



UNITED STATES AIR FORCE

Annual Financial Statement

2008





U.S. AIR FORCE

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U.S. AIR FORCE



Table of Contents

Message from the Secretary of the Air Force	ii
Message from the Assistant Secretary of the Air Force for Financial Management and Comptroller	iii
Management Discussion and Analysis	
Air Force Heritage	1
Air Force Core Values	1
Air Force Critical Capabilities	2
Air Force Goals	2
Air Force in Action – FY 2008	3
Reinvigorate the Air Force Nuclear Enterprise	3
Partner With The Joint and Coalition Team to Win Today’s Fight	3
Develop and Care for Airmen and Their Families	4
Modernize Our Aging Air and Space Inventories	4
Acquisition Excellence	4
Air Force Structure	5
Air Force Major Management Initiatives	9
Energy and Environmental Focus	9
Personnel Services Delivery	11
eLog21	11
Air Force Resources	12
Air Force Financial Management Evolution	13
CFO Compliance	13
Financial Services Transformation	13
Internal Controls	13
Continuous Improvement	14
Air Force General Fund	
Appropriations	15
Current and Future Financial Systems - DEAMS	16
Air Force Working Capital Fund	
Supply Management Activity Group	17
Depot Management Activity Group	18
Financing the Fight	21
Financial Statements	
General Fund	
Principal Statements	25
Notes to the Principal Statements	31
Required Supplementary Stewardship Information	73
Required Supplementary Information	81
Audit Opinion	89
Working Capital Fund	
Principal Statements	99
Notes to the Principal Statements	105
Required Supplementary Information	129
Audit Opinion	131



UNITED STATES AIR FORCE



November 2008

Message from the Secretary of the Air Force



I am pleased to present the Air Force Financial Statements for Fiscal Year 2008. These statements provide a transparent report on how the Air Force utilizes the resources entrusted to us to provide Global Vigilance, Global Reach and Global Power, defending and protecting the United States and its global interests. It also underscores our commitment to the responsible stewardship of the nation's resources and our determination to win today's fight, take care of our Airmen and prepare for tomorrow's challenges.

This year, we proudly celebrate the 60th anniversary of the U.S. Air Force's contributions to the Berlin Airlift, and in our remembrance, we see the embodiment of our Air Force values of Integrity First, Service before Self, and Excellence in All We Do. We also see reflected the past, present, and future role of the US Air Force in supporting Joint operations, assisting our allies, and contributing to America's security. Today, as then, Air Force Financial Management professionals provide a key capability that enables us to conduct operations which are critical to our nation's security.

We face a number of challenges in the coming year, and we face these with confidence because we have the best Airmen in the world. Airmen are on the front lines everyday, and it is our solemn responsibility to care for our Airmen and their families. We will continue to provide our full support to Operations Enduring Freedom and Iraqi Freedom while continuing to lean forward in every aspect as we support Joint operations. We will also commit to individual and organizational accountability by critically examining our internal processes, restoring discipline, identifying weaknesses, and aggressively solving problems, and we will overcome any challenge that impinges on our credibility, readiness, or the trust placed in us by others.

I am particularly proud of the efforts of the Financial Management community in support of the Air Force's priorities. Air Force Financial Management is leading by example. Financial Management continues to "Finance the Fight" through ongoing joint operations, by increasing Financial Management operational efficiency and providing enhanced decision support to Commanders by transforming its own operations to increase Total Force services to our Airmen.

From the Berlin Airlift to Operations Enduring Freedom and Iraqi Freedom, our Air Force has served with distinction and honor. Effective Financial Management remains a critical capability in achieving our mission and these statements provide a report on how the Air Force is delivering this capability. We will achieve our mission, and we will preserve the public faith placed in us as good stewards of America's trust. Integrity, Service, and Excellence are our hallmarks – past, present, and always.

Michael B. Donley
Michael B. Donley

Annual Financial Statement 2008



November 2008

Message from the Assistant Secretary of the Air Force for Financial Management and Comptroller



Air Force financial management is critical to achieving the Air Force mission and priorities and these financial statements provide a report on how the Air Force is managing the resources entrusted to it. These reports also detail how our Financial Management (FM) professionals are delivering financial management capability in support of Air Force operations at home and around the world.

Our FM priorities, goals and objectives reflect those of the Air Force. The financial statements are focused on the Air Force's goal to "Implement open, transparent business practices, and achieve a clean audit."

I am proud of our financial management community's activities and leadership in achieving Air Force priorities and goals. FM continues to provide support to ongoing joint operations such as Operations Enduring Freedom and Iraqi Freedom, while we continue to transform and improve our own operations; thereby enhancing services, reducing costs, and fostering process improvement.

In the past year, we have made great strides in increasing efficiency and providing improved financial services to Airmen at all levels. For example, the new Air Force Financial Center of Expertise at Buckley Air National Guard Base in Colorado provides expert, on-demand, specialized financial analysis to all Air Force installations and Major Commands. The Center of Expertise leverages the financial proficiency of the FM community to provide Air Force commanders enhanced decision support to make more fully informed and more effective decisions through detailed analysis of alternatives.

We also stood up the Air Force Financial Services Center at Ellsworth Air Force Base in South Dakota, consolidating transaction processing and providing enhanced customer service by providing a "one-stop shop" for Airmen to receive financial services. Additionally, Airmen in the field can now take advantage of programs such as Eagle Cash, a cash card that can be used at deployed bases. We also have web-based initiatives that will soon make travel pay and financial transactions easily accessible for self-service by Airmen around the world 24 hours a day, 7 days a week, 365 days a year. These are all part of our commitment to focus on enhanced customer service, providing expert advice and improving the operation of our Air Force.

The Financial Management world, like the rest of the Air Force, is managing change. Financial Management programs and initiatives continue to move toward greater transparency and efficiency while providing better support for decision-makers at all levels. One fundamental aspect that will not change is our steadfast stewardship of the resources entrusted to us in execution of our global mission. That mission is always supported by the Air Force's financial management professionals who are truly "*Financing the Fight.*"

A handwritten signature in black ink that reads "John H. Gibson, II".

John H Gibson, II



“People were hungry for food and freedom. We were giving them both and they were most grateful.”

-Col. Gail Halverson, USAF (ret),
the Berlin Airlift “Candy Bomber”

Management Discussion and Analysis

Air Force Heritage



West Berliners watch as a U.S. C-54 Skymaster delivers desperately needed supplies during the Berlin Airlift.

For over 60 years, America has depended upon its Airmen to provide dominance in the air, space, and the emerging cyberspace domains. This continues the execution of our charter. We draw on a proud heritage beginning with our founding as a separate service over six decades ago. This year we celebrate another historic milestone: the 60th anniversary of mission accomplishment of our first great challenge. In June 1948, the newly established United States Air Force (USAF) started the ultimately successful Berlin Airlift. This heroic effort by USAF Airmen ended the attempted strangulation of the people in the Western Sector of Berlin.

This year we also celebrate the 60th anniversary of the desegregation of the military. This was in no small part made possible by the Tuskegee Airmen, the group of brave

African-Americans who flew fighter escorts for U.S. bombers during World War II. Airmen such as General “Chappie” James, General Benjamin Davis and many other heroes facing racism and discrimination at home demonstrated sheer undaunted courage serving their country in a time of war. Tuskegee Airmen painted the tails of their aircraft red to identify themselves thus becoming known as “Red Tails.” Their skill and performance became legendary to both Axis and Allied forces.

These are two examples of our rich history, and this legacy of successful mission accomplishment continues today as the USAF is engaged in its worldwide mission. That mission is: *To fly, fight and win in Air, Space and Cyberspace.* We executed the Berlin Airlift mission, we led the way in desegregating the military, we are carrying out our current mission, and we are committed to the accomplishment of future missions. We are always aware of our history and our vision: Lasting Heritage... Limitless Horizons.

The Air Force strategic framework consists of these elements:

Our Core Values are:

- ▶ Integrity First
- ▶ Service Before Self
- ▶ Excellence in All That We Do

A loadmaster and maintenance personnel conduct pre-flight checks on a C-17 Globemaster III before taking off from Pegasus White Ice Runway, Antarctica.





UNITED STATES AIR FORCE

“It is my deep conviction that we have reached a turning point in the long history of our efforts to guarantee a freedom and equality to all our citizens...and when I say all Americans, I mean all Americans.”

- President Harry S. Truman



RAMITELLI, Italy -- Pilots of the 332nd Fighter Group, "Tuskegee Airmen," the elite, all-African American 332nd Fighter Group. From left to right, Lt. Dempsey W. Morgran, Lt. Carroll S. Woods, Lt. Robert H. Nelron, Jr., Capt. Andrew D. Turner, and Lt. Clarence P. Lester.

Our Critical Capabilities are:

- ▶ Global Vigilance
- ▶ Global Reach
- ▶ Global Power

Our Goals are:

- ▶ Foster Mutual Respect and Dignity
- ▶ Sustain Air, Space and Cyberspace Capabilities
- ▶ Provide Persistent Situational Awareness
- ▶ Develop Joint and Battle-Ready Airmen
- ▶ Improve the Total Force Quality of Life
- ▶ Achieve Open, Transparent Business Practices and a Clean Audit
- ▶ Foster Air Force Smart Operations for the 21st Century (AFSO21)

One of the key enablers of our operational success, whether on the approaches into Berlin in 1948 or in the skies over Iraq and Afghanistan today, remains our Air Force Financial Management professionals from all components of the Total Force. They demonstrate their devotion to duty, capabilities, and innovation on a daily basis. They are meeting their challenge of providing transforming efficiencies at all echelons.



Highly requested as fighter escorts among bomber pilots, the Tuskegee Airmen earned the nickname "Red Tail Angels" among bomber crews. The airmen flew several different aircraft but are most identified with the P-51.

Air Force in Action—FY 2008

America's Air Force has been conducting combat operations since Operations Desert Shield / Desert Storm. These operations continue today in Iraq and Afghanistan and in supporting locations worldwide. The Air Force has remained committed to achieving our top priorities as a service:

- ▶ Reinvalidate the Air Force Nuclear Enterprise
- ▶ Partner with the Joint and Coalition Team to Win Today's Fight
- ▶ Develop and Care for Airmen and Their Families
- ▶ Modernize our Aging Air and Space Inventories
- ▶ Acquisition Excellence



A Minuteman III intercontinental ballistic missile successfully launches from North Vandenberg AFB. The missile was configured with a National Nuclear Security Administration (NNSA) test assembly in which three unarmed re-entry vehicles traveled approximately 4,190 miles to their pre-determined targets.

Reinvigorate the Air Force Nuclear Enterprise

The U.S. nuclear deterrent mission capability forms the ultimate backdrop of our nation's strategic defense—dissuading and deterring opponents while reassuring allies.

- ▶ The Air Force is responsible for two-thirds of America's nuclear deterrent capability.
- ▶ We will bring what we are known for—precision and reliability—to this enterprise.
- ▶ The Secretary of the Air Force created the Air Force Nuclear Task Force to develop a strategic Roadmap for rebuilding our nuclear enterprise, and we will be aggressively taking action on its direction in FY 2009.



An A-10 Thunderbolt II aircraft moves into position to receive fuel from a KC-135 Stratotanker during a mission over Afghanistan. A-10s are highly accurate weapons-delivery platforms.

Partner with the Joint and Coalition Team to Win Today's Fight

The Air Force is committed to winning the Global War on Terror. Our Airmen operate on a global scale every day. Today's Air Force provides a range of capabilities for success in a variety of environments. Engagement in Operations IRAQI FREEDOM and ENDURING FREEDOM is but the tip of the iceberg, as Airmen deploy to other parts of the world in supporting operations as well. The Air Force also provides the aerial defense of our homeland by flight in support of Operation NOBLE EAGLE.



UNITED STATES AIR FORCE



The F-35 Joint Strike Fighter (JSF) "Lightning II" is a stealthy, supersonic 5th Generation, multi-role fighter designed, in specific variants, to replace aging aircraft across the joint forces.

Develop and Care for Airmen and their Families

We must prepare our Airmen for a future fraught with challenges, and foster their ability to learn, anticipate, and adapt. Our Airmen are our most precious resource, and taking care of them and their families will help maintain our competi-



HOLLOMAN AIR FORCE BASE, N.M. - Maj. Brian Collins, greets his family after returning from Kunsan Air Base, South Korea.

tive advantage. We are obligated to improve the quality of their lives, and those of Air Force families, so our Airmen can focus on continuing their extraordinary service to our nation. In part because of our care and concern for them through six decades of Air Force history, our Airmen have proven themselves in times of crisis—taking action, anytime, anywhere in defense of freedom.

Modernize Our Aging Air and Space Inventories

We must modernize our capabilities in air, space and cyberspace as we meet the challenges of the 21st Century. Recapitalizing our air superiority, strike, space, Intelligence, Surveillance and Reconnaissance (ISR), mobility and other systems will ensure we have the right equipment to deter or defeat future threats to our Nation. To that end our top acquisition priorities are:

- ▶ The KC-X Tanker
- ▶ The CSAR-X Helicopter
- ▶ Modern space systems vital to our joint warfighters
- ▶ The F-35A Joint Strike Fighter
- ▶ A new bomber fielded by 2018

Acquisition Excellence

We are committed to establishing and enforcing standards for transparency in acquisition and other business processes that are commensurate with "best-in-class" public and private sector organizations. Transparency is essential to good governance, and good governance is vital to ensuring our Air Force can produce and field the systems with which we will fly and fight. We will continue to perfect the acquisition processes and procedures that promote good governance through transparency and adherence to regulatory guidance.

"Amid challenges, however, we have at least two constants: The high quality of Airmen attracted to military service; and their commitment to the core values of Integrity First, Service Before Self, and Excellence in All We Do."

-Secretary of the Air Force Michael Donley

Air Force Structure

The command line of the Air Force flows from the President and the National Command Authority to the Secretary of Defense and the Department of the Air Force. The Air Force is headed by the Secretary of the Air Force (SECAF), with the Chief of Staff reporting to the Secretary. Immediately subordinate to the departmental headquarters are the Major Air Commands (MAJCOMs), Field Operating Agencies (FOAs), Direct Reporting Units (DRUs), and the Auxiliary.

Major Air Commands

MAJCOMs are primarily of two types: operational and support. Within the operational commands, the divisions are generally defined according to purpose or location (e.g., combat, movement of people and supplies, or Pacific and European theaters). The support commands generally are organized according to function (e.g., logistic, support, or training) and are directly subordinate to Air Force Headquarters. A list of the MAJCOMs and their missions follows:



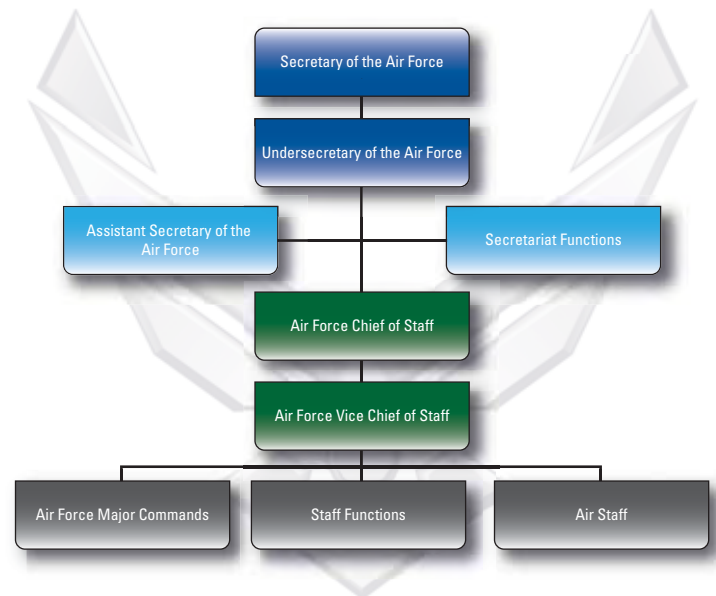
Air Combat Command (ACC)

Missions: Operate USAF bombers (active, Air National Guard, and Air Force Reserve Command); and USAF's CONUS-based fighter and attack, reconnaissance, battle management, and command and control aircraft, and

intelligence and surveillance systems. Provide combat airpower to America's warfighting commands (CENTCOM, EUCOM, NORTHCOM, PACOM, and SOUTHCOM); nuclear, conventional, and information operations forces to United States Strategic Command (STRATCOM); and air defense forces to North American Aerospace Defense Command (NORAD).

Command Personnel: 151,000

Primary Aircraft Inventory includes: Bombers; Fighters; Intelligence, ISR, and Trainers



An F-15E Strike Eagle from the 391st Expeditionary Fighter Squadron pops flares during an aerial training dog fight.



UNITED STATES AIR FORCE



Air Education and Training Command (AETC)

Missions: Recruit, train, and educate professional, expeditionary-minded Airmen to sustain the combat capability of America's Air Force. Conduct joint, readiness, and Air Force security assistance training. Provide basic military training, initial and advanced technical training, flying training and professional military and degree-granting professional education.

Command Personnel: 83,000

Primary Aircraft Inventory includes: Trainers, Fighters, Transports, Helicopters, and Tankers



Air Force Materiel Command (AFMC)

Missions: Deliver war-winning expeditionary capabilities to the warfighter through development and transition of technology, professional acquisition management, and world-class sustainment of all Air Force weapons systems. Provide exacting test and evaluation of all weapons and supporting systems.

Command Personnel: 78,000

Primary Aircraft Inventory includes: Bombers, Fighters, Transports, Tankers, Helicopters and Trainers



Air Force Space Command (AFSPC)

Missions: Operate and test USAF intercontinental ballistic missile (ICBM) forces for STRATCOM; missile warning radars, sensors, and satellites; national space-launch facilities and operational boosters; worldwide space surveillance radars and optical systems; worldwide space environment systems; and position, navigation, and timing systems.

Command Personnel: 27,000

Primary Inventory includes: Missile Warning Systems, ICBMs, Satellite Systems, and Space Surveillance Systems



A T-38A Talon pilot watches from the cockpit as another T-38 flies in formation during a local training mission.



The Atlas V rocket with the Wideband Global SATCOM satellite rolls out in preparation for launch.

Annual Financial Statement 2008

Management Discussion and Analysis



An Air Force MH-53M Pave Low from Air Force Special Operations performs "dust-out" training in Djibouti, Africa.



Air Force Special Operations Command (AFSOC)

Missions: Serve as America's specialized air power, providing combat search and rescue and delivering special operations power anytime, anywhere.

AFSOC is the Air Force component of U.S. Special Operations Command, a unified command. The command's core missions include battlefield air operations; agile combat support; aviation foreign internal defense; information operations; precision aerospace fires; psychological operations; specialized air mobility; specialized refueling; and intelligence, surveillance and reconnaissance.

Command Personnel: 13,000

Primary Aircraft Inventory includes: Special Operations Aircraft, Helicopters and Tankers



Air Mobility Command (AMC)

Missions: Provide rapid global mobility and sustainment through tactical and strategic airlift and aerial refueling for U.S. armed forces. Provide special duty and operational support aircraft and global humanitarian support.

Command Personnel: 136,000

Primary Aircraft Inventory includes: Transports, Helicopters, and Tankers



Pacific Air Forces (PACAF)

Missions: Provide ready air and space power to promote U.S. interests in the Asia-Pacific region during peacetime, crisis, and war.

Command Personnel: 43,000

Primary Aircraft Inventory includes: Fighters, Transports, and Tankers



U.S. Air Forces in Europe (USAFE)

Missions: Deliver airpower options to combatant commanders within the U.S. European Command Area of Responsibility. Plan, control, support and conduct joint, coalition NATO and war-

fighting headquarters operations in Europe, Asia and Africa based on taskings from the U.S. EUCOM Commander.

Command Personnel: 32,000

Primary Aircraft Inventory includes: Fighters, Transports, and Tankers



Four miles above Iraq, a KC-135 Stratotanker connects with an F-16 Fighting Falcon to offload more than 20,000 lbs. of fuel before resuming its close air support mission.



UNITED STATES AIR FORCE



Air Force Reserve Command (AFRC)

Missions: Support the active duty force. Serve in such missions as fighter, bomber, airlift, aerial port operations, aeromedical evacuation, aerial fire fighting, weather reconnaissance, space operations, airborne air control, flying training, flight testing, and aerial spraying. Provide support and disaster relief in the United States and support national counterdrug efforts.

operations, airborne air control, flying training, flight testing, and aerial spraying. Provide support and disaster relief in the United States and support national counterdrug efforts.

Command Personnel: 75,000

Primary Aircraft Inventory includes: Fighters, Transports, and Tankers



Air National Guard (ANG)

Missions: Provide combat capability to the warfighter and security for the homeland. Protect life and property and preserve peace, order, and public safety.

Command Personnel: 106,000

Primary Aircraft Inventory includes: Fighters, Transports, and Tankers

Field Operating Agency (FOA)

FOAs are subdivisions of the Air Force that carry out field activities under the operational control of Headquarters U.S. Air Force functional managers. FOAs have the same administrative and organizational responsibilities as MAJCOMs. Examples of FOAs include the Air Force Audit Agency, Air Force Center for Environmental Excellence, Air Force Financial Services Center, Air Force Services Agency, and Air Force Weather Agency, among others.

Direct Reporting Unit (DRU)

DRUs are subdivisions of the Air Force that are directly subordinate to Headquarters Air Force, separate from any MAJCOM or FOA because of a unique mission, legal requirements or other factors. DRUs have the same administrative and organizational responsibilities as MAJCOMs. The DRUs are the Air Force Academy, Air Force District of Washington, and Air Force Operational Test and Evaluation Center.



Auxiliary

An Air Force auxiliary is an organization created by statute that the Secretary of the Air Force may use to fulfill the Air Force's non-combat programs and missions. The Civil Air Patrol (CAP) is the only current U.S. Air Force auxiliary.



John Salvado, Civil Air Patrol's director of operations, describes the image capabilities of the Airborne Real Time Cueing Hyperspectral Enhanced Reconnaissance system at the CAP National Operations Center at Maxwell Air Force Base, Ala. The system is used to conduct aerial surveys for rescue missions.



The Virginia Air National Guard's 192nd Fighter Wing was the first Air National Guard unit in the country to fly the F-22 Raptor.

Annual Financial Statement 2008

Management Discussion and Analysis

Air Force Major Management Initiatives

The Air Force is justifiably proud of how it plans to master current challenges as well as anticipate future requirements in an ever-changing world. The initiatives briefly described below outline some of the Air Force responses to these challenges and how they will shape the future.

Air Force Sustainable Operations: an Energy and Environmental Focus

In accordance with the Air Force heritage, our role as a catalyst for innovation places us in a unique position to provide leadership. In response to rising energy costs, energy security considerations, and international concerns regarding greenhouse gas emissions, we are implementing an energy strategy that consists of: reducing our overall demand for energy, increasing the supply of secure energy, and changing the Air Force culture to ensure that we accomplish these energy objectives while maintaining mission readiness.

Our energy and environmental initiatives fit into a larger construct of sustainable operations. Viewing the contribution of those initiatives through this construct provides a new way to see the effectiveness of our efforts. Air Force Operational Sustainability is recognizing the direct and indirect impacts of Air Force operations on resources and achieving better understanding of the full measure of resources needed in the present and the future to ensure the successful conduct of Air Force operations. This sustainability also includes taking action by planning, designing, and executing mission requirements in a manner that provides for the long-term sustainability of operations in the face of constrained resources.



Members of the 23rd Equipment Maintenance Squadron Aerospace Ground Equipment shop at Moody Air Force Base, Ga. use an electric vehicle for their daily duties instead of a fuel powered vehicle.



Staff Sgt. Joe Wallis and Johnny Sniderhan reveal the Fischer-Tropsch synthetic fuel blend certification logo painted on the side of a B-52H Stratofortress at the certification ceremony at Edwards Air Force Base.

In FY 2008, the Air Force spent approximately \$7 billion to fuel our aircraft fleet and ground vehicles and provide utility services (primarily electricity and natural gas) to our bases. Much of the petroleum used to produce our aviation fuels originates from outside the United States, and it is in our interest to seek ways to reduce our dependence on foreign oil. Accordingly, we continue to research, test, and certify new technologies to displace our dependence on foreign oil with an alternative domestic fuel source. The Air Force is testing and certifying our entire inventory of aircraft for operations with a 50/50 synthetic Fischer-Tropsch fuel blend, and will complete this certification by early 2011. To date, we have certified the B-52, C-17 and B-1B fleets to fly using 50/50 synthetic fuel blend, and we expect to complete certification of the F-15, F-22 and KC-135 in FY 2009. It is our goal that by 2016, the Air Force will be prepared to cost competitively acquire 50% of the Air Force's domestic aviation fuel requirement via a synthetic fuel blend in which the synthetic component is derived from domestic sources produced in a manner that is greener than fuels produced from conventional petroleum. We are also evaluating other, bio-based alternative jet fuels, where fuel is produced using biomass or non-food plant products.



UNITED STATES AIR FORCE

The Air Force is also focused on aggressively implementing a strategy to generate or utilize renewable energy on bases with more solar, wind, and geothermal energy. We have been acknowledged as the largest purchaser of green power in the federal government over the past number of years, and third overall in the nation last year. Nellis AFB, Nevada, is an example of an installation with the resources and the need for a new energy direction. Nellis AFB engineers partnered with private industry and the local utility provider to be home to America's largest photovoltaic solar array, which produces over 14 megawatts of clean, renewable energy. The system, which covers only underutilized land, reduces base utility costs by approximately \$1 million per year and conserves funds to meet mission objectives.

Over the past two decades, the Air Force has strengthened its operational activities and programs to address an increasing universe of environmental laws, regulatory standards, and Executive Order mandates. Physical resource limitations, increasing local competition for those resources, regulatory restrictions, and other encroachment pressures are challenging the ability to meet current and emerging mission requirements. Through all this, the Air Force's programmatic approach—structured around the four environmental “pillars” of compliance, restoration, conservation, and pollution prevention—provided an impressive record of responsiveness to regulation in a manner that has been aligned with the military mission, and strategic mission goals and objectives of the Air Force. Our most recent environmental focus

is on fully implementing an Environmental Management System (EMS) approach at Air Force installations. The EMS approach allows us to identify aspects of Air Force operations where there is a potential environmental impact; prioritize those impacted or impacting operations for review, attention or investment; and seek continuous improvement opportunities that improve operational efficiency or effectiveness while reducing environmental impacts. Our efforts to improve support for the mission through environmental excellence have garnered many accolades, including:

- ▶ The Secretary of Defense recognized four Air Force bases through the 2008 *Secretary of Defense Environmental Awards*. The Air Force recipients included: Hill AFB, Utah, for its Environmental Quality Program based on individual and team achievements; Robins AFB, Georgia, for its Pollution Prevention Program as an Industrial Installation; Seymour Johnson AFB, North Carolina, for its Environmental Restoration Program as an installation; and Fairchild AFB, Washington, for its Environmental Excellence in Weapon System Acquisition.
- ▶ The Air Force received five 2008 *White House Closing the Circle Awards* or honorable mentions, which recognize the Federal workforce's commitment to meeting the President's directive to be good stewards of our nation's natural resources. The Air Force award recipients include: Robins AFB, Georgia, which received an award in the Environmental Management Systems category and an

The largest photovoltaic solar power plant in the United States is becoming a reality at Nellis Air Force Base.



Annual Financial Statement 2008

Management Discussion and Analysis

honorable mention in the Green Purchasing category; and Vandenberg AFB, California for Waste Pollution Prevention. Robins AFB, Charleston AFB, South Carolina, and Fairchild AFB, Washington, received Honorable Mentions in the Green Purchasing, Environmental Management Systems, and the Alternative Fuel and Fuel Conservation in Transportation categories, respectively.

- ▶ The Air Force Aeronautical Systems Center and Air Force Research Laboratory were awarded the 2007 *Best of the Best: Stratospheric Ozone Protection Award* by the U.S. Environmental Protection Agency (EPA) for Leadership in Aviation Halon Replacement and leadership in international stratospheric ozone protection.
- ▶ Air Force members and the Joint Strike Fighter Emissions Test team won the EPA 2007 *Climate Protection Award* for leadership in addressing air emissions from the Joint Strike Fighter.

Personnel Services Delivery (PSD)

Another key initiative for the Air Force is PSD transformation which will help lead to a leaner, more efficient force and provide more timely service delivery. The four major accomplishments of PSD will be:

- ▶ Redesign of Personnel Services Processes—eliminates unnecessary steps and approvals to speed up work and reduce workload
- ▶ Enhancement of Contact Center and Self Service Capabilities—expands online and contact center options to make personnel inquiries and self-service transactions available worldwide, 24/7
- ▶ Recasting of Field Organizations and Career Field—shifts personnelists' focus from routine transactions to even more valuable key advisory services for commanders and leaders
- ▶ Modernization of Architecture and Technology—puts the right system in place to support and integrate Web-based applications and enhanced call center capabilities

PSD provides a new personnel service delivery model which leverages the benefits of Web-based and call center-based services for many routine personnel actions previously done by a manpower-intensive, face-to-face network. PSD will be a supportable personnel system that will accomplish the Air Force-specific processes which will not be performed by the emerging Defense Integrated Military Human Resource System (DIMHRS). DIMHRS is the DoD-wide integrated



Tonya Harris, of the Air Force Personnel Center, briefs visitors from the U.S. Department of State's Bureau of Human Resources on the various Web-based technologies employed at AFPC's 24-hour Air Force Contact Center.

personnel/pay system currently in development. It will incrementally replace many of the capabilities of current Air Force Military Personnel Services systems.

The idea behind this transformation is to provide a convenient and secure way for Airmen to use any telephone or Internet-ready computer to conduct routine transactions and avoid waiting in lines, save time, and fit their personnel business into their own schedule. PSD will result in accurate information available on a 24/7 basis. It also gives Airmen more direct control over career-affecting matters. PSD has a multi-phased fielding with a goal of 85% of personnel transactions to be done through the Internet and 10% to be accomplished over the phone. This will reverse the pre-PSD operation which had 85% of transactions being done face-to-face. PSD maximizes use of technology while saving personnel spaces and providing timely and accurate service to our Airmen worldwide.

Expeditionary Logistics for the 21st Century (eLog21)

eLog21 is the Air Force's commitment to transform current logistics processes and deliver more efficient and effective support to the warfighter. This ongoing transformation uses a holistic approach focused on changing processes first, followed by organizational changes, all of which will be enabled by modern, integrated information technology systems. Some of the components of this initiative include Asset Marking and Tracking which improves visibility throughout the supply chain, and logistics data transformation which will improve data quality and reliability. The Air Force Working Capital Fund section has a description of other major components of eLog21.



UNITED STATES AIR FORCE

Air Force Resources

The three vital resources to successful accomplishment of the Air Force mission are:

- ▶ **Places:** A network of bases that reflect the Air Force’s global competencies. The Air Force is a global force, spanning facilities both in the United States and around the world, as shown in map below.
- ▶ **People:** Trained, motivated, and dedicated.
 - The Air Force consists of over 493,000 military and civilian personnel. Aerospace power is a proven necessity for victory on land, sea, air, space, and cyberspace. The foundation for this is our people.
 - The reserve component (Air Force Reserve and Air National Guard) has become more important than

ever in sustaining worldwide operations. These warriors make possible the successful accomplishment of Air Force missions.

- ▶ **Systems:** Modern weapons platforms that integrate air, space and cyber assets into an undefeatable force.
 - Air Force “systems” no longer mean only “manned aircraft.” Systems also include space launch vehicles; satellites; intelligence, surveillance and reconnaissance assets; unmanned aerial systems and the cohesive infrastructure to all Air Force systems. All Air Force systems are essential assets for Air Force people to accomplish the mission.
 - Manned systems, however, are still vital: The average age of the active duty fleet is over 23 years with some over 45 years; the average age of the

Major Air Force Facilities



produced by the Air Force Reserve Agency. Some other art and photos at www.af.mil

Air National Guard fleet is almost 26 years; and the average age of the Air Force Reserve fleet is over 28 years. All of these are actively involved in the Global War on Terror and we owe it to both America and our Airmen to modernize these systems.

Air Force Financial Management Evolution

Air Force Financial Management (FM) is also based on people, processes, and systems. The examples that follow illustrate some of the ways the Air Force FM community is proactively meeting future challenges and improving compliance and efficiency.

CFO Compliance

In 1990 the Chief Financial Officers Act was passed, ordering Federal agencies to centralize their financial systems to better account for their spending. In 1996, Congress passed the Federal Financial Management Improvement Act (FFMIA), enabling the advancement of Federal financial management by requiring that Federal financial management systems provide accurate, reliable, and timely financial management information to the government's managers.

Financial Services Transformation

The Financial Services Transformation establishes an innovative new way to deliver financial services to customers through an integrated end-to-end Financial Services Delivery Model (FSDM), providing superior customer service consistently across all geographies and theaters. The FSDM encompasses all areas of the FM organization from the base through the MAJCOMs to the Air Force Financial Services Center (AFFSC) at Ellsworth AFB, South Dakota, and all enabling technologies and processes that support how customers receive financial services. This effort began with the consolidation of back-office military pay and travel processing for 93 Active and Reserve bases into the AFFSC in September 2007. A 24/7 Contact Center is scheduled to open at the AFFSC in FY 2009. The future FSDM cohesively looks at all the elements that impact customers of FM financial delivery and looks to optimize the operations including organization, process, people, and technology.

With the standup of the AFFSC, the FM Community is able to dramatically reduce face-to-face customer interaction and

direct customers to self-service resources on the Air Force Portal or the Contact Center as the preferred option to initiate inquiries and transactions.

From the Comptroller Squadron through to the AFFSC, FM Personnel will have access to uniform processes, consistent roles, and a coordinated suite of resources. Customers receive the same answer whether they seek service online, at the AFFSC, or at their local Financial Service Office. Across the FSDM, process efficiencies are gained through centralization, benefiting the customer through quicker, more accurate, and more consistent pay transactions.



The first phase of Web Self-Service (WSS) is targeted for initial operating capability in early FY 2009 and additional functionality and new customer resources will continue to emerge. WSS, found on the Air Force Portal, will provide FAQs, a searchable index of questions, and other tools designed to resolve pay and travel questions. Looking ahead, the AFFSC is designed for full integration with Air Force Personnel Center and Air Reserve Personnel Center on the same technology platform allowing full customer visibility between centers and a range of service options through a single point of entry.

The FSDM of the future includes the integration of several enabling technologies to reduce functional overlaps and speed up time to deliver Integrated Operations. The enabling technologies are designed to provide access to all customer service assets from a single point of entry, enabling increased continuity of service through all channels of delivery.

Internal Controls

Air Force Financial Management Transformation, however, must be based on management integrity. To this end, we have put in place robust internal controls. The objectives of the system of internal accounting and administrative control of the Department of the Air Force are to provide reasonable assurance that:

- ▶ Obligations and costs comply with applicable law
- ▶ Funds, property, and other assets are safeguarded against waste, loss, unauthorized use, and misappropriation
- ▶ Revenues and expenditures applicable to Air Force operations are properly recorded and accounted for to



permit the preparation of accounts and reliable financial and statistical reports, and to maintain accountability over the assets, including nonappropriated fund activities

- ▶ Programs and administrative and operating functions are efficiently and effectively carried out in accordance with applicable law and management policy
- ▶ The internal control process emphasized prevention of waste, fraud, and mismanagement along with timely correction of internal control weaknesses

Internal Control Program Accomplishments and Highlights

The Federal Managers' Financial Integrity Act (FMFIA) implementation in the Air Force rests on a solid general control environment supported by positive endorsement from top management. FY 2008 was a year of strong internal control activity as our financial managers continued to integrate their job oversight responsibilities with the internal control program's evaluation procedures. Using pervasive technologies, MAJCOMs increased distribution of internal control information on their available Web sites.

During FY 2008, we continued to implement new program requirements directed in DoD Instruction 5010.40, Managers' Internal Control Program Procedures, in response to revised guidance in OMB Circular A-123, Management's Responsibility for Internal Control. The revised guidance included additional requirements to specifically address establishing and assessing internal controls over financial statement reporting. It also required the establishment of a senior assessment team to provide direction and oversight for the assessments.

The Office of the Under Secretary of Defense/Comptroller (OUSD/C) directed that our review encompass specific key focus areas material to DoD and the effectiveness of key business process internal controls, which significantly affect financial reports. During this year, we documented the required processes, performed risk analysis, developed swim-

lane flowcharts, and analyzed existing internal controls for the required focus areas. Based on this year's review effort, we identified three new material weaknesses, along with nine existing material weaknesses that were briefed to the Air Force Senior Assessment Team and approved to be included in the Secretary's Annual Statement of Assurance.

Continuous Improvement—AFSO21

During this time of reduced manpower and resources, Air Force Financial Management has taken action, by making Continuous Process Improvement (CPI) a priority. In 2008, SAF/FM completed several process improvement projects, on multiple cross-functional FM processes. Some of these included Centrally Billed Accounts, Travel Voucher Processing, Station Gain, Unexecuted Budget Authority, and Voucher Balancing. The process improvements, along with other project action items such as changes to policy and enhanced training, saved the Air Force time and money. The Air Force Financial Management staff collaborated with various cross functional stakeholders, such as the Defense Finance and Accounting Service (DFAS), United States Transportation Command (USTRANSCOM), Air Force Acquisition (SAF/AQ), Air Force Installations and Mission Support (AF/A7), and the Air Force Reserve Command (AFRC). The focus on end-to-end processes and cross-functional collaboration proved essential to ensure the process improvements were thorough and had a positive impact on the entire value stream.

In addition to leveraging AFSO21 tools and methods to conduct CPI and Lean events, SAF/FM is embedding continuous process improvement into its daily operations. We have developed Awareness Training to ensure that AFSO21 and CPI are introduced at the Air Staff, MAJCOM, and field levels. We take the opportunity to conduct AFSO21 workshops at leadership conferences such as the FMA/ALO World Wide Conference. FM leadership is committed to CPI concepts becoming intricate in the development of new business models. Organizations such as SAF/FMPI and FMB-BTO will continue to work to make continuous process improvement a way of life for Air Force Financial Management.

Air Force General Fund

The General Fund is the fund into which all receipts of the United States Government are deposited, except those from specific sources required by law to be deposited into other designated funds and from which appropriations are made by Congress to carry on the general and ordinary operations of the Government. The Notes to the Principal Statements provide more detail on the appropriations. The major appropriations in the Air Force General Fund and their uses are:

MILITARY PERSONNEL (MILPERS)

This appropriation provides funding for the care and feeding of our Airmen. It includes all direct military compensation for active duty, reserve, guard, and retired personnel including regular pay, allowances, and bonuses. Additionally, this appropriation funds all Permanent Change of Station (PCS) moves and supports a total force (active, reserve and guard) end strength of 502,800.

OPERATIONS AND MAINTENANCE (O&M)

This appropriation funds key readiness programs critical to prepare forces for combat operations and other peacetime missions. These include day-to-day operating costs such

as flying hours, depot maintenance, training, spare parts, and base operations. The FY 2008 appropriation supported 84 installations, produced over 1,200 pilots and funded approximately 1.4 million flying hours while sustaining an aircraft fleet of over 5,500 aircraft.

PROCUREMENT

This appropriation provides for purchase of aircraft, missiles, vehicles, electronic and telecommunications equipment, satellite and launch equipment, base maintenance and support equipment, and investment-type spares. The FY 2008 program supported the purchase of up to 177 aircraft including 20 F-22 Raptors.

RESEARCH, DEVELOPMENT, TEST AND EVALUATION

Provides funding for the research and development of next generation weapons and platforms and for the testing and evaluation of current prototypes and upgrades. The Air Force's top acquisition priorities are the Tanker replacement; the Combat Search and Rescue Helicopter; new space systems for early warning, targeting, communications, and navigation; the F-35A Joint Strike Fighter; and the New Bomber.

As one of the Air Force's top acquisition priorities officials are looking at proposals for a new strategic refueling aircraft, referred to as the KC-X, to replace the aging KC-135 Stratotanker.





A junior-enlisted multiplex under construction at Dover Air Force Base. At project completion in 2009, the 212 homes constructed in 2004 - 2005 will be joined by 768 new homes.

MILITARY CONSTRUCTION (MILCON)

Includes any construction, development, conversion, or extension of any kind carried out with respect to a military installation. Typically this appropriation applies to any projects that exceed \$1.5 million but can be applicable to projects exceeding a \$750 thousand threshold. A sub-element of this appropriation provides funding for family housing construction programs. The FY 2008 appropriation supported 86 Major and 4 Minor MILCON projects.

BASE REALIGNMENT AND CLOSURE (BRAC)

The law authorizes the BRAC accounts to fund one-time, nonrecurring costs that are a direct result of BRAC-directed base closure or realignment actions. Some costs do not qualify for BRAC funding as costs resulting from closure or realignment. The FY 2008 BRAC program was approximately \$1.1 billion.

Current and Future Financial Systems— DEAMS

Our systems enable us to maintain stewardship over the resources entrusted to us. The Defense Enterprise Accounting and Management System (DEAMS) is key to our current and future ability to manage the Air Force's resources. DEAMS was launched in August 2003 as a joint initiative of the Air Force, U.S. Transportation Command

(USTRANSCOM) and the DFAS under what is now the Defense Department's Business Transformation Agency. The DEAMS mission is to support the Nation's warfighters with timely, accurate, and reliable financial information, enabling more efficient and effective decision making by DoD managers. DEAMS is reengineering financial management activities with a unified enterprise architecture, standardized business rules and processes, and the first implementation of the new Standard Financial Information Structure.

The Air Force is implementing DEAMS through a two-increment development approach in five spirals. Spiral 1 is a commitment accounting technology demonstration that includes USTRANSCOM; Headquarters, Air Mobility Command; and Air Force active duty, Air National Guard and Air Force Reserve tenant organizations on or associated with Scott AFB, Illinois. With our partners at USTRANSCOM and DFAS, we took a major step forward in 2008 with that successful deployment.



Secretary of the Air Force Michael Donley addresses an Airmen's call audience during his visit to the 379th Air Expeditionary Wing. The secretary described his vision ahead for the Air Force, the challenges faced and the plan to move the Air Force into the future.

Spiral 2 will deploy in late 2009, taking the full Oracle I-Procurement functionality to those same units. Increment 2 will expand that capability to the remaining AMC bases and Army and Navy components of USTRANSCOM in Spiral 3. DEAMS will then be fielded to remaining MAJCOMs in two additional spirals over a period of three years. When fully fielded throughout the Air Force, DEAMS will transform financial management and set a new standard for effective and efficient stewardship of our Nation's Defense resources.

Air Force Working Capital Fund

The Air Force Working Capital Fund (AFWCF) supports Air Force warfighters and operations via three major business areas that function as revolving funds, i.e., suppliers charge users for the goods and services provided. Air Force Materiel Command (AFMC) manages more than 90% of AFWCF revenue and expense activity for Supply Management and Depot Maintenance activities. These functions provide goods and services to the Air Force and DoD customers, as well as customers outside the DoD (e.g., local and foreign governments). Supply Management provides expedited repair, replenishment, and inventory control for spare parts and associated logistics support services to fulfill Air Force needs during war and peacetime. Depot Maintenance provides economical and responsive repair, overhaul, and modification of aircraft, missiles, engines, other major end items, and associated components.

In FY 1998 the Air Force was appointed the Executive Agent for Transportation Working Capital Fund (TWCF) cash. Even though AFWCF manages TWCF's cash, daily operations are managed by the United States Transportation Command. As a result, TWCF's financial statements are reported with other Defense Agencies. The AFWCF allows the Air Force to accomplish the following:

- ▶ Ensure readiness through reduced support costs, stabilized rates, and responsive customer service
- ▶ Flexibility to respond to customer support needs in real-world situations
- ▶ Focus management attention on net operating results, including cost and performance
- ▶ Identify the total cost of providing support products and services
- ▶ Establish strong customer/provider relationships

Supply Management Activity Group

The Supply Management Activity Group (SMAG) provides policy, guidance, and resources to meet Air Force needs for spare parts. The SMAG manages approximately 1.6 million items including weapon systems spare parts, medical-dental supplies and equipment, and items used for non-weapon systems applications. The activity not only provides management of various inventories but also a wide range of logistics support services, to include requirements forecasting, item introduction, cataloging, provisioning, procurement, repair, technical support, data management, item disposal, distribution management, and transportation.



Air Force Working Capital Fund (AFWCF) supplies at Spangdahlem Air Base, Germany.

The SMAG consists of wholesale and retail operations. The Material Support Division (MSD) is the SMAG wholesale operation which is responsible for Air Force managed repairable and consumable spare parts. The SMAG retail operation is comprised of the General Support, Medical-Dental, and Air Force Academy Divisions. Although each division operates independently, all purchase large quantities of commodities that allows the Air Force to take advantage of economies of scale and achieve significant cost savings. The General Support Division (GSD) supports installation maintenance and administrative functions, field and depot maintenance of aircraft and other systems. The Medical-Dental Division provides supplies and equipment required to support a robust health care system for Air Force active military, retirees and family members. This division manages the Air Force war reserve materiel (WRM) requirement of medical supplies and equipment which is vital to support forces in combat and contingency operations. The Air Force Academy Division finances the purchase of uniforms and uniform accessories for sale to over 4,000 cadets.

AFMC manages MSD and GSD. The Air Force Medical Operations Agency manages the Medical-Dental Division, and the Air Force Academy's Mission Support Group manages the Air Force Academy Division. The activities support more than 80 Air Force installations located throughout the world.



A KC-135R Stratotanker sits inside the Oklahoma Air Logistics Center, Okla., waiting for a full maintenance overhaul. The Oklahoma Air Logistics Center is the worldwide manager for a wide range of aircraft, engines, software, avionics and accessories components.

SMAG Customer Support Performance Metrics

Mission Incapable (MICAP) and Customer Wait Time (CWT) metrics allow managers to assess quality of spares support provided and plan corrective action when needed. MICAP measures the number of hours a weapon system is not available due to non-availability of a spare part provided by MSD or GSD. CWT measures the average time elapsed between the customer demand and the delivery of a spare part to the customer, measured in days. MICAP hours for MSD managed items have improved significantly since 1999. MSD items accrued an average of five million MICAP hours during calendar year 2000. As of September 2008, MSD MICAP hours are 1.3 million. CWT is a newer metric but has also shown a significant improvement. The monthly average CWT for MSD items during 2004 was 7.4 days and has decreased to 5.8 days as of September 2008.

Depot Maintenance Activity Group

The Depot Maintenance Activity Group (DMAG) repairs systems and spare parts that ensure readiness in peacetime and provide sustainment to combat forces in wartime. In peacetime, the Air Force enhances readiness by efficiently and economically repairing, overhauling, and modifying aircraft, engines, missiles, components, and software to meet customer demands. The depots have unique skills and equipment required to support and overhaul both new, complex components as well as aging weapon systems.

A critical facet of the depots is that during wartime or contingencies, the Air Force can surge repair operations and realign capacity to support the warfighter's immediate needs. DMAG is managed by AFMC and employs over 21,000 personnel supporting four industrial locations.

DMAG sites include:

Ogden Air Logistics Center (OO-ALC), Ogden, Utah

Oklahoma City Air Logistics Center (OC-ALC), Oklahoma City, Oklahoma

Warner Robins Air Logistics Center (WR-ALC), Warner Robins, Georgia

Aerospace Maintenance and Regeneration Group (AMARG), Tucson, Arizona

DMAG Customer Support Performance Metrics

Due Date Performance and Quality Defect Rate metrics allow managers to assess production schedule and work quality. The Due Date Performance (ability of the depot to produce aircraft on the promised date) is 92% as of September 2008. The Quality Defect Rate (measures the number of production defects) is .23 defects per aircraft as of September 2008.

Air Force Working Capital Customers

AFWCF provides support to a variety of customers: Air Force Major Commands (including the Air National Guard and Air Force Reserve Command), the Army, the Navy, other WCFs, other government agencies, and foreign countries.

“The enduring responsibility of the United States Air Force is to provide strategic deterrence for the Nation and fly, fight and win as an integral part of the Joint team.”

- Gen. Norton Schwartz

Air Force Working Capital Financial Performance Measures

AFWCF tracks several metrics to assess financial performance. These measures are designed to achieve accountability at the appropriate level and also measure compliance with AFWCF budget objectives.

AFWCF assesses financial performance using the Net Operating Result (NOR) of an activity. The NOR is the difference between revenue and expenses, i.e., a bottom-line profit and loss indicator. The NOR objective of an activity group is to break even over a two-year period. Actual NORs are compared to the budget targets. Budget targets are identified in financial performance plans and are used to measure results during execution reviews. Prices are established to achieve this objective by recovering or returning prior year losses or gains. Revenues are amounts earned as a result of normal operations and usually result from sale of, or reimbursements for, goods and services provided to DoD activities, other federal government agencies, and the

public. Expenses are the resources used during an accounting period. Expenses occur from rendering services; acquiring, producing, or delivering goods; or carrying out other mission-related activities.

DoD cash management policy requires maintaining the minimum cash balance necessary to meet both operational requirements and disbursements in support of the capital investment program. Cash generated from operations is the primary means of maintaining adequate cash levels. Effective cash management is directly dependent on the availability of accurate and timely data on cash levels and operational results. Cash levels should be maintained to cover 7 to 10 days of operational costs as well as cash adequate to meet 6 months of capital disbursements.

Transformation Initiatives - eLog21

As introduced earlier, the eLog21 initiative is designed to bring logistics operations into the 21st century by modernizing processes and systems. As processes continue to improve, customers will receive the benefit of repaired weapon systems and spare parts at the right place, right time, and lowest cost. Two major initiatives included under the umbrella of e-Log21 are the Repair Network Transformation (RNT) and Global Logistics Support Center (GLSC).

The RNT establishes an enterprise-wide repair capability managed within a single supply chain. The GLSC is establishing an Air Force supply chain management capability that provides enterprise planning, global command and control, and a single focal point in support of logistics requirements.

Contract DMAG Closure

In FY 2003, the transition of contract depot maintenance out of the AFWCF began and completes at the end of FY 2008 when the activity stops accepting new orders. This change brings the user and provider of contract depot maintenance services closer together and removes the AFWCF from its current role as the “middleman.” This action will allow the depot managers to dedicate their time and efforts to organic production.

Flying Hour Revenue Recognition

In FY 2006, customers requested MSD and GSD simplify the billing process for reparable and consumable spare parts required to perform their flying hour mission. Analysis



UNITED STATES AIR FORCE



Maintenance on an F-16 Fighting Falcon at Balad Air Base, Iraq. The F-16 goes through an overhaul every 300 hours.

conducted by AFWCF analysts and flying hour customers determined a business model that would incorporate the customers' main objective to buy flying hour time, not spare parts. The cost of a flying hour represents the average cost of reparable and consumable parts required to fly an aircraft for one hour. Beginning 1st Quarter, FY 2008 AFWCF implemented the billing process change from recognizing revenue and receivables from the sale of a spare part to recognizing them on a flying hour basis.

Billing Elimination

In FY 2007 AFWCF began an initiative to eliminate billing transactions between MSD and DMAG. These activities still track assets and costs appropriately, but as of 1st Quarter FY 2008 MSD no longer bills DMAG for materiel purchases and DMAG no longer bills MSD for repair services. This initiative streamlined business processes and eliminated non-value added financial transactions.

Expeditionary Combat Support System (ECSS) Blueprinting

ECSS enables the transformation of Air Force Logistics by replacing the majority of legacy logistics systems with a single solution set of business processes, software applications, and data. ECSS will provide timely, consistent, and accurate information to enhance operations. The result will be standardized business processes and tools across the en-

tire enterprise, regardless of program or site. ECSS Process Area Blueprinting (Oct. 2007 - Jun. 2008) has defined how functions and capabilities of commercial software products and systems will support organizational and business needs. ECSS takes advantage of commercial best practices in driving end-to-end process designs and full integration of logistics activities.

Global War on Terrorism (GWOT) Support

The AFWCF is integral to the readiness and sustainability of Air Force weapon systems and the ability to deploy forces around the globe and across any theater in support of Global War on Terror operations and National Military Strategy requirements. Maintenance depots provide the equipment, skills, and repair services necessary to keep forces operating worldwide. Supply management activities procure and manage inventories of consumable and reparable spare parts required to keep all elements of the force structure mission ready.



An F-15E Strike Eagle crew chief assigned to the 492nd Expeditionary Aircraft Maintenance Unit salutes the pilot prior to his flight from Bagram Airfield, Afghanistan.

Directly or indirectly, AFWCF activities provide warfighters the key services needed to meet mission capability standards. For example, in 2008 GSD is procuring Individual Body Armor (IBA) and related equipment to protect warfighters. Additionally, the Medical-Dental Division's War Reserve Material (WRM) program provides supplies and equipment vital to support forces in combat for the first 60 days of a contingency operation, and provides basic force health protection to all deploying Air Force active, reserve, and guard personnel.


Financing the Fight

We are a country at war with an enemy that is elusive and unconventional. The Air Force has been, and must expect to be, in combat for years to support this effort in innovative ways. This requires creative thinking and action, not just from operational forces but from all the forces that support them. We are also rightly expected to be good stewards of our nation's—indeed our people's—resources.

Air Force professional Financial Management personnel are making that happen. They know they are part of a larger Air Force but play a key role. They have streamlined pay information to make it easier for Airmen to access, they are efficiently overseeing our financial transactions, and they have dedicated themselves to support our warfighting forces.

This applies across the board – deployed military and civilian – in supporting the national security goals of our country. They are indeed, “Financing the Fight.”





1. ASSETS (NOTE 2)

A. Intragovernmental:

1. Fund Balance with Treasury (Note 3)

a. Entity

b. Non-Entity Seized Iraqi Cash

c. Non-Entity-Other

2. Investments (Note 4)

3. Accounts Receivable (Note 5)

4. Other Assets (Note 6)

5. Total Intragovernmental Assets

B. Cash and Other Monetary Assets (Note 7)

C. Accounts Receivable, Net (Note 5)

D. Loans Receivable (Note 8)

E. Inventory and Related Property, Net (Note 9)

F. General Property, Plant and Equipment, Net (Note 10)

G. Investments (Note 4)

H. Other Assets (Note 6)

2. TOTAL ASSETS

3. LIABILITIES (NOTE 11)

A. Intragovernmental

1. Accounts Payable (Note 12)

2. Debt (Note 13)

3. Other Liabilities (Note 15 & 16)

4. Total Intragovernmental Liabilities

B. Accounts Payable (Note 12)

C. Military Retirement and Other Federal Employment Benefits (Note 17)

D. Environmental and Disposal Liabilities (Note 14)

E. Loan Guarantee Liability (Note 8)

F. Other Liabilities (Note 15 & Note 16)

4. TOTAL LIABILITIES

5. NET POSITION

A. Unexpended Appropriations - Earmarked Funds (Note 24)

B. Unexpended Appropriations - Other Funds

C. Cumulative Results of Operations - Earmarked Funds

D. Cumulative Results of Operations - Other Funds

6. TOTAL NET POSITION

7. TOTAL LIABILITIES AND NET POSITION

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

Fiscal Year 2008

Annual Financial Statements





Limitations to the Financial Statements

The principal financial statements have been prepared to report the financial position and results of operations of the entity, pursuant to the requirements of Title 31, United States Code, Section 3515 (b). While the statements have been prepared from the books and records of the entity, in accordance with Generally Accepted Accounting Principles for Federal entities and the formats prescribed by Office of Management and Budget, the statements are in addition to the financial reports used to monitor and control budgetary resources which are prepared from the same books and records. The statements should be read with the realization that they are for a component of the U.S. Government, a sovereign entity.



General Fund Principal Statements

Fiscal Year 2008

The FY 2008 Department of the Air Force General Fund Principal Statements and related notes are presented in the format prescribed by the Department of Defense Financial Management Regulation 7000.14-R, Volume 6B. The statements and related notes summarize financial information for individual activity groups and activities within the General Fund for the fiscal year ending September 30, 2008, and are presented on a comparative basis with information previously reported for the fiscal year ending September 30, 2007.

The following statements comprise the Department of the Air Force General Fund Principal Statements:

Consolidated Balance Sheet

The Consolidated Balance Sheet presents as of September 30, 2008 and 2007 those resources owned or managed by the Air Force which are available to provide future economic benefits (assets); amounts owed by the Air Force that will require payments from those resources or future resources (liabilities); and residual amounts retained by the Air Force, comprising the difference (net position).

Consolidated Statement of Net Cost

The Consolidated Statement of Net Cost presents the net cost of the Air Force's operations for the years ended September 30, 2008 and 2007. The Air Force's net cost of operations includes the gross costs incurred by the Air Force less any exchange revenue earned from Air Force activities.

Consolidated Statement of Changes in Net Position

The Consolidated Statement of Changes in Net Position presents the change in the Air Force's net position resulting from the net cost of Air Force's operations, budgetary financing sources other than exchange revenues, and other financing sources for the years ended September 30, 2008 and 2007.

Combined Statement of Budgetary Resources

The Combined Statement of Budgetary Resources presents the budgetary resources available to the Air Force during FY 2008 and 2007, the status of these resources at September 30, 2008 and 2007, and the outlay of budgetary resources for the years ended September 30, 2008 and 2007.

The Principal Statements and related notes have been prepared to report financial position pursuant to the requirements of the Chief Financial Officers Act of 1990, the Government Management Reform Act of 1994, and the Office of Management and Budget's Circular A-136, "Financial Reporting Requirements."



Consolidated Balance Sheet - General Fund

As of September 30, 2008 and 2007 (\$ in thousands)

	2008 Consolidated	2007 Consolidated
1. ASSETS (NOTE 2)		
A. Intragovernmental:		
1. Fund Balance with Treasury (Note 3)	\$ 92,909,909	\$ 80,126,396
2. Investments (Note 4)	874	823
3. Accounts Receivable (Note 5)	271,020	388,823
4. Other Assets (Note 6)	265,591	423,952
5. Total Intragovernmental Assets	\$ 93,447,394	\$ 80,939,994
B. Cash and Other Monetary Assets (Note 7)	111,976	107,908
C. Accounts Receivable, Net (Note 5)	502,182	545,796
D. Loans Receivable (Note 8)	0	0
E. Inventory and Related Property, Net (Note 9)	46,906,666	46,335,059
F. General Property, Plant and Equipment, Net (Note 10)	148,770,371	143,257,880
G. Investments (Note 4)	0	0
H. Other Assets (Note 6)	11,030,527	10,448,818
2. TOTAL ASSETS	\$ 300,769,116	\$ 281,635,455
3. STEWARDSHIP PROPERTY, PLANT & EQUIPMENT (Note 10)		
4. LIABILITIES (Note 11)		
A. Intragovernmental:		
1. Accounts Payable (Note 12)	\$ 2,002,120	\$ 1,509,631
2. Debt (Note 13)	0	0
3. Other Liabilities (Note 15 & 16)	1,952,785	2,033,326
4. Total Intragovernmental Liabilities	\$ 3,954,905	\$ 3,542,957
B. Accounts Payable (Note 12)	3,810,935	3,189,763
C. Military Retirement and Other Federal Employment Benefits (Note 17)	1,163,414	1,137,016
D. Environmental and Disposal Liabilities (Note 14)	8,266,375	6,898,867
E. Loan Guarantee Liability (Note 8)	0	0
F. Other Liabilities (Note 15 & Note 16)	6,379,597	6,081,496
5. TOTAL LIABILITIES	\$ 23,575,226	\$ 20,850,099
6. COMMITMENTS AND CONTINGENCIES (NOTE 16)		
7. NET POSITION		
A. Unexpended Appropriations - Earmarked Funds (Note 23)	\$ 0	\$ 0
B. Unexpended Appropriations - Other Funds	92,171,366	80,465,487
C. Cumulative Results of Operations - Earmarked Funds	5,355	4,548
D. Cumulative Results of Operations - Other Funds	185,017,169	180,315,321
8. TOTAL NET POSITION	\$ 277,193,890	\$ 260,785,356
9. TOTAL LIABILITIES AND NET POSITION	\$ 300,769,116	\$ 281,635,455

Consolidated Statement of Net Cost - General Fund

As of September 30, 2008 and 2007 (\$ in thousands)

	2008 Consolidated	2007 Consolidated
	<hr/>	<hr/>
1. Program Costs (Note 18)		
A. Gross Costs	\$ 148,089,758	\$ 142,462,370
B. (Less: Earned Revenue)	-5,875,708	-5,715,540
C. Net Program Costs	<hr/> \$ 142,214,050	<hr/> \$ 136,746,830
2. Cost Not Assigned to Programs	0	0
3. (Less: Earned Revenue Not Attributable to Programs)	0	0
4. Net Cost of Operations	<hr/> \$ 142,214,050 <hr/>	<hr/> \$ 136,746,830 <hr/>



Consolidated Statement of Changes in Net Position - General Fund

As of September 30, 2008 and 2007 (\$ in thousands)

	2008 Earmarked Funds	2008 All Other Funds	2008 Eliminations
CUMULATIVE RESULTS OF OPERATIONS			
1. Beginning Balances	\$ 4,546	\$ 180,315,323	\$ 0
2. Prior Period Adjustments:			
A. Changes in accounting principles (+/-)	0	0	0
B. Corrections of errors (+/-)	0	0	0
3. Beginning balances, as adjusted	<u>\$ 4,546</u>	<u>\$ 180,315,323</u>	<u>\$ 0</u>
4. Budgetary Financing Sources:			
A. Other adjustments (rescissions, etc.)	0	0	0
B. Appropriations used	0	144,550,203	0
C. Nonexchange revenue	1,088	0	0
D. Donations and forfeitures of cash and cash equivalents	2,544	0	0
E. Transfers-in/out without reimbursement (+/-)	0	88,000	0
F. Other budgetary financing sources	0	-157	0
5. Other Financing Sources:			
A. Donations and forfeitures of property	0	0	0
B. Transfers-in/out without reimbursement (+/-)	0	322,962	0
C. Imputed financing from costs absorbed by others	0	628,882	0
D. Other (+/-)	0	1,323,183	0
6. Total Financing Sources	<u>\$ 3,632</u>	<u>\$ 146,913,073</u>	<u>\$ 0</u>
7. Net Cost of Operations (+/-)	<u>2,823</u>	<u>142,211,227</u>	<u>0</u>
8. Net Change	<u>\$ 809</u>	<u>\$ 4,701,846</u>	<u>\$ 0</u>
9. Cumulative Results of Operations	<u>\$ 5,355</u>	<u>\$ 185,017,169</u>	<u>\$ 0</u>
UNEXPENDED APPROPRIATIONS			
10. Beginning Balances	\$ 0	\$ 80,465,487	\$ 0
11. Prior Period Adjustments:			
A. Changes in accounting principles	0	0	0
B. Corrections of errors	0	0	0
12. Beginning balances, as adjusted	<u>\$ 0</u>	<u>\$ 80,465,487</u>	<u>\$ 0</u>
13. Budgetary Financing Sources:			
A. Appropriations received	0	156,788,176	0
B. Appropriations transferred-in/out	0	2,662,362	0
C. Other adjustments (rescissions, etc.)	0	-3,194,456	0
D. Appropriations used	0	-144,550,203	0
14. Total Budgetary Financing Sources	0	11,705,879	0
15. Unexpended Appropriations	0	92,171,366	0
16. Net Position	<u><u>\$ 5,355</u></u>	<u><u>\$ 277,188,535</u></u>	<u><u>\$ 0</u></u>

Annual Financial Statement **2008**

General Fund

Principal Statements

2008 Consolidated	2007 Earmarked Funds	2007 All Other Funds	2007 Eliminations	2007 Consolidated
\$ 180,319,869	\$ 4,540	\$ 180,854,184	\$ 0	\$ 180,858,724
0	0	0	0	0
0	0	0	0	0
<u>\$ 180,319,869</u>	<u>\$ 4,540</u>	<u>\$ 180,854,184</u>	<u>\$ 0</u>	<u>\$ 180,858,724</u>
0	0	0	0	0
144,550,203	0	136,203,035	0	136,203,035
1,088	928	5	0	933
2,544	1,843	0	0	1,843
88,000	0	282,000	0	282,000
-157	0	0	0	0
0	0	0	0	0
322,962	0	261,389	0	261,389
628,882	0	724,671	0	724,671
1,323,183	0	-1,265,895	0	-1,265,895
<u>\$ 146,916,705</u>	<u>\$ 2,771</u>	<u>\$ 136,205,205</u>	<u>\$ 0</u>	<u>\$ 136,207,976</u>
142,214,050	2,765	136,744,066	0	136,746,831
<u>\$ 4,702,655</u>	<u>\$ 6</u>	<u>\$ -538,861</u>	<u>\$ 0</u>	<u>\$ -538,855</u>
<u>\$ 185,022,524</u>	<u>\$ 4,546</u>	<u>\$ 180,315,323</u>	<u>\$ 0</u>	<u>\$ 180,319,869</u>
\$ 80,465,487	\$ 0	\$ 70,186,334	\$ 0	\$ 70,186,334
0	0	0	0	0
0	0	0	0	0
<u>\$ 80,465,487</u>	<u>\$ 0</u>	<u>\$ 70,186,334</u>	<u>\$ 0</u>	<u>\$ 70,186,334</u>
156,788,176	0	147,671,923	0	147,671,923
2,662,362	0	579,271	0	579,271
-3,194,456	0	-1,769,006	0	-1,769,006
-144,550,203	0	-136,203,035	0	-136,203,035
11,705,879	0	10,279,153	0	10,279,153
92,171,366	0	80,465,487	0	80,465,487
<u><u>\$ 277,193,890</u></u>	<u><u>\$ 4,546</u></u>	<u><u>\$ 260,780,810</u></u>	<u><u>\$ 0</u></u>	<u><u>\$ 260,785,356</u></u>

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



Combined Statement of Budgetary Resources - General Fund

As of September 30, 2008 and 2007 (\$ in thousands)

	2008 Combined	2007 Combined
BUDGETARY FINANCING ACCOUNTS		
BUDGETARY RESOURCES:		
1. Unobligated balance, brought forward, October 1	\$ 21,175,345	\$ 17,112,927
2. Recoveries of prior year unpaid obligations	4,602,017	3,921,941
3. Budget authority		
A. Appropriation	156,791,805	147,674,697
B. Borrowing authority	0	0
C. Contract authority	0	0
D. Spending authority from offsetting collections		
1. Earned		
a. Collected	10,464,416	10,237,677
b. Change in receivables from Federal sources	-354,080	-517,749
2. Change in unfilled customer orders		
a. Advance received	-199,948	376,618
b. Without advance from Federal sources	38,934	250,810
3. Anticipated for rest of year, without advances	0	0
4. Previously unavailable	0	0
5. Expenditure transfers from trust funds	0	0
E. Subtotal	\$ 166,741,127	\$ 158,022,053
4. Nonexpenditure transfers, net, anticipated and actual	2,750,362	861,271
5. Temporarily not available pursuant to Public Law	0	0
6. Permanently not available	-3,194,456	-1,769,006
7. Total Budgetary Resources	\$ 192,074,395	\$ 178,149,186
STATUS OF BUDGETARY RESOURCES:		
8. Obligations incurred:		
A. Direct	\$ 155,042,972	\$ 146,524,833
B. Reimbursable	10,354,532	10,449,009
C. Subtotal	\$ 165,397,504	\$ 156,973,842
9. Unobligated balance:		
A. Apportioned	24,139,914	18,573,839
B. Exempt from apportionment	3,820	3,271
C. Subtotal	\$ 24,143,734	\$ 18,577,110
10. Unobligated balance not available	2,533,157	2,598,234
11. Total status of budgetary resources	\$ 192,074,395	\$ 178,149,186
CHANGE IN OBLIGATED BALANCE:		
12. Obligated balance, net		
A. Unpaid obligations, brought forward, October 1	\$ 60,933,360	\$ 53,989,101
B. Less: Uncollected customer payments from Federal sources, brought forward, October 1	-2,366,785	-2,633,723
C. Total unpaid obligated balance	\$ 58,566,575	\$ 51,355,378
13. Obligations incurred net (+/-)	\$ 165,397,504	\$ 156,973,842
14. Less: Gross outlays	-153,915,590	-146,107,640
15. Obligated balance transferred, net		
A. Actual transfers, unpaid obligations (+/-)	0	0
B. Actual transfers, uncollected customer payments from Federal sources (+/-)	0	0
C. Total Unpaid obligated balance transferred, net	\$ 0	\$ 0
16. Less: Recoveries of prior year unpaid obligations, actual	\$ -4,602,017	\$ -3,921,941
17. Change in uncollected customer payments from Federal sources (+/-)	315,146	266,938
18. Obligated balance, net, end of period		
A. Unpaid obligations	67,813,257	60,933,360
B. Less: Uncollected customer payments (+/-) from Federal sources (-)	-2,051,639	-2,366,785
C. Total, unpaid obligated balance, net, end of period	65,761,618	58,566,575
NET OUTLAYS		
19. Net Outlays:		
A. Gross outlays	\$ 153,915,590	\$ 146,107,640
B. Less: Offsetting collections	-10,264,468	-10,614,293
C. Less: Distributed Offsetting receipts	-201,497	-140,980
D. Net Outlays	\$ 143,449,625	\$ 135,352,367

General Fund

Fiscal Year 2008

Notes to the Principal Statements

Notes to the financial statements communicate information essential for fair presentation of the financial statements that is not displayed on the face of the financial statements.



Note 1. Significant Accounting Policies

1.A. Basis of Presentation

These financial statements have been prepared to report the financial position and results of operations of the Air Force, as required by the Chief Financial Officers Act of 1990, expanded by the Government Management Reform Act of 1994, and other appropriate legislation. The financial statements have been prepared from the books and records of the Air Force in accordance with the Department of Defense (DoD), Financial Management Regulation (FMR), Office of Management and Budget (OMB) Circular A-136, "Financial Reporting Requirements," and to the extent possible generally accepted accounting principles (GAAP). The accompanying financial statements account for all resources for which the Air Force is responsible unless otherwise noted.

Information relative to classified assets, programs, and operations is excluded from the statements or otherwise aggregated and reported in such a manner that it is not discernable.

The Air Force is unable to fully implement all elements of GAAP and OMB Circular A-136 due to limitations of its financial and nonfinancial management processes and systems that feed into the financial statements. The Air Force derives its reported values and information for major asset and liability categories largely from nonfinancial systems, such as inventory and logistic systems. These systems were designed to support reporting requirements for maintaining accountability over assets and reporting the status of federal appropriations rather than preparing financial statements in accordance with GAAP. The Air Force continues to implement process and system improvements addressing these limitations.

The Air Force incorporates internal controls, reconciliations, management by exception reports, and other management control information into its accounting processes to establish reliability and relevance of the financial information. When possible, the financial statements are presented on the accrual basis of accounting, as required by federal accounting standards.

The Air Force currently has twelve identified financial statement material weaknesses: (1) Financial Management Systems, (2) Intragovernmental Eliminations, (3) Unsupported Accounting Entries, (4) Fund Balance with Treasury, (5) Environmental Liabilities, (6) General Property, Plant, and Equipment, (7) Governmental Property and Material in Possession of Contractors, (8) Operating Materials and Supplies, (9) Statement of Net Cost, (10) Reconciliation of Net Cost of Operations to Budget, (11) Accounts Payable, and (12) Accounts Receivable. These findings are being addressed with corrective actions in the Financial Improvement Plan.

1.B. Mission of the Reporting Entity

The United States Air Force was created on September 18, 1947, by the National Security Act of 1947. The National Security Act Amendments of 1949 established DoD and made the Air Force a department within DoD. The overall mission of the Air Force is to fly, fight and win...in air, space and cyberspace.

1.C. Appropriations and Funds

The Air Force receives its appropriations and funds as general, trust, special, and deposit funds. The Air Force uses these appropriations and funds to execute its missions and subsequently report on resource usage.

General funds are used for financial transactions funded by congressional appropriations, including personnel, operation and maintenance, research and development, procurement, and military construction accounts. Trust funds contain receipts and expenditures of funds held in trust by the government for use in carrying out specific purposes or programs in accor-

dance with the terms of the donor, trust agreement, or statute. Certain trust and special funds may be designated as earmarked funds. Earmarked funds are financed by specifically identified revenues, required by statute to be used for designated activities, benefits or purposes, and remain available over time. Earmarked funds also have a requirement to account for and report on the receipt, use and retention of revenues and other financing sources that distinguish them from general revenues.

Special fund accounts are used to record government receipts reserved for a specific purpose.

Deposit funds are used to record amounts held temporarily until paid to the appropriate government or public entity. The Air Force is acting as an agent or custodian for funds awaiting distribution.

The Air Force is a party to allocation transfers with other federal agencies as a transferring (parent) entity and a receiving (child) entity. Allocation transfers are legal delegations by one agency of its authority to obligate budget authority and outlay funds for another agency. Generally, all financial activity related to these allocation transfers (e.g. budget authority, obligations, outlays) is reported in the financial statements of the parent entity.

Exceptions to this general rule apply to specific funds for which OMB has directed that all activity be reported in the financial statements of the child entity. Exceptions include all U.S. Treasury-Managed Trust Funds, Executive Office of the President (EOP), and all other funds specifically designated by OMB. The Air Force is a party to allocation transfers as the child for EOP (Foreign Military Sales – Military Assistance Program) meeting OMB exception, however, the activities for this fund is reported separately from DoD financial statements. In addition, the Air Force is a party to allocation transfers as the child for the Department of Agriculture.

The Air Force allocates funds, as the parent, to the Department of Transportation. The accounts used to prepare the financial statements are categorized as either entity or nonentity. The Air Force accounts consist of resources that are available for use in the operations of the entity. The Air Force is authorized to decide how to use resources in entity accounts or may be legally obligated to use these resources to meet entity obligations. Nonentity accounts, on the other hand, consist of assets that are held by an entity but that are not available for use in the operations of the entity. The following is a list of the major Air Force account numbers and titles (all accounts are entity accounts unless otherwise noted):

Air Force Account Number	Title
57 * 0704	Military Family Housing (O&M and Construction), Air Force
57 * 0740	Military Family Housing (Construction), Air Force
57 * 0745	Military Family Housing (O&M), Air Force
57 * 0810	Environmental Restoration, Air Force
57 * 1007	Medicare Eligible Retiree Health Fund Contributions, Air Force
57 * 1008	Medicare Eligible Retiree Health Fund Contributions, Air Force Reserve
57 * 1009	Medicare Eligible Retiree Health Fund Contributions, Air National Guard
57 * 3010	Aircraft Procurement, Air Force
57 * 3011	Procurement of Ammunition, Air Force
57 * 3020	Missile Procurement, Air Force
57 * 3080	Other Procurement, Air Force
57 * 3300	Military Construction, Air Force
57 * 3400	Operation and Maintenance (O&M), Air Force
57 * 3500	Military Personnel, Air Force
57 * 3600	Research, Development, Testing, and Evaluation (RDT&E), AF



57 * 3700	Personnel, Air Force Reserve
57 * 3730	Military Construction, Air Force Reserve
57 * 3740	Operation and Maintenance (O&M), Air Force Reserve
57 * 3830	Military Construction, Air National Guard
57 * 3840	Operation and Maintenance (O&M), Air National Guard
57 * 3850	Personnel, Air National Guard
57 X 5095	Wildlife Conservation, etc., Military Reservations, Air Force
57 X 8418	Air Force Cadet Fund
57 X 8928	Air Force General Gift Fund
57 * 3XXX (Incl Nonentity)	Budget Clearing Accounts
57 * 6XXX (Nonentity)	Deposit Fund Accounts
57 **** (Nonentity)	Receipt Accounts

1.D. Basis of Accounting

For FY 2008, the Air Force’s financial management systems are unable to meet all of the requirements for full accrual accounting. Many of the Air Force’s financial and nonfinancial feeder systems and processes were designed and implemented prior to the issuance of GAAP for federal agencies. These systems were not designed to collect and record financial information on the full accrual accounting basis as required by GAAP. Most of the Air Force’s (financial and nonfinancial) legacy systems were designed to record information on a budgetary basis. However, some accounts such as civilian pay, military pay and accounts payable are presented on the accrual basis of accounting on the financial statements, as required by federal accounting standards.

The DoD has undertaken efforts to determine the actions required to bring its financial and nonfinancial feeder systems and processes into compliance with GAAP. One such action is the current revision of its accounting systems to record transactions based on the U.S. Standard General Ledger (USSGL). Until all of the Air Force’s financial and nonfinancial feeder systems and processes are updated to collect and report financial information as required by GAAP, the Air Force’s financial data will be derived from budgetary transactions (obligations), transactions from nonfinancial feeder systems, and accruals made for major items such as payroll expenses, accounts payable, and environmental liabilities.

1.E. Revenues and Other Financing Sources

The Air Force receives congressional appropriations as financing sources for general funds on either an annual or multi-year basis. When authorized by legislation, these appropriations are supplemented by revenues generated by sales of goods or services. The Air Force recognizes revenue as a result of costs incurred for goods or services provided to other federal agencies and the public. Full cost pricing is the Air Force’s standard policy for services provided as required by OMB Circular A-25, Transmittal Memorandum #1, User Charges. The Air Force recognizes revenue when earned within the constraints of current system capabilities. In some instances, revenue is recognized when bills are issued.

The Air Force does not include nonmonetary support provided by U.S. allies for common defense and mutual security in amounts reported in the Statement of Net Cost and the Note 21, Reconciliation of Net Cost of Operations to Budget. The U.S. has cost sharing agreements with other countries. Examples include countries where there is a mutual or reciprocal defense agreement, where U.S. troops are stationed, or where the U.S. fleet is in a port.

1.F. Recognition of Expenses

For financial reporting purposes, DoD policy requires the recognition of operating expenses in the period incurred. However, because the Air Force's financial and nonfinancial feeder systems were not designed to collect and record financial information on the full accrual accounting basis, accruals are made for major items such as payroll expenses, accounts payable, environmental liabilities, and unbilled revenue. In the case of Operating Materials and Supplies (OM&S), operating expenses are generally recognized when the items are purchased. Efforts are underway to transition towards the consumption method for recognizing OM&S expenses.

1.G. Accounting for Intragovernmental Activities

Preparation of reliable financial statements requires the elimination of transactions occurring among entities within DoD or between two or more federal agencies. However, the Air Force cannot accurately eliminate intragovernmental transactions by customer because the Air Force's systems do not track at the transaction level. Generally, seller entities within DoD provide summary seller-side balances for revenue, accounts receivable, and unearned revenue to the buyer-side internal DoD accounting offices. In most cases the buyer-side records are adjusted to agree with DoD seller-side balances. IntraDoD balances are then eliminated. The volume of intragovernmental transactions is so large that after-the-fact reconciliations cannot be accomplished effectively with existing or foreseeable resources. The DoD is developing long-term system improvements to ensure accurate intragovernmental information, to include sufficient up-front edits and controls eliminating the need for after-the-fact reconciliations.

The U.S. Treasury Financial Management Service is responsible for eliminating transactions between DoD and other federal agencies. The Treasury Financial Manual, Part 2 – Chapter 4700, "Agency Reporting Requirements for the Financial Report of the United States Government," and the U.S. Treasury's "Federal Intragovernmental Transactions Accounting Policy Guide," provide guidance for reporting and reconciling intragovernmental balances. While the Air Force is unable to fully reconcile intragovernmental transactions with all federal partners, the Air Force is able to reconcile balances pertaining to investments in federal securities, Federal Employees' Compensation Act transactions with the Department of Labor, and benefit program transactions with the Office of Personnel Management.

The DoD's proportionate share of public debt and related expenses of the Federal Government are not included. The Federal Government does not apportion debt and its related costs to federal agencies. The DoD's financial statements, therefore, do not report any portion of the public debt or interest thereon, nor do the statements report the source of public financing whether from issuance of debt or tax revenues.

Financing for the construction of DoD facilities is obtained through appropriations. To the extent this financing ultimately may have been obtained through the issuance of public debt, interest costs have not been capitalized since the U.S. Treasury does not allocate such interest costs to the benefiting agencies.

1.H. Transactions with Foreign Governments and International Organizations

Each year, the Air Force sells defense articles and services to foreign governments and international organizations under the provisions of the "Arms Export Control Act of 1976." Under the provisions of the Act, DoD has authority to sell defense articles and services to foreign countries and international organizations generally at no profit or loss to the U.S. Government. Payment in U.S. dollars is required in advance.



1.I. Funds with the U.S. Treasury

The Air Force's monetary resources are maintained in U.S. Treasury accounts. The disbursing offices of the Defense Finance and Accounting Service (DFAS), the Military Departments, the U.S. Army Corps of Engineers (USACE), and the Department of State's financial service centers process the majority of the Air Force's cash collections, disbursements, and adjustments worldwide. Each disbursing station prepares monthly reports to the U.S. Treasury on check issues, electronic fund transfers, interagency transfers, and deposits.

In addition, the DFAS sites and USACE Finance Center submit reports to the U.S. Treasury by appropriation on interagency transfers, collections received, and disbursements issued. The U.S. Treasury records these transactions to the applicable Fund Balance with Treasury (FBWT) account. The Air Force's recorded balance in FBWT accounts and U.S. Treasury's FBWT accounts must balance monthly.

1.J. Foreign Currency

Cash is the total of cash resources under the control of DoD, which includes coin, paper currency, negotiable instruments, and amounts held for deposit in banks and other financial institutions. Foreign currency consists of the total U.S. dollar equivalent of both purchased and nonpurchased foreign currencies held in foreign currency fund accounts.

The majority of cash and all foreign currency is classified as nonentity and is restricted. Amounts reported consist primarily of cash and foreign currency held by disbursing officers to carry out their paying, collecting, and foreign currency accommodation exchange missions.

The Air Force conducts a significant portion of its operations overseas. The Congress established a special account to handle the gains and losses from foreign currency transactions for five general fund appropriations: operations and maintenance, military personnel, military construction, family housing operations and maintenance, and family housing construction. The gains and losses are computed as the variance between the exchange rate current at the date of payment and a budget rate established at the beginning of each fiscal year. Foreign currency fluctuations related to other appropriations require adjustments to the original obligation amount at the time of payment. The Air Force does not separately identify currency fluctuation transactions.

1.K. Accounts Receivable

As presented in the Balance Sheet, accounts receivable include three categories: accounts, claims, and refunds receivable from other federal entities or from the public. The allowance for uncollectible for the Air Force entity receivables is computed based on the average annual write off over a five year period. The DoD does not recognize an allowance for estimated uncollectible amounts from other federal agencies. Claims against other federal agencies are to be resolved between the agencies in accordance with dispute resolution procedures defined in the Intragovernmental Business Rules published in the Treasury Financial Manual.

1.L. Direct Loans and Loan Guarantees

Not Applicable

1.M. Inventories and Related Property

The Air Force manages only military or government specific materiel under normal conditions. Materiel is a unique term that relates to military force management, and includes all items (including self-propelled weapons, aircraft, etc., and

related spares, repair parts, and support equipment, but excluding real property, installations, and utilities) necessary to equip, operate, maintain, and support military activities without distinction as to its application for administrative or combat purposes. Items commonly used in and available from the commercial sector are not managed in the Air Force materiel management activities. The Air Force only holds materiel based on military need and support for contingencies.

Related property includes OM&S and stockpile materials. The majority of OM&S, with the exception of munitions not held for sale, are valued using the moving average cost method. Munitions not held for sale are valued at standard purchase price. The Air Force uses both the consumption method and the purchase method of accounting for OM&S. Items that are centrally managed and stored, such as ammunition and engines, are generally recorded using the consumption method and are reported on the Balance Sheet as OM&S. When current systems cannot fully support the consumption method, the Air Force uses the purchase method. Under this method, materiel and supplies are expensed when purchased. During FY 2008, the Air Force expensed significant amounts using the purchase method because the systems could not support the consumption method or management deemed that the item was in the hands of the end user. This is a material weakness for the DoD and long-term system corrections are in process. Once the proper systems are in place, these items will be accounted for under the consumption method of accounting.

The Air Force determined that the recurring high dollar value of OM&S in need of repair is material to the financial statements and requires a separate reporting category. Many high dollar items, such as aircraft engines, are categorized as OM&S rather than military equipment.

The Air Force recognizes condemned materiel as “Excess, Obsolete, and Unserviceable.” The cost of disposal is greater than the potential scrap value; therefore, the net value of condemned materiel is zero. Potentially redistributed materiel, presented in previous years as “Excess, Obsolete, and Unserviceable,” is included in the “Held for Use” or “Held for Repair” categories according to its condition.

The DoD does not attempt to account separately for “inventory held for sale” and “inventory held in reserve for future sale” based on SFFAS No. 3 definition, unless otherwise noted as it applies to OM&S.

1.N. Investments in U.S. Treasury Securities

The Air Force reports investments in U.S. Treasury securities at cost, net of amortized premiums or discounts. Premiums or discounts are amortized over the term of the investment using the effective interest rate method or another method obtaining similar results. The Air Force’s intent is to hold investments to maturity, unless they are needed to finance claims or otherwise sustain operations. Consequently, a provision is not made for unrealized gains or losses on these securities.

The Air Force invests in nonmarketable market-based U.S. Treasury securities. These are U.S. Treasury securities that are issued by the Bureau of Public Debt to federal agencies. They are not traded on any securities exchange but mirror the prices of particular U.S. Treasury securities traded in the government securities market.

1.O. General Property, Plant and Equipment

The Air Force uses the estimated historical cost for valuing military equipment. The DoD identified the universe of military equipment by accumulating information relating to program funding and associated military equipment, equipment useful life, program acquisitions, and disposals to establish a baseline. The military equipment baseline is updated using expenditure, acquisition and disposals information.



The Air Force's General Property, Plant and Equipment (General PP&E) capitalization threshold is \$100 thousand except for real property which is \$20 thousand. The Air Force has implemented the \$20 thousand real property threshold. The Air Force is currently using the capitalization threshold of \$100 thousand for all General PP&E.

General PP&E assets are capitalized at historical acquisition cost when an asset has a useful life of two or more years and when the acquisition cost equals or exceeds the DoD capitalization threshold. The DoD also requires the capitalization of improvements to existing General PP&E assets if the improvements equal or exceed DoD capitalization threshold and extend the useful life or increase the size, efficiency, or capacity of the asset. The DoD depreciates all General PP&E, other than land, on a straight-line basis.

General PP&E previously capitalized at amounts below \$100 thousand was written off General Fund financial statements in FY 1998.

When it is in the best interest of the government, the Air Force provides government property to contractors to complete contract work. The Air Force either owns or leases such property, or it is purchased directly by the contractor for the government based on contract terms. When the value of contractor-procured General PP&E exceeds DoD capitalization threshold, federal accounting standards require that it be reported on the Air Force's Balance Sheet.

The DoD is developing new policies and a contractor reporting process for Government Furnished Equipment that will provide appropriate General PP&E information for future financial statement reporting purposes. Accordingly, Air Force reports only government property in the possession of contractors that is maintained in Air Force's property systems. The DoD has issued new property accountability and reporting requirements that require Air Force to maintain, in their property systems, information on all property furnished to contractors. This action and other DoD proposed actions are structured to capture and report the information necessary for compliance with federal accounting standards.

1.P. Advances and Prepayments

When advances are permitted by law, legislative action, or presidential authorization, the DoD's policy is to record advances and prepayments in accordance with GAAP. As such, payments made in advance of the receipt of goods and services are reported as an asset on the Balance Sheet. The DoD's policy is to expense and/or properly classify assets when the related goods and services are received. The Air Force has not fully implemented this policy primarily due to system limitations.

1.Q. Leases

Lease payments for the rental of operating facilities are classified as either capital or operating leases. When a lease is essentially equivalent to an installment purchase of property (a capital lease), Air Force records the applicable asset and liability if the value equals or exceeds the current capitalization threshold. The Air Force records the amounts as the lesser of the present value of the rental and other lease payments during the lease term (excluding portions representing executory costs paid to the lessor) or the asset's fair market value. The discount rate for the present value calculation is either the lessor's implicit interest rate or the government's incremental borrowing rate at the inception of the lease. The Air Force as the lessee receives the use and possession of leased property, for example real estate, from a lessor in exchange for a payment of funds. An operating lease does not substantially transfer all the benefits and risk of ownership. Payments for operating leases are charged to expense over the lease term as it becomes payable.

Office space and leases entered into by Air Force in support of contingency operations are the largest component of operating leases. These costs were gathered from existing leases, General Services Administration (GSA) bills, and Interservice Support Agreements. Future year projections use the Consumer Price Index (CPI) rather than the DoD inflation factor. The CPI impacts increases to the leases, especially those at commercial lease sites.

1.R. Other Assets

Other assets include those assets, such as military and civil service employee pay advances, travel advances, and certain contract financing payments that are not reported elsewhere on Air Force's Balance Sheet.

The Air Force conducts business with commercial contractors under two primary types of contracts: fixed price and cost reimbursable. To alleviate the potential financial burden on the contractor that long-term contracts can cause, Air Force may provide financing payments. Contract financing payments are defined in the Federal Acquisition Regulations, Part 32, as authorized disbursements of monies to a contractor prior to acceptance of supplies or services by the Government. Contract financing payments clauses are incorporated in the contract terms and conditions and may include advance payments, performance-based payments, commercial advance and interim payments, progress payments based on cost, and interim payments under certain cost-reimbursement contracts.

Contract financing payments do not include invoice payments, payments for partial deliveries, lease and rental payments, or progress payments based on a percentage or stage of completion, which the Defense Federal Acquisition Regulation Supplement authorizes only for construction of real property, shipbuilding, and ship conversion, alteration, or repair. Progress payments for real property and ships are reported as Construction in Progress. It is DoD's policy to record certain contract financing payments as Other Assets.

1.S. Contingencies and Other Liabilities

The SFFAS No. 5, "Accounting for Liabilities of the Federal Government," as amended by SFFAS No. 12, "Recognition of Contingent Liabilities Arising from Litigation," defines a contingency as an existing condition, situation, or set of circumstances that involves an uncertainty as to possible gain or loss. The uncertainty will be resolved when one or more future events occur or fail to occur. The Air Force recognizes contingent liabilities when past events or exchange transactions occur, a future loss is probable, and the loss amount can be reasonably estimated.

Financial statement reporting is limited to disclosure when conditions for liability recognition do not exist but there is at least a reasonable possibility of incurring a loss or additional losses. Examples of loss contingencies include the collectibility of receivables, pending, or threatened litigation, and possible claims and assessments. The Air Force's risk of loss and resultant contingent liabilities arise from pending or threatened litigation or claims and assessments due to events such as aircraft and vehicle accidents; medical malpractice; property or environmental damages; and contract disputes.

Other liabilities arise as a result of anticipated disposal costs for Air Force assets. This type of liability has two components: nonenvironmental and environmental. Consistent with SFFAS No. 6, "Accounting for Property, Plant, and Equipment," recognition of an anticipated environmental disposal liability begins when the asset is placed into service. Nonenvironmental disposal liabilities are recognized for assets when management decides to dispose of an asset based upon DoD's policy, which is consistent with SFFAS No. 5, "Accounting for Liabilities of Federal Government." The Air Force does not recognize contingent liabilities associated with nonenvironmental disposals due to immateriality.

1.T. Accrued Leave

The Air Force reports as liabilities military leave and civilian earned leave, except sick leave, that has been accrued and not used as of the Balance Sheet date. Sick leave is expensed as taken. The liability reported at the end of the accounting period reflects the current pay rates.



1.U. Net Position

Net Position consists of unexpended appropriations and cumulative results of operations.

Unexpended Appropriations represent the amounts of authority that are unobligated and that have not been rescinded or withdrawn. Unexpended appropriations also represent amounts obligated for which legal liabilities for payments have not been incurred.

Cumulative Results of Operations represent the net difference, since inception of an activity, between expenses and losses and financing sources (including appropriations, revenue, and gains). Beginning with FY 1998, the cumulative results also include donations and transfers in and out of assets that were not reimbursed.

1.V. Treaties for Use of Foreign Bases

The DoD has the use of land, buildings, and other overseas facilities that are obtained through various international treaties and agreements negotiated by the Department of State. The Air Force purchases capital assets overseas with appropriated funds; however, the host country retains title to land and improvements. Generally, treaty terms allow the Air Force continued use of these properties until the treaties expire. In the event treaties or other agreements are terminated, whereby use of the foreign bases is prohibited, losses are recorded for the value of any nonretrievable capital assets. The settlement due to the U.S. or host nation is negotiated and takes into account the value of capital investments and may be offset by the cost of environmental clean-up.

1.W. Comparative Data

The Air Force's financial statements and notes are presented on a comparative basis.

1.X. Unexpended Obligations

The Air Force obligates funds to provide goods and services for outstanding orders not yet delivered. Unless the title has passed, the financial statements do not reflect a liability for payment for goods and services not yet delivered. Unexpended obligations includes both obligations for which goods and services have been delivered (title passed) and a liability recognized, and obligations for which no delivery has occurred and no liability recognized. The balance of unexpended obligations appears immediately before net outlays in the Statement of Budgetary Resources, and is referred to as "Total, unpaid obligated balances, net, end of period."

1.Y. Undistributed Disbursements and Collections

Undistributed disbursements and collections represent the difference between disbursements and collections matched at the transaction level to a specific obligation, payable, or receivable in the activity field records as opposed to those reported by the U.S. Treasury. These amounts should agree with the undistributed amounts reported on the monthly accounting reports. In transit payments are those payments that have been made, but have not been recorded in the fund holder's accounting records. These payments are applied to the entities' outstanding accounts payable balance. In transit collections are those collections from other agencies or entities that have not been recorded in the accounting records. These collections are also applied to the entities' accounts receivable balance.

The DoD policy is to allocate supported undistributed disbursements and collections between federal and nonfederal categories based on the percentage of distributed federal and nonfederal accounts payable and accounts receivable. Unsupported undistributed disbursements are recorded in accounts payable. Unsupported undistributed collections are recorded in other liabilities.

1.Z. Significant Events

Not Applicable

Note 2. Nonentity Assets

As of September 30	2008	2007
(Amounts in thousands)		
1. Intragovernmental Assets		
A. Fund Balance with Treasury	\$ 101,059	\$ 94,844
B. Accounts Receivable	1,430	2,376
C. Total Intragovernmental Assets	\$ 102,489	\$ 97,220
2. Nonfederal Assets		
A. Cash and Other Monetary Assets	\$ 111,976	\$ 107,908
B. Accounts Receivable	111,649	157,416
C. Other Assets	183,444	186,025
D. Total Nonfederal Assets	\$ 407,069	\$ 451,349
3. Total Nonentity Assets	\$ 509,558	\$ 548,569
4. Total Entity Assets	300,259,558	281,086,886
5. Total Assets	\$ 300,769,116	\$ 281,635,455

Relevant Information for Comprehension

Nonentity assets are assets for which the Air Force maintains stewardship accountability and responsibility to report, but are not available for the Air Force's operations.

Intragovernmental Fund Balance with Treasury represents amounts in Air Force's deposit fund and two suspense fund accounts (Uniformed Services Thrift Savings Plan Suspense and Thrift Savings Plan Suspense) that are not available for Air Force use.

Intragovernmental Accounts Receivable and Nonfederal Accounts Receivable, when collected, go to the U.S. Treasury as miscellaneous receipts. The Nonfederal Accounts Receivable amount also includes interest receivables on aged debt.

Nonfederal Cash and Other Monetary Assets represent disbursing officers' cash and undeposited collections as reported on the Statement of Accountability (Standard Form 1219). These assets are held by the Air Force disbursing officers as agents of the U.S. Treasury.

Nonfederal Other Assets consist of advances to contractors as part of the advance payment pool agreements with the Massachusetts Institute of Technology and other nonprofit institutions. These agreements are used for the financing of cost-type contracts with nonprofit educational research institutions for experimental research and development work when several contracts or a series of contracts require financing by advance payments.



Note 3. Fund Balance with Treasury

As of September 30	2008	2007
(Amounts in thousands)		
1. Fund Balances		
A. Appropriated Funds	\$ 92,800,590	\$ 80,023,587
B. Revolving Funds	0	0
C. Trust Funds	6,773	6,824
D. Special Funds	1,487	1,140
E. Other Fund Types	101,059	94,845
F. Total Fund Balances	<u>\$ 92,909,909</u>	<u>\$ 80,126,396</u>
2. Fund Balances Per Treasury Versus Agency		
A. Fund Balance per Treasury	\$ 94,578,060	\$ 81,162,222
B. Fund Balance per Air Force	92,909,909	80,126,396
3. Reconciling Amount	<u>\$ 1,668,151</u>	<u>\$ 1,035,826</u>

Other Fund Types include balances in deposit fund, receipt accounts, and Thrift Saving Plan (TSP).

The Air Force shows a reconciling amount of \$1.7 billion with U.S. Treasury, which is comprised of \$1.6 billion in withdrawal from the FBWT in the cancelling appropriations on September 30, 2008. These funds are included in FBWT of U.S. Treasury but are not included in the Air Force FBWT.

Status of Fund Balance with Treasury

As of September 30	2008	2007
(Amounts in thousands)		
1. Unobligated Balance		
A. Available	\$ 24,143,734	\$ 18,577,110
B. Unavailable	2,533,156	2,598,234
2. Obligated Balance not yet Disbursed	67,813,258	60,933,360
3. Nonbudgetary FBWT	472,259	385,286
4. NonFBWT Budgetary Accounts	-2,052,498	-2,367,594
5. Total	<u>\$ 92,909,909</u>	<u>\$ 80,126,396</u>

The Status of Fund Balance with Treasury (FBWT) reflects the budgetary resources to support the FBWT.

Unobligated Balance represents the cumulative amount of budgetary authority that has not been set aside to cover outstanding obligations. Unobligated Balance is classified as available or unavailable and is associated with appropriations expiring at fiscal year end that remain available only for obligation adjustments until the account is closed.

Obligated Balance not yet Disbursed represents funds that have been obligated for goods that have not been received, services that have not been performed, and goods and services that have been delivered/received but not yet paid.

Nonbudgetary FBWT includes entity and nonentity FBWT accounts which represents adjustments that do not have budgetary authority, such as unavailable receipt accounts or clearing accounts. The items reported as Nonbudgetary FBWT account comprises the FBWT for suspense, deposit and receipt accounts.

NonFBWT Budgetary Accounts represent adjustments to budgetary accounts that do not affect FBWT. The items that comprise the amount reported as NonFBWT receipts are from nonentity receivables, investments and discounts in U.S. Treasury securities, and unfilled customer orders without advances. This category reduces the Status of FBWT.

Unobligated balances are segregated to show available and unavailable amounts in the note schedule. Certain unobligated balances may be restricted to future use and are not apportioned for current use. The Unobligated Balance unavailable of \$2.5 billion is not available for new obligations because the period for new obligations established by law has expired.



Note 4. Investments and Related Interest

As of September 30	2008			
	Cost	Amortization Method	Amortized (Premium) / Discount	Investments, Net

(Amounts in thousands)

1. Intragovernmental Securities

A. Nonmarketable, Market-Based

1. Military Retirement Fund	\$ 0		\$ 0	\$ 0	\$ 0
2. Medicare Eligible Retiree Health Care Fund	0		0	0	0
3. US Army Corps of Engineers	0		0	0	0
4. Other Funds	868		-3	865	890
5. Total Nonmarketable, Market-Based	\$ 868		\$ -3	\$ 865	\$ 890

B. Accrued Interest

	9			9	9
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C. Total Intragovernmental Securities

	\$ 877		\$ -3	\$ 874	\$ 899
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2. Other Investments

A. Total Other Investments

	\$ 0		\$ 0	\$ 0	N/A
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As of September 30	2007			
	Cost	Amortization Method	Amortized (Premium) / Discount	Investments, Net

(Amounts in thousands)

3. Intragovernmental Securities

A. Nonmarketable, Market-Based

1. Military Retirement Fund	\$ 0		\$ 0	\$ 0	\$ 0
2. Medicare Eligible Retiree Health Care Fund	0		0	0	0
3. US Army Corps of Engineers	0		0	0	0
4. Other Funds	816		-1	815	820
5. Total Nonmarketable, Market-Based	\$ 816		\$ -1	\$ 815	\$ 820

B. Accrued Interest

	8			8	9
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C. Total Intragovernmental Securities

	\$ 824		\$ -1	\$ 823	\$ 829
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4. Other Investments

A. Total Other Investments

	\$ 0		\$ 0	\$ 0	N/A
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Relevant Information for Comprehension

The Federal Government does not set aside assets to pay future benefits and expenditures associated with earmarked funds. The cash generated from earmarked funds are deposited in U.S. Treasury, which uses the cash for general Government purposes. The U.S. Treasury securities are issued to the earmarked funds as evidence of earmarked fund receipts. The U.S.

Treasury securities are an asset to the Air Force and a liability to the U.S. Treasury. Because Air Force and U.S. Treasury are both parts of the Government, these assets and liabilities offset each other from the standpoint of the Government as a whole. For this reason, they do not represent an asset or a liability in the U.S. Governmentwide financial statements. The U.S. Treasury securities provide Air Force with authority to draw upon U.S. Treasury to make future benefit payments or other expenditures. When Air Force requires redemption of these securities, the Government finances the securities out of accumulated cash balances, by raising taxes or other receipts, by borrowing from the public or repaying less debt, or by curtailing other expenditures. This is the same way that the Government finances all other expenditures.

Intragovernmental Securities (Other) primarily represents the Air Force Gift Fund investment in U.S. Treasury Securities.

Note 5. Accounts Receivable

As of September 30	2008			2007	
	Gross Amount Due	Allowance For Estimated Uncollectibles	Accounts Receivable, Net	Accounts Receivable, Net	
(Amounts in thousands)					
1. Intragovernmental Receivables	\$ 271,020	N/A	\$ 271,020	\$ 388,823	
2. Nonfederal Receivables (From the Public)	\$ 619,412	\$ -117,230	\$ 502,182	\$ 545,796	
3. Total Accounts Receivable	<u>\$ 890,432</u>	<u>\$ -117,230</u>	<u>\$ 773,202</u>	<u>\$ 934,619</u>	

Note 6. Other Assets

As of September 30	2008		2007	
(Amounts in thousands)				
1. Intragovernmental Other Assets				
A. Advances and Prepayments	\$ 265,591		\$ 423,952	
B. Other Assets	0		0	
C. Total Intragovernmental Other Assets	<u>\$ 265,591</u>		<u>\$ 423,952</u>	
2. Nonfederal Other Assets				
A. Outstanding Contract Financing Payments	\$ 10,775,541		\$ 10,183,088	
B. Advances and Prepayments	71,542		79,705	
C. Other Assets (With the Public)	183,444		186,025	
D. Total Nonfederal Other Assets	<u>\$ 11,030,527</u>		<u>\$ 10,448,818</u>	
3. Total Other Assets	<u>\$ 11,296,118</u>		<u>\$ 10,872,770</u>	

Relevant Information for Comprehension

Nonfederal Other Assets (With the Public) is comprised primarily of advance payment pool agreements with nonprofit educational institutions. These agreements are funded under cost type contract procedures and are mainly for experimental research and development requirements.



Contract terms and conditions for certain types of contract financing payments convey certain rights to the Air Force that protect the contract work from state or local taxation, liens or attachment by the contractor’s creditors, transfer of property, or disposition in bankruptcy; however, these rights should not be misconstrued to mean that ownership of the contractor’s work has transferred to the Government. The Government does not have the right to take the work, except as provided in contract clauses related to termination or acceptance; therefore, the Air Force is not obligated to make payment to the contractor until delivery and acceptance.

The Outstanding Contract Financing Payments balance of \$10.8 billion is comprised of \$10.3 billion in contract financing payments and an additional \$533.2 million in estimated future payments that will be paid upon future delivery and Government acceptance of satisfactory products and services. (See additional discussion in Note 15, Other Liabilities).

Note 7. Cash and Other Monetary Assets

As of September 30	2008	2007
(Amounts in thousands)		
1. Cash	\$ 93,046	\$ 104,681
2. Foreign Currency	18,930	3,227
3. Other Monetary Assets	0	0
4. Total Cash, Foreign Currency, & Other Monetary Assets	\$ 111,976	\$ 107,908

Relevant Information for Comprehension

The amount reported as cash and foreign currency consists primarily of cash held by Disbursing Officers. The foreign currency amount reported is valued at U.S. Treasury’s prevailing exchange rate, which is the most favorable rate available to the Government for foreign exchange transactions. Foreign currency is primarily used to make vendor disbursements and to exchange U.S. dollars for military personnel.

Cash and foreign currency are nonentity assets and, as such, considered restricted assets that are held by the Air Force but are not available for use in its operations. These assets are held by the Air Force’s Disbursing Officers as agents of U.S. Treasury. The total balance of \$112.0 million is restricted.

Note 8. Direct Loan and/or Loan Guarantee Programs

Not Applicable

Note 9. Inventory and Related Property

As of September 30	2008		2007	
(Amounts in thousands)				
1. Inventory, Net	\$	0	\$	0
2. Operating Materials & Supplies, Net		46,906,666		46,335,059
3. Stockpile Materials, Net		0		0
4. Total	\$	<u>46,906,666</u>	\$	<u>46,335,059</u>

Inventory, Net

Not Applicable

Operating Materials and Supplies, Net

As of September 30	2008			2007		Valuation Method
	OM&S Gross Value	Revaluation Allowance	OM&S, Net	OM&S, Net		
(Amounts in thousands)						
1. OM&S Categories						
A. Held for Use	\$ 35,828,669	\$ 0	\$ 35,828,669	\$ 35,998,482		SP, LAC
B. Held for Repair	11,077,997	0	11,077,997	10,336,577		SP, LAC
C. Excess, Obsolete, and Unserviceable	1,904,436	-1,904,436	0	0		NRV
D. Total	<u>\$ 48,811,102</u>	<u>\$ -1,904,436</u>	<u>\$ 46,906,666</u>	<u>\$ 46,335,059</u>		

Legend for Valuation Methods:

Adjusted LAC = Latest Acquisition Cost, adjusted for holding gains and losses NRV = Net Realizable Value

SP = Standard Price

O = Other

AC = Actual Cost

General Composition of OM&S

The Operating Materials and Supplies (OM&S) include weapon systems spares, ammunition, tactical missiles, aerial target drones, uninstalled aircraft and cruise missile engines, and uninstalled intercontinental ballistic missile motors.

In addition to the account balances shown in Note 9, the federal accounting standard requires disclosure of the amount of OM&S held for future use. Except for an immaterial amount of munitions, the Air Force is not holding any items for future use.

Restrictions on the Use of OM&S

The Air Force does not maintain any OM&S restricted assets.



Decision Criteria for Identifying the Category to Which OM&S Items Are Assigned

The category Held for Use includes all materials available for issuance. OM&S classified as such is marked within each supply or inventory system.

The category Held for Repair includes all economically reparable materials as defined by the Military Standard Transaction Reporting and Accounting Procedures Manual (DoD 4000.25-2-M).

The category Held as Excess, Obsolete, and Unserviceable includes all materials that managers determine to be more costly to repair than to replace. Items retained for management purposes which are beyond economic repair are coded “condemned.” These items are held until proper disposal can be made. The net value of these items is zero and they are shown as Excess, Obsolete, and Unserviceable.

Changes in the Criteria for Identifying the Category to Which OM&S Items Are Assigned

The DoD’s approved methodology for determining historical cost is the Moving Average Cost (MAC). As of 3rd Quarter, FY 2007, Air Force has fully implemented MAC in three of the six systems used to report OM&S values into the accounting system. In two of the three remaining systems, the beginning inventory balances have been established, but the cost for the quantities on hand for each national stock number have not been validated. It is anticipated that a majority of the cost associated with the inventory balances in these two systems will be validated using MAC standards by December 31 2008. Validation of the beginning balance in the Combat Ammunitions System (CAS), which manages approximately 50% of all OM&S, is not scheduled to be completed until 1st Quarter, FY 2009.

Under current DoD policy, no allowance is made for serviceable, ready-to-issue, items (category Held for Use). An allowance equal to 100% of MAC or standard price, however, is made for the category Excess, Obsolete, and Unserviceable. This allowance results in a net book value of zero for items that have no intrinsic value to the Air Force. The category Held for Repair represents suspended, unserviceable (but reparable) items. Air Force will continue to report Held for Repair at MAC or standard price until Office of the Secretary of Defense guidance is provided on how to compute an allowance for repair.

Operating Materiel and Supplies (OM&S) Value

The OM&S data reported on the financial statements are derived from logistics systems designed for materiel management purposes. Some of these systems do not maintain the historical cost data necessary to comply with the valuation requirements of the Statement of Federal Financial Accounting Standards (SFFAS) No. 3, “Accounting for Inventory and Related Property.”

Items commonly used in and available from the commercial sector are not managed in the DoD materiel management activities. Further, unlike the commercial sector, the DoD operational cycles are based on national need and thereby are irregular. In addition, the military risks associated with stock-out positions (e.g., weapon systems that are not mission capable due to lack of supplies) are totally different from a commercial activities risk of losing sales. Therefore, DoD does not attempt to account separately for items held for current or future use.

In general, the Air Force uses the consumption method of accounting for OM&S, since OM&S is defined in SFFAS No. 3 as materiel that has not yet been issued to the end user. Once issued, the materiel is expensed. According to federal accounting standards, the consumption method of accounting should be used to account for OM&S unless: (1) the amount of OM&S is not significant, (2) OM&S are in the hands of the end user for use in normal operations, or (3) it is cost beneficial to expense OM&S when purchased (purchase method).

Other Air Force Disclosures

In the past, the Air Force provided only minimal OM&S accounting data that can be used to prepare the financial statements but has made considerable strides in improving the systems to provide actual transactions for completing the financial statements. However, in some cases, the data provided still consists of only beginning and ending balances for each of the asset accounts Held for Use; Excess, Obsolete, Unserviceable; and Held for Repair. Without the required additional data (acquisitions, transfers in, amounts consumed, transfers out, trading partner data, etc.), DFAS can only report the net change between prior period ending balances and the values reported as current period ending balances.

Although the Air Force OM&S systems, in most cases, capture some trading partner data at the transaction level, no electronic interfaces exist between the Air Force OM&S feeder systems, the DFAS accounting systems, other DoD services, and other federal agencies for reporting the data for all items transferred in and out. Consequently, intragovernmental transactions (trading partner data) could not always be reconciled. The Air Force and DFAS are currently developing processes, methodologies and standard electronic interfaces that will allow intragovernmental transactions to be reported monthly into the Air Force accounting system.

Stockpile Materials, Net

Not Applicable



Note 10. General PP&E, Net

As of September 30	2008					2007
	Depreciation/ Amortization Method	Service Life	Acquisition Value	(Accumulated Depreciation/ Amortization)	Net Book Value	Prior FY Net Book Value
(Amounts in thousands)						
1. Major Asset Classes						
A. Land	N/A	N/A	\$ 443,879	N/A	\$ 443,879	\$ 437,150
B. Buildings, Structures, and Facilities	S/L	20 or 40	49,696,527	\$ -28,272,596	21,423,931	20,624,376
C. Leasehold Improvements	S/L	lease term	0	0	0	0
D. Software	S/L	2-5 or 10	517,377	-163,801	353,576	435,089
E. General Equipment	S/L	5 or 10	36,802,784	-28,890,932	7,911,852	7,119,611
F. Military Equipment	S/L	Various	257,051,494	-142,591,486	114,460,008	111,053,515
G. Assets Under Capital Lease	S/L	lease term	393,002	-303,111	89,891	109,749
H. Construction-in-Progress	N/A	N/A	4,087,234	N/A	4,087,234	3,478,390
I. Other			0	0	0	0
J. Total General PP&E			\$ 348,992,297	\$ -200,221,926	\$ 148,770,371	\$ 143,257,880

See Note 15 for additional information on Capital Leases

S/L = Straight Line N/A = Not Applicable

Relevant Information for Comprehension

General Property, Plant and Equipment (PP&E)

There are restrictions on the Air Force’s ability to dispose of real property (land and buildings) located outside the continental United States.

The Air Force estimates historical values for capitalized military equipment using departmental internal records.

Other Air Force Disclosures

The value of the Air Force’s General PP&E real property in the possession of contractors is included in the values reported for the major asset classes of Land and Buildings, Structures, and Facilities. The value of General PP&E personal property major asset class of Software and Equipment does not include all of the General PP&E above the DoD capitalization threshold in the possession of contractors. The Air Force does not report the value of equipment purchased directly by the contractor. The Government Accountability Office, the Inspector General, DoD, and the Air Force are developing new policies and a contractor reporting process to capture General PP&E information for future reporting purposes in compliance with generally accepted accounting principles.

Heritage Assets and Stewardship Land

The overall mission of Air Force is to fly, fight and win in air, space and cyberspace, influence events, and advance U.S. interests across the full spectrum of military operations. As this mission has been executed, Air Force has become a large-scale owner of historic buildings, structures, archaeological sites and artifacts, aircraft, other cultural resources, and stewardship land. The protection of the nation's heritage assets and stewardship land is an important aspect of the Air Force's mission.

Heritage Assets and Stewardship Land are resources that protect, restore, enhance, modernize, preserve and sustain mission capability within the Air Force through effective planning and management of natural and cultural resources to guarantee access to air, land, and water. These assets are resources that are managed to provide multiple use activities for the public benefit. This includes actions to comply with requirements such as federal laws, Executive Orders, policies, final governing standards, and other binding agreements.

Heritage Assets consist of buildings and structures, archaeological sites, museum collection items (objects, not including fine art), and museum collection items (fine art). Stewardship Land consist of government owned land, state owned land, withdrawn public land, license and permitted land, public land, land easement, in-lease land, and foreign land. The Air Force has 7,592,000 acres of mission essential land under their administration. Stewardship decreased 108,000 acres in FY 2008 because of a change in category reporting requirement. Specifically, certain category codes are now reported as government owned land rather than withdrawn public land. Land purchased by the Air Force with the intent to construct buildings or facilities is considered General PP&E and is reported on the balance sheet. All stewardship land, as reported, is in acceptable condition, based on designated use.

Heritage Assets are PP&E of historical, natural, cultural, educational or artistic significance (e.g. aesthetic); or with significant architectural characteristics. Air Force policy is to promote and preserve indefinitely the identifiable human, environmental or civic value of these assets.

Stewardship Land comprises land and land rights other than that acquired for or in connection with General PP&E, land acquired via the public domain, or land acquired at no cost. Air Force policy is to promote and preserve indefinitely the identifiable human, environmental or civic value of such land.

Buildings and Structures: The Air Force considers 4,959 buildings and structures on Air Force bases and sites to be heritage assets. In order to be considered a heritage asset, the building and/or facility must be listed, eligible, or potentially eligible for the National Register. These buildings and structures are maintained by each base's civil engineering group as part of their overall responsibility.

Archaeological Sites: The Air Force has 1,930 archeological sites listed on or eligible for the National Register.

Museum Collection Items, Objects Not Including Fine Art: The Air Force has 117,134 museum collection items (not including fine art). During FY 2008, 4,009 objects have been added to the collection, primarily as a result of private donations or by being found on base.

Museum Collection Items, Fine Art: The Air Force has 9,370 fine art museum collections. During FY 2008, 111 paintings were received through donations.



Assets Under Capital Lease

As of September 30	2008	2007
(Amounts in thousands)		
1. Entity as Lessee, Assets Under Capital Lease		
A. Land and Buildings	\$ 393,002	\$ 405,988
B. Equipment	0	0
C. Accumulated Amortization	-303,111	-296,239
D. Total Capital Leases	\$ 89,891	\$ 109,749

Relevant Information for Comprehension

The Air Force is the lessee in eight capital leases for military housing acquired through the Section 801 Family Housing Program. The leases are capitalized and reported as an asset since their costs exceed the capitalization threshold of \$100.0 thousand. The net value of assets under capital leases are scheduled to expire by 4th Quarter, FY 2015. The Air Force is not acquiring any new capital leases.

Note 11. Liabilities Not Covered by Budgetary Resources

As of September 30	2008	2007
(Amounts in thousands)		
1. Intragovernmental Liabilities		
A. Accounts Payable	\$ 0	\$ 0
B. Debt	0	0
C. Other	823,278	512,987
D. Total Intragovernmental Liabilities	\$ 823,278	\$ 512,987
2. Nonfederal Liabilities		
A. Accounts Payable	\$ 394,075	\$ 234,292
B. Military Retirement and Other Federal Employment Benefits	1,158,232	1,132,550
C. Environmental Liabilities	7,519,475	6,093,809
D. Other Liabilities	3,033,988	2,706,792
E. Total Nonfederal Liabilities	\$ 12,105,770	\$ 10,167,443
3. Total Liabilities Not Covered by Budgetary Resources	\$ 12,929,048	\$ 10,680,430
4. Total Liabilities Covered by Budgetary Resources	10,646,178	10,169,668
5. Total Liabilities	\$ 23,575,226	\$ 20,850,098

Information Related to Liabilities Not Covered by Budgetary Resources

Liabilities Not Covered by Budgetary Resources are liabilities for which congressional action is needed before budgetary resources can be provided.

The material amounts and sensitive areas included in Total Liabilities Not Covered by Budgetary Resources are categorized

as not covered because there is no current or immediate appropriation available for liquidation. These liabilities will be included in future budget years as Liabilities Covered by Budgetary Resources. The Air Force fully expects to receive the necessary resources to cover these liabilities in future years.

Other Intragovernmental Liabilities are primarily comprised of liabilities representing the amount of nonentity assets held in a general receipt account or other U.S. Treasury account symbol for transfers to other entities, and the amount of the Federal Employees' Compensation Act (FECA) liability billed to the agency by Department of Labor for FECA payments made on the agency's behalf.

Other Nonfederal Liabilities are primarily comprised of the amounts recorded for unpaid leave earned to which an employee is entitled upon separation and for contingent liabilities which are probable and measurable and will require resources funded from future years' appropriations.

Military Retirement and Other Federal Employment Benefits not covered by budgetary resources are comprised of various employee actuarial liabilities not due and payable during the current fiscal year. These liabilities, totaling \$1.2 billion, are primarily comprised of the amount recorded by employer agencies for the actuarial present value of future FECA benefits provided to Federal employees or their beneficiaries as a result of work related deaths, disability, or occupational disease. Refer to Note 17, Military Retirement and Other Federal Employment Benefits, for additional details and disclosures.

Note 12. Accounts Payable

As of September 30	2008			2007
	Accounts Payable	Interest, Penalties, and Administrative Fees	Total	Total
(Amounts in thousands)				
1. Intragovernmental Payables	\$ 2,002,120	\$ N/A	\$ 2,002,120	\$ 1,509,630
2. Nonfederal Payables (to the Public)	3,810,464	471	3,810,935	3,189,763
3. Total	\$ 5,812,584	\$ 471	\$ 5,813,055	\$ 4,699,393

Relevant Information for Comprehension

The Air Force's systems do not track intragovernmental transactions by customer at the transaction level. Therefore, internal DoD buyer-side balances are adjusted to agree with internal seller-side balances for revenue, accounts receivable, and unearned revenue. Accounts Payable were reviewed on a case-by-case basis and adjusted to accrue additional payables and expenses as appropriate.

In FY 2007, the Air Force recognized accounts payable balances of the Mechanization of Contract Administration Services (MOCAS) system at gross value without reductions for partial and progress payments, and nonaccounts payable records. The overstated balances for FY 2007 were undeterminable due to system limitations; therefore no corrections have been made. Balances at FY 2008 are properly reported net of nonaccounts payable records, partial and progress payments of \$179.9 million.

Note 13. Debt

Not Applicable



Note 14. Environmental Liabilities and Disposal Liabilities

As of September 30	2008			2007
	Current Liability	Noncurrent Liability	Total	Total
(Amounts in thousands)				
1. Environmental Liabilities—Nonfederal				
A. Accrued Environmental Restoration Liabilities				
1. Active Installations—Installation Restoration Program (IRP) and Building Demolition and Debris Removal (BD/DR)	\$ 524,720	\$ 3,100,857	\$ 3,625,577	\$ 3,793,045
2. Active Installations—Military Munitions Response Program (MMRP)	22,849	1,369,593	1,392,442	1,397,049
3. Formerly Used Defense Sites—IRP and BD/DR	0	0	0	0
4. Formerly Used Defense Sites—MMRP	0	0	0	0
B. Other Accrued Environmental Liabilities—Non BRAC				
1. Environmental Corrective Action	14,280	165,468	179,748	165,375
2. Environmental Closure Requirements	21,750	1,108,139	1,129,889	87,363
3. Environmental Response at Operational Ranges	0	0	0	0
4. Asbestos	7,099	421,503	428,602	0
5. Non-Military Equipment	1,637	27,079	28,716	0
6. Other	0	0	0	0
C. Base Realignment and Closure Installations				
1. Installation Restoration Program	120,961	1,281,047	1,402,008	1,442,601
2. Military Munitions Response Program	177	2,221	2,398	3,520
3. Environmental Corrective Action / Closure Requirements	2,137	35,783	37,920	9,915
4. Asbestos	0	0	0	0
5. Non-Military Equipment	0	0	0	0
6. Other	0	0	0	0
D. Environmental Disposal for Military Equipment / Weapons Programs				
1. Nuclear Powered Military Equipment / Spent Nuclear Fuel	0	0	0	0
2. Non-Nuclear Powered Military Equipment	217	38,858	39,075	0
3. Other National Defense Weapons Systems	0	0	0	0
4. Other	0	0	0	0
E. Chemical Weapons Disposal Program				
1. Chemical Agents and Munitions Destruction (CAMD)	0	0	0	0
2. CAMD Assembled Chemical Weapons Assessment (ACWA)	0	0	0	0
3. Other	0	0	0	0
2. Total Environmental Liabilities	\$ 715,827	\$ 7,550,548	\$ 8,266,375	\$ 6,898,868

Other Information Related to Environmental Liabilities

An environmental liability is a probable and measurable future outflow or expenditure of resources that exist as of the financial reporting date for environmental cleanup costs resulting from past transactions or events. The Air Force acknowledges

that liabilities can change for environmental cleanup costs to include (1) costs associated with environmental restoration of sites funded under the Air Force portion of the Defense Environmental Restorations Program (DERP), (2) corrective actions funded with other than DERP, Base Realignment and Closure (BRAC), and (3) environmental costs associated with future closure or disposal of facilities, equipment, asbestos, and weapon systems. These costs include researching and determining the existence of hazardous waste, removing, containing, and/or disposing of hazardous waste from property, or material and/or property that consist of hazardous waste at the time of shutdown or disposal of the asset. Cleanup costs may include, but are not limited to, decontamination, decommissioning, site restoration, site monitoring, closure, and post closure costs related to Air Force operations that result in hazardous waste.

Applicable Laws and Regulations for Cleanup Requirements

The Air Force is required to clean up contamination resulting from past waste disposal practices, leaks, spills and other past activity, which has created a public human health or environmental risk. The Air Force does this in coordination with regulatory agencies, and if applicable, with other responsible parties. The Air Force is also required to recognize closure, post closure and disposal costs for its Property, Plant and Equipment (PP&E) and environmental corrective action costs for current operations. The Air Force is responsible for tracking and reporting all required environmental information related to environmental restoration and corrective action, closure and disposal costs of PP&E, and environmental costs related to BRAC actions that have taken place in prior years. Examples of relevant laws and regulations that are considered for discussion include:

- (a) Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA)
- (b) Superfund Amendments and Reauthorization Act (SARA)
- (c) Clean Water Act (CWA)
- (d) Clean Air Act (CAA)
- (e) Resource Conservation and Recovery Act (RCRA)
- (f) Toxic Substances Control Act (TSCA)
- (g) Military Munitions Rule in 40 CFR 266.201, Definition of Solid Waste

The two laws with the majority of cost estimates for active environmental cleanup are CERCLA and RCRA.

Types of Environmental Liabilities Identified

The Air Force has environmental liabilities to cover cleanup requirements for active installations: Installation Restoration Program (IRP), Building Demolition and Debris Removal (BD/DR), Military Munitions Response Program (MMRP), and Environmental Corrective Action (ECA). The Air Force also has environmental liabilities to cover cleanup requirements at BRAC installations. Finally, the Air Force has identified environmental liabilities for closure and disposal of PP&E to include facilities, general equipment, asbestos, and weapon systems.

Methods for Assigning Estimated Total Cleanup Costs to Current Operating Periods

The Air Force uses engineering estimates and independently validated models to estimate environmental cleanup costs. The models are either developed within the Remedial Action Cost Engineering Requirements application, or a historic comparable project, a specific bid, or an independent government cost estimate is referenced for the current project. The Air Force



validates the models in accordance with DoD Instruction 5000.61 and primarily uses the models to estimate environmental cleanup costs based on data received during a preliminary assessment and initial site investigation. The Air Force primarily uses engineering estimates after obtaining data during the remedial investigation/feasibility phase of the environmental project.

Once the environmental cleanup cost estimates are complete, Air Force will comply with accounting standards to assign costs to current operating periods for the unexpended obligations from prior periods and the future program. The Air Force Accrued Environmental Restoration Liabilities is accounted for as a totally self contained program. All direct and indirect costs of the program are captured and reported.

The Air Force has already expensed the costs for cleanup associated with General PP&E placed into service prior to October 1, 1997, unless the costs are intended to be recovered through user charges. If the costs are recovered through user charges, then the Air Force expenses the associated environmental cost systematically over the life of the asset.

The accounting standards also require environmental liabilities are recognized for closure and disposal requirements. The Air Force has closure requirements or disposal liabilities at active installations. Closure and disposal liabilities for facilities (including landfills), asbestos, general equipment and weapon systems are estimated for the applicable inventory of real property, general equipment and weapon systems. The Air Force uses a set of historical disposal factors to estimate the environmental disposal liability for each asset and the estimated closure and monitoring cost for landfills. The current liability for these classes of assets is determined from the related disposal programs including the resources expected to be expended in the next year from prior and future budgets.

For General PP&E placed into service after September 30, 1997, the Air Force expenses the associated environmental costs systematically over the life of the asset. The Air Force expenses the full cost to clean up contamination for Stewardship PP&E at the time the asset is placed into service.

The Air Force uses two methods for systematic recognition: physical capacity for operating landfills, and life expectancy in years for all other assets.

Nature of Estimates and the Disclosure of Information Regarding Possible Changes due to Inflation, Deflation, Technology, or Applicable Laws and Regulations

The Air Force is not aware of any pending changes to reported values of Environmental Liabilities. The Air Force does understand that liabilities can change in the future due to changes in laws, regulations, and changes in agreements with regulatory agencies.

Level of Uncertainty Regarding the Accounting Estimates used to Calculate the Reported Environmental Liabilities

Environmental liabilities for Air Force are based on accounting estimates which require certain judgments and assumptions to be made by management. The Air Force believes the estimates are reasonable based upon the information available at the time of calculation. Actual results may vary materially from the accounting estimates if agreements with regulatory agencies require remediation to a different degree than anticipated when the estimate was calculated. The liabilities can be further impacted if further investigation discovers contamination different from that which was known at the time of the estimate. The Air Force financial statements would be affected to the extent there are material differences between these estimates and actual costs. There are areas in which management judgment in selecting any available alternative could produce a materially different result.

In addition to the liabilities reported above, the Air Force has the potential to incur costs for restoration initiatives in conjunction with returning overseas Defense facilities to host nations. The Air Force is unable to provide a reasonable estimate at this time because the extent of restoration required is not known.

Environmental Disclosures

As of September 30	2008	2007
(Amounts in thousands)		
A. The unrecognized portion of the estimated total cleanup costs associated with general property, plant, and equipment.	\$ 363,012	\$ 67,280
B. Changes in total cleanup costs due to changes in laws, regulations, and/or technology.	223,300	-12,662
C. Portion of the changes in estimated costs due to changes in laws and technology that is related to prior periods.	-34,978	-4,357

The unrecognized portion of the total cleanup is the estimated total cleanup cost less the amount that is recognized on the financial statements.

Changes in environmental regulations and cleanup standards resulted in a reduction of total cleanup costs.



Note 15. Other Liabilities

As of September 30	2008			2007
	Current Liability	Noncurrent Liability	Total	Total
(Amounts in thousands)				
1. Intragovernmental				
A. Advances from Others	\$ 694,789	\$ 0	\$ 694,789	\$ 882,243
B. Deposit Funds and Suspense Account Liabilities	371,200	0	371,200	290,441
C. Disbursing Officer Cash	297,209	0	297,209	293,933
D. Judgment Fund Liabilities	0	0	0	0
E. FECA Reimbursement to the Department of Labor	130,059	171,153	301,212	295,090
F. Custodial Liabilities	0	194,800	194,800	187,038
G. Employer Contribution and Payroll Taxes Payable	63,176	0	63,176	53,138
H. Other Liabilities	30,399	0	30,399	31,443
I. Total Intragovernmental Other Liabilities	\$ 1,586,832	\$ 365,953	\$ 1,952,785	\$ 2,033,326
2. Nonfederal				
A. Accrued Funded Payroll and Benefits	\$ 2,032,464	\$ 0	\$ 2,032,464	\$ 2,066,760
B. Advances from Others	136,825	0	136,825	9,980
C. Deferred Credits	0	0	0	0
D. Deposit Funds and Suspense Accounts	101,064	0	101,064	95,073
E. Temporary Early Retirement Authority	0	0	0	0
F. Nonenvironmental Disposal Liabilities				
1. Military Equipment (Nonnuclear)	0	0	0	0
2. Excess/Obsolete Structures	0	0	0	0
3. Conventional Munitions Disposal	0	0	0	0
G. Accrued Unfunded Annual Leave	2,272,149	0	2,272,149	2,250,677
H. Capital Lease Liability	0	130,091	130,091	157,725
I. Contract Holdbacks	131,506	0	131,506	164,211
J. Employer Contribution and Payroll Taxes Payable	297,742	0	297,742	286,014
K. Contingent Liabilities	533,208	744,245	1,277,453	1,044,352
L. Other Liabilities	303	0	303	6,704
M. Total Nonfederal Other Liabilities	\$ 5,505,261	\$ 874,336	\$ 6,379,597	\$ 6,081,496
3. Total Other Liabilities	\$ 7,092,093	\$ 1,240,289	\$ 8,332,382	\$ 8,114,822

Relevant Information for Comprehension

The amount of Intragovernmental Other Liabilities represent Government contributions for employee benefits, unemployment compensation, education benefits, and custodial liabilities.

The amount of Nonfederal Other Liabilities represent legal contingencies, employee benefits, and contract holdbacks.

Contingent Liabilities include \$533.2 million in estimated future contract financing payments that will be paid to contractors upon delivery and Government acceptance, \$152.5 million in Contingent Liabilities nonfederal for open contractor claims greater than \$100.0 thousand, and \$591.7 million for claims and litigation against the Air Force handled by the Civil Law and Litigation Directorate. The nature and estimating methodology related to these liabilities are discussed further in Note 16.

Contractor claims are updated annually because there are only marginal changes.

Estimation Methodology

The Air Force General Counsel, through legal determination assesses and categorizes all contingent legal liability cases that equal or exceed the materiality threshold set by Department of Defense Inspector General (DoDIG). For the remaining cases falling below the dollar materiality threshold set by DoDIG, they are considered in aggregate, if the total amount of the cases equal or exceed the established materiality threshold.

The Air Force General Counsel also solicits case data through quarterly data calls from the Air Force JAC (Judge Advocate Civil Lawsuits and Litigation Directorate). Air Force financial management personnel use the solicited case data which includes the current reporting year and each of the prior two years to estimate the amounts of probable and reasonably possible contingent liabilities.

Air Force financial management personnel use a three year prior case analysis spreadsheet which was developed by the Air Force Audit Agency to calculate and estimate the amount of contingent liabilities (probable and reasonably possible) for reporting or disclosing in the quarterly financial statements. In cases where Air Force General Counsel discloses that a judgment has been awarded against the Air Force, these amounts will be reported on the Balance Sheet and within this note.



Capital Lease Liability

As of September 30	2008 Asset Category				2007
	Land and Buildings	Equipment	Other	Total	Total
(Amounts in thousands)					
1. Future Payments Due					
A. 2008	\$ 0	\$ 0	\$ 0	\$ 0	\$ 38,594
B. 2009	38,478	0	0	38,478	38,478
C. 2010	38,478	0	0	38,478	38,478
D. 2011	36,786	0	0	36,786	36,786
E. 2012	13,088	0	0	13,088	13,088
F. 2013	9,462	0	0	9,462	0
G. After 5 Years	17,376	0	0	17,376	26,838
H. Total Future Lease Payments Due	\$ 153,668	\$ 0	\$ 0	\$ 153,668	\$ 192,262
I. Less: Imputed Interest Executroy Costs	23,577	0	0	23,577	34,537
J. Net Capital Lease Liability	\$ 130,091	\$ 0	\$ 0	\$ 130,091	\$ 157,725
2. Capital Lease Liabilities Covered by Budgetary Resources				\$ 112,801	\$ 135,750
3. Capital Lease Liabilities Not Covered by Budgetary Resources				\$ 17,289	\$ 21,975

Note 16. Commitments and Contingencies

Relevant Information for Comprehension

The Air Force is a party in various administrative proceedings and legal actions, with claims that encompass environmental damage claims, equal opportunity matters, and contractual bid protests. We are not aware of any contingent liabilities for legal actions.

The Air Force has accrued contingent liabilities for legal actions where our Office of the General Counsel considers an adverse decision probable and the amount of loss is measurable. In the event of an adverse judgment against the Government, some of the liabilities may be payable from the Judgment Fund. The Air Force records Judgment Fund liabilities in Note 12, "Accounts Payable," and Note 15, "Other Liabilities."

Contractor claims having a reasonably possible liability is estimated at \$26.1 million. Claims and litigation from Civil Law having a reasonably possible liability is estimated at \$3.3 billion. Neither past payments nor the current contingent liability estimate provides a basis for accurately projecting the results of any individual lawsuit or claim. Since monetary judgments paid to civil litigants come from a judgment fund administered by U.S. Treasury, it is uncertain that claims will become a liability to the Air Force.

The amounts disclosed for litigation claims and assessments are fully supportable and agree with Air Force's legal representation letters and management summary schedule.

The amount of undelivered orders for open contracts citing cancelled appropriations which remain unfilled or unreconciled for which the Air Force may incur a contractual commitment for payment is \$766.4 million.

The Air Force is a party in numerous individual contracts that contain clauses, such as price escalation, award fee payments, or dispute resolution, that may or may not result in a future outflow of expenditures. Currently, Air Force does not have a systemic process by which it captures or assesses these potential contingent liabilities; therefore, the amounts reported may not fairly present the Air Force's contingent liabilities.

The estimated probable liability amount of \$1.3 billion was recognized in Note 15 as contingent liabilities.

The recognized contingent liability includes \$533.2 million in estimated future contract financing payments that will be paid to contractors upon delivery and Government acceptance. In accordance with contract terms, specific rights to the contractor's work vests with the Government when a specific type of contract financing payment is made. This action protects taxpayer funds in the event of contract nonperformance. These rights should not be misconstrued as the rights of ownership. The Air Force is under no obligation to pay the contractor for amounts greater than the amounts authorized in the contract until delivery and Government acceptance. Because it is probable that the contractor will complete its efforts and deliver a satisfactory product to the Air Force and the amount of potential future payments is estimable; the Air Force has recognized a contingent liability for estimated future payments, which are conditional pending delivery and Government acceptance.

The recognized contingent liability also includes the recorded estimated probable liability amount of \$152.5 million for open contractor claims greater than \$100.0 thousand. At this time, these claims are not in appeal or in litigation. In addition to the contractor claims under appeal and the open contractor claims for an amount greater than \$100.0 thousand, the Air Force was party to numerous other contractor claims in amounts less than \$100.0 thousand per claim. These claims are a routine part of the contracting business and are typically resolved through mutual agreement between the contracting officer and the contractor. Because of the routine nature of these claims, no requirement exists for a consolidated tracking mechanism to record the amount of each claim, the number of open claims, or the probability of the claim being settled in



favor of the claimant. The potential liability arising from these claims in aggregate would not materially affect the operations or financial condition of the Air Force.

In addition, Air Force recognized the total estimated probable liability for claims and litigation against the Air Force handled by the Civil Law and Litigation Directorate, as of September 30, 2008, valued at \$591.7 million included in Contingent Liabilities nonfederal. As of September 30, 2008, the Air Force was party to 16,787 claims and litigation actions. This liability dollar amount recorded in the financial statements is an estimate based on the weighted average payout rate for the previous three years. There are only two types of cases where U.S. Treasury will seek reimbursements from the affected agency, the Contract Dispute Act cases and select Federal Government personnel disciplinary matters.

The Air Force General Counsel developed the estimating methodology for the contingent liabilities recognized in Note 15. Through legal determination, the Air Force General Counsel assessed and categorized all contingent legal liability cases that equal or exceed the materiality threshold set by Department of Defense Inspector General (DoDIG). For the remaining cases falling below the dollar materiality threshold set by DoDIG, they are considered in aggregate, if the total amount of the cases equal or exceed the established materiality threshold.

The Air Force General Counsel also solicited case data through quarterly data calls from the Air Force JAC (Judge Advocate Civil Lawsuits and Litigation Directorate). Air Force financial management personnel used the solicited case data which included the current reporting year and each of the prior two years to estimate the amounts of probable and reasonably possible contingent liabilities.

Air Force financial management personnel used a three year prior case analysis spreadsheet which was developed by the Air Force Audit Agency to calculate and estimate the amount of contingent liabilities (probable and reasonably possible) for reporting or disclosing in the quarterly financial statements. In cases where Air Force General Counsel disclosed that a judgement has been awarded against the Air Force, these amounts were reported on the Balance Sheet and within Note 15.

Note 17. Military Retirement and Other Federal Employment Benefits

As of September 30	2008			2007
	Liabilities	Assumed Interest Rate (%)	(Less: Assets Available to Pay Benefits)	Liabilities
(Amounts in thousands)				
1. Pension and Health Actuarial Benefits				
A. Military Retirement Pensions	\$ 0		\$ 0	\$ 0
B. Military Retirement Health Benefits	0		0	0
C. Military Medicare-Eligible Retiree Benefits	0		0	0
D. Total Pension and Health Actuarial Benefits	\$ 0		\$ 0	\$ 0
2. Other Actuarial Benefits				
A. FECA	1,158,232		0	1,132,550
B. Voluntary Separation Incentive Programs	0		0	0
C. DoD Education Benefits Fund	0		0	0
D. Total Other Actuarial Benefits	\$ 1,158,232		\$ 0	\$ 1,132,550
3. Other Federal Employment Benefits	5,182		-5,182	0
4. Total Military Retirement and Other Federal Employment Benefits:	\$ 1,163,414		\$ -5,182	\$ 1,158,232
				\$ 1,137,016

Relevant Information for Comprehension

The Federal Employees' Compensation Act (FECA) liability is determined using a method that utilizes historical benefit payment patterns to predict the ultimate payments. The projected annual benefit payments are then discounted to present value using the Office of Management and Budget's economic assumptions for 10-year U.S. Treasury notes and bonds.

Interest rate assumptions utilized for discounting were as follows:

2008

4.368% in Year 1

4.770% in Year 2

And thereafter

To adjust more specifically for the effects of inflation on the liability for future workers' compensation benefits, wage inflation factors (Cost of Living Adjustments (COLAs)) and medical inflation factors (Consumer Price Index Medical (CPIMs)) were applied to the calculation of projected future benefits. The actual rates for these factors for the charge back year (CBY) 2007 were also used to adjust the methodology's historical payments to current year constant dollars.



UNITED STATES AIR FORCE

General Fund

Notes to the Principal Statements

The compensation COLAs and CPIMs used in the projections for various CBYs were as follows:

CBY	COLA	CPIM
2008	3.03%	4.71%
2009	3.87%	4.01%
2010	2.73%	3.86%
2011	2.20%	3.87%
2012	2.23%	3.93%
2013 +	2.30%	3.93%

The model's resulting projections were analyzed to ensure that the estimates were reliable. The analysis was based on four tests: (1) a sensitivity analysis of the model to economic assumptions, (2) a comparison of the percentage change in the liability amount by agency to the percentage change in the actual incremental payments, (3) a comparison of the incremental paid losses per case (a measure of case-severity) in CBY 2007 to the average pattern observed during the most current three charge back years, and (4) a comparison of the estimated liability per case in the FY 2007 projection to the average pattern for the projections of the most recent three years.

The Air Force's actuarial liability for workers' compensation benefits is developed and provided by Department of Labor at the end of each fiscal year. There is no change on a quarterly basis. A comparison of 4th Quarter, FY 2008, and 4th Quarter, FY 2007, disclosed a minor change.

Programs for which actuarial benefits are computed include FECA, the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases, plus a component for incurred but unreported claims.

Other Federal Employment Benefits is comprised of additional post employment benefits due and payable to military personnel.

Note 18. General Disclosures Related to the Statement of Net Cost

Intragovernmental Costs and Exchange Revenue As of September 30	2008	2007
(Amounts in thousands)		
1. Intragovernmental Costs	\$ 33,664,673	\$ 30,577,467
2. Public Costs	114,425,085	111,884,904
3. Total Costs	\$ 148,089,758	\$ 142,462,371
4. Intragovernmental Earned Revenue	\$ -4,937,405	\$ -4,571,324
5. Public Earned Revenue	-938,303	-1,144,216
6. Total Earned Revenue	\$ -5,875,708	\$ -5,715,540
7. Net Cost of Operations	\$ 142,214,050	\$ 136,746,831

Relevant Information for Comprehension

Intragovernmental costs and revenue are related to transactions made between two reporting entities within the Federal Government.

Public costs and revenues are exchange transactions made between the reporting entity and a nonfederal entity.

The Air Force's systems do not track intragovernmental transactions by customer at the transaction level. Therefore, internal DoD buyer-side balances are adjusted to agree with internal seller-side balances for revenue. Expenses were adjusted by accruing additional accounts payable and expenses as appropriate.

The Statement of Net Cost (SNC) represents the net cost of programs and organizations of the Federal Government supported by appropriations or other means. The intent of SNC is to provide gross and net cost information related to the amount of output or outcome for a given program or organization administered by a responsible reporting entity. The Air Force current processes and systems do not capture and report accumulated costs for major programs based upon the performance measures as required by the Government Performance and Results Act. The Air Force is in the process of reviewing available data and developing a cost reporting methodology as required by the Statement of Federal Financial Accounting Standards (SFFAS) No. 4, "Managerial Cost Accounting Concepts and Standards for the Federal Government."

The amounts presented in this statement are based on budgetary obligations, disbursements and collection transactions, as well as nonfinancial feeder systems that were adjusted to record known accruals for major items such as; payroll expenses, accounts payable, and environmental liabilities and may not meet accounting standards.

The Air Force's accounting systems do not capture information relative to heritage assets separately and distinctly from normal operations.

Note 19. Disclosures Related to the Statement of Changes in Net Position

Relevant Information for Comprehension

The Appropriations Received line item on the Statement of Changes in Net Position (SCNP) differs from that reported on the Statement of Budgetary Resources (SBR) because Appropriations Received on SCNP does not include appropriated dedicated and earmarked receipts. Dedicated and earmarked receipts are accounted for as either nonexchange revenue or donations and forfeitures of cash and cash equivalents. This resulted in a \$3.6 million difference due to additional resources included in the Appropriation Received on the SBR. Refer to Note 20 for additional details.

The eliminations column on SCNP will reflect zero dollars. In the SCNP, all offsetting balances (i.e. transfers-in and transfers-out, revenues, and expense) for intradepartmental activity between earmarked and other (nonearmarked) funds are reported on the same lines. This results in an eliminations column, which appears to contain no balances. In reality, the column contains all appropriate elimination entries, but all net to zero within each respective line, except for intraentity imputed financing costs.



Note 20. Disclosures Related to the Statement of Budgetary Resources

As of September 30	2008	2007
(Amounts in thousands)		
1. Net Amount of Budgetary Resources Obligated for Undelivered Orders at the End of the Period	\$ 70,594,923	\$ 64,119,346
2. Available Borrowing and Contract Authority at the End of the Period	0	0

Apportionment Categories

Funds are apportioned by three categories: (1) Category A is apportioned quarterly, (2) Category B is apportioned by activity or project, and (3) Exempt are funds not subject to apportionment. The amounts of direct and reimbursable obligations incurred are stated in the table.

	Category A	Category B	Exempt
Direct	\$86.9 billion	\$68.1 billion	\$2.1 million
Reimbursable	\$6.4 billion	\$4.0 billion	\$10.0 million

Intraentity Transactions

The Statement of Budgetary Resources (SBR) includes intraentity transactions because the statements are presented as combined.

Permanent Indefinite Appropriations

Permanent indefinite appropriations are as follows (reference Note 23 for additional information):

- Department of the Air Force General Gift Fund [10 USC 2601(b)]
- Wildlife Conservation Fund [16 USC 670(a)]
- Air Force Cadet Fund [37 USC 725(s)]

Legal limitations and time restrictions on the use of unobligated appropriation balances such as upward adjustments are provided under Public Law.

Appropriations Received

The Appropriations Received line item on the Statement of Changes in Net Position differs from that reported on SBR because Appropriations Received on the Statement of Changes in Net Position do not include dedicated appropriations and earmarked receipts. Dedicated appropriations and earmarked receipts are accounted for as either nonexchange revenue or donations and forfeitures of cash and cash equivalents. This resulted in a \$3.6 million difference.

Note 21. Reconciliation of Net Cost of Operations to Budget

As of September 30	2008	2007
(Amounts in thousands)		
Resources Used to Finance Activities:		
Budgetary Resources Obligated:		
1. Obligations incurred	\$ 165,397,504	\$ 156,973,842
2. Less: Spending authority from offsetting collections and recoveries (-)	-14,551,339	-14,269,297
3. Obligations net of offsetting collections and recoveries	\$ 150,846,165	\$ 142,704,545
4. Less: Offsetting receipts (-)	-201,497	-140,980
5. Net obligations	\$ 150,644,668	\$ 142,563,565
Other Resources:		
6. Donations and forfeitures of property	0	0
7. Transfers in/out without reimbursement (+/-)	322,962	261,389
8. Imputed financing from costs absorbed by others	628,882	724,671
9. Other (+/-)	1,323,184	-1,265,895
10. Net other resources used to finance activities	\$ 2,275,028	\$ -279,835
11. Total resources used to finance activities	\$ 152,919,696	\$ 142,283,730
Resources Used to Finance Items not Part of the Net Cost of Operations:		
12. Change in budgetary resources obligated for goods, services and benefits ordered but not yet provided:		
A. Undelivered Orders (-)	\$ -6,483,468	\$ -7,144,892
B. Unfilled Customer Orders	-161,014	627,428
13. Resources that fund expenses recognized in prior Periods (-)	-86,602	-801,933
14. Budgetary offsetting collections and receipts that do not affect Net Cost of Operations	201,497	140,978
15. Resources that finance the acquisition of assets (-)	-18,749,096	-15,504,535
16. Other resources or adjustments to net obligated resources that do not affect Net Cost of Operations:		
A. Less: Trust or Special Fund Receipts Related to exchange in the Entity's Budget (-)	0	0
B. Other (+/-)	-1,646,144	1,004,509
17. Total resources used to finance items not part of the Net Cost of Operations	\$ -26,924,827	\$ -21,678,445
18. Total resources used to finance the Net Cost of Operations	\$ 125,994,869	\$ 120,605,285
Components of the Net Cost of Operations that will not Require or Generate Resources in the Current Period:		
Components Requiring or Generating Resources in Future Period:		
19. Increase in annual leave liability	\$ 75,316	\$ 3,809
20. Increase in environmental and disposal liability	1,367,508	343,915
21. Upward/Downward reestimates of credit subsidy expense (+/-)	0	0
22. Increase in exchange revenue receivable from the public (-)	0	0
23. Other (+/-)	533,952	84,400
24. Total components of Net Cost of Operations that will Require or Generate Resources in future periods	\$ 1,976,776	\$ 432,124
Components not Requiring or Generating Resources:		
25. Depreciation and amortization	\$ 11,551,854	\$ 11,977,009
26. Revaluation of assets or liabilities (+/-)	4,323,066	1,429,657
27. Other (+/-)		
A. Trust Fund Exchange Revenue	0	0
B. Cost of Goods Sold	0	0
C. Operating Material and Supplies Used	22,597,444	25,927,617
D. Other	-24,229,959	-23,624,862
28. Total Components of Net Cost of Operations that will not Require or Generate Resources	\$ 14,242,405	\$ 15,709,421
29. Total Components of Net Cost of Operations that will not Require or Generate Resources in the current period	\$ 16,219,181	\$ 16,141,545
30. Net Cost Operations	\$ 142,214,050	\$ 136,746,830



Relevant Information for Comprehension

Due to Air Force financial system limitations, budgetary data is not in agreement with proprietary expenses and assets capitalized. An adjustment of \$519.7 million was made to the note schedule, in the Other Components Not Requiring or Generating Resources category, to bring it into balance with the Statement of Net Cost. The difference between budgetary and proprietary data is a previously identified deficiency.

The following note schedule lines are presented as combined instead of consolidated due to intraagency budgetary transactions not being eliminated:

- Obligations Incurred
- Less: Spending Authority from Offsetting Collections and Recoveries
- Obligations Net of Offsetting Collections and Recoveries
- Less: Offsetting Receipts
- Net Obligations
- Undelivered Orders
- Unfilled Customer Orders

Other Resources Used to Finance Activities consist of other gains and losses to adjust intragovernmental transfers in.

Other Resources Used to Finance Items Not Part of the Net Cost of Operations include adjustments to net obligated resources that do not affect the Net Cost of Operations such as net transfers in and transfers out without reimbursement, and other gains and losses to adjust intragovernmental transfers in.

Other Components Requiring or Generating Resources in Future Period consist of expenses due to Air Force active military personnel, expenses of Operations and Maintenance, and for family housing expense.

Other Components not Requiring or Generating Resources include expense for Operations and Maintenance, Research Development Test and Evaluation, Military Construction, Family Housing, and Military Personnel Expense.

Note 22. Disclosures Related to Incidental Custodial Collections

The Air Force collected \$23.4 million of incidental custodial revenues generated primarily from collection of accounts receivable in cancelled accounts. The Air Force distributed \$23.4 million to the U.S. Treasury.

Note 23. Earmarked Funds

BALANCE SHEET As of September 30	2008				
	Military Retirement Fund	Medicare Eligible Retiree Health Care Fund	Other Earmarked Funds	Eliminations	Total
(Amounts in thousands)					
ASSETS					
Fund balance with Treasury	\$ 0	\$ 0	\$ 8,260	\$ 0	\$ 8,260
Investments	0	0	874	0	874
Accounts and Interest Receivable	0	0	1	0	1
Other Assets	0	0	4	0	4
Total Assets	\$ 0	\$ 0	\$ 9,139	\$ 0	\$ 9,139
LIABILITIES AND NET POSITION					
As of September 30					
Military Retirement Benefits and Other Federal Employment Benefits	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
Other Liabilities	0	0	3,784	0	3,784
Total Liabilities	\$ 0	\$ 0	\$ 3,784	\$ 0	\$ 3,784
Unexpended Appropriations	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
Cumulative Results of Operations	0	0	5,355	0	5,355
Total Liabilities and Net Position	\$ 0	\$ 0	\$ 9,139	\$ 0	\$ 9,139
STATEMENT OF NET COST					
As of September 30					
Program Costs	\$ 0	\$ 0	\$ 12,867	\$ 0	\$ 12,867
Less Earned Revenue	0	0	-10,044	0	-10,044
Net Program Costs	\$ 0	\$ 0	\$ 2,823	\$ 0	\$ 2,823
Less Earned Revenues Not Attributable to Programs	0	0	0	0	0
Net Cost of Operations	\$ 0	\$ 0	\$ 2,823	\$ 0	\$ 2,823
STATEMENT OF CHANGES IN NET POSITION					
As of September 30					
Net Position Beginning of the Period	\$ 0	\$ 0	\$ 4,549	\$ 0	\$ 4,549
Net Cost of Operations	0	0	2,823	0	2,823
Budgetary Financing Sources	0	0	3,629	0	3,629
Other Financing Sources	0	0	0	0	0
Change in Net Position	\$ 0	\$ 0	\$ 806	\$ 0	\$ 806
Net Position End of Period	\$ 0	\$ 0	\$ 5,355	\$ 0	\$ 5,355



Earmarked Funds

Department of the Air Force General Gift Fund [10 USC 2601 (b)]

The Department of the Air Force General Gift Fund accepts, holds, and administers any gift, device, or bequest of real or personal property, made on the condition that it is used for the benefit (or in connection with the establishment, maintenance, or operation) of a school, hospital, library, museum, or cemetery under the Air Force's jurisdiction. The fund is available to such institutions or organizations subject to the terms of the gift, device, or bequest.

Conditional gifts are invested in U.S. Treasury securities, and any interest earned on these securities is added back into the fund.

Wildlife Conservation Fund [16 USC 670 (a)]

The Wildlife Conservation Fund provides for (1) the conservation and rehabilitation of natural resources on military installations, (2) the sustainable multipurpose use of the resources which include hunting, fishing, trapping, and nonconsumptive uses, and (3) the public access to military installations to facilitate its use, subject to safety requirements and military security. The fund is available to carry out these programs and other such expenses that may be necessary for the purpose of the cited statute.

Consisting of both appropriated and nonappropriated funding, this fund gives installation commanders the authority to collect fees from the sale of hunting and fishing permits.

Air Force Cadet Fund [37 USC 725 (s)]

The Air Force Cadet Fund is maintained for the benefit of Air Force Academy cadets. Disbursements are made for the personal services of cadets such as laundry, arts, and athletics while collections are received from the same cadets at least equal to any disbursements made.

The Air Force Cadet Fund is classified as a special fund, the Air Force General Gift Fund and Wildlife Conservation Fund are trust funds. All three funds utilize receipt and expenditure accounts in accounting for and reporting the funds.

Annual Financial Statement 2008

General Fund

Notes to the Principal Statements

BALANCE SHEET As of September 30	2007				
	Military Retirement Fund	Medicare Eligible Retiree Health Care Fund	Other Earmarked Funds	Eliminations	Total

(Amounts in thousands)

ASSETS

Fund balance with Treasury	\$	0	\$	0	\$	7,964	\$	0	\$	7,964
Investments		0		0		823		0		823
Accounts and Interest Receivable		0		0		2		0		2
Other Assets		0		0		5		0		5
Total Assets	\$	0	\$	0	\$	8,794	\$	0	\$	8,794

LIABILITIES AND NET POSITION As of September 30

Military Retirement Benefits and Other Federal Employment Benefits	\$	0	\$	0	\$	0	\$	0	\$	0
Other Liabilities		0		0		4,246		-1,930		2,316
Total Liabilities	\$	0	\$	0	\$	4,246	\$	-1,930	\$	2,316
Unexpended Appropriations	\$	0	\$	0	\$	0	\$	0	\$	0
Cumulative Results of Operations		0		0		4,548		0		4,548
Total Liabilities and Net Position	\$	0	\$	0	\$	8,794	\$	-1,930	\$	6,864

STATEMENT OF NET COST As of September 30

Program Costs	\$	0	\$	0	\$	16,632	\$	0	\$	16,632
Less Earned Revenue		0		0		-13,867		0		-13,867
Net Program Costs	\$	0	\$	0	\$	2,765	\$	0	\$	2,765
Less Earned Revenues Not Attributable to Programs		0		0		0		0		0
Net Cost of Operations	\$	0	\$	0	\$	2,765	\$	0	\$	2,765

STATEMENT OF CHANGES IN NET POSITION As of September 30

Net Position Beginning of the Period	\$	0	\$	0	\$	4,540	\$	0	\$	4,540
Net Cost of Operations		0		0		2,765		0		2,765
Budgetary Financing Sources		0		0		2,773		0		2,773
Other Financing Sources		0		0		0		0		0
Change in Net Position	\$	0	\$	0	\$	8	\$	0	\$	8
Net Position End of Period	\$	0	\$	0	\$	4,548	\$	0	\$	4,548



Note 24. Other Disclosures

As of September 30	2008 Asset Category			
	Land and Buildings	Equipment	Other	Total
(Amounts in thousands)				
1. ENTITY AS LESSEE-Operating Leases				
Future Payments Due				
Fiscal Year				
2009	\$ 55,633	\$ 0	\$ 103,258	\$ 158,891
2010	46,580	0	108,421	155,001
2011	43,516	0	113,842	157,358
2012	44,386	0	119,535	163,921
2013	46,180	0	125,511	171,691
After 5 Years	49,006	0	131,787	180,793
Total Future Lease Payments Due	\$ 285,301	\$ 0	\$ 702,354	\$ 987,655

Relevant Information for Comprehension

Leases in the land and buildings category include costs for operating leased housing facilities for the active Air Force in the United States and overseas. Section 801 Family Housing Program leases are not included in this category.

Other leases consist of Air Force vehicle leases from the General Services Administration and commercial lessors located in Europe, Southwest Asia, and the United States.

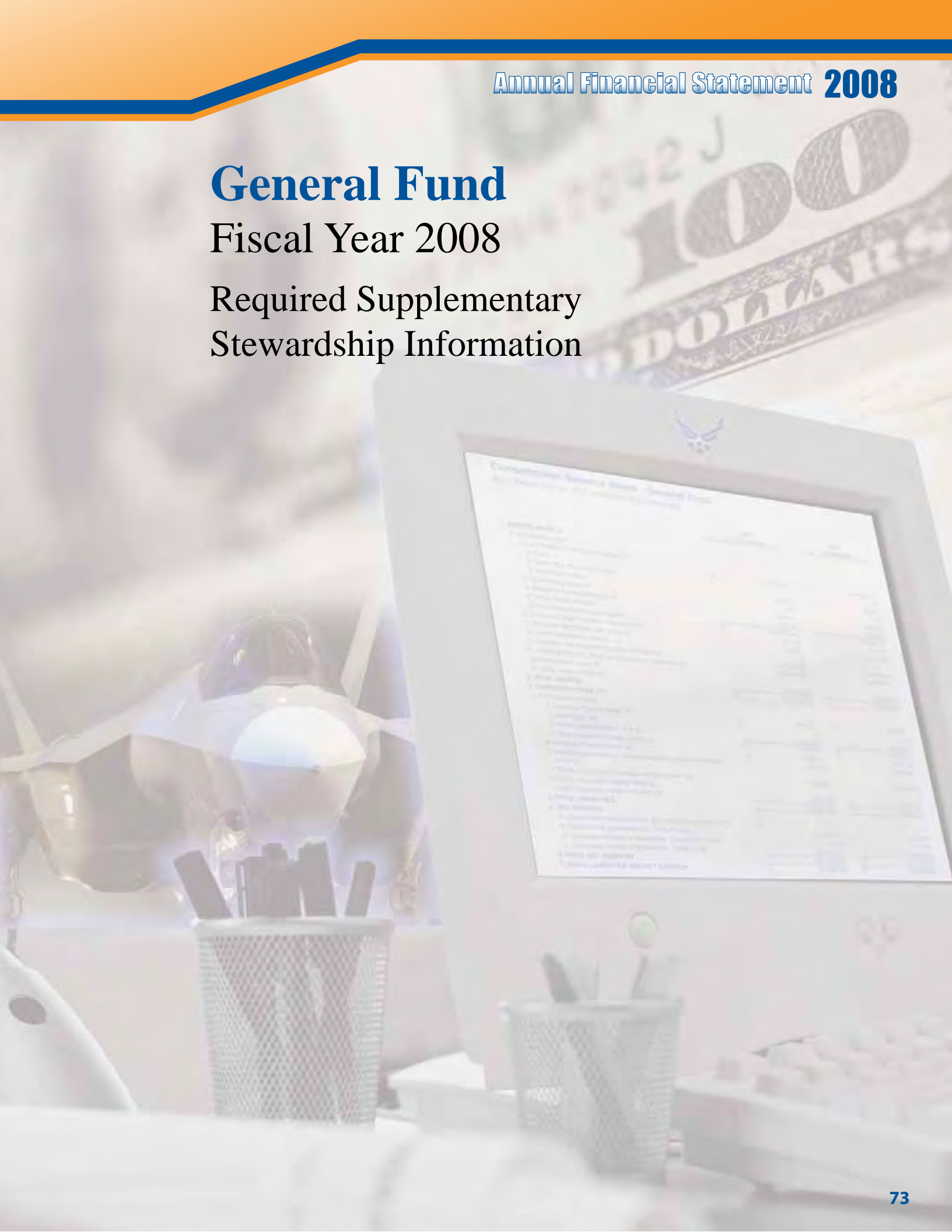
Note 25. Restatements

Not Applicable

General Fund

Fiscal Year 2008

Required Supplementary
Stewardship Information





STEWARDSHIP INVESTMENTS

Stewardship investments are substantial investments made by DoD for the long-term benefit of the nation and public, but are not physical assets owned by DoD. Stewardship investments include expenses incurred for federally financed, but not federally owned, physical property (Nonfederal Physical Property) and federally financed research and development (Research and Development).

NONFEDERAL PHYSICAL PROPERTY

Nonfederal Physical Property investments are expenses included in calculating net cost incurred by the reporting entity for the purchase, construction or major renovation of physical property owned by state and local governments. The expenses include the costs identified for major additions, alterations and replacements, purchases of major equipment, and purchases or improvements of other nonfederal assets. In addition, Nonfederal Physical Property Investments include federally-owned physical property transferred to state and local governments.

NONFEDERAL PHYSICAL PROPERTY
Yearly Investment in State and Local Governments
For the Current and Four Preceding Fiscal Years
(Amounts in millions)

Categories	2008	2007	2006	2005	2004
1. Transferred Assets: National Defense Mission Related	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
2. Funded Assets: National Defense Mission Related	19.6	2.8	8.5	8.3	18.3
Totals	\$ 19.6	\$ 2.8	\$ 8.5	\$ 8.3	\$ 18.3

The Air National Guard investments in Nonfederal Physical Property are strictly through the Military Construction Cooperative Agreements (MCCAs). These agreements involve the transfer of money only and allow joint participation with States, Counties, and Airport Authorities for construction or repair of airfield pavements and facilities required to support the flying mission assigned at these civilian airfields.

Investment values included in this report are based on Nonfederal Physical Property outlays (expenditures). Outlays are used because current DoD systems are unable to capture and summarize costs in accordance with the Federal GAAP requirements.

RESEARCH AND DEVELOPMENT

Research and Development investments are incurred in the search for new or refined knowledge and ideas, for the application or use of such knowledge, ideas for the development of new or improved products and processes, with the expectation of maintaining or increasing national economic productive capacity or yielding other future benefits.

INVESTMENTS IN RESEARCH AND DEVELOPMENT

Yearly Investment in Research and Development
For the Current and Four Preceding Fiscal Years
(Amounts in millions)

Categories	2008	2007	2006	2005	2004
1. Basic Research	\$ 389	\$ 383	\$ 374	\$ 373	\$ 209
2. Applied Research	1,051	1,032	1,034	919	735
3. Development					
Advanced Technology Development	611	937	970	924	681
Advanced Component Development and Prototypes	2,423	2,310	2,185	1,769	1,426
System Development and Demonstration	3,654	4,094	4,572	4,332	4,390
Research, Development, Test and Evaluation					
Management Support	1,323	1,286	1,381	1,125	890
Operational Systems Development	12,459	11,481	11,579	11,021	10,861
4. Totals	\$ 21,910	\$ 21,523	\$ 22,095	\$ 20,463	\$ 19,192

Basic Research is the systematic study to gain knowledge or understanding of the fundamental aspects of phenomena and of observable facts without specific applications, processes, or products in mind. Basic Research includes scientific study and experimentation directed toward increasing fundamental knowledge and understanding in those fields of the physical, engineering, environmental, and life sciences related to long-term national security needs. Major outputs are scientific studies and research papers.

Applied Research is the systematic study to gain knowledge or understanding necessary for determining the means by which a recognized and specific need may be met. It is a systematic expansion and application of knowledge to develop useful materials, devices, systems, and methods. This research points toward specific military needs with a view toward developing and evaluating the feasibility and practicality of proposed solutions and determining their parameters. Major outputs are scientific studies, investigations, research papers, hardware components, software codes, and limited construction of, or part of, a weapon system, to include nonsystem specific development efforts.

Development takes what has been discovered or learned from basic and applied research and uses it to establish technological feasibility, assessment of operability, and production capability. Development is comprised of the following five stages:

1. Advanced Technology Development includes development of subsystems and components plus efforts to integrate subsystems and components into system prototypes for field experiments and/or tests in a simulated environment. It also includes concept and technology demonstrations of subsystems and components or system models.
2. Advanced Component Development and Prototypes evaluates integrated technologies in as realistic an operating environment as possible to assess the performance or cost reduction potential of advanced technology. Programs in this phase are generally system specific. Major outputs of Advanced Component Development and Prototypes are hardware and software components, or complete weapon systems, ready for operational and developmental testing and field use.
3. System Development and Demonstration concludes the program or project and prepares it for production. It consists primarily of preproduction efforts, such as logistics and repair studies. Major outputs are weapon systems finalized for complete operational and developmental testing.



4. Research, Development, Test and Evaluation Management Support is support for installations and operations for general research and development use. This category includes costs associated with test ranges, military construction maintenance support for laboratories, operations and maintenance of test aircraft and ships, and studies and analysis in support of the R&D program.
5. Operational Systems Development is concerned with development projects in support of programs or upgrades still in engineering and manufacturing development, which have received approval for production, for which production funds have been budgeted in subsequent fiscal years.

The following are representative program examples for each of the above major categories:

Basic Research: The Air Force, working with researchers at the University of California at San Diego, created an inexpensive sensor the size of a penny that detects bombs made with improvised peroxide explosive devices. The sensors are made using ultra thin films and have a fast response time and sensitivity that enables them to detect even minute amounts of peroxide vapors in an environment. When peroxide is present, the film made of cobalt shows a reduction in current, while the copper films show an increase.

Air Force scientists have also demonstrated world-record performance of transparent transistors created from thin-film nanocrystalline zinc oxide that can function undetected on clear surfaces, such as glass or plastic. A combination of high channel mobility, mechanical flexibility, and high optical transparency at room temperature make the transparent transistors an excellent candidate to support a wide range of future Air Force electronics needs and applications.

Applied Research: The Air Force successfully developed and transitioned Automated Detection Identification and Tracking of Deceptive Terrorist Activity (AUDIT) technology to numerous DoD and Intelligence Community (IC) users. A variant of this technology is being used by the Air Force to fight cyber terrorism and network attacks. AUDIT technology is also in use, or in evaluation for use, by the U.S. Special Operations Command, the Joint Improvised Explosive Device Defeat Organization, and the Department of Homeland Security – Cargo Border Protection, among others.

The Air Force is currently developing the Wafer Scale Signal Processor (WSSP) for applications where size, weight, and power are severely constrained, such as space applications. The WSSP has six processors per chip and provides the most floating point operations (one Giga Floating point Operation Per Second) per watt of power ever built for any application. Processors will be a part of the Air Force's Plug-and-Play Satellite and are available for both satellite control and signal processing.

Advanced Technology Development: The Air Force developed and demonstrated a persistent electro-optical surveillance technology called AngelFire, which was deployed to Iraq in support of the United States Marine Corps in October 2007. Since then, it has operated continuously in a counter-improvised explosive device role. The Air Force is now developing the next phase of AngelFire which will include the addition of an infrared capability to provide nighttime coverage.

With its TacSat-2 program, the Air Force successfully demonstrated responsive space enabling technologies during its one year of mission operations. TacSat-2 served as the forerunner for speedy satellite production and launch, and direct theater operation. For payloads, TacSat-2 had tactical sensors, two innovative communication links, experimental solar arrays, star cameras, and propulsion systems, as well as payloads designed to answer basic scientific questions, such as how atmospheric density and radio frequency signal interference fluctuates with local and remote environmental conditions. Another historic first for TacSat-2 involved ground operators successfully tasking and receiving processed data within 90 minutes, with traceability to future turnaround times as short as ten minutes.

As part of efforts to reduce the U.S. military's reliance on foreign energy sources, the Air Force completed certification of an alternative jet fuel blend on the C-17 and B-1 aircraft as well as Air Force ground support equipment and vehicles in August 2008. The B-52 previously received certification in August 2007. These certifications allow operational use of the Fischer-Tropsch (FT) and JP-8 fuel blend in these aircraft and support equipment and vehicles. The F-15, F-22 and KC-135 aircraft flight tested the alternative jet fuel blend in August 2008. The F-22 and KC-135 also performed two aerial refuelings on the same sortie during these flight tests. This FT effort is part of the Pentagon's Assured Fuel Initiative that seeks to convert coal, of which the United States has abundant reserves, into liquid fuel. The fuel is derived from refining natural gas under the FT process, which is named after its German inventors in the 1920's. The Air Force plans to test and certify every airframe to fly on this synthetic fuel blend by early 2011. The Air Force developed improved turbine engine life-management tools that integrate state-of-the-art material analysis, enhanced non-destructive evaluation, and data management as a comprehensive life management system. Component cost avoidance is estimated to exceed \$300 million for the F100/F110 engine series alone.

The Air Force developed a custom-molded, noise-attenuating earplug that enables seamless voice communications to and from radios, while electronically passing all outside environmental sounds to the operator at safe levels. The Joint Unmanned Combat Air Systems (J-UCAS) program was terminated in December 2005. The two J-UCAS X-45A aircraft flew a total of 64 flights and performed limited demonstrations of precision weapon drops, multi-ship coordinated flights, and collaborative targeting technologies, illustrating the potential for future unmanned combat air systems development programs. The Air Force continued to advocate the Air Force Research Library (AFRL) Automated Air Refueling (AAR) program, which continues to make historic progress. The AAR program consists of a combination of simulation and flight tests in order to develop the appropriate requirements and system design for Unmanned Aerial Vehicle (UAV) refueling, which may also be applied to manned refueling. Phase I of the AAR demonstration program was completed with great success. In September 2007, the AAR Positions and Pathways Flight Test successfully demonstrated automated maneuvering with over 8 hours of hands-off formation flight, including movement from the observation position (off the wing of the tanker) to pre-contact position, to the contact position, and then back. February 2008 saw a successful four-ship CONOPS simulation involving Air Mobility Command operators in the loop. AFRL kicked off AAR Phase II in June 2008 by issuing solicitations for an overall Phase II integrating contractor and a Precision GPS developer; selection of the winning bidders is planned for 1st Quarter, FY 2009.

Demonstration and Validation (Advanced Component Development and Prototypes): The Air Force's Advanced Component Development and Prototypes programs are comprised of system specific advanced technology integration efforts accomplished in an operational environment to help expedite transition from the effort. In FY 2004, the Air Force successfully demonstrated Fighter Aircraft Command and Control Enhancement (FACE). FACE provides an improved, beyond-line-of-sight (BLOS) command and control link with fighter aircraft by integrating Iridium telephone communications equipment with existing aircraft communications equipment. BLOS capability has traditionally been provided by low-density, high-demand airborne platforms acting as communications relays. FACE provides relief for these overworked assets, while allowing combatant commanders to maintain positive control of the battle space. FACE has been approved for deployment to Afghanistan through the Air Force's Rapid Response Process, and has the potential for extensive use in virtually any area of responsibility, including Homeland Defense.

In FY 2005, the Air Force restructured and refocused the Space Radar (SR) program (formerly Space Based Radar) to address congressional concerns with technical risk, affordability, and DoD-IC integration. In January 2005 the Secretary of Defense and the Director of Central Intelligence signed a joint memo designating the SR program as the single space radar capability for the nation. In May 2007, the Deputy Secretary of Defense and the Principal Deputy Director of National Intelligence signed the Joint Radar Enterprise Memorandum, agreeing to a joint funding arrangement, acquisition strategy, and management structure. The details of this arrangement are being captured in the Joint Radar Enterprise Management Plan. The SR Initial Capabilities Document (ICD) was approved by the IC Mission Requirements Board (MRB) in De-



ember 2005 and the DoD Joint Requirements Oversight Council (JROC) in January 2006. The Capability Development Document is being prepared in parallel with the SR system concept of operations (CONOPS); both are on track for MRB and JROC approval in 1st Quarter, FY 2009. The SR program implemented a demonstration framework approach to system development. This approach will further technology maturity risk reduction and CONOPS experimentation through a mix of space, air, and land-based demonstration activities that will maximize existing assets. The SR program continues to make significant advancement towards the System Requirements Review milestone. The SR program will provide day/night, all-weather global surface moving target indications (MTI), SAR, and high-resolution terrain information (HRTI) capabilities from a space-based platform. Initial launch capability is planned for 4th Quarter, FY 2016.

System Development and Demonstration: The F-35 Joint Strike Fighter (JSF) program is developing a family of strike fighter aircraft for the Air Force, Navy, Marine Corps and our allies, with maximum commonality among the variants to minimize life cycle costs. The Air Force Conventional Takeoff and Landing (CTOL) variant will be a multi-role, primary air-to-ground aircraft to replace the F-16 and A-10, and complement the F-22. While the F-22 will establish air dominance, the F-35 with its combination of stealth, large internal payloads and multi-spectral avionics will provide persistent stealth and precision engagement to future battle space. The F-35 is in the 7th year of a 13-year System Development and Demonstration (SDD) effort. Significant program accomplishments in FY 2008 include:

- First flight of Short Takeoff and Vertical Landing (STOVL) variant on June 11, 2008
- Awarded Low Rate Initial Production (LRIP) Lot 2 contracts for 6 CTOLs on May 7, 2008 and 6 STOVLs on July 22, 2008
- Two STOVL test aircraft were delivered
- Ten flight test aircraft [4 CTOLs, 3 STOVLs, and 3 Combat Vehicles (CVs)] and five ground test aircraft (2 CTOLs, 1 STOVL, and 2 CVs) are currently in assembly

The Transformational Satellite Communications (TSAT) system will provide the essential capabilities required to enable the DoD's vision for 21st century military operations. TSAT, which consists of a five-satellite geosynchronous satellite constellation, network operations centers, and associated ground architecture, will establish global internet-like connectivity that is essential for U.S. and allied personnel to communicate as a joint networked force. It will also extend assured, protected communications connectivity to mobile forces in theater and vastly increase the overall capacity of our military satellite infrastructure. FY 2007 was proven to be a milestone year for TSAT. The program made excellent progress in demonstrating the maturity of its critical technology elements by successfully completing the third of three demonstrations at MIT Lincoln Laboratory (MIT/LL), testing each competing contractor's proposed Laser Communications (or 'lasercom') and next-generation satellite processor/router (NGPR) equipment. The program also completed a successful four-week system design review (SDR), where the government assessed the viability of the architecture designs for each competing contractor on the satellite segment and on the TSAT Mission Operations System (TMOS) ground segment, whose contract was awarded in January 2006.

Based upon the extent and success of risk reduction efforts accomplished thus far on this program, TSAT is prepared to meet a Key Decision Point-B (KDP-B) milestone in order to gain Milestone Decision Authority (MDA) acceptance to proceed into the Preliminary Design Phase of the program's acquisition cycle. In preparation for the KDP-B decision, several in-depth reviews were performed this summer on TSAT, including an Independent Program Assessment, an Independent Cost Evaluation, and a Technical Readiness Assessment. The underlying result of these detailed reviews was that the program structure, budgeting, and technical development are well defined, properly managed and mature enough to support the initiation of preliminary design activities. Additionally, in June 2007, the TSAT program released a Request for Proposals

(RFP) on the space segment development contract. The Air Force is reviewing bids from multiple contractors. Based on an Authority to Proceed from MDA in November 2007, the TSAT program anticipates a contract award announcement as early as 1st Quarter, FY 2009.

TSAT is extending its risk reduction efforts with a revised goal of a KDP-B review in October 2008. TSAT will award the space segment contract in FY 2009, starting its satellite design work and continuing the development of the TMOS segment. The launch of the first TSAT is targeted for 3rd Quarter, FY 2018.

The MQ-1 Predator UAV program is developing the capability to instantaneously derive and disseminate Joint Direct Attack Munition (JDAM)-quality coordinates from the viewpoint of its electro-optical/infra-red (EO/IR) full motion video sensor. Sensor improvements include development of a precise attitude reference system coupled with an off-the-shelf two color eye-safe laser rangefinder/designator plus development of an accurately timed metadata system. Aircraft will be modified with a new guidance system incorporating differential GPS. Fielding is scheduled to begin in FY 2010. Follow-on development will provide instantaneous JDAM-quality data for all pixels within the EO/IR image.

In February 2008, the Global Hawk program greatly accelerated their flight test program to support warfighter requirements. On March 22, 2008, the Global Hawk Block 20/30 flight test program exceeded a 28-hour key performance parameter endurance threshold by flying a 33.1 hour flight test. The first block of 30 aircraft was delivered to Edwards AFB in 2008 to support developmental flight test. The first flight with the Airborne Signals Intelligence Payload (ASIP) was flown, issuing in the era of Multi-INT Global Hawk capability.

The Airborne Warning and Control System (AWACS) aircraft continues to modernize its mission capabilities to remain an effective airborne battle management and surveillance system for command and control of combat forces. The Block 40/45 Upgrade improves the quality and timeliness of sensor data for shooters, improves combat identification, supports a Single Integrated Air Picture (SIAP) through multi-sensor integration, improves the AWACS contribution to Time Critical Targeting via Data Link Infrastructure, improves electronic support measures processing, and enables more effective, faster upgrades via an open system, Ethernet-based architecture. Block 40/45 began SDD in 2003, and successfully concluded mission system testing in 2008. The Navigation Warfare (NAVWAR) effort satisfies a Chairman Joint Chiefs of Staff Instruction for Global Positioning Satellite (GPS) users and incorporates new technology into the navigation sensor. The NAVWAR effort began SDD in 2006 and completed flight tests in 2008. Production and fielding will follow in 2009. The Next Generation Identification Friend or Foe (NGIFF) effort provides AWACS with a secure Mode 5 capability. NGIFF completed Risk Reduction efforts and commenced SDD in 2008.

Research, Development, Test and Evaluation Management Support: The Air Force's Research, Development, Test and Evaluation (RDT&E) Management Support efforts include projects directed toward support of installation or operations required for general research and development use. The projects include test ranges, military construction, maintenance support of laboratories, operation and maintenance of test aircraft and ships, and studies and analyses in support of the research and development program. An example of Air Force RDT&E management support is the Major Test and Evaluation Investment program, which funds the planning, improvements and modernization for three national asset test centers having over \$10 billion of unique test facilities/capabilities operated and maintained by the Air Force for the DoD test and evaluation missions, and available to others having a requirement for their unique capabilities.

Many efforts are contained within the Air Force I&M program, but two examples are the Air Force Electronic Warfare Evaluation Simulator (AFEWES) Gateway Project that designed, built and integrated a gateway computer capability linking an AFEWES threat missile simulator into a distributed simulation network that will use test capabilities at locations outside the AFEWES. Adding this capability will provide customers with a high fidelity end-game evaluation capability. In addition, the Propulsion Consolidation and Streamlining project at Arnold Engineering Development Center AFB upgrades



the Turbine Engine Test Facility Test Cell that contained antiquated and inefficient thrust stands, support systems, and control/monitoring equipment. This update will meet future test requirements by reducing operation and maintenance costs, improving facility systems' reliability/availability, streamlining the test process, and mitigating single point failure impacts.

Operational Systems Development: The Air Force's operational system efforts include projects in support of development acquisition programs or upgrades in SDD. The F-22 Raptor program continued full rate production, and will maintain its role as the key enabler of joint air dominance through an incremental modernization program funded through Operational Systems Development activities. Over 127 aircraft have been delivered through end of FY 2008. The development program will enhance the air vehicle, engine, and training systems to improve F-22A weapons, communications, and Intelligence Surveillance Reconnaissance (ISR) capabilities to further enhance Global Strike capabilities. Increment 2 is now resident in delivered aircraft and represents the first upgrade over initial operational capability. FY 2008 activities included development of the Increment 3 suite. A Critical Design Review (CDR) for Increment 3.1 focused on dramatically improving the F-22A Raptor's Air-To-Ground attack capabilities with 4th generation synthetic aperture radar and on completing a new weapon, the Small Diameter Bomb.

The Advanced Medium Range Air-to-Air Missile (AMRAAM) Phase 3 (AIM-120C-7) was approved for fielding in December 2007. Production for this variant began in 4th Quarter, FY 2004, and will complete in 2nd Quarter, FY 2009. The AIM-120C-7 provides a major upgrade over the AIM-120C-6 guidance section, particularly in the use of circular processor cards over previously used rectangular cards. These cards provide significant space savings within the missile for added capability, in addition to providing greater processing power.

AMRAAM Phase 4 (AIM-120D) builds on the AIM-120C-7 capability and is progressing. This new AIM-120D missile will add a GPS/INU and a 2-way Data Link to enhance accuracy and control, and thus, increase weapon effectiveness. In addition, the AIM-120D will have increased range and third party targeting which expands the High Off-boresight launch envelope. The SDD contract was awarded in December 2003. Captive flight testing has been initiated on the F/A-18C/D and F-15C/D. SDD is scheduled to complete in June 2009. Proof-of-design units and proof-of-manufacturing units are being used to support simulation/integration labs, production test equipment development, and ground and flight tests. Production for AIM-120D is scheduled to start in 2nd Quarter, FY 2009 and continue through FY 2024.

The Small Diameter Bomb II (SDB) program is a joint Air Force/Navy interest program that will fill a critical capability gap by providing stand-off, classification and in-weather capability against moving targets. A 42-month Risk Reduction competition between two contractors commenced in May 2006 to mature critical technologies for an all-up-round design. Following the Risk Reduction Phase, a single contractor will be selected in 1st Quarter, FY 2010 to complete a 72-month SDD Phase. Milestone B is scheduled for 1st Quarter, FY 2010. Required Assets Available on the F-15E is planned for FY 2014. The SDB II weapon program will retain the SDB I legacy capability against fixed surface targets, improve GPS anti-jam capability and deny adversaries sanctuary of weather for moving targets.

The SDB I Focused Lethality Munition (FLM), a variant of SDB I, is a Joint Capabilities Technology Development (JCTD) program that effectively demonstrated the military utility for prosecuting high-value targets by generating near-field blast effects in a high collateral risk environment. The FLM variant of SDB I has a composite-cased warhead with a Multi-phase Blast Explosive to reduce fragmentation effects while increasing blast effects. The Military Utility Assessment was completed in June 2008 with positive feedback in all areas. The assessment supports FLM's potential to fill a capability gap of engaging targets with 60 feet of collateral concerns. The FLM weapon consists of a low collateral damage warhead integrated into the SDB I weapon. This JCTD fully leveraged the SDB I program to facilitate rapid acquisition, with 50 residual assets being delivered in March 2008. The FLM capability will increase combatant commanders' strike options, particularly in an urban environment, while decreasing collateral damage risk.

General Fund

Fiscal Year 2008

Required Supplementary Information





UNITED STATES AIR FORCE

General Fund

Required Supplementary Information

Statement of Disaggregated Budgetary Resources - General Fund

As of September 30, 2008 and 2007 (\$ in thousands)

	Other	Research, Development, Test & Evaluation	Operation and Maintenance
BUDGETARY FINANCING ACCOUNTS			
BUDGETARY RESOURCES:			
1. Unobligated balance, brought forward, October 1	\$ 4,520	\$ 3,875,739	\$ 1,565,605
2. Recoveries of prior year unpaid obligations	111	570,699	2,363,569
3. Budget authority			
A. Appropriation	462,057	26,655,288	52,416,274
B. Borrowing authority	0	0	0
C. Contract authority	0	0	0
D. Spending authority from offsetting collections			
1. Earned			
a. Collected	10,143	3,568,684	5,820,324
b. Change in receivables from Federal sources	0	-51,949	-235,143
2. Change in unfilled customer orders			
a. Advance received	0	-170,791	30,198
b. Without advance from Federal sources	0	-67,928	216,548
3. Anticipated for rest of year, without advances	0	0	0
4. Previously unavailable	0	0	0
5. Expenditure transfers from trust funds	0	0	0
E. Subtotal	\$ 472,200	\$ 29,933,304	\$ 58,248,201
4. Nonexpenditure transfers, net, anticipated and actual	-456,154	151,073	731,793
5. Temporarily not available pursuant to Public Law	0	0	0
6. Permanently not available	-2,274	-598,060	-1,038,794
7. Total Budgetary Resources	\$ 18,403	\$ 33,932,755	\$ 61,870,374
STATUS OF BUDGETARY RESOURCES:			
8. Obligations incurred			
A. Direct	\$ 3,228	\$ 25,145,863	\$ 54,333,888
B. Reimbursable	10,044	3,444,640	5,988,768
C. Subtotal	\$ 13,272	\$ 28,590,503	\$ 60,322,656
9. Unobligated balance			
A. Apportioned	1,311	4,986,561	214,301
B. Exempt from apportionment	3,820	0	0
C. Subtotal	\$ 5,131	\$ 4,986,561	\$ 214,301
10. Unobligated balance not available	0	355,689	1,333,417
11. Total status of budgetary resources	\$ 18,403	\$ 33,932,753	\$ 61,870,374
CHANGE IN OBLIGATED BALANCE:			
12. Obligated balance, net			
A. Unpaid obligations, brought forward, October 1	\$ 4,471	\$ 9,380,793	\$ 20,892,264
B. Less: Uncollected customer payments from Federal sources, brought forward, October 1	0	-808,018	-1,359,177
C. Total unpaid obligated balance	\$ 4,471	\$ 8,572,775	\$ 19,533,087
13. Obligations incurred net (+/-)	\$ 13,272	\$ 28,590,503	\$ 60,322,656
14. Less: Gross outlays	-13,427	-28,063,521	-55,746,575
15. Obligated balance transferred, net			
A. Actual transfers, unpaid obligations (+/-)	0	0	0
B. Actual transfers, uncollected customer payments from Federal sources (+/-)	0	0	0
C. Total Unpaid obligated balance transferred, net	\$ 0	\$ 0	\$ 0
16. Less: Recoveries of prior year unpaid obligations, actual	\$ -111	\$ -570,699	\$ -2,363,569
17. Change in uncollected customer payments from Federal sources (+/-)	0	119,878	18,595
18. Obligated balance, net, end of period			
A. Unpaid obligations	4,206	9,337,076	23,104,777
B. Less: Uncollected customer payments (+/-) from Federal sources (-)	0	-688,140	-1,340,582
C. Total, unpaid obligated balance, net, end of period	4,206	8,648,936	21,764,195
NET OUTLAYS:			
19. Net Outlays			
A. Gross outlays	\$ 13,427	\$ 28,063,521	\$ 55,746,575
B. Less: Offsetting collections	-10,143	-3,397,892	-5,850,522
C. Less: Distributed Offsetting receipts	-201,497	0	0
D. Net Outlays	\$ -198,213	\$ 24,665,629	\$ 49,896,053

Annual Financial Statement 2008

General Fund

Required Supplementary Information

Procurement	Military Personnel	Military Construction / Family Housing	2008 Combined	2007 Combined
\$ 13,050,225	\$ 253,422	\$ 2,425,833	\$ 21,175,345	\$ 17,112,927
1,252,684	378,350	36,604	4,602,017	3,921,941
42,763,683	32,291,486	2,203,017	156,791,805	147,674,697
0	0	0	0	0
0	0	0	0	0
647,779	412,663	4,823	10,464,416	10,237,677
-14,896	-52,242	150	-354,080	-517,749
-61,690	0	2,336	-199,948	376,618
-109,656	-30	0	38,934	250,810
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
<u>\$ 43,225,220</u>	<u>\$ 32,651,877</u>	<u>\$ 2,210,326</u>	<u>\$ 166,741,127</u>	<u>\$ 158,022,053</u>
2,338,151	18,833	-33,334	2,750,362	861,271
0	0	0	0	0
-1,338,251	-186,675	-30,402	-3,194,456	-1,769,006
<u>\$ 58,528,029</u>	<u>\$ 33,115,807</u>	<u>\$ 4,609,027</u>	<u>\$ 192,074,395</u>	<u>\$ 178,149,186</u>
\$ 40,960,204	\$ 32,579,886	\$ 2,019,902	\$ 155,042,972	\$ 146,524,833
537,059	374,016	5	10,354,532	10,449,009
<u>\$ 41,497,263</u>	<u>\$ 32,953,902</u>	<u>\$ 2,019,907</u>	<u>\$ 165,397,504</u>	<u>\$ 156,973,842</u>
16,365,177	17,806	2,554,758	24,139,914	18,573,839
0	0	0	3,820	3,271
<u>\$ 16,365,177</u>	<u>\$ 17,806</u>	<u>\$ 2,554,758</u>	<u>\$ 24,143,734</u>	<u>\$ 18,577,110</u>
665,590	144,099	34,362	2,533,157	2,598,234
<u>\$ 58,528,030</u>	<u>\$ 33,115,807</u>	<u>\$ 4,609,027</u>	<u>\$ 192,074,395</u>	<u>\$ 178,149,186</u>
\$ 25,362,483	\$ 2,332,531	\$ 2,960,818	\$ 60,933,360	\$ 53,989,101
-234,945	35,354	0	-2,366,785	-2,633,723
<u>\$ 25,127,538</u>	<u>\$ 2,367,885</u>	<u>\$ 2,960,818</u>	<u>\$ 58,566,575</u>	<u>\$ 51,355,378</u>
\$ 41,497,263	\$ 32,953,903	\$ 2,019,907	\$ 165,397,504	\$ 156,973,842
-35,409,095	-32,502,319	-2,180,654	-153,915,590	-146,107,640
0	0	0	0	0
0	0	0	0	0
<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>
\$ -1,252,684	\$ -378,350	\$ -36,604	\$ -4,602,017	\$ -3,921,941
124,552	52,272	-150	315,146	266,938
30,197,966	2,405,765	2,763,468	67,813,257	60,933,360
-110,393	87,626	-150	-2,051,639	-2,366,785
<u>30,087,573</u>	<u>2,493,391</u>	<u>2,763,318</u>	<u>65,761,618</u>	<u>58,566,575</u>
\$ 35,409,095	\$ 32,502,319	\$ 2,180,654	\$ 153,915,590	\$ 146,107,640
-586,089	-412,663	-7,158	-10,264,468	-10,614,293
0	0	0	-201,497	-140,980
<u>\$ 34,823,006</u>	<u>\$ 32,089,656</u>	<u>\$ 2,173,496</u>	<u>\$ 143,449,625</u>	<u>\$ 135,352,367</u>



DISAGGREGATED STATEMENT OF BUDGETARY RESOURCES

The Air Force has performance measures based on missions and outputs. The Air Force, however, is unable to accumulate costs for major programs based on those performance measures, because its financial processes and systems were not designed to collect and report this type of cost information. Until the processes and systems are upgraded, the Department will break out programs by major appropriation groupings.

STEWARDSHIP PLANT, PROPERTY, AND EQUIPMENT (PP&E)

HERITAGE ASSETS

For Fiscal Year Ended September 30, 2008

(a)	(b)	(c)	(d)	(e)	(f)
Heritage Asset Categories	Measurement Quantity	As of 10/01/07	Additions	Deletions	As of 9/30/08
Buildings and Structures	Each	4,091	868	0	4,959
Archeological Sites	Sites	1,425	505	0	1,930
Museum Collection Items (Objects, Not Including Fine Art)	Each	113,210	4,009	85	117,134
Museum Collection Items (Fine Art)	Each	9,259	111	0	9,370

Heritage Assets are items of historical, natural, cultural, educational, or artistic significance (e.g., aesthetic) or items with significant architectural characteristics.

1. Buildings and Structures

As of September 15, 2008, the Air Force considers 12,719 buildings and structures as National Register of Historic Places (NRHP) listed and eligible buildings and structures. Vast majorities of these are Capehart-Wherry Era (CWE) houses (7,760), which are subject to a recently completed nationwide Program Comment (with the Advisory Council on Historic Preservation) that allows the Air Force to demolish or otherwise remove all but three CWE houses from the Air Force Inventory. Disposition has begun, but is proceeding slowly, so large numbers of CWE Housing remain on the Air Force Real Property Index. These numbers decreased significantly this year (3,068) and will continue to decrease in future years as CWE Housing is removed from the Air Force inventory or privatized. We do not consider CWE Housing as Heritage Assets for this Required Supplementary Information (RSI) report.

The Air Force has 4,959 non-CWE buildings and structures considered Heritage Assets. Of these, 1,314 are listed on NRHP and 3,552 are eligible for listing on NRHP. Since March 2007, Air Force has successfully completed three service-wide data calls to validate "Heritage Asset" information via populating the Automated Civil Engineer System-Real Property (ACES-RP) database (i.e., Air Force's Real Property Inventory). ACES-RP now designates/classifies the historic status of heritage assets (~13,000 historic buildings, structures, and districts) and now meets requirements. The large increase in the number of historic properties (868 from FY 2007) is primarily due to improved data reporting and validations of historic property data in ACES-RP. ACES-RP was initially designed to identify only those heritage assets/historic properties that were nominated and formally listed on the NRHP. ACES-RP now contains validated heritage asset data for 12 Historic Status Codes. Installation Cultural Resource Managers (vice Real Property Managers) across the Air Force were trained to use ACES-RP and successfully populate ACES-RP with data for the required additional 12 codes. The most recent round of historic property validations in ACES-RP is due to be completed by September 30, 2008. The cumulative effect of these validations has largely eliminated the previous, well-documented, disconnect between the Real Property and Cultural Resource com-

munities concerning the number and classification of “heritage assets”. Future annual reminders to Air Force installations will be conducted as part of the annual data call to fulfill a related requirement for archaeological sites. The later data call is sent out each January. Heritage Asset buildings and structures are maintained by each base civil engineering group and are considered to be in good condition. These buildings and structures are subject to National Historic Preservation Act Section 106 review and consultation requirements whenever Air Force undertakings might affect their historic characteristics. Section 106 reviews ensure State Historic Preservation Officers, tribal, and other party concerns are taken into account when Air Force decides to adversely affect Heritage Asset buildings and structures.

2. Archaeological Sites

The timing of this data call is such that Air Force cannot report year-end FY 2008 archaeological or historic building data at the end of FY 2008. Archaeological data reported herein are collected for the Annual Report to Congress on Federal Archaeological Activities, which is compiled by the Air Force Center for Engineering and the Environment from major command supplied data between January and March 2008. Historic building data, on the other hand, were compiled for this report through August 2008. We do not have, as of yet, databases that can provide nearly real-time data on archaeological historic assets, which is required to report up-to-date historic asset numbers at the end of the fiscal year.

As of September 15, 2008, the Air Force has (as reported in the FY 2007 Annual Report to Congress on Federal Archaeological Activity, submitted March 31, 2008) 1,930 archaeological sites listed on or eligible for listing on the NRHP. The Air Force has 9,600 recorded but unevaluated archaeological sites, and 5,455 sites considered ineligible for the NRHP. A total of 16,985 archaeological sites have been reported thus far from Air Force lands. Eligible listed sites (aka “Heritage Assets”) are protected from vandalism and looting, and are maintained in good condition on Air Force installations. Heritage asset archaeological sites are subject to NRHP Section 106 review and consultation when affected by Air Force undertakings. Section 106 reviews ensure State Historic Preservation Officers, tribal, and other party concerns are taken into account when Air Force decides to adversely affect Heritage Asset archaeological sites. All Heritage Asset and unevaluated archaeological sites are managed to prevent significant losses due to erosion and other natural causes.

The table shows 505 archaeological sites were added to the heritage asset list between FY 2007 and FY 2008.

3. Museum Collection Items, Objects Not Including Fine Art

This represents the initial reporting of the number of objects which meet the criteria for historical property as defined in Air Force Instruction 84-103 and that have been evaluated, accessioned, and catalogued in the Air Force national historic collection. No adjustments to past years are required. The National Museum of the United States Air Force (NMUSAF) performs inherently governmental functions by fulfilling statutory requirements properly delegated by the Secretary of the Air Force for management of the Air Force’s national historic collection. During FY 2008, 4,009 objects have been added to the collection, primarily as a result of private donations or by being found on base. One of the most significant acquisitions was the transfer from the Smithsonian Institution of the oldest surviving combat veteran B-17D bomber (“The Swoose”). 85 objects were deaccessioned from the collection as having been determined not to meet historic property criteria, in poor condition, or transferred to other agencies. The overall condition of the historic collection, which is primarily located at the NMUSAF, is very good as a result of both professional care from trained conservators and improved exhibit/storage conditions. The stewardship and condition of the national historic collection were determined to meet or exceed all established professional standards during the FY 2008 museum reaccreditation inspection of the NMUSAF by the American Association of Museums. As part of the NMUSAF’s collection management plans, the process of the accession and deaccession of objects is continuous.



4. Museum Collection Items, Fine Art

The art collection contains original oils, drawings, sketches and sculptures. Since the last report the Air Force Art Collection has received 111 newly donated paintings. These paintings were the direct result of the artists visiting bases and operations throughout Air Force.

The collection is maintained and kept in good condition. Each year during the annual inventory, Air Force Art Program Office requests the condition of the paintings as well. Maintenance continues to be a constant.

STEWARDSHIP LAND

STEWARDSHIP LAND

For Fiscal Year Ended September 30, 2008

(in thousands of acres)

(a) Facility Code	(b) Facility Title	(c) As of 10/01/07	(d) Additions	(e) Deletions	(f) As of 9/30/08
9110	Government Owned Land	1,508	0	7	1,501
9111	State Owned Land	0	0	0	0
9120	Withdrawn Public Land	7,593	0	1	7,592
9130	Licensed and Permitted Land	137	0	1	136
9140	Public Land	0	0	0	0
9210	Land Easement	178	0	6	172
9220	In-leased Land	44	48	0	92
9230	Foreign Land	308	0	18	290
Grand Total					9,783
Total - All Lands					2,191
Total - Stewardship Lands					7,592

Stewardship Land is land rights owned by the Federal Government but not acquired for, or in connection with, items of General Property, Plant, and Equipment (PP&E). "Acquired for or in connection with" is defined as including land acquired with the intent to construct general PP&E and land acquired in combination with general PP&E. Without exception, all land provided to the Department from the public domain, or at no cost, shall be classified as Stewardship Land, regardless of its use.

The Air Force has 7,592,000 acres of mission-essential Stewardship Land under their administration. The beginning balance (FY 2007 RSI reported ending balance) decreased by 108,000 acres because ACES-RP categorized Stewardship Land differently from the table above. Specifically, certain category codes are now reported as Government Owned Land rather than Withdrawn Public Land. Land purchased by the Air Force with the intent to construct buildings or facilities is considered PP&E and is reported on the balance sheet. All stewardship land, as reported, is in acceptable condition, based on designated use.

REAL PROPERTY DEFERRED MAINTENANCE**REAL PROPERTY DEFERRED MAINTENANCE**

For Fiscal Year Ended September 30, 2008

(Amounts in millions)

Property Type	Current Fiscal Year (CFY)		
	1. Plant Replacement Value	2. Required Work (deferred maintenance)	3. Percentage
1. Category 1: Buildings, Structures, and Utilities (Enduring Facilities)	\$262,065	\$17,906	7%
2. Category 2: Buildings, Structures, and Utilities (Excess Facilities or Planned for Replacement)	\$22,476	\$38	<1%
3. Category 3: Buildings, Structures, and Utilities (Heritage Assets)	\$10,596	\$914	9%

Use of Q-Rating versus Facilities Sustainment Model (FSM) to reflect Deferred Sustainment

The use of Q-Rating as a basis for calculated deferred maintenance is not prudent. The Service's Q-Rating database has not sufficiently matured compared with the FSM dataset.

At this stage of Q-Rating planning and development, facility Q-Ratings cannot be readily tied to actual obligations nor do they provide a consistent service-wide metric based on commercial standards.

Based on previous submissions, the use of FSM to benchmark facility requirements has proven itself in the Air Force Corporate Structure (AFCS) process by yielding data constancy and high fidelity. FSM can be linked to actual obligations, is consistent across the services, and uses commercial standards in its development, which provides the stability and credibility needed to defend program funding requirements in AFCS.

The inclusion of the "A" factor to represent "acceptable operating condition" is not currently valid. At this time, there is no dataset which can be used to underpin target Q-Rating percentages or to identify acceptable operating conditions for specific Air Force facilities.

At A=100%, the FY 2008 accumulated deferred sustainment based on Q-Ratings is \$17.9 billion as noted above. Although a backlog of \$17.9 billion obviously appears significant, this considerably large requirement adds little value to AFCS decision-making process. From our experience, AFCS will immediately question such a large backlog if used to defend our budget shortfalls. Variable "A" factors would need to be developed to make the proposed deferred maintenance concept feasible.

Strategically, the use of annual deferred sustainment maintenance based on FSM has already proven to be successful in defending our budgets through AFCS. In FY 2007, the annual deferred sustainment maintenance based on FSM was at a reasonable level of \$385.0 million.



MILITARY EQUIPMENT DEFERRED MAINTENANCE

For Fiscal Year Ended September 30, 2008

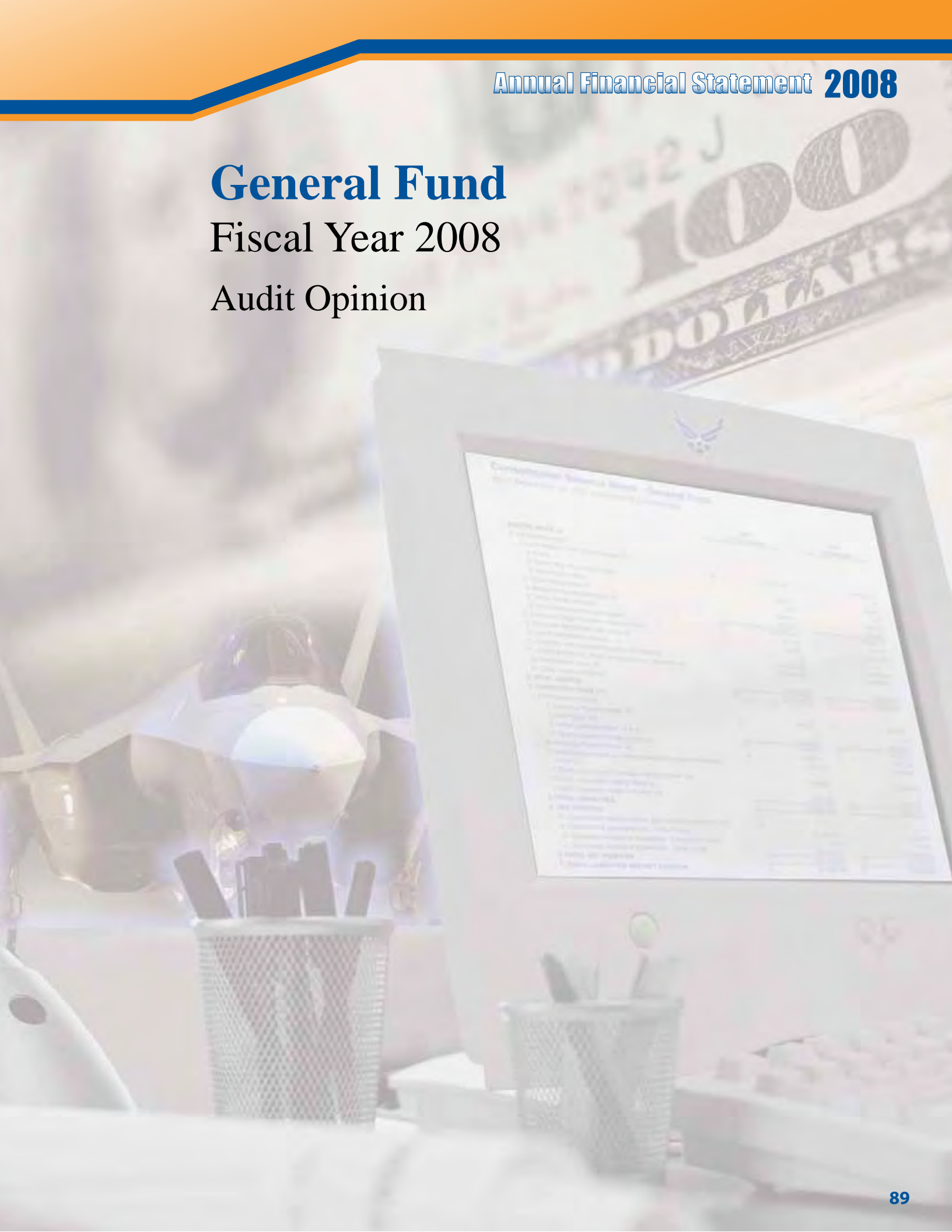
(Amounts in millions)

Major Categories	
1. Aircraft	\$ 257
2. Automotive Equipment	0
3. Combat Vehicles	0
4. Construction Equipment	0
5. Electronics and Communications Systems	72
6. Missiles	18
7. Ships	0
8. Ordnance Weapons and Munitions	0
9. General Purpose Equipment	0
10. All Other Items Not Identified to Above Categories	71
Total	\$ 1,118

The figures presented are projected deferred maintenance amounts for FY 2008 as reported in the FY 2010 Program Budget Review OP-30 budget exhibits. FY 2008 Global War on Terror Supplemental actual was not available.

The figures include Active Air Force, Air National Guard and Air Force Reserve.

General Fund
Fiscal Year 2008
Audit Opinion





INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
ARLINGTON, VIRGINIA 22202-4704

November 8, 2008

MEMORANDUM FOR ASSISTANT SECRETARY OF THE AIR FORCE
(FINANCIAL MANAGEMENT AND COMPTROLLER)

SUBJECT: Independent Auditor's Report on the Air Force General Fund FY 2008 and FY 2007
Basic Financial Statements (Report No. D-2009-016)

The Chief Financial Officers Act of 1990, as amended, requires the Department of Defense Inspector General to audit the accompanying Air Force General Fund Consolidated Balance Sheets as of September 30, 2008 and 2007, and the Consolidated Statement of Net Cost, the Consolidated Statement of Changes in Net Position, and the Combined Statement of Budgetary Resources for the fiscal years then ended. The financial statements are the responsibility of Air Force management. The Air Force is also responsible for implementing effective internal control and for complying with laws and regulations.

We are unable to express an opinion on the Air Force General Fund FY 2008 and FY 2007 Basic Financial Statements because of limitations on the scope of our work. Thus, the financial statements may be unreliable. In addition to our disclaimer of opinion on the financial statements, we are including the required Report on Internal Control and Compliance with Laws and Regulations. The Report on Internal Control and Compliance with Laws and Regulations is an integral part of our disclaimer of opinion on the financial statements and should be considered in assessing the results of our work.

Disclaimer of Opinion on the Financial Statements

The Assistant Secretary of the Air Force (Financial Management and Comptroller) acknowledged to us that the Air Force General Fund FY 2008 and FY 2007 Financial Statements would not substantially conform to accounting principles generally accepted in the United States of America (GAAP), and that Air Force financial management and feeder systems were unable to adequately support material amounts on the financial statements as of September 30, 2008. Section 1008(d) of the FY 2002 National Defense Authorization Act limits the Department of Defense Inspector General to performing only those audit procedures required by generally accepted government auditing standards that are consistent with the representations made by management. Accordingly, we did not perform auditing procedures required by U.S. Government auditing standards and Office of Management and Budget (OMB) Bulletin 07-04, "Audit Requirements for Federal Financial Statements," as amended,¹ to determine whether

¹ OMB Memorandum M-08-24, Technical Amendments to OMB Bulletin No. 07-04, "Audit Requirements for Federal Financial Statements," August 25, 2008

material amounts on the financial statements were fairly presented. Prior audits have identified, and Air Force has also acknowledged, the long-standing material internal control weaknesses identified in the Summary of Internal Control. These pervasive material weaknesses affect the reliability of certain information contained in the annual financial statement—much of which is taken from the same data sources as the basic financial statements.² Therefore, we are unable to express, and we do not express, an opinion on the basic financial statements. Additionally, the purpose of the audit was not to express an opinion on Management’s Discussion and Analysis, Required Supplementary Stewardship Information, Required Supplementary Information, and Other Accompanying Information presented with the basic financial statements. Accordingly, we express no opinion on that information.

Summary of Internal Control

In planning our work, we considered Air Force internal control over financial reporting and compliance with applicable laws and regulations. We did this to determine our procedures for auditing the financial statements and to comply with OMB guidance, but our purpose was not to express an opinion on internal control. Accordingly, we do not express an opinion on internal control over financial reporting and compliance with applicable laws and regulations. However, previously identified significant deficiencies, all of which are material, continued to exist in the following areas:

- **Financial Management Systems**
- **Operating Materials and Supplies**
- **General Property, Plant, and Equipment**
- **Government-Furnished Material and Contractor-Acquired Material**
- **Environmental Liabilities**
- **Statement of Net Cost**
- **Intragovernmental Eliminations**
- **Other Accounting Entries**
- **Reconciliation of Net Cost of Operations to Budget**

² The annual financial statement includes the basic financial statements, Management’s Discussion and Analysis, Required Supplementary Stewardship Information, Required Supplementary Information, and Other Accompanying Information.



We identified the following additional material weakness in FY 2008:

- **Fund Balance with Treasury Reconciliation**

A material weakness is a significant deficiency, or a combination of significant deficiencies, resulting in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected.³

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or a combination of control deficiencies, adversely affecting the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with GAAP. Significant deficiencies result in more than a remote likelihood that a misstatement of an entity's financial statements that is more than inconsequential will not be prevented or detected. The following is a list of previously identified significant deficiencies:

- **Reimbursable Programs**
- **Accounts Receivable Financial Reporting**
- **Accounts Payable Financial Reporting**

Internal control work that we conducted as part of our prior audits would not necessarily disclose all significant deficiencies. The Attachment offers additional details on these significant deficiencies, some of which we consider to be material internal control weaknesses.

The Air Force reported the above weaknesses in its 2008 Statement of Assurance, except for the material weaknesses involving the Statement of Net Cost and the Reconciliation of Net Cost of Operations to Budget and the significant deficiency involving reimbursable programs.

Summary of Compliance with Laws and Regulations

We limited our work to determine compliance with selected provisions of applicable laws and regulations related to financial reporting because management acknowledged that instances of noncompliance identified in prior audits continued to exist. The Assistant Secretary of the Air Force (Financial Management and Comptroller) acknowledged to us that Air Force financial management systems do not substantially comply with Federal financial management system requirements, GAAP, and the U.S. Government Standard General Ledger at the transaction level. Therefore, we did not determine whether Air Force complied with all applicable laws and regulations related to financial reporting. Providing an opinion on compliance with certain provisions of laws and regulations was not an objective of our audit and, accordingly, we do not

³ The term "remote" is defined as when the chance of a future event or events occurring is slight. Therefore, the likelihood of an event is "more than remote" when it is at least reasonably possible.

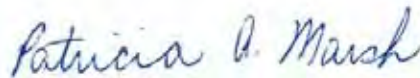
express such an opinion. See the Attachment for additional details on compliance with laws and regulations.

Management's Responsibilities

Management is responsible for:

- preparing the financial statements in conformity with GAAP;
- establishing, maintaining, and assessing internal control to provide reasonable assurance that the broad control objectives of the Federal Managers' Financial Integrity Act are met; and
- complying with applicable laws and regulations.

We provided a draft of this report to the Assistant Secretary of the Air Force (Financial Management and Comptroller), who provided technical comments, which have been incorporated as appropriate. Air Force officials expressed their continuing commitment to address the problems this report outlines.



Patricia A. Marsh, CPA
Assistant Inspector General
Defense Business Operations

Attachment:
As stated



Report on Internal Control and Compliance with Laws and Regulations

Internal Control

Management is responsible for implementing and maintaining effective internal control and for providing reasonable assurance that accounting data are accumulated, recorded, and reported properly; that the requirements of applicable laws and regulations are met; and that assets are safeguarded against misappropriation and abuse. Our purpose was not to, and we do not, express an opinion on internal control over financial reporting. However, we have identified the following material weaknesses and significant deficiencies that could adversely affect Air Force financial reporting.

Previously Identified Material Weaknesses. Management acknowledged that previously identified significant deficiencies, some of which are material, continued to exist in the following areas.

Financial Management Systems. Statement of Federal Financial Accounting Concepts No.1, "Objectives of Federal Financial Reporting," requires that financial management system controls be adequate to ensure that transactions are executed in accordance with budgetary and financial laws and other requirements, are consistent with the purposes authorized, and are recorded in accordance with Federal accounting standards. This statement also requires that financial management system controls ensure the proper safeguarding of assets to deter fraud, waste, and abuse, and provide adequate support for performance measurement information. The Assistant Secretary of the Air Force (Financial Management and Comptroller) acknowledged that many Air Force financial management systems do not substantially comply with Federal financial management system requirements. The design of Air Force financial management and feeder systems does not allow them to collect and record financial information based on a full-accrual accounting basis. Air Force financial reporting will be largely based on budgetary transactions and nonfinancial feeder systems until management updates these systems to collect and report financial information in compliance with GAAP.

Operating Materials and Supplies. The Air Force is required by Statement of Federal Financial Accounting Standards No.3, "Accounting for Inventory and Related Property," to use historical cost to value its Operating Materials and Supplies inventory. This statement also requires that an expense be recorded for Operating Materials and Supplies when the user consumes such items. The Air Force has acknowledged that significant amounts of Operating Materials and Supplies are valued using standard prices, and it does not always use the consumption method to recognize the related expense. Accordingly, management is not certain that the Operating Materials and Supplies balances reported in its basic financial statements are accurate.

General Property, Plant, and Equipment. The Air Force is required by Statement of Federal Financial Accounting Standards No.6, "Accounting for Property, Plant, and Equipment,"

to record General Property, Plant, and Equipment using acquisition cost, capitalized improvement costs, and depreciation expense. However, the Air Force has acknowledged that despite its implementation of a new system to improve its controls over recording real property, construction-in-progress, and related expenses; its controls need additional improvement to ensure that it does not materially misstate its financial reporting for General Property, Plant, and Equipment.

Government-Furnished and Contractor-Acquired Material. Statement of Federal Financial Accounting Standards No. 11, "Amendments to Accounting for Property, Plant, and Equipment," requires that the Government report on its balance sheet property and equipment in the possession of a contractor for use in accomplishing a contract. Government property should be accounted for based on the nature of the item, regardless of who has possession. The Air Force has acknowledged that its balance does not include the cost of all Government-furnished material in the hands of contractors where such value exceeds the capitalization threshold. As a result, Air Force does not reliably report the value of its property and material in the possession of contractors.

Environmental Liabilities. The Air Force is not currently able to support its environmental clean-up cost estimates as recorded in the Air Force Real Property Agency management information system. This system provides unsupported cost information for reporting in the annual financial statements.

Statement of Net Cost. Statement of Federal Financial Accounting Concepts No. 2, "Entity and Display," requires that the Statement of Net Cost present gross and net cost information for major organizations and programs and data related to their outputs and outcomes. The Air Force acknowledged that it accumulates the amounts reported in its Statement of Net Cost by major appropriation groups funded by Congress and not by major organizations and programs, as required. In addition, the Air Force does not accumulate cost information in accordance with GAAP. It presents the amounts for the General Fund based on budgetary obligations, disbursements, and collections, with adjustments made for only major items of known accruals and imputed expenses. Thus, the Statement of Net Cost may not report all actual costs or may report costs not actually incurred.

Intragovernmental Eliminations. Air Force accountants cannot always identify intragovernmental trading partners when recording transactions. Thus, the Air Force cannot properly eliminate all transactions among its internal organizational elements. In addition, the Air Force cannot reconcile intragovernmental accounts receivable, accounts payable, and revenues for transactions between its DoD and other Federal trading partners. This may prevent the Air Force from properly eliminating all of its intragovernmental transactions.

Other Accounting Entries. The Air Force acknowledged that it continues to enter material amounts of accounting adjustments without adequate detail transaction support. Additionally, there are material transactions that the Air Force has not properly recorded in the accounting records underlying the basic financial statements or the disclosed notes to the basic financial statements. The lack of adequate supporting documentation for material adjustments prevents an audit of the related financial statement amounts.



Reconciliation of Net Cost of Operations to Budget. Statement of Federal Financial Accounting Standards No.7, "Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting," states that the Reconciliation of Net Costs of Operations to Budget (in the footnotes to the basic financial statements) should reconcile resources obligated during the accounting period to the net cost of operations for that period. However, as stated in preceding paragraphs, the amounts presented in the Consolidated Statement of Net Costs and assets and liabilities reported in the balance sheet may be inaccurate. Therefore, Air Force does not reconcile budgetary amounts to actual proprietary expenses and assets and liabilities.

Material Weakness Identified During FY 2008. As a result of our financial-related work during FY 2008, we identified a significant deficiency that is material.

Fund Balance with Treasury Reconciliation. During an evaluation of internal controls, the Air Force discovered and confirmed deficiencies in the reconciliation of Fund Balance with Treasury between Air Force accounting records and the corresponding balances reported by Treasury. The Air Force does not have assurance that it can reconcile its reported balance of Fund Balance with Treasury to the balance the Treasury maintains because it currently does not receive transaction-level data from other DoD Components processing collection and disbursement data on its behalf.

Previously Identified Significant Deficiencies

Reimbursable Programs. Statement of Federal Financial Accounting Concepts No. 1, "Objectives of Federal Financial Reporting," requires the Air Force to track the cost of performing work reimbursed by other Government entities or by nonfederal customers. It defines costs as a measure of resources (personnel, material, and equipment) used to accomplish the work. The Air Force has acknowledged that its reimbursable programs may not recover all billable costs incurred in the fulfillment of reimbursable orders. Specifically, the Air Force is not always able to identify logistical, contractual, or labor costs incurred in support of reimbursable orders and, accordingly, such costs are not properly billed to the customer.

Accounts Receivable Financial Reporting. The Air Force cannot assure its Accounts Receivable financial statement line item because of weaknesses in the intragovernmental trading partner eliminations, Foreign Military Sales, and supporting documentation. These deficiencies result in the inability to properly reconcile and support the validity of Accounts Receivable.

Accounts Payable Financial Reporting. The Air Force cannot assure the amount of Accounts Payable reported in the basic financial statements because of financial system internal control weaknesses. Because of these weaknesses, the Air Force cannot support entries to Accounts Payable or reconcile the reported balance to transaction detail.

These financial management deficiencies may cause inaccurate management information. As a result, Air Force management decisions based in whole or in part on this information may be adversely affected. Financial information reported by DoD may also contain misstatements resulting from these deficiencies.

Compliance with Laws and Regulations

Management is responsible for compliance with existing laws and regulations related to financial reporting. We limited our work to determine compliance with selected provisions of the applicable laws and regulations because management acknowledged instances of noncompliance, and previously reported instances of noncompliance continue to exist. Therefore, we did not determine whether the Air Force was in compliance with selected provisions of all applicable laws and regulations related to financial reporting. Our objective was not to, and we do not, express an opinion on overall compliance with applicable laws and regulations.

Federal Financial Management Improvement Act of 1996. The Federal Financial Management Improvement Act of 1996 requires DoD to establish and maintain financial management systems that comply substantially with Federal financial management systems requirements, applicable Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level. The Federal Financial Management Improvement Act of 1996 also requires it to have a remediation plan for its noncompliant systems. For FY 2008, the Air Force did not fully comply with the Federal Financial Management Improvement Act of 1996. The Air Force acknowledged that many of its critical financial management and feeder systems did not substantially comply with Federal financial management systems requirements, Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level as of September 30, 2008. The Air Force has developed and published its Financial Improvement Plan as part of the DoD Financial Improvement and Audit Readiness Plan.

Antideficiency Act. Section 1341, title 31, United States Code (31 U.S.C. 1341) limits the Air Force and its agents to making or authorizing only expenditures or obligations that do not exceed the available appropriations or funds. Additionally, the Air Force or its agents may not contract or obligate for the payment of money until Congress makes an appropriation available for that contract or obligation unless otherwise authorized by law. According to 31 U.S.C. 1351, if an officer or employee of an executive agency violates the Antideficiency Act (ADA), the head of the agency must report immediately to the President and Congress all relevant facts and a statement of actions taken. During FY 2008, Air Force reported one case of violation of the ADA. Therefore, Air Force did not comply with 31 U.S.C. 1341.

DoD internal guidance limits the time from identification to reporting of ADA violations to 12 months. Our review of Air Force ADA investigations of potential violations shows that the Air Force did not process ADA violation cases within 12 months.

Audit Disclosures

The Assistant Secretary of the Air Force (Financial Management and Comptroller) acknowledged to us on March 6, 2008, and November 8, 2008, that the Air Force General Fund financial management and feeder systems cannot provide adequate evidence supporting various material amounts on the financial statements, and previously identified material weaknesses continue to exist. Therefore, we did not perform detailed testing related to material weaknesses. In addition,



we did not perform audit work related to the following selected provisions of laws and regulations: Federal Credit Reform Act of 1990, Pay and Allowance System for Civilian Employees, Prompt Payment Act, and the Provisions Governing Claims of the United States Government (including provisions of the Debt Collection Improvement Act of 1996).

This report does not include recommendations to correct the material internal control weaknesses and instances of noncompliance with laws and regulations, because previous audit reports contained recommendations for corrective actions or because audit projects currently in progress will include appropriate recommendations.

Working Capital Fund Principal Statements

Fiscal Year 2008

The FY 2008 Department of the Air Force Working Capital Fund Principal Statements and related notes are presented in the format prescribed by the Department of Defense Financial Management Regulation 7000.14-R, Volume 6B. The statements and related notes summarize financial information for individual activity groups and activities within the Working Capital Fund for the fiscal year ending September 30, 2008, and are presented on a comparative basis with information previously reported for the fiscal year ending September 30, 2007.

The following statements comprise the Department of the Air Force Working Capital Fund Principal Statements:

Consolidated Balance Sheet

The Consolidated Balance Sheet presents as of September 30, 2008 and 2007 those resources owned or managed by the Air Force which are available to provide future economic benefits (assets); amounts owed by the Air Force that will require payments from those resources or future resources (liabilities); and residual amounts retained by the Air Force, comprising the difference (net position).

Consolidated Statement of Net Cost

The Consolidated Statement of Net Cost presents the net cost of the Air Force's operations for the years ended September 30, 2008 and 2007. The Air Force's net cost of operations includes the gross costs incurred by the Air Force less any exchange revenue earned from Air Force activities.

Consolidated Statement of Changes in Net Position

The Consolidated Statement of Changes in Net Position presents the change in the Air Force's net position resulting from the net cost of Air Force's operations, budgetary financing sources other than exchange revenues, and other financing sources for the years ended September 30, 2008 and 2007.

Combined Statement of Budgetary Resources

The Combined Statement of Budgetary Resources presents the budgetary resources available to the Air Force during FY 2008 and 2007, the status of these resources at September 30, 2008 and 2007, and the outlay of budgetary resources for the years ended September 30, 2008 and 2007.

The Principal Statements and related notes have been prepared to report financial position pursuant to the requirements of the Chief Financial Officers Act of 1990, the Government Management Reform Act of 1994, and the Office of Management and Budget's Circular A-136, "Financial Reporting Requirements."



Consolidated Balance Sheet - Working Capital Fund

As of September 30, 2008 and 2007 (\$ in thousands)

	<u>2008 Consolidated</u>	<u>2007 Consolidated</u>
1. ASSETS (Note 2)		
A. Intragovernmental:		
1. Fund Balance with Treasury (Note 3)	\$ 959,598	\$ 1,287,399
2. Investments (Note 4)	0	0
3. Accounts Receivable (Note 5)	786,751	330,378
4. Other Assets (Note 6)	618	1,248
5. Total Intragovernmental Assets	<u>\$ 1,746,967</u>	<u>\$ 1,619,025</u>
B. Cash and Other Monetary Assets (Note 7)	0	0
C. Accounts Receivable, Net (Note 5)	117,894	117,808
D. Loans Receivable (Note 8)	0	0
E. Inventory and Related Property, Net (Note 9)	33,676,873	34,517,432
F. General Property, Plant and Equipment, Net (Note 10)	1,164,386	1,091,070
G. Investments (Note 4)	0	0
H. Other Assets (Note 6)	388,677	319,462
2. TOTAL ASSETS	<u><u>\$ 37,094,797</u></u>	<u><u>\$ 37,664,797</u></u>
3. STEWARDSHIP PROPERTY, PLANT & EQUIPMENT (Note 10)		
4. LIABILITIES (Note 11)		
A. Intragovernmental:		
1. Accounts Payable (Note 12)	\$ 94,776	\$ 117,965
2. Debt (Note 13)	0	0
3. Other Liabilities (Note 15 & 16)	86,302	135,036
4. Total Intragovernmental Liabilities	<u>\$ 181,078</u>	<u>\$ 253,001</u>
B. Accounts Payable (Note 12)	817,558	946,756
C. Military Retirement and Other Federal Employment Benefits (Note 17)	217,337	228,900
D. Environmental and Disposal Liabilities (Note 14)	0	0
E. Loan Guarantee Liability (Note 8)	0	0
F. Other Liabilities (Note 15 & Note 16)	624,331	714,711
5. TOTAL LIABILITIES	<u><u>\$ 1,840,304</u></u>	<u><u>\$ 2,143,368</u></u>
6. COMMITMENTS AND CONTINGENCIES (NOTE 16)		
7. NET POSITION		
A. Unexpended Appropriations - Earmarked Funds (Note 23)	0	0
B. Unexpended Appropriations - Other Funds	1,248	4,558
C. Cumulative Results of Operations - Earmarked Funds	0	0
D. Cumulative Results of Operations - Other Funds	35,253,245	35,516,871
8. TOTAL NET POSITION	<u><u>\$ 35,254,493</u></u>	<u><u>\$ 35,521,429</u></u>
9. TOTAL LIABILITIES AND NET POSITION	<u><u>\$ 37,094,797</u></u>	<u><u>\$ 37,664,797</u></u>

Consolidated Statement of Net Cost - Working Capital Fund

As of September 30, 2008 and 2007 (\$ in thousands)

	<u>2008 Consolidated</u>	<u>2007 Consolidated</u>
1. Program Costs		
A. Gross Costs	\$ 10,494,182	\$ 10,735,131
B. (Less: Earned Revenue)	-10,784,910	-10,431,762
C. Net Program Costs	\$ -290,728	\$ 303,369
2. Cost Not Assigned to Programs	0	0
3. (Less: Earned Revenue Not Attributable to Programs)	0	0
4. Net Cost of Operations	<u>\$ -290,728</u>	<u>\$ 303,369</u>



Consolidated Statement of Changes in Net Position - Working Capital Fund

As of September 30, 2008 and 2007 (\$ in thousands)

	2008 Earmarked Funds	2008 All Other Funds	2008 Eliminations
CUMULATIVE RESULTS OF OPERATIONS			
1. Beginning Balances	\$ 0	\$ 35,516,871	\$ 0
2. Prior Period Adjustments			
A. Changes in accounting principles (+/-)	0	0	0
B. Corrections of errors (+/-)	0	0	0
3. Beginning balances, as adjusted	<u>\$ 0</u>	<u>\$ 35,516,871</u>	<u>\$ 0</u>
4. Budgetary Financing Sources:			
A. Other adjustments (rescissions, etc.)	0	0	0
B. Appropriations used	0	69,073	0
C. Nonexchange revenue	0	0	0
D. Donations and forfeitures of cash and cash equivalents	0	0	0
E. Transfers-in/out without reimbursement (+/-)	0	-88,000	0
F. Other budgetary financing sources	0	0	0
5. Other Financing Sources			
A. Donations and forfeitures of property	0	0	0
B. Transfers-in/out without reimbursement (+/-)	0	-47,477	0
C. Imputed financing from costs absorbed by others	0	144,150	0
D. Other (+/-)	0	-632,100	0
6. Total Financing Sources	<u>\$ 0</u>	<u>\$ -554,354</u>	<u>\$ 0</u>
7. Net Cost of Operations (+/-)	0	-290,728	0
8. Net Change	<u>\$ 0</u>	<u>\$ -263,626</u>	<u>\$ 0</u>
9. Cumulative Results of Operations	<u>\$ 0</u>	<u>\$ 35,253,245</u>	<u>\$ 0</u>
UNEXPENDED APPROPRIATIONS			
10. Beginning Balances	\$ 0	\$ 4,558	\$ 0
11. Prior Period Adjustments:			
A. Changes in accounting principles	0	0	0
B. Corrections of errors	0	0	0
12. Beginning balances, as adjusted	<u>\$ 0</u>	<u>\$ 4,558</u>	<u>\$ 0</u>
13. Budgetary Financing Sources:			
A. Appropriations received	0	66,458	0
B. Appropriations transferred-in/out	0	0	0
C. Other adjustments (rescissions, etc)	0	-695	0
D. Appropriations used	0	-69,073	0
14. Total Budgetary Financing Sources	0	-3,310	0
15. Unexpended Appropriations	0	1,248	0
16. Net Position	<u><u>\$ 0</u></u>	<u><u>\$ 35,254,493</u></u>	<u><u>\$ 0</u></u>

Annual Financial Statement **2008**

Working Capital Fund

Principal Statements

2008 Consolidated	2007 Earmarked Funds	2007 All Other Funds	2007 Eliminations	2007 Consolidated
\$ 35,516,871	\$ 0	\$ 35,992,114	\$ 0	\$ 35,992,114
0	0	0	0	0
0	0	0	0	0
<u>\$ 35,516,871</u>	<u>\$ 0</u>	<u>\$ 35,992,114</u>	<u>\$ 0</u>	<u>\$ 35,992,114</u>
0	0	0	0	0
69,073	0	39,324	0	39,324
0	0	0	0	0
0	0	0	0	0
-88,000	0	-382,000	0	-382,000
0	0	0	0	0
0	0	0	0	0
-47,477	0	2,192	0	2,192
144,150	0	168,610	0	168,610
-632,100	0	0	0	0
<u>\$ -554,354</u>	<u>\$ 0</u>	<u>\$ -171,874</u>	<u>\$ 0</u>	<u>\$ -171,874</u>
<u>-290,728</u>	<u>0</u>	<u>303,369</u>	<u>0</u>	<u>303,369</u>
<u>\$ -263,626</u>	<u>\$ 0</u>	<u>\$ -475,243</u>	<u>\$ 0</u>	<u>\$ -475,243</u>
<u>\$ 35,253,245</u>	<u>\$ 0</u>	<u>\$ 35,516,871</u>	<u>\$ 0</u>	<u>\$ 35,516,871</u>
\$ 4,558	\$ 0	\$ 0	\$ 0	\$ 0
0	0	0	0	0
0	0	0	0	0
<u>\$ 4,558</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>
66,458	0	44,054	0	44,054
0	0	0	0	0
-695	0	-172	0	-172
-69,073	0	-39,324	0	-39,324
-3,310	0	4,558	0	4,558
1,248	0	4,558	0	4,558
<u><u>\$ 35,254,493</u></u>	<u><u>\$ 0</u></u>	<u><u>\$ 35,521,429</u></u>	<u><u>\$ 0</u></u>	<u><u>\$ 35,521,429</u></u>

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



Combined Statement of Budgetary Resources - Working Capital Fund

As of September 30, 2008 and 2007 (\$ in thousands)

	2008 Combined	2007 Combined
BUDGETARY FINANCING ACCOUNTS		
BUDGETARY RESOURCES:		
1. Unobligated balance, brought forward, October 1	\$ 1,073,782	\$ 925,137
2. Recoveries of prior year unpaid obligations	0	23,358
3. Budget authority		
A. Appropriation	66,458	44,054
B. Borrowing authority	0	0
C. Contract authority	6,633,730	9,804,575
D. Spending authority from offsetting collections		
1. Earned		
a. Collected	11,677,265	14,106,630
b. Change in receivables from Federal sources	407,049	-373,583
2. Change in unfilled customer orders		
a. Advance received	-77,781	-40,165
b. Without advance from Federal sources	-241,364	230,560
3. Anticipated for rest of year, without advances	0	0
4. Previously unavailable	0	0
5. Expenditure transfers from trust funds	0	0
E. Subtotal	\$ 18,465,357	\$ 23,772,071
4. Nonexpenditure transfers, net, anticipated and actual	-88,000	-382,000
5. Temporarily not available pursuant to Public Law	0	0
6. Permanently not available	-8,139,473	-9,162,481
7. Total Budgetary Resources	\$ 11,311,666	\$ 15,176,085
STATUS OF BUDGETARY RESOURCES:		
8. Obligations incurred:		
A. Direct	\$ 0	\$ 0
B. Reimbursable	10,968,071	14,102,303
C. Subtotal	\$ 10,968,071	\$ 14,102,303
9. Unobligated balance:		
A. Apportioned	343,595	1,073,782
B. Exempt from apportionment	0	0
C. Subtotal	\$ 343,595	\$ 1,073,782
10. Unobligated balance not available	0	0
11. Total status of budgetary resources	\$ 11,311,666	\$ 15,176,085
CHANGE IN OBLIGATED BALANCE:		
12. Obligated balance, net		
A. Unpaid obligations, brought forward, October 1	8,883,865	8,603,843
B. Less: Uncollected customer payments from Federal sources, brought forward, October 1	\$ -3,844,887	\$ -3,987,910
C. Total unpaid obligated balance	\$ 5,038,978	\$ 4,615,933
13. Obligations incurred net (+/-)	\$ 10,968,071	\$ 14,102,303
14. Less: Gross outlays	-11,905,048	-13,798,923
15. Obligated balance transferred, net		
A. Actual transfers, unpaid obligations (+/-)	0	0
B. Actual transfers, uncollected customer payments from Federal sources (+/-)	0	0
C. Total Unpaid obligated balance transferred, net	\$ 0	\$ 0
16. Less: Recoveries of prior year unpaid obligations, actual	\$ 0	\$ -23,358
17. Change in uncollected customer payments from Federal sources (+/-)	-165,685	143,023
18. Obligated balance, net, end of period		
A. Unpaid obligations	7,946,888	8,883,865
B. Less: Uncollected customer payments (+/-) from Federal sources (-)	-4,010,572	-3,844,887
C. Total, unpaid obligated balance, net, end of period	3,936,316	5,038,978
NET OUTLAYS		
19. Net Outlays:		
A. Gross outlays	\$ 11,905,048	\$ 13,798,923
B. Less: Offsetting collections	-11,599,484	-14,066,465
C. Less: Distributed Offsetting receipts	0	0
D. Total Net Outlays	\$ 305,564	\$ -267,542

Working Capital Fund

Fiscal Year 2008

Notes to the Principal Statements

Notes to the financial statements communicate information essential for fair presentation of the financial statements that is not displayed on the face of the financial statements.



Note 1. Significant Accounting Policies

1.A. Basis of Presentation

These financial statements have been prepared to report the financial position and results of operations of the Air Force Working Capital Fund (AFWCF), as required by the Chief Financial Officers Act of 1990, expanded by the Government Management Reform Act of 1994, and other appropriate legislation. The financial statements have been prepared from the books and records of the AFWCF in accordance with the Department of Defense (DoD), Financial Management Regulation (FMR), the Office of Management and Budget (OMB) Circular A-136, Financial Reporting Requirements, and to the extent possible generally accepted accounting principles (GAAP). The accompanying financial statements account for all resources for which the AFWCF is responsible unless otherwise noted.

The AFWCF is unable to fully implement all elements of GAAP and the OMB Circular A-136, due to limitations of its financial and nonfinancial management processes and systems that feed into the financial statements. The AFWCF derives its reported values and information for major asset and liability categories largely from nonfinancial systems, such as inventory and logistic systems. These systems were designed to support reporting requirements for maintaining accountability over assets and reporting the status of federal appropriations rather than preparing financial statements in accordance with GAAP. The AFWCF continues to implement process and system improvements addressing these limitations.

The AFWCF currently has eight auditor identified financial statement material weaknesses: (1) financial and nonfinancial feeder systems do not contain an adequate audit trail for the proprietary and budgetary accounts, (2) AFWCF may have material amounts of account adjustments that are not adequately supported, (3) AFWCF cannot accurately identify all intragovernmental transactions by customer, which is required for eliminations when preparing consolidated financial statements, (4) the value of the AFWCF government furnished and contractor acquired materiel and equipment may not be accurately reported, (5) AFWCF General Property, Plant, and Equipment (PP&E) may not be accurately valued, (6) operating materials and supplies (OM&S) are not reflected at historical cost, (7) cost of goods sold and work in progress are not recorded in accordance with the Statement of Federal Financial Accounting Standards (SFFAS) No. 3, "Accounting for Inventory and Related Property", and (8) supply management systems do not provide sufficient audit trails to confirm and value the in transit inventory reported as part of inventory held for sale on the Consolidated Balance Sheet.

1.B. Mission of the Reporting Entity

The United States Air Force was created on September 18, 1947, by the "National Security Act of 1947." The "National Security Act Amendments of 1949" established the DoD and made the Air Force a department within DoD. The overall mission of the United States Air is to fly, fight and win...in air, space and cyberspace. Our priorities are: (1) reinvigorate the Air Force nuclear enterprise, (2) partner with Joint and Coalition team to win today's fight, (3) develop and care for Airmen and their families (4) modernize our aging air and space inventories, and (5) achieve acquisition excellence.

The stock and industrial revolving fund accounts were created by the "National Security Act of 1947," as amended in 1949 and codified in United States Code 10 Section 2208. The revolving funds were established as a means to more effectively control the cost of work performed by DoD. The DoD began operating under the revolving fund concept July 1, 1951.

Since FY 2006, AFWCF operations consist of two major activity groups: Supply Management Activity Group (SMAG) and Depot Maintenance Activity Group (DMAG). All AFWCF SMAG and DMAG activities establish rates based on full cost recovery. If an operating loss or gain is incurred, the activity will make the appropriate adjustment in following year's prices to recoup the loss or return the gain to their customers.

The SMAG manages and finances the majority of Air Force supply requirements. Exceptions include an item financed with a procurement appropriation or when financing by other means has been deemed to be more economical and efficient. A stock fund operates as a revolving fund replenishing inventories with funds received from sales to customers.

There are four active business activities in SMAG: (1) Material Support Division (MSD), (2) General Support Division (GSD), (3) Medical-Dental Division, and (4) Air Force Academy Division.

A brief description is provided below for the four active SMAG business activities.

- MSD manages over 106 thousand depot level repair and unique consumable items to support Air Force weapon systems.
- GSD manages over 1.5 million consumable supply items, which support field and depot maintenance of aircraft, ground and airborne communication, and electronic systems.
- Medical-Dental manages over 7 thousand different items, which are used to support medical and dental supply and equipment requirements.
- Air Force Academy manages the procurement of uniforms and uniform accessories for sale to cadets.

The DMAG repairs weapon systems and spare parts that ensure readiness in peacetime and provide sustainment to combat forces in wartime. In peacetime, the Air Force enhances readiness by efficiently and economically repairing, overhauling, and modifying aircraft, engines, missiles, depot level reparable, and software to meet customer demands. Depots have unique skills and equipment required to support and overhaul both new, complex components as well as aging weapon systems. An extremely important facet of the depots is that during wartime or contingencies, the Air Force can surge repair operations and realign capacity to support the war fighters' immediate needs. This is achieved by employing the unique strengths of organic (in-house) and contracted (contract) repair resources.

1.C. Appropriations and Funds

The AFWCF receives its appropriations and funds as general and working capital (revolving) funds. The AFWCF uses these appropriations and funds to execute its missions and subsequently report on resource usage.

Working Capital Funds (WCF) received funding to establish an initial corpus through an appropriation or a transfer of resources from existing appropriations or funds. The corpus finances operations and transactions that flow through the fund. The WCF resources the goods and services sold to customers on a reimbursable basis and maintains the corpus. Reimbursable receipts fund future operations and generally are available in their entirety for use without further congressional action. At various times, Congress provides additional appropriations to supplement WCF as an infusion of cash when revenues are inadequate to cover costs within the corpus.

1.D. Basis of Accounting

For FY 2008, the AFWCF's financial management systems are unable to meet all of the requirements for full accrual accounting. Many of the AFWCF's financial and nonfinancial feeder systems and processes were designed and implemented prior to the issuance of GAAP for federal agencies. These systems were not designed to collect and record financial information on the full accrual accounting basis as required by GAAP. Most of the AFWCF's (financial and nonfinancial) legacy systems were designed to record information on a budgetary basis.



The DoD has undertaken efforts to determine the actions required to bring its financial and nonfinancial feeder systems and processes into compliance with GAAP. One such action is the current revision of its accounting systems to record transactions based on the U.S. Standard General Ledger (USSGL). Until all of AFWCF's financial and nonfinancial feeder systems and processes are updated to collect and report financial information as required by GAAP, the AFWCF's financial data will be derived from budgetary transactions (obligations, disbursements and collections), transactions from nonfinancial feeder systems, and accruals made of major items such as payroll expenses, accounts payable, and environmental liabilities.

1.E. Revenues and Other Financing Sources

Organic Depot Maintenance recognizes revenue according to the percentage-of-completion method. Contract Depot Maintenance recognizes revenue based on the number of units produced multiplied by the unit sales price which is recognized upon completion of the repair. Due to the closure of Contract Depot Maintenance in FY 2008, it is not cost-effective to implement system modifications to support the percentage-of-completion method. Supply Management recognizes revenue based on flying hours executed and the sale of inventory items.

1.F. Recognition of Expenses

For financial reporting purposes, the DoD policy requires the recognition of operating expenses in the period incurred. However, because the AFWCF's financial and nonfinancial feeder systems were not designed to collect and record financial information on the full accrual accounting basis, accruals are made for major items such as payroll expenses, accounts payable, and unbilled revenue. In the case of OM&S, the consumption method is used.

1.G. Accounting for Intragovernmental Activities

Preparation of reliable financial statements requires the elimination of transactions occurring among entities within DoD or between two or more federal agencies. However, the AFWCF cannot accurately eliminate intragovernmental transactions by customer because the AFWCF's systems do not track at the transaction level. Generally, seller entities within the DoD provide summary seller-side balances for revenue, accounts receivable, and unearned revenue to the buyer-side internal DoD accounting offices. In most cases, the buyer-side records are adjusted to agree with DoD seller-side balances. Intra-DoD intragovernmental balances are then eliminated. The volume of intragovernmental transactions is so large that after-the-fact reconciliation cannot be accomplished effectively with existing or foreseeable resources. The DoD is developing long-term system improvements to ensure accurate intragovernmental information, to include sufficient upfront edits and controls eliminating the need for after-the-fact reconciliations.

The U.S. Treasury Financial Management Service is responsible for eliminating transactions between DoD and other federal agencies. The Treasury Financial Manual Part 2 – Chapter 4700, "Agency Reporting Requirements for the Financial Report of the United States Government," and the U.S. Treasury's "Federal Intragovernmental Transactions Accounting Policy Guide" provide guidance for reporting and reconciling intragovernmental balances. While the AFWCF is unable to fully reconcile intragovernmental transactions with all federal partners, the AFWCF is able to reconcile balances pertaining to Federal Employees' Compensation Act transactions with the Department of Labor and benefit program transactions with the Office of Personnel Management.

The DoD's proportionate share of public debt and related expenses of the Federal Government is not included. The Federal Government does not apportion debt and its related costs to federal agencies. The DoD's financial statements, therefore, do not report any portion of the public debt or interest thereon, nor do the statements report the source of public financing whether from issuance of debt or tax revenues.

Financing for the construction of DoD facilities is obtained through appropriations. To the extent this financing ultimately may have been obtained through the issuance of public debt, interest costs have not been capitalized since the U.S. Treasury does not allocate such interest costs to the benefiting agencies.

1.H. Transactions with Foreign Governments and International Organizations

Each year, the AFWCF sells defense articles and services to foreign governments and international organizations under the provisions of the “Arms Export Control Act of 1976.” Under the provisions of the Act, DoD has authority to sell defense articles and services to foreign countries and international organizations generally at no profit or loss to the U.S. Government. Payment in U.S. dollars is required in advance.

1.I. Funds with the U.S. Treasury

The AFWCF’s monetary resources are maintained in U.S. Treasury accounts. The disbursing offices of Defense Finance and Accounting Service (DFAS), the Military Departments, the U.S. Army Corps of Engineers (USACE), and the Department of State’s financial service centers process the majority of AFWCF’s cash collections, disbursements, and adjustments worldwide. Each disbursing station prepares monthly reports to the U.S. Treasury on check issues, electronic fund transfers, interagency transfers, and deposits.

In addition, DFAS sites and the USACE Finance Center submit reports to the U.S. Treasury by appropriation on interagency transfers, collections received, and disbursements issued. The U.S. Treasury records these transactions to the applicable Fund Balance with Treasury (FBWT) account. The AFWCF’s recorded balance in the FBWT accounts and U.S. Treasury’s FBWT accounts must balance monthly.

1.J. Foreign Currency

Not Applicable

1.K. Accounts Receivable

As presented in the Balance Sheet, accounts receivable includes three categories: accounts, claims, and refunds receivable from other federal entities or from the public. Allowances for uncollectible accounts due from the public are based upon analysis of collection experience by fund type. The DoD does not recognize an allowance for estimated uncollectible amounts from other federal agencies. Claims against other federal agencies are to be resolved between the agencies in accordance with dispute resolution procedures defined in the Intragovernmental Business Rules published in the Treasury Financial Manual.

1.L. Direct Loans and Loan Guarantees

Not Applicable

1.M. Inventories and Related Property

The AFWCF values approximately 99% of its resale inventory using the moving average cost method. The AFWCF reports the remaining 1% of resale inventories at an approximation of historical cost using latest acquisition cost adjusted for holding gains and losses. The latest acquisition cost method is used because legacy inventory systems were designed for materiel management rather than accounting. Although these systems provide visibility and accountability over inventory items, they do not maintain historical cost data necessary to comply with SFFAS No. 3, “Accounting for Inventory and



Related Property.” Additionally, these systems cannot produce financial transactions using the USSGL, as required by the Federal Financial Management Improvement Act of 1996 (P.L. 104-208). By utilizing new systems development processes, the AFWCF is continuing to transition the balance of the inventories to the moving average cost method. However, since the on-hand balances which were transitioned were not, for the most part, baselined to auditable historical cost, the reported values remain noncompliant with SFFAS No. 3 and GAAP.

The AFWCF manages only military or government specific materiel under normal conditions. Materiel is a unique term that relates to military force management, and includes all items (including ships, tanks, self-propelled weapons, aircraft, etc., and related spares, repair parts, and support equipment, but excluding real property, installations, and utilities) necessary to equip, operate, maintain, and support military activities without distinction as to its application for administrative or combat purposes. Items commonly used in and available from the commercial sector are not managed in AFWCF materiel management activities. Operational cycles are irregular and military risks associated with stock-out positions have no commercial parallel. The AFWCF holds materiel based on military need and support for contingencies. The DoD does not attempt to account separately for “inventory held for sale” and “inventory held in reserve for future sale” based on SFFAS No. 3 definitions, unless otherwise noted.

Related property includes OM&S which is valued at standard purchase price. The AFWCF uses the consumption method of accounting for OM&S.

The AFWCF recognizes condemned materiel as “Excess, Obsolete, and Unserviceable.” The cost of disposal is greater than the potential scrap value; therefore, the net value of condemned materiel is zero. Potentially redistributed materiel, presented in previous years as “Excess, Obsolete, and Unserviceable,” is included in the “Held for Use” or “Held for Repair” categories according to its condition.

Inventory available and purchased for resale includes consumable spare and repair parts and repairable items owned and managed by the AFWCF. This inventory is retained to support military or national contingencies. Inventory held for repair is damaged inventory that requires repair to make suitable for sale. Often, it is more economical to repair these inventory items rather than to procure these items. The AFWCF often relies on weapon systems and machinery that are no longer in production. As a result, the AFWCF supports a process that encourages the repair and rebuilding of certain items. This repair cycle is essential in maintaining a ready, mobile, and armed military force. Work in process balances include costs related to the production or servicing of items, including direct material, direct labor, applied overhead, and other direct costs. Work in process also includes the value of finished products or completed services that are yet to be placed in service and transferred to an asset account. Work in process includes munitions in production and depot maintenance work with its associated labor, applied overhead, and supplies used in the delivery of maintenance services.

1.N. Investments in U.S. Treasury Securities

Not Applicable

1.O. General Property, Plant and Equipment

The DoD’s General Property, Plant & Equipment (General PP&E) capitalization threshold is \$100 thousand except for real property which is \$20 thousand. The AFWCF has not implemented the threshold for real property but expects to be fully compliant by FY 2010. AFWCF is currently using the capitalization threshold of \$100 thousand for all General PP&E.

General PP&E assets are capitalized at historical acquisition cost when an asset has a useful life of two or more years, and when the acquisition cost equals or exceeds the DoD capitalization threshold. The DoD also requires the capitalization of

improvements to existing GPP&E assets if the improvements equal or exceed DoD capitalization threshold and extend the useful life or increase the size, efficiency, or capacity of the asset. The DoD depreciates all GPP&E, other than land, on a straight-line basis.

The WCF capitalizes all General PP&E used in the performance of their mission. These capitalized assets are categorized as General PP&E, whether or not it meets the definition of any other General PP&E categories.

When it is in the best interest of the government, AFWCF provides government property to contractors to complete contract work. The AFWCF either owns or leases such property, or it is purchased directly by the contractor for the government based on contract terms. When the value of contractor-procured General PP&E exceeds the DoD capitalization threshold, Federal accounting standards require that it be reported on the AFWCF's Balance Sheet.

The DoD is developing new policies and a contractor reporting process for Government Furnished Equipment that will provide appropriate General PP&E information for future financial statement reporting purposes. Accordingly, AFWCF reports only government property in the possession of contractors that is maintained in AFWCF's property systems. The DoD has issued new property accountability and reporting requirements that require AFWCF to maintain, in their property systems, information on all property furnished to contractors. This action and other DoD proposed actions are structured to capture and report the information necessary for compliance with federal accounting standards.

1.P. Advances and Prepayments

When advances are permitted by law, legislative action, or presidential authorization, the DoD's policy is to record advances and prepayments in accordance with GAAP. As such, payments made in advance of the receipt of goods and services should be reported as an asset on the Balance Sheet. The DoD's policy is to expense and/or properly classify assets when the related goods and services are received. The AFWCF has implemented this policy.

1.Q. Leases

Not Applicable

1.R. Other Assets

Other assets includes those assets, such as military and civil service employee pay advances, travel advances, and certain contract financing payments that are not reported elsewhere on AFWCF's Balance Sheet.

The AFWCF conducts business with commercial contractors under two primary types of contracts: fixed price and cost reimbursable. To alleviate the potential financial burden on the contractor that long-term contracts can cause, AFWCF may provide financing payments. Contract financing payments are defined in the Federal Acquisition Regulations, Part 32, as authorized disbursements of monies to a contractor prior to acceptance of supplies or services by the Government. Contract financing payments clauses are incorporated in the contract terms and conditions and may include advance payments, performance-based payments, commercial advance and interim payments, progress payments based on cost, and interim payments under certain cost-reimbursement contracts.

Contract financing payments do not include invoice payments, payments for partial deliveries, lease and rental payments, or progress payments based on a percentage or stage of completion, which the Defense Federal Acquisition Regulation Supplement authorizes only for construction of real property, shipbuilding, and ship conversion, alteration, or repair. Progress payments for real property and ships are reported as Construction in Progress. It is DoD policy to record certain contract financing payments as Other Assets.



1.S. Contingencies and Other Liabilities

The SFFAS No. 5, “Accounting for Liabilities of the Federal Government,” as amended by SFFAS No. 12, “Recognition of Contingent Liabilities Arising from Litigation,” defines a contingency as an existing condition, situation or set of circumstances that involves an uncertainty as to possible gain or loss. The uncertainty will be resolved when one or more future events occur or fail to occur. The AFWCF recognizes contingent liabilities when past events or exchange transactions occur, a future loss is probable, and the loss amount can be reasonably estimated.

Financial statement reporting is limited to disclosure when conditions for liability recognition do not exist but there is at least a reasonable possibility of incurring a loss or additional losses. Examples of loss contingencies include the collectibility of receivables, pending or threatened litigation, and possible claims and assessments. The AFWCF’s risk of loss and resultant contingent liabilities arise from pending or threatened litigation or claims and assessments due to events such as aircraft, ship and vehicle accidents; medical malpractice; property or environmental damages; and contract disputes.

1.T. Accrued Leave

The AFWCF reports as a liability civilian earned leave, except sick leave, that has been accrued and not used as of the Balance Sheet date. Sick leave is expensed as taken. The liability reported at the end of the accounting period reflects the current pay rates.

1.U. Net Position

Net Position consists of unexpended appropriations and cumulative results of operations.

Unexpended Appropriations represent the amounts of authority that are unobligated and have not been rescinded or withdrawn. Unexpended appropriations also represent amounts obligated for which legal liabilities for payments have not been incurred.

Cumulative Results of Operations represent the net difference, since inception of an activity, between expenses and losses and financing sources (including appropriations, revenue and gains). Beginning with FY 1998, the cumulative results also include donations and transfers in and out of assets that were not reimbursed.

1.V. Treaties for Use of Foreign Bases

Not Applicable

1.W. Comparative Data

The AFWCF’s financial statements and notes are presented on a comparative basis.

1.X. Unexpended Obligations

The AFWCF obligates funds to provide goods and services for outstanding orders not yet delivered. Unless the title has passed, the financial statements do not reflect liability for payment for goods and services not yet delivered. Unexpended obligations includes both obligations for which goods and services have been delivered (title passed) and a liability recognized, and obligations for which no delivery has occurred and no liability recognized. The balance of unexpended obligations appears immediately before net outlays in the Statement of Budgetary Resources, and is referred to as “Total, unpaid obligated balances, net, end of period.”

1.Y. Undistributed Disbursements and Collections

Undistributed disbursements and collections represent the difference between disbursements and collections matched at the transaction level to a specific obligation, payable, or receivable in the activity field records as opposed to those reported by the U.S. Treasury. These amounts should agree with the undistributed amounts reported on the monthly accounting reports. Intransit payments are those payments that have been made, but have not been recorded in the fund holder's accounting records. These payments are applied to the entities' outstanding accounts payable balance. Intransit collections are those collections from other agencies or entities that have not been recorded in the accounting records. These collections are also applied to the entities' accounts receivable balance.

The DoD policy is to allocate supported undistributed disbursements and collections between federal and nonfederal categories based on the percentage of distributed federal and nonfederal accounts payable and accounts receivable. Unsupported undistributed disbursements are recorded in accounts payable. Unsupported undistributed collections are recorded in other liabilities.

1.Z. Significant Events

Not Applicable

Note 2. Nonentity Assets

As of September 30	2008	2007
(Amounts in thousands)		
1. Intragovernmental Assets		
A. Fund Balance with Treasury	\$ 0	\$ 0
B. Accounts Receivable	0	0
C. Total Intragovernmental Assets	\$ 0	\$ 0
2. Nonfederal Assets		
A. Cash and Other Monetary Assets	\$ 0	\$ 0
B. Accounts Receivable	0	0
C. Other Assets	0	0
D. Total Nonfederal Assets	\$ 0	\$ 0
3. Total Nonentity Assets	\$ 0	\$ 0
4. Total Entity Assets	37,094,797	37,664,797
5. Total Assets	\$ 37,094,797	\$ 37,664,797

Asset accounts are categorized as either entity or nonentity. Entity accounts consist of resources that are available for use in the operations of the entity. The AFWCF is authorized to decide how to use resources in entity accounts. The AFWCF may be legally obligated to use these resources to meet entity obligations.

Nonentity assets are assets for which the AFWCF maintains stewardship accountability and responsibility to report, but are not available for the AFWCF's operations.

The AFWCF has no Nonentity Assets.



Note 3. Fund Balance with Treasury

As of September 30	2008	2007
(Amounts in thousands)		
1. Fund Balances		
A. Appropriated Funds	\$ 0	\$ 0
B. Revolving Funds	959,598	1,287,399
C. Trust Funds	0	0
D. Special Funds	0	0
E. Other Fund Types	0	0
F. Total Fund Balances	\$ 959,598	\$ 1,287,399
2. Fund Balances Per Treasury Versus Agency		
A. Fund Balance per Treasury	\$ 1,384,148	\$ 1,705,484
B. Fund Balance per AFWCF	959,598	1,287,399
3. Reconciling Amount	\$ 424,550	\$ 418,085

The reconciling amount represents \$424.6 million for the United States Transportation Command (USTC), which is reported by the U.S. Treasury as part of the AFWCF. However, for the purposes of Audited Financial Statements (AFS), USTC is included with the Other Defense Organizations reporting which is separate from the AFWCF. Therefore, USTC funds are not included in the AFWCF AFS.

Status of Fund Balance with Treasury

As of September 30	2008	2007
(Amounts in thousands)		
1. Unobligated Balance		
A. Available	\$ 343,595	\$ 1,073,782
B. Unavailable	0	0
2. Obligated Balance not yet Disbursed	7,946,888	8,883,865
3. Nonbudgetary FBWT	0	0
4. NonFBWT Budgetary Accounts	-7,330,885	-8,670,248
5. Total	\$ 959,598	\$ 1,287,399

The Status of Fund Balance with Treasury (FBWT) reflects the budgetary resources to support the FBWT.

Unobligated Balance represents the cumulative amount of budgetary authority that has not been set aside to cover outstanding obligations. Unobligated Balance is classified as available or unavailable and is associated with appropriations expiring at fiscal year end that remain available only for obligation adjustments until the account is closed.

Obligated balance not yet disbursed represents funds that have been obligated for goods that have not been received, services that have not been performed, and goods and services that have been delivered/received but not yet paid.

Nonbudgetary FBWT includes entity and nonentity FBWT accounts which represent adjustments that do not have budgetary authority, such as unavailable receipt accounts or clearing accounts. AFWCF has no Nonbudgetary FBWT.

NonFBWT Budgetary Accounts represent adjustments to budgetary accounts that do not affect FBWT such as contract authority, accounts receivable, as well as the unfilled orders without advance from customers. This category reduces the Status of FBWT.

Unobligated balances are segregated to show available and unavailable amounts in the note schedule. Certain unobligated balances may be restricted to future use and are not apportioned for current use. There are no restrictions on the Unobligated Balance.

Note 4. Investments and Related Interest

The AFWCF has no Investments and Related Interest.

Note 5. Accounts Receivable

As of September 30	2008			2007
	Gross Amount Due	Allowance For Estimated Uncollectibles	Accounts Receivable, Net	Accounts Receivable, Net
(Amounts in thousands)				
1. Intragovernmental Receivables	\$ 786,751	N/A	\$ 786,751	\$ 330,378
2. Nonfederal Receivables (From the Public)	117,894	\$ 0	117,894	117,808
3. Total Accounts Receivable	<u>\$ 904,645</u>	<u>\$ 0</u>	<u>\$ 904,645</u>	<u>\$ 448,186</u>

Note 6. Other Assets

As of September 30	2008		2007	
(Amounts in thousands)				
1. Intragovernmental Other Assets				
A. Advances and Prepayments	\$	618	\$	1,248
B. Other Assets		0		0
C. Total Intragovernmental Other Assets	\$	618	\$	1,248
2. Nonfederal Other Assets				
A. Outstanding Contract Financing Payments	\$	148,718	\$	153,834
B. Advances and Prepayments		57,987		13,051
C. Other Assets (With the Public)		181,972		152,577
D. Total Nonfederal Other Assets	\$	388,677	\$	319,462
3. Total Other Assets	<u>\$</u>	<u>389,295</u>	<u>\$</u>	<u>320,710</u>

Contract terms and conditions for certain types of contract financing payments convey certain rights to the AFWCF that protect the contract work from state or local taxation, liens or attachment by the contractor's creditors, transfer of property, or disposition in bankruptcy; however, these rights should not be misconstrued to mean that ownership of the contractor's



work has transferred to the Government. The Government does not have the right to take the work, except as provided in contract clauses related to termination or acceptance, and the AFWCF is not obligated to make payment to the contractor until delivery and acceptance.

The Contract Financing Payments balance of \$148.7 million is comprised of \$126.7 million in contract financing payments and an additional \$22.0 million in estimated future payments that will be paid to the contractor upon future delivery and Government acceptance of a satisfactory product. (See additional discussion in Note 15, Other Liabilities).

The majority of the Nonfederal Other Assets – Other Assets (With the Public) balance is comprised of \$182.0 million for Supply Management Activity Group’s assets returned to vendors for which credit is pending.

Note 7. Cash and Other Monetary Assets

The AFWCF has no Cash and Other Monetary Assets.

Note 8. Direct Loan and Loan Guarantees

The AFWCF has no Direct Loan and/or Loan Guarantee Programs.

Note 9. Inventory and Related Property

As of September 30	2008	2007
(Amounts in thousands)		
1. Inventory, Net	\$ 33,483,296	\$ 34,273,552
2. Operating Materials & Supplies, Net	193,577	243,880
3. Stockpile Materials, Net	0	0
4. Total	\$ 33,676,873	\$ 34,517,432

Inventory, Net

As of September 30	2008			2007	Valuation Method
	Inventory, Gross Value	Revaluation Allowance	Inventory, Net	Inventory, Net	
(Amounts in thousands)					
1. Inventory, Categories					
A. Available and Purchased for Resale	\$ 23,066,474	\$ -10,479	\$ 23,055,995	\$ 23,861,178	LAC,MAC
B. Held for Repair	14,439,808	-4,145,848	10,293,960	10,199,635	LAC,MAC
C. Excess, Obsolete, and Unserviceable	472,249	-472,249	0	0	NRV
D. Raw Materials	0	0	0	0	MAC,SP,LAC
E. Work in Process	133,341	0	133,341	212,739	AC
F. Total	\$ 38,111,872	\$ -4,628,576	\$ 33,483,296	\$ 34,273,552	

Legend for Valuation Methods:

Adjusted LAC = Latest Acquisition Cost, adjusted for holding gains and losses

NRV = Net Realizable Value

SP = Standard Price

O = Other

AC = Actual Cost

MAC = Moving Average Cost

General Composition of Inventory

Inventory includes weapon system consumable and repairable parts, base supply items, and medical-dental supplies. Inventory is tangible personal property that is held for sale or held for repair for eventual sale, in the process of production for sale, or to be consumed in the production of goods for sale or in the provision of services for a fee.

Restrictions

There are no restrictions on the use, sale, or disposition of inventory except for War Reserve Materiel and nuclear related spare parts.

Definitions

Inventory Available and Purchased for Resale includes consumable and repairable parts owned and managed by AFWCF.

Inventory Held for Repair is damaged inventory that requires repair to make it suitable for sale. Many of the inventory items are more economical to repair than to procure. In addition, because AFWCF often relies on weapon systems and machinery no longer in production, AFWCF supports a process that encourages the repair and rebuilding of certain items. This repair cycle is essential to maintaining a ready, mobile, and armed military force.

Excess, Obsolete, and Unserviceable inventory consists of obsolete, excess to requirements, or items that cannot be economically repaired and are awaiting disposal.

Work in Process balances include costs related to the production or servicing of items, including direct material, direct labor, applied overhead, and other direct costs. Work in Process also includes the value of finished products or completed services pending the submission of bills to the customer.



Operating Materiel and Supplies, Net

As of September 30	2008			2007	Valuation Method
	OM&S Gross Value	Revaluation Allowance	OM&S, Net	OM&S, Net	
(Amounts in thousands)					
1. OM&S Categories					
A. Held for Use	\$ 193,577	\$ 0	\$ 193,577	\$ 243,880	SP, LAC, MAC
B. Held for Repair	0	0	0	0	SP, LAC, MAC
C. Excess, Obsolete, and Unserviceable	0	0	0	0	NRV
D. Total	\$ 193,577	\$ 0	\$ 193,577	\$ 243,880	

Legend for Valuation Methods:

Adjusted LAC = Latest Acquisition Cost, adjusted for holding gains and losses

SP = Standard Price

AC = Actual Cost

NRV = Net Realizable Value

O = Other

MAC = Moving Average Cost

General Composition of Operating Materiels and Supplies

Operating Materiel and Supplies (OM&S) includes consumable parts and supplies used to remanufacture spare parts and repair weapons systems.

Restrictions

There are no restrictions on the use, sale, or disposition of OM&S.

Definition

Held for Use includes consumable parts and supplies.

Stockpile Materiels, Net

The AFWCF has no Stockpile Materiels.

Note 10. General PP&E, Net

As of September 30	2008					2007
	Depreciation/ Amortization Method	Service Life	Acquisition Value	(Accumulated Depreciation/ Amortization)	Net Book Value	Prior FY Net Book Value
(Amounts in thousands)						
1. Major Asset Classes						
A. Land	N/A	N/A	\$ 0	N/A	\$ 0	\$ 0
B. Buildings, Structures, and Facilities	S/L	20 or 40	932,320	\$ -673,436	258,884	254,668
C. Leasehold Improvements	S/L	lease term	0	0	0	0
D. Software	S/L	2-5 or 10	1,097,939	-831,623	266,316	288,623
E. General Equipment	S/L	5 or 10	2,157,924	-1,573,174	584,750	496,554
F. Military Equipment	S/L	Various	0	0	0	0
G. Assets Under Capital Lease	S/L	lease term	0	0	0	0
H. Construction-in- Progress	N/A	N/A	54,436	N/A	54,436	51,225
I. Other			0	0	0	0
J. Total General PP&E			\$ 4,242,619	\$ -3,078,233	\$ 1,164,386	\$ 1,091,070

See Note 15 for additional information on Capital Leases

Legend for Valuation Methods:

S/L = Straight N/A = Not Applicable

AFWCF does not have any restrictions on the use or convertibility of General PP&E.

Assets Under Capital Lease

The AFWCF has no Assets Under Capital Lease.



Note 11. Liabilities Not Covered by Budgetary Resources

As of September 30	2008	2007
(Amounts in thousands)		
1. Intragovernmental Liabilities		
A. Accounts Payable	\$ 0	\$ 0
B. Debt	0	0
C. Other	0	0
D. Total Intragovernmental Liabilities	\$ 0	\$ 0
2. Nonfederal Liabilities		
A. Accounts Payable	\$ 0	\$ 0
B. Military Retirement and Other Federal Employment Benefits	217,337	228,900
C. Environmental Liabilities	0	0
D. Other Liabilities	28,376	28,376
E. Total Nonfederal Liabilities	\$ 245,713	\$ 257,276
3. Total Liabilities Not Covered by Budgetary Resources	\$ 245,713	\$ 257,276
4. Total Liabilities Covered by Budgetary Resources	1,594,591	1,886,092
5. Total Liabilities	\$ 1,840,304	\$ 2,143,368

Liabilities not covered by budgetary resources are liabilities for which Congressional action is needed before budgetary resources can be provided.

Military Retirement and Other Federal Employment Benefits not covered by budgetary resources are comprised of various employee actuarial liabilities not due and payable during the current fiscal year. These liabilities are primarily comprised of \$217.3 million for Federal Employee's Compensation Act. Refer to Note 17, Military Retirement and Other Federal Employment Benefits, for additional details and disclosures.

Nonfederal Other Liabilities includes \$28.4 million in foreign government deposits. These deposits represent foreign governments buy in to a Cooperative Logistics Supply Support Agreement (CLSSA). Foreign governments provide funds to buy their respective share of inventory that is owned and managed by the Air Force. This liability is established to offset an asset that belongs to another entity (foreign government). If the CLSSA is closed, they receive either a cash reimbursement or spare parts if approved by State Department. Historically foreign governments always request cash reimbursement versus spare parts. As a result deposits are classified as liabilities not covered by budgetary resources.

Note 12. Accounts Payable

As of September 30	2008			2007
	Accounts Payable	Interest, Penalties, and Administrative Fees	Total	Total
(Amounts in thousands)				
1. Intragovernmental Payables	\$ 94,776	N/A	\$ 94,776	\$ 117,965
2. Nonfederal Payables (to the Public)	817,558	0	817,558	946,756
3. Total	\$ 912,334	\$ 0	\$ 912,334	\$ 1,064,721

The AFWCF's systems do not track intragovernmental transactions by customer at the transaction level. Therefore, internal DoD buyer-side balances are adjusted to agree with internal seller-side balances for revenue, accounts receivable, and un-earned revenue. Accounts payable are adjusted by reclassifying amounts between federal and nonfederal accounts payable.

In FY 2007, the Department recognized accounts payable balances of the Mechanization of Contract Administration Services (MOCAS) system at gross value without reduction for partial, progress payments, and non-accounts payable records overstating accounts payable and expenses. The overstated balances for FY 2007 were undeterminable due to system limitations; therefore no corrections have been made. Balances at FY 2008 are properly reported net of non-account payable records, partial and progress payments of \$14.7 million.

Note 13. Debt

The AFWCF has no Debt.

Note 14. Environmental Liabilities and Disposal Liabilities

The AFWCF has no Environmental Liabilities and Disposal Liabilities.



Note 15. Other Liabilities

As of September 30	2008			2007
	Current Liability	Noncurrent Liability	Total	Total
(Amounts in thousands)				
1. Intragovernmental				
A. Advances from Others	\$ 74,062	\$ 0	\$ 74,062	\$ 124,243
B. Deposit Funds and Suspense Account Liabilities	0	0	0	0
C. Disbursing Officer Cash	0	0	0	0
D. Judgment Fund Liabilities	0	0	0	0
E. FECA Reimbursement to the Department of Labor	0	0	0	0
F. Custodial Liabilities	0	0	0	0
G. Employer Contribution and Payroll Taxes Payable	12,240	0	12,240	10,793
H. Other Liabilities	0	0	0	0
I. Total Intragovernmental Other Liabilities	\$ 86,302	\$ 0	\$ 86,302	\$ 135,036
2. Nonfederal				
A. Accrued Funded Payroll and Benefits	\$ 151,662	\$ 0	\$ 151,662	\$ 141,206
B. Advances from Others	24,926	0	24,926	26,115
C. Deferred Credits	0	0	0	0
D. Deposit Funds and Suspense Accounts	0	0	0	806
E. Temporary Early Retirement Authority	0	0	0	0
F. Nonenvironmental Disposal Liabilities	0	0	0	0
1. Military Equipment (Nonnuclear)	0	0	0	0
2. Excess/Obsolete Structures	0	0	0	0
3. Conventional Munitions Disposal	0	0	0	0
G. Accrued Unfunded Annual Leave	0	0	0	0
H. Capital Lease Liability	0	0	0	0
I. Contract Holdbacks	1,990	0	1,990	1,326
J. Employer Contribution and Payroll Taxes Payable	0	0	0	5,635
K. Contingent Liabilities	0	21,955	21,955	22,500
L. Other Liabilities	423,798	0	423,798	517,929
M. Total Nonfederal Other Liabilities	\$ 602,376	\$ 21,955	\$ 624,331	\$ 714,711
3. Total Other Liabilities	\$ 688,678	\$ 21,955	\$ 710,633	\$ 849,747

The majority of the Nonfederal Other Liabilities balance is comprised of \$378.3 million for Contract Depot Maintenance Activity Group's accrued material and labor liabilities.

Contingent liabilities balance includes \$22.0 million in estimated future contract financing payments that will be paid to the contractor upon delivery and Government acceptance. In accordance with contract terms, specific rights to the contractor's work vests with the Government when a specific type of contract financing payment is made. This action protects taxpayer funds in the event of contract nonperformance. These rights should not be misconstrued as the rights of ownership. The

AFWCF is under no obligation to pay the contractor for amounts greater than the amounts authorized in the contract until delivery and Government acceptance. Because it is probable that the contractor will complete its efforts and deliver a satisfactory product to the AFWCF and the amount of potential future payments is estimable; the AFWCF has recognized a contingent liability for estimated future payments, which are conditional pending delivery and Government acceptance.

Capital Lease Liability

The AFWCF has no Capital Lease Liability.

Note 16. Commitments and Contingencies

The AFWCF is a party in various administrative proceedings and legal actions, with claims including environmental damage claims, equal opportunity matters, and contractual bid protests. The AFWCF's Office of the General Counsel considers the possibility of the AFWCF sustaining any losses on these legal actions to be remote.

The AFWCF is a party in numerous individual contracts that contain clauses, such as price escalation, award fee payments, or dispute resolution, that may or may not result in a future outflow of expenditures. Currently, AFWCF does not have a process by which it captures or assesses these potential contingent liabilities; therefore no associated liabilities are recognized or disclosed.

Note 17. Military Retirement and Other Federal Employment Benefits

As of September 30	2008			2007	
	Liabilities	Assumed Interest Rate (%)	Less: Assets Available to Pay Benefits)	Unfunded Liabilities	Liabilities
(Amounts in thousands)					
1. Pension and Health Actuarial Benefits					
A. Military Retirement Pensions	\$ 0		\$ 0	\$ 0	\$ 0
B. Military Retirement Health Benefits	0		0	0	0
C. Military Medicare-Eligible Retiree Benefits	0		0	0	0
D. Total Pension and Health Actuarial Benefits	\$ 0		\$ 0	\$ 0	\$ 0
2. Other Actuarial Benefits					
A. FECA	217,337		\$ 0	217,337	228,900
B. Voluntary Separation Incentive Programs	0		0	0	0
C. DoD Education Benefits Fund	0		0	0	0
D. Total Other Actuarial Benefits	\$ 217,337		\$ 0	\$ 217,337	\$ 228,900
3. Other Federal Employment Benefits	0		0	0	0
4. Total Military Retirement and Other Federal Employment Benefits	\$ 217,337		\$ 0	\$ 217,337	\$ 228,900



Federal Employees Compensation Act (FECA)

The AFWCF actuarial liability for workers' compensation benefits is developed by the Department of Labor and is updated at the end of each fiscal year. The liability includes the estimated 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. The projected annual benefit payments are discounted to present value using the Office of Management and Budget's (OMB's) economic assumptions for 10-year Treasury notes and bonds. Cost of living adjustments (COLAs) and consumer price index medical (CPIM) factors are applied to the calculation of projected future benefits.

The liability for future workers' compensation (FWC) 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. Consistent with past practice, these projected annual benefits payments have been discounted to present value using the OMB's economic assumptions for 10-year Treasury notes and bonds. Interest rate assumptions utilized for discounting were as follows:

2008

4.368% in Year 1

4.770% in Year 2,

and thereafter

To provide more specifically for the effects of inflation on the liability for future workers' compensation benefits, wage inflation factors (COLAs) and medical inflation factors (CPIMs) were applied to the calculation of projected future benefits. The actual rates for these factors for the charge back year (CBY) 2008 are used to adjust the methodology's historical payments to current year constant dollars.

The compensation COLAs and CPIMs used in the projections for various CBY were as follows:

CBY	COLA	CPIM
2008	3.03%	4.71%
2009	3.87%	4.01%
2010	2.73%	3.86%
2011	2.20%	3.87%
2012	2.23%	3.93%
2013+	2.30%	3.93%

The model's resulting projections were analyzed to insure that the estimates were reliable. The analysis was based on four tests: (1) a sensitivity analysis of the model to economic assumptions, (2) a comparison of the percentage change in the liability amount by agency to the percentage change in the actual incremental payments, (3) a comparison of the incremental paid losses per case (a measure of case-severity) in CBY 2008 to the average pattern observed during the most current three charge back years, and (4) a comparison of the estimated liability per case in the 2008 projection to the average pattern for the projections of the most recent three years.

Note 18. General Disclosures Related to the Statement of Net Cost Intragovernmental Costs and Exchange Revenue

As of September 30	2008	2007
(Amounts in thousands)		
1. Intragovernmental Costs	\$ 4,292,130	\$ 3,956,343
2. Public Costs	6,202,052	6,778,788
3. Total costs	\$ 10,494,182	\$ 10,735,131
4. Intragovernmental Earned Revenue	\$ -10,176,218	\$ -9,697,266
5. Public Earned Revenue	-608,692	-734,496
6. Total Earned Revenue	\$ -10,784,910	\$ -10,431,762
7. Net Cost of Operations	\$ -290,728	\$ 303,369

Intragovernmental costs and revenue are related to transactions made between two reporting entities within the Federal Government.

Public costs and revenues are exchange transactions made between the reporting entity and a nonfederal entity.

The AFWCF's systems do not track intergovernmental transactions by customer at the transaction level. Therefore, internal DoD buyer-side balances are adjusted to agree with internal seller-side balances for revenue. Expenses are adjusted by reclassifying amounts between federal and nonfederal expenses.

The Statement of Net Cost (SNC) represents the net cost of programs and organizations of the Federal Government supported by appropriations or other means. The intent of SNC is to provide gross and net cost information related to the amount of output or outcome for a given program or organization administered by a responsible reporting entity. The Department's current processes and systems do not capture and report accumulated costs for major programs based upon the performance measures as required by the Government Performance and Results Act. The Department is in the process of reviewing available data and developing a cost reporting methodology as required by the Statement of Federal Financial Accounting Standards (SFFAS) No. 4, "Managerial Cost Accounting Concepts and Standards for Federal Government."

The AFWCF records transactions on an accrual basis. The AFWCF may not have all the actual costs and revenues input into the system in time for reporting. Accrual estimates based upon budget information, historical data, and current data not yet input are made as required by generally accepted accounting principles. These estimates reverse as actual costs or revenues are recorded.

Note 19. Disclosures Related to the Statement of Changes in Net Position

Statement of Changes in Net Position, Other Financing Sources, Other line is comprised of a \$632.1 million write-off of in-transit inventory.

Note 20. Disclosures Related to the Statement of Budgetary Resources

As of September 30	2008	2007
(Amounts in thousands)		
1. Net Amount of Budgetary Resources Obligated for Undelivered Orders at the End of the Period	\$ 6,596,132	\$ 7,196,353
2. Available Borrowing and Contract Authority at the End of the Period	0	0

All of AFWCF obligations are reimbursable obligations in apportionment category B.

The Statement of Budgetary Resources (SBR) includes intraentity transactions because the statements are presented as combined.



Note 21. Reconciliation of Net Cost of Operations to Budget

As of September 30	2008	2007
(Amounts in thousands)		
Resources Used to Finance Activities:		
Budgetary Resources Obligated:		
1. Obligations incurred	\$ 10,968,071	\$ 14,102,303
2. Less: Spending authority from offsetting collections and recoveries (-)	-11,765,169	-13,946,800
3. Obligations net of offsetting collections and recoveries	\$ -797,098	\$ 155,503
4. Less: Offsetting receipts (-)	0	0
5. Net obligations	\$ -797,098	\$ 155,503
Other Resources:		
6. Donations and forfeitures of property	0	0
7. Transfers in/out without reimbursement (+/-)	-47,477	2,192
8. Imputed financing from costs absorbed by others	144,150	168,610
9. Other (+/-)	-632,100	0
10. Net other resources used to finance activities	\$ -535,427	\$ 70,802
11. Total resources used to finance activities	\$ -1,332,525	\$ 326,305
Resources Used to Finance Items not Part of the Net Cost of Operations:		
12. Change in budgetary resources obligated for goods, services and benefits ordered but not yet provided:		
A. Undelivered Orders (-)	\$ 600,220	\$ -44,589
B. Unfilled Customer Orders	-319,145	190,395
13. Resources that fund expenses recognized in prior Periods (-)	-11,609	0
14. Budgetary offsetting collections and receipts that do not affect Net Cost of Operations	0	0
15. Resources that finance the acquisition of assets (-)	-4,945,969	-5,376,572
16. Other resources or adjustments to net obligated resources that do not affect Net Cost of Options:		
A. Less: Trust or Special Fund Receipts Related to exchange in the Entity's Budget (-)	0	0
B. Other (+/-)	679,577	-2,192
17. Total resources used to finance items not part of the Net Cost of Operations	\$ -3,996,926	\$ -5,232,958
18. Total resources used to finance the Net Cost of Operations	\$ -5,329,451	\$ -4,906,653
Components of the Net Cost of Operations that will not Require or Generate Resources in the Current Period:		
Components Requiring or Generating Resources in Future Period:		
19. Increase in annual leave liability	\$ 0	\$ 0
20. Increase in environmental and disposal liability	0	0
21. Upward/Downward reestimates of credit subsidy expense (+/-)	0	0
22. Increase in exchange revenue receivable from the public (-)	0	6
23. Other (+/-)	46	30,241
24. Total components of Net Cost of Operations that will Require or Generate Resources in future periods	\$ 46	\$ 30,241
Components not Requiring or Generating Resources:		
25. Depreciation and amortization	132,208	142,937
26. Revaluation of assets or liabilities (+/-)	844,543	1,893,247
27. Other (+/-)		
A. Trust Fund Exchange Revenue	0	0
B. Cost of Goods Sold	5,888,617	5,331,747
C. Operating Material and Supplies Used	0	0
D. Other	-1,826,691	-2,188,150
28. Total Components of Net Cost of Operations that will not Require or Generate Resources	\$ 5,038,677	\$ 5,179,781
29. Total Components of Net Cost of Operations that will not Require or Generate Resources in the current period	\$ 5,038,723	\$ 5,210,022
30. Net Cost of Operations	\$ -290,728	\$ 303,369

Due to the AFWCF's financial system limitations, budgetary data is not in agreement with proprietary expenses and assets capitalized. The difference between budgetary and proprietary data is a previously identified deficiency.

Resources That Finance the Acquisition of Assets is adjusted in order to align the note schedule with the amount reported on the Statement of Net Cost. This adjustment is \$256.2 million (absolute value).

The following schedule lines are presented as combined instead of consolidated due to intraagency budgetary transactions not being eliminated:

- Obligations Incurred
- Less: Spending Authority from Offsetting Collections and Recoveries
- Obligations Net of Offsetting Collections and Recoveries
- Less: Offsetting Receipts
- Net Obligations
- Undelivered Orders
- Unfilled Customer Orders

Resources Used to Finance Activities, Other line is comprised of a \$632.1 million write-off of in-transit inventory.

The majority of Other resources or adjustments to net obligated resources that do not affect Net Cost of Operations is comprised of a \$632.1 million write-off of in-transit inventory.

Components Requiring or Generating Resources in Future Periods, Other line is comprised of \$46.2 thousand in Federal Employees Compensation Act (FECA).

The majority of Other Components not Requiring or Generating Resources is comprised of (\$5.1) billion of DMAG completed production projects and of \$3.3 billion Supply Material Activity Group material to replace condemned and consumable parts required for depot production.

Note 22. Disclosures Related to Incidental Custodial Collections

The AFWCF has no Disclosures Related to Incidental Custodial Collections.

Note 23. Earmarked Funds

The AFWCF has no Earmarked Funds.

Note 24. Other Disclosures

The AFWCF has no Other Disclosures.

Note 25. Restatements

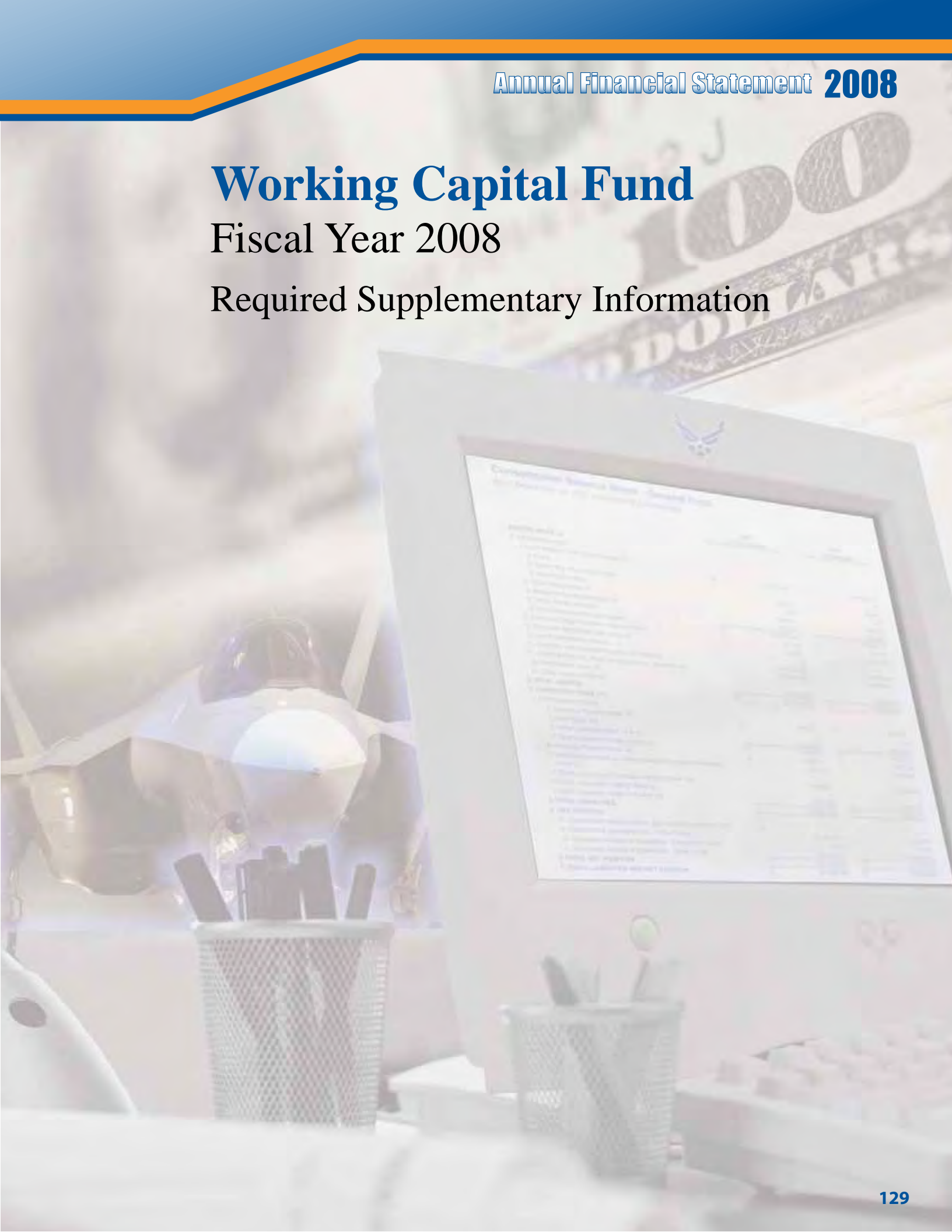
The AFWCF has no Restatements of prior period adjustments for material errors.



Working Capital Fund

Fiscal Year 2008

Required Supplementary Information





UNITED STATES AIR FORCE

Working Capital Fund

Required Supplementary Information

Statement of Disaggregated Budgetary Resources - Working Capital Fund

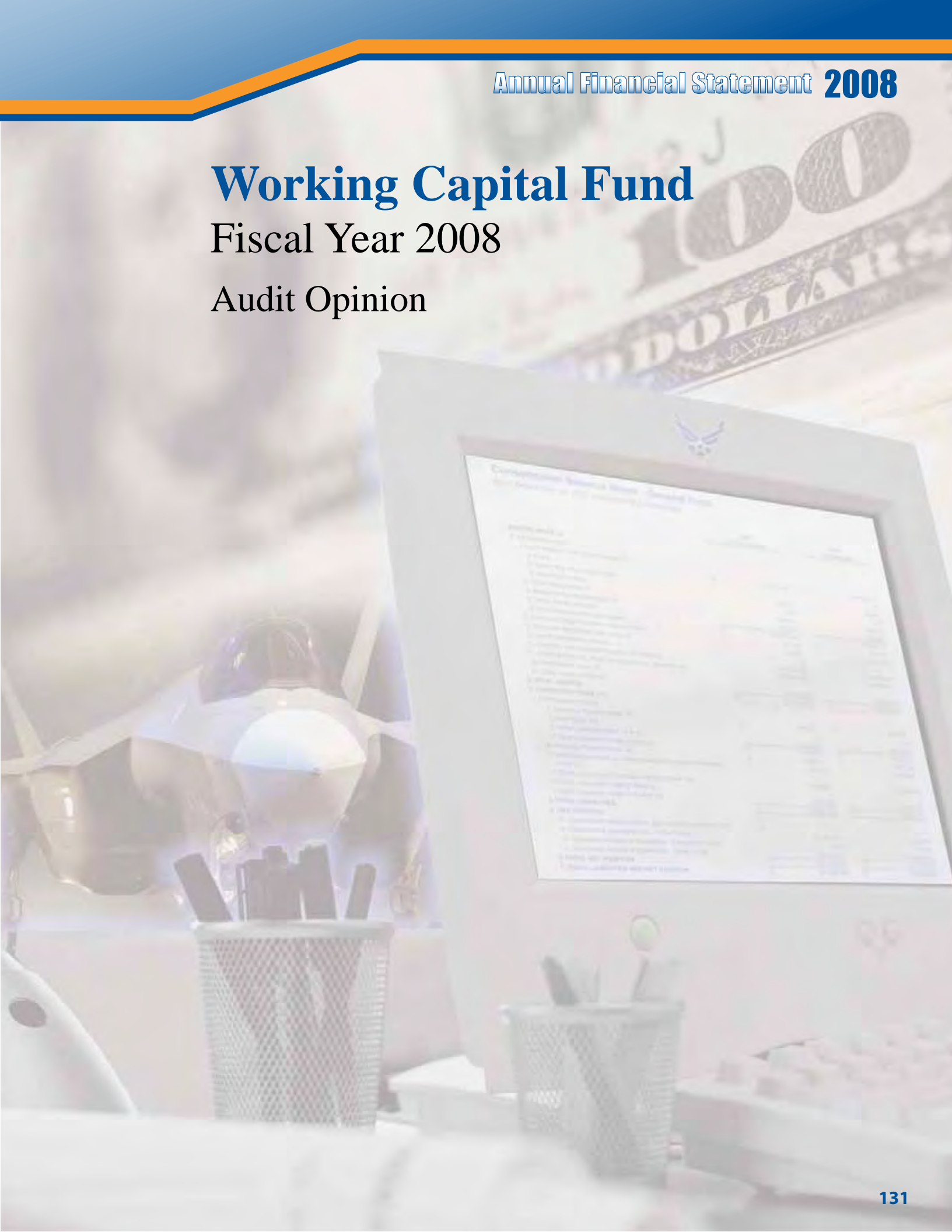
As of September 30, 2008 and 2007 (\$ in thousands)

	<u>Working Capital Fund</u>	<u>2008 Combined</u>	<u>2007 Combined</u>
BUDGETARY FINANCING ACCOUNTS			
BUDGETARY RESOURCES:			
1. Unobligated balance, brought forward, October 1	\$ 1,073,782	\$ 1,073,782	\$ 925,137
2. Recoveries of prior year unpaid obligations	0	0	23,358
3. Budget authority			
A. Appropriation	66,458	66,458	44,054
B. Borrowing authority	0	0	0
C. Contract authority	6,633,730	6,633,730	9,804,575
D. Spending authority from offsetting collections			
1. Earned			
a. Collected	11,677,264	11,677,265	14,106,630
b. Change in receivables from Federal sources	407,049	407,049	-373,583
2. Change in unfilled customer orders			
a. Advance received	-77,781	-77,781	-40,165
b. Without advance from Federal sources	-241,364	-241,364	230,560
3. Anticipated for rest of year, without advances	0	0	0
4. Previously unavailable	0	0	0
5. Expenditure transfers from trust funds	0	0	0
E. Subtotal	\$ 18,465,356	\$ 18,465,357	\$ 23,772,071
4. Nonexpenditure transfers, net, anticipated and actual	-88,000	-88,000	-382,000
5. Temporarily not available pursuant to Public Law	0	0	0
6. Permanently not available	-8,139,473	-8,139,473	-9,162,481
7. Total Budgetary Resources	\$ 11,311,665	\$ 11,311,666	\$ 15,176,085
STATUS OF BUDGETARY RESOURCES:			
8. Obligations incurred			
A. Direct	\$ 0	\$ 0	\$ 0
B. Reimbursable	10,968,070	10,968,071	14,102,303
C. Subtotal	\$ 10,968,070	\$ 10,968,071	\$ 14,102,303
9. Unobligated balance			
A. Apportioned	343,595	343,595	1,073,782
B. Exempt from apportionment	0	0	0
C. Subtotal	\$ 343,595	\$ 343,595	\$ 1,073,782
10. Unobligated balance not available	0	0	0
11. Total status of budgetary resources	\$ 11,311,665	\$ 11,311,666	\$ 15,176,085
CHANGE IN OBLIGATED BALANCE:			
12. Obligated balance, net			
A. Unpaid obligations, brought forward, October 1	\$ 8,883,865	\$ 8,883,865	\$ 8,603,843
B. Less: Uncollected customer payments from Federal sources, brought forward, October 1	-3,844,887	-3,844,887	-3,987,910
C. Total unpaid obligated balance	\$ 5,038,978	\$ 5,038,978	\$ 4,615,933
13. Obligations incurred net (+/-)	\$ 10,968,070	\$ 10,968,071	\$ 14,102,303
14. Less: Gross outlays	-11,905,048	-11,905,048	-13,798,923
15. Obligated balance transferred, net			
A. Actual transfers, unpaid obligations (+/-)	0	0	0
B. Actual transfers, uncollected customer payments from Federal sources (+/-)	0	0	0
C. Total Unpaid obligated balance transferred, net	\$ 0	\$ 0	\$ 0
16. Less: Recoveries of prior year unpaid obligations, actual	\$ 0	\$ 0	\$ -23,358
17. Change in uncollected customer payments from Federal sources (+/-)	-165,685	-165,685	143,023
18. Obligated balance, net, end of period			
A. Unpaid obligations	7,946,887	7,946,888	8,883,865
B. Less: Uncollected customer payments (+/-) from Federal sources	-4,010,572	-4,010,572	-3,844,887
C. Total, unpaid obligated balance, net, end of period	3,936,315	3,936,316	5,038,978
NET OUTLAYS:			
19. Net Outlays			
A. Gross outlays	\$ 11,905,048	\$ 11,905,048	\$ 13,798,923
B. Less: Offsetting collections	-11,599,484	-11,599,484	-14,066,465
C. Less: Distributed Offsetting receipts	0	0	0
D. Net Outlays	\$ 305,564	\$ 305,564	\$ -267,542

Working Capital Fund

Fiscal Year 2008

Audit Opinion





INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
ARLINGTON, VIRGINIA 22202-4704

November 8, 2008

MEMORANDUM FOR ASSISTANT SECRETARY OF THE AIR FORCE
(FINANCIAL MANAGEMENT AND COMPTROLLER)

SUBJECT: Independent Auditor's Report on the Air Force Working Capital Fund FY 2008 and
FY 2007 Basic Financial Statements (Report No. D-2009-017)

The Chief Financial Officers Act of 1990, as amended, requires the Department of Defense Inspector General to audit the accompanying Air Force Working Capital Fund Consolidated Balance Sheets as of September 30, 2008 and 2007, and the Consolidated Statement of Net Cost, the Consolidated Statement of Changes in Net Position, and the Combined Statement of Budgetary Resources for the fiscal years then ended. The financial statements are the responsibility of Air Force management. The Air Force is also responsible for implementing effective internal control and for complying with laws and regulations.

We are unable to express an opinion on the Air Force Working Capital Fund FY 2008 and FY 2007 Basic Financial Statements because of limitations on the scope of our work. Thus, the financial statements may be unreliable. In addition to our disclaimer of opinion on the financial statements, we are including the required Report on Internal Control and Compliance with Laws and Regulations. The Report on Internal Control and Compliance with Laws and Regulations is an integral part of our disclaimer of opinion on the financial statements and should be considered in assessing the results of our work.

Disclaimer of Opinion on the Financial Statements

The Assistant Secretary of the Air Force (Financial Management and Comptroller) acknowledged to us that the Air Force Working Capital Fund FY 2008 and FY 2007 Basic Financial Statements would not substantially conform to accounting principles generally accepted in the United States of America (GAAP) and that Air Force financial management and feeder systems were unable to adequately support material amounts in the financial statements as of September 30, 2008. Section 1008(d) of the FY 2002 National Defense Authorization Act limits the Department of Defense Inspector General to performing only those audit procedures required by generally accepted government auditing standards that are consistent with the representations made by management. Accordingly, we did not perform auditing procedures required by U.S. Government auditing standards and Office of Management and Budget (OMB) Bulletin 07-04, "Audit Requirements for Federal Financial Statements," as amended,¹ to determine

¹ OMB Memorandum M-08-24, Technical Amendments to OMB Bulletin No. 07-04, "Audit Requirements for Federal Financial Statements," August 25, 2008.

whether material amounts on the financial statements were fairly presented. Prior audits have identified, and the Air Force has also acknowledged, the long-standing material internal control weaknesses identified in the Summary of Internal Control. These pervasive material weaknesses affect the reliability of certain information contained in the annual financial statement—much of which is taken from the same data sources as the basic financial statements.² Therefore, we are unable to express, and we do not express, an opinion on the basic financial statements. Additionally, the purpose of the audit was not to express an opinion on Management's Discussion and Analysis, Required Supplementary Information, and Other Accompanying Information presented with the basic financial statements. Accordingly, we express no opinion on that information.

Summary of Internal Control

In planning our work, we considered Air Force Working Capital Fund internal control over financial reporting and compliance with applicable laws and regulations. We did this to determine our procedures for auditing the financial statements and to comply with OMB guidance, but our purpose was not to express an opinion on internal control. Accordingly, we do not express an opinion on internal control over financial reporting and compliance with applicable laws and regulations. However, previously identified significant deficiencies, all of which are material, continued to exist in the following areas:

- **Financial Management Systems**
- **In-Transit Inventory**
- **Operating Materials and Supplies**
- **General Property, Plant, and Equipment**
- **Subsidiary Ledgers and Special Journals**
- **Intragovernmental Eliminations**
- **Other Accounting Entries**

A material weakness is a significant deficiency, or a combination of significant deficiencies, resulting in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected.³

² The annual financial statement includes the basic financial statements, Management's Discussion and Analysis, Required Supplementary Information, and Other Accompanying Information.

³ The term "remote" is defined as when the chance of a future event or events occurring is slight. Therefore, the likelihood of an event is "more than remote" when it is at least reasonably possible.



A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or a combination of control deficiencies, adversely affecting the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with GAAP. Significant deficiencies result in more than a remote likelihood that a misstatement of an entity's financial statements that is more than inconsequential will not be prevented or detected. The following is a list of significant deficiencies identified:

- **Accounts Receivable**
- **Accounts Payable**

Internal control work that we conducted as part of our prior audits would not necessarily disclose all significant deficiencies. The Attachment offers additional details on significant deficiencies, most of which we consider to be material internal control weaknesses.

The Air Force reported the above weaknesses in its FY 2008 Statement of Assurance, except for the material weaknesses involving: Financial Management Systems; Operating Materials and Supplies; General Plant, Property, and Equipment; Subsidiary Ledgers and Special Journals; Intragovernmental Eliminations; and Other Accounting Entries.

Summary of Compliance with Laws and Regulations

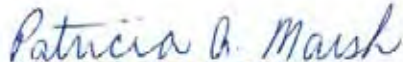
We limited our work to determine compliance with selected provisions of applicable laws and regulations related to financial reporting because management acknowledged that instances of noncompliance identified in prior audits continued to exist. The Assistant Secretary of the Air Force (Financial Management and Comptroller) acknowledged to us that Air Force's financial management systems do not substantially comply with Federal financial management system requirements, GAAP, and the U.S. Government Standard General Ledger at the transaction level. Therefore, we did not determine whether the Air Force complied with all applicable laws and regulations related to financial reporting. Providing an opinion on compliance with certain provisions of laws and regulations was not an objective of our audit and, accordingly, we do not express such an opinion. See the Attachment for additional details on compliance with laws and regulations.

Management's Responsibilities

Management is responsible for:

- preparing the financial statements in conformity with GAAP;
- establishing, maintaining, and assessing internal control to provide reasonable assurance that the broad control objectives of the Federal Managers' Financial Integrity Act are met; and
- complying with applicable laws and regulations.

We provided a draft of this report to the Assistant Secretary of the Air Force (Financial Management and Comptroller), who provided technical comments, which have been incorporated as appropriate. Air Force officials expressed their continuing commitment to address the problems this report outlines.


Patricia A. Marsh, CPA
Assistant Inspector General
Defense Business Operations

Attachment:
As stated



Report on Internal Control and Compliance with Laws and Regulations

Internal Control

Management is responsible for implementing and maintaining effective internal control and for providing reasonable assurance that accounting data are accumulated, recorded, and reported properly; that the requirements of applicable laws and regulations are met; and that assets are safeguarded against misappropriation and abuse. Our purpose was not to, and we do not, express an opinion on internal control over financial reporting. However, we have identified the following material weaknesses and significant deficiencies that could adversely affect Air Force financial management operations.

Previously Identified Material Weaknesses. Management acknowledged that previously identified significant deficiencies, all of which are material, continued to exist in the following areas.

Financial Management Systems. Statement of Federal Financial Accounting Concepts No. 1, "Objectives of Federal Financial Reporting," requires that financial management system controls be adequate to ensure that transactions are: executed in accordance with budgetary and financial law and other requirements; consistent with the purposes authorized; and recorded in accordance with Federal accounting standards. Statement of Federal Financial Accounting Concepts No. 1 also requires that financial management system controls ensure proper safeguards for assets to deter fraud, waste, and abuse, and that there is adequate support for performance measurement information. The Assistant Secretary of the Air Force (Financial Management and Comptroller) acknowledged that many Air Force financial management systems do not substantially comply with Federal financial management system requirements. The design of Air Force financial management and feeder systems does not allow them to collect and record financial information based on a full-accrual accounting basis. Until these systems are able to collect and report financial information in compliance with GAAP, budgetary transactions and nonfinancial feeder systems will continue to provide the basis for Air Force proprietary financial reporting.

In-Transit Inventory. Air Force supply management systems do not provide sufficient audit trails to confirm and value the in-transit inventory included as part of inventory held for sale on the Consolidated Balance Sheet.

Operating Materials and Supplies. The Air Force is required by Statement of Federal Financial Accounting Standards No. 3, "Accounting for Inventory and Related Property," to record an expense at the time a user consumes Operating Materials and Supplies. The Air Force does not record cost-of-goods-sold and work-in-process in accordance with Statement of Federal Financial Accounting Standards No. 3. Additionally, uncertainties exist regarding the existence and completeness of the quantities used to derive the balances reported in the financial statements for Operating Materials and Supplies inventory.

General Property, Plant, and Equipment. The Air Force is required by Statement of Federal Financial Accounting Standards No. 6, "Accounting for Property, Plant, and Equipment," to record General Property, Plant, and Equipment using acquisition cost, capitalized improvement costs, and depreciation expense. However, the Air Force cannot verify General Property, Plant, and Equipment values in accordance with Statement of Federal Financial Accounting Standards No. 6. In addition, the General Property, Plant, and Equipment line item on the Balance Sheet does not include all Government-furnished equipment (with values exceeding the capitalization threshold) in the hands of contractors.

Subsidiary Ledgers and Special Journals. Air Force Working Capital Fund resource managers do not always maintain adequate documentation or use transaction subsidiary ledgers and special journals to support recorded trial balance accounts. Air Force and Defense Finance and Accounting Service personnel do not perform reconciliations and system validations to verify the accuracy of accounts receivable from foreign military sales, progress payments to contractors, and accounts payable from the Materiel Support Division.

Intragovernmental Transaction Accounting. The Air Force cannot accurately identify all intragovernmental transactions by customer. Seller entities within DoD provide summary balances for revenue, accounts receivable, and unearned revenue to the buyer-side internal DoD accounting offices. In most cases, Air Force adjusts its buyer-side records to recognize unrecorded costs and accounts payable.

Other Accounting Entries. The Air Force acknowledges that it continues to make material adjustments for financial reporting that are not supported by detail transactions because of its inability to properly identify intergovernmental trading partner transactions and the deficiencies described above.

Previously Identified Significant Deficiencies. Management acknowledged that previously identified significant deficiencies continued to exist in the following areas.

Accounts Receivable. The Air Force cannot assure the validity of Accounts Receivable reported on the financial statements because of significant deficiencies in internal control. Specifically, the significant deficiencies include intragovernmental trading partner eliminations, foreign military sales, undistributed collections, the completeness of the Tri-Annual Review, and the lack of supporting documentation.

Accounts Payable. The Air Force cannot assure the accuracy of Accounts Payable reported in the basic financial statements because of significant deficiencies in intragovernmental trading partner elimination, accruals, supporting documentation, and the completeness of the Tri-Annual Review. Because of these weaknesses, Air Force is unable to properly reconcile and support the validity of Accounts Payable.

These financial management deficiencies may cause inaccurate management information. As a result, Air Force management decisions based in whole or in part on this information may be adversely affected. Financial information reported by DoD may also contain misstatements resulting from these deficiencies.



Compliance with Laws and Regulations

Management is responsible for compliance with existing laws and regulations related to financial reporting. We limited our work to determine compliance with selected provisions of the applicable laws and regulations because management acknowledged instances of noncompliance, and previously reported instances of noncompliance continue to exist. Therefore, we did not determine whether the Air Force was in compliance with selected provisions of all applicable laws and regulations related to financial reporting. Our objective was not to, and we do not, express an opinion on overall compliance with applicable laws and regulations.

Federal Financial Management Improvement Act of 1996. The Federal Financial Management Improvement Act of 1996 requires Air Force to establish and maintain financial management systems that comply substantially with Federal financial management systems requirements, applicable Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level. For FY 2008, the Air Force did not fully comply with the Federal Financial Management Improvement Act of 1996. The Assistant Secretary of the Air Force (Financial Management and Comptroller) acknowledged that many of its critical financial management and feeder systems did not substantially comply with Federal financial management systems requirements, Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level as of September 30, 2008.

Audit Disclosures

The Assistant Secretary of the Air Force (Financial Management and Comptroller) acknowledged to us on March 6, 2008, that the Air Force financial management and feeder systems cannot provide adequate evidence supporting various material amounts on the financial statements, and previously identified material weaknesses continue to exist. Therefore, we did not perform detailed testing related to previously identified material weaknesses. In addition, we did not perform audit work related to the following selected provisions of laws and regulations: Antideficiency Act, Federal Credit Reform Act of 1990, Pay and Allowance System for Civilian Employees, Prompt Payment Act, and Provisions Governing Claims of the United States Government (including provisions of the Debt Collection Improvement Act of 1996).

This report does not include recommendations to correct the material internal control weaknesses and instances of noncompliance with laws and regulations, because previous audit reports contained recommendations for corrective actions or because audit projects currently in progress will include appropriate recommendations.



U.S. AIR FORCE

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