MISSION STATEMENT
The mission of the Bureau of Engraving and Printing is to design and manufacture high quality security documents that meet customer requirements for quality, quantity and performance, including counterfeit deterrence.

VISION STATEMENT
The Bureau of Engraving and Printing is a world-class securities printer providing our customers and the public superior products through excellence in manufacturing and technological innovation.

ON THE COVER
Depicted on the cover is the door to one of the Bureau of Engraving and Printing’s vaults. This vault has been in continuous use for over 90 years; the door weighs approximately 18 tons and takes two employees to operate.
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This past year has been filled with challenges and opportunities for me and the Bureau of Engraving and Printing. In January 2006, after 23 years of Federal government service, with the last 13 at the Bureau, I was honored to be appointed the 25th Director of the Bureau of Engraving and Printing. Under my tenure, I plan to intensify continuous improvement efforts throughout the organization in order to deliver safe and secure U.S. currency notes to the Nation. I am proud of what the Bureau has accomplished in the past, and I am committed to leading the organization to higher levels of excellence and customer satisfaction.

Following the successful issuance of the redesigned $50 note in 2004, a redesigned $10 note entered into circulation on March 2, 2006. The new $10 note includes subtle shades of orange, yellow, and red and incorporates state-of-the-art counterfeit security features that make it safer, smarter, and more secure. These new notes are part of the current multi-year initiative to implement the most ambitious currency redesign in U.S. history.

During 2006, the Bureau delivered 8.2 billion Federal Reserve notes to the Federal Reserve System and is scheduled to produce 9.1 billion in 2007. This year’s currency order was again fulfilled on schedule and at lower cost than anticipated.

The Bureau is committed to a strong, world-class environmental management program and has begun the process of becoming certified by the International Organization for Standardization (ISO 14001) for this program. ISO 14001 certification will serve as a strong indication of the Bureau’s commitment to sound environmental stewardship. The Bureau attained certification of its environmental management at its Western Currency Facility on October 2, 2006 and expects to successfully complete the process with the certification of its Washington facility in the spring of 2007.

At my direction, the Bureau undertook a functional review of its organizational structure in 2006. The review focused on identifying activities that could be combined, eliminated, or reengineered to improve organizational responsiveness, take advantage of synergies, and improve cost effectiveness. Based on the review, an organizational realignment was recently completed that supports more streamlined business processes and positions the organization to be more customer focused and responsive.

The performance and financial data presented in this report is complete and accurate as outlined in guidance available from the Office of Management and Budget. The Bureau regularly uses this financial and performance data for decision making. Consequently, every effort is made to ensure its accuracy and reliability.

Finally, I would like to express my appreciation to all the employees at the Bureau for their outstanding efforts this year. As we continue to redesign the Nation’s currency to enhance counterfeit deterrence and facilitate commerce, we have to ensure flawless execution in all that we do. The Bureau’s employees have always been its most important resource and I am confident they will continue to rise to the challenge of maintaining the Bureau’s reputation as the world’s premier government securities printer.

Larry Felix, Director
I am pleased to present the Bureau of Engraving and Printing’s Chief Financial Officer Performance and Accountability Report for 2006. This report reflects a long tradition of strong financial management and timely financial reporting at the Bureau. This high standard for the Bureau’s financial management and reporting was recognized in 2006 when the Bureau received, for the second consecutive year, an unqualified opinion on its internal control over financial reporting. In addition, for the 22nd consecutive year, the Bureau received an unqualified opinion on its financial statements from an independent certified public accounting firm.

The financial statements and annual audit are important elements in the stewardship of the Bureau’s revolving fund. The annual audit and opinion on internal control over financial reporting help to ensure the integrity of the revolving fund and the reliability of financial data used for managerial decision-making.

In 2006, the Bureau delivered 8.2 billion currency notes to the Federal Reserve. This resulted in revenue of $477 million and an excess of expenses over revenues of $8.6 million. The excess of expenses over revenues was planned and funded out of working capital.

During the year, the Bureau continued to focus on improving productivity, reducing costs and streamlining operations. Overall program performance was favorable. Direct manufacturing costs for currency were below established standards. In particular, the inaugural production run of the new $10 note was highly successful with actual spoilage more than 20% below standard and manufacturing costs $2 million under budget.

In 2006, the Bureau began a multi-year recapitalization of the Washington, DC facility. This investment initiative features the replacement of existing currency production lines with state-of-the-art intaglio printing presses, automated electronic inspection, and finishing systems that will provide for a 50-subject (note) sheet format compared to the current 32-subject format. Successful implementation of this advanced technology will improve productivity and provide needed capabilities to produce increasingly more complex currency note designs.

As the Bureau prepares for the future, we will continue to focus on our commitment to product quality, superior customer service and efficient stewardship of resources so that we can continue to effectively meet the needs of the American public. The Bureau has positioned itself to meet these needs both from an operational and financial management perspective. The Bureau has the financial resources necessary to invest in its employees to maintain a talented and up-to-date workforce, and a well-disciplined capital investment strategy to enhance product quality, promote counterfeit deterrence, and ensure the cost effectiveness of the manufacturing processes.

Leonard R. Olijar
Chief Financial Officer

Leonard R. Olijar
Chief Financial Officer
Treasury Secretary Henry M. Paulson, Jr. visits the Bureau for the unveiling of the first paper currency with his signature.

Clockwise from top left:

a) The Bureau welcomes the 74th Secretary of the Treasury, Henry M. Paulson, Jr., on his first visit.

b) Robert Phelan, Office of Currency Production, and Secretary Paulson examining a finished sheet of currency bearing the Secretary’s signature.

c) Secretary Paulson holds finished notes.
In 2006, the Bureau of Engraving and Printing focused its resources on producing the most secure currency for the Nation. The redesigned $10 note was introduced to the public in late 2005 and put into circulation in early 2006. Work is continuing on the development and identification of new counterfeit deterrent features for the redesign of the $5 and $100 notes.

Additional financial and operational highlights for 2006 include:

- Henry M. Paulson, Jr. was sworn in as the 74th Secretary of the Department of the Treasury on July 10, 2006.
- In 2006, the Bureau began a multi-year recapitalization of its Washington, DC facility. This initiative will improve productivity and provide needed capabilities to produce increasingly more complex currency note designs.
- Direct manufacturing costs for currency were below established standards. In particular, the inaugural production run of the new $10 note was highly successful with actual spoilage more than 20% below standard and manufacturing costs $2 million under budget.
- The Bureau received an unqualified opinion on its internal control over financial reporting in 2006, and, for the 22nd consecutive year, the Bureau received an unqualified opinion on its financial statements.
- Lost workdays declined by 17%. Most significantly, the Bureau’s rates are below historical average rates for the private printing industry.

In 2006, the Bureau of Engraving and Printing delivered 8.2 billion notes to the Federal Reserve Banks. The Federal Reserve has ordered 9.1 billion notes for delivery in FY 2007.

The Bureau undertook a functional review of its organizational structure in 2006. The goal of the review was to streamline the organization by grouping similar functions to benefit from synergies, improve efficiency, reduce costs, improve response time, and facilitate currency redesign efforts.

The Bureau’s quality management system was audited in 2006 by its ISO registrar and was re-certified as ISO 9001 compliant through 2009.

The Bureau began to pursue ISO 14001 certification for its environmental management systems to institutionalize its commitment to sound environmental stewardship and employee health and safety. Certification is expected in 2007.

The Bureau sought designation as an Occupational Safety and Health Administration (OSHA) Voluntary Protection Program (VPP) site. VPP designation is OSHA’s official recognition of the outstanding efforts of employers and employees who have achieved exemplary occupational safety and health.

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<tr>
<th>(All Dollars in Millions)</th>
<th>2005</th>
<th>2006</th>
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<td>$477</td>
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<tr>
<td>Capital Investment</td>
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<tr>
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<td>Total Assets</td>
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<td>$553.5</td>
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<td>Excess of Revenue over Expenses</td>
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<td>($8.6)</td>
</tr>
<tr>
<td>Federal Reserve Notes Delivered (Billions)</td>
<td>8.5</td>
<td>8.2</td>
</tr>
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</table>

2006 CFO Report
Bureau of Engraving and Printing security through the years.

Despite all the technological advances during more than a century of currency production by the Bureau, there is no substitute for the dedicated service of the men and women who have protected the Nation’s currency through the years.

Current BEP Police Officers (from left to right): Rakeem Johnson, Raquel Welch, Sonepheth Sombat and Aileen Joy.
The mission of the Bureau of Engraving and Printing is to design and manufacture high quality security documents that deter counterfeiting and meet customer requirements for quality, quantity, and performance.

The Bureau of Engraving and Printing began printing currency in 1862. The Bureau operates on the basis of authority conferred upon the Secretary of the Treasury by 31 U.S.C. 321(a) (4) to engrave and print currency and other security documents. Operations are financed by a means of a revolving fund established in 1950 by Public Law 81-656. This fund is reimbursed through product sales for direct and indirect costs of operations including administrative expenses. In 1977, Public Law 95-81 authorized the Bureau to include an amount sufficient to fund capital investment and to meet working capital requirements in the prices charged for products. This eliminated the need for appropriations from Congress.

The Bureau produces U.S. currency and many other security documents issued by the federal government. Other activities at the Bureau include engraving plates and dies; manufacturing certain inks used to print security products; purchasing materials, supplies and equipment; and storing and delivering products in accordance with requirements of customers. In addition, the Bureau provides technical assistance and advice to other federal agencies in the design and production of documents, which, because of their innate value or other characteristics, require counterfeit deterrence. The Bureau audits cash destruction and unfit currency operations at Federal Reserve Banks, and is responsible for the accountability and destruction of internally generated security waste products. As a service to the public, the Bureau also processes claims for the redemption of mutilated paper currency.

The Bureau uses a standard cost accounting system to determine product prices. Prices are formulated from cost projections using historical cost data and projections for material, labor and benefits, depreciation, and overhead costs. The billing rates reflect the total estimated cost to fund operations plus a capital surcharge, if necessary.

The capital surcharge is determined by evaluating the estimated cash flows and depreciation necessary to:

- Provide the working capital needed to fund day-to-day operations in the forthcoming year,
- Provide the necessary cash reserve to ensure continuity of operations in the event of an emergency, since the Bureau does not have borrowing authority, and
- Meet the Bureau’s projected capital investments for the forthcoming year (or years in the case of large equipment purchases).

A positive surcharge would result when net working capital requirements are projected to exceed depreciation (a non-cash expense), resulting in increased billing rates to accumulate required capital funds. Conversely, no accumulation of capital funds is necessary when net working capital requirements are projected to be less than depreciation. In this case, the billing rate would include a negative surcharge, which would result in an excess of expenses over revenues (a planned loss).

The Bureau occupies three government-owned facilities. The Main and Annex buildings, located in
Washington, DC, produce Federal Reserve Notes and other security products. The Western Currency Facility, located in Fort Worth, Texas, produces Federal Reserve Notes. The Main Building became operational in 1914, the Annex Building in 1938, and the Western Currency Facility began operations in 1991. The Western Currency Facility was constructed to provide increased production capacity, reduce transportation costs, and enhance the Nation’s emergency preparedness.

In addition to housing production facilities, free tours of currency operations are offered to the general public in both Washington, DC and Fort Worth, TX. The tours include Visitor Centers with currency manufacturing displays, interactive kiosks and other information about the history of the Nation’s currency. The Visitor Centers also sell uncut sheets of currency, other collectibles, and engravings. In addition to the on-site sales centers, these items are available through mail order and the Bureau’s Internet site: www.moneyfactory.gov.

**Manufacturing**

In the last three years, the Bureau has redesigned and issued new $10, $20, and $50 notes to the Federal Reserve Banks. The new designs are part of the U.S. government’s ongoing efforts to maintain the integrity of U.S. currency. Work is continuing on the redesign of the $5 and $100 notes and the development of additional counterfeit deterrent features that may be used. The redesigned $5 note will begin circulating in spring 2008 and the new $100 note is currently scheduled for release in 2009.

During 2006, the Bureau delivered 8.2 billion Federal Reserve Notes to the Federal Reserve System. The Washington and Fort Worth facilities both produced the redesigned notes in 2006 and delivered 4.5 billion Federal Reserve Notes, respectively. For 2007, the Federal Reserve System has ordered 9.1 billion Federal Reserve Notes.

Manufacturing

In keeping with its tradition of product innovation and production efficiency, the Bureau took delivery of two new sheet-fed state-of-the-art intaglio printing presses. These presses have an indirect inking system and an automated electronic inspection system. Successful implementation of this advanced technology will improve productivity, reduce the Bureau’s environmental impact, and provide the ability to produce increasingly more complex currency note designs.

The Bureau’s quality management system for the production of U.S. currency has been registered as ISO 9001 compliant for the past five years. During 2006, the Bureau pursued a companion effort to obtain ISO 14001 certification for its environmental management systems (EMS) at both the Washington and Fort Worth facilities. The ISO certifications are indicative of the Bureau’s commitment to continuous process improvement and world-class management practices.
Information Technology

In 2006, the Bureau’s Chief Information Officer (CIO) continued to emphasize increased security and accountability, standardization of Bureau hardware, software, and information technology (IT) related processes and enhanced governance of the IT program and resources.

Maintaining a robust and comprehensive cyber security posture is a top priority. All of the Bureau’s systems have been evaluated, certified and accredited to meet requirements established by Federal policy. The Bureau has acquired and implemented technologies to encrypt laptop computers and removable hard drives to prevent information from being compromised, should an asset be lost or stolen. Patch management and active vulnerability scanning and feedback programs have been established that have resulted in a more resilient operational capability and a reduction in vulnerabilities.

During the year, the CIO Directorate has worked closely with the Management Directorate to support Treasury’s implementation of Homeland Security Presidential Directive-12. The CIO Directorate continues to refine policy and procedures for ensuring the adequacy of management controls throughout the life cycle of hardware and software, including contract and full time equivalent support for the implementation of National Institute of Standards and Technology (NIST) Special Publication (SP) 800-53 and 800-53A (management, operational, and technical controls for IT systems).

Also during 2006, the CIO participated in a number of reviews of financial, Federal Information Security Management Act (FISMA), and support IT systems as the Bureau continues to apply Sarbanes-Oxley Act Section 404 and Federal Information System Controls Audit Manual (FISCAM) audit standards in support of the annual audited financial statements. The CIO Directorate continues to be an active participant in Department of the Treasury Critical Infrastructure Protection Planning efforts, including testing of Continuity of Operation Planning (COOP) responses through Government- and Treasury-wide exercises and through biannual tests of the COOP plans for the Bureau’s mainframe computer, enterprise management information system, and public sales support systems.

As part of the Bureau’s emphasis on governance, configuration management (CM) policy and processes continue to mature and the implementation of CM software is progressing through application to the network, having been implemented for the mainframe computer. This software provides detailed tracking of software, hardware, and system configuration changes, as well as the reasons for and impact of these changes.

Organization

The Bureau’s executive structure consists of the Bureau Director, six Associate Directors, and a Chief Counsel. The executive committee structure includes an Executive Committee, the Capital Investment Committee and various planning committees and subcommittees. The planning committees and subcommittees are composed of a cross-section of Bureau senior and mid-level managers that represent diverse organizational units. By cutting across organizational lines, these groups serve to promote effective communication and participative, proactive management.

Staffing (FTE) by Function
Banknote 2006 Conference

Clockwise from top left:
- a) The Bureau welcomes the attendees of the Banknote 2006 Conference.
- b) Conference attendees inspect finished currency.
- c) Edward Rizzo, Office of Engraving, shows engraved plates to Conference attendees.
In the past three years the BEP has redesigned the $10, $20, and $50 notes. The redesign of a currency note is a joint effort involving input from the Federal Reserve, U.S. Secret Service, and the U.S. Department of the Treasury.

The Bureau continues to work on the development of new counterfeit deterrent features and the redesign of the $5 and $100 notes. The redesigned $5 note will begin circulating in spring 2008 and the new $100 note is scheduled to begin circulating in 2009.

The continued redesign of U.S. currency is an ongoing effort to stay ahead of the technological advances available to counterfeiters. Counterfeiting of U.S. currency has been kept at low levels through a combination of improvements in security features, aggressive law enforcement, and education to inform the public of the authentication features in use.

Some of the more prominent changes resulting from redesign efforts include subtle background colors and images of American icons. The use of color and images adds complexity to the note making counterfeiting more difficult.

The Bureau has continued to incorporate three basic counterfeit deterrent features into the redesign of currency notes:

The first one is the watermark, which is a portrait that can be seen from both sides of the note when held up to a light.

The second feature is the security thread which runs vertically on the note and can be seen from both sides of the note. It glows a denomination specific color when held under ultraviolet light.

The third feature is an improved color-shifting ink which is more dramatic and easier to see on the new design notes.

Because the improved security features in the redesigned currency are more effective only if the public knows about and uses them, a broad public education program is an integral part of the redesign effort. This program ensures that people all over the world know that the new currency is coming, and helps them to recognize and use the security features. With over $750 billion in circulation world wide, educating people is crucial to counterfeit deterrence and a major focus of the counterfeit deterrence effort.
The mission of the Bureau of Engraving and Printing is to design and manufacture high quality security documents that meet customer requirements for quality, quantity and performance, including counterfeit deterrence.

The mission of the CFO Directorate is to maintain the integrity of the Bureau's revolving fund, provide the financial resources necessary to meet customer requirements, and oversee management control functions and the mutilated currency redemption program.

The mission of the ECF is to assure the manufacturing of all government security documents in a cost-effective and efficient manner that satisfies the needs of the customer, and to provide a safe and secure working environment for employees in the Washington, DC facility.

The mission of the WCF is to assure the manufacturing of all government security documents in a cost-effective and efficient manner that satisfies the needs of the customer, and to provide a safe and secure working environment for employees in the Fort Worth, Texas facility.

The mission of the Management Directorate is to provide the highest quality Security, Human Resources, Labor Relations, Procurement and Administrative Services in support of the overall Bureau mission.

The mission of the Technology Directorate is to support the production of United States currency and other government securities by incorporating new covert features that prevent counterfeiting, by developing new production processes that enhance the quality and production of securities, by providing technical support to the production process, and by providing facility support and maintenance.

The mission of the Office of the Chief Counsel is to provide the highest quality legal services in support of the overall Bureau mission.
Lost Workdays declined by 17%. Most significantly, the Bureau’s rates are below historical average rates for the private printing industry.

In addition, the Bureau’s rates also exceeded the injury and illness goals set for all Department of Treasury Bureaus under President Bush’s Safety, Health, and Return to Employment (SHARE) initiative.

BEP’s on-line health and safety training system was highly successful with all employees completing 100% of the required OSHA and Environmental Protection Agency (EPA) courses.

With the retooling for 50 subject sheet production, the Bureau purchased the only intaglio presses in the world that are equipped with solvent and ink vapor capture systems that will help prevent employee exposure to these airborne materials.

Protecting the Environment

The Bureau is committed to a strong, world-class environmental management program and has begun the process of becoming ISO 14001 certified. ISO 14001 certification will serve as a strong indication of the Bureau’s commitment to sound environmental stewardship. An important part of the Bureau’s Environmental Management System is a series of Technical Work Groups (TWG) that include both labor

Improving Worker Health and Safety

The Bureau continues its sharp focus on reducing injuries, illnesses, and lost workdays. The Joint Occupational Safety, Health, and Environment Committee (JOSHEC) successfully transformed input and ideas from the labor force into risk-reducing solutions, such as, designing and fabricating material handling equipment, integrating customized aerators joggers, and improving employee health care delivery. The Bureau’s injury prevention efforts in 2006 again resulted in a safer, more healthful workplace, as indicated by the following year-end results:

In order to demonstrate its commitment to EHS excellence, the Bureau also continues to pursue ISO 14001 registry for its environmental management system and designation as an Occupational Safety and Health Administration (OSHA) Voluntary Protection Program (VPP) site. In the coming year, the Bureau is on track to achieve ISO 14001 registry, and expects to receive OSHA VPP designation.

<table>
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<tr>
<th>Year</th>
<th>Lost Work Days</th>
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<tr>
<td>2002</td>
<td>983</td>
</tr>
<tr>
<td>2003</td>
<td>672</td>
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<td>2006</td>
<td>385</td>
</tr>
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</table>
and management representatives. These TWGs have worked diligently to identify the Bureau’s significant EHS aspects, analyzing impacts, and implementing operational controls. Specific accomplishments include the following:

- The wiper solution recycling TWG at the Eastern Currency Facility identified the technology that will be sought to recycle wastewater, reduce chemicals used in the pretreatment process, reduce the amount of wastewater, and reduce the amount of wipe solution manufactured.

- The Bureau installed a solvent recycle unit at the Western Currency Facility to reduce solvent waste. As a result, no solvent waste was collected and shipped in 2006, compared to eighteen drums that were collected and shipped in 2005.

- The Plate Making TWG is researching technologies to replace chrome in the plating process.

- The use of low volatile organic compound (VOC) water based cleaners during the production process has allowed the Bureau to request a modification of the Title V permit to discontinue the use of the VOC control system for these presses.

- The new 50-subject sheet presses are designed to consume 30% - 50% less ink, which will result in a significant reduction in air emissions.

- The Bureau’s Western Currency Facility has completed the development of an Integrated Contingency Plan and conducted field-training exercises for medical emergencies and chemical spills.

- The Bureau has established job performance standards relating to environment, health, and safety (EHS) for managers and supervisors, and has proposed the development of job performance standards for non-managers.

Employee Recognition Awards

Management support for employee involvement in the EHS process was evident in 2006 as the Bureau’s Greenback and BSAFE Awards were given to six employees. Nominations are made to the JOSHEC for a quarterly and annual winner in each category. The Annual Award winners were as follows:

**BSAFE Award:** Kenneth Brooks, from the Office of Currency Production received the 2006 BSAFE Award for identifying the need for several design improvements to roller carts used during production. The new design has a lower center of gravity and is more stable. As material handling is the leading source of occupational injuries at BEP, this may significantly contribute to a reduction of occupational injuries.

**Greenback Award:** Andrew Jones, Sheldon Turner, Joseph Hicks, Ian Timoll and Hines Jackson of the Office of Facilities Support received the 2006 Greenback Award. These employees are members of an Environmental Management System work group created to identify and reduce environment, safety, and health impacts to the work environment. They received the award for their suggestion to crush burned out fluorescent light tubes and recycle them (due to a small amount of mercury in each bulb) rather than disposing of them as hazardous waste.
Resource Management: Manage Bureau resources to increase internal efficiency and effectiveness in support of the other strategic goals.

The Bureau of Engraving and Printing is the Government’s security printer. Its customers and stakeholders expect the highest degree of security in its products. The Bureau seeks to maintain the highest levels of security by incorporating counterfeit deterrent features into currency as well as maintaining a secure physical environment at its two facilities.

The Bureau also provides services directly to the public. The Bureau processes claims for redemption of damaged paper currency at no cost to the public. The Bureau also offers free public tours of its facilities. The public tour at the Western Currency Facility in Fort Worth, TX began in 2004. The tour of the Bureau’s Washington, DC facility and the Visitor’s Center are among the most popular attractions in the Nation’s Capital.

While manufacturing currency and other printed securities is the core business of the Bureau, the production operations are highly dependent on the effectiveness of support processes such as security, procurement, information systems, financial management, product accountability, human resources management, engineering, research, product development, and maintenance. Only when these processes work in concert can the Bureau be responsive to the needs of its customers.

The Bureau has identified five goals in its Strategic Plan that focus on investment in people, products and processes.

Customer Satisfaction: Satisfy the Federal Reserve Board and the public by providing responsive service and quality products.

Quality Manufacturing: Manufacture state-of-the-art currency of consistently high quality while improving productivity and cost performance.

Counterfeit Deterrence: Produce state-of-the-art currency that deters counterfeiting, contributes to public confidence, facilitates daily commerce and extends the useful life of notes in circulation.

Security and Accountability: Ensure an environment of comprehensive security and accountability for the Bureau’s personnel, facilities and products.

The vision guiding the Bureau’s Strategic Plan is to be “a world-class securities printer providing customers and the public superior products through excellence in manufacturing and technological innovation.” A copy of the Bureau’s current Strategic Plan can be viewed online by clicking “About the Bureau” on the Bureau’s web site: www.moneyfactory.gov. An executive level working group has begun to develop a new five year Strategic Plan that will be completed in 2007.

STRATEGIC PLAN
The Bureau of Engraving and Printing’s Community Outreach Program partners with community schools in the Washington, DC and Fort Worth, TX areas

During the 2006 school year, the Bureau donated surplus computers to Paint Branch Elementary School, located in College Park, Maryland and Diamond Hill-Jarvis High School in Fort Worth, Texas.

Clockwise from top left:
a) from left to right: Paint Branch Elem. Principal Edwin Saunders, Paint Branch Elem. Vice Principal April Morris, BEP Director Larry Felix and BEP Joint Labor Council Chairman Carlton Steward
b) Director Felix assists a young student in the school computer center.
c) from left to right: Former DHJHS Principal Dr. Juanita Ornelas, EEO Assistant Paula Rathers and Chief of the Bureau Resolution Center, Arthur Hicks. The Bureau received the Golden Achievement Award for Partnership Excellence from the Fort Worth Independent School District in recognition of its donation of surplus computers.
Ongoing efforts to improve internal controls include compliance reviews and an active internal control awareness program. The Bureau’s Compliance Review Teams (CRT) in both facilities promote compliance with Bureau operating policies and procedures by performing unannounced reviews in production, storage, and off-line components that have custody of security items. During 2006, the CRTs performed 146 unannounced reviews. The results of the reviews were reported to office chiefs, supervisors and managers responsible for enforcing policies and procedures, and implementing corrective actions.

The Internal Control Awareness Program is used to promote the visibility and understanding of internal control issues, objectives, and requirements. Internal review personnel conduct management and organizational reviews at both facilities to strengthen the Bureau’s internal controls, ensure compliance with existing policies and procedures, and safeguard Bureau assets. The Bureau’s quality management system for the production of U.S. currency has been registered as ISO 9001 compliant for five years. The internal review staffs support the maintenance and continuous improvement of the Bureau’s quality management system by conducting internal quality audits throughout the Bureau.

The Federal Managers’ Financial Integrity Act (FMFIA), which was passed in 1982, requires agencies to perform regular evaluations of internal controls and financial management systems to protect against fraud, waste, and abuse. The subsequent passage of the Chief Financial Officers Act, the Federal Financial Management Improvement Act, and the Sarbanes-Oxley Act of 2002 further increased the government’s internal control requirements.

The Bureau has a history of strong internal controls and an aggressive monitoring program. Key elements of this program include comprehensive financial management controls, personnel security controls, production and quality controls, computer security and information resources management programs, and strong physical security and product accountability functions to safeguard products and assets. The Bureau’s Strategic Plan reflects this emphasis. Security, accountability, and resource management are major strategic goals.

To enhance product accountability, the Bureau maintains an Accountability Help Desk at its facilities in Washington, DC and Fort Worth, Texas. The Help Desks are staffed with personnel knowledgeable in all aspects of the Bureau’s accountability system. They provide training and day-to-day assistance to accountability system users to prevent, minimize, or resolve product accountability issues. In addition, they review and update existing accountability procedures and reports to provide the controls needed to properly track and account for Bureau securities.

Raymond Sheriff, Office of Currency Production, performing a quality inspection on a sheet of currency.
The Bureau’s Internal Control Policy Committee (Committee) provides overall guidance and coordination to the internal control program and fosters a management environment in which accountability for results and cost effective controls are maintained to ensure the reliability of financial reporting, effectiveness of operations, and compliance with applicable laws and regulations. The Committee is comprised of senior level executives and is chaired by the Chief Financial Officer.

The accompanying financial statements and annual audit are important elements in the stewardship of the Bureau’s revolving fund. For the 22nd consecutive year, the Bureau has received an unqualified opinion on its financial statements from an independent, certified public accounting firm. The Bureau also received an unqualified opinion from the auditors on management’s assertion that the Bureau maintained effective internal control over financial reporting as of September 30, 2006, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO Framework) and the requirements of Appendix A of Office of Management and Budget Circular A-123, “Management’s Responsibility for Internal Control.” The unqualified audit opinion on the financial statements, the unqualified opinion on the internal control over financial reporting, and the FMFIA review process ensure the integrity of the revolving fund and the reliability of financial data used for managerial decision-making. In addition to the annual audit of the Bureau’s financial condition, OMB’s Program Assessment Rating Tool was used to evaluate the Bureau’s currency manufacturing, and protection and accountability programs to ensure they were functioning as intended and performance information was reliable.

Despite the Bureau’s strong organizational emphasis on controls, a suspected theft was detected at the Washington, DC Facility. The theft involved partially printed $100 currency sheets, which had not been overprinted with serial numbers or the Treasury seal. The theft was investigated by the Bureau’s Office of Security, the Department of the Treasury Office of Inspector General, the United States Secret Service,
and the Federal Bureau of Investigation. During the course of the investigation, it was determined that a Bureau employee was responsible for the theft. The employee was charged with theft of government property in the U.S. District Court in Washington, DC, and subsequently plead guilty to the charge. The employee is scheduled to be sentenced in early 2007.

In 2006, the Bureau’s Chief Information Officer (CIO) continued to emphasize increased security and accountability, standardization of Bureau hardware, software, and information technology (IT) related processes and enhanced governance of the IT program and resources. The Bureau continued to refine its Enterprise Architecture not only to address Federal Enterprise Architecture reference models, but also to address the specific needs of the Bureau relative to the documentation and modeling of manufacturing and administrative processes, legacy asset portfolios, and the development of performance metrics associated with assets included in legacy portfolios. Analysis of these processes has led to the identification and documentation of the Bureau’s “to-be” architecture. This architecture is also in use for the review of current and proposed IT assets.

To protect data, the Bureau has acquired technologies to encrypt laptop computers and removable hard drives. During the year, the CIO Directorate worked closely with the Management Directorate to support the Department of the Treasury’s implementation of Homeland Security Presidential Directive-12 (HSPD-12), and provide resources as well as policy and other support for HSPD-12 Working Groups and Treasury decision-making bodies.

Also during 2006, the CIO participated in a number of reviews of financial, Federal Information Security Management Act (FISMA), and support IT systems as the Bureau continues to apply Sarbanes-Oxley Act Section 404 and the Government Accountability Office’s Federal Information System Controls Audit Manual (FISCAM) standards in support of the annual audited financial statements. The CIO Directorate
continue to mature and the implementation of CM software is progressing through application to the network, having been implemented, certified, and accredited for the mainframe computer.

The Bureau’s enhanced Capital Planning and Investment Control Process has been implemented, and includes both IT and non-IT investment review committees. Business cases are routed through IT Security and Enterprise Architecture for scoring and commentary prior to final committee vote, as well as through Technical Security as appropriate.

As part of the Bureau’s emphasis on governance, configuration management (CM) policy and processes continues to be an active participant to Department of the Treasury Critical Infrastructure Protection Planning efforts, including testing of Continuity of Operations Planning (COOP) responses through government and Treasury-wide exercises and through biannual tests of the COOP plans for the Bureau’s mainframe computer, enterprise management information system, and public sales support systems.

Bureau Police Officers Sedley Randolph (left) and Charles Knicly (right) on patrol around the Washington, DC Facility perimeter.
Summary of Office of Inspector General and Government Accountability Office Audits

The Bureau began 2006 with seven open audit recommendations. Six of these recommendations were issued by the Office of Inspector General (OIG), and one was issued by the Government Accountability Office. These recommendations pertained to program and contract issues. During 2006, the Bureau received nine additional recommendations in four OIG audit reports. Eight recommendations were the result of OIG initiated audits of the Bureau’s currency billing rates, internal controls at the Western Currency Facility, and its review of the certified public accounting firm’s audit of the Bureau’s 2005/2004 financial statements. One recommendation resulted from an audit requested by a contracting officer and pertained to a contract issue. Four recommendations from the contract-type audit reports were implemented or addressed in 2006, and resulted in monetary benefits of about $9,985,000. In addition, seven recommendations from program-type audit reports were implemented or addressed in 2006. The remaining recommendations will be addressed as appropriate.
Visiting the Bureau’s Western Currency Facility

Clockwise from top left:

a) Visitors board the tour bus at the Bureau’s Western Currency Facility in Fort Worth, TX.
b) An engraver discusses the skills required to engrave a plate with visitors as one of the “living” exhibits of the Western Currency Facility tour.
c) Young visitors measure their height in currency at the exhibit, “How Tall are You Worth?”
In addition to the production of currency, the Bureau has many high-value items that are used for various purposes, such as research, product testing and historical reference. Consequently, the Bureau of Engraving and Printing has a unique fiduciary responsibility to the American public with respect to the custody and safeguarding of its assets and high-value items.

Currency products and other items used in test, experimental, research and other off-line activities normally are expensed immediately and are not carried as assets in the Bureau’s financial statements. While the costs expensed may be immaterial to the financial statements, many of these items have high intrinsic value. Therefore, the Bureau ensures that adequate controls are in place to properly safeguard these items. The Bureau also has display areas at each of its facilities and maintains historical collections at its headquarters in Washington, DC. The displays and historical collections include valuable artifacts related to currency and the former postage stamp operations, as well as other securities produced by the Bureau. While these collections are not included in the inventory balances as reported in the financial statements, appropriate custodial records and controls are maintained. Physical inventories are performed regularly to ensure accountability for these collections.

Although the Bureau does not hold title to any land or facilities, it maintains custodial control over the buildings occupied in Washington, DC and Fort Worth, Texas. In 1999, the Bureau began a multi-year project to substantially renovate the buildings in Washington, DC. This renovation includes roof replacement, and power system upgrades, as well as significant maintenance to the buildings’ exteriors and ventilation systems. In 2003, an expansion of the production area was completed in Fort Worth, Texas and a public tour opened in 2004.

In order to effectively manage its fiduciary and custodial responsibilities, the Bureau has implemented effective internal control and security systems. To ensure that these systems are functioning properly, management has institutionalized an organizational focus on the safeguarding and accountability of all assets. This focus is reflected in the Bureau’s organizational structure. Reporting to the Associate Director (Chief Financial Officer), who has oversight responsibility with respect to internal controls, is the Office of Management Control. This office evaluates and monitors internal control systems and maintains a comprehensive product accountability system. Also, reporting to the Associate Director (Chief Financial Officer) is an

Pressman Glenn Walker and Don Fravel of the Bureau’s Special Security Products Division monitoring the ink quality on the Bureau’s six-color offset printing press. This press is used to produce security products and forms for other agencies.
Assistant Chief Financial Officer at the Western Currency Facility who is responsible for monitoring internal control responsibilities at that facility. The Office of Security, which reports to the Associate Director (Management), plans, administers and monitors the Bureau’s security programs. These programs include personnel, physical and operational security as well as securities destruction. Through this structure, individual unit managers are held accountable and responsible for maintaining proper custody and safeguarding of all assets under their control. To further reinforce the internal control and security structure, a security and internal control element is included in each employee’s performance plan. Employees are rated annually regarding their performance with respect to this element.

Although the Bureau has a strong organizational emphasis on controls, a suspected theft of partially printed $100 currency sheets was detected and reported in 2006. These sheets had not been overprinted with serial numbers or the Treasury seal. The theft was investigated by the Bureau’s Office of Security, the Department of the Treasury Office of Inspector General, the United States Secret Service, and the Federal Bureau of Investigation.

from left to right:
a) The inside “face” of the vault depicted on the front cover of the Annual Report. (Foreman Aaron Alexander, Office of Currency Production).
b) Another view of the same vault door depicted on the front cover of the Annual Report (Currency Controller Verifier Pederick Knight, Office of Currency Production).
The Bureau measures the efficiency and effectiveness of its overall organizational performance by using program performance measures. Standards are developed annually by senior executive staff based on past year's performance, contracted price factors, and anticipated productivity improvement. Actual performance against standard depends on the Bureau’s ability to meet annual spoilage, efficiency and capacity utilization goals estimated for currency production. In addition to the existing Bureau-level performance measurement system, an office-level performance measurement system was implemented in 1995 under the umbrella of the Government Performance and Results Act (GPRA).

Bureau-level performance measures and associated results for 2006 are shown in the table below.

The Bureau does not receive Federal appropriations; operations at the Bureau are financed by a revolving fund that is reimbursed through product sales. Customer billings are the Bureau’s only means of recovering the costs of operations and generating funds for capital investment. Billing rates are based on established cost standards, which are predicated on historical costs, and factors such as changes in labor, material and overhead costs. To ensure that sufficient cash is provided for operations the Bureau must perform to these standard costs.

<table>
<thead>
<tr>
<th>Currency</th>
<th>2006 Standard</th>
<th>2006 Actual</th>
</tr>
</thead>
<tbody>
<tr>
<td>Federal Reserve Notes</td>
<td>$27.66</td>
<td>$27.42</td>
</tr>
<tr>
<td>Federal Reserve Notes Delivered (Billions)</td>
<td>8.2</td>
<td>8.2</td>
</tr>
<tr>
<td>Productivity Change 2005 to 2006</td>
<td>-10.8%</td>
<td>-5.6%</td>
</tr>
<tr>
<td>Currency Spoilage</td>
<td>4.2%</td>
<td>4.3%</td>
</tr>
</tbody>
</table>

The actual production cost per thousand currency notes, which includes direct labor and materials and applied manufacturing overhead, was about 0.9% below standard in 2006. This was due primarily to increased optically variable ink (OVI) mileage and favorable spoilage results for the
The review was to streamline the organization by grouping similar functions to benefit from synergies, improve efficiency, reduce costs, improve response time and facilitate currency redesign efforts.

<table>
<thead>
<tr>
<th>Product Deliveries</th>
<th>Order</th>
<th>Delivery</th>
</tr>
</thead>
<tbody>
<tr>
<td>Federal Reserve Notes (Billions)</td>
<td>8.2</td>
<td>8.2</td>
</tr>
</tbody>
</table>

In 2006, the Bureau delivered 8.2 billion Federal Reserve Notes to the Federal Reserve System. Deliveries and billings are based on orders received from the customer. The Federal Reserve Bank submits their requirements to the Bureau on an annual basis and indicates expected product volume; the Federal Reserve has ordered 9.1 billion notes for delivery in FY 2007.

<table>
<thead>
<tr>
<th>Productivity Change</th>
<th>Standard</th>
<th>Actual</th>
</tr>
</thead>
<tbody>
<tr>
<td>Productivity</td>
<td>-10.8</td>
<td>-5.6</td>
</tr>
</tbody>
</table>

Productivity is calculated based on units of output per labor hour. In 2006, overall productivity decreased by 5.6%. A decrease was anticipated due to a reduction in the amount of currency ordered by the Federal Reserve System and the elimination of postage stamp production.

Staffing levels (apprenticeship and training programs) have continued to focus on projected, long-term demand, demand trends and preparations necessary for the production of the next denomination of redesigned currency, not fluctuations in year-to-year orders. BEP undertook a functional review of its organizational structure in 2006. The goal of the review was to streamline the organization by grouping similar functions to benefit from synergies, improve efficiency, reduce costs, improve response time and facilitate currency redesign efforts.

<table>
<thead>
<tr>
<th>Currency Spoilage</th>
<th>Standard</th>
<th>Actual</th>
</tr>
</thead>
<tbody>
<tr>
<td>Federal Reserve Notes</td>
<td>4.2%</td>
<td>4.3%</td>
</tr>
</tbody>
</table>

Spoilage is an inherent result of any production process. The level of spoilage is an indicator of the overall effectiveness of the production process and quality of material inputs. As the Bureau’s commitment to quality and its ISO certification requirements have become institutionalized, the overall level of currency spoilage has remained stable for the last three years. However, in 2006 overall currency spoilage was slightly above standard as a result of challenges encountered with aging production equipment. To this end, the Bureau began to recapitalize the Washington, DC facility with the installation of two new intaglio presses, and will continue this effort over the next five years. These new presses will be ready for full production in early FY 2007, and represent the latest in printing technology.
Prompt Payment

To ensure that Federal agencies pay invoices in a timely manner, Congress passed the Prompt Payment Act and the Office of Management and Budget (OMB) issued Circular A-125, which is now codified as part of the Code of Federal Regulations (CFR). Generally, the CFR requires payment within 30 days from the later of either the receipt of a proper invoice or acceptance of the goods/services. If this timeframe is not met, an interest penalty must be paid to the vendor. Within the Department of Treasury, the standard for the late payment rate is that no more than 2% of the invoices subject to prompt payment shall be paid late (at least 98% paid within 30 days.)

The Bureau’s prompt payment performance for the past three years is presented below. As the percentages indicate, the Bureau has continued to exceed the Department standard for late payments.

<table>
<thead>
<tr>
<th>Comparable Performance Measures for Three Years</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Federal Reserve Notes (Cost Per Thousand Notes)</td>
<td>$28.13</td>
<td>$29.01</td>
<td>$27.42</td>
</tr>
<tr>
<td>2. Federal Reserve Notes Delivered (Billions)</td>
<td>8.8</td>
<td>8.5</td>
<td>8.2</td>
</tr>
<tr>
<td>3. Productivity Change 2005 to 2006</td>
<td>7.4%</td>
<td>-1.8%</td>
<td>-5.6%</td>
</tr>
<tr>
<td>4. Currency Spoilage</td>
<td>4.3%</td>
<td>4.3%</td>
<td>4.3%</td>
</tr>
</tbody>
</table>

For those performance measures that are comparable, the results of the past three years are presented. New cost and spoilage standards are developed annually for all product lines produced at the Bureau. Because performance to standard is a meaningful performance measure only in the applicable year, only actual manufacturing cost and spoilage data are presented.

<table>
<thead>
<tr>
<th>2004</th>
<th>2005</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Number of Invoices Paid</td>
<td>94</td>
<td>35</td>
</tr>
<tr>
<td>2. Interest Penalties Paid</td>
<td>$6,619</td>
<td>$790</td>
</tr>
<tr>
<td>3. Interest of Invoices Paid Late</td>
<td>1.3%</td>
<td>0.5%</td>
</tr>
</tbody>
</table>
The Bureau installs new state-of-the-art printing presses.

During the year, the Bureau installed two new sheet-fed state-of-the-art intaglio printing presses. The additional weight of these presses required substantial structural reinforcement and upgrade of the pressroom. (Upper right hand corner) These presses have an indirect inking system and an automated electronic inspection system. The presses will provide the Bureau the ability to produce increasingly complex currency note designs, while reducing the Bureau’s environmental impact.
During 2006, the Bureau focused its resources and efforts on producing the most secure currency ever issued by the Federal Reserve. The Nation’s new currency is enhanced by additional, advanced counterfeit deterrent features that are indicative of a world-class symbol of security and integrity.

When pricing the 2006 currency program, the Bureau anticipated incurring a loss. The Bureau included a surcharge in currency billing rates for the acquisition of capital assets for the start-up of the Western Currency Facility in the 1990s, resulting in revenue in excess of expenses. For 2006, the Bureau did not include the full amount of depreciation in its currency billing rates. Only the estimated amount of depreciation necessary to fund planned capital investments was included in the billing rates. However, the full cost of depreciation is included on the income statement, which contributed to the excess of expenses over revenue.

Revenue in 2006 decreased due to the reduction in the number of Federal Reserve Notes ordered and delivered to the Federal Reserve. Total Federal Reserve Notes delivered in 2006 were 8.2 billion notes, which was a decrease from the previous year’s delivery of 8.5 billion notes. Even so, the Bureau remains well capitalized with respect to its working capital requirements.

Cash, Accounts Receivable and Cash Flow
Cash and accounts receivable decreased by $18.5 million and $9 million, respectively in 2006. The decrease in the cash was a result of the increase in inventories and higher than anticipated capital spending. Accounts receivable decreased as a result of the reduction in the currency order and subsequent billing.

Inventories
Inventories increased from $75 million in 2005 to $83.5 million in 2006. This $8.5 million increase was a result...
of the addition to currency-related inventories in September 2006, as the Bureau prepared to meet its 2007 currency order of 9.1 billion notes, an 11% increase in production over the 2006 level.

**Property and Equipment**
Net property and equipment remained relatively unchanged in 2006.

**Other Assets**
Other Assets remained relatively unchanged in 2006.

**Accounts Payable**
Accounts payable decreased from $14 million in 2005 to $12 million in 2006. The principal cause of the decrease was the timing of cash disbursements for vendor payments.

**Accrued Current Liabilities**
Accrued current liabilities increased from $28 million in 2005 to $30 million in 2006. The $2 million increase was attributable to an increase in the payroll accrual.

**Research and Development Costs**
(Millions of Dollars)

**Advances**
Advances decreased by $3.0 million in 2006. The decrease was the result of the completion of several outstanding contracts.

**Workers’ Compensation Liabilities**
The actuarial workers’ compensation liability experienced a decrease of $6 million in 2006. The

### Average Billing Rate for Currency

<table>
<thead>
<tr>
<th>Year</th>
<th>Rate Per Thousand Notes</th>
<th>Single Note</th>
</tr>
</thead>
<tbody>
<tr>
<td>1996</td>
<td>$39.41</td>
<td>$0.039</td>
</tr>
<tr>
<td>1997</td>
<td>$37.40</td>
<td>$0.037</td>
</tr>
<tr>
<td>1998</td>
<td>$40.20</td>
<td>$0.040</td>
</tr>
<tr>
<td>1999</td>
<td>$44.36</td>
<td>$0.044</td>
</tr>
<tr>
<td>2000</td>
<td>$45.34</td>
<td>$0.045</td>
</tr>
<tr>
<td>2001</td>
<td>$46.64</td>
<td>$0.047</td>
</tr>
<tr>
<td>2002</td>
<td>$54.39</td>
<td>$0.054</td>
</tr>
<tr>
<td>2003</td>
<td>$57.16</td>
<td>$0.057</td>
</tr>
<tr>
<td>2004</td>
<td>$55.56</td>
<td>$0.056</td>
</tr>
<tr>
<td>2005</td>
<td>$56.08</td>
<td>$0.056</td>
</tr>
<tr>
<td>2006</td>
<td>$54.56</td>
<td>$0.055</td>
</tr>
</tbody>
</table>
decrease in the actuarial liability was the result of the Bureau’s continued focus on creating a safer working environment and reducing the loss of employee work time caused by injuries.

Revenue from Sales
Overall revenue from sales decreased from $512 million in 2005 to $477 million in 2006. This decrease was attributable to the termination of the postage program and to the reduction in the 2006 currency order.

Cost of Goods Sold
Cost of Goods Sold decreased from $473 million in 2005 to $422 million in 2006. The $51 million decrease was the result of reduced material costs related to the smaller 2006 currency order, the termination of the postage stamp program in 2005, reduced labor costs, and reduced FECA costs. Gross margin, as a percentage of revenue, increased from 8% in 2005 to 12% in 2006.

Operating Costs
Operating costs increased $6 million in 2006 to $64 million. The increase was the result of increased labor costs and increased research and development costs related to the production of NexGen currency.

A skid of Federal Reserve Notes being loaded into the vault before shipment to a Federal Reserve Bank. (Currency Shipment Processor Craig Turner, Office of Currency Production).
Limitations of the Financial Statements

The following financial statements are for the Bureau of Engraving and Printing, a component of the Department of the Treasury. As such, the statements should be read with the realization that they are for a component of the U.S. Government, a sovereign entity. The principal financial statements have been prepared to report the financial position, results of operations and cash flows of the Bureau. They have been prepared from the Bureau’s financial books and records maintained in accordance with private sector generally accepted accounting principles. These statements are in addition to the financial reports used to monitor and control budgetary resources, which are prepared from the same books and records.
Independent Auditors’ Report

The Inspector General, Department of the Treasury and
The Director of the Bureau of Engraving and Printing, Department of the Treasury:

We have audited the accompanying balance sheet of the Bureau of Engraving and Printing (Bureau) as of September 30, 2006, and the related statements of operations and cumulative results of operations and cash flows (hereinafter referred to as “financial statements”) for the year then ended. These financial statements are the responsibility of the Bureau’s management. Our responsibility is to express an opinion on these financial statements based on our audit. The accompanying financial statements of the Bureau as of and for the year ended September 30, 2005, were audited by other auditors whose report thereon, dated October 25, 2005, expressed an unqualified opinion on those financial statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 06-03, Audit Requirements for Federal Financial Statements. Those standards and OMB Bulletin No. 06-03 require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the 2006 financial statements referred to above present fairly, in all material respects, the financial position of the Bureau of Engraving and Printing as of September 30, 2006, and the results of its operations and its cash flows for the year then ended in conformity with U.S. generally accepted accounting principles.

As discussed in Note 2 to the financial statements, effective October 1, 2005, the Bureau adopted Financial Accounting Standards Board Interpretation No. 47, Accounting for Conditional Asset Retirement Obligations.

We have also examined management’s assertion that the Bureau maintained effective internal control over financial reporting as of September 30, 2006, and have issued our report thereon dated October 27, 2006. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report in assessing the results of our audit.
In accordance with Government Auditing Standards, we have also issued our report dated October 27, 2006, on our tests of the Bureau’s compliance with certain provisions of laws, regulations, contracts, and other matters. The purpose of that report is to describe the scope of our testing of compliance and the results of that testing, and not to provide an opinion on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report in assessing the results of our audit.

October 27, 2006
## ASSETS

Current assets
- Cash (Note 3) $164,729 $183,250  
- Accounts receivable (Note 10) 33,032 42,038  
- Inventories, net (Note 4) 83,516 75,246  
- Prepaid expenses 4,321 3,675  
Total current assets 285,598 304,209  

Property and equipment, net (Note 5) 250,364 249,403  
Other assets, net (Note 6) 17,525 17,322  
Total assets $553,487 $570,934  

## LIABILITIES AND EQUITY

Liabilities
- Current liabilities (Notes 7 and 8)  
  - Accounts payable $11,818 $13,564  
  - Accrued liabilities 29,765 27,815  
  - Advances 899 3,881  
Total current liabilities 42,482 45,260  
- Workers' compensation liability (Note 8) 59,007 65,097  
Total liabilities 101,489 110,357  

Equity
- Invested capital 32,435 32,435  
- Cumulative results of operations 419,563 428,142  
Total equity 451,998 460,577  
Total liabilities and equity $553,487 $570,934  

See accompanying notes to the financial statements.

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2006 CFO Report

36
THE DEPARTMENT OF THE TREASURY
BUREAU OF ENGRAVING AND PRINTING

Statements of Operations and
Cumulative Results of Operations
For the Years Ended September 30, 2006 and 2005

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>(In Thousands)</td>
<td></td>
</tr>
<tr>
<td>Revenue from sales (Note 10)</td>
<td>$ 477,297</td>
<td>$ 512,064</td>
</tr>
<tr>
<td>Cost of goods sold</td>
<td>421,637</td>
<td>472,478</td>
</tr>
<tr>
<td>Gross margin</td>
<td>55,660</td>
<td>39,586</td>
</tr>
</tbody>
</table>

Operating costs:

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>General and administrative expenses</td>
<td>53,489</td>
<td>50,465</td>
</tr>
<tr>
<td>Research and development</td>
<td>10,750</td>
<td>7,648</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Excess of expenses over revenues</th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>(8,579)</td>
<td>(18,527)</td>
</tr>
</tbody>
</table>

Cumulative results of operations at beginning of year | 428,142 | 446,669 |

Cumulative results of operations at end of year | 419,563 | 428,142 |

See accompanying notes to the financial statements.
THE DEPARTMENT OF THE TREASURY
BUREAU OF ENGRAVING AND PRINTING

Statements of Cash Flows
For the Years Ended September 30, 2006 and 2005

<table>
<thead>
<tr>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>(In Thousands)</td>
<td></td>
</tr>
</tbody>
</table>

**Cash flows from operating activities**

Excess of expenses over revenues

$ (8,579) $ (18,527)

Adjustments to reconcile excess of expenses over revenues to net cash provided by operating activities:

- Depreciation 32,484 34,618
- Loss from disposal of property and equipment 104 993

Changes in assets and liabilities:

- Decrease in accounts receivable 9,006 2,569
- (Increase) decrease in inventories (8,270) 28,145
- Increase in prepaid expenses (646) (527)
- Increase in other assets (203) (729)
- Decrease in accounts payable (1,746) (5,703)
- Increase (decrease) in accrued liabilities 1,950 (3,165)
- (Decrease) increase in advances (2,982) 3,420
- Decrease in workers' compensation costs (6,090) (2,800)

Net cash provided by operating activities 15,028 38,294

**Cash flows from investing activities**

Purchases of property and equipment (33,549) (23,972)

Net cash used in investing activities (33,549) (23,972)

Net (decrease) increase in cash (18,521) 14,322

Cash at beginning of year 183,250 168,928

Cash at end of year $ 164,729 $ 183,250

See accompanying notes to the financial statements.
1. Reporting Entity

The Bureau of Engraving and Printing (Bureau), a component of the United States (U.S.) Department of the Treasury, is the U.S. Government's security printer. The Bureau designs and produces U.S. currency. The Bureau also advises and assists Federal agencies in the design and production of other U.S. Government documents requiring counterfeit deterrence or secure production.

The Bureau operates under basic authorities conferred by the Act of July 11, 1862, (12 Stat. 532; also, 31 U.S.C. 5114) and other laws and regulations. In accordance with the provisions of Public Law 81-656, effective August 4, 1950, the operations of the Bureau are financed by means of a revolving fund. This fund is reimbursed through billings to the Bureau's customers for products delivered. Public Law 95-81 authorized the Bureau to include in its product prices an amount to provide funding for the acquisition of capital equipment and future working capital. Invested capital represents the historical value of the initial contribution made by the Federal Government.

The financial statements represent the consolidation of two Federal revolving funds. The majority of all financial transactions (approximately 99%) are contained in the Bureau of Engraving and Printing Revolving Fund, which finances Bureau operations. The other revolving fund, the Mutilated Currency Revolving Fund, is used to redeem damaged paper currency received from the public. All significant balances and transactions between the funds have been eliminated in consolidation.

2. Summary of Significant Accounting Policies

Basis of Accounting

The Bureau has historically prepared its financial statements in conformity with U.S. generally accepted accounting principles, based on accounting standards issued by the Financial Accounting Standards Board (FASB), the private-sector standards-setting body. Under such standards, the Bureau prepares its financial statements using the full accrual basis of accounting under which revenues are recognized when earned and expenses are recognized as incurred, regardless of when cash is exchanged.

The Federal Accounting Standards Advisory Board (FASAB) has been designated by the American Institute of Certified Public Accountants as the standards-setting body for financial statements of federal government entities, with respect to the establishment of generally accepted accounting principles. FASAB has indicated, however, that financial statements prepared based upon accounting standards published by the FASB may also be regarded as in conformity with generally accepted accounting principles for those federal agencies, such as the Bureau, that have issued financial statements based upon FASB accounting standards in the past.

(continued)
Accordingly, consistent with historical reporting, the Bureau’s financial statements are presented in accordance with accounting standards published by the FASB.

**Cash**

Cash represents the aggregate amount of the Bureau’s funds held on deposit with the U.S. Treasury and are available to pay liabilities. The Bureau historically does not maintain significant cash balances in commercial bank accounts, and owns no cash equivalents.

**Equipment and Spare Parts**

In July 2005, the Bureau permanently ceased production of postage stamps for the U.S. Postal Service. Postage stamp related production equipment and spare parts were disposed of in accordance with applicable U.S. Government regulations.

**Estimation Process**

The preparation of financial statements in accordance with U.S. Generally Accepted Accounting Principles (GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and related revenues and expenses. Those estimates most significant to the Bureau’s financial statements are the actuarial estimates made by the Department of Labor (DOL) in arriving at the liabilities for workers’ compensation, allowances for obsolescence, the useful lives of property and equipment, the likelihood of losses associated with contingent liabilities, and certain accrued expenses at the date of the financial statements. Such estimates and assumptions could change in the future as more information becomes known, which could impact the amounts reported and disclosed herein.

**Inventories**

Inventories are stated at standard cost, except for finished goods inventories, which are stated at weighted average unit cost. Both methods approximate actual cost. Cost elements included in work-in-process and finished goods inventories are direct materials, direct labor, manufacturing overhead, and manufacturing support.

**Property and Equipment**

Property and equipment are recorded at cost. Major alterations and renovations are capitalized, while maintenance and repair costs are charged to expense as incurred. The capitalization threshold is $50,000. The Bureau capitalizes all cost associated with new construction and building improvements.

The Bureau occupies and uses buildings and land owned by the Department of the Treasury. In accordance with the Act establishing the revolving fund, the Bureau is not charged for the use of the buildings or land, but is responsible for maintenance and repair of all buildings and land

(continued)
improvements. The land and building shell for the Bureau’s Western Currency Facility were donated by the City of Fort Worth, Texas to the Department of the Treasury. See Note 5 for details.

Other Assets

Other assets consist principally of machine repair parts and tools, which are used in the production of the Bureau's products. Other assets are stated at actual cost, net of reserve for obsolescence.

Depreciation

Depreciation of property and equipment is calculated using the straight-line method over the following estimated useful lives:

- Machinery and equipment: 3 - 15 years
- Building improvements: 3 - 40 years
- Information technology (IT) equipment and software: 3 - 5 years
- Office machines: 5 - 10 years
- Furniture and fixtures: 5 - 10 years
- Motor vehicles: 3 - 9 years

Employee Retirement Plans

Bureau employees participate in the contributory Civil Service Retirement System (CSRS) or Federal Employees' Retirement System (FERS), to which the Bureau and employees make contributions according to plan requirements. Consistent with reporting under multi-employer pension plans, the Bureau does not report CSRS and FERS assets, accumulated plan benefits or future liabilities, if any, applicable to its employees. This data is reported for plan participants by the Office of Personnel Management (OPM).

Postretirement Benefits Other than Pensions

Postretirement benefits for former Bureau employees, specifically health care costs and life insurance, are administered and paid by OPM through appropriations received from the U.S. Government. The Bureau does not reimburse OPM for these payments. The Bureau's financial statements do not include the cost of employee postretirement benefits paid by OPM, or the actuarial liability for such benefits.

Workers’ Compensation Costs

The Federal Employee 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 death is attributable to a job-related injury or occupational disease. Claims incurred for benefits for the Bureau's employees under FECA are administered by DOL and are ultimately paid by the Bureau.

(continued)
The FECA liability consists of two components. The first component, the accrued FECA liability, is based on actual claims paid by DOL but not reimbursed by the Bureau. The Bureau reimburses DOL for the amount of actual claims normally within one to two years after payment is made by DOL. As a result, the Bureau recognizes a current and non-current liability for actual claims paid by DOL, to be reimbursed by the Bureau.

The second component, the actuarial FECA liability, is the estimated liability for future benefit payments. These future workers' compensation estimates were generated from an application of actuarial procedures developed to estimate the liability for future FECA benefits. The actuarial liability for future worker's compensation benefits includes the expected liability for death, disability, medical and miscellaneous costs for approved compensation cases, plus a component for incurred but not reported claims. The liability is determined using a method that utilizes historical benefit payment patterns related to a specific incurred period to predict the ultimate payments related to that period. These annual benefit payments have been discounted to present value using OMB’s economic assumptions for 10-year Treasury notes and bonds, which resulted in a discount rate of 5.17% in year one and 5.31% thereafter. Based on information provided by DOL, the Department of the Treasury allocated the overall liability to Treasury components based on past claims paid.

Annual, Sick and Other Leave

Annual leave is accrued as a liability when earned and the accrual is reduced as leave is taken. The balance in this accrued liability account reflects current pay rates.

Sick leave and other types of non-vested leave are expensed as the leave is taken.

Revenue Recognition

Revenue from sales to the Federal Reserve System is recognized when finished goods satisfactorily pass all Bureau quality control standards and are delivered to the on-site Federal Reserve Depository vaults. Finished goods are released for shipment in accordance with customer requirements. Revenue from the sale of uncut currency to the public is recognized at the time the product is shipped. The Bureau does not record an allowance for returns because of a historically negligible return rate.

Research and Development Costs and Advertising Costs

Research and development costs and advertising costs are expensed as incurred. Advertising costs amounted to $5.9 million and $7.4 million in the years ended September 30, 2006 and 2005, respectively.
THE DEPARTMENT OF THE TREASURY
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Notes to the Financial Statements
September 30, 2006 and 2005

Tax Status

The Bureau is a Federal entity, and therefore is not subject to Federal, state, or local income taxes. Accordingly, no provision for income taxes is required in the accompanying financial statements.

Commitments and Contingencies

Liabilities from loss contingencies, including environmental remediation costs not within the scope of FASB Statement No. 143, Accounting for Asset Retirement Obligations, arising from claims, assessments, litigation, fines and penalties, and other sources, are recorded when it is probable that a liability has been incurred and the amount of the assessment and/or remediation can be reasonably estimated. Loss contingencies that do not meet these criteria, but are reasonably possible and estimable are not accrued, but are disclosed in Note 12.

Recently Adopted Accounting Standards

In March 2005, the FASB issued Interpretation No. 47, Accounting for Conditional Asset Retirement Obligations (FIN 47), which requires a liability to be accrued if the reporting entity has a legal obligation to perform asset retirement activities and a reasonable estimate of the fair market value of the obligation can be made at fiscal year-end. FIN 47 also provides guidance as to when an entity would have sufficient information to reasonably estimate the fair value of an asset retirement obligation. The Bureau adopted the provisions of FIN 47 effective October 1, 2005. However, because the Bureau has no conditional asset retirement obligations that meet the above criteria, the adoption of FIN 47 had no effect on the Bureau’s financial statements.

3. Cash

The year-end cash balances by fund are as follows as of September 30, 2006 and 2005:

<table>
<thead>
<tr>
<th>Fund</th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>(In Thousands)</td>
<td></td>
</tr>
<tr>
<td>Bureau of Engraving and Printing</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Revolving Fund</td>
<td>$163,992</td>
<td>$182,510</td>
</tr>
<tr>
<td>Mutilated Currency Revolving Fund</td>
<td>737</td>
<td>740</td>
</tr>
<tr>
<td>Total</td>
<td>$164,729</td>
<td>$183,250</td>
</tr>
</tbody>
</table>

The balance in the mutilated currency revolving fund, consisting of mutilated currency submitted by the public for redemption, is offset by a liability to the public.

(continued)
4. **Inventories, net**

Inventories consist of the following as of September 30, 2006 and 2005:

<table>
<thead>
<tr>
<th></th>
<th>2006 (In Thousands)</th>
<th>2005 (In Thousands)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Raw material and supplies</td>
<td>$33,019</td>
<td>$32,815</td>
</tr>
<tr>
<td>Work-in-process</td>
<td>32,688</td>
<td>28,818</td>
</tr>
<tr>
<td>Finished goods - currency</td>
<td>2,403</td>
<td>—</td>
</tr>
<tr>
<td>Finished goods - uncut currency</td>
<td>15,406</td>
<td>13,613</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$83,516</strong></td>
<td><strong>$75,246</strong></td>
</tr>
</tbody>
</table>

The allowance for inventory obsolescence was $615 thousand and $741 thousand, at September 30, 2006 and 2005, respectively.

5. **Property and Equipment, net**

Property and equipment consist of the following as of September 30, 2006 and 2005:

<table>
<thead>
<tr>
<th></th>
<th>2006 (In Thousands)</th>
<th>2005 (In Thousands)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Machinery and equipment</td>
<td>$416,782</td>
<td>$393,518</td>
</tr>
<tr>
<td>Building and land improvements</td>
<td>215,851</td>
<td>206,575</td>
</tr>
<tr>
<td>IT equipment and software</td>
<td>17,224</td>
<td>14,592</td>
</tr>
<tr>
<td>Office machines</td>
<td>1,103</td>
<td>1,201</td>
</tr>
<tr>
<td>Furniture and fixtures</td>
<td>1,385</td>
<td>1,385</td>
</tr>
<tr>
<td>Donated assets - art work</td>
<td>125</td>
<td>125</td>
</tr>
<tr>
<td>Motor vehicle</td>
<td>212</td>
<td>212</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>652,682</strong></td>
<td><strong>617,608</strong></td>
</tr>
<tr>
<td>Less accumulated depreciation</td>
<td>411,486</td>
<td>385,623</td>
</tr>
<tr>
<td><strong>Construction-in-progress</strong></td>
<td>241,196</td>
<td>231,985</td>
</tr>
<tr>
<td><strong>Net property and equipment</strong></td>
<td><strong>$250,364</strong></td>
<td><strong>$249,403</strong></td>
</tr>
</tbody>
</table>

Depreciation expense for the years ended September 30, 2006 and 2005, was $32.5 million and $34.6 million, respectively.

The Bureau occupies and uses buildings and land owned by the Department of the Treasury. The land and building shell for the Fort Worth, Texas facility were donated by the City of Fort Worth to the Department of the Treasury in 1987, which holds the title thereto. At the time of
donation, the land had an appraised value of $1.5 million and the building shell cost was $5.6 million. In accordance with the provisions of Public Law 81-656, Bureau financial statements include only the costs to build out the facility.

6. Other Assets, net

Other assets consist principally of machine repair parts and tools. The allowance for obsolescence for these parts and tools for the years ended September 30, 2006 and 2005, was $5.1 million and $4.8 million, respectively.

7. Current Liabilities

All current liabilities are funded and consist of the following as of September 30, 2006 and 2005:

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>(In Thousands)</td>
<td></td>
</tr>
<tr>
<td>Intragovernmental</td>
<td>$ 5,269</td>
<td>$ 7,222</td>
</tr>
<tr>
<td>Other</td>
<td>37,213</td>
<td>38,038</td>
</tr>
<tr>
<td>Total</td>
<td>$ 42,482</td>
<td>$ 45,260</td>
</tr>
</tbody>
</table>

Accrued current liabilities consist of the following as of September 30, 2006 and 2005:

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>(In Thousands)</td>
<td></td>
</tr>
<tr>
<td>Payroll</td>
<td>$ 13,924</td>
<td>$ 12,709</td>
</tr>
<tr>
<td>Annual Leave</td>
<td>10,315</td>
<td>10,183</td>
</tr>
<tr>
<td>Workers' compensation</td>
<td>4,766</td>
<td>4,420</td>
</tr>
<tr>
<td>Other</td>
<td>760</td>
<td>503</td>
</tr>
<tr>
<td>Total</td>
<td>$ 29,765</td>
<td>$ 27,815</td>
</tr>
</tbody>
</table>

8. Workers’ Compensation Liability

Claims incurred and paid by DOL as of September 30, 2006 and 2005, but not yet reimbursed to DOL by the Bureau, are approximately $10.2 million and $10.1 million, of which $4.7 million and $4.4 million represents a current liability, as of September 30, 2006 and 2005, respectively. The Bureau will reimburse DOL for these claims in the next two years. The Bureau's estimated non-current actuarially derived future workers’ compensation liability was $53.5 million and $59.4 million as of September 30, 2006 and 2005, respectively.

(continued)
9. Employee Retirement Plans and Postretirement Benefits Other than Pensions

Employer contributions to the retirement plans for 2006 and 2005 are $15.9 million and $15.7 million, respectively. The CSRS employer contribution rate for fiscal years 2006 and 2005 was 7.0%. The FERS agency contribution rate for fiscal years 2006 and 2005 was 11.2%. The cost of providing the CSRS and FERS benefits is more than the amounts contributed by the Bureau and the employees to OPM. The additional cost of providing benefits, including the cost financed by OPM, which is not included in the Bureau's Statements of Operations, totaled $23.7 million and $23.6 million in 2006 and 2005, respectively.

OPM paid costs totaling $10.9 million and $10.5 million for the Federal Employees Health Benefits Program (FEHBP) and Federal Employees Group Life Insurance (FEGLI) programs in 2006 and 2005, respectively. These costs are not included in the Bureau's Statements of Operations.

10. Related Party Transactions and Concentration of Revenue

The Bureau’s principal customers are other Federal and quasi-Federal governmental organizations. During 2006 and 2005, the Bureau’s sales to these organizations as well as the outstanding amounts due from them as of September 30, 2006 and 2005, are reflected in the following table:

<table>
<thead>
<tr>
<th>Sales for the year ended September 30</th>
<th>Accounts Receivable as of September 30</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2006</td>
</tr>
<tr>
<td>Federal Reserve System:</td>
<td></td>
</tr>
<tr>
<td>Currency Production</td>
<td>$444,297</td>
</tr>
<tr>
<td>Mutilated Currency</td>
<td>3,760</td>
</tr>
<tr>
<td>United States Postal Service</td>
<td>2,648</td>
</tr>
<tr>
<td>Other Federal Agencies</td>
<td>3,268</td>
</tr>
<tr>
<td>Total</td>
<td>453,973</td>
</tr>
<tr>
<td>Total with the Public</td>
<td>23,324</td>
</tr>
<tr>
<td>Total</td>
<td>$477,297</td>
</tr>
</tbody>
</table>

In 2001, the Bureau and the U.S. Postal Service entered into an agreement that gradually phased out production of postage stamps at the Bureau over a five-year period ending in 2005, with only delivery and storage services continuing through 2006.

(continued)
THE DEPARTMENT OF THE TREASURY
BUREAU OF ENGRAVING AND PRINTING

Notes to the Financial Statements
September 30, 2006 and 2005

Other Federal sales revenues are derived principally from the sale of security printing products to U.S. Government agencies and fees charged to the Federal Reserve for the redemption of mutilated currency.

11. Principal Suppliers

The Bureau is dependent upon sole suppliers for distinctive currency paper, certain advanced counterfeit deterrent inks and currency paper fibers.

12. Commitments and Contingencies

The Bureau is a party in various administrative proceedings, legal actions, and claims brought against the Federal Government by employees, contractors, and other parties. Contingencies for litigations involving the Bureau, where the risk of loss was reasonably possible, were approximately $2.9 million and $0 as of September 30, 2006 and 2005, respectively.

Since the risk of loss for these litigations was not probable, the Bureau did not record any liability. Management believes that the ultimate resolution of these litigations will not have a material impact on reported results of operations, financial position and cash flows.

Judgments resulting from litigation against the Bureau are paid by the Department of the Treasury Judgment Fund. The Bureau is required to reimburse the Judgment Fund for paid claims related to employee discrimination and contract disputes. There were no amounts due to the Judgment Fund in fiscal years 2006 and 2005.

In 2006, the Bureau contracted to purchase currency production equipment, incorporating automated inspection and packaging capabilities, costing approximately $34 million that will be delivered in 2007.

The Bureau does not carry commercial insurance on its physical assets because by law the Federal Government is self-insured.

The Bureau has not entered into any long-term leasing arrangements.

13. Staffing

In 2005, in order to better match facility staffing and production requirements, the Bureau offered voluntary employee separation incentives. As a result, in 2005, approximately 100 employees accepted the incentives and the Bureau incurred and paid the related expenses of approximately $2.6 million. No voluntary employee separation incentives were offered or paid in 2006.
We as management of the Bureau of Engraving and Printing (Bureau) are responsible for establishing and maintaining adequate internal control over financial reporting and for our assertion on the effectiveness of internal control over financial reporting. The Bureau’s internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with U.S. generally accepted accounting principles.

The Bureau’s internal control over financial reporting includes those policies and procedures that:

- pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect our transactions and dispositions of the assets of the Bureau;

- provide reasonable assurance that our transactions are recorded as necessary to permit preparation of our financial statements in accordance with U.S. generally accepted accounting principles, and that receipts and expenditures of the Bureau are being made in accordance with authorizations of management of the Bureau; and

- provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the Bureau’s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that internal controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

We assessed the effectiveness of the Bureau’s internal control over financial reporting as of September 30, 2006. In making this assessment, the Bureau used the criteria established in the Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

Based on our assessment and those criteria, we conclude that the Bureau maintained effective internal control over financial reporting as of September 30, 2006.

KPMG LLP, an independent public accounting firm, has issued their reports, included herein, on (1) our financial statements; (2) our compliance with certain provisions of laws, regulations, and contracts and other matters; and (3) our assertion on the effectiveness of internal control over financial reporting.

Larry R. Felix
Director

Leonard R. Olijar
Chief Financial Officer

October 27, 2006
Washington, DC
Independent Auditors’ Report on Internal Control Over Financial Reporting

To the Inspector General, Department of the Treasury, and
The Director of the Bureau of Engraving and Printing, Department of the Treasury:

We have examined management’s assertion, included in the accompanying “Management’s Report on Internal Control Over Financial Reporting,” that the Bureau of Engraving and Printing (Bureau) maintained effective internal control over financial reporting as of September 30, 2006, based on the criteria established in *Internal Control – Integrated Framework* issued by the Committee of Sponsoring Organizations (COSO) of the Treadway Commission. The Bureau’s management is responsible for maintaining effective internal control over financial reporting and for its assertion on the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management’s assertion based on our examination.

Our examination was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants and the standards applicable to attestation engagements contained in *Government Auditing Standards*, issued by the Comptroller General of the United States and, accordingly, included obtaining an understanding of internal control over financial reporting, testing, and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our examination provides a reasonable basis for our opinion.

Because of inherent limitations in any internal control, misstatements due to error or fraud may occur and not be detected. Also, projections of any evaluation of internal control over financial reporting to future periods are subject to the risk that the internal control may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management’s assertion that the Bureau maintained effective internal control over financial reporting as of September 30, 2006 is fairly stated, in all material respects, based on the criteria established in *Internal Control – Integrated Framework* issued by COSO.

In accordance with *Government Auditing Standards*, we are required to report findings of deficiencies in internal control, violations of certain provisions of laws, regulations, and contracts, noncompliance with which could have a direct and material effect on the determination of the Bureau’s financial statement amounts, certain other matters and any fraud and illegal acts that are more than inconsequential that come to our attention during our examination. We are also required to obtain the views of management on those matters. We performed our examination to express an opinion on management’s assertion, included in the accompanying “Management’s Report on Internal Control Over Financial Reporting,” that the Bureau maintained effective internal control over financial reporting as of September 30, 2006, based on the criteria established in *Internal Control – Integrated Framework* issued by COSO and not for
the purpose of expressing an opinion on compliance and other matters; accordingly, we express no such opinion. Our examination disclosed a condition that is required to be reported under Government Auditing Standards involving internal control over financial reporting and its operations that we consider to be a reportable condition. However, this reportable condition is not considered to be a material weakness. The condition, along with the view of management, is described in Exhibit I of this report.

Under standards issued by the American Institute of Certified Public Accountants, reportable conditions are matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the Bureau’s ability to record, process, summarize, and report financial data consistent with the assertions by management in the financial statements. Material weaknesses are reportable conditions in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud, in amounts that would be material in relation to the financial statements being audited, may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

In accordance with Government Auditing Standards, we also noted certain additional matters that we have reported to management of the Bureau in a separate letter dated October 27, 2006.

October 27, 2006
Controls over inventory held by others

The Bureau has a contract with a vendor that requires the vendor to ship a certain raw material directly to the Bureau’s paper provider for further processing before it can be shipped to the Bureau. Since the Bureau does not track the vendor’s use of this material in paper production, the Bureau assumes that all the purchases of these raw materials were used by its vendors in production instantly and therefore, the Bureau records the purchase price as cost of goods sold at the time the raw materials are shipped to the Bureau’s paper providers. However, at the end of FY 2006, the Bureau determined that there were approximately 28,000 pounds of this raw material with historical cost of $3.8 million that had not been used by the vendor in the paper production as of fiscal year end and as such, should have been reflected as inventory at fiscal year end in accordance with U.S. generally accepted accounting principles. Accordingly, the Bureau adjusted the inventory and cost of goods sold balances to properly report this amount in its financial statements. The Bureau had approximately $2.3 million of such raw materials held by the vendor as of September 30, 2005.

Without effective controls surrounding the tracking of the purchase and usage of such materials, inventory and cost of goods sold reported in the Bureau’s financial statements could be materially misstated.

Recommendations

We recommend that the Bureau:

- Implements controls to ensure that the purchase and usage of these type of materials are properly tracked and recorded in the Bureau’s financial statements in accordance with GAAP.
- Conducts periodic visits to the vendor’s facility and conduct an inventory count of the balance on hand specifically at fiscal year-end.

Management’s Response

We concur with the finding and will implement controls necessary to ensure that the purchase and usage of these type of materials are properly tracked and recorded in the Bureau’s financial statements, and will conduct periodic visits to vendors’ facilities to conduct inventory counts of the balance on hand.
Independent Auditors’ Report on Compliance and Other Matters

The Inspector General, Department of the Treasury and
The Director of the Bureau of Engraving and Printing, Department of the Treasury:

We have audited the balance sheet of the Bureau of Engraving and Printing (Bureau) as of September 30, 2006, and the related statements of operations and cumulative results of operations and cash flows (hereinafter referred to as “financial statements”) for the year then ended, and have issued our report thereon dated October 27, 2006. That report notes that the Bureau’s 2005 financial statements were audited by other auditors and that the Bureau implemented a new accounting standard effective October 1, 2005.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 06-03, Audit Requirements for Federal Financial Statements. Those standards and OMB Bulletin No. 06-03 require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

The management of the Bureau is responsible for complying with laws, regulations, and contracts applicable to the Bureau. As part of obtaining reasonable assurance about whether the Bureau’s financial statements are free of material misstatement, we performed tests of the Bureau’s compliance with certain provisions of laws, regulations, contracts, and other matters, noncompliance with which could have a direct and material effect on the determination of the Bureau financial statement amounts, and certain provisions of other laws and regulations specified in OMB Bulletin No. 06-03. We limited our tests of compliance to the provisions described in the preceding sentence, and we did not test compliance with all laws, regulations, and contracts applicable to the Bureau. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion.

The results of our tests of compliance described in the preceding paragraph, disclosed no instances of noncompliance or other matters that are required to be reported herein under Government Auditing Standards or OMB Bulletin No. 06-03.

This report is intended solely for the information and use of the Bureau’s management, the Department of the Treasury’s Office of Inspector General, OMB, the U.S. Government Accountability Office, and the U.S. Congress and is not intended to be and should not be used by anyone other than these specified parties.

October 27, 2006

KPMG LLP