) our report on internal control over financial reporting; and (3) our report on compliance with laws, regulations, contracts, and grant agreements.

Report on the Financial Statements

In accordance with Office of Management and Budget (OMB) Bulletin 19-01, we have audited VA Franchise Fund's financial statements. VA Franchise Fund's financial statements comprise consolidated balance sheets as of September 30, 2018 and 2017; the related consolidated statements of net cost, changes in net position, and the combined statements of budgetary resources for the fiscal years then ended; and the related notes to the financial statements.

We conducted our audits in accordance with U.S. generally accepted government auditing standards. We believe that the audit evidence we obtained is sufficient and appropriate to provide a basis for our audit opinion.

Management's Responsibility

VA Franchise Fund's management is responsible for (1) the preparation and fair presentation of these financial statements in accordance with U.S. generally accepted accounting principles; (2) preparing, measuring, and presenting the RSI in accordance with U.S. generally accepted accounting principles; and (3) maintaining effective internal control over financial reporting,

including the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. U.S. generally accepted government auditing standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement. We are also responsible for applying certain limited procedures to RSI included with the financial statements.

An audit of financial statements involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the auditor's assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit of financial statements also involves evaluating the appropriateness of the accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements. Our audits also included performing such other procedures as we considered necessary in the circumstances.

Opinion on Financial Statements

In our opinion, VA Franchise Fund's financial statements present fairly, in all material respects, VA Franchise Fund's financial position as of September 30, 2018, and 2017, and its net consolidated cost of operations, changes in net position, and consolidated budgetary resources for the fiscal years then ended in accordance with U.S. generally accepted accounting principles.

Other Matters

Required Supplementary Information

U.S. generally accepted accounting principles issued by the Federal Accounting Standards Advisory Board (FASAB) require that the RSI be presented to supplement the financial statements. Although the RSI is not a part of the financial statements, FASAB considers this information to be an essential part of financial reporting for placing the financial statements in appropriate operational, economic, or historical context. We have applied certain limited procedures to the RSI in accordance with U.S. generally accepted government auditing standards, which consisted of inquiries of management about the methods of preparing the RSI and comparing the information for consistency with management's responses to the auditor's inquiries, the financial statements, and other knowledge we obtained during the audit of the financial statements, in order to report omissions or material departures from FASAB guidelines, if any, identified by these limited procedures. We did not audit and we do not express an opinion or provide any assurance on the RSI because the limited procedures we applied do not provide sufficient evidence to express an opinion or provide any assurance.

Report on Internal Control over Financial Reporting

In connection with our audits of VA Franchise Fund's financial statements, we considered VA Franchise Fund's internal control over financial reporting, consistent with our auditor's responsibility discussed below. We performed our procedures related to VA Franchise Fund's internal control over financial reporting in accordance with U.S. generally accepted government auditing standards.

Management's Responsibility

VA Franchise Fund's management is responsible for maintaining effective internal control over financial reporting, including the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

In planning and performing our audit of VA Franchise Fund's financial statements as of and for the year ended September 30, 2018, in accordance with U.S. generally accepted government auditing standards, we considered the VA Franchise Fund's internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of VA Franchise Fund's internal control over financial reporting. Accordingly, we do not express an opinion on VA Franchise Fund's internal control over financial reporting. We are required to report all deficiencies that are considered to be significant deficiencies or material weaknesses. We did not consider all internal controls relevant to operating objectives, such as those controls relevant to preparing performance information and 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. A *significant deficiency* is a deficiency, or a 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.

Definition and Inherent Limitations of Internal Control over Financial Reporting

An entity's internal control over financial reporting is a process effected by those charged with governance, management, and other personnel, the objectives of which are to provide reasonable assurance that (1) transactions are properly recorded, processed, and summarized to permit the preparation of financial statements in accordance with U.S. generally accepted accounting principles, and assets are safeguarded against loss from unauthorized acquisition, use, or disposition, and (2) transactions are executed in accordance with provisions of applicable laws, including those governing the use of budget authority, regulations, contracts, and grant agreements, noncompliance with which could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent, or detect and correct, misstatements due to fraud or error.

Results of Our Consideration of Internal Control over Financial Reporting

Our consideration of internal control was for the limited purpose described above, and was not designed to identify all deficiencies in internal control that might be material weaknesses and significant deficiencies or to express an opinion on the effectiveness of VA Franchise Fund's internal control over financial reporting. Given these limitations, during our audit, we did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The Department of Veterans Affairs (VA) Independent Audit of VA's Financial Statements for Fiscal Years 2018 and 2017, dated November 26, 2018 reported five material weaknesses: "Information Technology (IT) Security Controls" (Repeat Condition); "Compensation, Pension, Burial and Education Actuarial Estimates" (Repeat Condition); "Community Care Obligation, Reconciliations, and Accrued Expenses" (Repeat Condition); "Financial Systems and Reporting" (Repeat Condition); and "CFO Organizational Structure for VA and VHA" (Repeat Condition). The audit report also identified two significant deficiencies: "Loan Guaranty Liability" (Repeat Condition)-(2017 material weakness - 2018 significant deficiency); and "Procurement, Undelivered Orders, Accrued Expenses and Reconciliations" (Repeat Condition).

These material weaknesses and significant deficiencies could have a direct effect on the VA Franchise Fund's internal control over financial reporting.

We also identified other deficiencies in VA Franchise Fund's internal control over financial reporting that we do not consider to be material weaknesses or significant deficiencies. Nonetheless, these deficiencies warrant VA Franchise Fund management's attention. We have communicated these matters to VA Franchise Fund management and we will report on them separately in a management letter.

Intended Purpose of Report on Internal Control over Financial Reporting

The purpose of this report is solely to describe the scope of our consideration of VA Franchise Fund's internal control over financial reporting and the results of our procedures, and not to provide an opinion on the effectiveness of the VA Franchise Fund's internal control over financial reporting. This report is an integral part of an audit performed in accordance with U.S. generally accepted government auditing standards in considering internal control over financial reporting. Accordingly, this report on internal control over financial reporting is not suitable for any other purpose.

Report on Compliance with Laws, Regulations, Contracts, and Grant Agreements

In connection with our audits of VA Franchise Fund's financial statements, we tested compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements consistent with our auditor's responsibility discussed below. We caution that noncompliance may occur and not be detected by these tests. We performed our tests of compliance in accordance with U.S. generally accepted government auditing standards.

Management's Responsibility

VA Franchise Fund's management is responsible for complying with laws, regulations, contracts, and grant agreements applicable to VA Franchise Fund.

Auditor's Responsibility

Our responsibility is to test compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements applicable to VA Franchise Fund that have a direct effect on the determination of material amounts and disclosures in VA Franchise Fund's financial statements, and perform certain other limited procedures. Accordingly, we did not test compliance with all laws, regulations, contracts, and grant agreements applicable to VA Franchise Fund.

Results of Our Tests for Compliance with Laws, Regulations, Contracts, and Grant Agreements

Our tests for compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements disclosed no instances of noncompliance for fiscal year 2018 that would be reportable under U.S. generally accepted government auditing standards. However, the objective of our tests was not to provide an opinion on compliance with laws, regulations, contracts, and grant agreements applicable to VA Franchise Fund. Accordingly, we do not express such an opinion.

Intended Purpose of Report on Compliance with Laws, Regulations, Contracts, and Grant Agreements

The purpose of this report is solely to describe the scope of our testing of compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements, and the results of that testing, and not to provide an opinion on compliance. This report is an integral part of an audit performed in accordance with U.S. generally accepted government auditing standards in considering compliance. Accordingly, this report on compliance with laws, regulations, contracts, and grant agreements is not suitable for any other purpose.

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

Louisville, KY
December 6, 2018

DEPARTMENT OF VETERANS AFFAIRS FRANCHISE FUND
CONSOLIDATED BALANCE SHEET
AS OF SEPTEMBER 30, 2018, and 2017
(Dollars in Thousands)

		2018		2017
ASSETS				
Intragovernmental:				
Fund Balance with Treasury (Note 2)	$	254,294	$	269,498
Accounts Receivable (Note 3)		118,718		88,818
Other Assets (Note 5)		1,117		0
Total Intragovernmental Assets		374,129		358,316
Public:				
Accounts Receivable (Note 3)		98		63
General Property, Plant and Equipment, Net (Note 4)		83,444		65,230
Other Assets (Note 5)		0		0
Total Public Assets		83,542		65,293
Total Assets	**$**	**457,671**	**$**	**423,609**
LIABILITIES				
Intragovernmental:				
Accounts Payable		14,495		16,286
Other Liabilities (Note 7)		24,932		25,450
		39,427		41,736
Public:				
Accounts Payable		70,369		73,939
Other Liabilities (Note 7)		12,858		13,866
Total Public Liabilities		83,227		87,805
Total Liabilities	**$**	**122,654**	**$**	**129,541**
Unexpended Appropriation		**0**		**0**
Cumulative Results of Operations		**335,117**		**294,068**
NET POSITION	**$**	**335,017**	**$**	**294,068**
TOTAL LIABILITIES AND NET POSITION	**$**	**457,671**	**$**	**423,609**

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

DEPARTMENT OF VETERANS AFFAIRS FRANCHISE FUND
CONSOLIDATED STATEMENT OF NET COST
FOR THE YEARS ENDED SEPTEMBER 30, 2018 and 2017
(Dollars in Thousands)

	2018	2017
PROGRAM COSTS:		
Gross Costs Intragovernmental (Note 10)	$ 877,102	$ 845,327
Less: Earned Revenue-Intragovernmental	(909,964)	(863,904)
Net Program Costs - Intragovernmental	$ (32,863)	$ (18,576)
Gross Costs Indirect Administrative	7,643	7,133
NET COST OF OPERATIONS	**$ (25,220)**	**$ (11,443)**

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

DEPARTMENT OF VETERANS AFFAIRS FRANCHISE FUND
CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION
FOR THE YEARS ENDED SEPTEMBER 30, 2018 and 2017
(Dollars in Thousands)

	2018	2017
CUMULATIVE RESULTS OF OPERATIONS:		
Beginning Balance	$ 294,068	$ 269,111
Prior Period Adjustments (+/-)	0	0
Beginning Balance, as Adjusted	**$ 294,068**	**$ 269,111**
BUDGETARY FINANCING SOURCES:		
Transfers Without Reimbursement	0	0
OTHER FINANCING SOURCES (NON-EXCHANGE):		
Transfers In/Out Without Reimbursement	5,459	6,335
Imputed Financing (Note 6)	10,270	7,179
Total Financing Sources	**15,729**	**13,514**
Net Cost of Operations	**(25,220)**	**(11,443)**
Net Change	**$ 40,949**	**$ 24,957**
NET POSITION	**$ 335,017**	**$ 294,068**

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

DEPARTMENT OF VETERANS AFFAIRS FRANCHISE FUND
COMBINED STATEMENT OF BUDGETARY RESOURCES
FOR THE YEARS ENDED SEPTEMBER 30, 2018 and 2017
(Dollars in Thousands)

	2018	2017
BUDGETARY RESOURCES:		
Unobligated Balance from Prior Year Budget Authority, Net	$ 152,646	$ 197,099
Spending Authority from Offsetting Collections	933,161	867,699
Total Budgetary Resources	**1,085,807**	**1,064,798**
STATUS OF BUDGETARY RESOURCES		
New Obligations and Upward Adjustments	1,062,577	949,796
Unobligated Balance, End of Year	23,230	115,002
Total Status of Budgetary Resources	**1,085,807**	**1,064,798**
OUTLAYS, NET		
Outlays, Gross	906,344	835,192
Actual Offsetting Collections	(891,140)	(876,283)
Net Outlays	**$ 15,204**	**$ (41,091**

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

Note 1. Summary of Significant Accounting Policies

A. Reporting Entity

VA was selected by the Office of Management and Budget in 1996 as one of six executive branch agencies to establish a franchise fund pilot program. In this program, entrepreneurial organizations or Enterprise Centers are authorized to sell common administrative support services to VA and other Government agencies and operate entirely on revenues earned from customers. Enterprise Centers receive no Federally appropriated funding. The VA Franchise Fund (Fund) was established under the authority of the Government Management Reform Act of 1994 and the VA and Housing and Urban Development and Independent Agencies Appropriations Act of 1997. In 2006, under Public Law 109-114, permanent status was conferred upon the VA Franchise Fund.

Created as a revolving fund, the VA Franchise Fund began providing services to VA and other Government agencies on a fee-for-service basis in 1997. By law, the business lines within the Fund can only sell to Federal entities. This organization accounted for its funds in seven activity centers (VA Enterprise Centers) and in one administrative organization: IT Infrastructure Operations, Debt Management Center, Financial Services Center, Law Enforcement Training Center, Security and Investigations Center, VA Records Center and Vault, Human Resources Enterprise Center and the Franchise Fund Oversight Office. The consolidated financial statements include the seven individual activity centers of the Fund. All material intrafund transactions have been eliminated.

B. Basis of Presentation

The VA Franchise Fund consolidated financial statements report all activities of VA Enterprise Centers. The consolidated financial statements differ from the financial reports used to monitor and control budgetary resources, but are prepared from the same books and records. The statements should be read with the understanding that the VA Franchise Fund is a component unit of the U.S. Government, which is a sovereign entity. VA Franchise Fund interacts with, and is dependent upon, the financial activities of the Federal Government. Therefore, the results of all financial decisions reflected in these consolidated financial statements are not the sole decisions of VA or VA Franchise Fund as a stand-alone entity. VA Franchise Fund's fiscal year end is September 30.

C. Basis of Accounting

The Franchise Fund's fiscal year (FY) 2018 and 2017 financial statements are prepared in accordance with generally accepted accounting principles (GAAP) as promulgated by the Federal Accounting Standards Advisory Board (FASAB) and the Office of Management and Budget's (OMB) Circular A-136, *Financial Reporting Requirements*, as revised. The Statement of Federal Financial Accounting Standards (SFFAS) 34, *The Hierarchy of Generally Accepted Accounting Principles, Including the Application of Standards Issued by the Financial Accounting Standards Board*, establishes a hierarchy of GAAP for Federal financial statements. The Franchise Fund's financial statements have been prepared to report the financial position, net cost of operations, changes in net position, and budgetary resources. The accompanying financial statements have been prepared on the accrual basis of accounting. Under the accrual method, revenues and other financing sources are recognized when earned and expenses are recognized when a liability is incurred, without regard to receipt or payment of cash.

D. Fund Balance with Treasury

The Department of the Treasury (Treasury) performs cash management activities for all Federal Government agencies. The fund balance with Treasury represents the right of the VA Franchise Fund to draw funds from the Treasury for allowable expenditures.

E. Accounts Receivable

Intragovernmental accounts receivable are from other Federal entities and are considered fully collectible; therefore, no allowance for uncollectible accounts is necessary.

Public accounts receivable are incurred when the Fund makes payments on behalf of their employees. Examples of this would be advances for Permanent Change of Station travel or advances for Federal Employees Health Benefits when employees are on leave without pay and their health benefits are paid to the health carriers. These receivables are considered fully collectible; therefore, no allowance for uncollectible accounts is necessary.

F. Property, Plant and Equipment

The majority of the general property, plant and equipment (PP&E) is used to provide common administrative services to the VA and other Federal entities and is valued at cost, including transfers from other Federal agencies. Major additions, replacements, and alterations are capitalized, whereas routine maintenance is expensed when incurred. Individual items are capitalized if the useful life is 2 years or more and the unit price is $1 million or greater. Buildings are depreciated on a straight-line basis over estimated useful lives of 25 to 40 years. Equipment is depreciated on a straight-line basis over its useful life, usually 5 to 20 years. Internal use software (IUS) is also subject to the $1,000,000 threshold for capital assets. The costs subject to capitalization are incurred during the software development phase. The capitalized costs are amortized on a straight-line basis, and the amortization term is in accordance with the planned life cycle established during the software's planning phase. The useful life in regards to capitalization of the IUS is determined on a per project basis, and amortize it over the useful life of 4 years or more, and consistent with the solution's longevity as limited by legal, regulatory, and/or contractual provisions. Preliminary design phase costs and post implementation costs are expensed as incurred.

Construction project costs are recorded in Construction Work-in-Process (WIP) accounts. The assets are transferred to either capitalized or non-capitalized PP&E, as appropriate, when placed in service. Construction projects completed in multiple phases are recorded as Construction WIP until the project phase is placed in service. Personal property and equipment that do not meet the capitalization criteria are expensed upon being placed in service.

Leasehold improvements and related depreciation are accounted for as Departmental assets. The Franchise Fund utilizes these assets in the production of revenue. Since the leasehold improvements are VA assets, they are recorded at the Departments threshold.

G. Other Assets

Other assets are generally made up of advances. There are three types of advances handled by the Fund. The first is when Treasury processes charges from other agencies to the Franchise Fund via the Intra-Governmental Payment and Collection System (IPAC). Charges are recorded as an advance until the applicable obligation is located and the charges can be transferred. These charges are for General Services Administration rent, Government Printing Office printing services, Federal Telecommunications Service, and motor pool.

The second type of advance is advances paid to employees for travel. This includes payment for both permanent change of station (PCS) and temporary duty (TDY) travel.

The third type of advance is set up when the purchase card payments are scheduled. Charges are then IPACed to the applicable agency to offset the advances.

H. Accounts Payable

Accounts payable are classified as either intragovernmental or public. Intragovernmental accounts payable consists of amounts owed to other Federal Government agencies. The remaining accounts payable consist of amounts due to the public. Accounts payable are amounts owed by the Fund for goods and services received, progress in contract performance, and rents due. Accounts payable do not include liabilities related to on-going continuous expenses such as employee's salaries, benefits, annuities for insurance programs, interest payable which are covered by other liabilities. When the Fund accepts title to goods, whether the goods are delivered or in transit, or incurs costs for services received, the Fund recognizes a liability for the unpaid amount of the goods and services. If invoices for those goods and services are not available when financial statements are prepared, the amounts owed are estimated. Intragovernmental and public accounts payable are covered by budgetary resources.

I. Other Liabilities

Other liabilities are classified as either intragovernmental or public. Intragovernmental liabilities arise from transactions between the Fund and Federal entities, whereas public liabilities arise from transactions between the Fund and non-Federal entities. Budgetary resources cover all other liabilities, both intragovernmental and public. All liabilities are current.

J. Revenues and Financing Sources

The Fund receives an annual apportionment that allows it to incur obligations and to recognize revenue from its customers on a "fee-for-service" basis. Revenue is recognized when earned. Expenses are recognized when incurred. All significant intra-entity balances and transactions have been eliminated in consolidation.

For financial reporting purposes under accrual accounting, operating expenses are recognized currently, while those for capital and other long-term assets are capitalized and depreciated and/or amortized over its useful life. Financing sources for these expenses, which derive from both current and prior year appropriations and operations, are also recognized this way.

K. Accounting for Intragovernmental Activities

In order to prepare reliable financial statements, transactions occurring among VA components must be eliminated. All significant intra-entity transactions were eliminated from the Fund's consolidated financial statements.

L. Annual, Sick and Other Types of Leave

Annual leave is accrued as it is earned and the accrual is reduced annually for actual leave taken. Each year, the accrued annual leave balance is adjusted to reflect the latest pay rates for leave that has been earned but not taken. Sick and other types of leave are expensed as taken.

M. Workers' Compensation Liability

The Federal Employees' Compensation Act (FECA) provides income and medical cost protection to covered Federal civilian employees injured on the job, employees who have incurred a work-related occupational disease, and beneficiaries of employees whose deaths are attributable to job-related injuries or occupational diseases. Claims incurred for benefits for VA Franchise Fund employees under FECA are administered by the Department of Labor (DOL) and are ultimately paid by VA Franchise Fund.

Workers' compensation comprises two components: (1) the accrued liability, which represents money owed by VA Franchise Fund to DOL for claims paid by DOL on behalf of VA Franchise Fund through the current fiscal year, and (2) the actuarial liability for compensation cases to be paid beyond the current year.

Future workers' compensation estimates are generated from an application of actuarial procedures developed by DOL to estimate the liability for FECA benefits. The liability for future workers' compensation benefits include the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases and for potential cases related to injuries incurred but not reported. The liability is determined by utilizing historical benefit payment patterns related to a period to estimate the ultimate payments related to that period.

N. Pension, Other Retirement Benefits, and Other Post-Employment Benefits

Each employing Federal agency is required to recognize its share of the cost and imputed financing of providing pension and postretirement health benefits and life insurance to its employees. Factors used in the calculation of these pensions and post-retirement health and life insurance benefit expenses are provided by the Office of Personnel Management (OPM) to each agency.

The Fund's employees are covered under the Civil Service Retirement System (CSRS) or the Federal Employees Retirement System (FERS); the Fund makes contributions according to both plan's requirements. CSRS and FERS are multiemployer plans administered by OPM. VA does not maintain or report information about the assets of the plans, nor does it report actuarial data for the accumulated plan benefits. That reporting is the responsibility of OPM.

O. Application of Critical Accounting Estimates

The financial statements are based on the selection of accounting policies and the application of significant accounting estimates, some of which require management to make significant assumptions. Further, the estimates are based on current conditions that may change in the future. Actual results could differ materially from the estimated amounts. The financial statements include information to assist in understanding the effect of changes in assumptions to the related information.

P. Commitments and Contingencies

VA is a party in various administrative proceedings, legal actions, and claims brought against it. In the opinion of VA Franchise Fund management and legal counsel, the ultimate resolutions of these proceedings, actions, and claims will not materially affect the financial position or results of VA Franchise Fund operations other than as disclosed in Note 9, Commitments and Contingencies.

Q. Subsequent Events

Subsequent events have been evaluated through the auditors' report date which is the date the financial statements were available to be issued, and management determined that there are no other items to disclose.

Note 2. Fund Balance with Treasury

The undisbursed account balance for the Fund is a revolving fund comprised of only entity assets. The funds available as of September 30,

	2018	2017
Fund Balance with Treasury	**$ 254,294**	**$ 269,498**

The Fund does not receive an appropriation from Congress. The Fund receives an annual apportionment that allows it to incur obligations and to recognize revenue from its customers on a "fee-for-service" basis.

Status of Fund Balance with Treasury

	2018	2017
Unobligated Apportionment		
Available	$ 23,230	$ 115,002
Obligated balance not yet Disbursed	$ 231,064	$ 154,496
Total Unexpended Apportionment	**$ 254,294**	**$ 269,498**

Note 3. Accounts Receivable

Intragovernmental accounts receivable consists of amounts due from the VA and other Federal agencies. No allowances for losses are required.

Public accounts receivable consists mainly of amounts due from VA employees. No allowance for losses is required, based on prior experience of collectibles.

Accounts Receivable as of September 30,

	2018	2017
Intragovernmental		
Accounts Receivable	$ 118,718	$ 88,818
Public		
Accounts Receivable	98	63
Total Accounts Receivable	**$ 118,816**	**$ 88,881**

Note 4. General Property, Plant and Equipment

General PP&E as of September 30, 2018:

	Acquisition Cost	Accumulated Depreciation	Net Book Value
Building	$ 19,416	$ (15,663)	$ 3,753
Work-In-Process	0		0
Structure	581	(228)	353
Furniture & Equipment	18,177	(6,273)	11,904
ADP Equipment	93,566	(70,180)	23,386
Capital Lease Equipment	2,119	(2,119)	0
Software	20,976	(15,672)	5,304
Software in Development	17,599	0	17,599
Leasehold Improvements	36,586	(15,441)	21,145
Total PP&E	**$ 209,020**	**$ (125,576)**	**$ 83,444**

General PP&E as of September 30, 2017:

	Acquisition Cost	Accumulated Depreciation	Net Book Value
Building	$ 18,273	$ (15,189)	$ 3,084
Work-In-Process	3,957		3,957
Structure	581	(198)	383
Furniture & Equipment	14,936	(5,455)	9,481
ADP Equipment	86,771	(62,262)	24,509
Capital Lease Equipment	2,119	(2,119)	0
Software	27,475	(24,553)	2,922
Software in Development	6,249	0	6,249
Leasehold Improvements	36,405	(21,760)	14,645
Total PP&E	**$ 196,766**	**$ 131,536)**	**$ 65,230**

Note 5. Other Assets

Other Assets as of September 30,

	2018	2017
Intragovernmental		
Advance Payment – Federal	$ 1,117	$ 0
Total Intragovernmental	**$ 1,117**	**$ 0**
Public		
Advances to Employees	$ 0	$ 0
Total Public	$ 0	$ 0
Total Other Assets	**$ 1,117**	**$ 0**

Note 6. Federal Employee Benefits

Imputed Expenses – Employee Benefits
For the Period ended September 30,

	2018	2017
Civil Service Retirement System	$ 1,221	$ 1,265
Federal Employees Retirement System	1,792	221
Federal Employee Health Benefits	7,237	5,672
Federal Employee Group Life Insurance	20	21
Total Imputed Expenses - Employee Benefits	**$ 10,270**	**$ 7,179**

Note 7. Other Liabilities

Budgetary resources fund all other liabilities, both intragovernmental and public. All liabilities are current.

Other Liabilities account balance as of September 30, 2018:

	FUNDED	UNFUNDED
Intragovernmental		
Accrued Expenses – Federal	$ 190	$ -
Payroll Taxes Payable	1,298	-
Advances – Federal	23,444	-
Total Intragovernmental Other Liabilities	**$ 24,932**	**$ -**
Public		
Payroll Taxes Payable	$ 4,724	$ -
Accrued Funded Annual Leave*	8,131	-
Capital Lease Liability	3	-
Total Other Public Liabilities	**$ 12,858**	**$ -**

Other Liabilities account balance as of September 30, 2017:

	FUNDED	UNFUNDED
Intragovernmental		
Accrued Expenses – Federal	$ 20	$ -
Payroll Taxes Payable	1,344	-
Advances – Federal	24,085	-
Total Intragovernmental Other Liabilities	**$ 25,450**	**$ -**
Public		
Payroll Taxes Payable	$ 4,899	$ -
Accrued Funded Annual Leave*	8,965	-
Capital Lease Liability	3	-
Total Other Public Liabilities	**$ 13,866**	**$ -**

*Annual leave is accrued when earned and is adjusted at the end of each reporting period to reflect current pay rates of cumulative leave earned but not taken. Sick and other types of leave are expensed as taken.

Note 8. Leases

The Franchise Fund has both capital leases and operating leases. The net capital lease liability is zero for both September 30, 2018 and September 30, 2017. The following is an analysis of the leased property under capital leases by major classes that is included in general PP&E as disclosed in Note 4.

CAPITAL LEASES

Capital Lease Assets - as of September 30, 2018	Cost	Accumulated Amortization	Net Book Value
Equipment	$2,119	$(2,119)	$0

Capital Lease Assets - as of September 30, 2017	Cost	Accumulated Amortization	Net Book Value
Equipment	$2,119	$(2,119)	$0

The Franchise Fund's FY 2018 operating lease costs were $10,964 for real property rentals and $244 for equipment rentals. The Franchise Fund's FY 2017 operating lease costs were $10,590 for real property rentals and $426 for equipment rentals. Operating leases consist of equipment and real property leases that are funded annually and expensed as incurred. Operating equipment leases generally consist of office equipment with terms of 5 years or less and level payments over the lease term. Operating real property leases generally consist of offices and administrative facilities that enable VA Franchise Fund Enterprise Centers to fulfill its mission.

Leases are executed by GSA on behalf of VA Franchise Fund. GSA charges rental rates for space that approximates commercial rental rates for similar properties. The terms of occupancy agreements (OAs) with GSA vary according to whether the underlying assets are owned directly by the Federal Government or rented by GSA from third-party commercial property owners.

Future commitments for real property and equipment operating leases are based on leases in effect as of September 30, 2018. VA Franchise Fund normally occupies leased real property for the entire initial lease term without exercising cancellation and termination options. The following chart represents the Franchise Fund's estimate for operating lease costs for the next 5 years, assuming a range of 3.0 to 3.1 percent annual increases in cost.

OPERATING LEASES

Fiscal Year	Percentage Increases	GSA OAs	Third-Party Direct Leases	Total Real Property
2019	3.0	$ 8,892	$2,652	$11,544
2020	3.1	9,168	2,734	11,902
2021	3.1	9,452	2,819	12,271
2022	3.1	9,745	2,906	12,651
2023	3.1	10,047	2,996	..13,043

Note 9. Intragovernmental Costs and Exchange Revenue

Cost and Exchange Revenue as of September 30,	2018	2017
Intragovernmental costs	$ 877,102	$ 845,327
Less: Earned Revenue - Intragovernmental	(909,965)	(863,903)
Net Intragovernmental Cost	(32,863)	(18,576)
Indirect Administrative Cost	7,643	7,133
Total Net Cost of Operations	**$ (25,220)**	**$ (11,443)**

Earned Revenue: Revenue earned by VA Franchise Fund (VAFF) for fees charged for services for the period ended September 30, 2018 was $909,965. Revenue earned by VAFF for fees charged for services for the period ended September 30, 2017 was $863,903.

Costs: By law, the VAFF, as an entity of the Department of Veterans Affairs (VA), provides centralized services to other VA entities and other government agencies. However, in certain cases, other VA entities and government agencies incur costs that are directly identifiable to VAFF operations. In accordance with Statement of Federal Financial Accounting Standards (SFFAS) No. 4, Managerial Cost Accounting, VAFF recognizes identified costs paid for by other agencies as expenses to VAFF.

Note 10. Disclosures Related to the Statement of Budgetary Resources

- **Apportionment Categories of Obligations Incurred**

Category A, Direct/Reimbursable, consists of amounts requested to be apportioned by each calendar quarter in the fiscal year. Category B, Direct/Reimbursable, consists of amounts requested to be apportioned on a basis other than calendar quarters, such as activities, projects, objects, or a combination of these categories. The VA Franchise Fund obligations are apportioned by activity.

Reimbursable Obligations as of September 30,

	2018	2017
Category B, Reimbursable Obligations	**$ 1,062,577**	**$ 949,796**

- **Undelivered Orders at the End of the Period**

For the period ended September 30, 2018 and 2017, budgetary resources obligated for undelivered orders are as follows:

		2018		2017
Paid Undelivered Orders Federal	$	1,117	$	309
Paid Undelivered Orders Non- Federal		0		2
Total Paid Undelivered Orders	$	1,117	$	311
Unpaid Undelivered Orders Federal		16,420		49,050
Unpaid Undelivered Orders Non-Federal		365,634		174,483
Total Undelivered Orders	**$**	**382,054**	**$**	**223,533**

- **Adjustments to Budgetary Resources and Prior Year Recoveries**

The Franchise Fund reported approximately $38M and $41M recoveries of prior year unpaid and paid obligations (recoveries) for fiscal years ended September 30, 2018 and 2017, respectively.

Note 11. Reconciliation of Net Cost of Operations to Budget

Statement of Federal Financial Accounting Standard 7 "requires a reconciliation of proprietary and budgetary information in a way that helps users relate the two." The standard states that "OMB will provide guidance regarding details of the display for the Statement of Financing, including whether it shall be presented as a basic financial statement or as a schedule in the notes to the basic financial statements."

Statement of Federal Financial Accounting Concept 2, Entity and Display, provides Concepts for Reconciling Budgetary and Financial Accounting by adding a category of financial information to further satisfy users' needs to understand "how information on the use of budgetary resources relates to information on the cost of program operations." The objective of this information is to provide an explanation of the differences between budgetary and financial (proprietary) accounting. This is accomplished by means of a reconciliation of budgetary obligations and non-budgetary resources available to the reporting entity with its net cost of operations.

FY 2018 Reconciliation of Net Cost of Operations to Budget

	2018	2017
Resources Used to Finance Activities:		
Budgetary Resources Obligated		
Obligations Incurred	$ 1,062,577	$ 949,796
Less: Spending Authority from Offsetting Collections and Adjustments	(970,805)	(908,682)
Net Obligations	91,772	41,114
Other Resources		
Transfers in/out	5,458	6,335
Imputed Financing from Costs Subsidies	10,270	7,179
Net Other Resources Used to Finance Activities	15,728	13,514
Total Resources Used to Finance Activities	107,500	54,628
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	(114,471)	(55,143)
Resources that Finance the Acquisition of Assets Property, Plant and Equipment	(36,505)	(27,343)
Resources that Fund Expenses Recognized in Prior Periods	(35)	(4)
Total Resources Used to Finance Items not Part of the Net Costs of Operations	(151,011)	(82,490)
Total Resources Used to Finance the Net Cost of Operations	(43,511)	(27,863)
Components Not Requiring or Generating Resources		
Depreciation and Amortization	14,804	14,653
Bad Debts	4	0
Loss on Disposition of Assets	3,487	1,916
Other	(4)	(148)
Total Components that Will Not Require or Generate Resources	18,291	16,420
Total Components that Will Not Require or Generate Resources in the Current Period	18,291	16,420
Net Cost of Operations	**$ (25,220)**	**$ (11,443)**

DEPARTMENT OF VETERANS AFFAIRS

Franchise Fund
ANNUAL REPORT

Contact the Department of Veterans Affairs for additional information on this report or download from the Web: www.va.gov/fund

Department of Veterans Affairs Franchise Fund Oversight Office 810 Vermont Ave, NW Washington, DC 20420

Debt Management Center

P.O.Box 11930 St. Paul, MN 55111
Phone: 612-713-6390
Fax: 612-970-5687
e-mail: dmc.ops@va.gov
Internet: www.va.gov/debtman

IT Infrastructure Operations

1615 Woodward Street
Austin, TX 78772
Phone: 512-326-6005
Fax: 512-326-6922
e-mail: 00b@va.gov

Financial Services Center

Business Management Section (104)
1615 Woodward Street
Austin, TX 78772
Phone: 512-460-5121
Fax: 512-460-5507
e-mail: vafscbusinessservices@va.gov
Internet: www.fsc.va.gov

Law Enforcement Training Center

2200 Fort Roots Drive, Building 104
North Little Rock, AR 72114
Phone: 501-257-4160
Fax: 501-257-4145
e-mail: james.ward4@va.gov
Internet: http://www.osp.va.gov/Law_Enforcement_Training_Center_LETC.asp

Records Center and Vault

1615 Woodward Street
Austin, TX 78772
Phone: 512-326-6576
Fax: 512-326-7442
e-mail: RCV BusinessOffice@va.gov
Internet: www.rcv.va.gov

Security and Investigations Center

2200 Fort Roots Drive, Building 192
North Little Rock, AR 72114
Phone: 501-257-4469/4490
Fax: 501-257-4018
e-mail: vhalitbackgroundinvestigations@va.gov
Internet: http://www.osp.va.gov/Security_and_Investigations_Center_FF.asp

Human Resource Enterprise Center

1100 1st Street NE
Washington, DC 20002
e-mail: Kathy.Biggs-Silver@va.gov
Internet: http://vaww.va.gov/FUND/index.asp