Fiscal Year 2004

United States Army Annual Financial Statement

Our Army at War — Relevant and Ready, Today and Tomorrow

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Our Army at War — Relevant and Ready, Today and Tomorrow

R.L. BROWNLEE

"Ultimately, successful transformation will depend in part upon our ability to improve the management of all Army functions. Every management unit must be fully accountable for its work. To achieve this accountability, we must improve the quality of the information that we generate."

For three years the United States Army has been engaged in the War on Terror. Deployed in Iraq, Afghanistan, and more than one hundred other countries, our Army is again fighting tyranny and oppression, taking the fight to the shadowy lairs and hideouts of those who seek to destroy us. American Soldiers are not only providing the opportunity for freedom and democracy for the 46 million people in Iraq and Afghanistan, but at the same time they are protecting the American people by attacking the terrorists where they hide – in their home nests and spawning grounds.

While fighting terrorism, the Army is also pursuing the most comprehensive transformation of its forces since the early years of World War II. It will become an Army of campaign quality with a Joint and expeditionary mindset, capable of dominating the complex land environment and sustaining that dominance as long as necessary, yet remaining flexible and agile to respond rapidly to the needs of the Combat Commander.

The heart of our transformation effort is the creation of modular, combined arms maneuver brigade combat teams. By shifting supporting capabilities from division- and corps-level into these brigade combat teams, they will be more lethal, more deployable, and more sustainable. To accomplish this, we will grow the Army temporarily by 30,000 Soldiers over the next several years using the authority provided in Title 10, USC, funded initially, from supplemental appropriations. With these resources the Army will stand up at least 10 new combat brigades, raising our total from 33 in FY03 to 43 by FY06.

At the start of the War on Terror, our force structure reflected the needs of the Cold War, not the current fight. Recent experience shows that the Army needs more military police, civil affairs, transportation, aviation, intelligence, and medical units. Therefore, we are restructuring our Army to provide the types of forces the Combat Commander needs and re-balancing within the mix of forces in the Active and Reserve components to be more responsive. Additionally, the Army is shifting from an individual personnel replacement system to a unit system. This change will increase unit cohesion, and will provide greater stability and predictability for our Army families, whose unconditional love and steadfast support to our Soldiers are invaluable in every aspect of what our Army does.

Ultimately, successful transformation will depend in part upon our ability to improve the management of all Army functions. Every management unit must be fully accountable for its work. To achieve this accountability, we must improve the quality of the information that we generate. We are continuing to fully integrate our financial and functional systems, modernizing and streamlining our systems and processes to deliver data that are timely, accurate and relevant to our mission.

We are stewards of the resources our Nation has entrusted to us, and mindful of our tremendous obligations. Our people are our most precious resource, and we must ensure that our young men and women have what they need to do the jobs we have sent them to accomplish. More efficient management process, and more accurate information in our management systems, will directly improve the support our Soldiers, Army Civilians, and Army families expect and deserve.

R.L. Brownlee
Secretary of the Army

VALERIE L. BALDWIN

"It is imperative that the financial management community be prepared to support the Army's strategic reality and its goal of providing capabilities to the Joint Force in order to dominate across the full range of military operations."

At the close of another fiscal year, the Army finds itself in a new strategic reality. We are heavily engaged in combat in Iraq and Afghanistan, and we know the Global War on Terrorism will be protracted. To carry out our duty in this new context, we are reshaping the force to be an Army of campaign quality with joint and expeditionary capabilities -- transforming to win the war today while simultaneously posturing the Army for future challenges.

It is imperative that the financial management community be prepared to support the Army's strategic reality and its goal of providing capabilities to the Joint Force in order to dominate across the full range of military operations.

In 2004, we made notable progress toward this objective. We eliminated material weaknesses in the automated mobilization system and the Army purchase card program. We improved accuracy of the fund balance with treasury, and investment valuations are now reported on our financial statements. We deployed the Defense Travel System (DTS), which is fully integrated with our financial management system, to 28 sites. Additionally, the Army reported more accurately criminal and civil fraud recoveries, corrected real property documentation deficiencies and prepared for internal audit of other liability valuations and stewardship land.

Even with these successes, there is more to do. We must continue to adhere to the Army Chief Financial Officers Strategic Plan and prepare to transition to the General Fund Enterprise Business System (GFEBS). GFEBS, a commercial, off-the-shelf financial management planning system, will provide the Army relevant and reliable financial information across the full spectrum of operations. I am pleased to say that the Army will reach the first major GFEBS milestone this spring: contract award for the initial phase of the program.

Equally important, the financial management community must continue to improve and to follow performance measures required by the President's Management Agenda (PMA). These standards help Army leadership to make decisions regarding human capital, competitive sourcing, financial performance, e-government and budget/performance integration, which will help to ensure the Army's future readiness.

It is vital that the Army financial management community be an effective, efficient provider of support to the Joint and Expeditionary Army. Therefore, it is crucial to leverage our available resources by studying good business practices, and implementing them where applicable and appropriate. Additionally, we must work with Army leadership to identify information needs and be prepared to meet those needs in a timely, reliable fashion. Finally, we must analyze requirements and prioritize them in accordance with available resources. Success in each of these areas requires that we ensure adequate financial and management controls are in place, and that our workforce is positioned to adapt to business modernization. We are committed to making these long-term changes.

In closing, I would like to acknowledge the work of my deputy, Mr. Ernest Gregory, who spent much of FY 2004 serving as acting assistant secretary of the Army (financial management and comptroller). Mr. Gregory's commitment to the mission of the Army and his leadership have paved the way to transformation, and for this the Army is truly grateful. After 38 years of dedicated service, Mr. Gregory retired in October and is moving into the next phase of his life. We extend our sincerest thanks to him for his service, and send our best wishes to him and his family.

Valerie L. Baldwin
Assistant Secretary of the Army
(Financial Management and Comptroller)

ERNEST J. GREGORY

"I am confident the Army will continue to leverage technology to further its transformation efforts. I am even more confident in the ability of our people to succeed in an ever-evolving financial management environment."

Fiscal Year (FY) 2004 was an unusually challenging year for the Army financial management community. With major operations in Iraq, Afghanistan and elsewhere, appropriations for the Army totaled $149.8 billion, including an exceptional $53.4 billion in supplemental funding. The FY 2004 Army Annual Financial Statement signifies another year of continued improvement in the management and reporting of our fiscal resources.

Transformation for the operational Army hinges on relevance and readiness. The Army's financial management community has a parallel to this, its own transformation focusing on the provision of relevant, reliable information. At the core of our transformation is the application of federal accounting standards, the full implementation of which will deliver an unqualified audit opinion and ensure compliance with the Chief Financial Officers (CFO) Act. Federal accounting standards also will provide financial managers unprecedented insight into the costs of goods and services and will enable better analysis of funding execution. By following these standards, Army leadership will have the information necessary to make properly informed decisions when assessing operational requirements or supporting the individual Soldier.

All organizational levels within the Army are reviewing their automated systems and processing procedures to ensure that financial information is timely, accurate and relevant. Where necessary, procedures will be altered. In addition, the Army is validating financial systems and nonfinancial feeder systems for audit and internal control purposes, among them the Integrated Facilities System, Property Book Unit Supply Enhanced (PBUSE) and procedural controls for environmental liabilities. All legacy systems that do not support CFO compliance initiatives eventually will be replaced.

In FY 2004 work continued on the key financial management initiatives of the CFO Strategic Plan (the blueprint for CFO compliance), on the Accounting for Internal Use software, on identifying government-furnished equipment to contractors, and on the pursuit of Army Business Initiatives Council recommendations. New programs implemented during the year include the Defense Travel System and PBUSE. These initiatives will help the Army achieve full compliance with the CFO Act and should make possible achievement of an unqualified audit opinion for the Army's General Fund and Working Capital Fund financial statements.

The conclusion of FY 2004 also marks the conclusion of my government career. It has been an honor to serve with the Soldiers, civilians and contractors who are the key elements of the defense of our great nation. I am particularly proud to have been associated with the Army's financial management community. I have seen significant change in the way the Army manages its fiscal resources, with manual processes giving way to automated systems and technological advancements revolutionizing the conduct of financial management operations. I am confident the Army will continue to leverage technology to further its transformation efforts. I am even more confident in the ability of our people to succeed in an ever-evolving financial management environment. I salute each and every member of the financial management community. I salute our Soldiers.

Ernest J. Gregory
Principal Deputy Assistant Secretary of the Army
(Financial Management and Comptroller)

JOHN PAUL WOODLEY, JR.

"Our nation's water resources are finite, and in managing those resources we are increasingly challenged to reach decisions that appropriately balance the social and economic benefits of development with the need to protect the environment."

Throughout its history, the Army Corps of Engineers has been committed to serving the nation in peace and war by providing comprehensive engineering, management and technical services. Our mandates over time have continually evolved to reflect America's priorities. At Bunker Hill and during the Revolutionary War, the Corps supported our military forces in time of war. Today, the nation's war on terrorism is our main priority and we are mobilizing our resources to help win this war. In this regard, Civil Works has established a Homeland Security Office in Corps Headquarters, as we undertake measures to enhance the security of critical water resources facilities.

In the mid-1820s, the Corps of Engineers conducted a survey of nationally important roads and canals for commercial use, military use, and mail transportation. Today's Civil Works mission does not have a national road component, but it does include water resource development activities in the primary program areas of flood control, navigation and environmental protection. Additionally, we have a critical role in emergency response. For example, the Corps became heavily engaged in protection and relief work when Hurricane Charley struck the west coast of Florida in August 2004. The Corps remains vigilant and we take great pride in lending assistance to the efforts of local communities during times of disaster.

The Corps of Engineers possesses an impressive body of knowledge on water resources, and we must exploit that knowledge and associated skills to fulfill the Federal government's responsibilities to the nation, both at home and abroad. Our nation's water resources are finite, and in managing those resources we are increasingly challenged to reach decisions that appropriately balance the social and economic benefits of development with the need to protect the environment. As science and engineering continue to advance, we will seek to leverage new development to achieve an optimal balance of these factors for the benefit of the nation.

Looking to the future, we must seek to do everything within our authorities to ensure that our country's economy remains strong and its natural resources protected. We are dedicated to continuing a national water resources program that serves the best interest of all our citizens. In that regard, a Strategic Plan for the Army Civil Works mission was published in March 2004. This plan, which covers a six-year period from FY 2004 to FY 2009, sets forth the framework for enhancing the sustainability of America's water resources.

John Paul Woodley, Jr.

John Paul Woodley, Jr.
Assistant Secretary of the Army
(Civil Works)

FY 2004 in Review

In Fiscal Year (FY) 2004, the United States Army and our sister services engaged in one of the most challenging periods in our history as we conducted the Global War on Terrorism (GWOT). In addition to the GWOT, our Army Soldiers participated in the Balkans stability and support operations, Sinai peacekeeping, and in Colombia, Africa, and the Philippines security operations. We continue to deter aggression in Korea and other areas around the world. Overall, the majority of our active and reserve combat forces were deployed to 120 countries. Global and frequent deployments require our forces to be more lethal, versatile, mobile, and efficient than at any time in our history.

Concurrent with this global mission, our Army accelerated the process of changing how we wage war and keep the peace. We continued to transform our Army to a more joint and expeditionary force. Through our transformation, we operated more effectively alongside our sister services and allied forces, and reduced the time needed to deploy forces capable of winning anywhere around the globe.

Our enemies employed new methods of attack that required us to counter with innovations to our tactics, training, and equipment. We improved the process for rapid development and deployment of new equipment, ranging from body armor to intelligence gathering. We also accelerated development of the Future Combat

"What Operation Enduring Freedom and Operation Iraqi Freedom have done is caused us as a department and as services to look where we have commonality and jointness across our formations so we can help each other out and kind of spread out the burden across the force. And that's what we see happening. The one thing we all share in common across the services (is) it does say 'U.S.' across our breast. It may say 'U.S. Air Force' or 'U.S. Army' or 'U.S. Marine Corps' or 'U.S. Navy,' but it all starts with the 'United States,' and that's our team logo."

—Gen. Richard A. Cody, Vice Chief of Staff, U.S. Army

Systems (FCS), a joint network of 18 systems linked to individual Soldiers in the field—a LandWarNet extending from the Pentagon to the foxhole and covering everything in between.

To improve the quality of life for our Soldiers and their families, we initiated a stabilization program aimed at increasing time spent at unit and post assignments. Historically, Soldiers spent an average of 31 months at one location before transferring to another assignment. To alleviate the stresses of frequent rotation on our Soldiers and their families, we are working to home-base Soldiers—officers and enlisted personnel—to the same posts for up to seven years, enabling their families to grow community roots and establish support structures during deployments.

At the conclusion of FY 2004, the Army had 1,046,592 men and women in the uniformed service, which included 499,543 active Soldiers, 204,131 Army Reservists, and 342,918 Army National Guard (ARNG) personnel. In addition, the Army employed 227,160 civilians.

Operation Iraqi Freedom and Iraq Reconstruction

The Army's most visible and resource-intensive activity during FY 2004 was Operation Iraqi Freedom and Iraq reconstruction. Our Army made considerable progress capturing former regime leadership, increasing security and rebuilding the infrastructure of Iraq with a force of nearly 124,000 active and reserve Soldiers. Infrastructure improvements for transportation, utilities, health care, and education provide a solid foundation for the establishment of a viable economy and the creation of a free and democratic state.

The U.S. Army Corps of Engineers (USACE), which is the world's largest public engineering, design, and construction management agency, leveraged our Nation's public and private engineering and technical know-how to address Iraqi infrastructure needs. Specifically, the U.S. Project and Contracting Office, an agency charged with oversight of the $18.4 billion appropriated by the U.S. Congress to support the reconstruction of Iraqi infrastructure, worked with the USACE to construct new Iraqi Army bases, an Iraqi Navy base, and the Ministry of Defense.

Iraq's first megawatt generator since 1976 is now operational. The 40-megawatt generator went online August 18, 2004 near Basrah, Iraq. Photo courtesy of U.S. Army.

Operation Enduring Freedom—Afghanistan

At the conclusion of FY 2004, there were approximately 14,000 Army uniformed personnel in Afghanistan. Their mission continues to ensure the peace, assist in rebuilding the country, and root out the perpetrators of the attack on September 11, 2001. We have set the conditions necessary for the country's first democratic presidential election. The Army has provided the security needed for registering voters to cast their ballots in even the most remote areas of the country. In some parts of Afghanistan, over 50 percent of the population have registered, and half of them are women. We trained Afghani police and military forces, built infrastructure, and remain committed to providing the security necessary to allow for free and open elections.

Spc. Mary Miller and two young Afghan girls in traditional costume plant a tree at the conclusion of the opening ceremony for the Provincial Reconstruction Team headquarters. Maj. Richard Sater

Homeland Security

For Operation Noble Eagle, the Army has engaged 17,000 Soldiers to defend the homeland. Among the Soldiers defending the homeland, the ARNG leads the domestic battle against terrorism. The ARNG's assistance to Homeland Security takes many forms. The Anti-Terrorism Force Protection and physical security programs safeguard facilities, personnel, and equipment, as well as monitor and maintain intrusion-detection systems that detect and assess threats at 397 critical sites. For example, in June 2004, Georgia National Guard troops provided security to the Group of Eight (G8) Summit for the leaders of the world's major industrial countries.

Members of the Missouri National Guard's new Chemical Biological, Radiological, Nuclear or High Yield Explosive Enhanced Response Force Package (CERFP) spray a "victim" of a toxic chemical attack during an Army evaluation of the team's ability to deal with a weapon of mass destruction near Jefferson City on July 24. Master Sgt. Bob Haskell

The Army participated in training exercises—such as Determined Promise '04 and Amalgam Virgo '04—aimed at responding to terrorist threats ranging from massive radiological explosions in Los Angeles, California, to handling the aftereffects of a terrorist attack on a cruise ship, a major auto race, a bridge, and two tunnels in Hampton Roads, Virginia. More than 4,000 Canadian and U.S. military personnel in three U.S. states and two Canadian provinces participated in these exercises. ARNG units have been trained to provide emergency medical care and to decontaminate victims if toxic chemical agents are ever delivered by weapons of mass destruction on American soil.

Army Reorganization and Transformation

Historically, division-level Army fighting forces were the units with the resources capable of conducting campaigns. In FY 2004, the Army started a major reorganization and restructuring aimed at fielding brigade-sized units with division-type resources. Key to this transformation is the concept of modularity, or modular units that are interchangeable, scalable, and tailorable to meet the immediate needs of the battlefield. These modular brigades are "plug-and-play" fighting units that can fit into a larger multi-unit force and have the capabilities to operate independently in the field.

The 3rd Infantry Division, which returned from Iraq in September 2003, is serving as the pilot for the Army's modularity concept. In October 2003, one of its brigades tested the new organization at the National Training Center, Fort Irwin, California. The 101st Airborne Division, which returned from Iraq in January 2004, and the 10th Mountain Division are the next units to undergo the organizational change.

In addition, the Army is rebalancing our force among the Active Component and the Reserve Component, the Guard, and the Army Reserve. This initiative will give our Army more troops with the skills we need to fight the GWOT. At the same time, the Army's intent is to have no more than 50 percent of the ARNG force involved in the nation's warfighting effort at any given time so that remaining ARNG forces can be immediately available for missions in their home states.

Gov. Arnold Schwarzenegger shakes hands with National Guard Soldiers of the 81st Armor Brigade (Separate) at the National Training Center and Fort Irwin, CA. Spc. Jacob A. McDonald

Another area of reorganization was in Army aviation. In FY 2004, the Army decided to cancel the RAH-66 Comanche reconnaissance/attack helicopter in favor of modernizing the existing fleet of Army helicopters. We updated the avionics and aircraft survivability systems for the UH-60 Black Hawk, AH-64, Apache, and CH-47 Chinook. In addition to the upgrade programs, we also standardized the composition of aviation units in both the active and reserve forces to enable modularity and uniformity.

Another successful initiative in FY 2004 was the Rapid Equipping Force (REF) program, which speeds the fielding of commercial innovations to battlefields. The REF reduces the lead-time required to field equipment by adapting readily available technologies. REF initiatives have been used for counter-mines, sniper fire, and mortar rounds as well as for the creation of new doctrine, battlefield robots, and electronic intelligence—all these are areas intended to safeguard our Soldiers and to give them new fighting capabilities.

Soldiers in Iraq prepare to deploy a small robot to check out a suspect object along a road. Photo courtesy REF.

Financial Management Systems and Improvements

A critical aspect of transforming the Army is improving our management functions. Throughout FY 2004, we improved the quality of the Army's financial information through streamlining our systems and focusing on clearing our material weaknesses. During the year, the Army's financial management and functional communities collaborated to eliminate legacy systems. We converted the Army National Guard Bureau from its old accounting system to the Standard Finance System and deployed the Defense Travel System (DTS) to all scheduled sites. We are making great strides toward enhancing our financial management functions while striving to adopt world-class business functions that display our trustworthy use of public resources.

With our Joint Reconciliation Program initiative, we reviewed commitment and obligation transactions for timeliness, accuracy, and completeness. We aggressively worked to reduce unliquidated obligations of canceling appropriations—a key performance measure of public sector financial management effectiveness. As a result of this initiative, we reduced the amount of these funds from $633 million at the start of the fiscal year to $26.2 million by the fiscal year's end. We have also implemented management controls and oversight to enforce the Anti-Deficiency Act (ADA). Our efforts resulted in the submission of more ADA cases in FY 2004 than in both FYs 2002 and 2003 combined. This is a positive indication that we are identifying and correcting problem areas.

The Army introduced initiatives to provide more timely and accurate accounting information and enhance the quality of financial management decisions. The Army Managerial Accounting Division was established to use Army Shared Knowledge-Financial Management (ASK-FM) and other analytical tools to improve the effectiveness of budget execution. ASK-FM, rolled out to the Army and the Major Commands in May 2004, is a web-based business intelligence application designed to provide access to near real-time data for accounting, disbursements, logistics, entitlements, pay, and other purposes. Basic users require little or no training to use ASK-FM—simple click and drill technology accesses published reports.

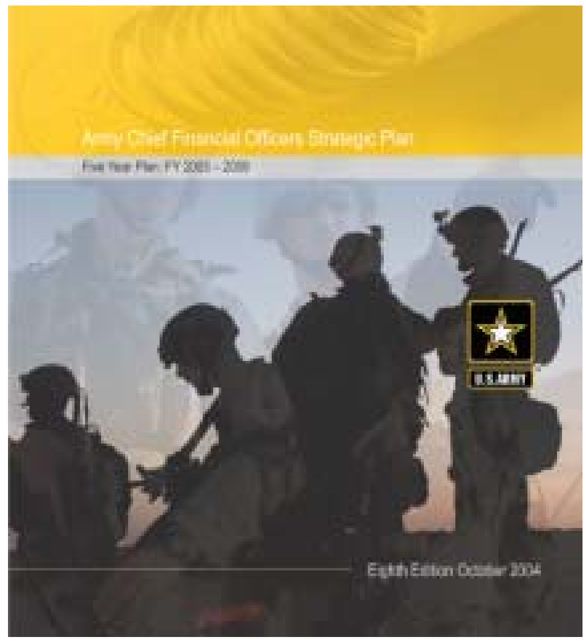
As we look forward into the future, we have begun to invest in a new financial management system that will meet the Army's ever-changing and highly complex environment. The cornerstone of our business management transformation is the General Fund Enterprise Business System (GFEBS). GFEBS is a commercial off-the-shelf enterprise resource planning system that will manage our daily functions through general ledger processing, vendor payments, receivables, funds control and execution, cost management, and fiscal reporting. GFEBS will assist in the creation of quality financial information and fiscal transactions that can be audited and result in an attestation.

Providing accurate, reliable, timely, and consistent financial information across all Army operations has long been a time-consuming challenge that continued to be addressed in FY 2004 through long-term enhancements to Army financial management. The new initiatives will enhance our ability to receive an unqualified audit opinion of our financial statements, improve budget formulation and resource execution, facilitate operational divestiture, eliminate legacy systems and business practices, and reduce Army and Defense personnel requirements for financial functions.

Army Systems Controls and Legal Compliance

The Army continues to place a high priority on improving its financial management processes and associated systems. To that end, we worked aggressively through FY 2004 toward our goal of ensuring that our critical financial feeder systems are compliant with the Chief Financial Officers (CFO) Act of 1990. The ongoing replacement or incorporation of Army systems into newer, evolving systems reduces the numerous noncompliant systems. Those critical financial feeder systems not scheduled for replacement are being evaluated for modification to achieve compliance, with each system being periodically monitored by the U.S. Army Audit Agency (AAA) as part of the Army's CFO Strategic Plan. This plan affixes responsibility and establishes a timeline for addressing and resolving problems of noncompliance, with periodic status reports going to Army leadership.

The Army CFO Strategic Plan—our road map to an unqualified audit opinion through the production of quality information—is one of many initiatives designed to improve business processes throughout the Army. As these business processes improve and evolve, so too will the quality of the information that is vital to the Army's leaders, decisionmakers, and stakeholders.



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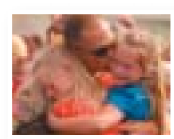
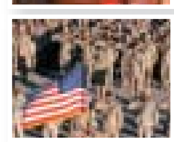
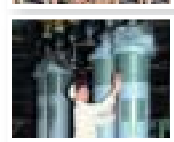
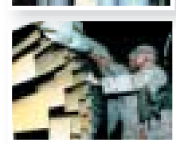





[Large Photo]
A Soldier is welcomed home by family members in Asheville, N.C., after more than 15 months deployed in support of Operation Iraqi Freedom. The Soldier is assigned to the 210th Military Police Company, North Carolina Army National Guard. This photo appeared on www.army.mil.

[Top Inset Photo]
Soldiers of the 25th Infantry Division's 1st Battalion, 27th Infantry Regiment, salute the colors during a recent ceremony in Iraq. The division currently has Soldiers deployed to both Iraq and Afghanistan. This photo appeared on www.army.mil. By Spc. Sean Kimmons

[Middle Inset Photo]
Bomb making—McAlester Army Ammunition Plant

[Bottom Inset Photo]
At Khor al Zabayr, north of Basra, BG(P) Steven R. Hawkins and Corps of Engineer's Ricky Wilson, Senior Electrician from Carters Lake Pump Storage Hydropower Facility, GA, Mobile District, inspect the new blades on a generator rotor as part of the Corps' "Restore Electricity to Iraq" Mission.

General Fund – Management's Discussion & Analysis

Overview

The Army General Fund, the largest Army fund, finances military operations, supporting services, personnel, facilities, and nearly every other function. A majority of the General Fund's revenue comes from Congressional appropriations. In FY 2004, the Army received $150 billion in appropriations.

Mission

For 229 years, the Army's primary mission has been warfighting, defending the United States and its territories, commonwealths, and possessions. Prepared at all times to fight and win the Nation's wars, Army Soldiers are also ready to go anywhere in the world to save lives, protect property, provide humanitarian aid, and keep the peace.

While the Army's warfighting mission has been the same during its 229-year history, the nature of conflict has from time to time undergone radical transformation. When that happens, the Army changes strategy, tactics, equipment, and organizational structure. One such major change is now underway with the advent of

> *We do not have the luxury to wait. So we must change while still fighting—this definitely is not business as usual.*
>
> *—Gen. Peter J. Schoomaker, Chief of Staff, U.S. Army*

the Global War on Terrorism. This is a war unlike any in our history. It is underway across both the globe and the full range of military operations. The enemies are rogue states and terrorists who cannot be discouraged, but nevertheless must be prevented from striking against our Nation, allies, and interests. They are waging war of a different type, tempo, pace, and duration than we have encountered previously. This means the Army must simultaneously fight and transform how its fights—a hard and often dangerous undertaking.

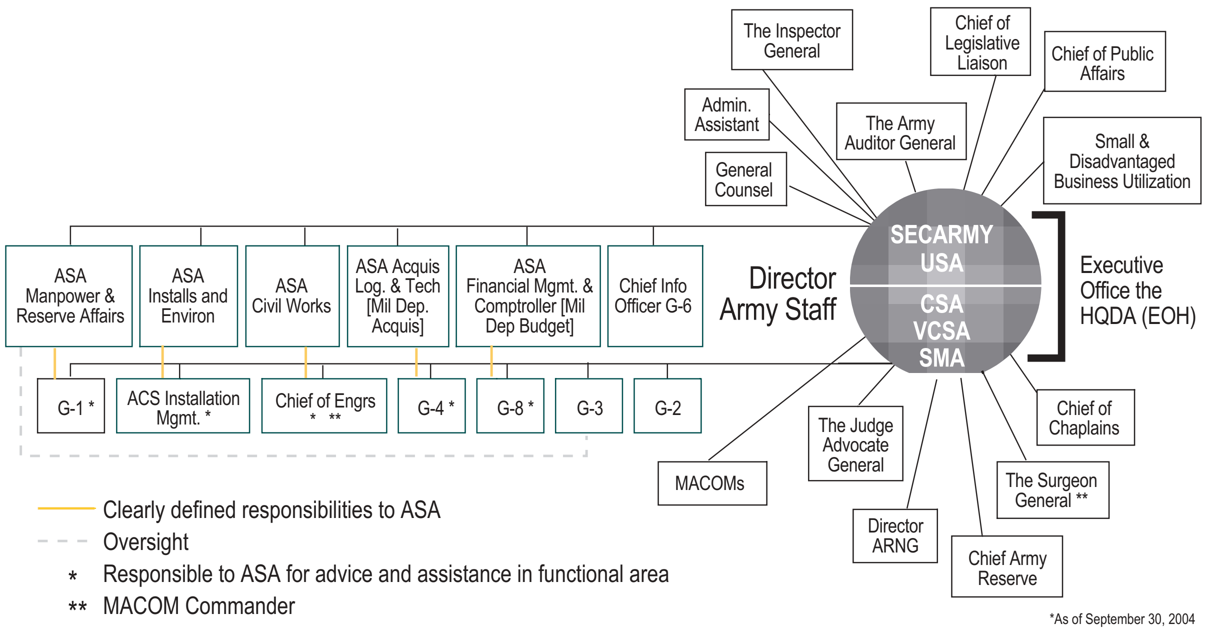
To transform itself, in FY 2004 the Army started the process of re-examining and challenging our most basic institutional assumptions, organizational structures, paradigms, policies, and procedures. The result of this examination will be a more relevant and ready Army—the Future Force.

Vision

Guiding the Army's transformation is a vision of a more relevant and ready Future Force—a campaign-quality Army with a joint and expeditionary mindset capable of defeating any adversary or controlling any situation across the full range of military operations. We will redesign our formations to provide modular, capabilities-based organizations. We will balance our forces to give them the ability to operate in an uncertain environment against an unpredictable threat. Our people will have an unprecedented level of adaptability.

Organization

Figure 1. Organization of the Department of the Army



The Army is an organization of headquarters, staffs, commands, and units integrated into a single system with a common mission. Figure 1 is an organizational chart of the Headquarters Department of the Army (HQDA). The Secretary of the Army, the Chief of Staff (CSA), and the other leaders of the Executive Office of HQDA together lead the HQDA. Decisionmaking authority is unified within this office, enabling quick, responsive actions to ever-evolving mission requirements.

Each of the major combat organizations, called armies, consists of (in descending order by size) the following formations: divisions, brigades, battalions, companies, platoons, and squads. At present, the centerpiece of Army combat forces is the division. In FY 2004, we began moving toward a focus on the smaller brigades that make up a division. These brigade-level units will be permanently organized to be more self-sufficient, modular formations called "Units of Action."

To meet global commitments across the full spectrum of military operations, the Army is made up of: the Active Component and Reserve Components. The Reserve Components are the United States Army Reserve (USAR) and the Army National Guard (ARNG). Since September 11, 2001, the Army has mobilized almost half of the Reserve Component. The combination of the increased use of Reserves and the shift to smaller, modular brigades may be the largest and most significant reorganization in the Army since World War II.

Soldiers of the 25th Infantry Division's Task Force 1st Battalion, 14th Infantry Regiment, re-enlist before heading out of Kirkuk Air Base for their second Najaf mission recently. This photo appeared on www.army.mil. By Staff Sgt. Klaus Baesu

Core Competencies

The U.S. Army has maintained two core competencies: (1) training and equipping Soldiers and growing leaders and (2) providing relevant and ready land power to Combatant Commanders as part of the Joint Force.

We report below, on the progress made in enhancing these competencies in FY 2004.

1) **Training and Equipping Soldiers and Growing Leaders.**

No Soldier can survive in the current battlespace without constant training in weapons and fieldcraft and a continuous immersion in the Army's Warrior Culture.

New Recruits. The Army inducted and provided basic training to 80,000 new recruits as well as advanced training in different military occupational specialties.

Everyone Is a Warfighter. The GWOT has no rear areas where cooks, clerks, drivers, and other non-combat personnel are safe from attack. Therefore, in both basic and other training, the Army is determined that all Soldiers, no matter what their job, will be qualified for combat.

Exercises. Field experience under close-to-combat conditions is integral to preparing officers and enlisted personnel for actual warfighting. In FY 2004, the Army conducted many such exercises.

Continuing Education. eArmyU, the Army's degree-granting virtual university, enrolled over 30,000 students around the world for graduate, undergraduate, and certificate degree programs. Started in January 2001, the program is on target to enroll 80,000 students by FY 2005.

Equipping Soldiers. Regarding equipment, in FY 2004, the Army's Rapid Fielding Initiative (RFI) upgraded 18 brigade combat teams (BCTs) and 8 enhanced Separate Brigades, serving in Operations Iraqi Freedom and Enduring Freedom. In addition, we accelerated fielding of select future capabilities, such as thermal weapon sights, enhanced night vision goggles, improved body armor, the Future Combat Rifle, and a new sniper rifle.

Pfc. Walker calls to fellow Soldiers after finding a cache of rockets hidden in a bush near Bayji, Iraq. This photo appeared on www.army.mil. By Pfc. Elizabeth Erste

A Soldier maintains security while a humvee carrying troops is towed from a river by another vehicle in Afghanistan. This photo appeared on www.army.mil.

Rapid Equipping Force (REF) works directly with operational commanders to find solutions to operational requirements. These solutions may be off-the-shelf or near-term developmental items that can be made quickly available. Because REF items incorporate technologies already available off the shelf, REF can get new equipment into the field in a fraction of the time previously required. Since the beginning of Operation Enduring Freedom, REF has fulfilled at least 50 requirements for items needed by Soldiers. For example, the then Army

"Our reorganization is going to be rapid and challenging. Keep in mind that this is the largest and most significant reorganization of our Army since World War II."

—General Schoomaker

Vice Chief of Staff General John M. Keane and the REF established a coordinated effort to supply U.S. Forces with a safer and more efficient way of searching wells and remote mountain caves. Within 45 days, Soldiers were utilizing the solution, the iRobot, in the theater.

Members of 2nd Brigade Recon Troop, provide perimeter security for other members of the Quick Response Force during a Search and Seizure mission, June 26, 2004. This photo appeared on www.army.mil.

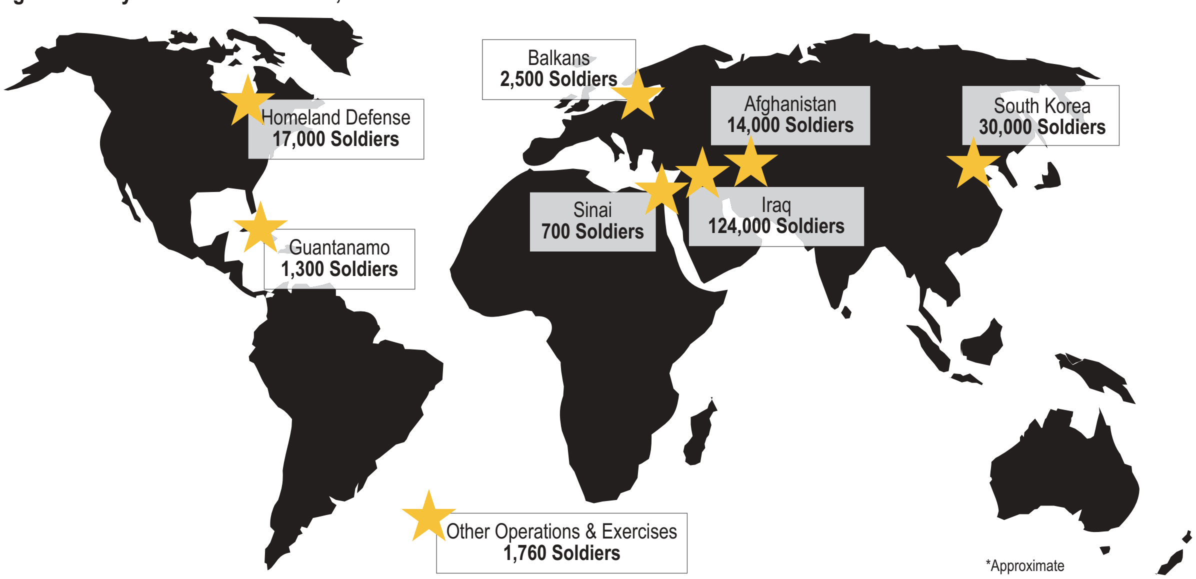
2) Providing Relevant and Ready Land Power to Combatant Commanders as Part of the Joint Force.

As may be seen in the map in Figure 2, by far the Army's most visible and resource-intensive activity during FY 2004 was the GWOT. For that conflict, we committed a force of over 139,000 Active and Reserve Soldiers to Iraq, Afghanistan, and Guantanamo and 17,000 to Operation Noble Eagle, the defense of the homeland.

REF Items Now in the Hands of Soldiers

- **FN303 Non-Lethal Weapon**, which shoots paint pellets at potential aggressors and marks them with ink to help with future identification or apprehension
- **WellCam**, a remote video system that precludes Soldiers from having to climb into wells and caves in search of weapons caches
- **electronic translators** that emit voice commands in Pashtu and Arabic
- **lock shims** that allow Soldiers to open padlocks, as is necessary during intelligence-driven home searches, without destroying locks and doors
- **a hand-held thermal viewer** for close-up images of forward sites
- **electronic countermeasures**, installed on Humvees, to jam frequencies the enemy is most likely to monitor
- **"Jaws of Life"** emergency extraction/rescue equipment sets used to free victims of aircraft and vehicle crashes
- **cables and power-supply adapters** used by engineers in Afghanistan to feed power to computers and other electrical devices from the Single Channel Ground and Airborne Radio Subsystem (SINCGARS) radio battery, after the battery no longer has sufficient power to run the SINCGARS

Figure 2. Army Global Commitments, FY 2004



In addition to supporting overseas actions, the ARNG plays an important domestic role, routinely responding to state emergencies. In FY 2004, there were 280 requests for emergency support, ranging from basic human needs to engineering support during natural disasters. Our ARNG has fielded 32 Weapons of Mass Destruction Civil Support Teams (CST), which assist first responders in the event of an incident. To date, these teams have responded to 74 different requests for support. Also, more than 8,000 ARNG Soldiers have executed critical force protection duties at 148 installations in the continental United States.

Army Campaign Plan

In FY 2004, the Army developed and started to implement a new Campaign Plan that is a road map to the Future Force. The senior leadership of the Army established focus areas for efforts to win the GWOT and increase the relevance and readiness of the Army. The focus areas range from developing flexible, adaptive, and competent Soldiers to accelerated fielding of Future Force capabilities, to creating modular, capabilities-based unit designs. Every focus area aims at transformation—a key concept of the Army today.

The Soldier: Develop flexible, adaptive, and competent Soldiers with a Warrior Ethos.

Soldiers rush into position to secure the perimeter during an exercise in Djibouti. The Soldiers are assigned to the Guam Army National Guard's 1st Battalion, 294th Infantry Regiment, deployed in support of the Combined Joint Task Force-Horn of Africa. This photo appeared on www.army.mil.

The Bench: Prepare future generations of senior leaders. Identify and prepare select Army leaders for key positions within joint, interagency, multinational, and Service organizations.

Combat Training Centers/Battle Command Training Program: Focus training at Combatant Training Centers and the Battle Command Training Program to meet requirements of the current security environment, and the Joint and Expeditionary Team.

Leader Development and Education: Train and educate Army members of the Joint Team.

Army Aviation: Conduct a holistic review of Army Aviation and its role on the Joint battlefield.

Current to Future Force: Accelerate fielding of select Future Force capabilities to enhance effectiveness of Current Force. Army transformation is a process of constant change.

The Network: Leverage and enable interdependent, network-centric warfare.

Modularity: Create modular, capabilities-based unit designs.

Joint and Expeditionary Mindset: Retain our campaign qualities while developing a Joint and Expeditionary mindset.

Stabilization

In FY 2004, the Army undertook several initiatives that will give Soldiers and their families more stable and predictable lives. We started keeping units together longer, extended tours of duty, and encouraged Soldiers to return to the same post repeatedly during their careers. This helps families become more connected to their communities and promotes continuity in schools, medical care, spouse career, education, and home ownership.

Active Component /Reserve Component Balance: Redesign the force to optimize the Active and Reserve component (AC/RC) mix across the defense strategy.

Force Stabilization: Ensure unit stability and continuity and provide predictability to Soldiers and their families.

Actionable Intelligence: Provide situational understanding to Commanders and Soldiers with the speed, accuracy, and confidence to impact current and future operations.

Installations as Flagships: Enhance installation ability to project power and support families.

Family members welcome home soldiers from the 3rd Brigade, 3rd Infantry Division to Fort Benning, GA.

Authorities, Responsibilities, and Accountability: Clarify roles and enable agile decisionmaking.

Resource Processes: Redesign resource processes to be flexible, responsive, and timely.

Strategic Communications: Tell the Army story so that the Army's relevance and direction are clearly understood and supported.

Transformation during a war is never easy, but it is a practice that appears many times in the history of our great Army. We must examine, design, and develop new solutions for a new and dangerous world, as we have done so successfully in our past. This will require the deep and personal commitment of every member of the Army team—every leader, every Soldier, every civilian, and every family member.

Modularity and Standardization

Modular units are interchangeable, scalable, and tailorable formations that are smaller and more self-contained than before. For example, a Future Force modular brigade has almost all the capabilities it needs in order to operate in the field: infantry, armor, aircraft, intelligence, medical, and others. It can be "plug-and-play," able to operate independently from its division and to fit with some precision into a larger multi-unit force, including Joint Force teams. Standardization is critical to the success of modularity. This means standard equipment, armament, training, and doctrine—often across the Army and the Joint Team.

More Autonomy for Flagship Installations

In FY 2004, in a marked departure from the past, funds for installations were routed to garrison commanders instead of being passed through major commands. This will ensure that funds earmarked for garrison operations are used for their intended purpose, improve accountability, and increase the overall support to Soldiers and their families.

General Fund Performance Results—Institutionalizing Performance Management

The current national security environment differs dramatically from that of the past. We no longer face a monolithic superpower; instead, we must contemplate and fight multiple adversaries in multiple places. As our enemy evolves, we are rapidly and dramatically altering our forces, our weapons, our training, and our tactics. One of the ways that the Army has evolved is our emphasis on changing our business processes and focus on performance management.

Performance management is nothing new to the Army. In the 1970s, we had Management By Objectives; in the 1980s, we focused on task, condition, and standards; and in the 1990s, we added a capabilities focus to The Army Plan. In this new century, we have introduced our balanced scorecard approach.

Through the balanced scorecard, we are formally institutionalizing performance management in the Army. Focusing on output measures, we use performance management techniques to verify we are doing the right things now and to look for trends in the future. For the first time in history, we utilized performance measures to justify our budget requests. In the FY 2005 budget, 60 percent of our programs were accompanied by measures and goals to gauge our success. By FY 2007, 100 percent of our budgeted programs will have associated metrics. Performance management allows us to measure our progress, identify issues, and address them before they become troublesome.

The Army does not fight alone—we are only one part of a joint team. This section of the Annual Financial Report highlights how we align ourselves to Congressional requirements, to the Department of Defense (DoD)'s balanced scorecard and its risk management framework, and to other members of the joint team. It represents one of the many steps along our road map for instituting performance management Army-wide.

Synchronizing Performance Management Efforts

There are four components to the Army's performance management approach. In calendar year 2004, the Army began synchronizing these components and is using them as a road map for institutionalizing performance management in the Army. These four diverse efforts intersect and include guidance from the Government Performance Results Act (GPRA), the Quadrennial Defense Report (QDR) risk framework, the President's Management Agenda (PMA), and the Management Initiative Decisions (MIDs).

The Government Performance Results Act of 1993

The Government's first step toward performance management was initiated by Congress in 1993. The GPRA was signed into law with the intent of shifting the focus of Government decisionmaking, management, and accountability from activities and processes to the results and outcomes they achieve. This constituted a shift away from a preoccupation with the activities that are undertaken—such as grants dispensed or inspections made—to a focus on the results of those activities. Focusing on results—such as real gains in employability, safety, responsiveness, or program quality—was a paradigm shift for the Government. GPRA also sought to gain information on the plans, goals, and strategies of Federal agencies. Under GPRA, agencies' annual performance plans were required to clearly inform the Congress and the public of:

(1) Annual performance goals for agencies' major programs and activities (i.e., DoD's Annual Defense Report or (ADR))

(2) Measures that will be used to gauge performance

(3) Strategies and resources required to achieve the performance goals

(4) Procedures that will be used to verify and validate performance information.

These annual plans, issued soon after transmittal of the President's budget, provide a direct linkage between the Army's longer-term goals and mission and its day-to-day activities. Subsequent annual performance reports are to report on the degree to which previous performance goals were met. The issuance of the Army's performance reports, due by March 31, represent a new and potentially more substantive phase in the implementation of GPRA—providing the opportunity to assess the Army's actual performance for the previous fiscal year and to consider what steps are needed to improve performance and reduce costs in the future.

Balancing Risk and the Quadrennial Defense Review Framework

With the release of the 2000 QDR, the Office of the Secretary of Defense (OSD) adopted the QDR balanced risk framework. Even as we accept some increased near-term risk as we prepare for the future, the FY 2005 budget also recognizes the advent of unexpected dangers and the need for flexibility. The Army's efforts mirror OSD's efforts.

The challenge is to do three difficult things simultaneously:

(1) Win the GWOT

(2) Prepare for the threats we will face later this decade

(3) Continue transforming for the threats we will face in 2010 and beyond

Any one of these challenges is difficult—and expensive. Taking on all three requires us to make tough choices among competing demands. We are obligated to effectively utilize the taxpayers' dollars and to show taxpayers the Army is willing to eliminate programs that we don't need and refocus funds into areas we do need.

To assist the Secretary and his senior military and civilian advisors in making these strategic trades, we have adopted a risk management framework to guide our decisionmaking in allocating resources. This framework creates a continual feedback loop from the Soldiers in the field to the managers making policy and resource decisions, improving the transparency of our decisionmaking process.

President's Management Agenda

The PMA was announced in the summer of 2001 as an aggressive strategy for improving the management of the Federal Government. It focuses on five key areas where the Government can make the most improvement.

The PMA focuses on the areas where deficiencies were most apparent and where the Government could begin to deliver concrete, measurable results. The Agenda includes five Government-wide initiatives and 10 program-specific initiatives that apply to a subset of Federal agencies. The PMA is helping departments and agencies adopt new disciplines to ensure that their focus on results is effective and enduring. The five key Government-wide initiatives are:

- **Strategic Management of Human Capital**—having processes in place to ensure the right person is in the right job, at the right time, and is not only performing, but performing well
- **Competitive Sourcing**—regularly examining commercial activities performed by the Government to determine whether it is more efficient to obtain such services from Federal employees or from the private sector
- **Improved Financial Performance**—accurately accounting for the taxpayers' money and giving managers timely and accurate program cost information to inform management decisions and control costs
- **Expanded Electronic Government**—ensuring that the Federal Government's $60 billion annual investment in information technology (IT) significantly improves the Government's ability to serve citizens, and that IT systems are secure and delivered on time and on budget
- **Budget and Performance Integration**—ensuring that performance is routinely considered in funding and management decisions, and that programs achieve expected results and work towards continual improvement

For each initiative, the PMA established clear, Government-wide goals or "Standards for Success." Agencies then developed and implemented detailed, aggressive action plans to achieve those goals. Most important, agencies are held publicly accountable for adopting these disciplines. Using a simple grading system of red, yellow, and green, agencies are rated on their status in achieving the overall goals for each initiative and on their progress in implementing their action plans each quarter.

Management Initiative Decisions

In FY 2002, OSD focused its performance management efforts by releasing a series of MIDs. Two of the MIDs released were MID 901 and MID 910.

MID 901 aligned the Office of Management and Budget (OMB) and DoD performance measurement activities (the PMA); the 2001 QDR; and GPRA of 1993. MID 901 assigns responsibility for OSD performance measurement collection and defines how supporting performance information is to be managed and reported. Additionally, MID 901 established a framework for executive-level performance goals and tracking results within OSD. This MID shifts the department's focus to outcome results and aligns the Army with the 2001 QDR Risk Management framework. Finally, MID 901 assigned responsibility for refining and cascading performance metrics to the Component level and required each Component to appoint a GO/SES-level Performance Management Coordinator (PMC). In the Army, the PMC is the Deputy Assistant Secretary of the Army for Cost and Economics.

MID 910 expanded the PMA initiative on Budget and Performance Integration (BPI). It reinforced the effort to cascade responsibility to the Components for implementing the President's Executive Scorecard on the BPI to the Components. It instructed the Components to associate performance metrics with resources in the FY 2004 and succeeding President's Budgets, and to report on metrics for selected programs reported in the FY 2003 President's Budget.

MID 910 directed that each Component be "graded" on its status and progress in displaying the linkage of plans-outputs-resources in budget justification materials; expanding the treatment of metrics in the FY 2004 Congressional justification materials; and establishing a quarterly system reporting on progress towards the performance goals.

The Army has enjoyed measurable successes in the BPI arena. MID 910 directed that each Service account for 60 percent of its programs last year—the Army quantified 71 percent. In the FY 2006 budget, MID 910 required that 81 percent of the Service's programs incorporate performance measures. The FY 2006 Army budget quantifies 97 percent of its programs. These excellent Army results are reflected in the PMA scorecard.

Army Performance Management—Where We are Going

Our goal is "a better Army every day—a relevant and ready campaign-quality force with a Joint and Expeditionary Mindset." The Army is improving its ability to execute its core competencies: (1) training and equipping Soldiers and growing leaders and (2) providing relevant and ready land power as part of the Joint Force. We monitor our progress and take action to remain on track based on our performance management system.

The Secretary of Defense observed that in the 21st century, "new and unexpected danger[s] will likely be waiting just over the horizon and . . . we must be flexible to face them." Meeting and defeating these threats requires the rapid and responsive efforts of the Joint Team. The Army is a critical member of that Team, uniquely able to contribute the complete spectrum of land power capabilities to the Joint Force commander, enabling him to dominate, and to sustain land warfare across the entire operational gamut.

The Army's challenge is to transform doctrine, organizations, processes, and its very culture to better provide essential capabilities to the Joint Force in a prompt and rapid manner. To meet this challenge, we must inculcate a Joint and Expeditionary mindset into every member of the Army team by embracing a forward-leaning, modularly structured, joint-interdependent, and capabilities-based Army led by and composed of aggressive, intelligent, and empowered Soldiers.

We must think of ourselves as vital members of the Joint Team first, and as a Service component second. The Joint Force is capable of sustained interoperability, but must attain joint interdependence as quickly as possible. The Joint Operational Concepts (JopsC) is the blueprint for achieving this posture. The Army is developing and nesting its concepts and capabilities within JopsC to ensure that the U.S. military reaches its goals.

Improving Today's Army
Our first priority is clear—winning the war. Adapting our forces to meet the challenges of the GWOT requires a capabilities-based, modular, flexible, and rapidly employable Joint-Army team. The Joint Force must be capable of dominating any adversary and controlling any situation across the full range of military operations. As a crucial member of this team, the Army must be positioned around the world with the right composition, numbers, and materiel to enable the maximum flexibility, agility, and lethality for operations across the full military spectrum.

In pursuit of these goals, the Army uses performance management to measure and adjust our efforts. The forcing function and intersecting point for all performance management initiatives are guided by OSD's QDR risk framework.

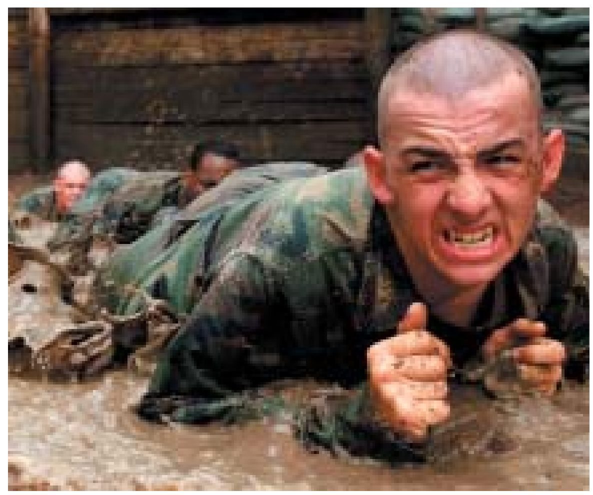
Force Management Risk

Providing trained and ready Soldiers is the business of the Army. To do so, we employ the tools of modern commerce to better manage our military and civilian workforce: more flexible compensation packages, contemporary recruiting and retention techniques, and improved training. Our working and living conditions must enable our people to perform at their best as we seek out and grow the skilled individuals demanded by the Future Force.

Maintain a Quality Force
The tempo of our international commitments has placed an exceptional demand on Active, ARNG, and USAR Soldiers, and that demand will continue for the years ahead. The Army must pursue selected programs to recruit and retain the high-quality Soldiers and civilians necessary to execute our mission. All of our Soldiers are warriors whose actions have strategic impact. Because we will remain at war for the foreseeable future, we must recruit men and women who already have the warrior ethos ingrained in their characters; seek to serve our Nation; and have the endurance and commitment to stay the course of the conflict. They must be confident, adaptive and competent to handle the full complexity of 21st century warfare.

One hundred percent of Soldiers we enlist will hold a high school diploma or equivalent, with no less than 90 percent holding high school diplomas The recruiting/retention goals and accomplishments for the Active Army and ARNG are shown in Table 1 below.

The Army's success at achieving its retention goals are a direct reflection of our quality leadership and our Soldiers' willingness to serve in a time of war. Those Soldiers who were undecided about whether to re-enlist were enticed through the use of retention bonuses. Results of our efforts are shown in Table 2.



Trainees crawl through the mud on an obstacle course during Army Basic Combat Training at Fort Jackson, S.C. This photo appeared on www.army.mil.

Support to Deployed Soldiers
To ease the effects of sustained deployment on our Soldiers, we have made available in-theater and on-location rest and relaxation. We are committed to providing these services as long as our troops remain deployed in the Central Command area of responsibility. Many of these initiatives are not yet

Table 1. Recruiting

	2002 Actual	2003 Actual	2004 Goal	2004 Actual
Active Army	79,585	74,132	77,000	77,587
Army Reserve	41,697	27,365	32,275	32,699
Army National Guard	63,251	84,202	56,002	49,210

Table 2. Active Component Retention

	2002 Actual	2003 Actual	2004 Goal	2004 Actual
First-Term Soldiers	19,433	21,838	23,000	24,903
Mid-Term Soldiers	23,074	19,509	20,292	21,120
Career Soldiers	15,730	12,804	12,808	13,987

quantifiable but include deployment cycle support to both Soldiers in the field and to their families at home; spouse employment; in-state tuition; and ARNG and USAR job centers.

Maintain Reasonable Force Costs

In the past, the term "force cost" has typically referred to military pay and allowances. However, a much broader strategy is needed to capture completely force-related activities, such as entitlements and benefits like health care and educational incentives, which drive overall labor costs. The Army is working with OSD to develop appropriate metrics for assessing the comparative cost of labor. This will improve our management practices and lead to more effective and efficient utilization of resources over the long term.

Shape the Force of the Future

Shaping the force of the future is not represented by any single process or system in the Army. Rather it is accomplished through the myriad daily activities and initiatives discussed throughout this report, such as impeccable training; taking care of Soldiers, their families, and our retirees; restructuring our forces; and spiraling future capabilities into the hands of today's troops. This reshaping includes a rebalance of the mix of Active Component (AC) and Reserve Component (RC) forces to ensure we have the right capabilities at the right place and time. This is a new initiative displayed in Table 3, that will evolve as Base Realignment and Closure (BRAC) decisions are made.

Cadets toss their caps into the air at the conclusion of their graduation ceremony at the United States Military Academy at West Point, N.Y., May 29. This photo appeared on www.army.mil.

Table 3. AC/RC Force Mix*

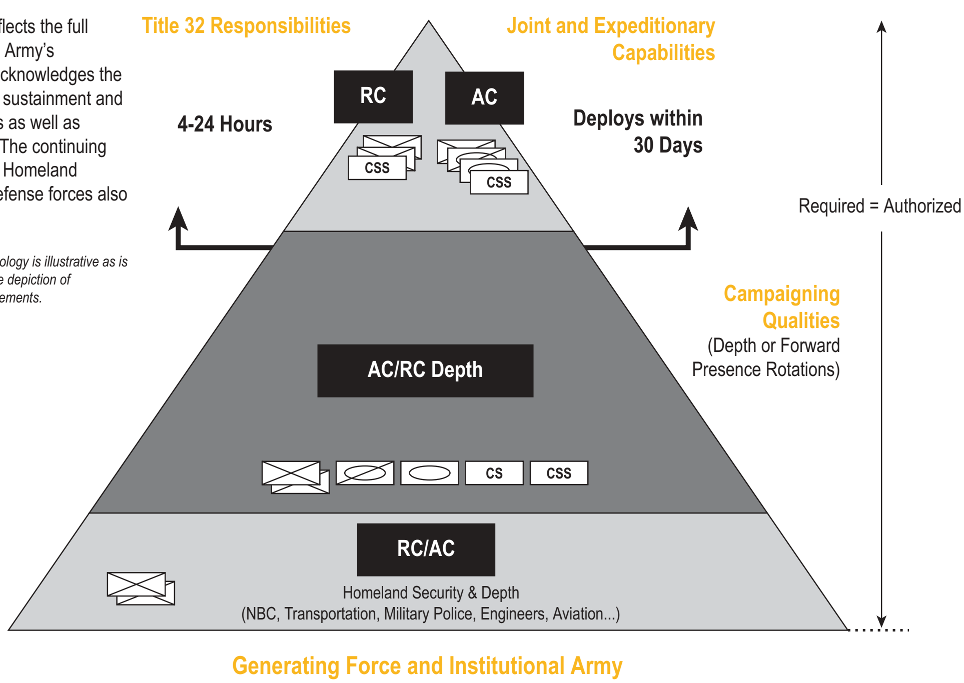
	FY 2004
Goal	4%
Actual	4%

**Represents percent of the force that has been rebalanced*

Figure 3. Structuring the Force

The pyramid reflects the full spectrum of the Army's capabilities. It acknowledges the requirement for sustainment and rotational forces as well as combat forces. The continuing requirement for Homeland Security and Defense forces also is depicted.

Organizational symbology is illustrative as is NOT and all-inclusive depiction of organizational requirements.



The Army plan is to rebalance the mix between Active and Reserve Component force structure and adjusting the quantities of certain military specialties. We expect to realign more than 100,000 positions across the Active and Reserve Components. In response to Secretary of Defense guidance, we already have addressed approximately 10,000 slots. The ARNG is on track to divest about 19,500 spaces from less frequently used force structure, which will help to reallocate resources to critical, high-demand units such as military police and special operations forces. We project that our rebalancing efforts will convert another 80,000 slots of lower-priority force structure, 26,000 of which should be completed in FY 2005.

Operational Risk

The Operational Risk area refers to our ability to overcome today's threats. This includes planning and adapting as events unfold; training for the next real-time mission; and sustaining the warfighters. Our first priority is clear—to win the war on terrorism. Our other priority is to train for war.

The Right Forces Will Be Available

The Army is committed to always providing the Combatant Commander with the land power required to accomplish the mission at hand. With this in mind and in light of today's radically different security environment, we have begun a multi-pronged redesign of our entire force structure as shown in Figure 3.

Our individual units will become more modular, flexible, and responsive, thus creating an array of balanced formations that can meet current and future requirements. This flexibility focuses not only on the Soldier, but on our equipment. In an effort to "lighten" our forces, the Army has begun to deploy the "high-tech" Stryker combat vehicle. Table 4 represents the number of Stryker Brigade Combat Teams (SBCT) structured in accordance with the Army Campaign Plan.

The USAR, in conjunction with Army Headquarters, is re-examining its configuration to determine how best to support the Combatant Commanders. One imperative of the Federal Reserve Restructuring Initiative (FRRI) establishes a Training, Transient, Holdees, and Students (TTHS) account similar to the process used by the Active component. USAR is piloting the TTHS in one command, the 81st Regional Readiness Command (RRC). The THHS initiative is being implemented in phases and will gradually expand to the entire USAR, enabling the USAR to provide the right capabilities to meet emerging mission requirements. The FRRI will be completed by the end of FY 2007, with current progress reported in Table 5.

Our Forces Are Postured to Succeed

In FY 2003, approximately two-thirds of our Active and Reserve combat formations were deployed in more than 120 countries around the world. As a result of the GWOT, we will remain in most of these locations for the foreseeable future.

As part of the effort to make sure that we have the right capabilities in the right place, the Army will continue to enhance the tools we place in our Soldiers' hands. We also are pursuing an aggressive aviation modernization program. Starting in FY 2005, the Army will undertake 19 Apache Longbow

Table 4. Numbers of SBCT Units Structured IAW: The Army Campaign Plan

	FY 2003	FY 2004
Goal	1	2
Actual	1	2

Table 5. USAR Federal Reserve Restructuring Initiative (FRRI)

	FY 2004 Q1	FY 2004 Q2	FY 2004 Q3	FY 2004 Q4
Program*	10%	10%	10%	10%
Actual	11.5%	12.1%	12.8%	13.9%

**Program represents the percentage of a unit desired to be counted against the TTHS personnel account.*

Table 6. OPTEMPO Ground Mileage

	FY 2002	FY 2003	FY 2004 Goal	FY 2004 Actual
Mileage	931	933	899	1,483

Table 7. OPTEMPO Air*

	FY 2002	FY 2003	FY 2004 Goal	FY 2004 Actual
Hours	13.1	15.5	14.5	17.4

** Expressed in average flight hours per crew.*

conversions; will upgrade 5 Black Hawks to the UH-60M configuration; and purchase 27 new UH-60Ls. Additionally, we will buy 4 new CH-47Fs; convert 16 existing CH-47s into F and G models; and procure 160 new, higher-power CH-47 engines. The Army will start a Lightweight Utility Helicopter program as well, under which we will acquire 10 new, off-the-shelf aircraft in FY 2005.

Special Forces Soldiers and a Marine Corps contingent maintain security as a medical evacuation helicopter lands to evacuate wounded Coalition personnel after a combat action south of Camp Blessing, Afghanistan. This photo appeared on www.army.mil.

Our Forces Are Ready

Our Army is adapting and changing dramatically to fight a sustained campaign against a new type of enemy. Our first priority is clear: we will prosecute and win the GWOT. This mindset is essential for the entire Army.

One of the ways we measure our success is by executing our training strategy to the Operational Tempo (OPTEMPO) of our equipment. OPTEMPO dollars are budgeted for training, yet we can report actual execution (for training and combat actions) of mileage driven by our ground vehicles and hours flown by our aircraft. Our training strategy incorporates an appropriate mix of live, virtual, and constructive training. Table 6 and Table 7 display our results for FY 2004.

In FY 2005, we will continue our commitment to fully execute the Active and Reserve Components' ground and air OPTEMPO training plans, which include actual miles driven and hours flown, as well as virtual miles associated with the use of simulators.

Our OPTEMPO is high and will no doubt remain so. Achieving our first priority of fighting and winning the GWOT requires a host of radical paradigm shifts in the way we view the face and nature of our global operating environment, as well as in the way that we conduct operations.

Table 8. Performance Management Agenda Cascaded Army Scores*

	FY 2004 Q1	FY 2004 Q2	FY 2004 Q3
Strategic Management Of Human Capital	R	R	G
Competitive Sourcing	R	R	G
Financial Management	G	G	G
Budget And Performance Integration	G	G	G
E-Government	R	R	R

**Scores cascaded from OSD results. Fourth Quarter Army scores were not available at time of printing.*
Legend: R=red; G=green.

Institutional Risk

The Institutional Risk area focuses on the Army support structure, emphasizing in particular our facilities and infrastructure, and our financial and acquisition processes. Our priorities are to operate efficiently and to streamline those processes.

Streamline Decision Processes, Improve Financial Management

The PMA consists of five Government-wide initiatives to improve management and service to our Nation's taxpayers. The PMA is one of the centerpieces of the Army's performance management initiatives. We have set aggressive targets for the Army in each area, consistent with our objectives of improving accuracy and ensuring that sound management principles are in place across the organization. Using a simple grading scale of red, yellow, and green, agencies are rated on their status in achieving the overall goals; the Army's FY 2004 results are reflected in Table 8.

The Army is committed to profound and far-reaching financial management reform that will guarantee decisionmakers access to reliable, relevant, and timely financial data with which to carefully and efficiently manage and account for taxpayer funds. To do this, the Army is leading the way in DoD efforts to replace antiquated and stand-alone, automated financial management systems with a robust financial management infrastructure. The

Army is following the guidance established by the Business Financial Management Modernization Program Office, which manages the enterprise architecture that links systems and business processes in a comprehensive and integrated fashion. The Army's CFO Strategic Plan outlines our path to improving financial management and correcting material weaknesses in our financial statements.

We also have established the Army Audit Committee to provide a forum to discuss and resolve a wide variety of Federal accounting and auditing issues. The committee is a major component of our efforts to meet the Defense Department's goal of receiving an unqualified audit opinion. We are making progress toward this objective and, by year-end FY 2005, will be ready for an independent audit of the entire financial statement for Army Civil Works, as well as the fund balance with Treasury for the Army General Fund.

Improve Financial Management

The Army has numerous ongoing efforts that will yield significant progress toward quality financial management during FY 2004 and beyond. Two of these initiatives are described below.

Improve The Readiness and Quality of Key Facilities

Support Installations

Installations are essential to maintaining the premier Army in the world—they serve as our flagships. Our short-term planning strategies for installations center on three essential tasks: (1) posturing installations as deployment platforms with robust, reach-back capabilities; (2) adjusting installation support to meet the needs of an Army at war in the midst of transformation; and (3) supporting the well-being of all Soldiers and their families.

Care for Our Solders and Their Families

The Army must support our warfighters and ensure safe living and working conditions. Sustaining a good quality of life is crucial to recruiting, retention, and readiness. Our commitment to improving single-Soldier and family housing is an excellent example of these efforts.

The Army intends to eliminate inadequate family housing by FY 2007 and inadequate permanent-party, single-Soldier housing by FY 2008. The primary vehicle for improving family housing is privatization, specifically the Residential Communities Initiative. So far, over 40,000 homes across multiple installations will have transitioned to privatized operations. In FY 2005 and 2006, we will privatize an additional 71,000 homes on 34 installations. Our aggressive program to improve permanent-party, single-soldier housing has funded the modernization of 75 percent (119,000 spaces) of the requirement. In FY 2005, the Army has programmed $700 million to continue this effort. Our next objective is to upgrade trainee barracks. Progress toward our goal is displayed in Table 9.

Senator Hillary Rodham Clinton (center) breaks ground for new privatized family housing at Fort Hamilton, NY, along with (left to right) Sgt. 1st Class James Gilliam and Dejamison Gilliam; Acting Assistant Secretary of the Army for Installations and Environment Geoffrey G. Prosch; and Mayor Michael R. Bloomberg. To right of the senator is Mrs. James Gilliam and Jalaya Gilliam; Housing Development Corporation President Emily A. Youssouf; and Maj. Gen. Galen Jackman, Military District of Washington commander.

We are in the process of reversing the decay in Army housing, but much remains to be done. Our overall goal is to achieve C-2 quality (minimal impact on mission accomplishment) by 2010, with specific facility types achieving C-1 ratings. The estimated bill to attain C-2 status is $12.1 billion. In FY 2005, the Army has programmed $2.5 billion in sustainment, restoration and modernization funding to stop deterioration and to improve our

Table 9. Eliminate Inadequate Family Housing by 2007*

	FY 2002	FY 2003	FY 2004*
Goal	14,143	13,756	11,522
Actual	14,082	14,196	11,373

**Represents inadequate housing units.*

***FY 2004 "Actual" includes funds for two programmed projects in Europe (208 units) that were not appropriated by Congress.*

facilities; within those funds, sustainment dollars will cover 95 percent of requirements. Reducing the recapitalization rate of facilities also is an indication of improving quality. The FY 2005 recapitalization rate is estimated at 80 years (total Army), compared with 124 years for FY 2004. The Army's goal is to achieve a 67-year recapitalization rate by FY 2008. In addition to recapitalization, the Army is disposing of excess property as directed by BRAC. See Table 10 for FY 2004 results.

Realigning Support for the Warfighter

We have adapted and continue to improve our acquisition and fielding processes to better support the warfighter. In 2002, as Soldiers reported equipment shortages in Afghanistan and elsewhere, the Army implemented the RFI to ensure that all of our troops deploy with the latest available individual equipment. Equipment fielding schedules were revised to support unit-rotation plans, and procurement and fielding cycles were radically compressed, as presented in Table 11.

Seen through a night-vision device, Sgt. Ray Villanueva takes part in a night patrol in Tahrir, Iraq. This photo appeared on www.army.mil.

The RFI is one of the many success stories in the Army. At the start of FY 2004, the planned goals were revised upward to support the soldiers deploying to trouble spots. The Army exceeded the revised goals by 156 percent. The Army is able to do that because it truly cares about equipping our Soldiers with what they need to survive and succeed against our terrorist enemies. More than $100 million has been programmed to continue RFI in FY 2005. Additionally, the Army REF works directly with operational commanders to field equipment solutions at an accelerated rate through the acquisition process. Solutions to operational requirements may include commercial off-the-shelf or near-term developmental items.

Another key performance metric used by the Army to gauge success in supporting the Soldier is Customer Wait Time (CWT). It measures the elapsed time from order to receipt of a material item, which may be obtained from assets on hand at the customer's military installation or naval vessel, or through the wholesale logistics system. For purposes of this enterprise-level metric, CWT includes orders for spare and repair parts requested by organizational maintenance activities. The FY 2005 goal is to reduce CWT to 16 days. Our current year results are in Table 12 below.

Future Challenges Risk

The future challenges risk area addresses the continual process of preparing for an uncertain future. Historically, the Army has evolved to meet the challenges posed by conventional and unconventional threats and the dynamic international landscape. Today, our efforts require a cultural metamorphosis that will forever influence the Army's change process. The purpose is to make our Soldiers

Table 10. Base Realignment and Closure*

	FY 2003	FY 2004**
Goal	100,000	8,818
Actual	100,833	4,971

**Represents acreage disposed of as required by previous BRAC legislation.*

*** Environmental restoration completion taking longer than originally planned which will move the actual transfer past September 30, 2004.*

Table 11. Rapid Fielding Initiative*

	FY 2004 Q1	FY 2004 Q2	FY 2004 Q3	FY 2004 Q4
Planned Goal	4,200	42,350	72,100	119,000
Revised Goal	4,290	42,350	96,600	151,160
Actual	4,296	45,512	104,414	185,814

**Measurement represents numbers of Soldiers.*

Table 12. Customer Wait Time*

	FY 2002	FY 2003	FY 2004 Goal	FY 2004 Actual
Customer Wait Time (Days)	16	21	20	26

**The OSD goal for 2004 was 16 days. The Army goal is higher due to the sheer volume of material being moved into theater.*

and our institutions more innovative, adaptive, and able to meet the challenges of a full-spectrum Joint and Expeditionary environment.

In FY 2005, we will continue to develop collaboratively these emerging joint concepts and architectures, and will nest our own concepts and architectures within them.

The Army Transformation Concept Development and Experimentation Campaign Plan (AT-CDEP) identifies our efforts to support exploration of new joint warfare concepts in concert with the Joint Forces Command Joint Experimentation Campaign Plan. FY 2005 milestones for the AT-CDEP include development of the Unit of Action Combined Arms Training Strategy; Future Combat Systems (FCS) Milestone B update and Capabilities Production Document; FCS Complementary System design; and Unit of Employment organization and pooled-assets design. The Army also will participate in joint and sister service experimentation and demonstration exercises, to include JFCOM's Unified Quest.

Develop More Effective Organizations
The Army has begun the most significant restructuring of forces to occur in the last 50 years. Our new force design will be "brigade-based." Our goal is to increase the number of Active Component brigade combat teams from 33 to 43 by FY 2006. A corollary increase in National Guard brigade teams also is planned. In February 2004, the 3rd Infantry Division began reorganizing as a prototype; it will transition from a three-brigade to a four-brigade division. Through FY 2005, the Army will restructure the 101st Airborne (Air Assault), the 10th Mountain, the 4th Infantry and the 25th Infantry divisions in order to reach 39 brigades. By the end of FY 2006, the Army will comprise 43 brigades. At that point, we will decide whether to continue the process in FY 2007 to achieve a total of 48 brigades in the Active Component. Success will be measured through the Unit Status Reports for these new units. Executing these redesigns on time is critical to maintaining overall force readiness.

Define and Develop Transformational Capabilities
Networking the Force. Key to the success of all future efforts within the Army is the ability to connect and to communicate securely at both the tactical and strategic levels.

The Network Enterprise Technology Command (NETCOM) is implementing an enterprise concept to improve the capacity, performance, and security of Army networks at every level. As part of this effort, in FY 2005 the Army will field Commercially based Satellite Communications (SATCOM) on the move to critical deploying units. This satellite communications system maintains 24/7 communications connectivity, supporting command and control requirements and eliminating gaps in

Figure 4. Joint Tactical Radio System

Future Challenges Risk | Define and Develop Transformational Capabilities

Category	Wave Forms		Cluster 1		Cluster 5	
Performance Characteristics	G	24	Y	2	G	5
Test and Evaluation	G	24	GA	21	GA	3
Logistics Requirements	GA	↓	GA	4	G	5
Cost Performance	Y	14	Y	↓	G	5
Funding	R	2	YA	↓	Y	↓
Schedule Performance	GA	7	Y	↓	Y	3
Contracts	G	2	Y	↓	Y	3
Production	G	24	GA	↓	G	5
Management	GA	23	GA	2	G	5
Interoperability	G	24	G	24	G	5
	POS 77		POS 86		POS 82	

↓ Rating Worsened ↑ Rating Improved

** Numbers indicate the number of months the rating remained unchanged.*

Key Points:
Probability of Success Scores – 77 for Wave Forms, 86 for Cluster 1, 82 for Cluster 5

Description: AFC 11 - Joint Tactical Radio System (JTRS)
The JTRS MAPR compares actual to planned progress as expressed in the Acquisition Program Baseline and other documents.

Parameter:
Green: >80%, Yellow: =>60% to 79%, Red: <60%

Metric: Probability of Success metric is an index of quantitative and external qualitative metrics: requirements, resources, execution, program fit, and program advocacy

Owner: ASA(ALT)

As of September 20, 2004

information flow. Additionally, we will continue redesigning our signal force to match the Unit of Action concept.

The Joint Tactical Radio System (JTRS) and the Warfighter Information Network–Tactical (WIN-T) are two key components of network-centric warfare. During FY 2005, JTRS will remain in the system design and development phase; a Milestone C decision is scheduled for FY 2006, and a multi-service Operational Test and Evaluation in FY 2007. Figure 4 shows the status of JTRS.

The WIN-T moved into the system design and development phase in July 2003. Using modeling and simulation, prototypes will be developed and tested in FY 2005 to support a Milestone C decision in FY 2006, as displayed in Figure 5.

Conclusion

An old Army television commercial used to say, “Freedom Isn’t Free.” No phrase has ever rung more true. For more than 229 years, America has entrusted the Army with its sons and daughters. Soldiers remain the centerpiece of our force, and we are bound by our honor and integrity to give them the best training, leadership and equipment that we can provide.

Whether in Afghanistan, Iraq or anywhere else in the world, our Soldiers continue to demonstrate their superb military skills and their fine personal character. Time and again our land forces provide the versatile and decisive action across the full spectrum of joint operations that enables the United States to succeed.

Our continuing responsibility is to give Soldiers the tools and training needed for the tough missions to which we assign them. There is much to do, and resources are limited. We will use performance management to help us make smarter decisions and to monitor our progress. As we proceed, our environment will change but our performance management processes will enable us to respond effectively.

We have achieved sustainable momentum in Army Transformation, and institutionalizing performance management will serve as a key tool for fielding the Future Force. After three and a half years of undiminished support from the Administration and the Congress, and the incredible dedication of Soldiers and Department of the Army civilians, we have begun to deliver The Army Vision. With continued strong support, we will fight as a joint team to win the GWOT. We will meet our obligations to our friends and allies. We will remain ready to prevail over the unpredictable, and we will transform ourselves for decisive victories on future battlefields.

Figure 5. Warfighter Information Network –Tactical (WIN-T)

Future Challenges Risk | Define and Develop Transformational Capabilities

Category		
Performance Characteristics	G	10
Test and Evaluation	G	10
Logistics Requirements	G	10
Cost Performance	G	10
Funding	Y	↑
Schedule Performance	G	10
Contracts	G	10
Production	G	10
Management 2	G	10
Interoperability	G	10

↓ Rating Worsened ↑ Rating Improved

* Numbers indicate the number of months the rating remained unchanged.

Probability of Success
Score: 88.0%

Description: AFC 18 - Warfighter Info Network Tactical (WIN-T)
The WIN-T MAPR compares actual to planned progress for this developmental system.

Parameter:
Green: >80%, Yellow: =>60% to 79%, Red: <60%

Metric: Probability of Success metric is an index of quantitative and external qualitative metrics: requirements, resources, execution, program fit, and program advocacy

Owner: ASA(ALT)

Analysis of Financial Statements

Throughout FY 2004, the Army General Fund continued to improve upon the myriad processes linked to producing auditable financial statements in compliance with the CFO Act of 1990.

The financial statements were compiled in accordance with guidance issued by the OMB and supplementary guidance provided by DoD. The DoD Office of the Inspector General (IG DoD) was unable to audit the Army General Fund financial statements due to the lack of Army management system adherence to Federal financial management systems requirements and the lack of adequate evidence supporting various material amounts on the financial statements. As a result, the IG DoD did not express an opinion on the Army General Fund Balance Sheet, Statement of Net Cost, Statement of Changes in Net Position, Statement of Budgetary Resources, Statement of Financing, and Statement of Custodial Activity. In his letter to the Chief Financial Officer, the DoD Inspector General identified 13 internal control weaknesses. Army management has initiated actions to correct these weaknesses through the Army CFO Strategic Plan.

The financial statements for the General Fund are presented in a comparative format, providing financial information for FY 2003 and FY 2004.

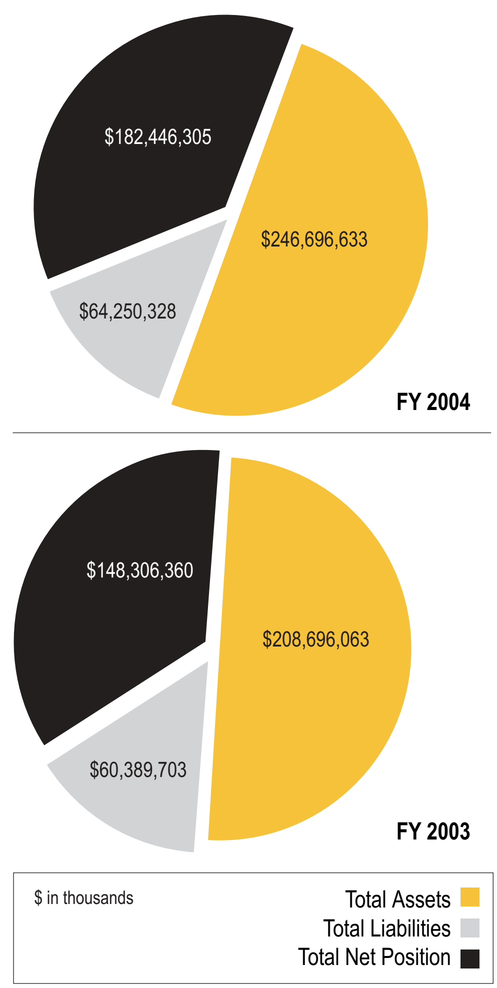
With that in mind, below are the financial highlights of each statement. These highlights focus on significant balances or conditions to help clarify the General Fund's operations. Additional explanatory information may also be found in the notes that accompany these statements.

Balance Sheet

This statement presents the assets, liabilities, and net position of the General Fund as of 30 September 2003 and 2004. As shown in Figure 6, the General Fund assets amounted to $246.7 billion at FY 2004 year-end—over an 18 percent increase from the previous year. Of the total assets, 46 percent of the dollar value resides in the general property, plant, and equipment accounts. Relative to its total assets, the General Fund liabilities are quite low, amounting to $64.3 billion; however, that represents an increase of almost $4 billion or 6 percent. This increase is due primarily to completion of the Army inventory for closed ranges in the environmental liabilities line item, resulting in an 82 percent increase from FY 2003 to $5.8 billion.

The third major component of the balance sheet is net position. In aggregate, the various elements of the net position section on the balance sheet are also referred to as "equity." Equity is the residual interest in the assets of the entity that remains after deducting its liabilities. For FY 2004, the General Fund net position amounted to $182.4 billion, representing over a $34 billion, or 23 percent, increase from FY 2003.

Figure 6. Balance Sheet Results



Statement of Net Cost

This statement presents the annual cost of operating the various General Fund mission operations. To the extent an Army entity generates revenues, these amounts offset gross costs to arrive at the net cost of operations. For FY 2004, program costs amounted to $35.5 billion, representing an 18 percent increase from the previous year. Additionally, program revenues increased 15 percent from FY 2003, climbing to $1.1 billion. Overall for FY 2004, the General Fund achieved a 26.4 percent increase in the net cost of operations, increasing net costs to $135.8 billion—a $28 billion increase from the previous year.

Statement of Changes in Net Position

This statement presents those accounting items that caused the net position section of the balance sheet to change from the beginning to the end of the reporting period. The General Fund saw an increase of $8.6 billion, or nearly 9 percent, in the cumulative result of operations. The Net Position at year-end was $182.4 billion, a 23 percent increase from the previous year.

Statement of Budgetary Resources

This statement provides information on the General Fund's budgetary financing accounts and the status or remaining balances of those accounts at year-end. This includes information on obligation and outlays or actual cash disbursements for the year. In FY 2004, the General Fund had appropriations totaling $149.6 billion, including $53.4 billion in supplemental funds.

Statement of Finance

This is a reconciling statement that tracks the relationship between the proprietary accounts and the budgetary accounts of the General Fund. The Statement of Financing provides data on the total resources provided to the General Fund during the fiscal year and how those resources were used.

The first section of the statement, Resources Used to Finance Activities, shows a total of nearly $142 billion. This is the amount for which the General Fund may have a future liability that would eventually require cash payments.

The second section, Resources Used to Finance Items not Part of the Net Costs of Operations, identifies and adjusts budgetary transactions recorded by the General Fund for changes in the amount of goods, services, and benefits ordered but not received; the costs capitalized on the balance sheet; and financing sources that fund costs of prior periods. For FY 2004, the fund had a negative $21.1 billion in adjustments.

The first two sections are netted together to yield the total resources used to finance the net cost of operations. For FY 2004, total resources used to finance net costs increased 45.8 percent over the previous year and amounted to approximately $121 billion. The largest factor in this increase is attributable to the elimination of the North Atlantic Treaty Organization Security Investment Program liability, which is now being reported by the Defense Agencies.

Finally, the third section, Components of the Net Cost of Operations that will not Require or Generate Resources in the Current Period, is used to adjust the total resources used to finance the net cost of operations (the net amount of the first and second sections) in order to determine the net cost of operations. Thus, sections one and two are reconciled with section three to yield a net cost of operations of $135.8 billion. This amount ties back to the Statement of Net Cost.

Statement of Custodial Activity

FY 2004 was the second presentation of the Statement of Custodial Activity. The statement represents the assets the U.S. Government seized from the Iraqi government during Operation Iraqi Freedom that will be used in support of the Iraqi people. The total disposition of collections decreased over 85 percent, or $691 million, due to disbursements on behalf of the Iraqi people.

Management Integrity

The Army's approach to assuring management control and integrity is anchored in the fundamental philosophy that all commanders and managers have an inherent management control responsibility. The Headquarters Department of the Army (the Integrating Subsystem) functional proponents are responsible for establishing sound management controls in their policy directives and for exercising oversight to ensure compliance with these policies. Commanders and managers throughout the Army are responsible for establishing and maintaining the control and integrity of their operations.

In the 21 reporting years since the inception of the Army's management control process, Army commanders and managers have reported 1,371 material weaknesses to the Secretary. These were the weaknesses remaining after a filtering and value-added reporting process from line managers up through each higher echelon of management. After aggregating similar problems and weeding out lesser issues, the Army reported 231 new material weaknesses to DoD. Only 12 of these remain open. The following is the status of the material weakness:

Open material weaknesses as of September 30, 2003	13
Plus: New material weaknesses identified in FY 2004	1
Less: Material weaknesses corrected in FY 2004	2
Open material weaknesses as of September 30, 2004	12

Weakness Identified During FY 2004

The Army identified one new management control weakness during FY 2004. The following section provides a brief description of the weakness and the target date for correction.

Logistics Asset Visibility and Accountability

The Army does not have adequate visibility over all requisitions, equipment, and supplies transported to, from, and within Theaters of operation, nor across the Army. The supply chain does not effectively support asset visibility and distribution capability in Theaters of operation, nor can it effectively manage and transport the large amount of supplies and equipment deployed to support significant Theater operations such as Operation Iraqi Freedom. Army policies have reduced stock levels and numbers of items carried on prescribed load listings and authorized stockage lists. The result is a lean supply chain without the benefit of either an improved distribution system or an enhanced information system.

A United States Government Accountability Office (GAO) letter dated December 18, 2003, Subject: *Defense Logistics Observations on the Effectiveness of Logistics Activities During Operation Iraqi Freedom* documented the fact that logistics asset visibility, in conjunction with Theater distribution and integrated supply chain, is a material weakness. In addition, these weaknesses were identified in after-action reviews with commanders and Soldiers at deployed sites and supporting personnel involved in the day-to-day support of deployed forces. Forums included the Office of the Deputy Chief of Staff (ODCS) G-4 Class IX Supply Policy Summit General Officer Steering Committee August 4, 2003, and the Combined Arms Support Command (CASCOM) OIF Distribution review March 10-12, 2004.

Radio Frequency Identification (RFID) that tracks assets shipped to and within Theater is now fully supported within DoD and is being expanded and integrated into the Joint Distribution Systems of Record. The use of RFID is being instituted in resident training within Army logistics schoolhouses but still not used in a uniform and consistent manner at the tactical level. The Army has taken measures to improve tactical communications, but many small units do not have continuous assured access to use DoD logistics and asset visibility systems. DoD distribution systems are now linked to the RFID In-Transit Visibility servers and are capable of exchanging data to maintain inside the box content level visibility of shipments. Training has improved for DoD and service personnel on the use of RFID tags and other tracking tools, but is not fully instituted in doctrinal publications for effective asset visibility.

For an extended period of time during Operation Iraqi Freedom, a discrepancy of $1.2 billion worth of supplies existed between what was shipped to Army activities in Theater, and what was acknowledged as received by those activities. The discrepancy is reduced to $375 million. Since this issue surfaced, Army has taken action to implement the Automated Manifest System for throughput and cross-docking management at Theater distribution centers and provided the Standard Army Retail Supply System with an automated transportation receipt capability using RFID. Cannibalization of vehicles in Theater and potential reduction in equipment readiness resulting from unavailability of parts that were either not in the DoD inventory, or which could not be located because of inadequate asset visibility, has been reduced. Some shipments were "pushed" into Theater by Program Managers/Integrated Materiel Management Center, unsolicited by the Command. Shipments consigned to activities in Theater were diverted to an alternate activity.

Distribution of supplies to go forward in Theater is restricted because adequate transportation assets, such as cargo trucks and material handling equipment, are not available early on during Theater operations, when distribution is most critical to success. Distribution of supplies is delayed because cargo arriving in shipping containers and pallets must be separated and repackaged several times for delivery to multiple units in different locations. DoD's lack of an effective process for prioritizing cargo for delivery precludes effective use of scarce Theater transportation assets. Adequate numbers of Army and Marine logistics personnel do not deploy to the Theater until after combat troops arrive and sometimes not until after operations are well under way. In addition, some logistics personnel are not trained on numerous logistics systems, such as operating material handling equipment and managing Theater distribution centers.

The target date for correction of this weakness is the 4th Quarter, FY 2008.

Weaknesses Corrected During FY 2004

The Army corrected two management control weaknesses during FY 2004. The following section provides a brief description of said weaknesses.

Automated Mobilization System

This weakness, while open for 16 years, has faced major challenges during that time, such as restructuring systems, changes in technology, and size of mobilization deployments. The fielding of the Reserve Component Automation System provides the Army Reserve Component mobilization planning, notification, and preparation needs through timely and accurate data.

Army mobilization exercises in 1976, 1978, and 1980 highlighted that the capability did not exist within the Reserve Component (RC) structure (Army National Guard and Army Reserve) for maintaining mobilization essential data, and the ability to respond rapidly to mobilization requirements was lacking. Managers at mobilization stations and transportation agencies did not have access to timely and accurate information necessary for the mobilization decisionmaking process. These mobilization needs were to be originally satisfied through the Continental Army Management Information System (CAMIS) initiated in 1979. In August 1986, the Army restructured this effort as the Reserve Component Automation System (RCAS) and in February 1988, the RCAS Project was assigned to the Chief, National Guard Bureau (CNGB). In FY 1995, the RCAS Project was restructured to constrain cost growth, establish a realistic requirements baseline, and leverage new information management technology. The approved Mission Need Statement (April 1996), Critical Operational Issues and Criteria (COIC) Document (April 1996), and Operational Concept Description (OCD) (April 1996) tasked the Project to satisfy the Army RC's mobilization planning, notification, and preparation needs (phases 1-3 of the Army's Mobilization Process). Mobilization phases 4 and 5 (validation and deployment) were not within the scope of the restructured Project's charter. RCAS will satisfy the automation requirements of the RC for day-to-day operations and will significantly enhance their mobilization preparedness and mobilization execution capability. It provides timely and accurate data that can be accessed at the various echelons to support commanders, staffs, and functional managers in the mobilization planning and administration of RC forces. This material weakness was corrected in 4th Quarter, FY 2004, after U.S. Army Audit Agency (USAAA) validated the effectiveness of our corrective actions.

Army Purchase Card Program
GAO identified a lack of adherence by field activities to established purchase card internal controls. Although no substantial instances of fraud, waste, or abuse were identified, an environment existed that could have easily fostered fraud. As a result, GAO has expanded the audit to include a review of the Army and other DoD components.

The Army has positively addressed every GAO finding regarding the Army Purchase Card Program. To correct this problem, the Office of the Assistant Secretary of the Army (Acquisition, Logistics and Technology) has aggressively sought to establish positive controls in areas of weaknesses found. This material weakness was corrected in 2nd Quarter, FY 2004, after USAAA validated the effectiveness of our corrective actions.

Previously Reported Weaknesses

The Army reported five weaknesses last year that it had expected to close during FY 2004. Various circumstances prevented this from happening. The following sections provide a brief description of each weakness and the revised target date for correction.

Financial Reporting of Real Property
The Army's real property database does not allow for depreciation, and subsequent entries in dollar values override previous dollar values with no audit trail of transactions.

The attempted solution of the Defense Property Accountability System (DPAS) interface with Integrated Facilities System (IFS) did not work for Real Property financial statement reporting. In addition, data mismatches and negative numbers from IFS were not allowed in DPAS, which resulted in dollar values being overridden and audit trails being lost. The decision was made to discontinue the DPAS interface and to modify IFS to calculate depreciation and run financial reports directly from each site. In October 2002, the Army requested a waiver from OSD to modify IFS to process and capture financial statement information. OSD approval was received in May 2003 for making IFS modifications. The current target date for correction of this weakness is 2nd Quarter, FY 2005, with the release of IFS Skip 16, and USAAA validation.

Reserve Component Mobilization Accountability
Lack of synchronization exists among automated management tools available to ensure Reserve Component (RC) mobilization accountability. Interagency accountability must provide better integrated management controls for tracking RC personnel in the "mobilization pipeline." Of particular concern is the tracking of RC personnel from home station to mobilization station to duty station, through deployment, redeployment, and demobilization or release from active duty. This challenge is further complicated for personnel in a medical hold status remaining on active duty on an original HQDA mobilization order after demobilization of the parent unit.

Additionally, the use of Derivative Unit Identified Codes (DUIC) has exacerbated force tracking. Limitations imposed by dual military pay systems (Defense Joint Military Pay System—Active Component (DJMS-AC) and Defense Joint Military Pay System—Reserve Component (DJMS-RC)) also impairs accountability of mobilized personnel.

The current target date to correct this weakness is 4th Quarter, FY 2006.

Contract Administration of Service Contracts
The USAAA identified a significant weakness in administering service contracts. Service contracts represent an ever-increasing percentage of the overall contract dollars and now have surpassed the dollars awarded under major weapon systems programs.

Significant audit findings include ineffective planning for quality assurance requirements. Although contracting officers generally appointed quality assurance personnel for contracts, they often did not adequately train the quality assurance personnel about their responsibilities and limitations of authority. They also did not make sure evaluators were versed in proper quality assurance procedures and that the quality assurance evaluators understood specific contract requirements.

In addition, there was a lack of surveillance plans overall, resulting in the lack of a systematic inspection system and ineffective documentation of contract performance. Proper quality assurance procedures require surveillance plans that serve as roadmaps for monitoring contractor performance. This is a key element of establishing strong internal controls that ensure the Army receives value for its service contracting dollar. Due in part to the lack of documentation, procedures for validating and approving contractor invoices sometimes were not adequate. In addition, responsibilities and processes for approving invoices were not properly defined.

Several Major Army Commands (MACOMs) have actions ongoing to improve various aspects of contract administration. These actions are steps in the right direction but an overall strategy for administering service contracts is needed. The current target date to correct this weakness is 3rd Quarter, FY 2005, after the USAAA has validated the effectiveness of our corrective actions.

Financial Reporting of General Equipment

The Army does not currently meet Federal Accounting Standards for the financial reporting of General Equipment. This Standard requires Federal agencies to present fairly the cost and depreciation of these assets in their financial statements.

To meet the requirements of this Standard, the Army fielded DPAS, a CFO Act-compliant system for reporting Real Property and General Equipment. DPAS replaced noncompliant systems to bring the Army into compliance with Federal Accounting Standards. Failure to meet this standard for financial reporting does not mean the Army lacks property accountability. However, the Army's inability to identify an item's acquisition date and cost prevents the computation of depreciation and the determination of value for financial reporting. The current target date to correct this weakness is 1st Quarter, FY 2006, after the USAAA has validated the effectiveness of our corrective actions.

Information Systems Security

There is widespread recognition that the Army's unclassified automated information systems and telecommunications networks have been attacked and successfully penetrated by unauthorized personnel. These intrusions have led to the identification of systemic deficiencies in systems and network security design and implementation; incident response, containment, and implementation of countermeasures; Information Systems Security education, training, awareness; and professional development.

The decisiveness, effectiveness, and potential safety of the warfighter in attaining national security objectives is at risk because sustaining base information systems and networks have proven to be highly vulnerable to malicious attack. Not only is the information processed and transmitted throughout the Army's systems vulnerable to compromise and exploitation by hostile forces, but also control of the information systems and networks themselves could easily be lost to hostile forces during a national crisis.

To correct these weaknesses, Army leadership has, in the Command and Control (C2) Protect Program Management Plan, outlined the measures that Army leadership will undertake to ensure the Army's portion of the Defense Information Infrastructure is adequately protected. The C2 Protect Program Management Plan is designed to manage and control the growth of C2 Protect initiatives, is in consonance with the Army Enterprise Strategy, and supports the Defense Information Warfare efforts. It had been developed to address the identified weaknesses, and had been formally signed by the Office of the Deputy Chief of Staff, (ODCS), G-3, the Chief Information Officer (CIO)/G-6, and the ODCS, G-2. The current target date for correcting this weakness is 2nd Quarter, FY 2005, after the USAAA has validated the effectiveness of our corrective actions.

Future Effects of Existing Conditions

Force Management Risk

Critical to Transformation is the need to determine the mix of civilian, military, and contractor personnel that will best assure the Army's success. This determination must include an assessment of core competencies across the full spectrum of military operations. As the Army seeks to increase its "tooth–to-tail" ratio, it must carefully weigh the important roles played by combat support and combat service support personnel. There is a temptation to reduce the number of personnel that perform these roles in order to convert their positions to combat roles, but there are some essential support positions that must be retained and filled by military personnel. Logistical support to the troops in combat in particular must not be compromised.

While many support tasks can be outsourced, the Army must ensure that it can meet the demands of "the last logistical mile." In many instances, it would not be appropriate to rely on contractors or civilian employees to perform these tasks. The Army must therefore balance the economic gains of outsourcing against the need to ensure that the military force structure can deliver the necessary logistics on the battlefield. Selecting the right structure for a force of nearly 500,000 is a complex task involving many tradeoffs. The challenge facing the Army is to determine precisely the core competencies it requires to sustain combat operations and to ensure that it retains the right mix of combat and support troops.

Operational Risk

The Army's current force is very similar to that of the Army that 13 years ago fought so decisively in Desert Storm. In the intervening years the nature of the threat facing America has evolved. The force that deployed in the first Gulf War was developed under a strategy that envisioned a scenario of two simultaneous major regional conflicts. Instead, the 2001 terrorist attacks on America introduced an enemy that would employ asymmetrical warfare to avoid our strengths and attack our vulnerabilities. It is difficult to assess exactly what form future threats will take. As a consequence, the Army has moved away from a threat-based force and is intent on building a capabilities-based force equipped to function across the full spectrum of military operations.

Identified as the Objective Force, this new force will fight in a noncontiguous manner and will be capable of rapid deployment in a crisis either to fight or ideally to deter conflict. It will have the capability of being projected anywhere in the world—not just to easily accessible areas with multiple air and seaports, but also to remote, landlocked, and infrastructure-poor areas. The importance of this capability was demonstrated in Afghanistan, where the rapid engagement of U.S. forces contrasted dramatically with the long build-up that preceded Desert Storm. Failure at this point to develop this capability to project sustainable combat power anywhere in the world—that is, failure to realize the Objective Force—could leave America's worldwide interests vulnerable to attack.

Institutional Risk

The Army must make the best use of its resources in its day-to-day operations. This requires that it transform its business practices to improve its financial management and that it streamline its infrastructure.

Business practices have in the last decade changed fundamentally, leading to significantly greater productivity, lower costs, and higher-quality outputs. The Army has not kept pace. To free up resources that can be applied to the fielding of the Objective Force, we must transform how we do business. Many functional activities need to be examined and improved, streamlined, or eliminated. This requires imagination and innovation.

It is essential to the effort to reduce costs and increase productivity that Army leaders and managers be supplied with reliable information. The Army's inability thus far to achieve an unqualified audit opinion on its financial statements indicates that the information that our leaders are given is not reliable, with the result that Army resources are not being used to their best effect. The Army estimates that 80 percent of the data found in its financial systems comes from functional area systems such as logistics, personnel, acquisition, and other systems. Realizing the capability to deliver reliable information will require the integration of these functional management systems with financial management systems. Until this is done, the Army will continue to be at risk of suboptimizing its use of resources.

Advancing the President's Management Agenda

The PMA provides a route to greater efficiency and the means whereby the Army can identify the actions it must take to improve management performance at all levels. In the same way that the Army is reinventing itself as a modular force, it is changing the way that it conducts the business of supporting that force.

The PMA contains five Government-wide goals designed to improve Federal management and to deliver results that matter to the American people. They reflect the Administration's commitment to achieve immediate, concrete, and measurable results. The five goals, which are being pursued in advance of, not instead of, other necessary management improvements, are mutually reinforcing. For example:

- Workforce planning and restructuring undertaken as part of the Strategic Management of Human Capital will be defined in terms of each agency's mission, goals, and objectives—a key element of Budget and Performance Integration.
- Agency restructuring is expected to incorporate organizational and staffing changes resulting from competitive sourcing and Expanded E-Government.

Efforts toward Budget and Performance Integration will reflect improved program performance and savings achieved from Competitive Sourcing and will benefit from the financial and cost-accounting and information systems that are part of the effort to realize improved financial management.

A description of how the Army is undertaking each of the five Government-wide goals is contained in the following sections.

Strategic Management of Human Capital

A key element of successful personnel management is providing people with information and trusting them to use it to the benefit of the organization as a whole. The Army is taking steps to empower its Soldiers and civilian employees with greater knowledge.

- The Army is integrating civilian workforce issues into Joint, DoD, and Army strategic planning efforts. In addition, the Army is participating in Total Army Analysis in support of Army planning efforts to forecast and achieve the Civilian Future Force based on future missions. We are developing a CHR strategic plan fully cascaded with the OASA (M& RA)/ Army G1 and OSD strategic plans. Furthermore, the Army is synchronizing revisions to the strategic plan with budget and legislative cycles.
- During FY 2004, the Army conducted a series of Town Hall meetings and Focus Group sessions to obtain input for consideration in the National Security Personnel System (NSPS) design process. As key members of the NSPS Design Work Groups, the Army developed an NSPS Change Management Strategy that includes methods for assuring that managers have the skills necessary for the desired performance.
- The Army served as the Executive Agent for the Coalition Provisional Authority, a DoD initiative in support of the GWOT.
- We responded to the emerging business need for providing expert recruitment services, obtaining required exceptions, and developing and implementing business processes.
- The Army provided operations and advisory assistance to CPA officials in identifying manpower requirements, making selections, and conducting assessments.
- We established a link to the Support Our Friends in Iraq and Afghanistan (SOFIA) website on the Civilian Personnel On Line web page.
- The Army collaborated with OPM to feature the SOFIA link prominently on their employment page.
- Senior Executive Service (SES) performance

standards are being tailored to reflect the Army's mission, goals, and outcomes. Success is defined as personal accomplishment supporting desired agency outcomes. A recent review by Army Commands with SES personnel management responsbilities found more than 80 percent of their SES personnel's performance plans were linked to agency mission and goals. From that, the Army has extrapolated that at least that percentage of compliance exists at management levels subordinate to those SES members. Periodic monitoring of SES personnel performance plan linkage to mission, goals, and outcomes will be conducted by the Civilian Personnel Evaluation Agency during scheduled human resource management functional reviews. During FY 2004, Army representatives also participated in NSPS workgroups on Performance Management. A major focus of the group was recommending performance design features in NSPS that will further tie accomplishments to agency mission.

Competitive Sourcing

Many of the tasks performed by Government employees can be contracted out to the commercial marketplace, often at savings in a range of 20 to 50 percent. The Army continues to lead DoD in seeking savings by outsourcing non-core functions. Successful outsourcing will also contribute to the efforts to fully man combat units while preserving the institutional Army.

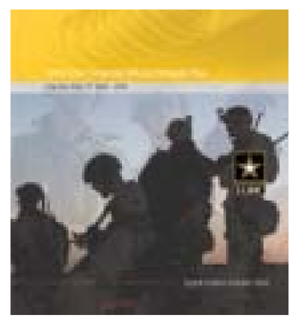
- The Army has 1,461 Army Corps of Engineers (USACE) Information Technology (IT) positions and 55 Public Works positions announced for competition in FY 2004 under the revised OMB Circular A-76. The USACE began the IT competition in June 2004 with public announcement in the FedbizOpps.gov. This is the first OSD competition under the revised 29 May 2003 OMB Cir A-76. Forthcoming is the Fort McCoy Directorate of Information Management competition of 57 positions. The Army is currently coordinating a memorandum with the Army Staff directing major commands and field operating agencies to submit their plans for conducting public-private competitions for FY 2005 through FY 2008 on 43,661 remaining positions from Program Budget Decision No. 729.

Improved Financial Performance

During FY 2004, the Army built upon a number of initiatives began in FY 2003 that will enable the Army to make better use of its funds. The Army is also pursuing other long-term initiatives aimed at putting more useful and more reliable financial information in the hands of managers, with the aim of enabling them to make more efficient use of resources.

CFO Strategic Plan

Army leaders, as they work to comply with myriad financial management mandates, must do so within the context of the Army vision. To successfully achieve this vision, the Army must have sufficient resources with which to take care of its Soldiers, ensure near-term readiness, and transform itself for the 21st century. The CFO Strategic Plan was developed in recognition of the fact that high-quality financial information is one of the foundations upon which the Army's vision will be built. The CFO Strategic Plan is an Army-wide management plan designed to synchronize efforts across the Army's functional areas to integrate processes and systems while improving upon the quality of management information.



The plan involves 14 cross-functional Army organizational elements, as well as the Defense Finance and Accounting Service (DFAS), the OSD (Comptroller), and the IG DoD. Using a five-year planning horizon, the CFO Strategic Plan identifies the steps each organizational element must take to integrate fully all financial and nonfinancial processes and systems that impact Army resources. The Army's ability to produce high-quality financial information for reporting will provide the public with greater confidence that the Army has accountability over its resources. Achieving greater accountability requires that all assets and liabilities, revenues and expenses, and the full costs of programs and activities be consistently, completely, and accurately recorded, monitored, and reported.

The Army will use the latest technology to develop flexible, streamlined procedures and processes that will provide the type of information that will enable sound decisionmaking. The financial management and functional communities are identifying unnecessary systems that may be eliminated and those essential systems that must be retained and brought into compliance with all statutory, regulatory, and audit requirements. The DoD Business Management Modernization Program (BMMP) is also working with the Army to identify these systems, to map processes, and to determine an optimal architecture for the future. The CFO Strategic Plan will in this way assist in the coordination and execution of Army efforts in support of BMMP initiatives.

By effectively integrating the financial processes and systems with the many other functional processes and systems that affect a commander's resources, we can provide our commanders with relevant and reliable information on the availability of funds. With this information, commanders will be better positioned to accurately assess their ability to train and maintain their forces and will be better able to articulate to the chain of command the financial costs and benefits associated with the options available to them.

Expanded Electronic Government

The PMA asserts that the Government can leverage electronic technoloigies both to reduce costs and provide better service. The Army accordingly is pursuing a number of electronic initiatives aimed at providing better service to its Soldiers and civilian employees.

Major Army IT investments are reviewed for cost, schedule, and performance goals of less than 10 percent based on a variety of analyses, including: CIO Assessments, Approved Acquisition Program Baselines, Approved Acquisition Decision Memorandum, and Monthly Major Acquisition Program Reviews. In addition, the Army submitted 43 Exhibit 300 reports to the OMB as part of the FY 2005 President's Budget (PB05), which include reporting on cost, schedule, and performance goals. As of the PB05 submission, all major IT investments have cost and schedule overruns that average less than 10 percent and performance shortfalls that average less than 10 percent. The Army continues to monitor the cost, schedule, and performance goals for major IT investments and will submit updated Exhibit 300 reports in September to the OMB for the FY 2006 Budget Estimate Submission.

Budget and Performance Integration

Improvements in the management of human capital, competitive sourcing, and financial performance, and expanding electronic government will matter little if they are not linked to better results. Everyone agrees that scarce federal resources should be allocated to programs and managers that deliver results. Budget Performance Integration supports the principles of transparency, accountability, efficiency and effectiveness in government. Current cost documents already contain some performance information, but the Army will increase the quantity of performance measures and use the same measures to link all documents. Future documents will provide evidence of results achieved for funds invested. Ultimately this process will hold managers accountable for expenditures. To that end, the PMA directed government agencies to associate performance measures with their budgets. The Army has seen the value of developing budget performance measures and using them to assist the leadership with difficult resourcing decisions. The Army recently approved performance measures for 80 percent of its FY06 President's Budget submission and is in the process of reviewing and refining measures for the remaining resources. The Army plans to continue it development of Budget Performance Integration measures and their use in execution and program review. These measures can be mapped via the Resource Framework to the objectives in the DoD Balanced Scorecard.

The Army's measures in the ADR are linked to the DoD Balanced Scorecard and the QDR. During the Fourth Quarter the Army has made a concentrated effort to refine its ADR measures, clarify verification and validation sheets specified by OMB Circular A-11, and populate the measures with data. The Army PMC briefs the Army Executive Council quarterly on the progress of the measures in the ADR. As of the latest briefing, the Army had validated 68 measures and populated 58 of 76 measures in the ADR. Eight new measures remain under development. The Army will report the same measures in the annual Performance Accountability Report, the annual Financial Statement, and quarterly financial briefings to OSD. The Army is working to improve linkage of the ADR measures with The Army Plan and the Army Balanced Scorecard.

Learn More About America's Army

http://www.army.mil

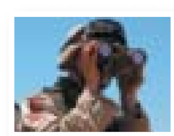
General Fund Introduction Page Photos

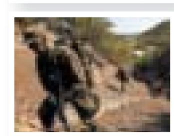
[Large Photo]
A Soldier uses binoculars to look for enemy activity while providing security at a checkpoint in Ba'qubah, Iraq, while helping to restore stability to the city following an outbreak of violence. This photo appeared on www.army.mil. By Staff Sgt. Klaus Baesu

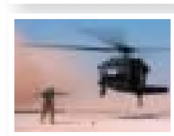
[Top Inset Photo]
Soldiers from the Army's 166th Infantry, 2nd Battalion, Charlie Company, conduct a dismounted patrol in Guantanamo Bay, Cuba. DoD photo by Chief Petty Officer John F. Williams, U.S. Navy.

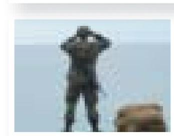
[Middle Inset Photo]
A Soldier of the 101st Airborne Division's 159th Aviation Brigade guides a UH-60 Black Hawk helicopter ambulance to a landing during a medical evacuation training mission near Mosul, Iraq. U.S. Army photo by Spc. Kieran Moore.

[Botton Inset Photo]
An infantryman scans the Caribbean Sea while conducting a dismounted patrol of the Camp Delta perimeter in Guantanamo Bay, Cuba. The Soldier is assigned to Company C, 1st Battalion, 181st Infantry Regiment, 29th Infantry Division, Massachusetts Army National Guard. Photo courtesy of the Department of Defense.









General Fund Principal Financial Statements, Notes, and Supplementary Information

Limitations

Limitations of the Financial Statements

The financial statements have been prepared to report the financial position and results of operations for 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 the formats prescribed by the 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.

To the extent possible, the financial statements have been prepared in accordance with federal accounting standards. At times, the Department is unable to implement all elements of the standards due to financial management systems limitations. The Department continues to implement system improvements to address these limitations. There are other instances when the Department's application of the accounting standards is different from the auditor's application of the standards. In those situations, the Department has reviewed the intent of the standard and applied it in a manner that management believes fulfills that intent.

The statements should be read with the realization that they are for a component of the United States Government, a sovereign entity. One implication of this is that the liabilities cannot be liquidated without legislation that provides resources to do so.

Limitations Concerning National Defense Property, Plant and Equipment

The Federal Accounting Standards Advisory Board (FASAB) revised the Statement of Federal Financial Accounting Standards No. 6 to require the capitalization and depreciation of military equipment (formerly National Defense Property, Plant and Equipment/ND PP&E) for fiscal years (FY) 2003 and beyond, and encouraged early implementation.

Department of Defense- Department of the Army

CONSOLIDATED BALANCE SHEET

As of September 30, 2004 and 2003 ($ in Thousands)

ASSETS (Note 2)	**2004 Consolidated**	**2003 Consolidated**
Intragovernmental:		
Fund Balance with Treasury (Note 3)		
Entity	$89,297,373	$54,695,897
Non-Entity Seized Iraqi Cash	113,430	278,139
Non-Entity-Other	137,806	61,443
Investments (Note 4)	1,496	1,231
Accounts Receivable (Note 5)	461,867	523,347
Other Assets (Note 6)	556,380	83,474
Total Intragovernmental Assets	$90,568,352	$55,643,531
Cash and Other Monetary Assets (Note 7)	$1,525,090	$954,368
Accounts Receivable (Note 5)	492,394	514,579
Loans Receivable (Note 8)	0	0
Inventory and Related Property (Note 9)	37,647,721	32,676,658
General Property, Plant and Equipment (Note 10)	113,111,572	115,337,906
Investments (Note 4)	0	0
Other Assets (Note 6)	3,351,504	3,569,021
TOTAL ASSETS	$246,696,633	$208,696,063
LIABILITIES (Note 11)		
Intragovernmental:		
Accounts Payable (Note 12)	$1,706,731	$1,084,965
Debt (Note 13)	0	0
Environmental Liabilities (Note 14)	0	0
Other Liabilities (Note 15 & Note 16)	2,402,903	1,670,318
Total Intragovernmental Liabilities	$4,109,634	$2,755,283
Accounts Payable (Note 12)	$9,460,194	$9,089,097
Military Retirement Benefits and Other Employment-Related Actuarial Liabilities (Note 17)	1,632,843	1,761,318
Environmental Liabilities (Note 14)	40,366,172	37,395,412
Loan Guarantee Liability (Note 8)	12,293	1,273
Other Liabilities (Note 15 and Note 16)	8,669,192	9,387,320
Debt Held by Public	0	0
TOTAL LIABILITIES	$64,250,328	$60,389,703
NET POSITION		
Unexpended Appropriations (Note 18)	$73,238,304	$47,674,714
Cumulative Results of Operations	109,208,001	100,631,646
TOTAL NET POSITION	$182,446,305	$148,306,360
TOTAL LIABILITIES AND NET POSITION	$246,696,633	$208,696,063

Department of Defense- Department of the Army

CONSOLIDATED STATEMENT OF NET COST

As of September 30, 2004 and 2003 ($ in Thousands)

	2004 Consolidated	2003 Consolidated
Program Costs		
Intragovernmental Gross Costs	$35,460,140	$30,100,949
(Less: Intragovernmental Earned Revenue)	(7,388,378)	(6,519,008)
Intragovernmental Net Costs	$28,071,762	$23,581,941
Gross Costs With the Public	108,861,815	84,768,855
(Less: Earned Revenue From the Public)	(1,152,055)	(919,139)
Net Costs With the Public	$107,709,760	$83,849,716
Total Net Cost	$135,781,522	$107,431,657
Cost Not Assigned to Programs	0	0
(Less: Earned Revenue Not Attributable to Programs)	0	0
Net Cost of Operations	$135,781,522	$107,431,657

Department of Defense- Department of the Army

CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION

As of September 30, 2004 and 2003 ($ in Thousands)

	2004 Consolidated	2003 Consolidated
CUMULATIVE RESULTS OF OPERATIONS		
Beginning Balances	$100,631,646	$5,790,837
Prior period adjustments (+/-)		
Prior Period Adjustments - Restated (+/-)	0	0
Beginning Balance, Restated	100,631,646	5,790,837
Prior Period Adjustments - Not Restated (+/-)	0	97,897,585
Beginning Balances, as adjusted	$100,631,646	$103,688,422
Budgetary Financing Sources:		
Appropriations received	0	0
Appropriations transferred-in/out (+/-)	0	0
Other adjustments (rescissions, etc) (+/-)	0	0
Appropriations used	127,335,114	106,904,931
Nonexchange revenue	5,143	131
Donations and forfeitures of cash and cash equivalents	4,663	15,003
Transfers-in/out without reimbursement (+/-)	13,189,641	479,218
Other budgetary financing sources (+/-)	2,540,445	(3,636,630)
Other Financing Sources:		
Donations and forfeitures of property	0	0
Transfers-in/out without reimbursement (+/-)	400,794	(321,356)
Imputed financing from costs absorbed by others	882,077	818,482
Other (+/-)	0	115,102
Total Financing Sources	$144,357,877	$104,374,881
Net Cost of Operations (+/-)	135,781,522	107,431,657
Ending Balances	$109,208,001	$100,631,646
UNEXPENDED APPROPRIATIONS		
Beginning Balances	$47,674,714	$31,468,721
Prior period adjustments (+/-)		
Prior Period Adjustments - Restated (+/-)	0	0
Beginning Balance, Restated	47,674,714	31,468,721
Prior Period Adjustments - Not Restated (+/-)	0	0
Beginning Balances, as adjusted	$47,674,714	$31,468,721
Budgetary Financing Sources:		
Appropriations received	149,547,719	117,667,977
Appropriations transferred-in/out (+/-)	4,745,349	6,042,747
Other adjustments (rescissions, etc) (+/-)	(1,394,364)	(599,800)
Appropriations used	(127,335,114)	(106,904,931)
Nonexchange revenue	0	0
Donations and forfeitures of cash and cash equivalents	0	0
Transfers-in/out without reimbursement (+/-)	0	0
Other budgetary financing sources (+/-)	0	0
Other Financing Sources:		
Donations and forfeitures of property	0	0
Transfers-in/out without reimbursement (+/-)	0	0
Imputed financing from costs absorbed by others	0	0
Other (+/-)	0	0
Total Financing Sources	$25,563,590	$16,205,993
Net Cost of Operations (+/-)	0	0
Ending Balances	$73,238,304	$47,674,714

Department of Defense- Department of the Army

COMBINED STATEMENT OF BUDGETARY RESOURCES

As of September 30, 2004 and 2003 ($ in Thousands)

	BUDGETARY FINANCING ACCOUNTS		NON-BUDGETARY FINANCING ACCOUNTS	
BUDGETARY RESOURCES	**2004 Combined**	**2003 Combined**	**2004 Combined**	**2003 Combined**
Budget Authority:				
Appropriations received	$149,559,892	$117,695,530	$0	$0
Borrowing authority	0	0	0	0
Contract authority	0	0	0	0
Net transfers (+/-)	2,517,085	5,307,441	0	0
Other	0	0	0	0
Unobligated balance:				
Beginning of period	8,212,989	5,858,110	1,272	730
Net transfers, actual (+/-)	4,698,264	1,214,524	0	0
Anticipated Transfers Balances	0	0	0	0
Spending authority from offsetting collections:				
Earned	0	0	0	0
Collected	18,739,994	14,095,736	152	543
Receivable from Federal sources	412,742	12,974	0	0
Change in unfilled customer orders	0	0	0	0
Advance received	306,576	119,338	0	0
Without advance from Federal sources	1,896,851	3,655,318	0	0
Anticipated for the rest of year, without advances	0	0	0	0
Transfers from trust funds	0	0	0	0
Subtotal	$21,356,163	$17,883,366	$152	$543
Recoveries of prior year obligations	13,996,679	8,001,403	0	0
Temporarily not available pursuant to Public Law	0	0	0	0
Permanently not available	(1,394,364)	(1,304,580)	0	0
Total Budgetary Resources	$198,946,708	$154,655,794	$1,424	$1,273

STATUS OF BUDGETARY RESOURCES	BUDGETARY FINANCING ACCOUNTS 2004 Combined	BUDGETARY FINANCING ACCOUNTS 2003 Combined	NON-BUDGETARY FINANCING ACCOUNTS 2004 Combined	NON-BUDGETARY FINANCING ACCOUNTS 2003 Combined
Obligations incurred:				
Direct	$152,590,936	$128,012,383	$0	$0
Reimbursable	23,475,016	18,430,419	0	0
Subtotal	$176,065,952	$146,442,802	$0	$0
Unobligated balance:				
Apportioned	21,458,641	6,947,148	1,424	1,273
Exempt from apportionment	13,411	25,665	0	0
Other available	0	0	0	0
Unobligated Balances Not Available	1,408,704	1,240,179	0	0
Total, Status of Budgetary Resources	$198,946,708	$154,655,794	$1,424	$1,273
Relationship of Obligations to Outlays:				
Obligated Balance, Net - beginning of period	$46,482,855	$33,662,267	$0	$0
Obligated Balance transferred, net (+/-)	0	0	0	0
Obligated Balance, Net - end of period:				
Accounts receivable	(1,893,446)	(1,480,706)	0	0
Unfilled customer order from Federal sources	(12,713,171)	(10,816,319)	0	0
Undelivered orders	56,509,574	44,735,892	0	0
Accounts payable	15,119,442	14,043,988	0	0
Outlays:				
Disbursements	149,220,137	121,952,521	0	0
Collections	(19,046,568)	(14,215,073)	(152)	(543)
Subtotal	$130,173,569	$107,737,448	($152)	($543)
Less: Offsetting receipts	(63,289)	(95,571)	0	0
Net Outlays	$130,110,280	$107,641,877	($152)	($543)

Department of Defense- Department of the Army

COMBINED STATEMENT OF FINANCING

As of September 30, 2004 and 2003 ($ in Thousands)

Resources Used to Finance Activities:	**2004 Combined**	**2003 Combined**
Budgetary Resources Obligated		
Obligations incurred	$176,065,951	$146,442,802
Less: Spending authority from offsetting collections		
and recoveries (-)	(35,352,991)	(25,885,311)
Obligations net of offsetting collections and recoveries	$140,712,960	$120,557,491
Less: Offsetting receipts (-)	(63,289)	(95,571)
Net obligations	$140,649,671	$120,461,920
Other Resources		
Donations and forfeitures of property	0	0
Transfers in/out without reimbursement (+/-)	400,794	(321,356)
Imputed financing from costs absorbed by others	882,077	818,482
Other (+/-)	0	115,102
Net other resources used to finance activities	1,282,871	612,228
Total resources used to finance activities	$141,932,542	$121,074,148
Resources Used to Finance Items not Part of the Net Cost of Operations		
Change in budgetary resources obligated for goods,		
services and benefits ordered but not yet provided		
Undelivered Orders (-)	($12,185,137)	($16,480,237)
Unfilled Customer Orders	2,203,425	3,774,656
Resources that fund expenses recognized in prior periods	(870,785)	(282,695)
Budgetary offsetting collections and receipts that		
do not affect net cost of operations	63,441	15,085
Resources that finance the acquisition of assets	(9,901,005)	(25,214,843)
Other resources or adjustments to net obligated resources		
that do not affect net cost of operations		
Less: Trust or Special Fund Receipts Related to Exchange in the Entity's Budget (-)	0	0
Other (+/-)	(400,794)	0
Total resources used to finance items not part of the net cost of operations	($21,090,855)	($38,188,034)
Total resources used to finance the net cost of operations	$120,841,687	$82,886,114
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:		
Increase in annual leave liability	$95,284	$291,488
Increase in environmental and disposal liability	3,103,711	2,317,132
Upward/Downward reestimates of credit subsidy expense (+/-)	10,869	0
Increase in exchange revenue receivable from the the public (-)	0	0
Other (+/-)	63,634	409,303
Total components of Net Cost of Operations that will require or generate resources in future periods	$3,273,498	$3,017,923
Components not Requiring or Generating Resources:		
Depreciation and amortization	9,815,563	21,363,920
Revaluation of assets or liabilities (+/-)	515,037	(10,681)
Other (+/-)		
Trust Fund Exchange Revenue	(36)	(48)
Cost of Goods Sold	0	0
Operating Material & Supplies Used	0	0
Other	1,335,773	174,429
Total components of Net Cost of Operations that will not require or generate resources	$11,666,337	$21,527,620
Total components of net cost of operations that will not require or generate resources in the current period	$14,939,835	$24,545,543
Net Cost of Operations	$135,781,522	$107,431,657

Department of Defense- Department of the Army

STATEMENT OF CUSTODIAL ACTIVITY

As of September 30, 2004 and 2003 ($ in Thousands)

SOURCE OF COLLECTIONS	2004 Combined	2003 Combined
Deposits by Foreign Governments	$0	$0
Seized Iraqi Cash	118,349	808,866
Other Collections	0	0
Total Cash Collections	$118,349	$808,866
Accrual Adjustments (+/-)	0	0
Total Custodial Collections	$118,349	$808,866
DISPOSITION OF COLLECTIONS		
Disbursed on Behalf of Foreign Governments and International Organizations	$0	$0
Seized Assets Disbursed on behalf of Iraqi People	283,058	530,727
Increase (Decrease) in Amounts to be Transferred	0	0
Collections Used for Refunds and Other Payments	0	0
Retained by The Reporting Entity	0	0
Seized Assets Retained for Support of the Iraqi People	(164,709)	278,139
Total Disposition of Collections	$118,349	$808,866
NET CUSTODIAL COLLECTION ACTIVITY	$0	$0

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 Department of the Army, as required by the Chief Financial Officers Act of 1990 (CFO Act), expanded by the Government Management Reform Act of 1994 (GMRA), and other appropriate legislation. The financial statements have been prepared from the books and records of the Army in accordance with the Department of Defense (DoD) Financial Management Regulation; Office of Management and Budget (OMB) Bulletin No. 01-09, *Form and Content of Agency Financial Statements*; and to the extent possible, Federal Generally Accepted Accounting Principles (GAAP). The accompanying financial statements account for all resources for which the Army is responsible. Under the above guidance, classified assets, programs, and operations have been excluded from the statements or aggregated and reported in such a manner that they are no longer classified. The Army's financial statements are in addition to the financial reports prepared by the Army pursuant to OMB directives that are used to monitor and control the Army's use of budgetary resources.

The Army is unable to fully implement all elements of Federal GAAP and OMB Bulletin No. 01-09 due to limitations of its financial and non-financial management processes and systems. The Army derives its reported values and information for major asset and liability categories largely from nonfinancial feeder systems, such as inventory and logistic systems. These were designed to support reporting requirements focusing on maintaining accountability over assets and reporting the status of federal appropriations, rather than preparing financial statements in accordance with Federal GAAP. As a result, the Army cannot currently implement every aspect of Federal GAAP and OMB Bulletin No. 01-09. The Army continues to implement process and system improvements addressing the limitations of its financial and non-financial feeder systems. Further explanation of these financial statement elements is provided in the applicable note.

Fiscal Year (FY) 2004 is the fourteenth year that the Army has prepared financial statements required by the CFO Act, GMRA, and Federal Financial Management Improvement Act of 1996 (FFMIA), (P.L. 104-208). The purpose of the CFO Act was to bring more effective general and financial management practices to the Federal government through statutory provisions; provide for improvement of accounting, systems, financial management, and internal controls; and provide for the production of complete, reliable, timely, and consistent financial information. GMRA extended the CFO Act to all activities of Executive Branch agencies. FFMIA expanded reporting requirements under the CFO Act. The reporting entities within the Army changed to facilitate these reporting requirements.

1.B. Mission of the Reporting Entity

The overall mission of the Army is to organize, train, equip, and support armed forces to deter aggression and, if necessary, defeat aggressors of the United States and its allies. It is no longer a world in which two hostile superpowers face each other. It is our nation's force of decision—a full spectrum force—trained and ready to respond to a wide range of crises, from fighting and winning major theater wars, to peacekeeping, humanitarian relief missions, and disaster relief in communities at home.

The primary mission of the Army remains constant: to fight and win the nation's wars. In an uncertain world, the Army performs a wide variety of other missions around the world and at home including deterring potential adversaries, reassuring and lending stability to allies, supporting our communities in times of emergency, preserving peace and security, supporting national policies, and implementing national objectives. In addition to its military operations, the Army is frequently deployed both at home and abroad in response to natural disasters. Nationally, the Army provides substantial support to relief operations associated with storms, tornadoes, and hurricanes. The Army also provides support and relief assistance abroad. Whatever the mission, committing the Army, commits the nation.

1.C. Appropriations and Funds

The Army's appropriations and funds are divided into the general, working capital (revolving funds), trust, special, and deposit funds. These appropriations and funds are used to fund and report how the resources have been used in the course of executing the Army's missions.

General funds are used for financial transactions arising under congressional appropriations, including personnel, operation and maintenance, research and development, procurement, and construction accounts.

Revolving funds receive their initial working capital through an appropriation or a transfer of resources from existing appropriations or funds and use those capital resources to finance the initial cost of products and services. Financial resources to replenish the initial working capital and to permit continuing operations are generated by the acceptance of customer orders. Revolving funds operate with financial principles that provide improved cost visibility and accountability to enhance business management and improve the decision making process. The activities provide goods and services on a reimbursable basis. Receipts derived from operations are normally available in their entirety for use without further congressional action.

Trust funds represent the receipt and expenditure of funds held in trust by the government for use in carrying out specific purposes or programs in accordance with the terms of the donor, trust agreement, or statute.

Special funds account for government receipts earmarked for a specific purpose.

Deposit funds are generally used to: (1) hold assets for which the Army is acting as an agent or custodian or whose distribution awaits legal determination, or (2) account for unidentified remittances.

1.D. Basis of Accounting

The Army generally records transactions on a budgetary basis and not an accrual accounting basis as is required by Federal GAAP. For FY 2004, the Army's financial management systems were unable to meet all of the requirements for full accrual accounting. Many of the Army's financial and nonfinancial feeder systems and processes were designed and implemented prior to the issuance of Federal GAAP and therefore, were not designed to collect and record financial information on the full accrual accounting basis as required by Federal GAAP. In addition, most of the Army's financial management systems do not comply with the U.S. Government Standard General Ledger (USSGL) at the transaction level. The Army has undertaken efforts to determine the actions required to bring its financial and nonfinancial feeder systems and processes into compliance with all elements of Federal GAAP. One such action is the current revision of Army accounting systems to record transactions based on the USSGL. Until such time as the Army's systems and processes are updated to collect and report financial information as required by Federal GAAP, the Army's financial data will be based on budgetary transactions, non-financial feeder system transactions, and adjustments for known accruals of major items such as payroll expenses, accounts payable, and environmental liabilities. When possible, the financial statements are presented on the accrual accounting basis. One example of information presented on the budgetary basis is data on the Statement of Net Cost. Much of this information is based on obligations and disbursements and may not always represent accrued costs.

In addition, the Army identifies programs based upon the major appropriation groups provided by Congress. The Army does not, however, accumulate costs for major programs based on performance measures because its financial processes and systems do not account for costs in line with established measures. The Army is reviewing available data and attempting to develop a cost reporting methodology that provides the cost information required by the Statement of Federal Financial Accounting Standard (SFFAS) No. 4, *Managerial Cost Accounting Concepts and Standards for the Federal Government.*

1.E. Revenues and Other Financing Sources

Financing sources for general funds are provided primarily through congressional appropriations that are received on both an annual and a multiyear basis. When authorized, these appropriations are supplemented by revenues generated by sales of goods or services through a reimbursable order process. The Army recognizes revenue as a result of costs incurred or services performed on behalf of other federal agencies and the public. Revenue is recognized when earned under the reimbursable order process.

The Army does not include non-monetary support provided by U.S. Allies for common defense and mutual security in its list of other financing sources that appears in the Statement of Financing. The U.S. has agreements with foreign countries that include both direct or indirect sharing of costs that each country incurs in support of the same general purpose. Examples include countries where there is a mutual or reciprocal defense agreement or where U.S. troops are stationed. DoD is reviewing these types of financing and cost reductions in order to establish accounting policies and procedures to identify what, if any, of these costs are appropriate for disclosure in the financial statements in accordance with GAAP. Recognition of support provided by host nations would affect both financing sources and recognition of expenses.

1.F. Recognition of Expenses

For financial reporting purposes, the DoD policy requires recognition of operating expenses in the period incurred. However, because the Army's financial and nonfinancial feeder systems were not designed to collect and record financial information on the full accrual accounting basis, accrual adjustments are made for major items such as payroll expenses, accounts payable, and environmental liabilities. Expenditures for capital and other long-term assets are not recognized as expenses in the Army operations until depreciated in the case of Property, Plant and Equipment (PP&E) or consumed in the case of Operating Materials and Supplies (OM&S). Net increases or decreases in unexpended appropriations are recognized as a change in net position. Certain expenses, such as civilian annual leave and military leave earned but not taken, are financed in the period in which payment is made.

The Army adjusted operating expenses as a result of the elimination of balances between DoD components. See Note 19.I., Intragovernmental Expenses and Revenue for disclosure of adjustment amounts.

1.G. Accounting for Intra-governmental Activities

The Army, as an agency of the Federal government, interacts with and is dependent upon the financial activities of the Federal government as a whole. Therefore, these financial statements do not reflect the results of all financial decisions applicable to the Army as though the agency was a stand-alone entity.

The Army'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 Army's financial statements, therefore, do not report any portion of the public debt or interest, nor do the statements report the source of public financing whether from issuance of debt or tax revenues.

Financing for the construction of Army facilities is obtained through budget appropriations. To the extent this financing was obtained through issuance of public debt, interest costs were not capitalized since the Department of the Treasury does not allocate these interest costs to the benefiting agencies.

The Army's civilian employees participate in the Civil Service Retirement System (CSRS) and the Federal Employees Retirement System (FERS), while military personnel are covered by the Military Retirement System (MRS). Additionally, employees and personnel covered by FERS and MRS also have varying coverage under social security. The Army funds a portion of the civilian and military pensions. Reporting civilian pensions under CSRS and FERS is the responsibility of the Office of Personnel Management (OPM). The Army recognizes an imputed expense for the portion of civilian employee pensions and other retirement benefits funded by OPM in the Statement of Net Cost; and recognizes corresponding imputed revenue from the civilian employee pensions and other retirement benefits in the Statement of Changes in Net Position.

Assets, funded actuarial liability, and unfunded actuarial liability for military personnel are reported in the Military Retirement Fund (MRF) financial statements. The actuarial liability for military retirement health benefits is recognized in the Other Defense Organization General Fund column of DoD Agency-wide consolidating/combining statements.

To prepare reliable financial statements, transactions occurring between components or activities within the Army must be eliminated. However, the Army, as well as the rest of the federal government, cannot accurately identify all intragovernmental transactions by customer. The Defense Finance and Accounting Service (DFAS) is responsible for eliminating transactions between components or activities of the Army. For FYs 1999 and beyond, seller entities within the DoD provided 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 have been adjusted to recognize unrecorded costs and accounts payable. Intra-DOD intragovernmental balances were then eliminated.

The Army's accounting systems do not capture trading partner information at the transaction level. Therefore, current systems cannot produce data necessary for reconciliations between buyers and sellers, nor eliminate all intragovernmental transactions between trading partners. As a result, the Army's balances are compared to seller-side data summarized at the component trial balance level. Based on these comparisons, the amount of intragovernmental transactions on the buyer-side is forced to agree with seller-side information.

The Department of the Treasury, Financial Management Service (FMS), is responsible for eliminating transactions between the Army and other federal agencies. In September 2000, FMS issued the "Federal Intragovernmental Transactions Accounting Policies and Procedures Guide." The Army was not able to fully implement the policies and procedures in this guide related to reconciling intragovernmental assets, liabilities, revenues, and expenses for non-fiduciary transactions. The Army, however, was able to implement the policies and procedures contained in the "Intragovernmental Fiduciary Transactions Accounting Guide," as updated by the "Federal Intragovernmental Transactions Accounting Policies and Procedures Guide," issued October 2002, for reconciling intragovernmental transactions. These transactions pertain to investments in Federal securities, borrowings from the United States Treasury and the Federal Financing Bank, Federal Employees' Compensation Act transactions with the Department of Labor (DoL), and benefit program transactions with OPM.

1.H. Transactions with Foreign Governments and International Organizations

Each year, the Army components sell defense articles and services to foreign governments and international organizations, primarily under the provisions of the Arms Export Control Act of 1976. Under the provisions of the Act, the Army 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. Customers may be required to make payments in advance.

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

The Army's financial resources are maintained in U.S. Treasury accounts. The majority of cash collections, disbursements, and adjustments are processed worldwide at the DFAS, Military Services, and the US Army Corp of Engineers (USACE) disbursing stations, as well as the Department of State financial service centers. Each disbursing station prepares monthly reports, which provide information to the U.S. Treasury on check issues, electronic fund transfers, interagency transfers and deposits.

In addition, the DFAS sites and the USACE Finance Center submit reports to the Department of the Treasury, by appropriation, on interagency transfers, collections received, and disbursements issued. The Department of the Treasury then records this information to the applicable Fund Balance with Treasury (FBWT) account maintained in the Treasury's system. Differences between the Army recorded balance in the FBWT accounts and Treasury's FBWT accounts sometimes result and are subsequently reconciled. Material disclosures are provided in Note 3, Fund Balance With Treasury. Differences between accounting offices' detail-level records and Treasury's FBWT accounts are disclosed in Note 1.Y, specifically, differences caused by in-transit disbursements and unmatched disbursements (which are not recorded in the accounting offices' detail-level records).

1.J. Foreign Currency

The Army 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 (operation and maintenance, military personnel, military construction, family housing operation 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. These currency fluctuations are not separately identified.

1.K. Accounts Receivable

As presented in the Balance Sheet, accounts receivable includes accounts, claims, and refunds receivable from other federal entities or from the public. The Army bases the allowances for uncollectible accounts that are due from the public upon analysis of collection experience by fund type. The Army 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. See Note 5., Accounts Receivable, for material disclosures.

1.L. Loans Receivable

Not Applicable

1.M. Inventories and Related Property

Effective October 1, 2002, SFFAS No. 23, *Eliminating the Category National Defense Property, Plant, and Equipment*, revises accounting principles for military equipment (previously referred to as National Defense Property, Plant, and Equipment). This standard renames National Defense Property, Plant, and Equipment to military equipment, classifies military equipment (e.g., ships, aircraft, combat vehicles, and weapons) as general property, plant, and equipment, and requires the capitalization and depreciation of the cost of military equipment, including the cost of modifications and upgrades. Likewise, military equipment (previously referred to as NDPP&E) also includes items which will now be classified as OM&S.

Inventories are reported at approximate historical cost using Latest Acquisition Cost (LAC) adjusted for holding gains and losses.

The Army uses the LAC method because its inventory systems were designed for material management rather than accounting. The systems provide accountability and visibility over inventory items. They do not maintain historical cost data necessary to comply with SFFAS No. 3, *Accounting for Inventory and Related Property.* They are also unable to directly produce financial transactions using the USSGL, as required by FFMIA of 1996 (P.L. 104-208). DoD is transitioning to a Moving Average Cost methodology for valuing inventory that when fully implemented will allow the Army to comply with SFFAS No. 3.

SFFAS No. 3 distinguishes between inventory held for sale and inventory held in reserve for future sale. There is no difference in how these accounts are managed or valued. Normally, the Army manages only military or government-specific material. The Army does not manage items commonly used in and available from the commercial sector. In addition, operational cycles are irregular, and the military risks associated with stock-out positions have no commercial equivalent. The Army holds material based on military need and support for contingencies. Therefore, the Army does not attempt to account separately for items held for current or future sale.

Related property includes OM&S and stockpile materials. OM&S, including munitions not held for sale, are valued at standard purchase price. For the most part, the Army uses the consumption method of accounting for OM&S by expensing material when issued to the end user. Where current systems cannot fully support the consumption method, the Army uses the purchase method – that is, items are expensed when purchased. The Army reported significant amounts using the purchase method either because the systems could not support the consumption method or because management deems that the item is in the hands of the end user.

The Army accounts for condemned material as excess, obsolete, and unserviceable. The net value of condemned material is zero because disposal costs are greater than potential scrap value.

In addition, past audit results identified uncertainties about the completeness and existence of quantities used to produce the reported values. Material disclosures related to inventory and related property are provided in Note 9, Inventory and Related Property.

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

The Army reports investments in Treasury securities at cost, net of unamortized premiums or discounts. Premiums or discounts amortize into interest income over the term of the investment using the effective interest rate method or another method obtaining similar results. The Army's intent is to hold investments until maturity, unless needed to finance claims or otherwise sustain operations. Consequently, the Army does not make provisions for unrealized gains or losses on these securities. Material disclosures related to investments in treasury securities are provided in Note 4, Investments.

1.O. General Property, Plant and Equipment

General PP&E assets are capitalized at historical acquisition cost plus capitalized improvements when an asset has a useful life of two or more years, and when the acquisition cost equals or exceeds the DoD capitalization threshold of $100,000. All General PP&E, other than land, is depreciated on a straight-line basis. Land is not depreciated.

Military Equipment

Effective October 1, 2002, SFFAS No. 23, *Eliminating the Category National Defense Property, Plant, and Equipment,* revises accounting principles for military equipment (previously referred to as National Defense Property, Plant, and Equipment). This standard renames National Defense Property, Plant, and Equipment to military equipment, classifies military equipment (e.g., ships, aircraft, combat vehicles, and weapons) as general property, plant, and equipment, and requires the capitalization and depreciation of the cost of military equipment, including the cost of modifications and upgrades.

Contractor Provided

When it is in the best interest of the government, the Army provides to contractors government property necessary to complete contract work. Such property is either owned or leased by the Army, or purchased directly by the contractor for the government based on contract terms. When the value of contractor procured General PP&E meets the normal DoD capitalization criteria, such PP&E is required to be included in the value of General PP&E reported on the Army's Balance Sheet. DoD is developing new policies and a contractor reporting process that will provide appropriate General PP&E information for future financial statement reporting purposes. Accordingly, the Army currently reports only the portion of government property in the possession of contractors that is maintained in the Army's property systems.

To bring the Army into fuller compliance with federal accounting standards, the DoD has issued new property accountability and reporting regulations that require the DoD Components to maintain, in DoD Component 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.

Material disclosures related to General PP&E are provided in Note 10, General PP&E, Net.

1.P. Advances and Prepayments

Payments in advance of the receipt of goods and services are recorded as advances or prepayments and reported as an asset on the Balance Sheet. Advances and prepayments are recognized as expenditures and expenses when the related goods and services are received.

1.Q. Leases

Generally, lease payments are for the rental of operating facilities and are classified as either capital or operating leases. When a lease is essentially equivalent to an installment purchase of property (a capital lease) the Army records the applicable asset and liability if the value equals or exceeds the current DoD capitalization threshold. The Army 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 value. The Army deems the use of estimates for these costs as adequate and appropriate due to the relatively low dollar value of capital leases. Imputed interest was necessary to reduce net minimum lease payments to present value calculated at the incremental borrowing rate at the inception of the leases. In addition, the Army classifies leases that do not transfer substantially all of the benefits or risks of ownership as operating leases and records payment expenses over the lease term.

1.R. Other Assets

The Army 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, the Army provides financing payments. One type of financing payment that the Army makes, for real property, is based upon a percentage of completion. In accordance with SFFAS No. 1, *Accounting for Selected Assets and Liabilities*, such payments are treated as construction in process and are reported on the General PP&E line and in Note 10, General PP&E, Net.

In addition, based on the Federal Acquisition Regulation, the Army makes financing payments under fixed price contracts that are not based on a percentage of completion. The Army reports these financing payments as advances or prepayments in the "Other Assets" line item. The Army treats these payments as advances or prepayments because the Army becomes liable only after the contractor delivers the goods in conformance with the contract terms. If the contractor does not deliver a satisfactory product, the Army is not obligated to reimburse the contractor for its costs and the contractor is liable to repay the Army for the full amount of the advance.

DoD has completed a review of all applicable federal accounting standards; applicable public laws on contract financing; Federal Acquisition Regulation Parts 32, 49, and 52; and the OMB guidance in 5 Code of Federal Regulations Part 1315, *Prompt Payment*. DoD concluded that SFFAS No. 1 does not fully or adequately address the subject of progress payment accounting and is considering what further action is appropriate.

1.S. Contingencies and Other Liabilities

SFFAS No. 5, *Accounting for Liabilities of the Federal Government*, defines a contingency as an existing condition, situation, or set of circumstances that involves an uncertainty as to possible gain or loss to the Army. The uncertainty will be resolved when one or more future events occur or fail to occur. A contingency is recognized as a liability when a past event or exchange transaction has occurred, a future loss is probable, and the amount of loss can be reasonably estimated.

Financial statement reporting is limited to disclosure when conditions for liability recognition do not exist but at least a reasonable possibility that a loss or additional loss will be incurred. Loss contingencies include the collectibility of receivables, pending or threatened litigation, and possible claims and assessments. The Army's loss contingencies arising as a result of pending or threatened litigation or claims and assessments occur due to events such as aircraft, ship and vehicle accidents; medical malpractice; property or environmental damages; and contract disputes.

Other liabilities arise as a result of anticipated disposal costs for the Army's assets. This type of liability has two components -- nonenvironmental and environmental. Recognition of an anticipated environmental disposal liability commences when the asset is placed into service, consistent with SFFAS No. 6, *Accounting for Property, Plant, and Equipment.* Based upon the Army's policies, which are consistent with SFFAS No. 5, Accounting for Liabilities of Federal Government, a nonenvironmental disposal liability is recognized for an asset when management decides to dispose of the asset.

The Army, by means of the Armament Retooling and Manufacturing Support (ARMS) Initiative legislation, has been authorized to establish a loan guarantee program to facilitate commercial firms' use of specified ammunition manufacturing facilities and the Army recognizes the loan guarantee liability. The Army is authorized by Public Law 103-337, the National Defense Authorization Act for Fiscal Year 1995, to enter into this agreement with the U.S. Department of Agriculture Rural Business-Cooperative Service (RBS).

For material disclosures, see:

- Notes 8, Direct Loan and/or Loan Guarantee Program.
- Note 14, Environmental Liabilities and Disposal Liabilities.
- Note 15, Other Liabilities.

1.T. Accrued Leave

Civilian annual leave and military leave that has been accrued and not used as of the balance sheet date is reported as a liability. The liability reported at the end of the fiscal year reflects the current pay rates.

1.U. Net Position

Net Position consists of unexpended appropriations and cumulative results of operations. Unexpended appropriations represent budget authority, which is unobligated and has not been rescinded or withdrawn, and funds obligated but for which legal liabilities have not been incurred.

Cumulative results of operations represents the difference, since inception of an activity, between expenses and losses and financing sources (including appropriations, revenue, and gains). Beginning with FY 1998, this included the cumulative amount of donations and transfers of assets in and out without reimbursement.

1.V. Treaties for Use of Foreign Bases

The DoD Components have the use of land, buildings, and other facilities, which are located overseas and have been obtained through various international treaties and agreements negotiated by the Department of State. DoD capital assets overseas are purchased with appropriated funds; however, title to land and improvements are retained by the host country. Generally, treaty terms allow the DoD Components continued use of these properties until the treaties expire. These fixed assets are subject to loss in the event treaties are not renewed or other agreements are not reached which allow for the continued use by DoD. Therefore, in the event treaties or other agreements are terminated whereby use of the foreign bases is no longer allowed, losses will be recorded for the value of any non-retrievable capital assets after negotiations between the U.S. and the host country have been concluded to determine the amount to be paid the U.S. for such capital investments.

1.W. Comparative Data

The Financial Statements and accompanying Notes to the Financial Statements report the financial position and results of operations for FY 2004. Financial statement fluctuations greater than 2 percent of total assets on the Balance Sheet and/or greater than 10 percent between FY 2003 and FY 2004, are explained within the Notes to the Financial Statements.

1.X. Unexpended Obligations

The Army obligates funds to provide goods and services for outstanding orders not yet delivered. The financial statements do not reflect this liability for payment for goods/services not yet delivered. See Note 18, Unexpended Appropriations for material disclosures.

1.Y. Problem Disbursements

(Amounts in thousands)	September 2002	September 2003	September 2004	Increase / (Decrease) from 2003 to 2004
Problem Disbursements				
Absolute Unmatched Disbursements	$160,726	$259,857	$69,857	($190,000)
Negative Unliquidated Obligations	$20,985	$26,251	$24,424	($1,827)
In-transit Disbursements, Net	$710,194	$1,086,574	$1,652,211	$565,637

Definitions:

Absolute value is the sum of the positive values of debit and credit transactions without regard to the sign.

Unmatched Disbursements (UMDs) occur when payments do not match to a corresponding obligation in the accounting system.

Negative Unliquidated Obligations (NULOs) occur when payments have a valid obligation but the payment is greater than the amount of the obligation recorded in the official accounting system. These payments use available funds for valid receiving reports on delivered goods and services under valid contracts.

In-Transits represents the net value of disbursements and collections made by a DoD disbursing activity on behalf of an accountable activity but not yet attempted to be posted in an accounting system.

Aged UMDs and NULOs: The Army absolute value UMDs, NULOs, and negative $54,001 thousand in aged in-transit disbursements represent problem disbursements. UMDs and NULOs are considered to be problem disbursements immediately, while in-transits are considered normal business activity up to the 30-day aging category. After 30 days, they become perceived as problem disbursements. Sixty seven percent of the increase in Net In-transit Disbursements occurred at DFAS Rome (DFAS-RO) where there are several issues being worked to help decrease the processing time of the Third Army charges from the Global War on Terrorism (GWOT). DFAS-RO received $268 million in freight and passenger charges in late September 2004 as a result of the GWOT. These were received at the end of the month and could not be confirmed by Third Army for proper posting by DFAS-RO before closing September 2004. Fluctuations in the schedule represent normal activity for UMDs and NULOs based on the inflow of undistributed disbursements received for processing. Total in-transit balances have increased at the primary accounting sites supporting the war, contingency operations, and supply and materiel replenishment.

1.Z. Development Fund for Iraq

On June 28, 2004, transfer of power from the Coalition Provisional Authority (CPA) to the Interim Iraqi Government (IIG) occurred. Prior to the transfer, the CPA was responsible for the management and accounting of the Development Fund for Iraq (DFI). Ongoing resolution of issues surrounding transfers of approximately $1.7 billion of DFI assets, including $86 million transferred from IIG to the Multi-National Force-Iraq in August 2004, may require additional disclosure in future financial statements. Therefore, no amounts for these assets are included in the financial statements.

Note 2. Nonentity Assets

As of September 30

(Amounts in thousands)	2004	2003
1. Intra-governmental Assets		
A. Fund Balance with Treasury	$251,236	$339,582
B. Investments	0	0
C. Accounts Receivable	0	0
D. Other Assets	0	0
E. Total Intra-governmental Assets	$251,236	$339,582
2. Non-Federal Assets		
A. Cash and Other Monetary Assets	$1,525,090	$954,368
B. Accounts Receivable	187,140	228,833
C. Loans Receivable	0	0
D. Inventory & Related Property	0	0
E. General PP&E	0	0
F. Investments	0	0
G. Other Assets	0	0
H. Total Non-Federal Assets	$1,712,230	$1,183,201
3. Total Non-Entity Assets	$1,963,466	$1,522,783
4. Total Entity Assets	$244,733,167	$207,173,280
5. Total Assets	$246,696,633	$208,696,063

Relevant Information for Comprehension

Nonentity Assets of $1,963,466 thousand are assets held by the Army, but are not available to fund mission operations.

Nonentity Intragovernmental Fund Balance with Treasury of $251,236 thousand is made up of $113,430 thousand in Iraqi custodial funds that coalition forces seized during Operation Iraqi Freedom to be used in support of the Iraqi people, $138,440 thousand in deposit funds, and $(634) thousand in suspense accounts. Further explanation on the Iraqi custodial funds is disclosed in Note 23.

Nonentity Non-Federal Cash and Other Monetary Assets of $1,525,090 thousand represent both cash and foreign currency.

Nonentity Non-Federal Accounts Receivable of $187,140 thousand represents receivables that originated in appropriations that are closed and are no longer available to execute Army missions. Army continues to pursue collection actions and any amounts collected are deposited into the Treasury's miscellaneous receipt account.

The Army has $244,733,167 thousand in Entity Assets. Entity Assets consist of resources that the Army has the authority to use, or where management is legally obligated to use funds to meet current year obligations.

Fluctuations and/or Abnormalities:

Nonentity Intragovernmental Fund Balance with Treasury decreased $88,346 thousand or 26 percent. The fluctuation is attributed to a decrease of $164,709 thousand in Iraqi custodial funding, due to the exhaustion of funds recovered in Iraq without recovering any additional funds, offset by an increase of $76,363 thousand in miscellaneous suspense accounts and deposit funds.

The increase in the miscellaneous suspense and deposit funds is due to $37,009 thousand increase in Army Member Savings Deposits caused by an increase in deployed Soldiers drawing imminent danger pay who are authorized to deposit funds and later withdraw the funds with interest; $19,896 thousand in Withheld State Income Taxes; $14,859 thousand in Small Escrow Accounts due to the increase of Soldiers using the post office and Army Air Force Exchange Service in Kuwait and Iraq; and the remaining $4,599 thousand in miscellaneous suspense and deposit funds.

Cash and foreign currency increased $570,722 thousand or 60 percent, primarily to support the contingency missions Operation Iraqi Freedom and Operation Enduring Freedom. Overall foreign currency increased approximately $182,604 thousand or 105 percent, which includes currency to pay foreign vendors and cash in the custody of foreign agents primarily in support of the Army's forward deployed tactical units. Other increases occurred in the U.S. Army Corps of Engineers as the Republic of Korea increased agreements for reimbursable work to be performed.

Accounts Receivable decreased $41,693 thousand or 18 percent, primarily due to erroneous reporting of canceling accounts receivable in the individual appropriations in FY 2003. Per Treasury, all canceling year Accounts Receivable should be reported in Receipt Account 3200 Collections of Receivables from Cancelled Accounts.

Note Reference

For additional line item discussion, see:

Note 3, Fund Balance With Treasury
Note 4, Investments
Note 5, Accounts Receivable
Note 6, Other Assets
Note 7, Cash and Other Monetary Assets
Note 8, Direct Loan and/or Loan Guarantee Programs
Note 9, Inventory and Related Property
Note 10, General PPE, Net
Note 23, Disclosures Related to the Statement of Custodial Activity

Note 3.A. Fund Balance with Treasury

As of September 30
(Amounts in thousands)

	2004	2003
1. Fund Balances		
A. Appropriated Funds	$79,827,618	$54,145,086
B. Revolving Funds	36,457	50,503
C. Trust Funds	2,862	2,502
D. Other Fund Types	9,681,672	837,388
E. Total Fund Balances	$89,548,609	$55,035,479
2. Fund Balances Per Treasury Versus Agency		
A. Fund Balance per Treasury	$89,548,609	$55,035,479
B. Fund Balance per Army General Fund	89,548,609	55,035,479
3. Reconciling Amount	$0	$0

The Fund Balance is reconciled to the Treasury Trial Balance. During September 2004, Army made a net adjustment of $45,888 thousand for unsupported undistributed disbursements and collections to bring the Fund Balance reported by Army into agreement with Treasury.

Fluctuations and/or Abnormalities

The Fund Balance represents the amount of available funding to be utilized for executing the Army mission. Army Fund Balances increased $34,513,130 thousand or 63 percent, from FY 2003. The primary increase is due to the $31,864,362 thousand increase in FY 2004 funding. Fund Balance positions increased as follows (in thousands):

Program	Fund Balance
Military Personnel	$ 2,137,401
Operation & Maintenance	18,777,982
Research, Development, Test, and Evaluation	1,899,561
Military Construction	(143,948)
Procurement	2,482,144
Vested Iraqi Cash	38,358
Other Miscellaneous	9,321,632
	$34,513,130

Intragovernmental Payment and Collection (IPAC)

The Intragovernmental Payment and Collection (IPAC) differences are reconcilable differences that represent amounts recorded by Treasury but not reported by the organization. The Army had no IPAC differences greater than 180-days old as of September 2004.

Automated reconciliation tools have virtually eliminated all existing differences for the Army. Field sites requiring additional backup to record the transaction in their accounting system, accounting errors, or timing differences between disbursing and Treasury cut-off dates are the primary reasons for an IPAC difference to exist today.

Check Issue Discrepancy

For September 2004, the Army 2100 Comparison of Checks Issued Report received from Treasury includes the following (in thousands):

DFAS	0-60 Days	61-180 Days	> 180 Days	Total
Indianapolis	$406,264	$452	$0	$406,716
Columbus (Army DSSNs)*	15,614	0	0	15,614
Columbus (Transp Pay)	713	0	0	713
Columbus (Def Agencies)	30,269	0	0	30,269
TOTAL (2100 ARMY)	**$452,860**	**$452**	**$ 0**	**$453,312**

**DSSN is Disbursing Station Symbol Number*

Check issue differences in the 0-60 days category are considered timing differences due to in-transit time between reporting check issues by the field and processing into the Treasury Check Payments and Reconciliation System.

The differences in the 0-60 days and the 61-180 days are expected to clear in October 2004.

Deposit Differences

The deposit differences are reconcilable differences reported by the Treasury or the Army. The Army has $60 thousand in deposit differences greater than 180 days old as of September 2004. The cause of the differences are not known at this time but expected to clear in October 2004.

Vested Iraqi Cash

Since inception of the account, the Army has collected $1,724,131 thousand of Vested Iraqi Cash. This cash is vested in accordance with the International Emergency Economic Powers Act, Section 1701 and will be used in support of the Iraqi people. The Army has disbursed $1,685,773 thousand in support of the Iraqi people as follows:

	Amounts in thousands
Collected	$1,724,131
Disbursed	
Iraqi Salaries	$1,184,926
Repair/Reconstruction/Humanitarian Assistance	140,862
Iraqi Ministry Operations (Ministry of Finance, Defense, etc.)	359,985
Total Disbursed	$1,685,773
Remaining Funds	$38,358

Other Fund Types

The $9,681,672 thousand in Other Fund Types consists of $9,394,285 thousand in the Iraqi Relief and Reconstruction Fund, $138,440 thousand in deposit funds, $113,430 thousand in Iraqi Custodial Funds (Seized Iraqi Cash), $36,152 thousand in special fund and receipt accounts, and $(634) thousand in suspense accounts.

Other Fund Types increased by $8,844,284 thousand from FY 2003 which consists of increases of $8,929,483 thousand in Iraqi Relief and Reconstruction Fund, $37,009 thousand in Army Member Savings Deposits due to the increase in deployed Soldiers drawing imminent danger pay who are authorized to deposit funds and later withdraw the funds with interest, $19,896 thousand in Withheld State Income Taxes, $14,859 thousand in Small Escrow Accounts due to the increase of Soldiers using the post office and Army Air Force Exchange Service in Kuwait and Iraq, and $7,746 thousand in Other Miscellaneous Fund Accounts. In addition, there was a decrease of $164,709 thousand in Iraqi Seized Assets due to the exhaustion of funds recovered in Iraq without recovering any additional funds.

Canceling Appropriated Funds

As of September 2004, Army withdrew $659,532 thousand in canceling appropriated funds in accordance with Treasury's policy.

Note Reference

See Note 1.I. – Funds with the U.S. Treasury for additional discussion on financial reporting requirements and DoD policies governing Funds with the U.S. Treasury.

See Note 2 Nonentity Assets and Note 23 Disclosures Related to the Statement of Custodial Activity for further discussions on Other Fund Balance Types (e.g., Suspense, Budget Clearing, Special and Deposit, Seized Iraqi Cash, etc.).

Note 3.B. Disclosures Related to Suspense/Budget Clearing Accounts

As of September 30 (Amounts in thousands)	2002	2003	2004	(Decrease)/ Incrcrease from FY 2003-2004
Account				
F3875	$0	$0	$0	$0
F3880	0	0	0	0
F3882	(739)	(908)	(820)	88
F3885	0	0	0	0
F3886	5,690	200	187	(13)
Total	$4,951	($708)	($633)	$75

The Army established policies and procedures to ensure accurate and consistent use of Suspense and Budget Clearing accounts. Suspense reconciliations have been reported as a material weakness since 1997. The Army is currently implementing Public Law 107-314 which includes provisions for the write-off of unsupported balances and improvements in tracking and reporting Army suspense balances.

On September 30 of each fiscal year, most of the uncleared suspense/budget clearing account balances are reduced to zero (as required by the Department of Treasury) by transferring the balances to proper appropriation accounts. In the following month, the uncleared suspense/clearing account balances are reestablished. The Army transferred the following accounts to their Operation and Maintenance Account (21 2020) for FY 2004 (in thousands):

	Accounts	FY 2004	FY 2003
21 F3875	Budget Clearing Accounts	$37,389	$82,292
21 F3880	Check Cancellations	33,815	2,913
21 F3885	Intergovernmental Payment and Collection	(18,896)	370,885

In addition, Budget Clearing Accounts such as the Uniformed Service Thrift Savings Plan (F3882) and Federal Employees Retirement System (F3886) remain open at fiscal year-end. Negative amounts shown above do not indicate abnormal balances, but a preponderance of disbursements over collections.

Note 4. Investments

As of September 30 (Amounts in thousands)	2004					2003
	Cost	Amortization Method	Amortized (Premium/ Discount)	Investments, Net	Market Value Disclosure	Investments, Net
1. Intra-governmental Securities:						
A. Marketable	$0		$0	$0	$0	$0
B. Non-Marketable, Par Value	0		0	0	0	0
C. Non-Marketable, Market-Based	1,492	Effective Interest	(1)	1,491	1,492	1,225
D. Subtotal	$1,492		($1)	$1,491	$1,492	$1,225
E. Accrued Interest	$5			$5	$5	$6
F. Total Intragovernmental Securities	$1,497		($1)	$1,496	$1,497	$1,231
2. Other Investments:	$0		$0	$0	N/A	$0

Fluctuations and/or Abnormalities

The Army Investments increased $265 thousand or 22 percent in FY 2004. The increase was caused by a timing difference of a bond redemption in FY 2003 that artificially lowered the balance for FY 2003.

Other Information Related to Investments

The Army Gift Fund was established to control and account for the disbursement and use of monies donated to the Army along with the interest received from the investment of such donations. The related earnings are allocated to appropriate Army activities to be used in accordance with the directions of the donor. These funds are recorded as Non-Marketable Market-Based U.S. Treasury Securities, which are not traded on any securities exchange, but mirror the prices of marketable securities with similar terms.

Note Reference

See Note Disclosure 1.N. – Investments in U.S. Treasury Securities for additional DoD policies governing Investments in U.S. Treasury Securities.

Note 5. Accounts Receivable

As of September 30 (Amounts in thousands)	2004 Gross Amount Due	2004 Allowance For Estimated Uncollectibles	2004 Accounts Receivable, Net	2003 Accounts Receivable, Net
1. Intra-governmental Receivables:	$461,867	N/A	$461,867	$523,347
2. Non-Federal Receivables (From the Public):	$628,934	($136,540)	$492,394	$514,579
3. Total Accounts Receivable:	$1,090,801	($136,540)	$954,261	$1,037,926

4. Allowance Method:

The method to estimate Allowance for Loss on Accounts Receivable was changed from percentage of actual write-offs to percentage of aged receivables by category. The allowance is calculated by using 50 percent of aged receivables in the 180 day to 2-year category and 100 percent of aged receivables in the greater than 2-year category. The aged categories are taken from the FY 2004 Quarterly Accounts Receivable Report. The Allowance for Loss on Accounts Receivable will be reestimated annually in compliance with standards.

5. Other information:

Fluctuations and/or Abnormalities

Intragovernmental Receivables decreased $61,480 thousand or 12 percent from FY 2003 to FY 2004. The decrease was seen in receivable balances from the Department of Justice for $10,021 thousand, Department of the Air Force for $28,013 thousand, and Department of Transportation for $26,564 thousand.

Net Non-Federal Accounts Receivables (from the Public) decreased $22,185 thousand or 4 percent from FY 2003 to FY 2004. The decrease is primarily attributable to the increase in the Allowance for Loss on Accounts Receivable $68,615 thousand and an increase in undistributed collections of $34,600 thousand. The estimation method was changed during the fiscal year to include aged vendor and contractor debt from DoD's centralized collection activity in Columbus. Percentages for aged balances were also changed to more accurately reflect collectable receivables. Both of these changes caused the net realizable receivable balances to decrease. Some increases were also seen in areas impacted by contingency mission as In-Service and Out-of-Service debts increased $45,358 thousand and debts from Foreign Governments increased $29,833 thousand.

Non-Federal Accounts Receivable (from the Public) consists of accounts receivable, refund receivable, claims receivable and interest receivable. The following schedule illustrates the major contributors to Non-Federal Accounts Receivable (from the Public), by type of debt (in thousands):

Type of Debt	Amount
Contractor Debt	$ 104,252
Individual (Out-of-Service)	165,707
Military Pay (In-Service)	100,716
Civilian Pay (In-Service)	24,552
Sales of Goods & Services	49,500
Interest	49,843
Foreign Military Sales	68,029
Foreign Governments	76,438
Non-Appropriated Funds Instrumentalities	13,512
Vendor Debt	6,483
Other	37,008
Subtotal	$ 696,040
Undistributed Collections Public	(67,106)
Note 5, Line 2, Column 1	$ 628,934

Relevant Information for Comprehension

Allocation of Undistributed Collections

The Army reported $67,106 thousand of supported undistributed collections. The Army supported undistributed collections are reported as either federal or public using the reimbursable source code.

Elimination Adjustments

The Army's General Fund accounting systems do not capture trading partner data at transaction level in a manner that facilitates trading partner aggregations. Therefore, the Army is unable to reconcile Intragovernmental Accounts Receivable balances with its trading partners. The Army intends to develop long-term systems improvements that will include sufficient up-front edits and controls to eliminate the need for after-the-fact reconciliations. These improvements will be implemented incrementally through planned fielding of a compliant financial management system for all Army activities.

Accounts Receivable Over 180 Days

The Army reported $168,871 thousand of Non-Federal Accounts Receivable (from the Public) and $3,541 thousand of Intragovernmental Accounts Receivable over 180 days. Over 92 percent of Non-Federal Accounts Receivable (from the Public) consisted of personnel and contractor debt. The Intragovernmental Accounts Receivable consisted of debt from reimbursable transactions within DoD.

Non-Federal Refunds Receivable

(in thousands)

FY 2004 Non-Federal Refunds Receivable	FY 2004 Non-Federal Accounts Receivable (Net)	Percent of Net Amount
$267,061	$492,394	54

Amounts reported for Public Refunds Receivable primarily originated from debts owed by military service members collectible to Army's active military personnel appropriation.

Note Reference

See Note Disclosure 1.K. - Significant Accounting Policies for additional discussion on financial reporting requirements and DoD policies governing Accounts Receivable.

Note 6. Other Assets

As of September 30
(Amounts in thousands)

	2004	2003
1. Intra-governmental Other Assets:		
A. Advances and Prepayments	$556,380	$83,474
B. Other Assets	0	0
C. Total Intra-governmental Other Assets	$556,380	$83,474
2. Non-Federal Other Assets:		
A. Outstanding Contract Financing Payments	$2,789,090	$3,163,668
B. Other Assets (With the Public)	562,414	405,353
C. Total Non-Federal Other Assets	$3,351,504	$3,569,021
3. Total Other Assets:	$3,907,884	$3,652,495

4. Other Information Related to Other Assets:

Fluctuations and/or Abnormalities

Intragovernmental Advances and Prepayments

Intragovernmental Advances and Prepayments increased $472,906 thousand or 567 percent from FY 2003. Improved business processes allowed us to capture the advances to others with agencies outside of DoD for FY 2004. Advances to the Department of Interior for $389,750 thousand and Department of Transportation for $83,907 thousand make up the majority of the overall increase.

Non-Federal Other Assets

- Outstanding Contract Financing Payments

  The Army has reported outstanding financing payments for fixed price contracts as an advance and prepayment. The Army becomes liable after the contractor delivers the goods in conformance with the contract terms of fixed price contracts. The Army is not obligated to reimburse the contractor for its costs and the contractor is liable to repay the Army the full amount of the outstanding contract financing payments if a satisfactory product is not delivered.

  Outstanding Contract Financing Payments decreased $374,578 thousand or 12 percent from FY 2003. The majority of the decrease occurred in the appropriations for Missile Procurement, Army of $258,900 thousand and Procurement of Weapons & Tracked Combat Vehicles, Army of $87,584 thousand.

  - Other Assets (With the Public) (Amounts in thousands)

    The following chart provides a breakdown of the report data types for FY 2004:

Type of Assets	FY 2004	FY 2003
Advances to Others:		
Contractor Advance	$329,930	$160,917
Travel Advances	232,484	195,681
Other	0	48,755
Totals	$562,414	$405,353

The Other Assets (With the Public) increased $157,061 thousand or 39 percent due to increases in contractor advances and military personnel travel advances in support of the Global War on Terrorism (GWOT).

Intragovernmental Eliminations

The buyer-side Advances and Prepayments balances were adjusted upward $717,530 thousand to agree with seller-side unearned revenue on the books for other DoD reporting entities. In addition, $166,176 thousand of intra-Army General Fund transactions were eliminated leaving a balance of $556,380 thousand.

Note Reference

See Note Disclosure 1. R. – Significant Accounting Policies for additional discussion on financial reporting requirements and DoD policies governing Other Assets.

For Regulatory Discussion on Other Assets see, Department of Defense Financial Management Regulation, Volume 6B, Chapter 10, paragraph 1008.

Note 7. Cash and Other Monetary Assets

As of September 30
(Amounts in thousands)

	2004	2003
1. Cash	$1,168,692	$780,574
2. Foreign Currency (non-purchased)	356,398	173,794
3. Other Monetary Assets	0	0
4. Total Cash, Foreign Currency, & Other Monetary Assets	$1,525,090	$954,368

5. Other Information Pertaining to Entity Cash & Other Monetary Assets:

Definitions:

Cash – The total of cash resources under the control of the Army, which includes coin, paper currency, negotiable instruments, and amounts on deposit in banks and other financial institutions. Cash available for agency use includes petty cash funds and cash held in revolving funds which will not be transferred into the U.S. Government General Fund.

Foreign Currency – Consists of the total U.S. dollar equivalent of purchased foreign currencies held in foreign currency fund accounts. Non-purchased foreign currency is limited to the Treasury Index 97X7000 fund account.

Other Monetary Assets - Includes gold, special drawing rights, and U.S. Reserves in the International Monetary Fund. This category is principally for use by the Department of the Treasury.

Fluctuations and/or Abnormalities

Cash and foreign currency increased $570,722 thousand or 60 percent, primarily to support the contingency missions Operation Iraqi Freedom and Operation Enduring Freedom. Overall foreign currency increased approximately $182,604 thousand or 105 percent, which includes currency to pay foreign vendors and cash in the custody of foreign agents primarily in support of the Army's forward deployed tactical units. Other increases occurred in the U.S. Army Corps of Engineers as the Republic of Korea increased agreements for reimbursable work to be performed.

Other Information Related to Cash and Other Monetary Assets

Cash and foreign currency reported consists primarily of cash held by disbursing officers to carry out their paying, collecting and foreign currency accommodation exchange mission. Foreign currency is valued using the Department of Treasury Prevailing Rate of Exchange. This rate is the most favorable rate that would legally be available to the U.S. Government's acquisition of foreign currency for its official disbursements and accommodation of exchange transactions. All of the Army's cash and foreign currency, $1,525,090 thousand, is non-entity and is therefore restricted.

Note Reference

See Note Disclosure 1. J. - Foreign Currency for additional discussion on financial reporting requirements and DoD policies.

Note 8. A. Direct Loan and/or Loan Guarantee Programs

1. Direct Loan and/or Loan Guarantee Programs: The entity operates the following direct loan and/or Loan guarantee program(s):

Military Housing Privatization Initiative

Armament Retooling & Manufacturing Support Initiative

2. Other Information:

Armament Retooling and Manufacturing Support Initiative

The Armament Retooling and Manufacturing Support Initiative (ARMS), Title 10 United States Code (USC) 4551-4555, is designed to encourage commercial use of the Army's inactive ammunition plants through many incentives for businesses willing to locate to a government ammunition production facility. These facilities have production capacity greater than the current military requirements; however, this capacity could be needed in the event of a major war. The revenues from the property rental are used to pay for the operation, maintenance and environmental clean up at the facilities. This savings in overhead cost lowers the production cost of the goods manufactured and funds the environmental clean up at no cost to the government.

The Army, by means of ARMS Initiative legislation, established a loan guarantee program to facilitate commercial firms' use of specified ammunition manufacturing facilities. The Army and Department of Agriculture Rural Business-Cooperative Service (RBS) established a Memorandum of Understanding for the RBS to administer the ARMS Initiative Loan Guarantee Program (AILG).

Note 8.B. Direct Loans Obligated After FY 1991

Not Applicable

Note 8.C. Total Amount of Direct Loans Disbursed

Not Applicable

Note 8.D. Subsidy Expense for Post-1991 Direct Loans

Not Applicable

Note 8.E. Subsidy Rate for Direct Loans

Not Applicable

Note 8.F. Schedule for Reconciling Subsidy Cost Allowance Balances for Post-1991 Direct Loans

Not Applicable

Note 8.G. Defaulted Guaranteed Loans from Post-1991 Guarantees

Not Applicable

Note 8.H. Guaranteed Loans Outstanding

As of September 30 (Amounts in thousands)	Outstanding Principal, Guaranteed Loans, Face Value	Amount of Outstanding Principal Guaranteed
Guaranteed Loans Outstanding:		
1. Military Housing Privatization Initiative	$0	$0
2. Armament Retooling & Manufacturing Support Initiative	$27,051	$24,267
3. Total	$27,051	$24,267
2004		
New Guaranteed Loans Disbursed:		
1. Military Housing Privatization Initiative	$0	$0
2. Armament Retooling & Manufacturing Support Initiative	$0	$0
3. Total	$0	$0
2003		
New Guaranteed Loans Disbursed:		
1. Military Housing Privatization Initiative	$0	$0
2. Armament Retooling & Manufacturing Support Initiative	$0	$0
3. Total	$0	$0

Note 8.I. Liability for Post-1991 Loan Guarantees, Present Value

As of September 30
(Amounts in thousands)

	2004	2003
Loan Guarantee Program Title		
1. Military Housing Privatization Initiative	$0	$0
2. Armament Retooling & Manufacturing Support Initiative	12,293	1,273
3. Total	$12,293	$1,273

4. Other Information:

Fluctuations and/or Abnormalities

Total Loan Guarantee Liabilities increased $11,020 thousand between FY 2003 and FY 2004 primarily due to the new FY 2004 loan obligation and a liability for an impending loss claim.

Note 8.J. Subsidy Expense for Post-1991 Loan Guarantees

As of September 30
(Amounts in thousands)

2004	Interest Differential	Defaults	Fees	Other	Total
1. Subsidy Expense for New Loan Guarantees Disbursed:					
Military Housing Privatization Initiative	$0	$0	$0	$0	$0
Armament Retooling & Manufacturing Support Initiative	0	174	(56)	0	118
Total	$0	$174	($56)	$0	$118

2003	Interest Differential	Defaults	Fees	Other	Total
2. Subsidy Expense for New Loan Guarantees Disbursed:					
Military Housing Privatization Initiative	$0	$0	$0	$0	$0
Armament Retooling & Manufacturing Support Initiative	0	145	(8)	37	174
Total	$0	$145	($8)	$37	$174

2004	Modifications	Interest Rate Reestimates	Technical Reestimates	Total Reestimates	Total
3. Loan Guarantee Modifications and Reestimates:					
Military Housing Privatization Initiative	$0	$0	$0	$0	$0
Armament Retooling & Manufacturing Support Initiative	0	0	7,451	0	7,451
Total	$0	$0	$7,451	$0	$7,451

2003	Modifications	Interest Rate Reestimates	Technical Reestimates	Total Reestimates	Total
4. Loan Guarantee Modifications and Reestimates:					
Military Housing Privatization Initiative	$0	$0	$0	$0	$0
Armament Retooling & Manufacturing Support Initiative	0	0	0	0	0
Total	$0	$0	$0	$0	$0

2000	2004	2003
5. Total Loan Guarantee Subsidy Expense:		
Military Housing Privatization Initiative	$0	$0
Armament Retooling & Manufacturing Support Initiative	7,569	174
Total	$7,569	$174

6. Other Information:

Total Loan Guarantee Subsidy Expense increased $7,395 thousand between FY 2003 and FY 2004, primarily due to a liability for an impending loss claim. See Note 8.L Schedule for Reconciling Loan Guarantee Liability Balances for Post-1991 Loan Guarantees.

Note 8.K. Subsidy Rate for Loan Guarantees

Loan Guarantees:	Interest Supplements	Defaults	Fees and other Collections	Other	Total
1. Military Housing Privatization Initiative:	0.00%	0.00%	0.00%	0.00%	0.00%
2. Armament Retooling & Manufacturing Support Initiative	0.00%	4.97%	-1.60%	0.00%	3.37%

3. Other Information:

This budgeted subsidy rate in effect for the FY 2004 remained the same for the entire fiscal year.

Note 8.L. Schedule for Reconciling Loan Guarantee Liability Balances for Post-1991 Loan Guarantees

Beginning Balance, Changes and Ending Balance (Amounts in thousands)	2004	2003
1. Beginning Balance of the Loan Guarantee Liability	$1,273	$730
2. Add: Subsidy Expense for Guaranteed Loans Disbursed during the Reporting Years by Component		
A. Interest Supplement Costs	$0	$0
B. Default Costs (Net of Recoveries)	174	145
C. Fees and Other Collections	(56)	(8)
D. Other Subsidy Costs	0	37
E. Total of the above Subsidy Expense Components	$118	$174
3. Adjustments		
A. Loan Guarantee Modifications	$0	$0
B. Fees Received	0	324
C. Interest Supplements Paid	0	0
D. Foreclosed Property and Loans Acquired	0	0
E. Claim Payments to Lenders	0	0
F. Interest Accumulation on the Liability Balance	3,451	45
G. Other	0	0
H. Total of the above Adjustments	$3,451	$369
4. Ending Balance of the Loan Guarantee Liability before Re-estimates	$4,842	$1,273
5. Add or Subtract Subsidy Re-estimates by Component		
A. Interest Rate Re-estimate	0	0
B. Technical/default Re-estimate	7,451	0
C. Total of the above Re-estimate Components	$7,451	$0
6. Ending Balance of the Loan Guarantee Liability	$12,293	$1,273

7. Other Information:

Note 8.M. Administrative Expense

As of September 30 (Amounts in thousands)	2004	2003
1. Direct Loans:		
Military Housing Privatization Initiative	$0	$0
Armament Retooling & Manufacturing Support Initiative	0	0
Total	$0	$0
2. Loan Guarantees:		
Military Housing Privatization Initiative	$0	$0
Armament Retooling & Manufacturing Support Initiative	0	14
Total	$0	$14

3. Other Information:

No administrative expenses were processed in FY 2004.

Note 9. Inventory and Related Property

As of September 30 (Amounts in thousands)	2004	2003
1. Inventory, Net (Note 9.A.)	$204,707	$293,228
2. Operating Materials & Supplies, Net (Note 9.B.)	37,443,014	32,383,430
3. Stockpile Materials, Net (Note 9.C.)	0	0
4. Total	$37,647,721	$32,676,658

Note 9.A. Inventory, Net

	2004			2003	
As of September 30 (Amounts in thousands)	Inventory, Gross Value	Revaluation Allowance	Inventory, Net	Inventroy, Net	Valuation Method
1. Inventory Categories:					
A. Available and Purchased for Resale	$20,470	($7,702)	$12,768	$33,686	LAC
B. Held for Repair	0	0	0	0	
C. Excess, Obsolete, and Unserviceable	13,006	(13,006)	0	0	NRV
D. Raw Materials	0	0	0	0	
E. Work in Process	191,939	0	191,939	259,542	SP
F. Total	$225,415	($20,708)	$204,707	$293,228	

Legend for Valuation Methods:

Adjusted LAC = Latest Acquisition Cost, adjusted for holding gains and losses
NRV = Net Realizable Value
O = Other
SP = Standard Price
AC = Actual Cost

2. Restrictions of Inventory Use, Sale, or Disposition:

There are no restrictions on the use, sale, or disposition of inventory except in the following situations:

1) Distributions without reimbursements made when authorized by DoD directives;

2) War Reserve Material includes fuels and subsistence items that are considered restricted; and
3) Inventory, with the exception of safety stocks, may be sold to foreign, state and local governments, private parties, and contractors in accordance with current policies and guidance or at the direction of The President.

3. Other Information:

General Composition of Inventory

Inventory is comprised of ammunition in the Conventional Ammunition Working Capital Fund (CAWCF). Inventory is tangible personal property that is:

1) Held for Sale, or Held for Repair for eventual sale;
2) In the process of production for sale; or
3) To be consumed in the production of goods for sale or in the provision of services for a fee.

Excess, obsolete and unserviceable inventory is condemned material that must be retained for management purposes. 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. The U.S. Standard General Ledger does not include a separate Work-in-Process account unrelated to sales.

Decision Criteria for Identifying the Category to Which Inventory is Assigned

Managers determine which items are more costly to repair than replace. Items retained for management purposes are coded condemned. The net value of these items is zero, and is shown as excess, obsolete, and unserviceable. The category held for sale includes all issuable material. Economically reparable material is categorized as held for repair. Prior to FY 2002, the Army showed potentially redistributable material, regardless of condition, as excess, obsolete, and unserviceable.

Fluctuations and/or Abnormalities

The CAWCF reports balances for Inventory Available and Purchased for Resale; Inventory Excess, Obsolete, and Unserviceable; and Inventory Work-in-Process. Inventory sales are primarily made to the Military Departments. CAWCF Total Inventory, Net, showed an overall decrease of $88,521 thousand or 30 percent, in FY 2004. CAWCF Available and Purchased for Resale Inventory, Net showed a decrease of $20,918 thousand or 62 percent with the decrease attributable to the close out of CAWCF Inventory Work-in-Process that decreased $67,603 thousand or 26 percent. The year to year decrease in CAWCF Inventory is expected as the Army's CAWCF progresses to final closeout by September 30, 2005. However, the fund will remain open through September 30, 2007 to complete the cleanup and disposal of CAWCF-owned inventories of munitions, components and general supplies. Effective September 30, 1998, CAWCF officially closed for the acceptance of new orders for the procurement of Conventional Ammunitions. Currently undelivered customer orders have not been filled because of incidents beyond control at production facilities. This includes litigation and lack of government furnished materials required to complete production on time. All deliveries of existing CAWCF orders are expected to be made prior to September 2005. The CAWCF final financial position will be determined before CAWCF's October 31, 2005 closeout. The above dates are not firm and are subject to change. The majority of CAWCF Work-in-Process is performed at Government Owned Contractor Operated plants.

Note Reference

See Note Disclosure 1. M. - Significant Accounting Policies for additional discussion on financial reporting requirements and DoD policies governing Inventory and related Property.

Note 9.B. Operating Materials and Supplies, Net

As of September 30	2004			2003	
(Amounts in thousands)	OM&S Gross Value	Revaluation Allowance	OM&S, Net	OM&S, Net	Valuation Method
1. OM&S Categories:					
A. Held for Use	$37,443,014	$0	$37,443,014	$32,383,430	LAC
B. Held for Repair	0	0	0	0	
C. Excess, Obsolete, and Unserviceable	980,073	(980,073)	0	0	SP
D. Total	$38,423,087	($980,073)	$37,443,014	$32,383,430	

Legend for Valuation Methods:

Adjusted LAC = Latest Acquisition Cost, adjusted for holding gains and losses.
SP = Standard Price

2. Restrictions on OM&S:

Tonnage

The total tonnage of munitions stock, to include chemical stocks awaiting destruction for FY 2004 and out years, is 411,969 tons.

Balances

The Army reported $5,000,000 thousand of Operating Materials and Supplies (OM&S) Held for Future Use. This amount represents ammunition held under a host nation treaty agreement and is not intended for use by U.S. Forces. The ammunition is intended for use in defense of the host nation by the host nation.

3. Other Information:

General Composition of OM&S

OM&S includes spare and repair parts, ammunition, and tactical missiles.

Changes in the Criteria for Identifying the Category to which OM&S are Assigned

The category Held for Use includes all issuable material. Economically reparable material is categorized as held for repair.

Decision Criteria for Identifying the Category to which OM&S are Assigned

Managers determine which items are more costly to repair than to replace. Items retained for management purposes are coded condemned. The net value of these items is zero, and is shown as Excess, Obsolete, and Unserviceable.

Other Information Related to OM&S, Net

Fluctuations and/or Abnormalities

OM&S, Net, increased by $5,059,584 thousand or 16 percent between FY 2003 and FY 2004. The net increase is attributable to $2,827,358 thousand increase in Missile Procurement, Army OM&S reported by the U.S. Army Aviation and Missile Command and a $2,320,112 thousand increase being reported in the Worldwide Ammunition Reporting System (WARS). The increase in Missile Procurement, Army is the result of movement of funding from Procurement, Defense Wide to Missile Procurement, Army for the Patriot Advance Capability 3 in support of the Global War on Terrorism. The WARS increase is the result of Operation Iraqi Freedom, movement to uses other than basic load and training, retrograde and asset movement from troops to ammunition storage points, and Central Command (CENTCOM) inventory reconciliation.

Total Excess, Obsolete and Unserviceable

The Army establishes an allowance for excess, obsolete, and unserviceable OM&S and inventory at 100 percent of the carrying amount in accordance with DoD policy.

Government Furnished Material (GFM) and Contractor Acquired Material (CAM)

The value of the Army's GFM and CAM in the hands of contractors is normally not included in the OM&S values reported above. The DoD is presently reviewing its process for reporting these amounts in an effort to determine the appropriate accounting treatment and the best method to annually collect and report required information without duplicating information in other existing logistics systems.

Note Reference

See Note Disclosure 1. M. - Significant Accounting Policies for additional discussion on financial reporting requirements and DoD policies governing Inventory and Related Property.

Note 9.C. Stockpile Materials, Net

Not Applicable

Note 10. General PP&E, Net

As of September 30 (Amounts in thousands)	2004					2003
	Depreciation/ Amortization Method	Service Life	Acquisition Value	(Accumulated Depreciation/ Amortization)	Net Book Value	Prior FY Net Book Value
1. Major Asset Classes:						
A . Land	N/A	N/A	$464,254	N/A	$464,254	$438,580
B. Buildings, Structures, and Facilities	S/L	20 Or 40	42,244,123	($26,647,486)	15,596,637	14,216,010
C. Leasehold Improvements	S/L	lease term	11,455	(9,311)	2,144	1,807
D. Software	S/L	2-5 Or 10	391,865	(99,801)	292,064	51,442
E. General Equipment	S/L	5 or 10	2,682,225	(1,755,619)	926,606	95,272,905
F. Military Equipment	S/L	Various	383,210,000	(292,930,000)	90,280,000	0
G. Assets Under Capital Lease[1]	S/L	lease term	166,071	(130,074)	35,997	44,384
H. Construction-in-Progress	N/A	N/A	5,495,062	N/A	5,495,062	5,294,164
I. Other			18,808	0	18,808	18,614
J. Total General PP&E			$434,683,863	($321,572,291)	$113,111,572	$115,337,906

[1] Note 15.B for additional information on Capital Leases

Legend for Valuation Methods:

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

2. Other Information:

Fluctuations and/or Abnormalities

- The net book value (NBV) of Buildings, Structures, and Facilities increased by $1,380,627 thousand or 10 percent. This increase is from the continued recording of previously omitted real property data. Personnel from the Assistant Secretary of the Army (Financial Management & Comptroller) and Assistant Chief of Staff for Installation Management (ACSIM) determined that the Army is the proper reporting entity for this data.

- The NBV of Leasehold Improvements increased $337 thousand or 19 percent. The increase is attributed to more accurate reporting as a result of quality assurance/quality control reviews by the ACSIM.
- The Army reported an increase in Software NBV of $240,622 thousand or 468 percent. This increase is attributed to an initiative to report internal use software such as: Reserve Component Automation System, Joint Computer Aided Acquisition and Logistic Support, Transportation Information System Block I, Property Book Unit Supply Enhancement and various other projects.
- In FY 2004, Treasury issued guidance to report military equipment and general equipment on separate lines for footnote reporting. Therefore, FY 2003 equipment includes the military equipment NBV of $94,430,000 thousand and general equipment NBV of $842,905 thousand. This change causes the amounts reported in the table to be inaccurate in their comparative breakdown of General and Military Equipment. The fluctuations explained below are the accurate representations of General and Military Equipment:
  - The NBV of General Equipment increased $83,701 thousand or 10 percent due primarily to the U.S. Army Materiel Command- Logistics Support Activity reporting previously omitted general equipment.
  - The NBV of Military Equipment decreased $4,150,000 thousand or 4 percent due to the revision of the estimate by the Bureau of Economic Analysis (BEA). See below for additional information.
- Assets Under Capital Lease – See explanation in Note 10.A.

Relevant Information for Comprehension

Military Equipment

In FY 2004, the Army reported military equipment with an acquisition value of $383,210,000 thousand and accumulated depreciation of $292,930,000 thousand for a NBV of $90,280,000 thousand.

The Federal Accounting Standards Advisory Board issued Statement of Federal Financial Accounting Standards No. 23, *Eliminating the Category National Defense Property, Plant, and Equipment,* in May 2003. This standard, which is effective for accounting periods beginning after September 30, 2002, established generally accepted accounting principles (GAAP) for valuing and reporting military equipment (e.g., ships, aircraft, combat vehicles, weapons) in Federal financial statements. The standard requires the capitalization and depreciation of the cost of military equipment, including the cost of modifications and upgrades.

The DoD has determined that it is not practical at this time to accumulate from internal records the information necessary to value military equipment in accordance with GAAP, because the Army and DoD are currently working to revise their accounting processes and systems to support informational needs of management and compliance with GAAP. In the interim, DoD will base the value of military equipment for financial statement presentation purposes on data provided by the BEA, Department of Commerce.

The data provided by BEA consist of investment and net book value data for 84 groups of military equipment such as tracked vehicles, aircraft, ships and combat vehicles. DoD adjusted BEA data to eliminate equipment items that are not accounted for as military equipment, such as spares, munitions, and inventory items, which are accounted for and reported as Inventory and Related Property.

BEA uses DoD budget, expenditure, and delivery data to calculate the Army's annual investment in military equipment, after recognizing any equipment transfers or war losses. BEA recently revised its FY 2003 data, resulting in a decrease of 6 percent in the Acquisition Value and an increase of 4 percent in the Accumulated Depreciation of the Army military equipment. Previous data was based, in part, on BEA projections because source data was not available. The revised data for FY 2003 is based on updated and more complete source data. Further, the revised data reflects changes in the methods and data BEA uses to estimate the investment in, and depreciation of, military equipment resulting from BEA's 2003 Comprehensive Revision of the National Income and Product Accounts. A major factor in the reduction of the Acquisition Value of military equipment was new data that showed that governments purchased a smaller proportion of the domestic supply of software than had previously been estimated.

Other

The $18,808 thousand for Other represents the projected value of forest product sales (timber reserves) for FY 2004.

Note Reference

See Note Disclosure 1. O. – General Property, Plant and Equipment for additional discussion on financial reporting requirements and DoD policies.

Note 10.A. Assets Under Capital Lease

As of September 30 (Amounts in thousands)	2004	2003
1. Entity as Lessee, Assets Under Capital Lease:		
A. Land and Buildings	$166,071	$166,071
B. Equipment	0	0
C. Other	0	0
D. Accumulated Amortization	(130,074)	(121,687)
E. Total Capital Leases	$35,997	$44,384

2. Description of Lease Arrangements:

3. Other Information:

Fluctuations and/or Abnormalities

The Assets under Capital Lease decreased by $8,387 thousand or 19 percent due to straight-line depreciation of leased assets.

Relevant Information for Comprehension

The Army is the lessee in eight Section 801 Family Housing Leases for two on-post and six off-post housing facilities. These leases have between four and ten years remaining on their terms. As shown in Note 15.A., the liability is valued at $12,765 thousand for current and $46,632 thousand for non-current. The future executory and imputed interest costs, as shown in Note 15.B., are $14,765 thousand and $13,379 thousand, respectively. Future executory costs are estimates based on historical data. The imputed interest that was necessary to reduce the net minimum lease payments to the present value was calculated at the incremental borrowing rate at the inception of the leases.

Note Reference

See Note Disclosure 1. Q. - Significant Accounting Policies for additional discussion on financial reporting requirements and DoD policies governing leases.

Note 11. Liabilities Not Covered by Budgetary Resources

As of September 30 (Amounts in thousands)	2004	2003
1. Intra-governmental Liabilities		
A. Accounts Payable	$0	$0
B. Debt	0	0
C. Environmental Liabilities	0	0
D. Other	593,847	382,806
E. **Total Intra-governmental Liabilities**	$593,847	$382,806
2. Non-Federal Liabilities		
A. Accounts Payable	$73,766	$0
B. Military Retirement Benefits and Other Employment-Related Actuarial Liabilities	1,632,843	1,761,317
C. Environmental Liabilities	37,494,670	34,503,765
D. Loan Guarantee Liability	0	0
E. Debt Held by Public	0	0
F. Other Liabilities	4,871,124	5,566,897
G. **Total Non-Federal Liabilities**	$44,072,403	$41,831,979
3. Total Liabilities Not Covered by Budgetary Resources	$44,666,250	$42,214,785
4. Total Liabilities Covered by Budgetary Resources	$19,584,078	$18,174,918
5. Total Liabilities	$64,250,328	$60,389,703

Liabilities Not Covered by Budgetary Resources

Liabilities Not Covered by Budgetary Resources are those liabilities which are not considered funded by realized budgetary resources as of the balance sheet date.

Reporting requirements for this note changed in FY 2004. The FY 2003 Note 11 comparison was total Liabilities Covered and Not Covered by Budgetary Resources. In FY 2004, the comparison is only for Liabilities Not Covered by Budgetary Resources. The schedule below identifies the Army Other Intragovernmental and Non-Federal liabilities. Fluctuation explanations are presented in Note 15.

(Amounts in thousands)

Intragovernmental Liabilities-Other	FY 2004	FY 2003
FECA	$281,613	$156,445
Unemployment Benefits	133,628	78,516
Cancelled Receivables	95,693	0
Judgment Fund	81,923	144,221
No FEAR	990	0
Education Benefits Fund	0	3,624
Total Intragovernmental- Other	$593,847	$382,806
Non-Federal Liabilities - Other Liabilities		
Annual Leave	$2,656,508	$2,634,641
Nonenvironmental – Disposal	1,325,886	1,192,935
Contingent Liabilities	742,237	1,335,090
Iraqi Seized Cash	113,430	278,139
Capital Leases	33,063	44,549
Cancelled Appropriations	0	81,543
Total Non-Federal- Other	$4,871,124	$5,566,897

The FY 2004 revised Treasury Financial Manual guidance affected the reporting of several accounts. Cancelled Receivables was first reported in 2nd Quarter. The Judgment Fund liability for the Notification and Federal Employee Antidiscrimination and Retaliation (No FEAR) Act of 2002 was first reported in 3rd

Quarter. Cancelled Appropriations was changed from Non-Federal Other Liabilities and since 3rd Quarter is being reported as Accounts Payable. Education Benefits Fund changed from Unfunded to Funded in 4th Quarter, FY 2004.

Note Reference

For Additional Line Item discussion, see:
Note 2, Nonentity and Entity Assets
Note 8, Direct Loan and/or Loan Guarantee Programs
Note 12, Accounts Payable
Note 13, Debt
Note 14, Environmental Liabilities and Disposal Liabilities
Note 15, Other Liabilities
Note 16, Commitments and Contingencies
Note 17, Military Retirement Benefits and Other Employment Related Actuarial Liabilities
Note 23, Disclosures Related to the Statement of Custodial Activity

Note 12. Accounts Payable

	2004			2003
As of September 30 (Amounts in thousands)	Accounts Payable	Interest, Penalties, and Administrative Fees	Total	Total
1. Intra-governmental Payables:	$1,706,731	N/A	$1,706,731	$1,084,965
2. Non-Federal Payables (to the Public):	$9,460,025	$169	$9,460,194	$9,089,097
3. Total	$11,166,756	$169	$11,166,925	$10,174,062

4. Other Information:

Intragovernmental Accounts Payable consists of amounts owed to other federal agencies for goods or services ordered and received but not paid. Interest, penalties and administrative fees are not applicable to intragovernmental payables. Non-Federal Accounts Payable (to the Public) are payables to entities other than the federal government.

Fluctuations and/or Abnormalities

Intragovernmental Accounts Payable

Intragovernmental Accounts Payable with entities other than the Army General Fund increased $621,766 thousand or 57 percent, in FY 2004. Increases were reported by the following activities (amounts in thousands).

Activities/Trading Partner	FY 2004	FY 2003	Change	Percent Change
General Service Administration	$364,219	$0	$364,219	100
US Transportation Command Component	121,546	374,156	(252,610)	(68)
Department of the Treasury	152,583	0	152,583	100
Defense Logistics Agency Component	290,829	103,781	187,048	180
Tricare Management Agency Component Level	7,897	100,927	(93,030)	(92)
Department of Labor	86,502	0	86,502	100
Department of Energy	31,810	0	31,810	100
Homeland Security	30,949	0	30,949	100
Environmental Protection Agency	24,901	0	24,901	100
Navy General Fund Component Level	22,323	4,294	18,029	420
Navy WCF Component Level	33,598	17,241	16,357	95

(continued)

Activities/Trading Partner	FY 2004	FY 2003	Change	Percent Change
Other Defense Organizations General Fund Component Level	2,063	16,014	(13,951)	(87)
Army Working Capital Fund Component Level	371,336	365,836	5,500	2
Department of Agriculture	12,518	0	12,518	100
Department of State	11,277	0	11,277	100
Other Fluctuations	142,379	102,717	39,664	39
Totals	**$1,706,730**	**$1,084,966**	**$621,766**	**57**

The increase is attributable to improved business processes for reporting Accounts Payable with agencies outside of DoD for FY 2004. This resulted in an overall increase in Accounts Payable of $738,651 thousand or 119 percent of the total increase in Intragovernmental Accounts Payable.

Non-Federal Accounts Payable

Non-Federal payables increased $371,097 thousand or 4 percent in FY 2004. The majority of the increase occurred in appropriations that received additional funding to support the contingency missions Operations Enduring Freedom, Iraqi Freedom, and Noble Eagle. The support included the activation of reserve personnel, the maintenance of warfighting equipment, and the replacement of equipment lost or damaged in active conflict. Other areas of support included warfighting readiness, force protection, anti-terrorism base operations, and other security programs.

Relevant Information for Comprehension

Mapping Changes

In FY 2004, Treasury Financial Manual guidance changed the report mapping requiring all entities to report Accounts Payable-Cancelled Appropriations as part of Accounts Payable. This resulted in an increase of $73,766 thousand for FY 2004.

Undistributed Disbursements

Undistributed disbursements are the difference between disbursements/collections recorded at the detailed level to a specific obligation, payable, or receivable in the activity field records versus those reported by the U.S. Treasury via the reconciled DD 1329, Statement of Transactions and DD 1400, Statement of Interfund.

Supported undistributed disbursements are allocated to Non-Federal Accounts Payable. As a result, Accounts Payable was adjusted downwards in the amount of $1,797,162 thousand. Unsupported undistributed disbursements were taken from the Undistributed Disbursements and Collections Report, HDF 090, and recorded in U.S. Standard General Ledger account 2120, Disbursements in Transit.

Intragovernmental Eliminations

The Army accounting systems do not capture trading partner data at the transaction level in a manner that facilitates trading partner aggregations for intra-agency sales. Therefore, the Army was unable to reconcile intragovernmental accounts payable to the related intragovernmental account receivable that generated the payable.

The DoD summary level seller Accounts Receivables were compared to the Army Accounts Payable. An adjustment was posted to Accounts Payable based on the comparison with the Accounts Receivable of the DoD Components providing goods and services to the Army. Intra-governmental Accounts Payable were adjusted downward for $977,479 thousand while Non-Federal Accounts Payable were adjusted upward for the same amount. The Army intends to develop long-term systems improvements that will include sufficient upfront edits and controls to eliminate the need for after-the-fact reconciliations. In addition, $1,292,676 thousand of intra-Army General Fund transactions were eliminated leaving a balance of $1,706,730 thousand.

Note Reference

See Note Disclosure 1. G. – Accounting for Intragovernmental Activities for additional discussion on financial reporting requirements and the DoD policies.

Note 13. Debt

Not Applicable.

Note 14. Environmental Liabilities and Disposal Liabilities

As of September 30 (Amounts in thousands)	2004 Current Liability	2004 Noncurrent Liability	2004 Total	2003 Total
1. Environmental Liabilities – Non Federal				
A. Accrued Environmental Restoration (DERP funded) Costs:				
1. Active Installations--Environmental Restoration (ER)	$846,688	$2,673,653	$3,520,341	$3,696,102
2. Active Installations--ER for Closed Ranges	26,222	5,754,833	5,781,055	3,182,708
3. Formerly Used Defense Sites (FUDS) -- ER	341,026	3,980,250	4,321,276	4,239,384
4. FUDS--ER for Transferred Ranges	149,299	13,934,982	14,084,281	13,624,347
B. Other Accrued Environmental Costs (Non-DERP funds)				
1. Active Installations--Environmental Corrective Action	38,385	220,649	259,034	287,857
2. Active Installations--Environmental Closure Requirements	9,822	41,393	51,215	37,074
3. Active Installations--Environ.Response at Active Ranges	62,500	205,132	267,632	264,368
4. Other	0	0	0	0
C. Base Realignment and Closure (BRAC)				
1. BRAC Installations--Environmental Restoration (ER)	84,005	513,342	597,347	518,716
2. BRAC Installations--ER for Transferring Ranges	5,571	474,551	480,122	496,075
3. BRAC Installations--Environmental Corrective Action	1,637	23,328	24,965	48,031
4. Other	209,437	0	209,437	190,435
D. Environmental Disposal for Weapons Systems Programs				
1. Nuclear Powered Aircraft Carriers	0	0	0	0
2. Nuclear Powered Submarines	0	0	0	0
3. Other Nuclear Powered Ships	0	0	0	0
4. Other National Defense Weapons Systems	0	0	0	0
5. Chemical Weapons Disposal Program	1,096,909	9,672,558	10,769,467	10,810,315
6. Other	0	0	0	0
2. Total Environmental Liabilities:	$2,871,501	$37,494,671	$40,366,172	$37,395,412

3. Other Information Related to Environmental Liabilities:

Relevant Information For Comprehension

Environmental Cost Liabilities

The Defense Environmental Restoration Program (DERP) was established by Section 211 of the Superfund

Amendments and Reauthorization Act of 1986 codified in Title 10 of the United States Code (USC) 2701. Related sections in Title 10 of the USC, 2701-2706 and 2810-2811 further define the program. The DERP is implemented in accordance with the Department of Defense (DoD) Directive 4715.1, Environmental Security, February 24, 1996; and DoD Instruction 4715.7, Environmental Restoration Program, April 22, 1996, and the Management Guidance for the Defense Environmental Restoration Program, September 28, 2001. Environmental liabilities for the Department of the Army DERP and the Base Realignment and Closure (BRAC) are prepared in accordance with the Management Guidance for the Defense Environmental Restoration Program and the DoD Financial Management Regulation (FMR) 7000.14.

The assigned total current liability cost includes the current year budget (FY 2005) and the total prior year (FY 2004) unliquidated obligations.

There is no unrecognized portion of the estimated total cleanup cost associated with general property, plant and equipment and there are no material changes in the total estimated liability due to changes in laws, technology, or plans. The major change in technology affecting the liability estimate was standardizing use of the estimating tools consistently across the Army programs.

The estimates used for environmental liability calculations are estimates of the cost to complete all activities at a site of environmental concern. The cost estimates are calculated at the site level using a validated cost-estimating model or an engineered cost and entered into a database. There were no changes to the total liability cost due to inflation, deflation, or applicable laws and regulations.

Environmental Disposal Cost Liabilities

Army Accrued Environmental Costs (Non-DERP) – The Resource Conservation and Recovery Act (RCRA), as well as host nation requirements, require the Army to take corrective actions to clean up areas where there has been a release related to hazardous material/waste handling and/or storage activities. A release includes any activity that resulted in contamination due to disposal practices, leaks, spills, and other activities that create a risk to public health or the environment. Failure to comply with legal mandates and agreements can put the Army at risk of fines and penalties.

Range Characteristics

For FY 2004 and FY 2003, the Army estimated that its environmental liability at closed, transferred, and transferring ranges was $20,345,458 thousand and $17,303,130 thousand, respectively. The Army has completed its inventory of all closed, transferred and transferring ranges.

Closed Ranges

The Army identified $5,781,055 thousand to characterize, investigate and cleanup closed ranges. An inventory of closed ranges was completed in December 2003. Closed ranges have been taken out of service as a range and put to new use (incompatible with range activities), or are not considered by the Military Departments to be a potential range area. A closed range is still under the control of a DoD Component.

Transferring Ranges

Site level investigations reveal that the total environmental liability for these types of ranges is $480,122 thousand. Transferring ranges are proposed for transfer or will be returned from DoD to another entity, including other federal entities.

Transferred Ranges

An inventory of these ranges has been completed and the estimated liability for those ranges is $14,084,281 thousand. These are properties formerly used as a military range that are no longer under military control and have been leased by DoD, transferred, or returned from the DoD to another entity, including federal entities.

Active Ranges

At this time, the Army is conducting only one active range investigation and characterization, that being for Massachusetts Military Reservation. The cost of characterization and investigation is $267,632 thousand. This amount pays for sampling and analysis, groundwater monitoring, feasibility studies, soil and groundwater cleanup, and unexploded ordnance (UXO) investigation and response. Active ranges include military ranges that are currently in service and are being regularly used, that are still considered by the cognizant Military Service to be a potential range area, and that have not been put to a new use that is incompatible with range activities.

Methodology Used to Estimate Environmental Liabilities

The Army uses annual cost-to-complete estimates as the basis for the environmental liability calculation. A cost-to-complete estimate is prepared for each site in the DERP in accordance with the Management Guidance for the DERP and the DoD FMR 7000.14.

Accrued Environmental Restoration (DERP Funded) Costs:

For Active Installations the cost-to-complete estimate is collected in the Army Environmental Database - Restoration (AEDB-R). The Unliquidated Obligations (ULO) data are pulled from reports provided by Defense Finance and Accounting Service (DFAS). Non-current liabilities include the cost-to-complete estimates from FY 2006 through program completion in accordance with the Management Guidance for the DERP and the DoD FMR 7000.14. Quarterly updates to the current liability numbers are based on changes to the ULOs reported in DFAS monthly reports.

At Formerly Used Defense Sites (FUDS) properties, the cost-to-complete estimate is collected in the FUDS Management Information System (FUDSMIS). The ULO data are obtained from the U.S. Army Corps of Engineers Financial Management System (CEFMS), which feeds the DFAS monthly reports. Non-current liabilities include the cost-to-complete estimates from FY 2006 through program completion in accordance with the Management Guidance for the DERP and the DoD FMR 7000.14. Quarterly updates to the current liability numbers are based on changes to the unliquidated obligations recorded in CEFMS.

<u>Active Installations – Environmental Restoration (ER) for Closed Ranges</u>

The liability for ER for closed ranges is a developing requirement based on the results of an Army-wide inventory of all ranges. The inventory for closed ranges is 100 percent complete as of December 2003. The ER liability estimate for closed ranges is the probable cost and is based on site level data.

<u>FUDS – Environmental Restoration for Transferred Ranges</u>

The liability for ER for transferred ranges is based on results of site level cost data developed for inventoried properties.

Other Accrued Environmental Costs (Non-DERP Funds):

<u>Active Installations – Environmental Corrective Action</u>

This reflects the total of active projects in the FY 2004 Environmental Program Requirements (EPR) database which are reported under 1) RCRA Subtitle C with Environmental Category (ECAT) Corrective Actions (CORA), 2) RCRA Subtitle D with ECAT CORA, 3) RCRA Subtitle I with ECAT Underground Storage Tanks and the Superfund/Cleanup with all ECATs (including those for Preliminary Assessments/Site Investigations, Remedial Action (CONUS Cleanup), and Removal Actions (Overseas Cleanup). The current liability total reflects costs recorded in the EPR for FY 2004, while the non-current liability total reflects total estimated costs for FY 2005 through FY 2016.

Active Installations – Environmental Closure Requirements

Reflects the total of validated December 2003 (FY 2004) active projects in the EPR database which are reported under 1) the Law/Reg RCRA-C with ECAT Closure Plan (CPLN) and 2) RCRA-D with ECAT CPLN. The current liability total reflects costs recorded in the EPR for FY 2004, while the non-current liability total reflects total estimated costs for FY 2005 through FY 2016.

Active installations – Environmental Response at Active Ranges

The estimated total Non-DERP liability for Environmental Response at Active Ranges reflects costs for the Massachusetts Military Reservation, broken out into current and non-current liabilities. This amount includes soil and groundwater cleanup and UXO detection and removal.

Base Realignment and Closure (BRAC):

For BRAC installations, the cost-to-complete estimate is collected in the AEDB-R. Because BRAC installations are funded separately using the base closure account, restoration and program management are reported as environmental restoration liabilities; munitions response is reported as Environmental Restoration for Transferring Ranges; and compliance is reported as Environmental Corrective Action. For current liabilities, the number is based on the FY 2005 allocation and reported ULOs. Because prior year BRAC ULOs are not identified by individual program, BRAC ULOs are provided as BRAC-Other. Non-current liabilities include the cost-to-complete estimates from FY 2006 through program completion (collected in AEDB-R) in accordance with the Management Guidance for the DERP and the DoD FMR 7000.14. Quarterly updates to the current liability numbers are based on changes to the ULO obligations reported in DFAS monthly reports.

BRAC – Environmental Restoration for Transferring Ranges: The liability for ER for transferring ranges is based on results of an inventory of sites at transferring ranges. The inventory of transferring ranges is 100 percent complete with site level cost data.

Environmental Disposal for Weapons Systems Programs:

The Chemical Demilitarization Program is based on the fiscal year 1986 National Defense Authorization Act (PL 99-145, as amended by subsequent acts) that directed the DoD to destroy the unitary chemical stockpile by April 29, 2004. The Army, as Executive Agent within the DoD, provides policy, direction, and oversight for both the Chemical Stockpile Program and the Non-Stockpile Chemical Materiel Project. As such, the Army is responsible for the safe and economical disposal of the U.S. stockpile of lethal and incapacitating chemical warfare agents and munitions. The program objective is to destroy the U.S. stockpile of unitary chemical agents and munitions in accordance with the public law and the schedules approved by the Defense Acquisition Decision Memorandum dated September 26, 2001, and updated in the April 2003 Acquisition Program Baseline.

Changes in the Liability Estimate (greater than 10 percent change)

The FY 2004 total Active Installations – ER liability for Closed Ranges of $5,781,055 thousand increased 82 percent from $3,182,708 thousand reported in FY 2003. The major factor contributing to the increase is the completion of the Army inventory for closed ranges resulting in 100 percent reporting of site level data.

The FY 2004 total Active Installations – Environmental Corrective Action liability of $259,034 thousand decreased 10 percent from $287,857 thousand reported in FY 2003. The major factors contributing to the changes are improved cost estimates and revised estimated cleanup levels. The FY 2004 total Active Installations – Environmental Closure liability of $51,215 thousand increased 38 percent from the $37,074 thousand liability reported in FY 2003 due to receipt of an updated EPR report with improved cost estimates and site changes (both new sites identified and old ones determined not to require the original estimated costs). Additionally, Class 0 projects (projects with relatively fixed costs such as personnel, training, and hazardous waste disposal) are now included; where they were not in the last year's estimate.

The FY 2004 total BRAC Installations – Environmental Restoration (ER) liability of $597,347 thousand increased 15 percent from $518,716 thousand in FY 2003 due to increased remediation efforts required at several sites. The FY 2004 total BRAC Installations – Environmental Corrective Action liability of $24,965 thousand is a 48 percent decrease from the $48,031 thousand liability reported in FY 2003. The major factor contributing to the decrease is a change in cleanup action required at a site. The FY 2004 BRAC - Other liability increased $19, 002 thousand or 10 percent due to an increase in actual base closure environmental liabilities recorded during the fiscal year.

The Low Level Radioactive Waste (LLRW) Disposal Program facilitates the process of identifying, investigating, and remediating sites contaminated by low-level radioactive waste through RCRA corrective actions or Comprehensive Environmental Response, Compensation, and Liability Act response actions. The program classified its liabilities as possible and remote for FY 2004 financial reporting. This information is disclosed in Note 16, Commitments and Contingencies.

Other Information

Others Category Disclosure Comparative Table (amounts in thousands):

Types	FY 2004	FY 2003
BRAC – Other		
Prior Year BRAC ULOs That Cannot Be Identified To A Specific Program	$ 209,437	$ 190,435
Total	**$ 209,437**	**$ 190,435**

Note 15.A. Other Liabilities

As of September 30 (Amounts in thousands)	2004 Current Liability	Noncurrent Liability	Total	2003 Total
1. Intragovernmental:				
A. Advances from Others	$95,733	$0	$95,733	$56,968
B. Deferred Credits	0	0	0	0
C. Deposit Funds and Suspense Account Liabilities	137,806	0	137,806	67,914
D. Resources Payable to Treasury	0	0	0	0
E. Disbursing Officer Cash	1,525,090	0	1,525,090	952,130
F. Nonenvironmental Disposal Liabilities:				
(1) National Defense PP&E (Nonnuclear)	0	0	0	0
(2) Excess/Obsolete Structures	0	0	0	0
(3) Conventional Munitions Disposal	0	0	0	0
(4) Other	0	0	0	0
G. Accounts Payable-- Cancelled Appropriations	0	0	0	0
H . Judgment Fund Liabilities	82,913	0	82,913	144,222
I. FECA Reimbursement to the Department of Labor	124,634	156,979	281,613	276,419
J. Capital Lease Liability	0	0	0	0
K. Other Liabilities	279,748	0	279,748	172,665
L. Total Intra-governmental Other Liabilities	$2,245,924	$156,979	$2,402,903	$1,670,318
2. Non-Federal:				
A. Accrued Funded Payroll and Benefits	$2,083,447	$0	$2,083,447	$2,310,623
B. Advances from Others	750,119	0	750,119	589,621
C. Deferred Credits	0	0	0	0
D. Loan Guarantee Liability	0	0	0	0
E. Liability for Subsidy Related to Undisbursed Loans	0	0	0	0
F. Deposit Funds and Suspense Accounts	0	0	0	0
G. Temporary Early Retirement Authority	0	0	0	306
H. Nonenvironmental Disposal Liabilities:				
(1) National Defense PP&E (Nonnuclear)	0	0	0	0
(2) Excess/Obsolete Structures	0	0	0	0
(3) Conventional Munitions Disposal	0	1,325,886	1,325,886	1,192,935
(4) Other	0	0	0	0
I. Accounts Payable--Cancelled Appropriations	0	0	0	81,543
J. Accrued Unfunded Annual Leave	2,656,508	0	2,656,508	2,634,641
K. Accrued Entitlement Benefits for Military Retirees and Survivors	0	0	0	0
L. Capital Lease Liability	12,765	46,632	59,397	71,139
M. Other Liabilities	1,051,598	742,237	1,793,835	2,506,512
N. Total Non-Federal Other Liabilities	$6,554,437	$2,114,755	$8,669,192	$9,387,320
3. Total Other Liabilities:	$8,800,361	$2,271,734	$11,072,095	$11,057,638

4. Other Information Pertaining to Other Liabilities:

Intragovernmental Liabilities

Advances from Others increased $38,765 thousand or 68 percent. The majority of the increase is attributable to advances to the US Army Corps of Engineers for war rebuilding in Afghanistan and Iraq. In addition, the US Army Medical Research and Materiel Command advances with the National Institute of Allergy and Infectious Diseases increased for research on human immunodeficiency virus/acquired immune deficiency syndrome (HIV/AIDS).

The balance reported for the Deposit Funds and Suspense Account liabilities increased by $69,892 thousand or 103 percent in accounts impacted by contingency operations. The majority is attributable to increase in the miscellaneous suspense and deposit funds is due to $37,009 thousand increase in Army Member Savings Deposits caused by an increase in deployed soldiers drawing imminent danger pay who are authorized to deposit funds and later withdraw the funds with interest; $19,896 thousand in Withheld State Income Taxes; $14,859 thousand in Small Escrow Accounts due to the increase of Soldiers using the post office and Army Air Force Exchange Service in Kuwait and Iraq.

Disbursing Officer Cash increased $572,960 thousand or 60 percent primarily to support contingency missions Operation Iraqi Freedom and Operation Enduring Freedom.

Judgment Fund Liabilities net decreased $61,309 thousand or 43 percent based on litigation settlements. New guidance for the Judgment Fund Liability for the Notification and Federal Employee Antidiscrimination and Retaliation (No FEAR) Act of 2002 was reported for the first time in FY 2004 to comply with Treasury Financial Manual Guidance.

Other Liabilities increased $107,083 thousand or 62 percent. The majority is attributable to Cancelled Accounts Receivables of $95,693 thousand that was reported for the first time in FY 2004. Other Liabilities for employee benefits account for the remaining of $11,390 thousand increase. Voluntary Separation Incentive Pay (VSIP) closed this fiscal year as agencies are no longer required to contribute to VSIP as of FY 2004.

Non-Federal Liabilities

Accrued Funded Payroll and Benefits decreased $227,176 thousand or 10 percent. The decrease is primarily due to improvements in the process for recording accrued payroll. Beginning in FY 2004, payroll data from the Defense Joint Military Payroll System was used to calculate accrued payroll. Previously, military pay obligation data from the Army Budget Office were used as a basis for determining the accrued payroll for active Army personnel. This change allows the Army to more accurately record and report this liability for active Army military personnel.

Advances from Others increased $160,498 thousand or 27 percent primarily due to pre-payments for military construction in South Korea and from the Kuwaiti government in support of the Global War on Terrorism (GWOT). The advances were received by the USACE Pacific Ocean Division for various construction projects.

Nonenvironmental Disposal Liabilities, Conventional Munitions Disposal increased $132,951 thousand or 11 percent due to a stockpile expansion of 7,258 tons.

Accounts Payable Cancelled Appropriations were reported as part of Other Liabilities in FY 2003.Treasury Report Mapping changes instituted in June 2004 required all entities to report these balances as Accounts Payable. See Note 12 for additional disclosures.

Temporary Early Retirement Authority (TERA) decreased to zero as Soldiers retiring under the TERA program transitioned to the military retirement program as of FY 2004. No remaining TERA balances are reported as an Other Liability.

Capital Lease Liability decreased $11,742 thousand or 17 percent as a result of annual amortization. See Note 15.B. for additional disclosures.

Other (Non-Federal) Liabilities:

Other Liabilities decreased overall by $712,677 thousand or 28 percent. The decrease is primarily attributable to decreases in the following programs: Iraqi Seized Cash of $164,709 thousand, Contingent Liabilities probable (non-current and current) for U.S. Claims Service (Personnel Claims, Tort Claims, Judgment Fund Liabilities and North Atlantic Treaty Organization – Status of Forces Agreement (NATO SOFA)), the

Chemical Demilitarization (Non-Stockpile) in the net amount of $534,983 thousand, and Contract Holdbacks of $12,985 thousand. The decrease for NATO North Atlantic Treaty Organization Security Investment Program (NSIP) $742,237 was incorrectly reported for Army last year, and this fiscal year moved to Other Defense Organizations.

Note 15.B. Capital Lease Liability

As of September 30 (Amounts in thousands)	2004 Asset Category Land and Buildings	2004 Equipment	2004 Other	2004 Total	2003 Total
1. Future Payments Due:					
A. 2004	$20,785	$0	$0	$20,785	$20,785
B. 2005	20,785	0	0	20,785	20,785
C. 2006	18,009	0	0	18,009	20,785
D. 2007	8,529	0	0	8,529	18,009
E. 2008	5,376	0	0	5,376	8,529
F. After 5 Years	14,058	0	0	14,058	19,243
G. Total Future Lease Payments Due	$87,542	$0	$0	$87,542	$108,136
H. Less: Imputed Interest Executory Costs	28,144	0	0	28,144	36,996
I. Net Capital Lease Liability	$59,398	$0	$0	$59,398	$71,140
2. Capital Lease Liabilities Covered by Budgetary Resources:				$26,334	$26,590
3. Capital Lease Liabilities Not Covered by Budgetary Resources:				$33,063	$44,549

4. Other Information:

The Army is the lessee in eight capital leases for military family housing. The Office of Management and Budget Bulletin 01-09 and Circular A-11 direct that any capital leases entered into during FY 1992 or later are required to be fully funded in the first year of the lease.

Capital Lease Liabilities Covered by Budgetary Resources

The present value of the lease payments, $26,334 thousand, for leases originating after FY 1991 plus the current portion of the Pre-1992 leases is shown as Covered by Budgetary Resources.

Capital Lease Liabilities Not Covered by Budgetary Resources

The remaining six leases, that originated before FY 1992, are funded on a fiscal year basis causing the noncurrent amounts of $33,063 thousand to be shown as Not Covered by Budgetary Resources.

Note 16. Commitments and Contingencies

Disclosures Related to Commitments and Contingencies:

Relevant Information for Comprehension

Nature of Contingency

The Army General Fund has other contingent liabilities in which the possibility of loss is considered reasonable. These liabilities are not accrued in the Army's financial statements.

As of September 30, 2004, the Army General Fund has approximately $10,343,018 thousand in claims considered reasonably possible. These contingent liabilities and estimates are presented in the following table:

Estimate of the Possible Liability
(Amounts in thousands)

Title of Contingent Liabilities	Estimate
Non-Stockpile Chemical Materiel Demilitarization	$9,020,000
Environmental Restoration – Active Installations	846,688
Litigation Division	236,165
Army Environmental Law Division	39,676
Army Contract Appeals Division	33,000
Low-Level Radioactive Waste Disposal	41,421
Administrative Tort Claims (Army Fund)	85,000
European Environmental Claims (Army Fund)	40,000
Network Enterprise Technology Command	908
Personnel Claims	160
Total	$10,343,018

Note Reference

See Note Disclosure 1. S. - Significant Accounting Policies for additional discussion on financial reporting requirements and DoD policies governing Contingencies and Other Liabilities.

Note 17. Military Retirement Benefits and Other Employment Related Actuarial Liabilities

As of September 30 (Amounts in thousands)	2004				2003
	Actuarial Present Value of Projected Plan Benefits	Assumed Interest Rate (%)	(Less: Assets Available to Pay Benefits)	Unfunded Actuarial Liability	Unfunded Actuarial Liability
1. Pension and Health Benefits:					
A. Military Retirement Pensions	$0		$0	$0	$0
B. Military Retirement Health Benefits	0		0	0	0
C. Medicare-Eligible Retiree Benefits	0		0	0	0
D. Total Pension and Health Benefits	$0		$0	$0	$0
2. Other:					
A. FECA	$1,632,843	4.88%	$0	$1,632,843	$1,761,318
B. Voluntary Separation Incentive Programs	0		0	0	0
C. DoD Education Benefits Fund	0		0	0	0
D. ______	0		0	0	0
E. Total Other	$1,632,843		$0	$1,632,843	$1,761,318
3. Total Military Retirement Benefits and Other Employment Related Actuarial Liabilities:	$1,632,843		$0	$1,632,843	$1,761,318

4. Other Information Pertaining to Military Retirement Benefits and Other Employment-Related Actuarial Liabilities:

Market Value of Investments in Market-based and Marketable Securities: Not applicable.
Military Retirement Pensions: The portion of the military retirement benefits actuarial liability applicable to the Army is reported on the financial statements of the Military Retirement Fund.

Military Retirement Health Benefits: Health benefits are funded centrally at the DoD level. As such the portion of the health benefits actuarial liability that is applicable to the Army is reported only on the DoD Agency-wide financial statements.

Medicare-Eligible Retiree Benefits: Not reported by Military Retirement Systems.

Federal Employees Compensation Act (FECA):

Actuarial Cost Method Used: The Army's actuarial liability for Workers' Compensation benefits is developed by the Department of Labor and provided to the Army each fiscal year end. The liability includes the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases. The liability is determined using a method that utilizes historical benefit payment patterns to predict the ultimate payments.

Assumptions: The projected annual benefit payments are then discounted to the present value using the Office of Management and Budget's economic assumptions for 10-year U.S. Treasury notes and bonds. Cost of living adjustments and medical inflation factors are also applied to the calculation of projected future benefits.

Note 18. Unexpended Appropriations

As of September 30 (Amounts in thousands)	2004	2003
1. Unexpended Appropriations:		
A. Unobligated, Available	$21,044,297	$6,386,616
B. Unobligated, Unavailable	1,408,704	1,240,179
C. Unexpended Obligations	50,785,303	40,047,919
D. Total Unexpended Appropriations	$73,238,304	$47,674,714

2. Other Information Pertaining to Unexpended Appropriations:

Definitions:

Unexpended appropriations - Budget authority remaining for disbursement against current or future obligations.

Unobligated balances – Fund balances classified as available or unavailable but not obligated. Unobligated balances associated with appropriations expiring at fiscal year end remain available only for obligation adjustments until the account is closed.

Unexpended obligations - Goods and services that have been ordered but not yet received/performed.

Fluctuations and/or Abnormalities:

The significant increase of $25,563,590 thousand or 54 percent in Unexpended Appropriations reflects the overall increase in the FY 2004 Army budget. Detailed explanations for the increases are disclosed in Note 21, Disclosures Related to the Statement of Budgetary Resources.

Relevant Information for Comprehension:

Unexpended Obligations reported as a component of Unexpended Appropriations include both Undelivered Orders-Unpaid and Undelivered Orders-Paid only by Direct Appropriated funds. This amount is distinct from Change in Amount of Goods, Services, and Benefits Ordered but Not Yet Provided on the Statement of Financing, which includes the change during the fiscal year in Unexpended Obligations against budget authority from the Army.

Note Reference

See Note 21, Disclosures Related to the Statement of Budgetary Resources for additional line item information.

Note 19.A General Disclosures Related to the Statement of Net Cost

Disclosures Related to the Statement of Net Cost

The Consolidated Statement of Net Cost in the federal government is unique because its principles are driven on understanding the net cost of programs and/or organizations that the federal government supports through appropriations or other means. This statement provides gross and net cost information that can be related to the amount of output or outcome for a given program and/or organization administered by a responsible reporting entity. The amounts presented in the Consolidated Statement of Net Cost are based on funding, obligation, accrual and disbursing transactions, which are not always recorded using accrual accounting. Army systems do not always record the transactions on an accrual basis as is required by the generally accepted accounting principles. The information presented also includes data from non-financial feeder systems to capture all cost and financing sources for the Army.

Program Costs:

The Total Net Costs increased by $28,349,865 thousand or 26 percent between FY 2004 and FY 2003. The net increase in Intragovernmental Net Costs of $4,489,821 thousand or 19 percent, and the increase in Net Costs With the Public of $23,860,044 thousand or 28 percent are due to the increased accrued expenditures in support of contingency operations. Further explanation on the increased funding is disclosed in Note 21.

Program Revenues:

Intragovernmental Earned Revenue increased $869,370 thousand or 13 percent. The increase reflects the additional revenues of $412,859 thousand from Intragovernmental programs supporting contingency missions for security services, munitions and communications. Revenues were also received for research and construction projects of $172,677 thousand and other logistics and personnel related support of $218,047 thousand.

Earned Revenue from the Public increased $232,916 thousand or 25 percent. The increase is attributable to Acquisition and Cross Servicing Agreements for logistical support to the militaries of foreign governments in support of the Global War on Terrorism (GWOT).

Note 19.B. Gross Cost and Earned Revenue by Budget Functional Classification

Not Applicable

Note 19.C. Gross Cost to Generate Intra-governmental Revenue and Earned Revenue (Transactions with Other Federal—Non-DoD—Entities) by Budget Functional Classification

Not Applicable

Note 19.D. Imputed Expenses

As of September 30 (Amounts in thousands)	2004	2003
1. Civilian (e.g.,CSRS/FERS) Retirement	$330,114	$339,888
2. Civilian Health	472,428	403,346
3. Civilian Life Insurance	1,557	1,480
4. Military Retirement Pension	0	0
5. Military Retirement Health	0	0
6. Judgment Fund	77,978	73,768
7. Total Imputed Expenses	$882,077	$818,482

8. Other Information

The total imputed expenses consist of: Civilian Retirement, Civilian Health, Civilian Life Insurance, Military Retirement Pension, Military Retirement Health and Judgment Fund. The $69,083 thousand or 17 percent increase in the Civilian Health is attributable to the use of a higher cost factor by the Office of Personnel Management. For FY 2004, the cost factor is $4,419 per enrolled employee. (See the OPM Benefit Administration Letter, Number 04-306 and dated August 16, 2004).

Note 19.E. Benefit Program Expenses

Not Applicable

Note 19. F. Exchange Revenue

Disclosures Related to the Exchange Revenue:

Exchange Revenue arises when a government entity provides goods and services to the public or to another Government entity for a price, "earned revenue." Exchange revenue includes most user charges other than taxes, i.e., regulatory user charges. The Army recognizes earned revenue for full recovery of costs incurred, to provide goods and services to other entities.

Note 19.G. Amounts for Foreign Military Sales (FMS) Program Procurements from Contractors

Not Applicable

Note 19.H. Stewardship Assets

Disclosures Related to Stewardship Assets:

Stewardship assets include Heritage Assets, Stewardship Land, Non-Federal Physical Property, Investments in Research and Development, and Military Equipment Deferred Maintenance. The current year cost of acquiring, constructing, improving, reconstructing, or renovating stewardship assets are included in the Statement of Net Cost. Yearly investment amounts related to stewardship assets are provided in the Required Supplemental Stewardship Information section of this financial statement.

Note 19.I. Intra-governmental Revenue and Expense

Disclosures Related to Intra-governmental Revenue and Expense:

Intragovernmental Revenue. The Army's accounting systems do not capture trading partner data at the transaction level in a manner that facilitates trading partner aggregations. Therefore, the Army was unable to reconcile intragovernmental revenue balances with its trading partners. The Army intends to develop long-term systems improvements that will include sufficient up-front edits and controls to eliminate the need for after-the-fact reconciliations. The volume of intragovernmental transactions is so large that such reconciliations can not be accomplished with the existing systems.

The Army's operating expenses were adjusted based on a comparison between the Army accounts payable and summary level seller accounts receivables. An adjustment was posted to accounts payable and operating expenses to reflect unrecognized accounts payable and operating expenses. The operating expenses of the Army were reclassified from public to governmental in the amount of $23,485,994 thousand to match trading partner revenues in accordance with DoD Financial Management Regulation, Chapter 13 guidance.

Note 19.J. Suborganization Program Costs

Not Applicable

Note 20. Disclosures Related to the Statement of Changes in Net Position

As of September 30 (Amounts in thousands)	Cumulative Results of Operations 2004	Unexpended Appropriations 2004	Cumulative Results of Operations 2003	Unexpended Appropriations 2003
1. Prior Period Adjustments Increases (Decreases) to Net Position Beginning Balance:				
A. Changes in Accounting Standards	$0	$0	$97,897,585	$0
B. Errors and Omissions in Prior Year Accounting Reports	0	0	0	0
C. Other Prior Period Adjustments	0	0	0	0
D. Total Prior Period Adjustments	$0	$0	$97,897,585	$0
2. Imputed Financing:				
A. Civilian CSRS/FERS Retirement	$330,114	$0	$339,888	$0
B. Civilian Health	472,428	0	403,346	0
C. Civilian Life Insurance	1,557	0	1,480	0
D. Military Retirement Pension	0	0	0	0
E. Military Retirement Health	0	0	0	0
F. Judgment Fund	77,978	0	73,768	0
G. Total Imputed Financing	$882,077	$0	$818,482	$0

3. Other Information:

Other Prior Period Adjustments

Changes in Accounting Standards

Effective October 1, 2002, the Statement of Federal Financial Accounting Standards No. 23, *Eliminating the Category National Defense Property, Plant and Equipment (NDPP&E)*, revising the accounting principles for reporting Military Equipment (previously referred to as NDPP&E). The standard renames NDPP&E to Military Equipment, classifies Military Equipment as general property, plant, and equipment (GPP&E), and requires the capitalization and depreciation of the cost of Military Equipment, including the cost of modifications and upgrades.

Changes in Accounting Standards decreased by $97,897,585 thousand or 100 percent. Army recorded a prior period adjustment in FY 2003 for $97,897,585 thousand. The total decrease is attributable to the recording of Military Equipment in FY 2003.

Imputed Financing:

The $69,082 thousand or 17 percent increase in Civilian Health is attributable to the use of a higher cost factor by the Office of Personnel Management (OPM). For FY 2004, the cost factor is $4,419 per enrolled employee. (See the OPM Benefit Administration Letter, Number 04-306 and dated August 16, 2004). The total imputed expenses consist of Civilian Retirement, Civilian Health, Civilian Life Insurance, Military Retirement Pension, Military Retirement Health and Judgment Fund.

Other Disclosures:

Cumulative Results of Operations

Appropriations Used increased $20,430,183 thousand or 19 percent and is directly related to the $31,879,742 thousand or 27 percent increase in Appropriations Received. See Note 21 Disclosures Related to the Statement of Budgetary Resources.

Non-Exchange Revenue presents an increase of $5,012 thousand or 3,826 percent. However, Nonexchange Revenue was incorrectly reported on Other and overstated in FY 2003. The correct amount should have been $12,494 thousand causing a $7,351 thousand or 59 percent decrease. The decrease is primarily due a decrease of $3,906 thousand in collections for the Forest and Wildlife Conservation and ($2,325) thousand in overpayments received for the Army Conventional Ammunition.

Donations and forfeitures of cash and cash equivalents decreased $10,340 thousand or 69 percent due to reduced donations for West Point Military Academy in FY 2004.

Transfers-in/out Without Reimbursement increased $12,710,423 thousand or 2,652 percent due largely to the $10,243,641 thousand transfer for the Iraqi Relief and Reconstruction Fund. In FY 2003, only $466,000 thousand was transferred to Army, which represents the majority of the FY 2003 balance.

The $13,189,641 thousand in Transfers-in/out without reimbursements consists of $10,253,641 thousand in transfers from the Department of the Executive Office of the President for the Iraqi Relief and Reconstruction Fund and $2,936,000 thousand in transfers from Defense Working Capital Funds. The Iraqi Relief and Reconstruction Fund is a material child transfer account that Treasury requires to be reported on the child's financial statements except for the Statement of Budgetary Resources. The transfers from Defense Working Capital Funds are classified as a Cumulative Results of Operation transfer rather than an Unexpended Appropriation transfer because Working Capital Funds transferred budgetary resources from their operations, rather than appropriations.

Other budgetary Financing Sources increased $6,177,075 thousand or 170 percent. The $2,540,445 thousand in Other budgetary financing sources represents adjustments to bring the proprietary accounts into agreement with the budgetary accounts. Due to system deficiencies, there are unreconciled differences between the budgetary and proprietary trial balances. The net effect of these adjustments is reflected on Other Budgetary Financing Sources of the Statement of Net Position. The $6,177,075 thousand increase is due to fluctuations in the differences between budgetary and proprietary balances from FY 2003.

Transfers in/out without reimbursement increased $722,150 thousand or 225 percent due to Construction in Progress of $88,270 thousand and Property, Plant & Equipment for $312,524 thousand. The Construction in Progress was transferred to Air Force for $9,386 thousand, from Defense Logistics Agency for $84,619 thousand, from Missile Defense Agency for $6,237 thousand, and from Defense Health Organization for $6,800 thousand. The Property, Plant, & Equipment was transferred from Defense Logistics Agency for $4,259 thousand, from Office of the Secretary of Defense for $44,228 thousand, from Special Command Operations for $16,055 thousand, from Tricare Management Activity for $8,667 thousand, from Missile Defense Agency for $27,891 thousand, from Other Defense Agencies for $129,381 thousand, from Air Force for $150,936 thousand, and to U. S. Army Corps of Engineers for $68,893 thousand.

Other Financing Sources – Other decreased $115,102 thousand or 100 percent due to incorrect reporting of Nonexchange Revenue related to Receipt Accounts in FY 2003. The correct reporting is in Line 4.E. Nonexchange Revenue.

Unexpended Appropriations

Increases in Appropriations received, Appropriations transferred-in/out, and Appropriations used relate directly to the increase in the overall Army appropriations.

Other adjustments increased $794,564 thousand or 132 percent due to erroneously reporting the withdrawal of canceled funds in Appropriation Used in FY 2003. The FY 2003 Other adjustments should have reported $1,304,581 thousand causing an actual increase of $89,783 or 7 percent.

Note Reference

For Regulatory Disclosure Related to "The Statement of Changes in Net Position" see, *Department of Defense Financial Management Regulation,* Volume 6B, Chapter 10, paragraph 1022.

Note 21. Disclosures Related to the Statement of Budgetary Resources

As of September 30 (Amounts in thousands)	2004	2003
1. Net Amount of Budgetary Resources Obligated for Undelivered Orders at the End of the Period	$60,568,539	$0
2. Available Borrowing and Contract Authority at the End of the Period	0	0.00

3. Other Information:

Fluctuations and/or Abnormalities:

Overall FY 2004 funding increased $31,864,362 thousand or 27 percent; the major fluctuations are influenced by the Presidential approval of the Emergency Wartime Supplemental Appropriations Act (PL 108-11). Congressional funding for the Global War on Terrorism was received through appropriated and supplemental funding in FY 2004.

Military Pay appropriations increased $7,253,171 thousand primarily in support of contingency missions for Operations Enduring Freedom, Iraqi Freedom, and Noble Eagle. The increase supports the incremental costs of Reserve forces on active duty in a war zone versus peacetime training. Additionally, the military pay appropriations received a 3.7 percent pay increase for all soldiers and a pay raise of up to 6.25 percent for selected military pay grades. Increased rates were also provided for incentive pay, family separation allowance, and special pay for duty subject to hostile fire or imminent danger. The total Military Pay funding supports Active Component, Army National Guard, and Army Reserve personnel and provides better pay and incentives.

Operation and Maintenance appropriations increased $21,406,623 thousand. The additional funding was directed for Army Transformation, which ensures warfighting readiness and force protection, and to support contingency missions for Operations Enduring Freedom, Iraqi Freedom, and Noble Eagle. The appropriation increase funded approximately one-third of antiterrorism base operations and force protection needs. Additionally, the budget increased to fund training and recruiting, administrative and service wide activities, and land forces readiness. Security programs increased significantly because of the need for more security equipment.

Procurement appropriations increased $391,616 thousand due to escalated combat operations.

Research, Development, Test, and Evaluation appropriation increased by $2,711,370 thousand. The funding included increases for medical technology, combat vehicle and automotive technology, and aircraft modification and improvement programs.

Budget Authority - Net Transfers of $2,517,085 thousand consists of appropriation transfers of $1,423,816 thousand from the Iraqi Freedom Fund in support of contingency missions, $877,250 thousand from the Office of the President for the Security and Stability of Iraqi, $677,384 thousand in Environmental Restoration and Restoration of Formerly Used Defense Sites, $366,623 thousand in Drug Interdiction for Military Personnel, $(418,210) thousand transferred to the Defense Health Program, $(269,853) thousand transferred to the Foreign Currency Fluctuation Fund, and $(139,925) thousand in miscellaneous transfers.

The decrease of $2,790,356 thousand is largely due to decreases in transfers received from the Office of the President and the Iraqi Freedom Fund in support of Iraqi Security and Stability and contingency missions.

Unobligated Balance – Net Transfers, Actual of $4,698,264 thousand consists of prior year appropriation transfers of $2,936,000 thousand from Defense Working Capital Funds, $880,459 thousand from the Iraqi Freedom Fund in support of contingency missions, $300,000 thousand from Natural Resources Risk Remediation Fund, and $581,805 thousand in miscellaneous transfers. The increase is largely due to additional funds received from Defense Working Capital Funds and the Iraqi Freedom Fund.

Spending Authority from Offsetting Collections increased $3,472,797 thousand due to a $1,025,124 thousand increase in reimbursable authority related to the support of land force readiness including environmental conservation, pollution prevention, environmental compliance, real property services, and base communications; $1,112,499 thousand in reimbursable construction; $597,556 thousand in reimbursable authority from the Army's logistics chain; $385,279 thousand in reimbursable authority from fully training active Combat Corps members; $315,582 thousand in reimbursable ammunition components; and the remaining $36,754 thousand is for other miscellaneous reimbursable authority.

Recoveries of Prior Year Obligations or deobligations increased $5,995,277 thousand or 75 percent from FY 2003 largely due to increases in contractual service and supplies. The actual FY 2004 net deobligations is $3,847,210 thousand.

Unobligated Balance – Apportioned increased $14,511,493 thousand or 209 percent primarily due to a $13,550,000 thousand supplemental received in September 2004 for Operations and Maintenance related to Operation Iraqi Freedom. As of September 2004, only $2,518 thousand had been obligated causing the material increase in unobligated balances for Army General Fund.

Unobligated Balance – Exempt from Apportionment decreased $12,254 thousand or 48 percent primarily due to the Iraqi Relief and Reconstruction Fund erroneously reporting a Statement of Budgetary Resources in FY 2003. Treasury requires that a material child transfer account be reported on the child's financial statements except for the Statement of Budgetary Resources. The Iraqi Relief and Reconstruction Fund is a material child transfer account that reported $11,235 thousand in Unobligated – Exempt from Apportionment funds in FY 2003 that was not reported in FY 2004.

Offsetting Receipts presents a decrease of $32,282 thousand. However, the balance was incorrectly reported in FY 2003 and should have been $113,272 thousand. The actual decrease of $49,983 thousand is attributed to $25,184 thousand in General Fund Proprietary Receipts largely from decreased input from Military Pay Operations, $13,516 thousand in Recoveries under Foreign Military Sales due to an overcharged voucher to Taiwan, $5,569 thousand in Collections of Receivables from Cancelled Accounts, $3,906 thousand in collections for the Forest and Wildlife Conservation, $1,221 thousand in collections for the Sale of Hunting and Fishing Permits, and the remaining $587 thousand decrease is due to other miscellaneous receipts.

The Net Amount of Budgetary Resources Obligated for Undelivered Orders at the End of the Period and specific Statement of Budgetary Resources line variances not explained above, between FY 2003 and FY 2004 are mainly due to the 27 percent increase in funding.

Accounting Standard U.S. Standard General Ledger

The Army has not fully implemented the U.S. Government Standard General Ledger in all operational accounting systems. Guidance from the Treasury Financial Manual, Part 2, Chapter 4000, Federal Agencies' Centralized Trial Balance System II is used to populate the Army Statement of Budgetary Resources.

The Army accounting systems do not provide or capture data needed for obligations incurred and recoveries of prior year obligations in accordance with Office of Management and Budget (OMB) Circular A-11, *Preparation, Submission, and Execution of the Budget* requirements. Although the Army developed an alternative methodology to calculate these items, the amount of distortion cannot be reliably determined, and may or may not be material.

Intra-entity Transactions

The Statement of Budgetary Resources does not include eliminating entries and therefore a Disaggregated Statement of Budgetary Resources is included in the Required Supplementary Information section of the financial statements.

Apportionment Categories

OMB Bulletin No. 01-09 section 9.27 specifically requires disclosure of the amount of direct and reimbursable obligations incurred against amounts apportioned under Category A, Category B and Exempt from Apportionment. Obligations incurred consists of $148,242,209 thousand in Category A, Direct; $4,348,726 thousand in Category B, Direct; and $23,475,016 thousand in Category A, Reimbursable. This disclosure agrees with the aggregate of the related information as reported on the agency's Budgetary Execution Report (SF 133) and Obligations Incurred on the Statement of Budgetary Resources.

Separate Column for Non-budgetary Credit Program Financing Accounts

A Non-budgetary Credit Program Financing Account column allows for a clear distinction between budgetary and non-budgetary credit program financing. Non-budgetary credit financing accounts are reported separately from the budgetary totals in the Budget of the United States Government. Separate reporting on the Statement of Budgetary Resources enhances reconciliation of the two sets of information. Further information on the credit financing accounts is provided in Note 8.

Offsetting Receipts Line

Receipts are collections that are credited to the general, special, or trust fund receipt accounts. In addition, they represent offsetting receipts distributed to the Army. Offsetting receipts offset budget authority and outlays at the agency level in the Budget of the United States Government. Offsetting receipts must be included in the Statement of Budgetary Resources to reconcile it to information in the Budget of the United States Government.

Spending Authority from Offsetting Collections

Adjustments in funds that are temporarily not available pursuant to Public Law, and those that are permanently not available are not included in the Spending Authority From Offsetting Collections on the Statement of Budgetary Resources or the Spending Authority for Offsetting Collections and Recoveries on the Statement of Financing.

Undelivered Orders

Undelivered Orders presented in the Statement of Budgetary Resources includes Undelivered Orders-Unpaid for both direct and reimbursable funds.

Deobligations

Systemic processes record deobligations in expired accounts separately from the obligation. Army funds management policy requires quarterly joint reviews of obligations by program managers and accounting sites. Goals and metrics reported by each Command track efforts to liquidate or deobligate expired obligations by fiscal year. The Recoveries of Prior Year Obligations presentation does not provide visibility of expired deobligation/obligation execution as corresponding obligations in the same expired account are included in the overall Obligations Incurred. In FY 2004, net deobligations for expired accounts amounted to $1,566,429 thousand versus the $11,715,898 thousand reported in the Recoveries of Prior Year Obligations and $10,149,469 thousand reported in Obligations Incurred. The remaining $2,280,781 thousand of the $13,996,679 thousand in deobligations are attributable to multi-year appropriations after the first year of unexpired status.

Note 22. Disclosures Related to the Statement of Financing

Disclosures Related to the Statement of Financing:

The Statement of Financing was expanded to further articulate and detail the relationship between net obligations from budgetary accounting and net cost of operations from proprietary accounting. Some items reported last year as a single line were subdivided to reflect its components. Several new line items were added to separately identify and further explain the use of resources to finance net obligations or net cost of operations. These changes show key differences between net obligations and net cost of operations.

Intra-entity transactions have not been eliminated; therefore, the statements are presented as combined and combining.

Fluctuations and/or Abnormalities:

The changes to Obligations incurred, Spending authority from offsetting collections and recoveries, Undelivered Orders and Unfilled Customer Orders relate directly to the $31,864,362 thousand or 27 percent increase in Army appropriations. An increase in direct appropriations generates an increase in reimbursable activity along with all other stages of budget execution when the new funds are obligated and executed. Refer to Note 21, Disclosures Related to the Statement of Budgetary Resources for a complete description of the additional funding.

Offsetting receipts and Budgetary offsetting collections and receipts that do not affect net cost of operations are primarily comprised of $35,850 thousand in General Fund Miscellaneous Income, $12,138 thousand in Collections of Receivables from Cancelled Accounts, $9,912 thousand in Recoveries of Government Property, $6,944 thousand in Rocky Mountain Arsenal Restoration, and $1,739 thousand in Sales of Hunting and Fishing Permits.

Transfers in/out without reimbursement and Other resources or adjustments to net obligated resources that do not affect net cost of operation are comprised of Construction in Progress of $88,270 thousand and Property, Plant & Equipment of $312,524 thousand. The Construction in Progress was transferred to Air Force for $9,386 thousand, from Defense Logistics Agency for $84,619 thousand, from Missile Defense Agency for $6,237 thousand, and from Defense Health Organization for $6,800 thousand. The Property, Plant, & Equipment was transferred from Defense Logistics Agency for $4,259 thousand, from Office of the Secretary of Defense for $44,228 thousand, from Special Command Operations for $16,055 thousand, from Tricare Management Activity for $8,667 thousand, from Missile Defense Agency for $27,891 thousand, from Other Defense Agencies for $129,381 thousand, from Air Force for $150,936 thousand, and to U. S. Army Corps of Engineers for $68,893 thousand.

Other Resources – Other decreased by $115,102 thousand or 100 percent due to incorrect reporting of Nonexchange Revenue related to Receipt Accounts in FY 2003. The correct reporting does not effect the Statement of Financing.

Resources that fund expenses recognized in prior periods decreased $588,090 thousand primarily due to $406,747 thousand in contingent liabilities with the North Atlantic Treaty Organization Security Investment Program no longer reported on Army's financial statements. The liability is now reported by the Defense Agencies. Further explanation for the fluctuations is provided in Notes 11, 14, and 16.

Resources that finance the acquisition of assets decreased by $15,313,838 thousand and Depreciation and amortization decreased by $11,548,357 thousand. Army bases the value of military equipment for financial statement presentation purposes on projections provided by the Bureau of Economic Analysis (BEA), Department of Commerce. BEA revised the military equipment projections resulting in decreases in the projected purchase and depreciation of military equipment. Further explanation is provided in Note 10.

Increase in annual leave liability decreased $196,204 thousand primarily due to overstatement of the Army National Guard's Civilian Annual Leave Liability in FY 2003.

Increase in environmental and disposal liability increased $786,579 thousand primarily due to increases in environmental liabilities related to closed ranges. Further explanation for the fluctuations is provided in Note 14.

Upward/Downward reestimates of credit subsidy expense increased by $10,869 thousand due to a September 2004 reestimation of an impending loss claim for the Armament Retooling and Manufacturing Support Initiative. Further explanation is provided in Note 8.

Exchange revenue receivable from the public increased $453,389 thousand. Due to business practices, exchange revenue receivable from the public is captured as a budgetary resource, and therefore reported in Spending authority from offsetting collections rather than Increase in exchange revenue receivable from the public.

Components Requiring or Generating Resources in Future Periods – Other decreased $345,669 thousand or 84 percent due to Contingent Liabilities increasing in FY 2003 from FY 2002 causing a $375,090 thousand effect in FY 2003. In FY 2004, Contingent Liabilities decreased causing a zero effect on Components Requiring or Generating Resources in Future Periods – Other.

Revaluation of assets or liabilities is comprised of $515,037 thousand in excess, obsolete, and unserviceable Operating Material and Supplies. The $525,718 thousand increase is due to increases in the amount of excess, obsolete, and unserviceable inventory.

Other Trust Fund Exchange Revenue increased by $12 thousand or 25 percent due to higher revenue bearing investments in FY 2004.

Cost of Goods Sold and Operating Material & Supplies Used can not be properly captured or estimated for FY 2004. The Army is continually reviewing and developing procedures to accurately report these values in the future.

Other is comprised of ($387) thousand in bad debt expense and $1,336,160 thousand in Other Expenses not Requiring Budgetary Resources, which represents expenses for the Iraqi Relief and Reconstruction Fund. The Iraqi Relief and Reconstruction Fund is a material child transfer where Army is the child and the Department of the Executive Office of the President is the parent. Treasury requires that the financial statements of a material child transfer account be presented in the child's financial statements except for the Statement of Budgetary Resources. Because obligations incurred on the Statement of Financing does not include expenses related to the Iraqi Relief and Reconstruction Fund, a reconciling item is included in Other in the Other Components not Requiring or Generating Resources section of the Statement of Financing.

Note Reference

For additional information related to the Statement of Financing, see:

Note 8, Direct Loan and/or Loan Guarantee Programs
Note 10, General Property Plant & Equipment, Net
Note 11, Liabilities Not Covered By Budgetary Resources
Note 14, Environmental Liabilities and Disposal Liabilities
Note 16, Commitments and Contingencies
Note 21, Disclosures Related to the Statement of Budgetary Resources

Note 23. Disclosures Related to the Statement of Custodial Activity

Disclosures Related to the Statement of Custodial Activity:

During Operation Iraqi Freedom, the U.S. Government seized assets in FY 2003 from the Iraqi Government that will be used in support of the Iraqi people. As of September 30, 2004, $113,430 thousand of monetary seized assets remain to be disbursed in support of the Iraqi people. The Statement of Custodial Activity displays only current year activity, therefore, the negative $164,709 thousand shown as Retained for Future Support of the Iraqi People actually displays the change in the liability to the Iraqi people between FY 2003 and FY 2004. The $690,517 thousand decrease in Seized Iraqi Cash, $247,670 thousand decrease in Seized Assets Disbursed on behalf of Iraqi People, and the $442,848 thousand decrease in Seized Assets Retained for Support of the Iraqi People are due to the Army seizing and disbursing less Iraqi assets in FY 2004 than FY 2003.

(Amounts in thousands)	During FY 2004	Cumulative from Inception
Source of Collections		
Seized Iraqi Cash	$118,349	$927,215
Disposition of Collections		
Iraqi Salaries	$648	$30,838
Repair/Reconstruction/Humanitarian Assistance	273,093	443,728
Iraqi Ministry Operations (Ministry of Finance, Defense, etc.)	9,317	263,907
Fuel/Supplies	0	75,312
Total Disbursed on behalf of the Iraqi People	$283,058	$813,785
Retained for Future Support of the Iraqi People	(164,709)	113,430
Total Disposition of Collections	$118,349	$927,215
Net Custodial Collection Activity	$0	$0

Note 24.A. Other Disclosures

1. ENTITY AS LESSEE–Operating Leases
As of September 30
(Amounts in thousands)

B. Future Payments Due:

Fiscal Year	2004 Land and Buildings	2004 Equipment	2004 Other	2004 Total	2003 Total
2005	$6,790	$0	$0	$6,790	$7,917
2006	6,303	0	0	6,303	6,790
2007	6,298	0	0	6,298	6,303
2008	4,950	0	0	4,950	6,298
2009	3,794	0	0	3,794	4,950
After 5 Years	17,669	0	0	17,669	21,462
Total Future Lease Payments Due	$45,804	$0	$0	$45,804	$53,720

Fluctuations and Abnormalities:

Total operating lease commitments decreased by $7,916 thousand or 15 percent, due to payments made on these leases. As operating leases expire, the Army moves to owned properties or enters into lease contracts that are cancelable.

Definitions:

- Lessee – A person or entity who receives the use and possession of leased property (e.g. real estate or equipment) from a lessor in exchange for payment of funds.
- Operating Lease - A lease which does not substantially transfer all the benefits and risks of ownership. Payments are charged to an expense account over the lease term as it becomes payable.

Land and Buildings Leases consist of:

Description of Leases:

Land and Building lease periods vary and are not expected to be renewed at the end of the lease term. There are no material escalation clauses or contingent rental restrictions. Costs are gathered from existing leases, General Service Administration (GSA) bills, and Inter-service Support Agreements of which the largest component is office space. 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.

Note 24.B. Other Disclosures

Not applicable

Department of Defense- Department of the Army

CONSOLIDATING BALANCE SHEET

As of September 30, 2004 and 2003 ($ in Thousands)

ASSETS (Note 2)	**Active Army**	**Army Reserve**	**Army National Guard**
Intragovernmental:			
Fund Balance with Treasury (Note 3)			
Entity	$84,262,101	$1,604,208	$3,431,064
Non-Entity Seized Iraqi Cash	113,430	0	0
Non-Entity-Other	137,806	0	0
Investments (Note 4)	1,496	0	0
Accounts Receivable (Note 5)	1,689,003	14,877	61,531
Other Assets (Note 6)	5,034	0	(8)
Total Intragovernmental Assets	$86,208,870	$1,619,085	$3,492,587
Cash and Other Monetary Assets (Note 7)	$1,525,090	$0	$0
Accounts Receivable (Note 5)	437,714	23,036	31,644
Loans Receivable (Note 8)	0	0	0
Inventory and Related Property (Note 9)	37,647,721	0	0
General Property, Plant and Equipment (Note 10)	110,775,501	1,523,174	812,897
Investments (Note 4)	0	0	0
Other Assets (Note 6)	3,230,402	34,762	86,340
TOTAL ASSETS	$239,825,298	$3,200,057	$4,423,468
LIABILITIES (Note 11)			
Intragovernmental:			
Accounts Payable (Note 12)	$3,577,333	$305,920	$104,501
Debt (Note 13)	0	0	0
Environmental Liabilities (Note 14)	0	0	0
Other Liabilities (Note 15 & Note 16)	2,512,173	9,535	47,371
Total Intragovernmental Liabilities	$6,089,506	$315,455	$151,872
Accounts Payable (Note 12)	$6,775,957	$525,468	$1,181,290
Military Retirement Benefits and Other Employment-Related Actuarial Liabilities (Note 17)	1,304,029	55,046	273,768
Environmental Liabilities (Note 14)	40,366,172	0	0
Loan Guarantee Liability (Note 8)	12,293	0	0
Other Liabilities (Note 15 and Note 16)	7,892,408	203,957	572,827
Debt Held by Public	0	0	0
TOTAL LIABILITIES	$62,440,365	$1,099,926	$2,179,757
NET POSITION			
Unexpended Appropriations (Note 18)	$69,762,599	$761,566	$1,996,609
Cumulative Results of Operations	107,622,334	1,338,565	247,102
TOTAL NET POSITION	$177,384,933	$2,100,131	$2,243,711
TOTAL LIABILITIES AND NET POSITION	$239,825,298	$3,200,057	$4,423,468

Component Level	Combined Total	Eliminations	2004 Consolidated	2003 Consolidated
$0	$89,297,373	$0	$89,297,373	$54,695,897
0	113,430	0	113,430	278,139
0	137,806	0	137,806	61,443
0	1,496	0	1,496	1,231
(1,303,544)	461,867	0	461,867	523,347
551,354	556,380	0	556,380	83,474
($752,190)	$90,568,352	$0	$90,568,352	$55,643,531
$0	$1,525,090	$0	$1,525,090	$954,368
0	492,394	0	492,394	514,579
0	0	0	0	0
0	37,647,721	0	37,647,721	32,676,658
0	113,111,572	0	113,111,572	115,337,906
0	0	0	0	0
0	3,351,504	0	3,351,504	3,569,021
($752,190)	$246,696,633	$0	$246,696,633	$208,696,063
($2,281,023)	$1,706,731	$0	$1,706,731	$1,084,965
0	0	0	0	0
0	0	0	0	0
(166,176)	2,402,903	0	2,402,903	1,670,318
($2,447,199)	$4,109,634	$0	$4,109,634	$2,755,283
$977,479	$9,460,194	$0	$9,460,194	$9,089,097
0	1,632,843	0	1,632,843	1,761,318
0	40,366,172	0	40,366,172	37,395,412
0	12,293	0	12,293	1,273
0	8,669,192	0	8,669,192	9,387,320
0	0	0	0	0
($1,469,720)	$64,250,328	$0	$64,250,328	$60,389,703
$717,530	$73,238,304	$0	$73,238,304	$47,674,714
0	109,208,001	0	109,208,001	100,631,646
$717,530	$182,446,305	$0	$182,446,305	$148,306,360
($752,190)	$246,696,633	$0	$246,696,633	$208,696,063

Department of Defense- Department of the Army

CONSOLIDATING STATEMENT OF NET COST

As of September 30, 2004 and 2003 ($ in Thousands)

Program Costs	Active Army	Army Reserve	Army National Guard
A. Military Personnel			
Intragovernmental Gross Costs	$8,877,009	$0	($60,951)
(Less: Intragovernmental Earned Revenue)	(391,588)	(20,690)	40,282
Intragovernmental Net Costs	$8,485,421	($20,690)	($20,669)
Gross Costs With the Public	$29,727,054	$3,278,137	$5,201,310
(Less: Earned Revenue From the Public)	16,173	(200)	2,831
Net Costs With the Public	$29,743,227	$3,277,937	$5,204,141
Total Net Cost	$38,228,648	$3,257,247	$5,183,472
B. Operation and Maintenance			
Intragovernmental Gross Costs	$8,681,801	$18,954	$20,884
(Less: Intragovernmental Earned Revenue)	(10,641,212)	(48,784)	(181,268)
Intragovernmental Net Costs	($1,959,411)	($29,830)	($160,384)
Gross Costs With the Public	$55,944,989	$1,895,305	$4,899,545
(Less: Earned Revenue From the Public)	(822,065)	(2,842)	(7,309)
Net Costs With the Public	$55,122,924	$1,892,463	$4,892,236
Total Net Cost	$53,163,513	$1,862,633	$4,731,852
C. Procurement			
Intragovernmental Gross Costs	$826,430	$0	$0
(Less: Intragovernmental Earned Revenue)	(778,486)	0	0
Intragovernmental Net Costs	$47,944	$0	$0
Gross Costs With the Public	$17,237,458	$0	$0
(Less: Earned Revenue From the Public)	(64,604)	0	0
Net Costs With the Public	$17,172,854	$0	$0
Total Net Cost	$17,220,798	$0	$0
D. Research, Development, Test & Evaluation			
Intragovernmental Gross Costs	$2,588,330	$0	$0
(Less: Intragovernmental Earned Revenue)	(2,703,026)	0	0
Intragovernmental Net Costs	($114,696)	$0	$0
Gross Costs With the Public	$8,684,468	$0	$0
(Less: Earned Revenue From the Public)	(123,475)	0	0
Net Costs With the Public	$8,560,993	$0	$0
Total Net Cost	$8,446,297	$0	$0
E. Military Construction/Family Housing			
Intragovernmental Gross Costs	$2,328,172	$12,757	$0
(Less: Intragovernmental Earned Revenue)	(3,267,676)	0	0
Intragovernmental Net Costs	($939,504)	$12,757	$0
Gross Costs With the Public	$1,395,328	$19,956	$540,742
(Less: Earned Revenue From the Public)	(144,173)	0	0
Net Costs With the Public	$1,251,155	$19,956	$540,742
Total Net Cost	$311,651	$32,713	$540,742
F. Other			
Intragovernmental Gross Costs	$10,628	$0	$0
(Less: Intragovernmental Earned Revenue)	(8,268)	0	0
Intragovernmental Net Costs	$2,360	$0	$0
Gross Costs With the Public	$3,373,193	$0	$0
(Less: Earned Revenue From the Public)	(6,391)	0	0
Net Costs With the Public	$3,366,802	$0	$0
Total Net Cost	$3,369,162	$0	$0

Component Level	Combined Total	Eliminations	2004 Consolidated	2003 Consolidated
	$8,816,058	$0	$8,816,058	$9,294,722
	(371,996)	0	(371,996)	(641,567)
	$8,444,062	$0	$8,444,062	$8,653,155
	$38,206,501	$0	$38,206,501	$35,425,693
	18,804	0	18,804	(25,470)
	$38,225,305	$0	$38,225,305	$35,400,223
	$46,669,367	$0	$46,669,367	$44,053,378
	$8,721,639	$0	$8,721,639	$6,231,078
	(10,871,264)	0	(10,871,264)	(7,247,979)
	($2,149,625)	$0	($2,149,625)	($1,016,901)
	$62,739,839	$0	$62,739,839	$48,460,407
	(832,216)	0	(832,216)	(600,068)
	$61,907,623	$0	$61,907,623	$47,860,339
	$59,757,998	$0	$59,757,998	$46,843,438
	$826,430	$0	$826,430	($1,424,376)
	(778,486)	0	(778,486)	(661,925)
	$47,944	$0	$47,944	($2,086,301)
	$17,237,458	$0	$17,237,458	$7,133,239
	(64,604)	0	(64,604)	(57,532)
	$17,172,854	$0	$17,172,854	$7,075,707
	$17,220,798	$0	$17,220,798	$4,989,406
	$2,588,330	$0	$2,588,330	$2,076,608
	(2,703,026)	0	(2,703,026)	(2,524,616)
	($114,696)	$0	($114,696)	($448,008)
	$8,684,468	$0	$8,684,468	$7,737,924
	(123,475)	0	(123,475)	(76,858)
	$8,560,993	$0	$8,560,993	$7,661,066
	$8,446,297	$0	$8,446,297	$7,213,058
	$2,340,929	$0	$2,340,929	$3,527,786
	(3,267,676)	0	(3,267,676)	(2,117,682)
	($926,747)	$0	($926,747)	$1,410,104
	$1,956,026	$0	$1,956,026	$301,508
	(144,173)	0	(144,173)	(181,682)
	$1,811,853	$0	$1,811,853	$119,826
	$885,106	$0	$885,106	$1,529,930
$12,156,126	$12,166,754	$0	$12,166,754	$10,395,131
10,612,338	10,604,070	0	10,604,070	6,674,761
$22,768,464	$22,770,824	$0	$22,770,824	$17,069,892
($23,335,670)	($19,962,477)	$0	($19,962,477)	($14,289,916)
0	(6,391)	0	(6,391)	22,471
($23,335,670)	($19,968,868)	$0	($19,968,868)	($14,267,445)
($567,206)	$2,801,956	$0	$2,801,956	$2,802,447

Department of Defense- Department of the Army

CONSOLIDATING STATEMENT OF NET COST

As of September 30, 2004 and 2003 ($ in Thousands)

	Active Army	Army Reserve	Army National Guard
G. Total Program Costs			
Intragovernmental Gross Costs	$23,312,370	$31,711	($40,067)
(Less: Intragovernmental Earned Revenue)	(17,790,256)	(69,474)	(140,986)
Intragovernmental Net Costs	$5,522,114	($37,763)	($181,053)
Gross Costs With the Public	$116,362,490	$5,193,398	$10,641,597
(Less: Earned Revenue From the Public)	(1,144,535)	(3,042)	(4,478)
Net Costs With the Public	$115,217,955	$5,190,356	$10,637,119
Total Net Cost	$120,740,069	$5,152,593	$10,456,066
Cost Not Assigned to Programs	$0	$0	$0
(Less: Earned Revenue Not Attributable to Programs)	0	0	0
Net Cost of Operations	$120,740,069	$5,152,593	$10,456,066

Component Level	Combined Total	Eliminations	2004 Consolidated	2003 Consolidated
$12,156,126	$35,460,140	$0	$35,460,140	$30,100,949
10,612,338	(7,388,378)	0	(7,388,378)	(6,519,008)
$22,768,464	$28,071,762	$0	$28,071,762	$23,581,941
($23,335,670)	$108,861,815	$0	$108,861,815	$84,768,855
0	(1,152,055)	0	(1,152,055)	(919,139)
($23,335,670)	$107,709,760	$0	$107,709,760	$83,849,716
($567,206)	$135,781,522	$0	$135,781,522	$107,431,657
$0	$0	$0	$0	$0
0	0	0	0	0
($567,206)	$135,781,522	$0	$135,781,522	$107,431,657

Department of Defense- Department of the Army

CONSOLIDATING STATEMENT OF CHANGES IN NET POSITION

As of September 30, 2004 and 2003 ($ in Thousands)

CUMULATIVE RESULTS OF OPERATIONS	Active Army	Army Reserve	Army National Guard
Beginning Balances	$99,380,846	$1,136,623	$114,177
Prior period adjustments (+/-)			
Prior Period Adjustments - Restated (+/-)	0	0	0
Beginning Balance, Restated	99,380,846	1,136,623	114,177
Prior Period Adjustments - Not Restated (+/-)	0	0	0
Beginning Balances, as adjusted	$99,380,846	$1,136,623	$114,177
Budgetary Financing Sources:			
Appropriations received	0	0	0
Appropriations transferred-in/out (+/-)	0	0	0
Other adjustments (rescissions, etc) (+/-)	0	0	0
Appropriations used	111,896,996	5,390,230	10,615,094
Nonexchange revenue	5,143	0	0
Donations and forfeitures of cash and cash equivalents	4,663	0	0
Transfers-in/out without reimbursement (+/-)	13,189,641	0	0
Other budgetary financing sources (+/-)	2,602,295	(35,695)	(26,103)
Other Financing Sources:			
Donations and forfeitures of property	0	0	0
Transfers-in/out without reimbursement (+/-)	400,742	0	0
Imputed financing from costs absorbed by others	882,077	0	0
Other (+/-)	0	0	0
Total Financing Sources	$128,981,557	$5,354,535	$10,588,991
Net Cost of Operations (+/-)	120,740,069	5,152,593	10,456,066
Ending Balances	$107,622,334	$1,338,565	$247,102
UNEXPENDED APPROPRIATIONS			
Beginning Balances	$44,005,556	$840,033	$2,678,801
Prior period adjustments (+/-)			
Prior Period Adjustments - Restated (+/-)	0	0	0
Beginning Balance, Restated	44,005,556	840,033	2,678,801
Prior Period Adjustments - Not Restated (+/-)	0	0	0
Beginning Balances, as adjusted	$44,005,556	$840,033	$2,678,801
Budgetary Financing Sources:			
Appropriations received	133,733,892	5,655,785	10,158,042
Appropriations transferred-in/out (+/-)	5,158,694	(291,362)	(121,983)
Other adjustments (rescissions, etc) (+/-)	(1,238,547)	(52,661)	(103,156)
Appropriations used	(111,896,996)	(5,390,229)	(10,615,095)
Nonexchange revenue	0	0	0
Donations and forfeitures of cash and cash equivalents	0	0	0
Transfers-in/out without reimbursement (+/-)	0	0	0
Other budgetary financing sources (+/-)	0	0	0
Other Financing Sources:			
Donations and forfeitures of property	0	0	0
Transfers-in/out without reimbursement (+/-)	0	0	0
Imputed financing from costs absorbed by others	0	0	0
Other (+/-)	0	0	0
Total Financing Sources	$25,757,043	($78,467)	($682,192)
Net Cost of Operations (+/-)	0	0	0
Ending Balances	$69,762,599	$761,566	$1,996,609

Component Level	Combined Total	Eliminations	2004 Consolidated	2003 Consolidated
$0	$100,631,646	$0	$100,631,646	$5,790,837
0	0	0	0	0
0	100,631,646	0	100,631,646	5,790,837
0	0	0	0	97,897,585
$0	$100,631,646	$0	$100,631,646	$103,688,422
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
(567,206)	127,335,114	0	127,335,114	106,904,931
0	5,143	0	5,143	131
0	4,663	0	4,663	15,003
0	13,189,641	0	13,189,641	479,218
(52)	2,540,445	0	2,540,445	(3,636,630)
0	0	0	0	0
52	400,794	0	400,794	(321,356)
0	882,077	0	882,077	818,482
0	0	0	0	115,102
($567,206)	$144,357,877	$0	$144,357,877	$104,374,881
(567,206)	135,781,522	0	135,781,522	107,431,657
$0	$109,208,001	$0	$109,208,001	$100,631,646
$150,324	$47,674,714	$0	$47,674,714	$31,468,721
0	0	0	0	0
150,324	47,674,714	0	47,674,714	31,468,721
0	0	0	0	0
$150,324	$47,674,714	$0	$47,674,714	$31,468,721
0	149,547,719	0	149,547,719	117,667,977
0	4,745,349	0	4,745,349	6,042,747
0	(1,394,364)	0	(1,394,364)	(599,800)
567,206	(127,335,114)	0	(127,335,114)	(106,904,931)
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
$567,206	$25,563,590	$0	$25,563,590	$16,205,993
0	0	0	0	0
$717,530	$73,238,304	$0	$73,238,304	$47,674,714

Department of Defense- Department of the Army

COMBINING STATEMENT OF BUDGETARY RESOURCES

As of September 30, 2004 and 2003 ($ in Thousands)

	Active Army	Army Reserve	Army National Guard
BUDGETARY FINANCING ACCOUNTS			
BUDGETARY RESOURCES			
Budget Authority:			
Appropriations received	$133,746,065	$5,655,785	$10,158,042
Borrowing authority	0	0	0
Contract authority	0	0	0
Net transfers (+/-)	2,789,121	(163,358)	(108,678)
Other	0	0	0
Unobligated balance:			
Beginning of period	7,482,962	243,423	486,604
Net transfers, actual (+/-)	4,839,573	(128,004)	(13,305)
Anticipated Transfers Balances	0	0	0
Spending authority from offsetting collections:			
Earned	0	0	0
Collected	18,504,799	72,650	162,545
Receivable from Federal sources	429,957	(133)	(17,082)
Change in unfilled customer orders	0	0	0
Advance received	306,329	277	(30)
Without advance from Federal sources	1,876,903	16,390	3,558
Anticipated for the rest of year, without advances	0	0	0
Transfers from trust funds	0	0	0
Subtotal	$21,117,988	$89,184	$148,991
Recoveries of prior year obligations	11,411,800	722,278	1,862,601
Temporarily not available pursuant to Public Law	0	0	0
Permanently not available	(1,238,547)	(52,661)	(103,156)
Total Budgetary Resources	$180,148,962	$6,366,647	$12,431,099
STATUS OF BUDGETARY RESOURCES			
Obligations incurred:			
Direct	$135,058,437	$6,087,352	$11,445,147
Reimbursable	23,075,048	94,168	305,800
Subtotal	158,133,485	6,181,520	11,750,947
Unobligated balance:			
Apportioned	21,185,220	44,443	228,978
Exempt from apportionment	13,411	0	0
Other available	1	0	(1)
Unobligated Balances Not Available	816,845	140,684	451,175
Total, Status of Budgetary Resources	$180,148,962	$6,366,647	$12,431,099
Relationship of Obligations to Outlays:			
Obligated Balance, Net - beginning of period	$42,236,948	$1,497,554	$2,748,353
Obligated Balance transferred, net (+/-)	0	0	0
Obligated Balance, Net - end of period:			
Accounts receivable	(1,810,267)	(15,745)	(67,434)
Unfilled customer order from Federal sources	(12,679,854)	(26,080)	(7,237)
Undelivered orders	54,754,445	552,918	1,202,211
Accounts payable	12,588,082	907,988	1,623,372
Outlays:			
Disbursements	133,799,368	5,521,458	9,899,311
Collections	(18,811,127)	(72,926)	(162,515)
Subtotal	$114,988,241	$5,448,532	$9,736,796
Less: Offsetting receipts	(63,289)	0	0
Net Outlays	$114,924,952	$5,448,532	$9,736,796

Component Level	2004 Combined	2003 Combined
$0	$149,559,892	$117,695,530
0	0	0
0	0	0
0	2,517,085	5,307,441
0	0	0
0	8,212,989	5,858,110
0	4,698,264	1,214,524
0	0	0
0	0	0
0	18,739,994	14,095,736
0	412,742	12,974
0	0	0
0	306,576	119,338
0	1,896,851	3,655,318
0	0	0
0	0	0
$0	$21,356,163	$17,883,366
0	13,996,679	8,001,403
0	0	0
0	(1,394,364)	(1,304,580)
$0	$198,946,708	$154,655,794
$0	$152,590,936	$128,012,383
0	23,475,016	18,430,419
0	176,065,952	146,442,802
0	21,458,641	6,947,148
0	13,411	25,665
0	0	0
0	1,408,704	1,240,179
$0	$198,946,708	$154,655,794
$0	$46,482,855	$33,662,267
0	0	0
0	(1,893,446)	(1,480,706)
0	(12,713,171)	(10,816,319)
0	56,509,574	44,735,892
0	15,119,442	14,043,988
0	149,220,137	121,952,521
0	(19,046,568)	(14,215,073)
$0	$130,173,569	$107,737,448
0	(63,289)	(95,571)
$0	$130,110,280	$107,641,877

Department of Defense- Department of the Army

COMBINING STATEMENT OF BUDGETARY RESOURCES

As of September 30, 2004 and 2003 ($ in Thousands)

	Active Army	Army Reserve	Army National Guard
NONBUDGETARY FINANCING ACCOUNTS			
BUDGETARY RESOURCES			
Budget Authority:			
Appropriations received	$0	$0	$0
Borrowing authority	0	0	0
Contract authority	0	0	0
Net transfers (+/-)	0	0	0
Other	0	0	0
Unobligated balance:			
Beginning of period	1,272	0	0
Net transfers, actual (+/-)	0	0	0
Anticipated Transfers Balances	0	0	0
Spending authority from offsetting collections:			
Earned	0	0	0
Collected	152	0	0
Receivable from Federal sources	0	0	0
Change in unfilled customer orders	0	0	0
Advance received	0	0	0
Without advance from Federal sources	0	0	0
Anticipated for the rest of year, without advances	0	0	0
Transfers from trust funds	0	0	0
Subtotal	$152	$0	$0
Recoveries of prior year obligations	0	0	0
Temporarily not available pursuant to Public Law	0	0	0
Permanently not available	0	0	0
Total Budgetary Resources	$1,424	$0	$0
STATUS OF BUDGETARY RESOURCES			
Obligations incurred:			
Direct	$0	$0	$0
Reimbursable	0	0	0
Subtotal	$0	$0	$0
Unobligated balance:			
Apportioned	1,424	0	0
Exempt from apportionment	0	0	0
Other available	0	0	0
Unobligated Balances Not Available	0	0	0
Total, Status of Budgetary Resources	$1,424	$0	$0
Relationship of Obligations to Outlays:			
Obligated Balance, Net - beginning of period	$0	$0	$0
Obligated Balance transferred, net (+/-)	0	0	0
Obligated Balance, Net - end of period:			
Accounts receivable	0	0	0
Unfilled customer order from Federal sources	0	0	0
Undelivered orders	0	0	0
Accounts payable	0	0	0
Outlays:			
Disbursements	0	0	0
Collections	(152)	0	0
Subtotal	($152)	$0	$0
Less: Offsetting receipts	0	0	0
Net Outlays	($152)	$0	$0

Component Level	2004 Combined	2003 Combined
$0	$0	$0
0	0	0
0	0	0
0	0	0
0	0	0
0	1,272	730
0	0	0
0	0	0
0	0	0
0	152	543
0	0	0
0	0	0
0	0	0
0	0	0
0	0	0
0	0	0
$0	$152	$543
0	0	0
0	0	0
0	0	0
$0	$1,424	$1,273
$0	$0	$0
0	0	0
$0	$0	$0
0	1,424	1,273
0	0	0
0	0	0
0	0	0
$0	$1,424	$1,273
$0	$0	$0
0	0	0
0	0	0
0	0	0
0	0	0
0	0	0
0	0	0
0	(152)	(543)
$0	($152)	($543)
0	0	0
$0	($152)	($543)

Department of Defense- Department of the Army

COMBINING STATEMENT OF FINANCING

As of September 30, 2004 and 2003 ($ in Thousands)

Resources Used to Finance Activities:	**Active Army**	**Army Reserve**
Budgetary Resources Obligated		
Obligations incurred	$158,133,485	$6,181,520
Less: Spending authority from offsetting collections and recoveries (-)	(32,529,939)	(811,461)
Obligations net of offsetting collections and recoveries	$125,603,546	$5,370,059
Less: Offsetting receipts (-)	(63,289)	0
Net obligations	$125,540,257	$5,370,059
Other Resources		
Donations and forfeitures of property	0	0
Transfers in/out without reimbursement (+/-)	400,742	0
Imputed financing from costs absorbed by others	882,077	0
Other (+/-)	0	0
Net other resources used to finance activities	$1,282,819	$0
Total resources used to finance activities	$126,823,076	$5,370,059
Resources Used to Finance Items not Part of the Net Cost of Operations		
Change in budgetary resources obligated for goods, services and benefits ordered but not yet provided		
Undelivered Orders (-)	($12,499,620)	$4,280
Unfilled Customer Orders	2,183,232	16,666
Resources that fund expenses recognized in prior periods	(778,523)	(2,220)
Budgetary offsetting collections and receipts that do not affect net cost of operations	63,441	0
Resources that finance the acquisition of assets	(9,338,486)	(406,389)
Other resources or adjustments to net obligated resources that do not affect net cost of operations		
Less: Trust or Special Fund Receipts Related to Exchange in the Entity's Budget (-)	0	0
Other (+/-)	(400,742)	0
Total resources used to finance items not part of the net cost of operations	($20,770,698)	($387,663)
Total resources used to finance the net cost of operations	$106,052,378	$4,982,396
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:		
Increase in annual leave liability	$79,075	$10,589
Increase in environmental and disposal liability	3,103,711	0
Upward/Downward reestimates of credit subsidy expense (+/-)	10,869	0
Increase in exchange revenue receivable from the the public (-)	0	0
Other (+/-)	59,383	585
Total components of Net Cost of Operations that will require or generate resources in future periods		
Components not Requiring or Generating Resources:	$3,253,038	$11,174
Depreciation and amortization	9,582,597	160,101
Revaluation of assets or liabilities (+/-)	514,672	0
Other (+/-)		
Trust Fund Exchange Revenue	(36)	0
Cost of Goods Sold	0	0
Operating Material & Supplies Used	0	0
Other	1,337,420	(1,078)
Total components of Net Cost of Operations that will not require or generate resources	$11,434,653	$159,023
Total components of net cost of operations that will not require or generate resources in the current period	$14,687,691	$170,197
Net Cost of Operations	$120,740,069	$5,152,593

Army National Guard	Component Level	2004 Combined	2003 Combined
$11,750,946	$0	$176,065,951	$146,442,802
(2,011,591)	0	(35,352,991)	(25,885,311)
$9,739,355	$0	$140,712,960	$120,557,491
0	0	(63,289)	(95,571)
$9,739,355	$0	$140,649,671	$120,461,920
0	0	0	0
0	52	400,794	(321,356)
0	0	882,077	818,482
0	0	0	115,102
$0	$52	$1,282,871	$612,228
$9,739,355	$52	$141,932,542	$121,074,148
$877,409	($567,206)	($12,185,137)	($16,480,237)
3,527	0	2,203,425	3,774,656
(90,042)	0	(870,785)	(282,695)
0	0	63,441	15,085
(156,130)	0	(9,901,005)	(25,214,843)
0	0	0	0
0	(52)	(400,794)	0
$634,764	($567,258)	($21,090,855)	($38,188,034)
$10,374,119	($567,206)	$120,841,687	$82,886,114
$5,620	$0	$95,284	$291,488
0	0	3,103,711	2,317,132
0	0	10,869	0
0	0	0	0
3,666	0	63,634	409,303
$9,286	$0	$3,273,498	$3,017,923
72,865	0	9,815,563	21,363,920
365	0	515,037	(10,681)
0	0	(36)	(48)
0	0	0	0
0	0	0	0
(569)	0	1,335,773	174,429
$72,661	$0	$11,666,337	$21,527,620
$81,947	$0	$14,939,835	$24,545,543
$10,456,066	($567,206)	$135,781,522	$107,431,657

Department of Defense- Department of the Army

COMBINING STATEMENT OF CUSTODIAL ACTIVITY

As of September 30, 2004 and 2003 ($ in Thousands)

SOURCE OF COLLECTIONS	Active Army	Army Reserve	Army National Guard
Deposits by Foreign Governments	$0	$0	$0
Seized Iraqi Cash	118,349	0	0
Other Collections	0	0	0
Total Cash Collections	118,349	0	0
Accrual Adjustments (+/-)	0	0	0
Total Custodial Collections	$118,349	$0	$0
DISPOSITION OF COLLECTIONS			
Disbursed on Behalf of Foreign Governments and International Organizations	$0	$0	$0
Seized Assets Disbursed on behalf of Iraqi People	283,058	0	0
Increase (Decrease) in Amounts to be Transferred	0	0	0
Collections Used for Refunds and Other Payments	0	0	0
Retained by The Reporting Entity	0	0	0
Seized Assets Retained for Support of the Iraqi People	(164,709)	0	0
Total Disposition of Collections	$118,349	$0	$0
NET CUSTODIAL COLLECTION ACTIVITY	$0	$0	$0

SOURCE OF COLLECTIONS	Component Level	2004 Combined	2003 Combined
Deposits by Foreign Governments	$0	$0	$0
Seized Iraqi Cash	0	118,349	808,866
Other Collections	0	0	0
Total Cash Collections	0	118,349	808,866
Accrual Adjustments (+/-)	0	0	0
Total Custodial Collections	$0	$118,349	$808,866
DISPOSITION OF COLLECTIONS			
Disbursed on Behalf of Foreign Governments and International Organizations	$0	$0	$0
Seized Assets Disbursed on behalf of Iraqi People	0	283,058	530,727
Increase (Decrease) in Amounts to be Transferred	0	0	0
Collections Used for Refunds and Other Payments	0	0	0
Retained by The Reporting Entity	0	0	0
Seized Assets Retained for Support of the Iraqi People	0	(164,709)	278,139
Total Disposition of Collections	$0	$118,349	$808,866
NET CUSTODIAL COLLECTION ACTIVITY	$0	$0	$0

Required Supplementary Stewardship Information

Heritage Assets

For Fiscal Year Ended September 30, 2004

(a)	(b) Measurement/ Quantity	(c) As Of 10/1/03	(d) Additions	(e) Deletions	(f) As Of 9/30/04
Museums (Note 2)	Each	117	0	0	117
Monuments & Memorials (Note 3)	Each	889	527	5	1,411
Cemeteries (Note 4)	Sites	524	4	5	523
Archeological Sites	Sites	0	0	0	0
Buildings & Structures (Note 1)	Each	9,846	694	521	10,019
Major Collections (Note 5)	Each	6	0	0	6

Narrative Statement:

In most cases, the additions/deletions are the result of sites/installations: (a) identifying cemeteries and historical facilities; (b) disposing of BRAC Closure property or excess installations; and, (c) privatization/ RCI program.

Notes:

1. Historical Buildings and Structures: buildings and structures designated as historical exclude museums, monuments, and memorials. The number of Buildings and Structures increased as a result of the following initiatives:

- Installations conducting real property surveys and making adjustments according to their findings
- Active installations now reporting previously omitted National Guard Bureau buildings and structures designated as heritage assets
- Both National Guard and Reserve are now reporting new buildings and structures designated as heritage assets

2. Museums: The Army Museum System consists of 117 museums and museum activities worldwide that comprise the active Army, Army Reserve, and the National Guard (Federal property only). In addition, there is historical property displayed in numerous regimental rooms, trophy rooms, officer's clubs, visitor's centers, chapels, and headquarters building elements that are not recognized by the Department of the Army as a museum or museum activity. Solely for reporting purposes, we have consolidated all of these separate and smaller collections during this reporting period.
3. Memorial/Monuments: includes category code 76020 (monuments).
4. Cemeteries: includes category code 76030 (cemetery), 76031 (National Cemetery), 76032 (Veterans Cemetery), and excludes 76033 (Pet Cemeteries).
5. The US Army Tank-automotive & Armaments Command is reporting two (2) major collections under the Donation Program; Ceremonial Rifles and Monuments/Static. The U.S. Army Center of Military History is the proponent for all Army Historical property. Currently, there are four (4) major or significant collections that are maintained outside the definition of an Army museum and museum activity. The collections consist of the U.S. Army Center of Military History, Museum Division, Collections Branch, the Anniston Historical Clearinghouse, the Maple Leaf and Benton Small Arms collections. The general condition of the historical collection is stable. Multi-year conservation contracts have been let with certified conservators, who are members in good standing with the American Institute of Conservators. The ongoing effort ensures that the historical collection is preserved in accordance with statutory requirements, Army regulations, and professional museum standards, and is interpreted in the interest of history, the U.S. Army, and the American people. Furthermore, the historical collection actively supports training and development, and serves as a bridge for common interest between the military and civilian communities.

Stewardship Land

For Fiscal Year Ended September 30, 2004 (Acres in Thousands)

(a) Land Use	(b) As of 10/1/03	(c) Additions	(d) Deletions	(e) As of 09/30/04
1. Mission (Note 1)	6,932.8	245.3	268.1	6,910.0
2. Parks & Historic Sites (Note 2)	.91	.54	.51	.94

Narrative Statement:

Additions/deletions are the result of: (a) acquiring additional land through donation or withdrawal from public domain; (b) identification of missing land records; and, (c) disposal of BRAC Closure sites or transfer of land to another DOD agency.

Notes:

1. Mission Land: includes the following category codes: 91120, 91131, 91141, 91210, 91310, 91320, 91330, 91410, 92111, 92121, 92131, 92190. These category codes represent land that was not purchased, but was either donated or withdrawn from public domain.
2. Parks/Historic Sites: Same as Cemetery Acreage on Heritage Report (includes category codes 76030, 76031, and 76032; excludes Pet Cemeteries). Unable to determine if cemeteries are purchased, donated or transferred property. This value could be double reported within Mission Related; therefore; this report should not be totaled.

Nonfederal Physical Property

Yearly Investment in State and Local Governments
For Fiscal Years FY 2000 through FY 2004
(In Millions of Dollars)

(a) Categories	(b) FY 2000	(c) FY 2001	(d) FY 2002	(e) FY 2003	(f) FY2004
Transferred Assets:					
1. National Defense Mission Related	$4.7	$94.8	$7.4	$85.0	$54.7
Funded Assets:					
2. National Defense Mission Related	0	0	0	0	0
Total	$4.7	$94.8	$7.4	$85.0	$54.7

Narrative Statement:

Investments in Nonfederal Physical Property refers to those expenses incurred by the Army for the purchase, construction, or major renovation of physical property owned by State and Local Governments, including major additions, alterations and replacements; the purchase of major equipment; and the purchase of improvement of other physical assets. The following is a schedule of estimated investments value of state-owned properties that are used by the Federal Government.

Notes:

1. 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 Accounting Standards requirements.
2. Data provided here are significant because these are properties that are owned by the various U.S. Property and Fiscal Offices and are essential in accomplishing the mission of the Army National Guard.
3. Costs of maintenance of these non-federal assets are included in the budgetary resources of Army National Guard.
4. These properties represent non-cash items that were transferred to State and local governments.

Investments in Research and Development

Yearly Investment in Research and Development
For Fiscal Years FY 2000 through FY 2004
(In Millions of Dollars)

(a) Categories	(b) FY 2000	(c) FY 2001	(d) FY 2002	(e) FY 2003	(f) FY 2004
1. Basic Research	$187.1	$209.2	$206.4	$226.9	$291.6
2. Applied Research	677.6	806.6	864.1	847.2	886.8
3. Development:					
Advanced Technology Development	701.2	821.9	863.1	988.6	1,010.4
Advanced Component Development and Prototypes	476.5	622.6	897.7	880.1	767.7
Systems Development and Demonstration	1,326.4	1,653.0	1,954.9	2,265.1	3,288.3
Research, Development, Test and Evaluation Management Support	961.9	888.8	880.9	979.4	1,069.8
Operational Systems Development	605.4	849.3	970.4	964.9	929.8
Total	$4,936.1	$5,851.4	$6,637.5	$7,152.2	$8,244.4

Narrative Statement:

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

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 involves the gathering of a fuller knowledge or understanding of the subject under study. Major outputs are scientific studies and research papers. The work in this program is consistent with the Army Campaign Plan, the Army Science and Technology Master Plan (ASTMP) and the Defense Technology Area Plan (DTAP). The following are two representative program examples for this category:

Defense Research Sciences (PE0601102A): This program sustains U.S. Army scientific competence as the foundation for ensuring that our Soldiers have superior land warfighting capability. This research provides new technology concepts and operational applications for the Army's Future Force. These investments also provide the resources to exploit scientific breakthroughs and avoid technological surprises. This program fosters innovation in Army niche areas and where the commercial incentive to invest is lacking due to limited markets. It also focuses university single investigators on research in areas of Army interest. The in-house portion of the program capitalizes on the Army's scientific talent and specialized facilities to expeditiously transition knowledge and technology into practical applications. The extramural program leverages the research efforts of other government agencies, academia, and industry. This promotes efficiency while eliminating undesirable duplication to achieve a well-integrated program that is executed by five primary contributors: 1) the Army Research Laboratory (ARL), which includes the Army Research Office; 2) the Research, Development and Evaluation Command (RDECOM) Research, Development and Engineering Centers (RDECs); 3) the Army Corps of Engineers Research and Development Center (ERDC); 4) the Army Medical Research and Materiel Command laboratories; and 5) the Army Research Institute. The basic research program is coordinated with the other Services through the Joint Directors of Laboratories panels, OSD's Tri-Service Reliance, and other interservice working groups. This program responds to the scientific and technological requirements of the Department of Defense Basic Research Plan by enabling the technologies that can significantly improve joint war fighting capabilities.

U**niversity and Industry Research Centers (PE0601104A):** This program leverages research in the private sector through Collaborative Technology Alliances (CTA), Centers of Excellence, and the University Affiliated Research Centers. CTAs are innovative alliances among government, industry and academic organizations to exploit scientific and technological breakthroughs and to transition these breakthroughs to applied research. This program includes the Army's Centers of Excellence, which couple state-of-the-art research programs at academic institutions with broad-based graduate education programs to increase the number of scientists and engineers in materials science, electronics and rotary wing technology. Also included in this program is the Army's national web-based competition to stimulate interest in science, math and technology in middle and high school students (eCYBERMISSION). This program also includes three "paradigm shifting" research centers seeking to accelerate opportunities in specific areas of potentially high payoff. These three centers are: the Institute for Soldier Nanotechnologies (ISN) at the Massachusetts Institute of Technology, the Institute for Collaborative Biotechnologies, the Army's Institute of Creative Technologies (ICT)-- a partnership with academia and the entertainment and gaming industries pursuing research in immersive simulations. Further, the Army funds Historically Black Colleges and Universities and Minority Institution (HBCU/MI) Centers of Excellence to address critical research areas for Army Transformation.

Applied Research: This area of technology investment funds the efforts to transform knowledge and understanding into practical warfighting applications. This research focuses on satisfying specific military needs. Major outputs are scientific studies, investigations, and research papers, hardware components, software codes, and limited construction of, or part of, a weapon system to include non-system specific development efforts. Work is consistent with the Army Campaign Plan, the Army Science and Technology Master Plan (ASTMP) and the Army Modernization Plan, and the Defense Technology Area Plan (DTAP). The following are two representative program examples for this category:

Materials Technology (PE0602105A): This program matures materials technology for armor and armaments to provide America's Soldiers with overmatching lethality and survivability compared to that of our adversaries. Many of the products from this applied research will be further matured for fielding in the Future Combat Systems (FCS) and other Future Force systems. When operational requirements demand new capabilities and where feasible, technology products from this program will be inserted into Current Force systems. This program also translates new materials concepts into applications using nanomaterials to increase performance while reducing weight of individual soldier support equipment, armor, armaments, aircraft, ground combat vehicles.

Combat Vehicle and Automotive Technology (PE0602601A): This program researches, investigates and matures combat vehicle and automotive technologies to improve survivability, mobility, sustainability, and maintainability of Army ground vehicles. Implementing DoD's transformation goals requires the Army to develop smaller and lighter systems to achieve essential strategic responsiveness. Technologies to make these lighter systems survivable are pursued in this program such as: active protection systems and advanced lightweight armor. This program also advances technologies for critical power, propulsion and electric components, including energy storage, power distribution and pulse forming networks. This program adheres to Tri-Service Reliance agreements in advanced materials, fuels and lubricants, and ground vehicles, with oversight and coordination provided by the Joint Directors of Laboratories. This program is coordinated with the Departments of Energy, Commerce, Transportation, and Defense Advanced Research Projects Agency (DARPA).

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 five stages defined below:

1. Advanced Technology Development: This area of technology includes all efforts to mature technology (hardware or software) sufficient for demonstration in an operational environment—this may be live or virtual. In this program experimental systems or subsystems are demonstrated to prove the technical feasibility and military utility of the approach selected. Advanced technology development provides the path for the rapid development and demonstration of new components and systems. The most complex efforts in this program are designated as Advanced Technology Demonstrations (ATDs). The Army's ATDs are developed to facilitate the smooth transition of advanced technology into systems as part of formal acquisition program.

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 Demonstration and Validation are hardware and software components, or complete weapon systems, ready for operational and developmental testing and field use.

1. 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 weapons systems finalized for complete operational and developmental testing.

2. RDT&E 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, operation and maintenance of test aircraft and ships, and studies and analyses in support of the R&D program.

3. 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 three representative program examples for this category:

Electronic Warfare Advanced Technology (PE0603008A): The goal of this program is to provide technologies for a secure, mobile, wireless network that operates in diverse and complex terrain all the time, in all environments for the Army's Future Force and, where feasible, exploit opportunities to enhance Current Force capabilities. A key goal of the work is to demonstrate the capability to seamlessly integrate communications technologies across all network tiers, ranging from unattended networks and sensors, through maneuver elements and airborne/space assets. To accomplish this goal the program will investigate and leverage external communication technologies and combine technology options in a series of Command, Control, Communications, and Computers Intelligence, Surveillance and Reconnaissance (C4ISR) On-The-Move (OTM) experimentations to measure the battlefield effectiveness for Future Combat Systems (FCS) and the Future Force. This program also matures: protection technologies for tactical wireless networks against modern network attacks; smart communication technologies to enable network and control of unmanned systems shortening the sensor-decider-engagement time to defeat critical targets. Several efforts of this program are conducted in conjunction with the Defense Advanced Research Projects Agency (DARPA) and the other Services.

Missile and Rocket Advanced Technology (PE0603313A): The emphasis in this program is on smaller, lighter weight, more affordable missiles. This program matures advanced missile technology to increase weapon system performance and countermeasures to defeat threat missile systems. This program funds demonstrations of advanced tactical missiles, real-time hardware-in-the-loop simulations, and multi-role seeker technology efforts. The technologies funded in this program demonstrate improved target location accuracy in clutter, lightweight missile launchers, precision guidance, hypervelocity missile flight, and missile communications, command and control. Specific efforts in this program include: Compact Kinetic Energy Missile (CKEM), Advanced Multi-Mission Precision Guided Munition (AMMPGM), Air Defense for the Unit of Action (concentrating on defense against Rockets, Artillery and Mortars (RAM)), and Helicopter Defensive Aides Suites for Integrated Survivability (HDAS/IS). The CKEM technology program will demonstrate a prime candidate to provide overwhelming lethality for the Future Combat Systems (FCS) Direct Fire System.

Army Test Ranges and Facilities: This program provides the institutional funding required to operate the developmental test activities required by Department of Defense (DoD), Department of the Army (DA) weapons systems developers and Research, Development, and Engineering Centers. This program provides resources to operate Army's Major Range and Test Facility Bases (MRTFB): White Sands Missile Range (WSMR), New Mexico; Aberdeen Test Center (ATC), Aberdeen Proving Ground (APG), Maryland; Yuma Proving Ground (YPG), Arizona. This program also provides the resources to operate the Army's developmental test capability at: Aviation Technical Test Center, Fort Rucker, AL; and Redstone Technical Test Center, Redstone Arsenal, AL. It also provides the resources for test planning and safety verification/confirmation. Developmental test capabilities at the test range have been uniquely established, are in place to support test and evaluation (T&E) requirements of funded weapons programs, and are required to assure technical performance, adherence to safety requirements, reliability, logistics supportability, and quality of materiel in development and in production. This program sustains the developmental T&E capability required to support all elements of Army Transformation, as well as Joint Service or Other Service systems, hardware, and technologies.

General Property, Plant, and Equipment

Real Property Deferred Maintenance Amounts
As of September 30, 2004

Narrative Statement:

FY2004 sustainment requirements for the Army are from version 4.1 of the DoD Facilities Sustainment Model (FSM). The required and executed amounts represent facilities funded from Operations & Maintenance (O&M), Army Family Housing (AFH), and Working Capital Fund (WCF) appropriations, and from Non-Appropriated Funds (NAF). Sustainment funding contributions from host nation funding (Japan) and military pay are included. The appropriated amount includes no contribution from WCF, NAF and host nation funding as these funds are not appropriated by Congress. Army sustainment data includes facilities that are multi-use heritage assets. The sustainment data excludes facilities funded from Research, Development, Test and Evaluation (RDTE), and Procurement appropriations, and Chemical Depots, because we lack separately identifiable sustainment funding for these locations.

Annual Sustainment FY 2004

Property Type	1. Required	2. Appropriated	3. Executed	4. Difference
Buildings, Structures, and Utilities	$3,322.8M	$2,696.1M	$2, 362.9M	$959.9M

Annual Deferred Sustainment Trend

Property Type	FY 2001	FY 2002	FY 2003	FY 2004
Buildings, Structures, and Utilities	$1,167M	$913.4M	$792.3M	$959.9M

Army Restoration & Modernization (R&M) requirements are modeled in the annual Installation Status Report (ISR). During ISR data collection, facility occupants evaluate the condition of each facility against published standards. Facilities are rated Green (complies with standards), Amber (does not fully meet standards), or Red (dysfunctional or substandard). ISR establishes a C-rating for groups of facilities, based on the proportion of facilities rated Green, Amber, and Red. Facility groups are rated C-1 (facilities fully support the mission), C-2 (facilities support the majority of assigned missions), C-3 (facilities impair mission performance), or C-4 (facilities significantly impair mission performance).

ISR develops cost estimates to improve groups of facilities to higher C-ratings. Using industry based improvement cost factors for each facility type, ISR builds the cost to improve Red and Amber facilities to Green in order to achieve higher C-ratings. The requirement reported for General PP&E R&M is the ISR cost to improve the quality of facilities to full up C-1 status, which represents all facilities being rated Green. For FY2004, these requirements address facility types funded from Army appropriated operations and maintenance (O&M), working capital fund (WCF), and Army family housing (AFH) funds. The Army’s R&M requirement does not include requirements for facilities funded by Department of Defense agencies (DECA, DLA, TMA, DODDS), non-appropriated funds-NAF (recreation, sports), Army Air Force Exchange Service, and private funding. The R&M requirement also excludes costs for utilities planned for privatization, closures from base realignment and closure (BRAC) decisions, ammunition plants and chemical depots.

Army facilities are predominantly C-3, due to years of underfunding sustainment. The Army's estimate to return these facilities to a full-up C-1 status for FY2004 is $32.1B, based on the 2004 ISR. The restoration & modernization requirement reported for FY2003 has been corrected from $26.5B as reported in September 2003, to $34.3B. The reason for this correction is to provide a cost consistent with full-up C-1 status, rather than the minimum C-1 status as previously reported. Reduced requirements for FY 2004 reflect improvements to the inventory from recent R&M investments.

Restoration & Modernization Requirements

Property Type	End FY 2003	End FY 2004	Change
Buildings, Structures, and Utilities	$34.3B	$32.1B	-$2.2B

Military Equipment

Deferred Maintenance Amounts
As of September 30, 2004
(Amount in Thousands)

(a) Major Type	(b)
1. Aircraft	$ 38,600
2. Ships	0
3. Missiles	49,800
4. Combat Vehicles	128,564
5. Other Weapons Systems	231,100
6. Total	$448,060

Department of Defense- Department of the Army

STATEMENT OF DISAGGREGATED BUDGETARY RESOURCES

As of September 30, 2004 and 2003 ($ in Thousands)

BUDGETARY RESOURCES **Budgetary Financing Accounts**	**Other**	**Research, Development, Test & Evaluation**	**Operation and Maintenance**
Budget Authority:			
Appropriations received	$1,937,452	$10,363,941	$69,934,146
Borrowing authority	0	0	0
Contract authority	0	0	0
Net transfers (+/-)	483,125	(49,367)	2,785,095
Other	0	0	0
Unobligated balance:			
Beginning of period	177,247	1,312,353	924,944
Net transfers, actual (+/-)	(402,025)	13,233	4,548,877
Anticipated Transfers Balances	0	0	0
Spending authority from offsetting collections:			
Earned	0	0	0
Collected	7,722	2,803,480	11,176,525
Receivable from Federal sources	6,900	23,021	526,955
Change in unfilled customer orders	0	0	0
Advance received	(22)	62,538	36,494
Without advance from Federal sources	(16,587)	483,759	619,738
Anticipated for the rest of year, without advances	0	0	0
Transfers from trust funds	0	0	0
Subtotal	($1,987)	$3,372,798	$12,359,712
Recoveries of prior year obligations	44,570	901,335	8,863,267
Temporarily not available pursuant to Public Law	0	0	0
Permanently not available	(3,274)	(126,400)	(470,471)
Total Budgetary Resources	$2,235,108	$15,787,893	$98,945,570
STATUS OF BUDGETARY RESOURCES			
Obligations incurred:			
Direct	$1,930,407	$10,353,336	$71,080,811
Reimbursable	17,614	3,697,451	13,343,901
Subtotal	$1,948,021	$14,050,787	$84,424,712
Unobligated balance:			
Apportioned	268,247	1,658,382	13,671,157
Exempt from apportionment	13,411	0	0
Other available	0	0	0
Unobligated Balances Not Available	5,429	78,724	849,701
Total, Status of Budgetary Resources	$2,235,108	$15,787,893	$98,945,570
Relationship of Obligations to Outlays:			
Obligated Balance, Net - beginning of period	$1,238,805	$3,775,317	$22,800,300
Obligated Balance transferred, net (+/-)	0	0	0
Obligated Balance, Net - end of period:			
Accounts receivable	(8,944)	(192,534)	(1,334,880)
Unfilled customer order from Federal sources	(16,833)	(2,029,559)	(5,256,056)
Undelivered orders	986,944	6,808,364	25,257,909
Accounts payable	221,966	663,854	9,250,334
Outlays:			
Disbursements	1,968,809	11,167,864	69,297,745
Collections	(7,700)	(2,866,019)	(11,213,019)
Subtotal	$1,961,109	$8,301,845	$58,084,726
Less: Offsetting receipts	(63,289)	0	0
Net Outlays	$1,897,820	$8,301,845	$58,084,726

Procurement	Military Personnel	Military Construction/Family Housing	2004 Combined	2003 Combined
$13,839,049	$51,091,331	$2,393,973	$149,559,892	$117,695,530
0	0	0	0	0
0	0	0	0	0
798,312	(1,502,535)	2,455	2,517,085	5,307,441
0	0	0	0	0
3,486,034	223,179	2,089,235	8,212,989	5,858,110
514,878	106,882	(83,581)	4,698,264	1,214,524
0	0	0	0	0
0	0	0	0	0
846,539	591,573	3,314,155	18,739,994	14,095,736
(3,448)	(238,383)	97,695	412,742	12,974
0	0	0	0	0
(4,090)	0	211,654	306,576	119,338
118,419	14,505	677,016	1,896,851	3,655,318
0	0	0	0	0
0	0	0	0	0
$957,420	$367,695	$4,300,520	$21,356,163	$17,883,366
600,789	2,390,363	1,196,356	13,996,679	8,001,403
0	0	0	0	0
(296,606)	(218,511)	(279,101)	(1,394,364)	(1,304,580)
$19,899,876	$52,458,404	$9,619,857	$198,946,708	$154,655,794
$15,779,790	$50,534,797	$2,911,796	$152,590,936	$128,012,383
1,062,073	674,086	4,679,891	23,475,016	18,430,419
$16,841,863	$51,208,883	$7,591,687	$176,065,952	$146,442,802
2,912,567	921,961	2,026,327	21,458,641	6,947,148
0	0	0	13,411	25,665
0	0	0	0	0
145,446	327,561	1,843	1,408,704	1,240,179
$19,899,876	$52,458,405	$9,619,857	$198,946,708	$154,655,794
$12,534,218	$3,576,399	$2,557,816	$46,482,855	$33,662,267
0	0	0	0	0
(68,508)	(167,122)	(121,458)	(1,893,446)	(1,480,706)
(1,528,514)	(14,505)	(3,867,703)	(12,713,171)	(10,816,319)
15,707,261	1,681,367	6,067,729	56,509,574	44,735,892
1,334,144	3,187,717	461,426	15,119,442	14,043,988
13,215,938	47,931,340	5,638,441	149,220,137	121,952,521
(842,449)	(591,573)	(3,525,809)	(19,046,568)	(14,215,073)
$12,373,489	$47,339,767	$2,112,632	$130,173,569	$107,737,448
0	0	0	(63,289)	(95,571)
$12,373,489	$47,339,767	$2,112,632	$130,110,280	$107,641,877

Department of Defense- Department of the Army

STATEMENT OF DISAGGREGATED BUDGETARY RESOURCES

As of September 30, 2004 and 2003 ($ in Thousands)

BUDGETARY RESOURCES **Non-Budgetary Financing Accounts**	**Other**	**Research, Development, Test & Evaluation**	**Operation and Maintenance**
Budget Authority:			
Appropriations received	$0	$0	$0
Borrowing authority	0	0	0
Contract authority	0	0	0
Net transfers (+/-)	0	0	0
Other	0	0	0
Unobligated balance:			
Beginning of period	1,273	0	0
Net transfers, actual (+/-)	0	0	0
Anticipated Transfers Balances	0	0	0
Spending authority from offsetting collections:			
Earned	0	0	0
Collected	152	0	0
Receivable from Federal sources	0	0	0
Change in unfilled customer orders	0	0	0
Advance received	0	0	0
Without advance from Federal sources	0	0	0
Anticipated for the rest of year, without advances	0	0	0
Transfers from trust funds	0	0	0
Subtotal	$152	$0	$0
Recoveries of prior year obligations	0	0	0
Temporarily not available pursuant to Public Law	0	0	0
Permanently not available	0	0	0
Total Budgetary Resources	$1,425	$0	$0
STATUS OF BUDGETARY RESOURCES			
Obligations incurred:			
Direct	$0	$0	$0
Reimbursable	0	0	0
Subtotal	0	0	0
Unobligated balance:			
Apportioned	1,424	0	0
Exempt from apportionment	0	0	0
Other available	0	0	0
Unobligated Balances Not Available	0	0	0
Total, Status of Budgetary Resources	$1,424	$0	$0
Relationship of Obligations to Outlays:			
Obligated Balance, Net - beginning of period	$0	$0	$0
Obligated Balance transferred, net (+/-)	0	0	0
Obligated Balance, Net - end of period:			
Accounts receivable	0	0	0
Unfilled customer order from Federal sources	0	0	0
Undelivered orders	0	0	0
Accounts payable	0	0	0
Outlays:			
Disbursements	0	0	0
Collections	(152)	0	0
Subtotal	($152)	$0	$0
Less: Offsetting receipts	0	0	0
Net Outlays	($152)	$0	$0

Procurement	Military Personnel	Military Construction/Family Housing	2004 Combined	2003 Combined
$0	$0	$0	$0	$0
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	1,272	730
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	152	543
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
$0	$0	$0	$152	$543
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
$0	$0	$0	$1,424	$1,273
$0	$0	$0	$0	$0
0	0	0	0	0
0	0	0	0	0
0	0	0	1,424	1,273
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
$0	$0	$0	$1,424	$1,273
$0	$0	$0	$0	$0
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	(152)	(543)
$0	$0	$0	($152)	($543)
0	0	0	0	0
$0	$0	$0	($152)	($543)

Required Supplemental Information - Part A

AT21 - Army General Fund

Government Transactions from the Consolidating Trial Balance

Schedule, Part A DoD Intragovernmental Asset Balances ($ Amounts in Thousands).	Treasury Index:	Fund Balance with Treasury	Accounts Receivable	Loans Receivable	Investments	Other
Executive Office of the President	11		$56			
Department of Agriculture	12		$323			$895
Department of Commerce	13		$462			$6,690
Department of the Interior	14		$143			$389,750
Department of Justice	15		$4,839			$573
Department of Labor	16		$44			
Navy General Fund	17		$59,749			
Department of State	19		$5,604			
Department of the Treasury	20	$89,548,609	$9,970		$1,497	$2,148
Library of Congress	3		$114			
Department of Veterans Affairs	36		$484			
General Service Administration	47		$2,767			
National Science Foundation	49					$157
Central Intelligence Agency	56		$1,608			
Air Force General Fund	57		$155,513			$15,155
Federal Emergency Management Agency	58		$458			
Environmental Protection Agency	68		$759			$2,553
Department of Transportation	69		$745			$83,907
Homeland Security	70		$8,288			$17,844
Small Business Administration	73					$1,426
Department of Health and Human Services	75		$15,631			$176
National Aeronautics and Space Administration	80		$788			$4,994
Department of Energy	89		$900			$6,009
Selective Service System	90		$152			
Department of Education	91		$3			
U.S. Army Corps of Engineers	96		$6,604			$98
Other Defense Organizations General Funds	97		$115,402			$63
Other Defense Organizations Working Capital Funds	97-4930		$38,713			$17,448
Army Working Capital Fund	97-4930.001		$30,871			$6,092
Air Force Working Capital Fund	97-4930.003		$876			$401
Totals:		**$89,548,609**	**$461,866**		**$1,497**	**$556,379**

Required Supplemental Information - Part B

AT21 - Army General Fund

Government Transactions from the Consolidating Trial Balance

Schedule, Part B DoD Intragovernmental entity liabilities ($ Amounts in Thousands).	Treasury Index:	Accounts Payable	Debts/Borrowings From Other Agencies	Other
Executive Office of the President	11	$2		$33,483
Department of Agriculture	12	$12,518		$58
Department of Commerce	13	$391		
Department of the Interior	14	$4,123		
Department of Justice	15	$691		$36
Department of Labor	16	$86,502		$415,241
Navy General Fund	17	$38,049		$154
Department of State	19	$11,277		$2,194
Department of the Treasury	20	$152,583		$84,496
Office of Personnel Management	24	$2,026		$47,564
Federal Communications Commission	27	$1,445		
Library of Congress	3	$504		$35
Nuclear Regulatory Commission	31	$54		
Department of Veterans Affairs	36	$2,606		$80
Government Printing Office	4	$325		
U.S. Equal Employment Opportunity Commission	45	$0		
General Service Administration	47	$364,219		$57
National Science Foundation	49	$697		
Federal Labor Relations Authority	54	$1		
Central Intelligence Agency	56			$493
Air Force General Fund	57	$14,203		$2,880
Federal Emergency Management Agency	58			$64
Tennessee Valley Authority	64	$5,703		
Environmental Protection Agency	68	$24,901		
Department of Transportation	69			$356
Homeland Security	70	$30,949		$2,111
Small Business Administration	73	$167		
Department of Health and Human Services	75	$1,257		$51,259
National Aeronautics and Space Administration	80	$3,898		$715
Department of Energy	89	$31,810		$52
Federal Mediation and Conciliation Services	93	$1		
U.S. Army Corps of Engineers	96	$848		
Other Defense Organizations General Funds	97	$31,010		$2,984
Other Defense Organizations Working Capital Funds	97-4930	$475,399		
Army Working Capital Fund	97-4930.001	$371,336		$1
Navy Working Capital Fund	97-4930.002	$33,598		
Air Force Working Capital Fund	97-4930.003	$3,637		
The General Fund of the Treasury	99			$1,758,589
Totals:		**$1,706,730**	**$0**	**$2,402,902**

Required Supplemental Information - Part C

AT21 - Army General Fund

Government Transactions from the Consolidating Trial Balance

Schedule, Part C DoD Intragovernmental revenue and related costs ($ Amounts in Thousands).	Treasury Index:	Earned Revenue
The Judiciary	10	$10
Executive Office of the President	11	$17,629
Department of Agriculture	12	$3,378
Department of Commerce	13	$3,482
Department of the Interior	14	$804
Department of Justice	15	$42,019
Department of Labor	16	$49
Navy General Fund	17	$672,175
Department of State	19	$65,236
Department of the Treasury	20	$20,197
Library of Congress	3	$696
Department of Veterans Affairs	36	$2,072
General Service Administration	47	$3,770
Central Intelligence Agency	56	$9,801
Air Force General Fund	57	$1,490,825
Federal Emergency Management Agency	58	$3,414
Environmental Protection Agency	68	$4,192
Homeland Security	70	$43,282
Department of Health and Human Services	75	$44,937
National Aeronautics and Space Administration	80	$17,473
Department of Energy	89	$5,376
Other Legislative Branch Agencies	9	$43
Department of Education	91	$3
U.S. Army Corps of Engineers	96	$102,192
Other Defense Organizations General Funds	97	$3,953,026
Other Defense Organizations Working Capital Funds	97-4930	$358,955
Army Working Capital Fund	97-4930.001	$371,129
Air Force Working Capital Fund	97-4930.003	$5,973
The General Fund of the Treasury	99	($81,596)
DoD Medicare-Eligible Retiree Health Care Fund		$146,240
Totals:		**$7,306,782**

Required Supplemental Information - Part E

AT21 - Army General Fund

Government Transactions from the Consolidating Trial Balance

Schedue, Part E DoD Intragovernmental Non-exchange Revenues ($ Amounts in Thousands).	Treasury Index:	Transfers In	Transfers Out
Executive Office of the President	11	$10,253,641	
Air Force General Fund	57	$44,393	$9,386
US Army Corps of Engineers	96	$331	$78
Other Defense Organizations General Funds	97	$430,168	$68,893
Other Defense Organizations Working Capital Funds	97-4930	$983,259	
Army Working Capital Fund	97-4930.001	$1,407,000	
Navy Working Capital Fund	97-4930.002	$200,000	
Air Force Working Capital Fund	97-4930.003	$350,000	
Totals:		**$13,668,792**	**$78,357**

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

November 8, 2004

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

SUBJECT: Independent Auditor's Report on the Fiscal Year 2004 Army General Fund Financial Statements (Report No. D-2005-011)

The Chief Financial Officers Act of 1990, as amended by the Federal Financial Management Act of 1994, requires Federal agency Inspectors General appointed under the Inspector General Act of 1978, as amended, to audit their respective agency's financial statements or determine that "an independent external auditor" should conduct such audits. Pursuant to this statutory authority, the undersigned Inspector General assumed responsibility for auditing the accompanying Army General Fund Consolidated Balance Sheet as of September 30, 2004 and 2003, the related Consolidated Statement of Net Cost, the Consolidated Statement of Changes in Net Position, the Combined Statement of Budgetary Resources, the Combined Statement of Financing, and the Statement of Custodial Activity for the fiscal years then ended.

The financial statements are the responsibility of Army management. The Army is also responsible for implementing effective internal control and for complying with laws and regulations. We are unable to give an opinion on the Fiscal Year 2004 financial statements of the Army General Fund. 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 the audit.

Disclaimer of Opinion on the Financial Statements

The Assistant Secretary of the Army (Financial Management and Comptroller) acknowledged to us that financial management systems do not substantially comply with Federal financial management system requirements, generally accepted accounting principles, or the U.S. Government Standard General Ledger at the transaction level, and cannot provide adequate evidence supporting various material amounts on the financial statements. Therefore, we did not perform auditing procedures to determine whether material amounts on the financial statements were fairly presented. We did not perform these and other auditing procedures because Section 1008(d) of the FY 2002 National Defense Authorization Act limits the Inspector General of the Department of Defense to performing only audit procedures required by generally accepted government auditing standards consistent with the representations made by management. The Army has also acknowledged, and prior audits have identified, the material weaknesses listed in the Summary of Internal Control. These material weaknesses also affect the reliability of certain information contained in the

"A regular Statement and Account of the Receipts and Expenditures of all public Money shall be published from time to time."—Constitution of the United States, Article I, Section 9

annual financial statements—much of which is taken from the same data sources as the principal financial statements.[1] As described above, we are unable to express, and we do not express, an opinion on the financial statements and the accompanying information.

Summary of Internal Control

In planning our audit, we considered Army internal control over financial reporting and compliance. We did this to determine our procedures for auditing the financial statements and to comply with Office of Management and Budget 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. However, previously identified reportable conditions,[2] all of which are material, continued to exist in the following areas:

- Financial Management Systems;
- Accounting Adjustments;
- Intragovernmental Transactions and Eliminations;
- Abnormal Account Balances;
- Fund Balance With Treasury;
- Accounts Receivable;
- Inventory and Related Property;
- General Property, Plant, and Equipment;
- Accounts Payable;
- Environmental Liabilities;
- Statement of Net Cost;
- Statement of Budgetary Resources; and
- Statement of Financing.

A material weakness is a condition that precludes the entity's internal control from providing reasonable assurance that misstatements, losses, or noncompliance that are material in relation to the financial statements would be prevented or detected on a timely basis. Our internal control work would not necessarily disclose all material weaknesses. See the Attachment for additional details on material internal control weaknesses.

Summary of Compliance With Laws and Regulations

Our work to determine compliance with selected provisions of applicable laws and regulations related to financial reporting was limited because management acknowledged, and prior audits confirm, that instances

[1] The annual financial statements include the principal financial statements, management discussion and analysis, consolidating and combining financial statements, Required Supplementary Stewardship Information, Required Supplementary Information, and Other Accompanying Information.

[2] Reportable conditions are matters coming to the auditor's attention that, in his or her judgment, should be communicated to management because they represent significant deficiencies in the design or operation of internal control, which could adversely affect the organization's ability to initiate, record, process, and report financial data consistent with the assertions of management in financial statements.

of noncompliance continue to exist. The Assistant Secretary of the Army (Financial Management and Comptroller) acknowledged to us that the Army was unable to comply with the requirements of the CFO Act of 1990, as amended. The Army has also acknowledged that many of its financial management and feeder systems do not comply with the requirements of the Federal Financial Management Information Act of 1996. The Army was also unable to comply with Government Performance and Results Act (GPRA) requirements because it did not have cost accounting systems in place to collect, process, and report operating costs. Therefore, we did not determine whether the Army was in compliance with all applicable laws and regulations related to financial reporting. See the Attachment for additional details on compliance with laws and regulations.

Management Responsibility

Management is responsible for:

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

We provided a draft of this report to Army officials. Army officials concurred with the facts and conclusions in the report. Army officials expressed their commitment to address the problems the report outlines.

Joseph E. Schmitz
Inspector General
Department of Defense

Paul J. Granetto, CPA
Assistant Inspector General
Defense Financial Auditing Service

Attachment:
As stated

"A regular Statement and Account of the Receipts and Expenditures of all public Money shall be published from time to time."—Constitution of the United States, Article I, Section 9

Report on Internal Control and Compliance with Laws and Regulations

Internal Control

Management is responsible for implementing effective internal control and for providing reasonable assurance that accounting data are accumulated, recorded, and reported properly 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 because management acknowledged that previously identified reportable conditions, all of which are material, continue to exist. The following financial management deficiencies are indications of material weaknesses in internal control that may adversely affect any decision by the Army that is based, in whole or in part, on information that is inaccurate because of these deficiencies. Financial information reported for the Army also may contain misstatements resulting from these deficiencies.

Financial Management Systems. Army accounting systems lacked a single standard transaction-driven general ledger. The Army also needed to upgrade or replace many of its non-financial feeder systems so that financial statement reporting requirements could be met. The lack of integrated, transaction-driven, financial management systems will continue to prevent the Army from preparing auditable financial statements.

The Army has acknowledged that its financial management systems were unable to meet all of the requirements for full accrual accounting. Many of the Army financial systems, non-financial feeder systems, and processes were designed and implemented prior to the issuance of generally accepted accounting principles and therefore, were not designed to collect and record financial information on the accrual basis. Until such time as the Army's systems and processes are updated in accordance with generally accepted accounting principles, the Army's financial data will be based on budgetary transactions, non-financial feeder system transactions, and adjustments for known accruals of major items. The Army derives its reported values and information for major asset and liability accounts from non-financial feeder systems, such as inventory and logistics systems. Major assets include Property, Plant, and Equipment and Inventory and Related Property. Budgetary transactions were recorded, for example, in Fund Balance with Treasury, Accounts Receivable, Accounts Payable, Gross Costs, and Earned Revenue. Until the Army systems are updated, Army financial data will be based on budgetary transactions (obligations, disbursements, and collections).

Accounting Adjustments. Because of inadequate financial management systems and processes, journal voucher adjustments and data calls were used to prepare the Army General Fund financial statements. General ledger adjustments were processed to make the summary proprietary balances match budgetary status appropriation balances when preparing Army's financial statements. In addition, DFAS Indianapolis did not adequately support $258.1 billion in journal voucher adjustments used to prepare the Army General Fund financial statements. Specifically, Defense Finance and Accounting Service (DFAS) Indianapolis made:

- $134.6 billion in unsupported adjustments to force amounts to agree with other sources of information and records or financial statement lines;
- $53.3 billion in unsupported adjustments to intragovernmental accounts to force the accounts to agree with the records of the Army's trading partners;
- $45.5 billion in unsupported adjustments to correct errors and reclassify amounts to other accounts; and
- $24.7 billion in unsupported adjustments to force general ledger accounts to agree with status of appropriations data (or ending balance adjustments) without reconciling the differences or determining which data source was correct.

Intragovernmental Transactions and Eliminations. DoD is unable to collect, exchange, and reconcile buyer and seller intra-governmental transactions, resulting in adjustments that cannot be verified. This is primarily because of systems limitations, as the majority of the systems currently used within DoD do not allow for the capture of buyer-side information for use in reconciliations and eliminations. DoD and Army accounting systems were unable to capture trading partner data at the transaction level in a manner that facilitated required trading partner eliminations, and DoD guidance did not require adequate support for eliminations. In addition, DoD procedures required that buyer-side transaction data be forced to agree with seller-side transaction data without performing proper reconciliations. Therefore, DFAS Indianapolis made $53.3 billion in unsupported adjustments to intragovernmental accounts to force the accounts to agree with the records of Army's trading partners.

Abnormal Account Balances. DFAS Indianapolis did not effectively detect, report, or take effective action to eliminate abnormal balances included in the Army General Fund accounting records. The abnormal balances were included on trial balances submitted to DFAS Indianapolis during FY 2004. Abnormal balances not only distort the Army General Fund financial statements, but also indicate internal control and operational deficiencies. The existence of abnormal balances may also conceal instances of fraud. There is also the potential for the errors causing abnormal balances to be perpetuated in the Defense Departmental Reporting System-Budgetary Module, when it is implemented.

Fund Balance with Treasury. DoD and its Components, including the Army, have had long-standing problems in reconciling transaction activity in their Fund Balance with Treasury accounts. Appropriation balances recorded in the accounting records do not agree with balances held at Treasury. Therefore, DFAS Indianapolis made unsupported adjustments that had a net effect of $1.1 billion on the financial statement line items. In addition, material uncertainties exist in Fund Balance with Treasury, especially with regards to suspense accounts.

Accounts Receivable. DoD has acknowledged weaknesses in its accounts receivable management. The weaknesses are considered to be DoD-wide and apply to both public and intragovernmental receivables at the Army General Fund level. Weaknesses include:

- noncompliance with policies and procedures regarding referrals to Debt Management and Treasury and for write-offs of two-year old debt,
- a lack of controls to ensure all entitlement system receivables (vendor pay, civilian pay, and interest) are recorded in the accounting systems, and
- a lack of controls to ensure that accounts receivable balances are supportable at the transaction level.

As a result, DFAS Indianapolis made $783.3 million in unsupported adjustments for FY 2004 that decreased accounts receivable balances by $596.2 million.

Inventory and Related Property. Inventories are reported at approximate historical cost using Latest Acquisition Cost adjusted for holding gains and losses. The systems do not maintain historical cost data necessary to comply with Statement of Federal Financial Accounting Standards (SFFAS) No. 3, "Accounting for Inventory and Related Property." The systems are also unable to produce financial transactions using the U.S. Government Standard General Ledger. SFFAS No. 3 states that Operating Materials and Supplies shall be expensed when the items are consumed. However, DoD has acknowledged that significant amounts of Operating Materials and Supplies were expensed when they were purchased instead of when they were consumed.

General Property, Plant, and Equipment. SFFAS No. 6, "Accounting for Property, Plant, and Equipment," requires that all General Property, Plant, and Equipment be recorded at cost, and that depreciation expense be recognized on all general property, plant, and equipment. The Army has acknowledged that real property was not recorded at acquisition or historical cost and did not include all costs needed to bring the real property to a form and location suitable for its intended use. Also, the Army could not support the reported cost of Military Equipment in accordance with SFFAS No. 6. Military Equipment was not recorded at acquisition or historical cost and did not include all costs needed to bring the equipment to a form and location suitable for its intended use. The Army also lacks FFMIA-compliant property accountability systems for all its Military Table of Equipment unit property books.

Accounts Payable. The Army is unable to properly account for and report Accounts Payable. DFAS Indianapolis made $63.7 billion in unsupported adjustments for FY 2004 that decreased Accounts Payable balances by $27.1 billion. In addition, the Army accounting systems do not capture trading partner data at the transaction level in a manner that facilitates trading partner aggregations for intra-agency sales. Therefore, the Army has acknowledged that it was unable to reconcile intragovernmental accounts payable to the related intragovernmental accounts receivable that generated the payables.

Environmental Liabilities. The Army has not properly estimated and reported its environmental liabilities. For example, the data and processes used to report Defense Environmental Restoration Program, Base Realignment and Closure, and non-Defense Environmental Restoration Program environmental liabilities on the financial statements did not have adequate documentation and audit trails. Although estimators were properly qualified to perform estimates, the Army did not document supervisory reviews of estimates, and adequate quality control programs were not in place to ensure the reliability of data. DFAS has identified ongoing actions to correct the reporting of environmental liabilities by October 2006.

Statement of Net Cost. The Statement of Net Cost is not presented by programs that align with major goals and outputs described in the DoD strategic and performance plans required by the GPRA. In addition, revenues and expenses are reported by appropriation categories because financial processes and systems do not collect costs in line with performance measures. The amounts presented in the Statement of Net Cost are based on funding, obligation, accrual and disbursing transactions, which are not always recorded using accrual accounting. Army systems do not always record the transactions on an accrual basis as is required by the generally accepted accounting principles. The information presented also includes data from non-financial feeder systems to capture all cost and financing sources for the Army. Also, Army General Fund budgetary and proprietary information does not correlate. Therefore, DFAS Indianapolis made $9.2 billion in unsupported adjustments to force costs to agree with obligation information. Specifically, these adjustments forced costs reported on the Statement of Net Cost to match the value of Expended Appropriations minus the amount of Capitalized Assets reported on the Statement of Financing.

Statement of Budgetary Resources. The Army accounting systems do not provide or capture data needed for obligations incurred and recoveries of prior year obligations in accordance with Office of Management and Budget Circular A 11, "Preparation, Submission, and Execution of the Budget Requirements." Although the Army developed an alternative methodology to calculate these items, the amount of distortion cannot be reliably determined. The Statement of Budgetary Resources does not include eliminating entries and therefore a Disaggregated Statement of Budgetary Resources is included in the Required Supplementary Information section of the financial statements. The Army uses budget execution data, which is composed of transaction report codes, to prepare the monthly Standard Form 133 and the quarterly Federal Agencies Centralized Trial Balance System II budgetary general ledger accounts. DFAS Indianapolis personnel use the Federal Agencies Centralized Trial Balance System II data to prepare the Statement of Budgetary Resources. Since both the Standard Form 133 and the Statement of Budgetary Resources are prepared using budget execution data, there is no true reconciliation between the two reports. Office of Management and Budget Bulletin 01 09 states that the Statement of Budgetary Resources should be based on the entity's budgetary general ledger, instead of based on budget execution data. In FY 2004, DFAS Indianapolis prepared $5.0 billion in unsupported adjustments that affected general ledger accounts used in the Statement of Budgetary Resources.

Statement of Financing. The Office of Management and Budget requires a consolidated Statement of Financing, except for the budgetary information used to calculate net obligations, which must be presented on a combined basis. However, the Statement of Financing for the Army General Fund is prepared on a combined basis. Also, because the differences between the Statement of Net Cost and the Statement of Financing were not reconciled, the Statement of Financing does not accurately present the relationship between budgetary obligations incurred by the Army General Fund and its Net Cost of Operations. This is evidenced by DFAS Indianapolis preparing $9.2 billion in unsupported adjustments to force costs to agree with obligation information.

Compliance With Laws and Regulations

Management is responsible for compliance with existing laws and regulations related to financial reporting. Our work to determine compliance with selected provisions of the applicable laws and regulations was limited because management acknowledged instances of non compliance, and previously reported instances of non compliance continue to exist. Therefore, we did not determine whether the Army 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 compliance with applicable laws and regulations.

Statutory Financial Management Systems Reporting Requirements. The Army is required to comply with the following financial management systems reporting requirements. For example, the Federal Financial Management Information Act of 1996 requires the Army 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. In addition, the Federal Managers' Financial Integrity Act of 1982 requires DoD to evaluate the systems and to annually report whether those systems are in compliance with applicable requirements. The CFO Act requires that each agency develop and maintain an integrated agency accounting and financial management system, including financial reporting and internal control. The system should comply with internal control standards; applicable accounting principles, standards, and requirements; and provide for complete, reliable, consistent, and timely information.

The Army acknowledged that many of its critical financial management and feeder systems do not comply substantially with Federal financial management systems requirements, Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level. The Army is also unable to comply with the CFO Act because its financial management systems were not integrated and it has acknowledged that many of its financial management and feeder systems do not comply with applicable Federal accounting standards.

In an attempt to comply with statutory reporting requirements and applicable financial systems requirements in the future, the Secretary of Defense has initiated a comprehensive financial management reform program for the Department. The Department is currently undergoing a major reevaluation of the ways in which it performs its financial management operations. The centerpiece of this financial management reform effort is the development of a Department-wide financial Business Enterprise Architecture. The enterprise architecture essentially will be a blueprint describing the Department's future financial management systems and processes.

Government Performance and Results Act. GPRA requires that each Federal agency prepare a strategic plan and annual performance plans and reports. The Army did not comply with GPRA because it did not have cost accounting systems in place to collect, process, and report operating costs. This resulted in the Army General Fund Statement of Net Cost being unable to provide cost-of-operations data that were consistent with GPRA performance goals and measures.

Audit Disclosures

We did not perform audit work related to the following selected provisions of laws and regulations:

- Antideficiency Act
- Provisions Governing Claims of the United States Government
- Federal Credit Reform Act of 1990
- Pay and Allowance System for Civilian Employees
- Prompt Payment Act

The Assistant Secretary of the Army (Financial Management and Comptroller) acknowledged to us on March 3, 2004, that Army General Fund financial management systems cannot provide adequate evidence supporting various material amounts on the financial statements. As a result, we were unable to obtain adequate evidential matter to form or express an opinion on the financial statements, internal control, and compliance with laws and regulations.

This report does not include recommendations to correct the material internal control weaknesses and instances of noncompliance because previous audit reports contained recommendations for corrective actions. Recommendations to correct identified weaknesses were made in other audit reports.

Working Capital Fund—Management's Discussion & Analysis

Overview

For the second year in a row, troop deployments in Iraq and Afghanistan have caused demand to surge for the products and services of activities operating under the Army Working Capital Fund (AWCF). Largely commercial or industrial in nature, the activities design, develop, acquire, produce, repair, overhaul, test, or manage combat weapons systems and their components.

The Army organizes these activities into three groups: Supply Management, Army (SMA); Depot Maintenance; and Ordnance. In FY 2004, the three groups together had revenues of over $14 billion. They employed over 21,000 civilians and 45 uniformed personnel at 18 locations in the continental United States (CONUS). Until FY 2004, the AWCF included a fourth activity: the Information Services activity group. This group was decapitalized effective September 30, 2003, and is no longer part of the AWCF financial structure.

The primary mission of AWCF activities is to help the Army maintain constant readiness by providing supplies, equipment, and ordnance necessary to support the projection and sustainment of our forces as and when required by the Nation.

Mission

The primary mission of AWCF activities is to help the Army maintain constant readiness by providing supplies, equipment, and ordnance necessary to support the projection and sustainment of our forces as and when required by the Nation. In carrying out this mission, the activities are obligated to control or reduce costs. In addition, the Activities must maintain their capability to expand quickly in order to ramp up from a peacetime workload level to support wartime requirements for operations such as Operation Iraqi Freedom, Operation Enduring Freedom, and Operation Noble Eagle.

Supply Management Mission

SMA activity group buys and maintains assigned stocks of materiel for sale to its customers, primarily Army operating units. The Army's equipment and operational readiness and its combat capability are directly linked to the availability of this materiel. The activity group is managed by the major subordinate commands of the U.S. Army Materiel Command (AMC).

Depot Maintenance Mission

The Depot Maintenance activity group provides the Army with an organic industrial capability to repair, overhaul, modify, and upgrade weapons systems, component parts, and support equipment. In addition to the maintenance mission, the activity group provides installation base support to Army, DoD, as well as to other

Governmental and private sector tenants. Depot Maintenance activities both compete and partner with private industry to deliver goods and services efficiently and effectively.

Depots are under the direct command and control of Major Subordinate Commands (MSCs) of the AMC and are aligned in accordance with the nature of their mission and the items that are repaired. Corpus Christi and Letterkenny Army Depots report to the Aviation and Missile Command (AMCOM), Redstone Arsenal, AL, Anniston, and Red River report to the Tank-automotive and Armaments Command (TACOM), Warren, MI, and Tobyhanna Army Depot report to the Communication-Electronics Command (CECOM), Fort Monmouth, NJ. The depots have been designated as Centers of Technical Excellence for the performance of core maintenance missions supporting all of DoD and our foreign allies.

Ordnance Mission

The Ordnance activity group produces armaments and munitions; manufactures, renovates, and demilitarizes material; and provides ammunition stockpile management for all Services within the DoD and for foreign military customers. Three activities of the AMC manage this activity group. The TACOM, located at Warren, MI, manages Rock Island Arsenal, Watervliet Arsenal, and Sierra Army Depot. The Chemical Materials Agency (CMA), located at Aberdeen Proving Ground, MD, manages Pine Bluff Arsenal. The Army Field Support Command (AFSC), located at Rock Island, IL, manages Crane Army Ammunition Activity, Blue Grass Army Depot, McAlester Army Ammunition Plant, and Tooele Army Depot.

The Ordnance activity group provides an organic industrial capability to manufacture and sell quality munitions and large-caliber weapons critical to the Army's capability to execute its warfighting mission. A number of these facilities provide the full range of ammunition maintenance for modern weapons. The activity group also provides logistics management, including follow-on procurement, production, maintenance, engineering, and integrated logistics support management of ordnance for all U.S. Military Services. Additionally, seven of the eight activities provide installation base support to tenant activities.

Organization

Figure 7

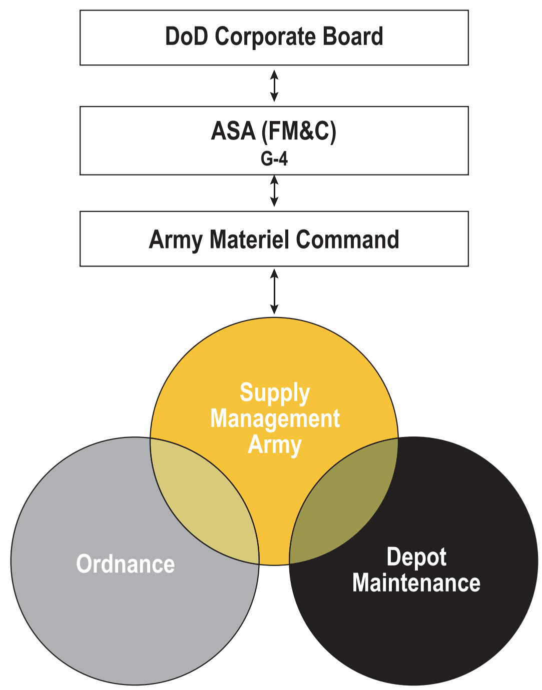


Table 13. Supply Management, Army

"Wholesalers" who buy and maintain stocks of materiel for sale to Operating Forces units and other customers

Command/Location	Area of Materiel Support
Aviation and Missile Command, Huntsville, AL (AMCOM)	Aircraft and aviation ground support items; missile system items.
Communications–Electronics Command, Fort Monmouth, NJ (CECOM)	Communication and electronics items.
Tank–automotive and Armaments Command, Warren, MI (TACOM)	Combat, automotive, and construction items.
Tank–automotive and Armaments Command, Acquisition and Logistics Activity, Rock Island, IL (TACOM-RI)	Weapons, special weapons, and fire control systems.
Tank–automotive and Armaments Command, Soldier and Biological Chemical, Natick, MA (TACOM-SBC)	Ground support items and chemical weapons.

The AMC controls AWCF activities through the major Supply Management subordinate commands shown in Table 13, the AFSC at Rock Island, IL, and the CMA at Aberdeen Proving Ground, MD. AMC reports to the Army Deputy Chief of Staff, G-4 and to the Assistant Secretary of the Army (Financial Management and Comptroller) (ASA (FM&C)). A DoD corporate board provides oversight of Working Capital Fund functions; the board includes the Under Secretary of Defense (USD) (Comptroller), Principal Deputy Under Secretary of Defense (Comptroller), and representatives from each of the following member organizations: USD (Acquisition and Technology), USD (Personnel and Readiness), Assistant Secretary of Defense (Command, Control, Communications and Intelligence), Assistant Secretaries for Financial Management and Comptroller of the Army, Navy and Air Force

Table 14. Depot Maintenance

Activities that repair, overhaul, or upgrade weapons and manufacture, test, and field communication-electronics systems and missile guidance and control systems.

Command/Activity/Location	Combat Systems
TACOM Anniston Army Depot, Anniston, AL*	Heavy-tracked combat vehicles and artillery.
AMCOM Corpus Christi Army Depot, Corpus Christi, TX	Rotary wing aircraft, engines, and components.
AMCOM Letterkenny Army Depot, Chambersburg, PA*	Tactical missile systems.
TACOM Red River Army Depot, Texarkana, TX*	Light armored vehicles and select missile systems.
CECOM Tobyhanna Army Depot, Tobyhanna, PA*	Communications—electronics and missile guidance and control systems and equipment

**Also provides base support services to tenant organizations.*

Table 15. Ordnance

Activities that produce, renovate, or manage ordnance materiel such as ammunition, artillery, and defensive devices.

Activity/Location	Mission
CMA Pine Bluff Arsenal—Pine Bluff, AR*	Manufactures conventional ammunition and chemical and biological defense items. Produces and rebuilds decontaminating kits, large filters, masks, and defensive chemical test equipment.
TACOM Rock Island Arsenal—Rock Island, IL*	Produces weapons for infantry, artillery, and air defense; armament for tanks, artillery, and personnel- and cargo-carriers; and special tools and tool sets.
TACOM Watervliet Arsenal—Watervliet, NY*	Produces mortars, recoilless rifles, cannon for tanks and towed and self-propelled artillery, special tool sets, and training devices and simulators.
AFSC Crane Army Ammunition Activity—Crane, IN	Produces, loads and assembles, stores, distributes, renovates, maintains, and demilitarizes conventional ammunition and ammunition-related components.
AFSC McAlester Army Ammunition Plant—McAlester, OK	Produces, loads and assembles, stores, distributes, renovates, maintains, and demilitarizes bombs, missiles, and conventional ammunition and missiles.
TACOM Sierra Army Depot—Herlong, CA*	Responsible for receipt, storage, and care of supplies in storage; as well as repair, assembly, disassembly, and shipment of major and secondary items for operational project stocks.
AFSC Tooele Army Depot—Tooele, UT*	Designs and develops ammunition-peculiar equipment. Stores, maintains, distributes, and demilitarizes conventional ammunition.
AFSC Blue Grass Army Depot—Richmond, KY*	Responsible for receipt, issue, storage, testing, and minor repair of chemical defense equipment. Stores, maintains, distributes, and demilitarizes conventional ammunition.
AFSC Red River Munitions Center—Texarkana, TX AFSC Letterkenny Munitions Center—Chambersburg, PA AFSC Anniston Munitions Center—Anniston, AL	Store, maintain, distribute, and demilitarize conventional ammunition.

**Also provides base support services to tenant organizations.*

(Program Analysis and Evaluation), Office of USD (Comptroller), Inspector General DoD (IG DoD), U.S. Transportation Command, Defense Logistics Agency, Defense Finance and Accounting Service (DFAS), and the Office of Management and Budget. Tables 13 through 15 show the three activity groups of the AWCF: Supply Management, Army; Depot Maintenance; and Ordnance.

Each subordinate command manages Depot Maintenance (see Table 14) and Ordnance (Table 15) activities. In addition to their primary missions of supporting combat weapons systems, most of the activities are "landlords" of their locations and provide base support services to tenant organizations.

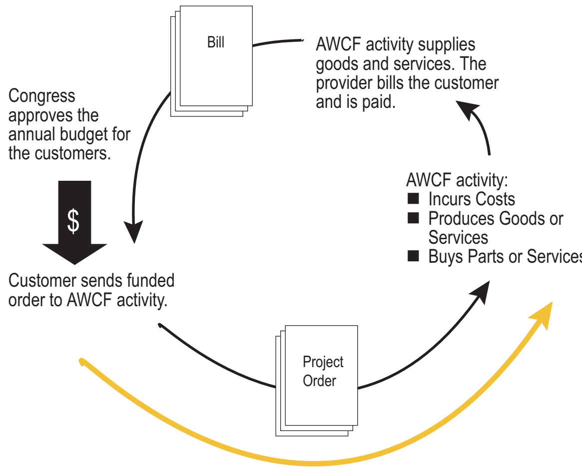
UH60 Recapitalization facility.

About Working Capital Funds

The AWCF is a revolving fund, which is an account or fund that derives its income from its operations and can finance these operations without fiscal year limitation (no-year account). The fund operates through the five step process shown in Figure 8.

As shown in Figure 8, in the first of five steps in the process Congress appropriates funds for projects and programs of AWCF customers. Second, a customer sends an AWCF activity a funded request for a given amount of products or services, such as overhauling 100 tanks. Third, the activity does the work, incurring costs such as labor and materials, and the AWCF supplies the working capital to cover these costs. Fourth, the activity invoices the customer for the cost of the order. Fifth, the customer deposits payment in the AWCF, thus replenishing the fund so that it can supply working capital to other projects.

Figure 8. How the AWCF Operates



Pricing

AWCF activities bill customers for costs and a small fee or surcharge. They charge standard rates on a unit cost basis; for each function, rates are calculated as follows:

- **Supply Management:** Rates include cost of goods plus a surcharge that recovers the actual costs of operating the supply business.
- **Depot Maintenance:** Rates include costs incurred in repair, rework, or modification of depot-level reparable items or components, expressed as cost per direct labor hour.
- **Ordnance:** Rates include costs incurred in the manufacturing of quality munitions and large-caliber weapons and of the storage, maintenance, distribution, and de-militarization of conventional ammunition, expressed as cost per direct labor hour.

During execution, activities charge customers a standard rate for goods and services. The standard rate is held constant once set in the budget process. This enables customers to plan their budgets and appropriation requests with more certainty than if costs reflected short-term variations in market prices for material and labor.

Support services provided by AWCF activities are essential to the success of the Operating Forces, and the activities themselves are an integral part of the defense team. Provided on the following pages is more detailed information on the activities and their performance in FY 2004.

Working Capital Fund Performance Results

Corporate Performance

The mission of the AWCF is to provide support services to the operating forces in the most efficient and cost-effective manner possible. Assessing the performance of the AWCF through the use of financial and program performance measures indicates how well the AWCF is accomplishing its mission.

Performance Measures

Cash Management

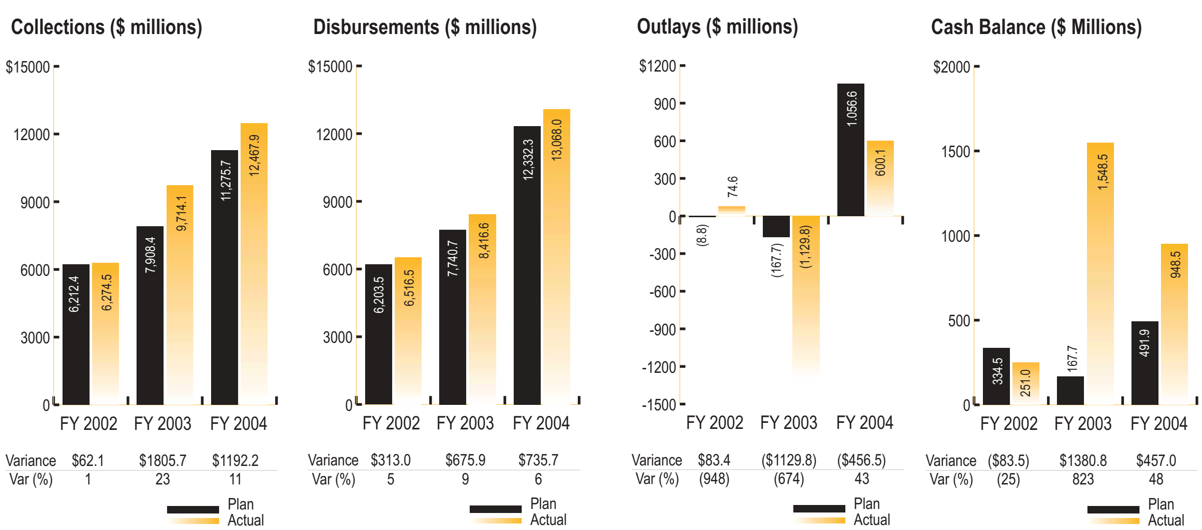
The ability to generate cash is dependent on: setting rates to recover full costs, including any previous year losses; accurately projecting workload; and meeting established operational goals. The Army must maintain sufficient cash on hand in the AWCF account at the U.S. Treasury to pay liabilities when due. Unlike the private sector, the Army does not have the ability to take advantage of lines of credit. To minimize the cash balance required for operating and capital disbursements, the Army manages cash at the corporate level. Rather than having to maintain a positive cash balance, the AWCF activity groups and installations project collections and disbursements on a monthly basis, working within a 10 percent margin of error.

Projecting cash flows has in past years proven challenging. A direct correlation can be made between monthly revenue and collections, but no direct correlation can be made between monthly expenses and disbursements. The difficulty arises within the SMA activity group. Monthly expenses are based on the cost of goods sold, while disbursements are based on deliveries of materiel on order or in repair.

The DFAS, the Army's accounting services provider, is currently implementing systems improvements that are expected to enable the Army to see collections and disbursements in real-time.

Figure 9 shows the planned and actual collections, disbursements, and outlays at the Army corporate level for the last three fiscal years, and the resulting cash balance that will be used to pay our suppliers and producers of goods. The AWCF ended FY 2004 with a cash balance of $948.5 million, $456.6 million above plan. This represents a variance of 48 percent. The ending cash balance reflects the results of the increase in consumption of repair parts and production at our industrial facilities associated with the Global War on Terrorism (GWOT). In addition, in FY 2004 the Army transferred $1.3 billion in cash (included with disbursements in Figure 9) to the Operation and Maintenance, Army (OMA)

Figure 9. Corporate Cash Management



appropriation in support of the GWOT. The $1.3 billion will need to be returned to the fund at a future date in order for the fund to pay its suppliers and producers of goods. When the operations in Iraq and Afghanistan begin to slow down and payments associated with the delivery of replacement stocks and repair of equipment are made, the AWCF cash balance should return to a level closer to our corpus requirement.

Total Revenue

Total revenue is an indicator of the volume of work completed by the AWCF activity groups. The total projected revenue for FY 2004 was $13.2 billion. Actual revenue was $14.1 billion, 7 percent greater than projected. This was primarily due to operations in support of the war on terrorism.

Table 16 displays total corporate revenue by customer. The largest customer for the AWCF is OMA, which accounted for revenues of $10.3 billion.

Table 17 displays total revenue and appropriation by activity group. SMA is the largest, accounting for over $10.5 billion in revenue, or 74 percent of all AWCF revenue. In addition to the revenue shown in Table 16 and Table 17, the AWCF received $219.3 million in FY 2004 in direct appropriations.

Personnel Resources

To achieve maximum efficiency of performance, the AWCF activity groups need to achieve the optimum configuration of skilled workforce appropriate to the workload. Skill mismatches sometimes occur as a result of deviations between planned and actual workload. They also can be caused by workforce reductions realized through voluntary separation and hiring freezes. Such mismatches can lead to unplanned operating losses.

As Figure 10 shows, the FY 2004 actual full-time equivalents and military end strength were below plan, resulting in a negative variance.

Table 16. Total Corporate Revenues by Customer ($ millions)

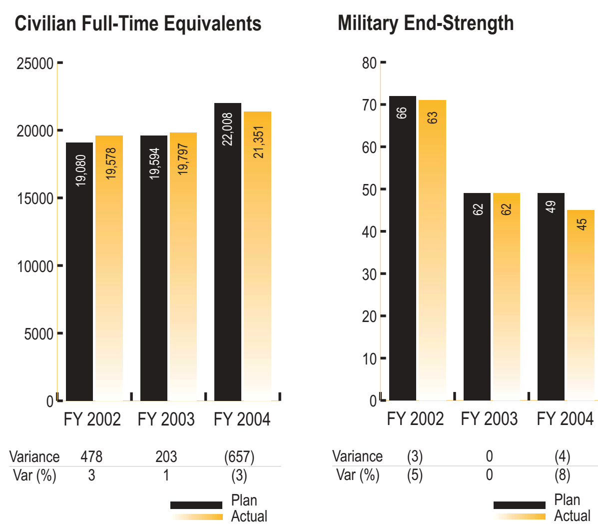
Customer	FY 2002	FY 2003	FY 2004
Operation and Maintenance, Army	$5,336.9	$8,358.3	$10,297.7
Army Procurement	627.2	680.0	493.7
AWCF	969.9	1,570.4	1,441.8
Other Army	174.6	224.0	337.0
Other Services	460.2	641.2	825.7
Other DoD	127.8	351.9	284.0
Foreign Military Sales	201.9	315.4	318.0
Non-DoD	228.7	40.8	87.5
Total Revenue	**$8,217.2**	**$12,182.0**	**$14,085.4**

Table 17. Total Revenue and Appropriation by Activity Group ($ millions)

Appropriation	FY 2002	FY 2003	FY 2004
Supply Management, Army	$6,001.4	$9,545.7	$10,620.6
Depot Maintenance	1,668.4	2,119.4	2,713.4
Ordnance	669.8	765.9	970.7
Information Services[1]	104.9	96.7	0.0
Total Revenue and Appropriation	**$8,445.5**	**$12,527.7**	**$14,304.7**

[1] Information Services was decapitalized in FY 2003

Figure 10. Corporate Personnel Indicators



Supply Management, Army

Program Scope

Customer Revenue (Program Size)

SMA revenue from customer sales in FY 2004 was $10.5 billion. This exceeded plan, with the increased revenue a direct result of unforeseen operations conducted in support of the war on terrorism. In addition to the revenue shown in Table 18, SMA received direct appropriations of $163.6 million in FY 2002, $189 million in FY 2003 and $105.4 million in FY 2004.

Personnel

As Figure 11 shows, the FY 2004 actual full-time equivalents varied less than 1 percent from plan, with no variation in military end-strength.

Performance Measures

Financial Performance

The financial performance of the SMA activity group is evaluated on a variety of fiscal measures. The primary measure, unit cost, is used as a managerial control and relates resources consumed to outputs produced. The aim of the unit cost is to associate total cost to the work or output. Other measures include total gross sales; revenue; cost; net operating results; capital investment; cash collections, disbursements and outlays; and stock availability and stock turn.

Wholesale Unit Costs. The wholesale division sells principally to Federal Government customers and, through the Foreign Military Sales Program, to foreign governments. Wholesale costs include the costs of logistics operations and of materiel obligations for repair or procurement, and credit issued to customers for materiel returns. Unit cost is measured by dividing these costs by gross wholesale sales.

In FY 2004, the wholesale division achieved a unit cost of $1.08. The initial unit cost goal (UCG) of $0.92 was revised during the fiscal year to allow the execution of immediate requirements for Operation Iraqi Freedom and the GWOT. The revision was based on both higher than expected sales and high hardware obligations also attributable to Operation Iraqi Freedom and the GWOT.

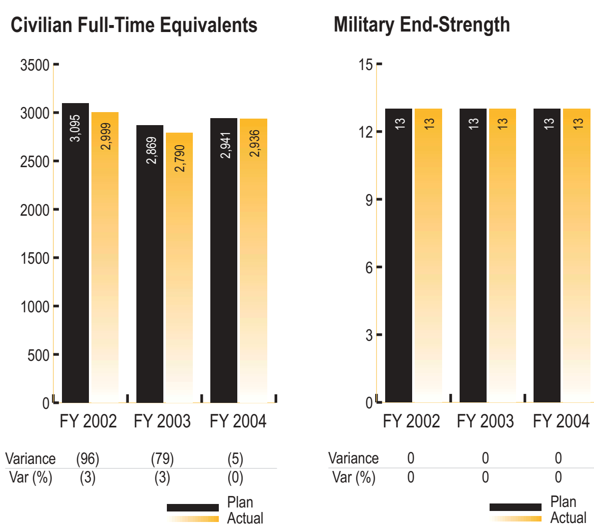
NAMI/Retail Unit Costs. Implementation of the Single Stock Fund (SSF) has altered the mission of the retail division. Prior to SSF, the retail divisions sold to authorized customers within their local geographical area. The retail divisions bought and sold both Army Managed Items (AMI) and non-Army Managed Items (NAMI) at the catalog price of the source of supply. Under SSF, the retail division consists only of NAMI.

In FY 2004, gross material costs were greater than planned, producing a unit cost of $1.03 that was

Table 18. Total SMA Revenue by Customer ($ millions)

Appropriation	FY 2002	FY 2003	FY 2004
Operation and Maintenance, Army	$4,473.6	$7,379.8	$8,785.4
Army Procurement	208.4	374.8	161.5
AWCF	405.2	468.5	434.5
Other Army	121.7	187.4	209.3
Other Services	366.5	562.1	589.5
Other DoD	58.6	93.6	22.3
Foreign Military Sales	114.0	281.1	271.2
Non-DoD	89.4	9.4	41.5
Total Revenue	**$5,837.4**	**$9,356.7**	**$10,515.2**

Figure 11. SMA Personnel Indicators



above the UCG of $0.95. Gross material costs were greater than planned due to increased inventory requirements in support of Operation Iraqi Freedom and the GWOT.

Gross Sales. Attaining projected sales levels is key to achieving goals in inventory management and operations management, as well as for recouping operations costs. Figure 12 shows the FY 2004 results.

Financial Operation Measures. Budgetary guidelines require the activity group to recover its operating costs and fees while achieving zero accumulated operating results at the end of the budget period. To achieve this goal, AWCF activities set stabilized rates eight or more months prior to the beginning of each fiscal year. These rates use forecasting methods to determine the potential workload and the cost of meeting workload requirements. This projection is then used to set a standard price for AWCF goods and services. Since revenue is defined as gross sales at standard price, revenue, cost, and net operating results are the logical financial measures of AWCF operations. In FY 2004, the rates were set to achieve a net operating result (NOR) of $45.5 million. The actual NOR, less extraordinary items, was a gain of $134 million. Results of operations, computed according to budget guidance, are presented in Table 19.

Results of operations, when computed according to financial accounting standards, can vary with inventory valuations due to the timing of cost recognition, transfer fees, and the inclusion of nonrecoverables such as planned inventory reductions.

Capital Investment. The SMA activity group's capital investment program as shown in Table 20, is focused primarily on the development of computer software to assist managerial decisionmaking, to enable the sharing of databases, and to support the development of more efficient business practices.

FY 2004 Capital Investment Program (CIP) projects include the purchase of the following:

Terminal Servers ($1.2 million). Terminal servers are required to enhance productivity throughout the AMC community by connecting stand-alone desktop computers to centralized servers. The project's main focus is to decrease maintenance costs associated with the Procurement Automated Data Distribution System.

Figure 12. SMA Gross Sales

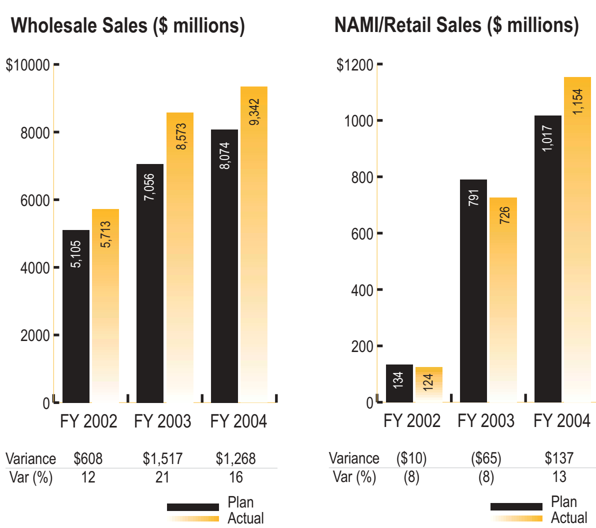


Table 20. Capital Budget Obligations for SMA ($ millions)

Category	FY 2002	FY 2003	FY 2004
Equipment	$0.0	$0.0	$0.0
ADPE and Telecom	0.0	0.0	1.2
Software	61.2	45.7	31.3
Total	**$61.2**	**$45.7**	**$32.5**

Table 19. Financial Operation Measures for SMA ($ millions)

	FY 2002			FY 2003			FY 2004		
	Plan	Actual	Variance (%)	Plan	Actual	Variance (%)	Plan	Actual	Variance (%)
Revenue	$5,239	$5,837	11	$5,595	$9,358	67	$9,097	$10,515	31
Cost of Goods Sold	5,645	6,192	10	4,496	8,450	87	9,052	10,381	30
Net Operating Results	(242)	(355)	(47)	239	908	280	45	134	197
Accumulated Operating Results	($38)	$198	(2,366)	$11	$29	164	$99	$29	(71)

Logistics Modernization Program (LMP) ($28 million). The goal of LMP is to re-engineer existing logistics processes to provide flexibility in support of CONUS-based power projection scenarios. It leverages modern information technology enablers to provide real-time visibility of the entire logistics supply chain and thereby support the transformation of military logistics.

Common Operating Environment (COE) ($1.6 million). COE provides Windows-based common technology architecture for the various wholesale logistics processes, enabling users of logistics systems to perform all business functions from a single workstation. It will also interface with LMP.

Single Stock Fund (SSF) ($0.5 million). The SSF concept integrates retail and wholesale inventory, management, and financial accounting functions to deliver business process improvements and improve the efficiency of inventory management. This vertical stock fund for Army-managed items will eliminate duplication in logistical and financial processing and provide greater visibility of assets.

Cash Management

The Army manages AWCF cash at the corporate level. The performance of individual activity groups is measured against planned collections, disbursements, and outlays rather than against independent cash balances.

FY 2004 collections were greater than projected, as shown in Figure 13, because of the increase in customer sales associated with Operation Iraqi Freedom and the GWOT.

Program Performance

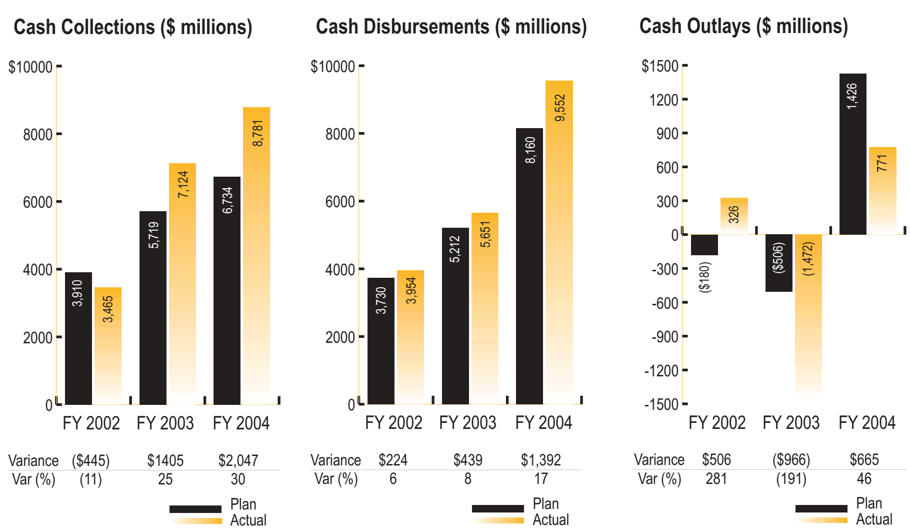
Supply Management uses the following program performance measure:

Stock Availability: Stock availability measures the percentage of SMA requisitions for stocked items completely filled within Uniform Materiel Movement and Issue Priority System (UMMIPS) timeframes. DoD and the Army have set a target of 85 percent stock availability. High demands continued in FY 2004 as shown in Table 21. Ongoing contingency operations and the level of OPTEMPO in support of Operation Iraqi Freedom and the GWOT continue to impact stock availability as Item Managers focus on high-priority demands for deployed forces. Adverse environmental impacts and long supply pipelines continued to draw down strategic assets faster than we could replace them.

Table 21. SMA Stock Availability (percentage)

	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter
FY 2002	85	86	87	86
FY 2003	85	80	75	70
FY 2004	73	69	74	76

Figure 13. SMA Cash Management



Depot Maintenance

Program Scope

Customer Revenue (Program Size)

Customer requirements govern the size and type of the Depot Maintenance workload. The revenue from customer sales in FY 2004 was $2.7 billion. Table 22 displays customer revenue for the past three fiscal years.

Total revenue increased by $580 million, or 27.4 percent, between FY 2003 and FY 2004. This was despite a rate increase of only 8.3 percent. Increased revenue was primarily attributable to heightened global commitments and operating tempo. In addition to the revenue shown in Table 22, Depot Maintenance received direct appropriations of $2.3 million in FY 2002, $5.8 million in FY 2003, and $19.7 million in FY 2004.

Personnel

A key objective of the Army is to have the correct number of appropriately skilled people in the right places to meet the demands of workload.

In FY 2004, depots received $2.6 billion in new orders, which was slightly 2.6 percent less than forecasted. The depots expanded their workforce, employed contract support, and used high levels of overtime in an effort to meet customer demands. Though it is estimated that the depots did not exceed their full-time equivalents (see Figure 14), they did exceed their planned overtime by 750,000 hours, or 75 percent.

Performance Measures

Financial Performance

There are five fiscal performance measures for Depot Maintenance: cost per direct labor hour, financial operating measures, customer revenue rate, capital investment, and cash management.

Cost per Direct Labor Hour. The cost per direct labor hour (DLH) is computed by taking the sum of all labor and non-labor expenses (direct, indirect, and general and administrative (G&A)), plus the change in work in process, and dividing that sum by the total number of DLHs worked during the fiscal year. The FY 2004 Depot Maintenance DLH is shown in Table 23.

Table 24 breaks down DLH costs into their component parts. Direct costs include civilian labor, materiel, supplies, equipment, and other costs that are directly related to a funded order (travel, training, and purchased services). The indirect/G&A elements comprise all costs not directly related to an order

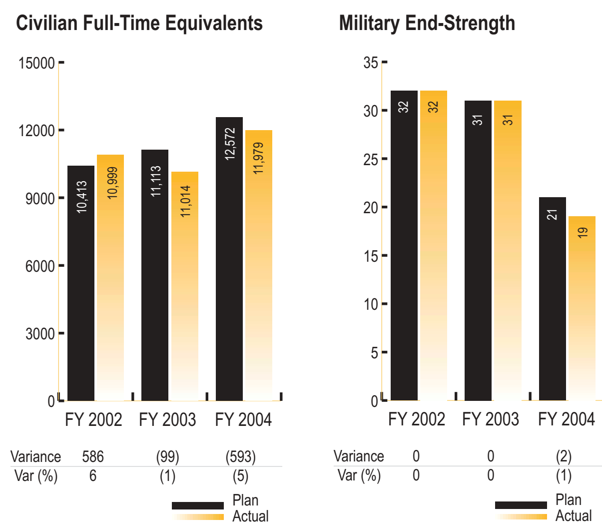
Table 22. Total Depot Maintenance Revenue by Customer ($ millions)

Appropriation	FY 2002	FY 2003	FY 2004
Operations and Maintenance, Army	$627.0	$675.4	$1,080.0
Army Procurement	253.3	131.3	141.2
AWCF	488.9	999.3	900.6
Other Army	30.1	10.8	98.9
Other Services	79.6	44.6	207.9
Other DoD	7.2	231.8	229
Foreign Military Sales	67.0	17.1	27.9
Non-DoD	113.0	3.3	7.3
Total Revenue	**$1,666.1**	**$2,113.6**	**$2,693.6**

Table 23. Depot Maintenance Cost per Direct Labor Hour

	FY 2002 Actual	FY 2003 Actual	FY 2004 Actual[1]
Cost per Direct Labor Hour	$152.36	$158.48	$153.03
Change from Prior Year (%)	12	4	(3)
Direct Labor Hours (000s)	11,592	12,769	16,335

Figure 14. Depot Maintenance Personnel Indicators



and that are recovered as overhead expenses. These include administrative personnel costs, base support costs, support personnel costs, and facility repair and maintenance costs.

Financial Operating Measures. Under the full-cost recovery concept, stabilized rates are set such that they should cover all costs and produce a zero accumulated operating result (AOR) at the end of the budget year. During execution, the activity group may experience either a positive or negative net operating result. The gain or loss shown in the NOR is added to the AOR from past years. Stabilized rates are included in the President's Budget, published approximately eight months in advance of the year of execution. The rates are stabilized so that customers' programs will not be affected during execution, even though the actual costs of the AWCF activity may be higher or lower than planned.

Deviations from the plan impact the activity group to the extent that an unplanned gain or loss must be included in the following year's rates to bring the AOR to zero. Any change in rates may in turn result in an increase or decline in the customer's buying power.

Table 25 shows the operation measures for the past three fiscal years. FY 2004 revenue and costs were $2.7 billion and $2.5 billion, respectively. Typically, acceptable deviation from the plan is plus or minus 10 percent. In FY 2004, revenue and cost deviations from plan were (13.5) percent and (20.0) percent, respectively. Because depots experienced delays in receipt of carcasses (assets to repair) early in FY 2004, actuals were lower than planned for revenue and cost of goods sold.

Customer Revenue Rate. In Depot Maintenance, customer revenue rates are set per direct labor hour. These rates are stabilized so that the customer's buying power is protected in the year of execution. Table 26 shows the stabilized revenue rates per DLH.

Capital Investment. The Depot Maintenance activity group seeks to maintain and develop its capabilities through the acquisition of new equipment and the execution of minor construction projects. The capital budget provides for equipment acquisitions to replace obsolete and unserviceable equipment, to eliminate environmental hazards, and to decrease costs through improvements in

Table 24. Depot Maintenance Direct Labor Costs ($ millions)

Elements	FY 2002	FY 2003	FY 2004
Direct Labor	$418.4	$294.0	NA
Indirect Labor	293.5	222.1	NA
General and Administrative Labor	14.5	16.6	NA
Direct Materiel	635.9	774.4	NA
Indirect Materiel	71.3	58.4	NA
Indirect Other	299.8	658.1	NA
Total	**$1,733.4**	**$2,023.6**	**NA**

[1] *Data was not available at time of printing*

Table 26. Depot Maintenance Stabilized Rates

Direct Labor Rate	FY 2002	FY 2003	FY 2004
Customer Revenue Rate ($)	$124.57	$133.80	$144.91
Customer Rate Change (%)	3	7	8

Table 25. Financial Operation Measures for Depot Maintenance ($ millions)

	FY 2002		FY 2003		FY 2004	
	Plan	Actual	Plan	Actual	Plan	Actual
Total Revenue	$1,580.0	$1,668.4	$1,731.3	$2,119.4	$3,136.0	$2,713.4
Cost of Goods Sold	1,599.0	1,766.2	1,749.6	2,023.6	3,120.6	2,499.7
Operating Results	(19.0)	(97.8)	(18.3)	95.8	15.4	213.7
(less Cash Surcharge)	0.2	0.6	0.1	0.3	0.0	0.0
(less Extraordinary Items)	0.0	0.0	0.0	0.0	0.0	0.0
Net Operating Results	(19.2)	(98.4)	(18.4)	95.5	15.4	213.7
Beginning AOR	64.6	83.2	(45.8)	(39.0)	77.8	77.8
(less Prior Year Adjustment)	0	(23.8)	0.0	21.3	(74.7)	25.8
Beginning AOR Adjusted	64.6	59.4	(45.8)	(17.7)	3.1	103.6
AOR (NOR plus adjusted AOR)	$45.4	($39.0)	$(64.2.	$77.8	$18.5	$317.3

productivity. Table 27 represents the obligation authority of the capital budget.

FY 2004 Capital Investment Program (CIP) projects include purchase of the following:

Various Capital Equipment—Replacement (<$500K) ($6.2 million). This program seeks to replace depot equipment items costing less than $500,000 that have outlived their useful lives, become uneconomical to repair, or become unsafe to operate.

Various Capital Equipment—Productivity (<$500K) ($2.4 million). This program seeks to modernize equipment costing less than $500,000 to improve depot productivity and efficiency and reduce operating costs.

Bridge Crane 30-ton Bldg 170 ($1.3 million). The purchase of two 30-ton Bridge Cranes will bring the 1955 10-ton crane system up to current Operational Safety and Health Administration standards and increase its lift capacity.

Generator Load Bank ($0.6 million). The purchase of the Generator Load Bank provides a safe compact unit that can test all generators and will have many fewer downtime problems.

XT-1410 Transmission Test Stand ($0.6 million). The purchase of the XT-1410 Transmission Test Stand provides a more reliable and accurate piece of equipment. Test time will be reduced by three hours per transmission.

CNC Vertical Machining Center ($1.2 million). The purchase of four CNC Vertical Machining Centers alleviates delays in production schedules.

Boring Mill ($0.9 million). The purchase of the Boring Mill enhances production capabilities, resulting in labor savings, maintenance cost saving, and reduced downtime.

Plastic Media blast System ($2.1 million). The purchase of the Plastic Media Blast System provides adequate space for removing paint from large airframes, fall protection, and integrated work platforms for safely reaching all areas of the airframe.

Aircraft Corrosion Control Equipment ($0.6 million). The purchase of the Aircraft Corrosion Control Equipment increases production throughput and decreases aircraft travel time by including all preparation and painting processes in one facility.

H-60 Alignment Fixture ($1.8 million). The purchase of the H-60 Alignment Fixture increases production capacity to meet a 200 percent increase in alignment workload.

Abrasive Waterjet Cutting Machine ($0.6 million). The purchase of the Abrasive Waterjet Cutting Machine relieves the existing machine that is being used 24 hours per day, 7 days per week.

Vertical Grinder ($0.6 million). The purchase of the Vertical Grinder helps meet the current schedule of 90 T-700 Engine compressor cases per month.

Apache Realignment Fixture ($2.3 million). The purchase of the Apache Realignment Fixture allows the depot to process an additional six aircraft per year, reducing backlog of aircraft.

Various Minor Construction (<$750 thousand) ($6.4 million). This program corrects various workload and production shortcomings and improves health, safety, environmental, and security conditions.

Army Workload and Performance System (AWPS) ($2.3 million). AWPS is a personal computer-based network software solution designed to integrate existing production and financial data into a single graphic program. This will assist the TACOM, CECOM, and AMCOM, in managing complex workload and employment strategies. This is a Congressional mandate.

Logistics Modernization Program ($6.4 million).

Table 27. Depot Maintenance Capital Budget ($ millions)

Category	FY 2002	FY 2003	FY 2004
Equipment	$7.1	$31.2	$29.3
Minor Construction	1.1	3.1	7.7
ADPE[1] and Telecom	0.0	0.0	0.0
Software	16.7	16.6	8.6
Total	$24.9	$50.9	$45.6

[1] *Automated Data Processing Equipment.*

LMP seeks to re-engineer existing logistics processes to provide flexibility in support of CONUS-based power projection scenarios to leverage modern information technology enablers to provide real-time visibility of the entire logistics supply chain, and thereby to support the revolution in military logistics.

Cash Management.
The Army manages AWCF cash at the corporate level. The performance of individual activity groups is measured against planned collections, disbursements, and outlays rather than in terms of cash balances. Depot Maintenance collections and disbursements in FY 2004 were $2.7 billion and $2.6 billion, respectively. Figure 15 graphically represents these results.

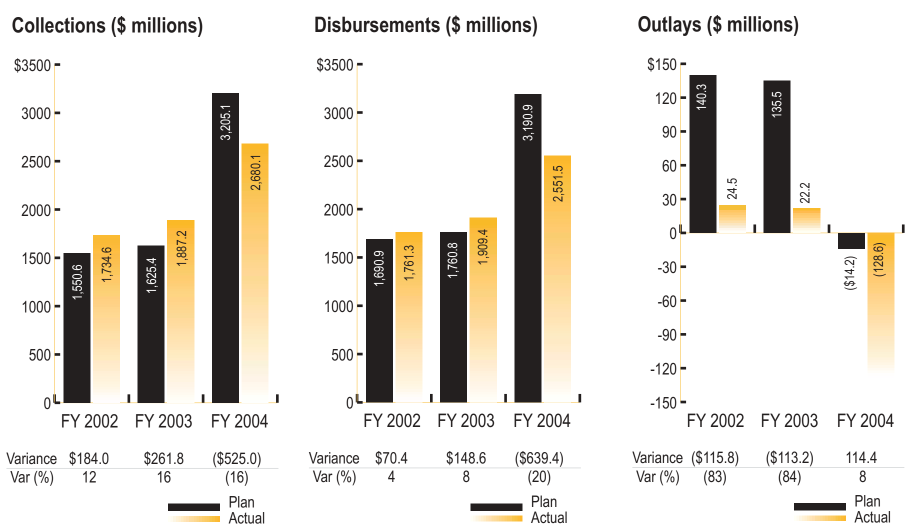
Both collections and disbursements were under the plan and reflect the revenue and expense positions of Depot Maintenance activity group.

Program Performance
The Army's industrial base is crucial to readiness in that it offers rapid response and the flexibility to perform a variety of missions anytime and anywhere in the world. Warfighting is about risk, and the industrial base has played a major role to help mitigate that risk. FY 2004 highlights include:

- Completed overhaul/repair to over 85,000 weapon systems, major items and components
- Provided 24/7 operations support to produce rubber for combat vehicle tracks
- Production of High-Mobility Multipurpose Wheeled Vehicle (HMMWV) Add-On Armor to protect against side attacks of explosives and small arms critical to operational effectiveness and Soldier safety
- Provided cross-service support on 154 Sidewinder missiles for the Air Force and 129 Maverick missiles for the Air Force/Navy and overhauled 50 M1A1 Abrams Tanks for the Marine Corps
- Deployed hundreds of civilians to Southwest Asia (SWA) and the Continental United States (CONUS) installations in support of forward repair capabilities

Lean/Six Sigma has played a major role in the success achieved by the industrial base in providing more reliable, responsive, accurate, and cost-effective support to the warfighter with the total workforce focusing on efforts to increase the value of products and services. All installations are actively involved in this initiative. Process improvements have resulted in millions of dollars of savings that will be passed back directly to customers in the form of reduced costs and/or more production output. For example, repair cycle time was significantly reduced for several go-to-war systems such as countermeasures aircraft survivability equipment used on most

Figure 15. Depot Maintenance Cash Management



helicopters, (a 31 percent reduction,) and radio terminal sets, (a 41 percent reduction). Aviation depot materiel requisitioning improved to such an extent that there is now a 30 percent increase in on-time delivery of parts to the UH-60 production line.

The Depot Maintenance activity group uses two program performance measures: production output and schedule conformance.

Production Output. Table 28 lists the quantity and customer price for five presentative end items for the last three fiscal years. The table highlights one specific item at each of the major repair depots that is receiving A1 (cyclic, normal overhaul, rebuild) work. The prices indicated are the unit prices by year for this type of work; price fluctuations are due to changes in materiel and labor costs, distribution of overhead costs, accumulated operating result (AOR) recovery, and the cash surcharge.

Schedule Conformance. This performance measure records the number of units completed on schedule as a percentage of the number of units scheduled. Units completed are defined as major end items plus repairables. FY 2004 results are displayed in Table 29.

Table 28. Depot Maintenance Production Output

	FY 2002		FY 2003		FY 2004			
Item (Installation)	Actual Quantity	Unit Price ($)	Actual Quantity	Unit Price ($)	Proposed Quantity	Actual Quantity	Deviation (%)	Unit Price ($)
Rear Module, M1A1 (ANAD)	334	68,613	347	$67,822	136	116	(15)	$65,677
Engine, Turbine, T700-GE (CCAD)	120	256,083	55	$264,751	130	118	(10)	$258,972
Patriot Launcher (LEAD)	28	440,615	40	$699,575	40	40	(0)	$653,725
Wheel, Solid Rubber (RRAD)**	2,800	249	8,945	$208	8,975	6,909	(23)	$214
Visual Display Unit, AH64 (TYAD)	60	8,263	49	$8,438	60	50	(17)	$8,755

*** The quantities and unit prices reflected for RRAD are for 26x6 roadwheels only.*

M1 Tank Track

Ordnance

Program Scope

Customer Revenue (Program Size)

Customer requirements dictate the size of the Ordnance workload. Table 30 displays customer revenue for the past three fiscal years.

Revenue from customer orders in FY 2004 was $876.6 million, an increase of $164.9 million, or 23.2 percent. This increase is due to increased orders as a direct result of the GWOT, coupled with a slight rate increase (1.4 percent) from FY 2003. In addition to the revenue shown in Table 30, the Ordnance activity group received $94.2 million in direct appropriations during FY 2004, $54.2 million in FY 2003, and $46.1 million in FY 2002.

The increase in revenue is due to increased shipments in support of overseas military operations, troop support/force protection, and receipt of unplanned orders and miscellaneous spares.

Personnel

A key objective of the Army is to have the correct number of appropriately skilled people in the right places to meet workload requirements. As workload has increased, staffing levels have also been increased to accomodate operational requirements. Figure 16 shows the FY 2004 staffing levels.

Performance Measures

Financial Performance

There are four financial performance measures for Ordnance. These are cost per direct labor hour, customer revenue rate, capital investment, and cash management.

Financial Operation Measures. Under the full-cost recovery concept, stabilized rates are set to cover all costs and produce a zero AOR at the end of the budget year. During execution, the activity group may experience either a positive or negative net operating result. The gain or loss shown in the NOR is added to the AOR from prior years. Stabilized rates are included in the President's Budget, published approximately eight months in advance

Table 29. Depot Maintenance Schedule Conformance (percentage)

	FY 2002	FY 2003	FY 2004
Plan	90%	96%	96%
Actual	94%	95%	95%
Variance (percentage)	4	(1)	(1)

Figure 16. Ordnance Personnel Indicators

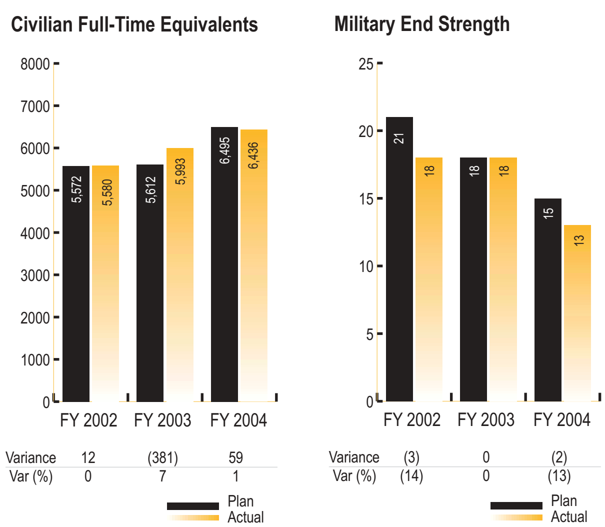


Table 30. Total Ordnance Revenue by Customer ($ millions)

Appropriation	FY 2002	FY 2003	FY 2004
Operation and Maintenance, Army	$236.3	$303.1	$431.5
Procurement, Army	165.5	173.9	191.0
AWCF	75.8	102.6	106.7
Other Army	22.8	25.8	28.8
Other Services	14.1	34.5	28.3
Other DoD	62.0	26.5	32.7
Foreign Military Sales	20.9	17.2	18.9
Non-DoD	26.3	28.1	38.7
Total Revenue	**$623.7**	**$ 711.7**	**$876.6**

of the year of execution. The rates are stabilized so that customers' programs will not be affected during execution, even though the actual costs of the AWCF activity may be higher or lower than planned.

Deviations from the plan impact the activity group to the extent that an unplanned gain or loss must be included in the following year's rates to bring the AOR to zero. Any change in rates may in turn result in an increase or decline in the customer's buying power.

Table 31 shows the operation measures for Ordnance for the past three fiscal years. FY 2004 total revenue and costs were $970.7 million and $966.9 million, within the acceptable deviation from plan of plus or minus 10 percent.

Cost per Direct Labor Hour. The cost per DLH rate is computed by dividing the sum of all labor and non-labor expenses (direct, indirect, and general and administrative plus the change in work in process by the total number of productive DLHs worked in the fiscal year. The FY 2004 DLH is shown in Table 32.

Table 33 breaks down the overall costs for FY 2004. Direct costs are the costs of civilian labor, material, supplies, equipment, and other costs that are directly related to a funded order. Indirect costs are those not directly related to an order, such as administrative personnel costs, base support costs, support personnel costs, and facility repair and maintenance costs.

Table 31. Ordnance Financial Operation Measures ($ millions)

	FY 2002		FY 2003		FY 2004	
	Plan	Actual	Plan	Actual	Plan	Actual
Total Revenue	$663.7	$669.2	$609.0	$765.8	$951.9	$970.7
Cost of Goods Sold	680.5	696.1	608.6	797.2	987.0	966.9
Operating Results	(46.8)	(26.3)	0.4	(31.4)	(35.1)	3.8
(less Cash Surcharge)	1.8	1.9	0.3	0.4	0.5	0.6
(less Extraordinary Items)	0.0	0.0	0.0	0.0	0.0	0.0
Net Operating Results	(48.6)	(28.2)	0.1	(31.8)	(35.6)	3.2
Beginning AOR	66.7	51.6	181.5	181.6	136.1	136.1
(less prior year adjustment)	0.0	158.2	0.0	(13.7)	0.0	(1.4)
Beginning AOR (adjusted)	66.7	209.8	181.5	167.9	136.1	134.7
AOR (NOR plus adjusted AOR)	$18.1	$181.6	$181.6	$136.1	$100.5	$137.9

Table 32. Ordnance Cost per Direct Labor Hour

	FY 2002	FY 2003	FY 2004
Cost per Direct Labor Hour ($)	$155.69	$137.85	$146.26
Change from Prior Year (%)	3	(11)	6
Direct Labor Hours (000s)	4,471	5,783	6,611

Table 33. Ordnance Direct Labor Cost ($ millions)

Elements	FY 2002	FY 2003	FY 2004[1]
Direct Labor	$168.8	$200.9	NA
Indirect Labor	139.5	136.5	NA
General and Administrative Labor	46.2	61.8	NA
Direct Materiel	82.4	99.3	NA
Indirect Materiel	25.5	27.3	NA
Other	231.9	268.0	NA
Total	**$694.3**	**$793.8**	**NA**

[1] *Data was not available at time of printing*

Customer Revenue Rate. The Ordnance activity group sets customer revenue rates per direct labor hour. These rates are stabilized so that the customer's buying power is protected in the year of execution. Table 34 shows the revenue rate per DLH, and indicates a 1 percent rate increase between FY 2003 and FY 2004.

Capital Investment Program. The Ordnance group seeks to maintain and develop its capabilities through the acquisition of equipment and the execution of minor construction projects. The capital budget provides for equipment acquisition to replace obsolete and unserviceable equipment, to eliminate environmental hazards, and to decrease repair costs by improving productivity. Table 35 represents the obligation authority of the capital budget.

FY 2004 Capital Investment Program (CIP) projects include purchase of the following:

Various Capital Equipment—Replacement ($6.1 million). This program funds the replacement of items of equipment costing less than $500,000 that have outlived their useful lives, are uneconomical to repair, or are unsafe to operate.

Bar and Chucking Lathe ($0.5 million). The acquisition of the Bar and Chucking Lathe used to machine tools/fixtures and ammunition components allows one machine to do the work of two with increased accuracy and output.

CNC Milling Machine ($0.7 million). The acquisition of the CNC Milling Machine used to manufacture critical parts for the 19/M198 Howitzers and the M182 Gun Mount for the M109 A6 Paladin increases machining time with less scrap and meets OSHA safety standards.

Automated M295 Line ($1.3 million). The acquisition of the Automated M295 Line used to produce the M295 individual Equipment Decontamination Kit (chemical agent removal) increases production and cuts both labor and repair costs by 50 percent.

Automated CDE Conveyor System ($1.2 million). The acquisition of the Automated CDE Conveyor System used for packaging and shipping of Chemical Defense Equipment (CDE) increases productivity, reduces the time required to ship CDE, and reduces injuries inherent to manual operations.

Premix Equipment ($0.9 million). The acquisition of the Premix Equipment used for mixing inert/non-explosive materials in the production of bombs increases production by 60 percent and reduces the unit price of the bombs produced.

Automated Starter Patch Fabrication System ($0.7 million). The acquisition of the Automated Starter Patch Fabrication System used for preparing terry cloth with starter mix slurry, and cut to shape for use in grenades, increases grenade throughput by 20 percent, improves quality of starter patches, and reduces operators from nine to five.

Rough Terrain Crane ($1.2 million). The acquisition of the Rough Terrain Crane—used for loading non-drivable tanks, Bradley Fighting Vehicles and M113 personnel carriers, etc., on to rail cars for storage—provides Sierra Army Depot the ability to perform this task at the most economical cost.

Minor Construction (<$750K) ($7.6 million). This program addresses and corrects various problems at Ordnance installations facilities that give rise to poor

Table 34. Ordnance Stabilized Rates

Direct Labor Hourly Rate	FY 2002	FY 2003	FY 2004
Customer Revenue Rate ($)	$94.59	$69.07	$70.5
Customer Rate Change (%)	(8)	(27)	1

Table 35. Capital Budget for Ordnance ($ millions)

Category	FY 2002	FY 2003	FY 2004
Equipment	$2.8	$9.6	$12.6
Minor Construction	1.3	1.4	7.6
ADPE and Telecom	1.9	0.0	2.6
Software	4.7	4.7	12.3
Total	**$10.7**	**$15.7**	**$35.1**

working conditions that in turn reduce productivity, lack energy conservation features, compromise security, fail to comply with fire and safety codes, or present health hazards.

Miscellaneous Automated Data Processing Equipment (<$500K) ($2.1 million). The ADPE program replaces old, obsolete, and irreparable equipment with state-of-the-art equipment to bring Ordnance sites up to Army standards and to improve communications with other Army sites. New technology will also improve security and reduce the threat of intrusion by unauthorized sources.

Network Enterprise Management System ($0.5 million). This centralized, fully integrated network management system allows computer technicians to diagnose problems and fix these problems without leaving their work site.

Army Workload and Performance System (AWPS) ($3.7 million). AWPS is a personal computer-based network software solution designed to integrate existing production and financial data into a single graphic program. It will enable production and resource managers to isolate scheduling and cost problems at the product level and to estimate the workforce needed to accomplish various levels of workload. This is a Congressional mandate.

Enterprise Resource Planning/Industrial Base Modernization WVA ($4.3 million). The Enterprise Resource Planning (ERP) system is part of LMP. It will develop an Industrial Base Modernization System that fully integrates the requirements performed by the numerous legacy systems with the standard ERP solution.

ERP/Industrial Base Modernization PBA ($4.3 million). The ERP system is part of the LMP. It will develop an Industrial Base Modernization System (IBM) that fully integrates the requirements performed by the numerous legacy systems with the standard ERP solution.

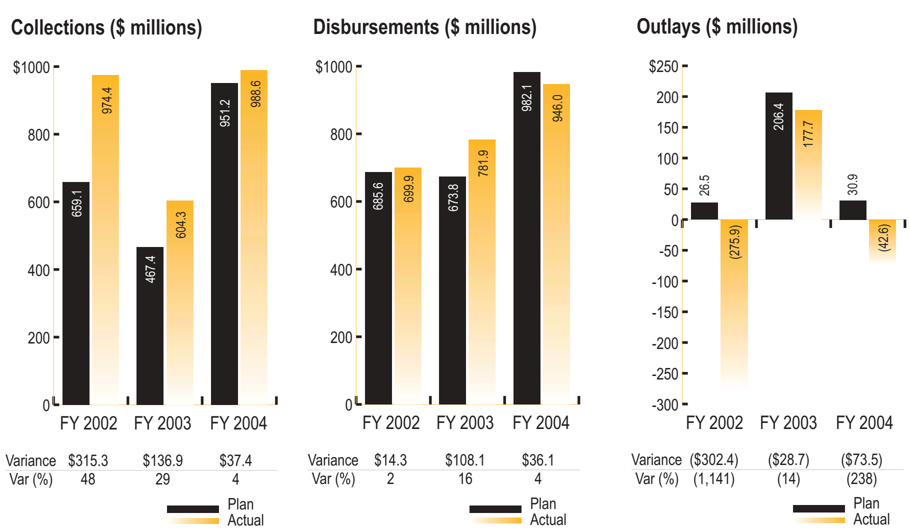
Cash Management

The Army manages AWCF cash at the corporate level. The performance of individual activity groups is measured against planned collections, disbursements, and outlays, not against cash balances. The FY 2004 plan for Ordnance projected a $30.9 million outlay on cash but the actual result outlay was only ($42.6) million. Collections were above plan for the year by 4 percent, as shown in Figure 17.

Program Performance

The Army's industrial base is crucial to readiness in that it offers rapid response and the flexibility to perform a variety of missions anytime and anywhere

Figure 17. Ordnance Cash Management



in the world. Warfighting is about risk, and the industrial base has played a major role to help mitigate that risk. FY 2004 highlights include:

- Manufacture of thousands of spare components for the 105mm/155mm cannons, and M137 cannons used by the Air Force
- Production of over 140,000 bombs
- Shipment of over 20,000 tons of ammunition to SWA and over 20,000 tons of ammunition to CONUS installations to support deployment and mobilization training
- Heavy involvement in retrograde and reset of ammunition from the SWA and U.S. Pacific Command theaters for all services.

Lean/Six Sigma has played a major role in the success achieved by the industrial base in providing more reliable, responsive, accurate, and cost-effective support to the warfighter with the total workforce focusing on efforts to increase the value of the products and services. All installations are actively involved in this initiative. Process improvements have resulted in millions of dollars of savings that will be passed back directly to customers in the form of reduced costs and/or more production output. For example, elimination of the potential for creating five critical defects in the M67 Hand Grenade process resulted in no production stoppages due to these defects. Lean events conducted on the illuminating candle production line resulted in a 12 percent reduction in manpower devoted to that operation, a 15 percent increase in the production rate, and a 50 percent reduction in delivery schedules. Another lean initiative looked at packing stations and ammunition shipping and receiving processes, all of which resulted in increased productivity. Analysis of a bomb line resulted in redeployment of 31 employees and reduced flow time by 64 percent in the production acceptance process.

The Ordnance activity group uses two program performance measures: schedule conformance and ammunition short tons.

Schedule Conformance. This performance measure shows the number of units completed on schedule as a percentage of the number of units scheduled. Units completed are defined as major end items plus repairable items. FY 2004 results are shown in Table 36.

Ammunition Short Tons. This measures the amount of short tons of ordnance received, issued, or demilitarized. (A short ton is 2,000 pounds of ammunition.) Based on standards at the installations, this figure has a direct correlation to personnel, funding, and rates. Table 37 displays the FY 2004 ammunition short tons measures.

Table 36. Schedule Conformance

	FY 2002	FY 2003	FY 2004
Plan	286.3	96	96
Actual	297.6	96	96
Variance (percentage)	4	0	0

Table 37. Ammunition Short Tons

	FY 2002	FY 2003	FY 2004		
	Actual	Actual	Plan	Actual	Variance (%)
Receipts	131,700	162,395	143,965	257,744	179%
Issues	165,800	202,655	158,697	198,661	125%
Demilitarized	27,759	19,780	14,705	19,806	135%

Analysis of Financial Statements

Throughout FY 2004, the AWCF continued to improve upon the myriad processes linked to producing auditable financial statements in compliance with the Chief Financial Officers Act of 1990.

The financial statements were compiled in accordance with guidance issued by the Office of Management and Budget and supplementary guidance provided by DoD. The IG DoD was unable to audit the AWCF financial statements due to the lack of Army management system adherence to Federal financial management systems requirements, generally accepted accounting principles, and the U.S. Government Standard General Ledger at the transaction level. As a result, the IG DoD did not express an opinion on the Army Working Capital Fund Balance Sheet, Statement of Net Cost, Statement of Changes in Net Position, Statement of Budgetary Resources, and Statement of Financing. In his letter to the Chief Financial Officer, the IG DoD identified eight internal control weaknesses. Army management has initiated actions to correct these weaknesses through the Army CFO Strategic Plan.

The financial statements for the AWCF are presented in a comparative format, providing financial information for FY 2003 and FY 2004.

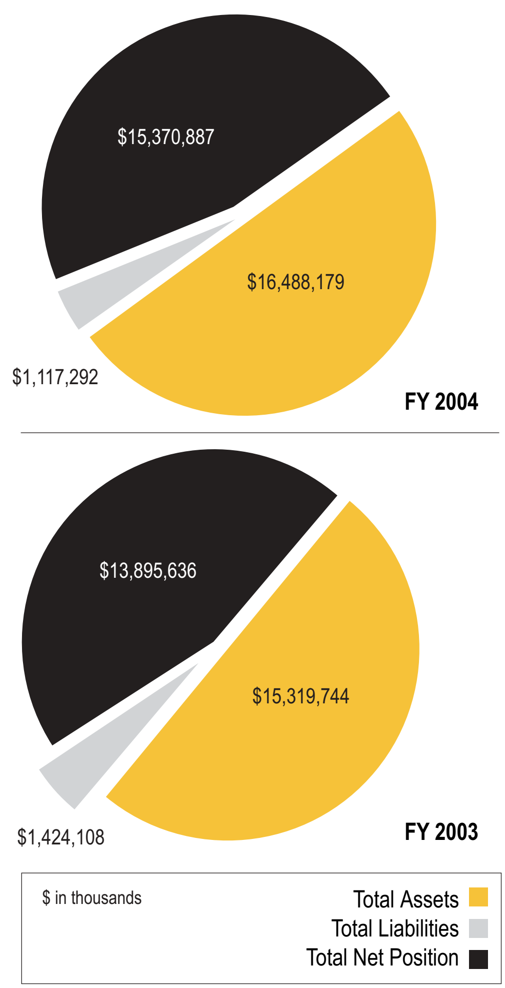
With that in mind, the following are the financial highlights of each statement. These highlights focus on significant balances or conditions to help clarify the AWCF's operations. Additional explanatory information may also be found in the notes that accompany these statements.

Balance Sheet

This statement presents the assets, liabilities, and net position of the AWCF as of 30 September 2003 and 2004. As shown in Figure 18, the Army Working Capital assets amounted to $16.5 billion at FY 2004 year-end, nearly an 8 percent increase from the previous year. Of the total assets, over 84 percent of the dollar value resides in the inventory and related property account. Relative to its total assets, the AWCF liabilities are quite low, amounting to $1.1 billion, a decrease of over $306 million, or 22 percent. This decrease is mainly due to a reduction in the accounts payable line item, as a result of paying the Defense Logistics Agency (DLA) for the FY 2003 over-ocean transportation costs.

The third major component of the balance sheet is net position. In aggregate, the various elements of the net position section on the balance sheet are also referred to as "equity." Equity is the residual interest in the assets of the entity that remains after deducting its liabilities. For FY 2004, the AWCF net position amounted to $15.4 billion, representing almost a $1.5 billion, or 11 percent, increase from FY 2003.

Figure 18. Balance Sheet Results



Statement of Net Cost

This statement presents the annual cost of operating the various AWCF activity groups. To the extent a program generates revenues, these amounts offset gross costs to arrive at the net cost of operations. For FY 2004, program costs amounted to $11 billion, representing a 10 percent increase from the previous year. Additionally, program revenues increased 28 percent from FY 2003, climbing to $13.4 billion. Overall for FY 2004, the AWCF achieved a 361 percent decrease in the net cost of operations, increasing net revenue to $2.4 billion—a $1.9 billion increase from the previous year.

Statement of Changes in Net Position

This statement presents those accounting items that caused the net position section of the balance sheet to change from the beginning to the end of the reporting period. The AWCF saw an increase of $1.5 billion, or 11 percent, in the cumulative result of operations. The Net Position at year-end was $15.4 billion, a 11 percent increase from the previous year.

Statement of Budgetary Resources

This statement provides information on the AWCF's budgetary financing accounts and the status or remaining balances of those accounts at year-end. This includes information on obligation and outlays or actual cash disbursements for the year.

Statement of Financing

This is a reconciling statement that tracks the relationship between the proprietary accounts and the budgetary accounts of the AWCF. The Statement of Financing provides data on the total resources provided to the AWCF during the fiscal year and how those resources were used.

The first section of the statement, *Resources Used to Finance Activities*, shows a total of $1.6 billion. This is the amount for which the AWCF may have a future liability that would eventually require cash payments.

The second section, *Resources Used to Finance Items not Part of the Net Costs of Operations*, identifies and adjusts budgetary transactions recorded by the AWCF for changes in the amount of goods, services, and benefits ordered but not received, the costs capitalized on the balance sheet, and financing sources that fund costs of prior periods. For FY 2004, the AWCF had a negative $8.9 billion in adjustments.

The first two sections are netted together to yield the total resources used to finance the net cost of operations. For FY 2004, total resources used to finance net costs increased 2,524 percent over the previous year and amounted to approximately $7.3 billion. The largest factor in this increase is the change in the Resources that Finance the Acquisition of Assets, which increased $5.9 billion, or 1,817 percent, from FY 2003 to FY 2004. An accounting procedure change to report capitalized purchases more accurately caused this increase. Memorandum accounts were added to capture the capitalized costs during the year.

Finally, the third section, *Components of the Net Cost of Operations that will not Require or Generate Resources in the Current Period*, is used to adjust the total resources used to finance the net cost of operations (the net amount of the first and second sections) in order to determine the net cost of operations. Thus, sections 1 and 2 are reconciled with section 3 to yield a net cost of operations of $2.4 billion. This amount ties back to the Statement of Net Cost.

Management Integrity

A discussion of the Army management control weaknesses that were identified during FY 2004, and those weaknesses reported during FY 2003 that the Army expected to close during FY 2004, can be found on page 20 of the Army General Fund Section.

Future Effects of Existing Conditions

Logistics Transformation

As part of Army Transformation, several financial reform initiatives have been recommended by the Logistics Transformation Task Force that may result in a change to the pricing and recording of products and/or services sold by the AWCF. The proposed changes will be reviewed by the task force and, if approved, will be implemented during FY 2005–FY 2007. The goal of these reform initiatives is to promote cost visibility while streamlining price development. If this is achieved as required, buyer/seller relationships will benefit.

Facilities Recapitalization

The Army has identified a need for a facilities framework capable of properly supporting its future worldwide missions. This will require programs and budgets that ensure the day-to-day readiness of modern facilities relevant to future operations and services. The Army will use standard tools and metrics to determine the appropriate investment levels for this facilities recapitalization.

The recapitalization rate metric is one element of a larger paradigm that has been under development in DoD since 1999. This paradigm is composed of restructured programs and new performance metrics for facilities sustainment, restoration, and modernization (S/RM). The new S/RM paradigm is expected to solve several longstanding problems that have challenged the Army in its determination of facilities funding requirements. It supports both the Government Performance and Results Act and the Chief Financial Officers Act.

The Defense Planning Guidance for FY 2004–FY 2009 provides a revised investment strategy based on S/RM principles. However, the challenge of how to implement the strategy remains. Successful implementation will require a major change to existing practices and a long-term commitment to resolve the problem.

Using the S/RM-based strategy, the Army plans to first forecast its required inventory and then:

- Fully sustain its assets and stop the loss of service life
- Restore by 2010, where appropriate and affordable, C-2 readiness to facilities rated C-3 or C-4 in the near-term, buying back lost service life
- Modernize for the future, establishing by 2007 a recapitalization investment stream tied to average expected service life (67 years).

For mainstream recapitalization programs—and for recapitalization typically funded by traditional military construction, operations, and maintenance, and working capital fund resources—the recapitalization rate metric is ready and usable for the FY 2004–FY 2009 program and budget cycle. Additional research and analysis are required before the metric can be successfully applied to selected specialty areas such as family housing programs, foreign- or internationally funded programs, and non-appropriated fund programs

Advancing the President's Management Agenda

The President's Management Agenda has great relevance in the logistics arena. By improving their management efficiency, all AWCF activities should be able to lower the rates they charge to customers.

Strategic Management of Human Capital

A key element of successful personnel management within the AWCF is providing people with information and trusting them to use it to the benefit of the organization as a whole. To that end, the AWCF has taken the following steps to empower its Soldiers and civilian employees with greater knowledge.

Workforce Revitalization

The AWCF has a critical role in helping ensure the success of Army Transformation, but the ability of the AWCF workforce to perform its mission is in peril. The AWCF is afflicted by a growing number of retirement-driven shortages in vital areas, and after more than a decade of cutbacks is facing serious skill imbalances. The limited intake of new personnel furthermore means that employees now average more than 20 years of service; unless someone is in place to inherit their legacy, as each staff member leaves, knowledge and experience will be lost with them.

The Army Materiel Command is seeking to put in place a Workforce Revitalization Program that will institute hiring programs for apprentices, interns, and multidisciplinary fellows. Using a range of innovative recruiting techniques, AMC will assess the abilities of applicants and new employees and determine and address their development needs. The desired result is a viable and skilled workforce able to share the knowledge of experienced employees.

Improved Financial Performance

During FY 2004, the AWCF built upon a number of initiatives began in FY 2003 that will enable the AWCF to make better use of its funds. In addition, the AWCF is also pursuing other long-term initiatives aimed at putting more useful and more reliable financial information in the hands of managers, with the aim of enabling them to make more efficient use of resources.

Logistics Modernization Program

The Logistics Modernization Program, a key component of Army Transformation, will update our national-level logistics business practices and supporting information technology. It will provide integrated logistics management capabilities such as total asset visibility, a single source of data, better forecasting accuracy and real-time access to enterprise information. We also expect that LMP will measurably improve Army readiness. AMC completed initial implementation of the first phase in July 2003 as shown in Figure 19 on the following page. Deployment to 12 Working Capital Fund sites will be completed in FY 2006.

Expand Electronic Goverment

The President's Management Agenda asserts that, through electronic means, Government can both reduce costs and provide better service. The AWCF accordingly, is pursuing electronic initiatives aimed at providing better service to its Soldiers and civilian employees. An example of one such initiative is described below.

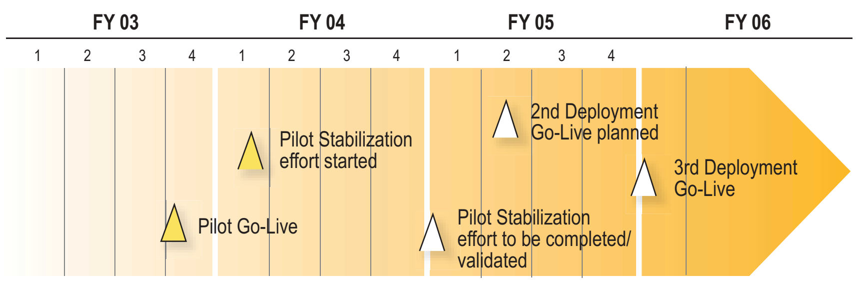
Logistics Enterprise Integration

The Army's Logistics Enterprise Integration involves integrating several modernizing initiatives, including LMP and the Global Combat Support System Army (GCSS Army) map, within the DoD Future Logistics Enterprise (FLE). The FLE (also commonly referred to as Business Enterprise Architecture (BEA)-Logistics, or "BEA-LOG") has six principal components: Total Lifecycle Systems Management (TLCSM), End-to-End Customer Support, Condition-Based Maintenance, Depot Partnering, Executive Agency, and Enterprise Integration. All services must ensure that their enterprise integration efforts and architectures map to the FLE/BEA-LOG, which in turn maps to the BEA. The desired outcome is that within DoD all services and the Defense Logistics Agency (DLA) will operate a single, integrated solution, the technical and functional architecture of which is focused on the warfighter.

The central objective of logistics enterprise integration is the development, through collaborative planning, knowledge management, and best business practices, of a fully integrated knowledge environment that builds, sustains, and generates warfighting capability. Logistics, financial, acquisition, and product data will be brought together in an environment that operates in a near seamless fashion from the soldier across the major Army commands, across the military services, across DoD, and across industry. Our business systems will capture and integrate the data flowing from automatic identification technology and embedded weapons system diagnostics, and will make these data available to both logisticians and system engineers. The timely creation of an environment for many participants that delivers vertical and horizontal visibility, that supports a robust predicative capability, and that meets the demands of the concept of warfighter operations in the future battlespace is essential to Army Transformation.

Figure 19. Logistics Modernization Program

Institutional Risk	Streamline Decision Processes, Financial Management Acquisition Excellence



Pilot
Communications-Electronics Command (CECOM)
HQ Army Materiel Command (AMC)
Tobyhanna Army Depot (TYAD)
Defense Finance & Accounting Service (DFAS)

2nd Deployment
Aviation & Missle Command (AMCOM)
Corpus Christi Army Depot (CCAD)
Letterkenny Army Depot (LEAD)

3rd Deployment
Tank-automotive & Armaments Command (TACOM)
Anniston Army Depot (ANAD)
Red River Army Depot (RRAD)
Army Field Support Command (AFSC)
Joint Munitions Command (JMC)

Description: AIR 13 - Log Modernization Program
Provide the Army with integrated logistics management capabilities such as total asset visibility, a single source or data, improved forecasting accuracy, and realtime access to enterprise information.

Parameter:
Green: On schedule, Yellow: 1 Quarter behind schedule, Red: 2 Quarters behind schedule

Metric: Milestones planned/achieved

Owner: AMC

LMP is in Pilot Stabilization Phase

Making Steady Progress in Correcting Items to Complete This Phase.

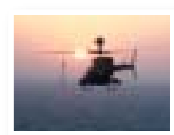
Overall LMP is Rated Yellow

- As of 30 July 2004, 584 of 722 items completed (81 percent through Pilot Stabilization).
- Pilot Stabilization/Financial Correction will be completed end of October

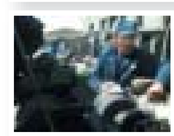
*As of July 2004.

Working Capital Fund Introduction Page Photos

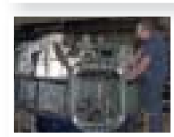
[Large Photo]
As the sun rises over Baghdad, 1st Lt. Matt Sun and Chief Warrant Officer Pete Horton conduct a mission in an OH-58D Kiowa Warrior helicopter. This photo appeared on www.army.mil. By CW3 Chris Wilson



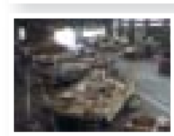
[Top Inset Photo]
Engine Repair



[Middle Inset Photo]
Helicopter Repair – Corpus Christ Army Depot, TX.



[Bottom Inset Photo]
Abrams Tank Repair shop – Anniston Army Depot, AL.



Army Working Capital Fund Principal Financial Statements, Notes, and Supplementary Information

Limitations

Limitations of the Financial Statements

The financial statements have been prepared to report the financial position and results of operations for 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 the formats prescribed by the 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.

To the extent possible, the financial statements have been prepared in accordance with federal accounting standards. At times, the Department is unable to implement all elements of the standards due to financial management systems limitations. The Department continues to implement system improvements to address these limitations. There are other instances when the Department's application of the accounting standards is different from the auditor's application of the standards. In those situations, the Department has reviewed the intent of the standard and applied it in a manner that management believes fulfills that intent.

The statements should be read with the realization that they are for a component of the United States Government, a sovereign entity. One implication of this is that the liabilities cannot be liquidated without legislation that provides resources to do so.

Limitations Concerning National Defense Property, Plant and Equipment

The Federal Accounting Standards Advisory Board (FASAB) revised the Statement of Federal Financial Accounting Standards No. 6 to require the capitalization and depreciation of military equipment (formerly National Defense Property, Plant and Equipment/ND PP&E) for fiscal years (FY) 2003 and beyond, and encouraged early implementation.

Department of Defense- Army Working Capital Fund

CONSOLIDATED BALANCE SHEET

As of September 30, 2004 and 2003 ($ in Thousands)

ASSETS (Note 2)	2004 Consolidated	2003 Consolidated
Intragovernmental:		
Fund Balance with Treasury (Note 3)		
Entity	$948,463	$1,548,546
Non-Entity Seized Iraqi Cash	0	0
Non-Entity-Other	0	0
Investments (Note 4)	0	0
Accounts Receivable (Note 5)	444,923	411,254
Other Assets (Note 6)	79	329
Total Intragovernmental Assets	$1,393,465	$1,960,129
Cash and Other Monetary Assets (Note 7)	$0	$0
Accounts Receivable (Note 5)	13,482	31,176
Loans Receivable (Note 8)	0	0
Inventory and Related Property (Note 9)	13,916,672	12,131,811
General Property, Plant and Equipment (Note 10)	899,438	926,751
Investments (Note 4)	0	0
Other Assets (Note 6)	265,122	269,877
TOTAL ASSETS	$16,488,179	$15,319,744
LIABILITIES (Note 11)		
Intragovernmental:		
Accounts Payable (Note 12)	$159,150	$435,586
Debt (Note 13)	0	0
Environmental Liabilities (Note 14)	0	0
Other Liabilities (Note 15 & Note 16)	67,660	94,499
Total Intragovernmental Liabilities	$226,810	$530,085
Accounts Payable (Note 12)	$372,054	$342,365
Military Retirement Benefits and Other Employment-Related Actuarial Liabilities (Note 17)	304,976	320,654
Environmental Liabilities (Note 14)	0	0
Loan Guarantee Liability (Note 8)	0	0
Other Liabilities (Note 15 and Note 16)	213,452	231,004
Debt Held by Public	0	0
TOTAL LIABILITIES	$1,117,292	$1,424,108
NET POSITION		
Unexpended Appropriations (Note 18)	$53	$11,960
Cumulative Results of Operations	15,370,834	13,883,676
TOTAL NET POSITION	$15,370,887	$13,895,636
TOTAL LIABILITIES AND NET POSITION	$16,488,179	$15,319,744

Department of Defense- Army Working Capital Fund

CONSOLIDATED STATEMENT OF NET COST

As of September 30, 2004 and 2003 ($ in Thousands)

	2004 Consolidated	2003 Consolidated
Program Costs		
Intragovernmental Gross Costs	$2,847,994	$2,651,517
(Less: Intragovernmental Earned Revenue)	(8,456,053)	(10,283,891)
Intragovernmental Net Costs	($5,608,059)	($7,632,374)
Gross Costs With the Public	8,161,299	7,334,031
(Less: Earned Revenue From the Public)	(4,951,052)	(222,087)
Net Costs With the Public	$3,210,247	$7,111,944
Total Net Cost	($2,397,812)	($520,430)
Cost Not Assigned to Programs	0	0
(Less: Earned Revenue Not Attributable to Programs)	0	0
Net Cost of Operations	($2,397,812)	($520,430)

Department of Defense- Army Working Capital Fund

CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION

As of September 30, 2004 and 2003 ($ in Thousands)

	2004 Consolidated	2003 Consolidated
CUMULATIVE RESULTS OF OPERATIONS		
Beginning Balances	$13,883,676	$11,913,102
Prior period adjustments (+/-)		
Prior Period Adjustments - Restated (+/-)	0	0
Beginning Balance, Restated	13,883,676	11,913,102
Prior Period Adjustments - Not Restated (+/-)	0	0
Beginning Balances, as adjusted	$13,883,676	$11,913,102
Budgetary Financing Sources:		
Appropriations received	0	0
Appropriations transferred-in/out (+/-)	0	0
Other adjustments (rescissions, etc) (+/-)	0	0
Appropriations used	231,207	267,083
Nonexchange revenue	0	0
Donations and forfeitures of cash and cash equivalents	0	0
Transfers-in/out without reimbursement (+/-)	(1,448,600)	0
Other budgetary financing sources (+/-)	175,918	(63,903)
Other Financing Sources:		
Donations and forfeitures of property	0	0
Transfers-in/out without reimbursement (+/-)	0	908,588
Imputed financing from costs absorbed by others	130,821	121,312
Other (+/-)	0	217,064
Total Financing Sources	($910,654)	$1,450,144
Net Cost of Operations (+/-)	(2,397,812)	(520,430)
Ending Balances	$15,370,834	$13,883,676
UNEXPENDED APPROPRIATIONS		
Beginning Balances	$11,960	$30,043
Prior period adjustments (+/-)		
Prior Period Adjustments - Restated (+/-)	0	0
Beginning Balance, Restated	11,960	30,043
Prior Period Adjustments - Not Restated (+/-)	0	0
Beginning Balances, as adjusted	$11,960	$30,043
Budgetary Financing Sources:		
Appropriations received	219,300	249,000
Appropriations transferred-in/out (+/-)	0	0
Other adjustments (rescissions, etc) (+/-)	0	0
Appropriations used	(231,207)	(267,083)
Nonexchange revenue	0	0
Donations and forfeitures of cash and cash equivalents	0	0
Transfers-in/out without reimbursement	0	0
Other budgetary financing sources (+/-)	0	0
Other Financing Sources:		
Donations and forfeitures of property	0	0
Transfers-in/out without reimbursement (+/-)	0	0
Imputed financing from costs absorbed by others	0	0
Other (+/-)	0	0
Total Financing Sources	($11,907)	($18,083)
Net Cost of Operations (+/-)	0	0
Ending Balances	$53	$11,960

Department of Defense- Army Working Capital Fund

COMBINED STATEMENT OF BUDGETARY RESOURCES

As of September 30, 2004 and 2003 ($ in Thousands)

	BUDGETARY RESOURCES		NON-BUDGETARY RESOURCES	
	2004 Combined	**2003 Combined**	**2004 Combined**	**2003 Combined**
BUDGETARY FINANCING ACCOUNTS				
Budget Authority:				
Appropriations received	$219,300	$249,000	$0	$0
Borrowing authority	0	0	0	0
Contract authority	2,106,368	67,627	0	0
Net transfers (+/-)	(1,448,600)	0	0	0
Other	0	0	0	0
Unobligated balance:				
Beginning of period	2,093,703	1,708,247	0	0
Net transfers, actual (+/-)	0	0	0	0
Anticipated Transfers Balances	0	0	0	0
Spending authority from offsetting collections:				
Earned	0	0	0	0
Collected	12,265,860	9,644,303	0	0
Receivable from Federal sources	(53,776)	236,175	0	0
Change in unfilled customer orders	0	0	0	0
Advance received	(17,246)	(179,239)	0	0
Without advance from Federal sources	(128,900)	2,351,152	0	0
Anticipated for the rest of year, without advances	0	0	0	0
Transfers from trust funds	0	0	0	0
Subtotal	$12,065,938	$12,052,391	$0	$0
Recoveries of prior year obligations	499,733	587,959	0	0
Temporarily not available pursuant to Public Law	0	0	0	0
Permanently not available	0	0	0	0
Total Budgetary Resources	$15,536,442	$14,665,224	$0	$0
STATUS OF BUDGETARY RESOURCES				
Obligations incurred:				
Direct	$0	$249,028	$0	$0
Reimbursable	14,006,202	12,322,493	0	0
Subtotal	$14,006,202	$12,571,521	$0	$0
Unobligated balance:				
Apportioned	1,530,241	2,093,704	0	0
Exempt from apportionment	0	0	0	0
Other available	(1)	(1)	0	0
Unobligated Balances Not Available	0	0	0	0
Total, Status of Budgetary Resources	$15,536,442	$14,665,224	$0	$0
Relationship of Obligations to Outlays:				
Obligated Balance, Net - beginning of period	$1,898,332	$918,667	$0	$0
Obligated Balance transferred, net (+/-)	0	0	0	0
Obligated Balance, Net - end of period:				
Accounts receivable	(462,602)	(516,379)	0	0
Unfilled customer order from Federal sources	(4,522,713)	(4,651,613)	0	0
Undelivered orders	8,334,654	6,085,073	0	0
Accounts payable	618,741	981,250	0	0
Outlays:				
Disbursements	11,619,397	8,416,571	0	0
Collections	(12,248,614)	(9,465,064)	0	0
Subtotal	($629,217)	($1,048,493)	$0	$0
Less: Offsetting receipts	0	0	0	0
Net Outlays	($629,217)	($1,048,493)	$0	$0

Department of Defense- Army Working Capital Fund

COMBINED STATEMENT OF FINANCING

As of September 30, 2004 and 2003 ($ in Thousands)

	2004 Combined	2003 Combined
Resources Used to Finance Activities:		
Budgetary Resources Obligated		
Obligations incurred	$14,006,202	$12,571,521
Less: Spending authority from offsetting collections and recoveries (-)	(12,565,671)	(12,640,348)
Obligations net of offsetting collections and recoveries	$1,440,531	($68,827)
Less: Offsetting receipts (-)	0	0
Net obligations	$1,440,531	($68,827)
Other Resources		
Donations and forfeitures of property	0	0
Transfers in/out without reimbursement (+/-)	0	908,589
Imputed financing from costs absorbed by others	130,821	121,312
Other (+/-)	0	217,064
Net other resources used to finance activities	130,821	1,246,965
Total resources used to finance activities	$1,571,352	$1,178,138
Resources Used to Finance Items not Part of the Net Cost of Operations		
Change in budgetary resources obligated for goods services and benefits ordered but not yet provided		
Undelivered Orders (-)	($2,497,681)	($3,301,433)
Unfilled Customer Orders	(146,147)	2,171,911
Resources that fund expenses recognized in prior periods	(23,337)	(2,765)
Budgetary offsetting collections and receipts that do not affect net cost of operations	0	0
Resources that finance the acquisition of assets	(6,214,549)	(324,219)
Other resources or adjustments to net obligated resources that do not affect net cost of operations		
Less: Trust or Special Fund Receipts Related to Exchange in the Entity's Budget (-	0	0
Other (+/-)	6,872	0
Total resources used to finance items not part of the net cost of operations	($8,874,842)	($1,456,506)
Total resources used to finance the net cost of operations	($7,303,490)	($278,368)
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		
Increase in annual leave liability	$1,376	$1,995
Increase in environmental and disposal liability	0	0
Upward/Downward reestimates of credit subsidy expense (+/-)	0	0
Increase in exchange revenue receivable from the the public (-	0	(6,079)
Other (+/-)	172	16,466
Total components of Net Cost of Operations that will require or generate resources in future periods	$1,548	$12,382
Components not Requiring or Generating Resources		
Depreciation and amortization	82,909	194,093
Revaluation of assets or liabilities (+/-)	257,468	(448,537)
Other (+/-)		
Trust Fund Exchange Revenue	0	0
Cost of Goods Sold	5,003,845	0
Operating Material & Supplies Used	0	0
Other	(440,092)	0
Total components of Net Cost of Operations that will not require or generate resources	$4,904,130	($254,444)
Total components of net cost of operations that will not require or generate resources in the current period	$4,905,678	($242,062)
Net Cost of Operations	($2,397,812)	($520,430)

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 Army Working Capital Fund (AWCF), 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 AWCF in accordance with the Department of Defense (DoD) Financial Management Regulation, Office of Management and Budget (OMB) Bulletin No. 01-09, Form and Content of Agency Financial Statements, and, to the extent possible, Federal Generally Accepted Accounting Principles (GAAP).

The accompanying financial statements account for all resources for which the AWCF is responsible. Under the above guidance, classified assets, programs, and operations have been excluded from the statement, or otherwise aggregated and reported, in such a manner that they are no longer classified. The AWCF financial statements are in addition to the financial reports also prepared by the AWCF pursuant to OMB directives that are used to monitor and control the AWCF's use of budgetary resources.

The AWCF is unable to fully implement all elements of Federal GAAP and OMB Bulletin No. 01-09 due to limitations of its financial and nonfinancial management processes and systems. The Army derives its reported values and information for major asset and liability categories largely from nonfinancial feeder systems, such as inventory and logistics systems. These systems were designed to support reporting requirements focusing on maintaining accountability over assets and reporting the status of federal appropriations rather than preparing financial statements in accordance with Federal GAAP. As a result, the AWCF cannot currently implement every aspect of Federal GAAP and OMB Bulletin No. 01-09. The AWCF continues to implement process and system improvements addressing the limitations of its financial and nonfinancial feeder systems. Further explanation of these financial statement elements is provided in the applicable note.

The accounting structure of federal agencies is designed to reflect both accrual and budgetary accounting transactions. Under the accrual method of accounting, revenues are recognized when earned, and expenses are recognized when incurred, without regard to receipt or payment of cash. The budgetary accounting principles, on the other hand, are designed to recognize the obligation of funds according to legal requirements, which in many cases is prior to the occurrence of an accrual-based transaction. The recognition of budgetary accounting transactions is essential for compliance with legal constraints and controls over the use of federal funds.

1.B. Mission of the Reporting Entity

The AWCF is part of the Defense Working Capital Fund, and is divided into three separate business areas: Supply Management, Depot Maintenance, and Ordnance. As of October 1, 2003, a fourth business area, Information Services, was closed out of the AWCF and now operates as a part of the Army General Fund. These separate business areas ensure delivery of critical items, such as petroleum products, repair parts, consumable supplies, depot maintenance services, munitions and weapons to support the deployment and projection of lethal force as and when required by the nation.

1.C. Appropriations and Funds

The Army's appropriations and funds are divided into the general, working capital (revolving funds), trust, special, and deposit funds. These appropriations and funds are used to fund and report how the resources have been used in the course of executing the Army's missions.

Working capital funds (revolving funds) receive their initial working capital through an appropriation or a transfer of resources from existing appropriations or funds and use those capital resources to finance the initial cost of products and services. Financial resources to replenish the initial working capital and to permit continuing operations are generated by the acceptance of customer orders. The AWCF operates with financial principles that provide improved cost visibility and accountability to enhance business management and improve the decision-making process. The activities provide goods and services on a reimbursable basis. Receipts derived from operations generally are available in their entirety for use without further congressional action.

1.D. Basis of Accounting

The AWCF generally records transactions on an accrual accounting basis as is required by Federal GAAP. For FY 2004, the AWCF's financial management systems are unable to meet all of the requirements for full accrual accounting. Many of the AWCF's financial and nonfinancial feeder systems and processes were designed and implemented prior to the issuance of Federal GAAP for federal agencies and, therefore, were not designed to collect and record financial information on the full accrual accounting basis as required by Federal GAAP.

The AWCF has undertaken efforts to determine the actions required to bring all of its financial and nonfinancial feeder systems and processes into compliance with all elements of Federal GAAP. One such action is the current revision of its accounting systems to record transactions based on the U.S. Standard General Ledger (USSGL). At this time, not all AWCF accounting systems are USSGL compliant. In addition, with the full implementation of the Logistics Modernization Program (LMP), the AWCF will be in compliance with Statement of Federal Financial Accounting Standard (SFFAS) No. 4, "Managerial Cost Accounting Concepts and Standards for the Federal Government." As of December 31, 2003, LMP has been implemented at Tobyhanna Army Depot, Communications and Electronics Command, Soldiers System Command, and selected Army Materiel Command Headquarter activities. LMP will not be fully implemented until the end of FY 2005. Until such time as all of the processes are updated to collect and report financial information as required by Federal GAAP, some of the AWCF's financial data will be based on budgetary transactions (obligations, disbursements, collections), and nonfinancial feeder systems. For example, most financial information presented on the Statement of Net Costs is based on accrued costs; however, some of the financial information is based on obligations and disbursements.

In addition, the Army identifies programs based upon the major appropriation groups provided by Congress. The Army does not, however, accumulate costs for major programs based on performance measures because its financial processes and systems do not account for costs in line with established measures. The Army is reviewing available data and attempting to develop a cost reporting methodology that provides the cost information required by the Statement of Federal Financial Accounting Standard (SFFAS) No. 4, Managerial Cost Accounting Concepts and Standards for the Federal Government.

1.E. Revenues and Other Financing Sources

The AWCF's revenue is recognized according to the percentage of completion method for Depot Maintenance and Ordnance activities. Revenue for Supply Management activities is recognized when an inventory item is sold. Prices set for products and services offered through the AWCF are intended to recover the full costs (cost plus administrative fees) incurred by these activities. Unearned revenue is recorded as deferred revenue until earned.

Other financing sources reported by the AWCF do not include non-monetary support provided by our allies for common defense and mutual security. The U.S. has agreements with foreign countries that include both direct and indirect sharing of costs that each country incurs in support of the same general purpose. 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 serviced in a port. The DoD is reviewing these types of financing and cost reductions in order to establish accounting policies and procedures to identify what, if any, of these costs are appropriate for disclosure in the AWCF's financial statements in accordance with Federal GAAP. Recognition of support provided by host nations would affect both financing sources and expense recognition.

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 AWCF's financial and nonfinancial feeder systems were not designed to collect and record financial information on the full accrual accounting basis, accrual adjustments are made for major items such as payroll expenses and accounts payable. Expenditures for capital and other long-term assets are not recognized as expenses in the AWCF's operations until depreciated as in the case of property, plant and equipment (PP&E). Net increases or decreases in unexpended appropriations are recognized as a change in the net position. Certain expenses, such as annual leave earned but not taken, are recognized in the period in which payments are made.

The AWCF adjusted operating expenses as a result of the elimination of balances between DoD Components. See Note 19.A, General Disclosures related to the Statement of Net Cost, for disclosure of elimination amounts.

1.G. Accounting for Intragovernmental Activities

The AWCF, as an agent of the Federal government, interacts with and is dependent upon the financial activities of the Federal government as a whole. Therefore, these financial statements do not reflect the results of all financial decisions applicable to the AWCF as though it was a stand-alone entity.

The AWCF's proportionate share of public debt and related expenses of the Federal government are not included. Debt issued by the Federal government and the related costs are not apportioned to federal agencies. The AWCF's financial statements, therefore do not report any portion of the public debt or interest, nor do the financial 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 budget appropriations. To the extent this financing may have been obtained through the issuance of public debt, interest costs have not been capitalized since the Department of Treasury does not allocate such interest costs to the benefiting agencies.

The AWCF's civilian employees participate in the Civil Service Retirement System (CSRS) or the Federal Employees Retirement Systems (FERS). Employees and personnel covered by FERS also have varying coverage under Social Security. The AWCF funds a portion of civilian and military pensions. Reporting civilian pensions under CSRS and FERS is the responsibility of the Office of Personnel Management (OPM). The AWCF recognizes an imputed expense for the portion of civilian employee pensions and other retirement benefits funded by the OPM in the Statement of Net Cost and recognizes corresponding imputed revenue from the civilian employee pensions and other retirement benefits in the Statement of Changes in Net Position.

To prepare reliable financial statements, transactions occurring between components or activities within the AWCF must be eliminated for consolidated financial reporting purposes. However, the entire Federal government, including the AWCF, cannot accurately identify all intragovernmental transactions by its related components or activities. The Defense Finance and Accounting Service (DFAS) is responsible for eliminating transactions between components or activities of the AWCF. Beginning in FY 1999, seller entities within the AWCF provided summary seller-side balances for revenue, accounts receivable, transfers-in/out, and unearned revenue to the buyer-side internal AWCF accounting offices. In most cases, the buyer-side records have been adjusted to recognize unrecorded costs and accounts payable. The AWCF intragovernmental balances are then eliminated.

The Department of the Treasury Financial Management Service (FMS) is responsible for eliminating transactions between the DoD and other federal agencies. In September 2000, the FMS issued the "Federal Intragovernmental Transactions Accounting Policies and Procedures Guide." The AWCF was not able to fully implement the policies and procedures in this Guide relating to reconciling intragovernmental assets, liabilities, revenues, and expenses for non-fiduciary transactions. However, the AWCF was able to implement the policies and procedures contained in the "Intragovernmental Fiduciary Transactions Accounting Guide," as updated by the "Federal Intragovernmental Transactions Accounting Policies and Procedures Guide" issued in October 2002 for reconciling intragovernmental transactions. These transactions pertain to Federal Employees' Compensation Act transactions with the Department of Labor (DOL), and benefit program transactions with the OPM.

1.H. Transactions with Foreign Governments and International Organizations

Each year, the AWCF sells defense items and services to foreign governments and international organizations, primarily under the provisions of the Arms Export Control Act of 1976. Under the provisions of the Act, the DoD has the authority to sell defense articles and services to foreign countries and international organizations generally at no profit or loss to the U.S. government. Customers may be required to make payments in advance.

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

The AWCF's financial resources are maintained in U.S. Treasury accounts. DFAS, Military Services, U.S. Army Corp of Engineers (USACE) disbursing stations as well as the Department of State financial service centers process the majority of cash collections, disbursements, and adjustments for the Federal government worldwide. Each disbursing station prepares monthly reports, which provide information to the U.S. Treasury on check issues, electronic fund transfers, interagency transfers and deposits.

In addition, the DFAS sites and the USACE Finance Center submit reports to the Department of the Treasury, by appropriation, on interagency transfers, collections received, and disbursements issued. The Department of the Treasury then records this information to the applicable Fund Balance with Treasury (FBWT) account maintained in the Treasury's system. Differences between the AWCF's and Treasury's records sometime result and are subsequently reconciled. Material disclosures are provided in Note 3. Differences between accounting offices' detail-level records and Treasury's FBWT accounts are disclosed in Note 1.Y (Problem Disbursements) specifically, differences caused by in-transit disbursements and unmatched disbursements which are not recorded in the accounting offices' detail-level records.

1.J. Foreign Currency

Not applicable

1.K. Accounts Receivable

As presented in the Balance Sheet, accounts receivable includes accounts, claims, and refunds receivables from other federal agencies and the public. Federal accounts receivable arise generally from the provision of goods and services to other federal agencies and, with the exception of occasional billing disputes, are considered to be fully collectible. Receivables from the public generally arise from the provision of goods and services to state, local, and foreign governments. Refunds receivable, however, are overpayments by the Federal government in the process of being collected. An allowance for doubtful accounts is established for reporting purposes based on past experience in the collection of accounts receivable and analysis of outstanding balances by fund type. The AWCF 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. The Army Working Capital Fund (AWCF) recognizes an allowance of 50 percent for all non-federal debt between 180 days and two years old and a 100 percent allowance for all non-federal debt over two years old. The allowance will be updated annually, based on the aged accounts receivable at the end of the 2nd Quarter. Material disclosures are provided in Note 5, Accounts Receivable.

1.L. Loans Receivable

Not applicable

1.M. Inventories and Related Property

Not all of the AWCF inventory reported in the financial statements is valued using the same valuation method. The AWCF inventories are reported using the Latest Acquisition Cost (LAC), which approximates historical cost, adjusted for holding gains and losses, and Moving Average Cost (MAC), which computes a new average cost each time a purchase is made. The AWCF uses the LAC method because its inventory systems were designed for material management rather than accounting, except for activities that have transitioned to the Logistics Modernization Program (LMP). The systems provide accountability and visibility over inventory items. They do not maintain the exact historical cost data necessary to comply with SFFAS No. 3, "Accounting for Inventory and Related Property," nor can they directly produce financial transactions using the USSGL, as required by the Federal Financial Management Improvement Act of 1996. The AWCF transition to LMP will also allow the use of a MAC methodology for valuing inventory that, when fully implemented, will allow the AWCF to comply with SFFAS No. 3. (See Note 9, Inventory and Related Property)

SFFAS No. 3 distinguishes between inventory held for sale and inventory held in reserve for future sale. There is no management or valuation difference between the two USSGL accounts. Further, the DoD manages only military or government-specific material under normal conditions. Items commonly used in and available from the commercial sector are not managed in the DoD material management activities. Operational cycles are irregular, and the military risks associated with stock-out positions have no commercial parallel. The AWCF holds material based on military need and support for contingencies. Therefore, the AWCF does not attempt to account separately for items held for current or future sale.

In accordance with new DoD policy, the Army accounts for condemned material as excess, obsolete, and unserviceable. The net value of this type of condemned material is zero, because the costs of disposal are greater than the potential scrap value. Potentially redistributable material, presented in previous years as excess, obsolete, and unserviceable, is included in held for use or held for repair categories according to its condition.

In addition, past audit results identified uncertainties about the completeness and existence of quantities used to produce the reported values. Material disclosures related to inventory and related property are provided in Note 9, Inventory and Related Property.

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

Not applicable

1.O. General Property, Plant and Equipment

General Property, Plant & Equipment (PP&E) assets are capitalized at historical acquisition cost plus capitalized improvements when an asset has a useful life of two or more years, and when the acquisition cost equals or exceeds the DoD capitalization threshold of $100,000. Also, improvement costs over the DoD capitalization threshold of $100,000 for General PP&E are required to be capitalized. All General PP&E, other than land, is depreciated on a straight-line basis. Land is not depreciated.

Prior to FY 1996, General PP&E with an acquisition cost of $15,000, $25,000, and $50,000 for FY 1993, FY 1994, and FY 1995 respectively, and an estimated useful life of two or more years was capitalized. These assets remain capitalized and reported on AWCF financial statements. General PP&E previously capitalized at amounts below $100,000 were written off General Fund financial statements in FY 1998.

For the AWCF activities, all PP&E used in the performance of their mission is categorized as General PP&E, whether or not it meets the definition of any other PP&E categories. For Heritage Assets and Stewardship Land owned or maintained on an AWCF installation are reported in the Supplemental Stewardship Report of the applicable military department. Material disclosures are provided in Note 10, General PP&E, Net.

Internal use software is capitalized at cost if the acquisition cost is $100,000 or more. For commercial off-the-shelf software, the capitalized costs include the amount paid to the vendor for the software; for contractor-developed software it includes the amount paid to a contractor to design, program, install, and implement the software. Capitalized costs for internally developed software include the full cost (direct and indirect) incurred during the software development stage. The estimated useful life for calculating amortization of software is 2 to 5 years using the straight-line method.

1.P. Advances and Prepayments

The AWCF records payments made prior to the receipt of goods and services as advances or prepayments and reports them as assets on the Balance Sheet. Advances and prepayments are recognized as expenditures and expenses when the related goods and services are received.

1.Q. Leases

Not applicable

1.R. Other Assets

The AWCF 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, the AWCF provides financing payments. One type of financing payment that the AWCF makes, for real property, is based upon a percentage of completion. In accordance with the SFFAS No. 1, “Accounting for Selected Assets and Liabilities,” such payments are treated as construction-in-process and are reported on the General PP&E line and in Note 10, General PP&E, Net.

In addition, based on the Federal Acquisition Regulation, the AWCF makes financing payments under fixed price contracts that are not based on a percentage of completion. The AWCF reports these financing payments as advances or prepayments in the “Other Assets” line item. The AWCF treats these payments as advances or prepayments because the AWCF becomes liable only after the contractor delivers the goods in conformance with the contract terms. If the contractor does not deliver a satisfactory product, the AWCF is not obligated to reimburse the contractor for its costs and the contractor is liable to repay the AWCF for the full amount of the advance.

The DoD has completed a review of all applicable federal accounting standards; applicable public laws on contract financing; Federal Acquisition Regulation Parts 32, 49, and 52; and the OMB guidance in 5 Code of Federal Regulations Part 1315, “Prompt Payment.” The DoD has concluded that SFFAS No. 1 does not fully or adequately address the subject of progress payment accounting and is considering what further action is appropriate.

1.S. Contingencies and Other Liabilities

The SFFAS No. 5, “Accounting for Liabilities of the Federal Government,” defines a contingency as an existing condition, situation, or set of circumstances that involves an uncertainty as to possible gain or loss to the AWCF. The uncertainty will be resolved when one or more future events occur or fail to occur. A contingency is recognized as a liability when a past event or exchange transaction has occurred, a future loss is probable and the amount of loss 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 that a loss or additional loss will be incurred. Loss contingencies include the collectibility of receivables, pending or threatened litigation, and possible claims and assessments. The Army's loss contingencies arising as a result of pending or threatened litigation or claims and assessments occur due to events such as aircraft, ship and vehicle accidents; medical malpractice; property or environmental damages; and contract disputes.

1.T. Accrued Leave

Civilian annual leave that has been accrued and not used as of the balance sheet date is reported as a liability. The liability reported at the end of the fiscal year reflects the current pay rates.

1.U. Net Position

Net Position consists of unexpended appropriations and cumulative results of operations. Unexpended appropriations represent budget authority, which is unobligated and has not been rescinded or withdrawn, and funds obligated but for which legal liabilities have not been incurred.

Cumulative results of operations for AWCF represents the excess of revenues over expenses less refunds to customers and returns to the U.S. Treasury since fund inception.

1.V. Treaties for Use of Foreign Bases

Not applicable

1.W. Comparative Data

The Financial Statements and accompanying Notes to the Financial Statements report the financial position and results of operations for the 4th Quarter, FY 2004. Financial statement fluctuations greater than two percent of total assets on the Balance Sheet and/or greater than ten percent between the 4th Quarter, FY 2003 and the 4th Quarter, FY 2004 are explained within the Notes to the Financial Statements.

1.X. Unexpended Obligations

The AWCF obligates funds to provide goods and services for outstanding orders not yet delivered. The financial statements do not reflect this liability for payment for goods or services not yet delivered.

1.Y. Problem Disbursements

(Amounts in thousands)	September 2002	September 2003	September 2004	Decrease/Increase from 2003 to 2004
1. Total Problem Disbursements				
Absolute Unmatched Disbursements	$17,301	$46,298	$25,484	($20,814)
Negative Unliquidated Obligations	4,476	2,850	3,810	960
2. Total In-transit Disbursements, Net	$65,368	$69,687	$135,730	$66,043
3. Other Information Related to Problem Disbursements and In-transit Disbursement				

Definitions:

Absolute value is the sum of the positive values of debit and credit transactions without regard to the sign.

Unmatched Disbursements (UMDs) occur when payments do not match to a corresponding obligation in the accounting system.

Negative Unliquidated Obligations (NULOs) occur when payments have a valid obligation but the payment is greater than the amount of the obligation recorded in the official accounting system. These payments use available funds for valid receiving reports on delivered goods and services under valid contracts.

In-Transits represents the net value of disbursements and collections made by a DoD disbursing activity on behalf of an accountable activity but not yet attempted to be posted in an accounting system.

Aged UMDs and NULOs:
The Army absolute value UMDs, NULOs, and a negative $1,798 thousand in aged in-transit disbursements (of the total net in-transit disbursements of $135,730 thousand) represent problem disbursements. UMDs and NULOs are considered aged immediately, while in-transits are considered normal business activity up to the 30-day aging category. After 30-days, they become perceived as problem disbursements.

Fluctuations in the schedule represent normal activity for UMDs and NULOs based on the inflow of undistributed disbursements received for processing. Total intransit balances have increased at the primary accounting sites supporting the war, contingency operations and supply and materiel replenishment.

Note 2. Nonentity Assets

As of September 30 (Amounts in thousands)	2004	2003
1. Intragovernmental Assets		
A. Fund Balance with Treasury	$0	$0
B. Investments	0	0
C. Accounts Receivable	0	0
D. Other Assets	0	0
E. Total Intragovernmental Assets	$0	$0
2. Non-Federal Assets		
A. Cash and Other Monetary Assets	$0	$0
B. Accounts Receivable	0	0
C. Loans Receivable	0	0
D. Inventory & Related Property	0	0
E. General PP&E	0	0
F. Investments	0	0
G. Other Assets	0	0
H. Total Non-Federal Assets	$0	$0
3. Total Non-Entity Assets	$0	$0
4. Total Entity Assets	$16,488,179	$15,319,744
5. Total Assets	$16,488,179	$15,319,744

Assets are categorized as:

Nonentity asset are assets held by an entity but are not available for use in the operations of the entity. The Army Working Capital Fund (AWCF) does not have nonentity assets.

Entity assets are resources that the AWCF has the authority to use or where management is legally obligated to use funds to meet entity obligations.

Note Reference

For additional line item discussion, see:
Note 3, Fund Balance With Treasury
Note 5, Accounts Receivable
Note 6, Other Assets
Note 9, Inventory and Related Property
Note 10, General PPE, Net

Note 3.A. Fund Balance with Treasury

As of September 30 (Amounts in thousands)	2004	2003
1. Fund Balances		
A. Appropriated Funds	$53	$0
B. Revolving Funds	948,410	1,548,546
C. Trust Funds	0	0
D. Other Fund Types	0	0
E. Total Fund Balances	$948,463	$1,548,546
2. Fund Balances Per Treasury Versus Agency		
A. Fund Balance per Treasury	$948,463	$1,548,546
B. Fund Balance per Army Working Capital Fund	948,463	1,548,546
3. Reconciling Amount	$0	$0

Fluctuations and/or Abnormalities

Appropriated Funds increased $53 thousand, or 100 percent, from FY 2003 to FY 2004. This balance includes FY 2000 appropriations that have not been expended and were reported in Revolving Funds in FY 2003. All Army Working Capital Fund (AWCF) FY 2004 appropriations received have been obligated and expended.

The Fund Balance With Treasury (FBWT) available for the AWCF decreased by $600,083 thousand, or 39 percent, from FY 2003 to FY 2004. In FY 2004, the AWCF eliminated credit on equipment returns from Operations Iraqi Freedom and Enduring Freedom to compensate for higher current and future repair and replacement costs. Additional funds were also realized from increased sales in support of the contingency missions Operations Enduring Freedom, Iraqi Freedom, and Noble Eagle. In addition, the AWCF received direct appropriations of $105,400 thousand for war reserves and $113,900 thousand received for industrial mobilization capacity, totaling $219,300 thousand.

During the 2nd Quarter FY 2004, Program Budget Decision 614 transferred $41,600 thousand to the Defense Commissary Agency. Also, during the 3rd Quarter, Defense Reprogramming Action FY 04-60 IR transferred $107,000 thousand and FY 04-68 IR transferred $1,050,000 thousand to the Army General Fund. In 4th Quarter 2004, Defense Reprogramming Action FY 04-81 IR transferred $250,000 thousand to the Army General Fund.

Other Disclosures

Defense Finance and Accounting Service increased field-reported data by $1,917 thousand to agree with the Fund Balance With Treasury reported on the Treasury trial balance.

The deposit differences are reconcilable differences reported by the Treasury or the Army. The Army has $60 thousand in deposit differences greater than 180 days old as of September 30, 2004. These differences are expected to clear by November 2004.

The Intragovernmental Payment and Collection (IPAC) differences are reconcilable differences that represent amounts recorded by the Treasury but not reported by the organization. The Army had no IPAC differences greater than 180 days old as of June 30, 2004.

Automated reconciliation tools have virtually eliminated all existing differences for the Army. Field sites requiring additional documentation to record the transaction in their accounting system, accounting errors, or timing differences between disbursing and Treasury cut-off dates are the only reasons for an IPAC difference to exist today.

Note Reference

See Note 1.I, Funds with the U.S. Treasury

Note 3.B. Disclosures Related to Suspense/Budget Clearing Accounts

The Suspense/Budget Clearing Accounts are maintained and reported by the Army General Fund. Some transactions relating to the AWCF may be in suspense accounts, but are not identifiable. When they are identified to the AWCF, they will be transferred from the suspense/clearing account to the correct Treasury appropriation.

Note 4. Investments

Not applicable.

Note 5. Accounts Receivable

As of September 30 (Amounts in thousands)	2004 Gross Amount Due	2004 Allowance For Estimated Uncollectibles	2004 Accounts Receivable, Net	2003 Accounts Receivable, Net
1. Intra-governmental Receivables:	$444,923	N/A	$444,923	$411,254
2. Non-Federal Receivables (From the Public):	26,438	(12,956)	13,482	31,176
3. Total Accounts Receivable:	$471,361	$(12,956)	$458,405	$442,430

4. Allowance method:

The Army Working Capital Fund (AWCF) recognizes an allowance of 50 percent for all non-federal debt between 180 days and two years old and a 100 percent allowance for all non-federal debt over two years old. The allowance will be updated annually, based on the aged accounts receivable at the end of the 2nd Quarter.

5. Other information:

Fluctuations and/or Abnormalities

Non-Federal Receivables decreased by $17,694 thousand, or 57 percent, between FY 2003 and FY 2004. The majority of the decrease is attributed to the establishment of an allowance for estimated uncollectible receivables, which totals $12,956 thousand. The remainder of the decrease is attributed to the collection of delinquent contractor debts.

Other Disclosures

The DoD policy is to allocate supported undistributed collections between intragovernmental and non-federal categories based on the percentage of each category of receivables. A review of data for the previous twelve months found no transactions for undistributed collections involving a non-federal entity. Therefore, all undistributed collections are assigned to federal entities.

For FY 2004, the AWCF reported unsupported undistributed collections of $854 thousand. These collections are reported as a Liability for Deposit Funds, Clearing Funds, and Undeposited Collections, as required by the DFAS-Arlington year-end guidance.

The AWCF accounting systems do not capture trading partner data at the transaction level in a manner that facilitates trading partner aggregations. Therefore, the AWCF was unable to reconcile intragovernmental accounts receivable balances with its trading partners' accounts payable balances. The DoD intends to develop long-term systems improvements that will address this issue.

Intragovernmental accounts receivable include $3,594 thousand in receivables over 180 days old which is less than one percent of the total intragovernmental accounts receivable.

Non-federal accounts receivable includes $10,468 thousand over 180 days old. Of this amount, $7,724 thousand was for contractor debt. The remaining amount is due to Foreign Military Sales and travel advances.

For FY 2004, AWCF reported non-federal refunds receivable of $13,568 thousand.

Note Reference

For additional line item discussion, see:
Note 1.K, Accounts Receivable
Note 12, Accounts Payable
Note 15A, Other Liabilities

Note 6. Other Assets

As of September 30 (Amounts in thousands)	**2004**	**2003**
1. Intra-governmental Other Assets:		
A. Advances and Prepayments	$79	$329
B. Other Assets	0	0
C. Total Intra-governmental Other Assets	$79	$329
2. Non-Federal Other Assets:		
A. Outstanding Contract Financing Payments	$262,338	$250,142
B. Other Assets (With the Public)	2,784	19,735
C. Total Non-Federal Other Assets	$265,122	$269,877
3. Total Other Assets:	$265,201	$270,206

4. Other Information Related to Other Assets:

Fluctuations and/or Abnormalities

Intragovernmental advances and prepayments decreased by $250 thousand, or 76 percent, from FY 2003 to FY 2004. This account balance is dictated by trading partner reports of unearned revenue made by other DoD entities. The majority of the change is a result of Army Working Capital Fund (AWCF) advances to the Air Force decreasing $222 thousand.

Other Assets (With the Public) decreased $16,951 thousand, or 86 percent. During the 4th Quarter FY 2004, the United States Army Medical Materiel Agency reported a decrease of $17,408 thousand, as it closed out an advance it had reported for several years.

Non-Federal Other Assets - Other Assets (With the Public):

(Amounts in thousands)

Type of Assets	2004	2003
Advances to Others:		
Contractor Advance	$2,010	$19,418
Travel Advances	73	53
Prepayments	701	231
Creditable Material Returns	0	33
Totals	$2,784	$19,735

Advances and Prepayments

In accordance with DoD elimination guidance, the FY 2004 AWCF intragovernmental advances to others balance increased by $758 thousand to agree with seller-side unearned revenue from other DoD reporting entities. The note also reflects $679 thousand in elimination entries within the AWCF, leaving a balance of $79 thousand in these accounts.

Note Reference

See Note 1.R, Other Assets

Note 7. Cash and Other Monetary Assets

Not Applicable

Note 8. A. Direct Loan and/or Loan Guarantee Programs

Not applicable

Note 8.B. Direct Loans Obligated After FY 1991

Not applicable

Note 8.C. Total Amount of Direct Loans Disbursed

Not applicable

Note 8.D. Subsidy Expense for Post-1991 Direct Loans

Not applicable

Note 8.E. Subsidy Rate for Direct Loans

Not applicable

Note 8.F. Schedule for Reconciling Subsidy Cost Allowance Balances for Post-1991 Loan Guarantees

Not applicable

Note 8.G. Defaulted Guaranteed Loans from Post-1991 Guarantees

Not applicable

Note 8.H. Guaranteed Loans Outstanding
Not applicable

Note 8.I. Liability for Post-1991 Loan Guarantees, Present Value
Not applicable

Note 8.J. Subsidy Expense for Post-1991 Loan Guarantees
Not applicable

Note 8.K. Subsidy Rate for Loan Guarantees
Not applicable

Note 8.L. Schedule for Reconciling Loan Guarantee Liability Balances for Post-1991 Loan Guarantees
Not applicable

Note 8.M. Administrative Expense
Not applicable

Note 9. Inventory and Related Property

As of September 30 (Amounts in thousands)	2004	2003
1. Inventory, Net (Note 9.A.)	$13,916,672	$12,131,811
2. Operating Materials & Supplies, Net (Note 9.B.)	0	0
3. Stockpile Materials, Net (Note 9.C.)	0	0
4. Total	$13,916,672	$12,131,811

Note 9.A. Inventory, Net

	2004			2003	
As of September 30 (Amounts in thousands)	Inventory, Gross Value	Revaluation Allowance	Inventory, Net	Inventory, Net	Valuation Method
1. Inventory Categories:					
A. Available and Purchased for Resale	$15,499,542	$(3,032,467)	$12,467,075	$11,225,500	O, LAC
B. Held for Repair	3,081,372	(1,653,069)	1,428,303	895,098	O, LAC
C. Excess, Obsolete, and Unserviceable	455,004	(455,004)	0	0	NRV
D. Raw Materials	21,294	0	21,294	9,777	O
E. Work in Process	0	0	0	1,436	LAC
F. Total	$19,057,212	$(5,140,540)	$13,916,672	$12,131,811	

Legend for Valuation Methods:

Adjusted LAC = Latest Acquisition Cost, adjusted for holding gains and losses
NRV = Net Realizable Value
O = Other
SP = Standard Price

2. Restrictions of Inventory Use, Sale, or Disposition:

There are no restrictions on the use, sale, or disposition of inventory except in the following situations:

1) Distributions without reimbursement are made when authorized by DoD directives;
2) War reserve material includes petroleum products and subsistence items that are considered restricted; and
3) Inventory, with the exception of safety stocks, may be sold to foreign, state and local governments; private parties; and contractors in accordance with current policies and guidance or at the direction of the President.

3. Other Information:

Definitions

Other - Moving Average Cost (MAC)

Inventory - spare and repair parts, clothing and textiles, petroleum products, and ammunition.

Inventory held for repair - damaged material that requires repair to make it usable.

Excess, obsolete, and unserviceable inventory - condemned materiel that must be retained for management purposes.

Raw materials - items consumed in the production of goods for sale or in the provision of services for a fee.

Work in process - munitions in production and maintenance work with its associated labor, applied overhead, and supplies used in the delivery of maintenance services.

Future Sales

In addition to the account balances shown in Table 9.A., Federal Generally Accepted Accounting Principles require disclosure of the amount of inventory held for future sale. The Army Working Capital Fund (AWCF) estimates that none of the Inventory Held for Sale will be sold more than 24 months after the end of FY 2004.

Fluctuations and/or Abnormalities

Total inventory increased $1,784,861 thousand, or 15 percent, from FY 2003 to FY 2004. This increase is detailed in the paragraphs below.

The Inventory Available and Purchased for Resale increased $1,241,575 thousand, or 11 percent, from FY 2003 to FY 2004. The Supply Management business area, specifically the Tank-automotive and Armaments Command and the Aviation and Missile Command, received additional contract authority in FY 2003 and FY 2004 to purchase spare parts. These commands received these parts in FY 2004, which caused the inventory increase from FY 2003 to FY 2004.

The Inventory Held for Repair increased $533,205 thousand, or 60 percent, from FY 2003 to FY 2004 because of an increase in the volume of returned items needing repair in support of the contingency missions Operations Enduring Freedom, Iraqi Freedom, and Noble Eagle.

Raw Materials increased $11,517 thousand, or 118 percent and is attributable increases reported at Tobyhanna Army Depot.

Work in Process decreased $1,436 thousand, or 100 percent, from FY 2003 to FY 2004 at the Watervliet Arsenal. The decrease from FY 2003 is a result of Watervliet Arsenal billing all FY 2004 costs and all FY 2003 carry-over costs.

Other Disclosures

The AWCF began transitioning to the Logistics Modernization Program during June FY 2003. Therefore, not all of the AWCF's inventory reported in Note 9 is valued under the same method. Inventory at Tobyhanna Army Depot, Communications-Electronics Command, and Soldiers System Command is valued at MAC, with the exception of Tobyhanna's Project Stock, while the remainder of the AWCF's inventory is valued at LAC.

The Commodity Command Standard System inventory reported as Available and Purchased for Resale includes a net upward adjustment of $3,368,724 thousand to bring financial records into agreement with the logistics records. The Defense Finance and Accounting Service (DFAS) implemented new procedures in FY 2004 to reconcile the financial and logistics records. Some transactions are not passing from logistical records to financial records. DFAS continues to work to identify the problems so that complete reconciliations can be completed.

Note Reference

For additional line item discussion, see:
Note 19.A. General Disclosures Related to the Statement of Net Cost

Note 9.B. Operating Materials and Supplies, Net

Not applicable. The AWCF expenses rather than capitalizes OM&S because it is normally used within a year of purchase.

Note 9.C. Stockpile Materials, Net

Not Applicable.

Note 10. General PP&E, Net

As of September 30 (Amounts in thousands)			2004			2003
	Depreciation/ Amortization Method	Service Life	Acquisition Value	(Accumulated Depreciation/ Amortization)	Net Book Value	Prior FY Net Book Value
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	$1,811,251	($1,284,559)	$526,692	$553,827
C. Leasehold Improvements	S/L	Lease term	95,320	(73,735)	21,585	24,681
D. Software	S/L	2-5 Or 10	312,610	(209,395)	103,215	88,227
E. General Equipment	S/L	5 or 10	1,485,511	(1,266,966)	218,545	216,594
F. Military Equipment	S/L	Various	0	0	0	0
G. Assets Under Capital Lease[1]	S/L	lease term	0	0	0	0
H. Construction-in-Progress	N/A	N/A	29,401	N/A	29,401	42,928
I. Other			0	0	0	494
J. Total General PP&E			$3,734,093	($2,834,655)	$899,438	$926,751

[1] Note 15.B for additional information on Capital Leases

Legend for Valuation Methods:

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

2. Other Information:

Leasehold Improvements – The entire amount shown on this line is for improvements made to facilities at Corpus Christi Army Depot, which is a tenant on a Navy installation, but does not maintain a lease with the Navy. Improvements made on these facilities are recorded as leasehold improvements. The decrease of $3,096 thousand, or 13 percent, from FY 2003 and FY 2004 is due to depreciation recorded.

Software – Software increased $14,988 thousand, or 17 percent, between 4th Quarter of FY 2003 and FY 2004. This is combination of two factors. Between FY 2003 and FY 2004, the acquisition value for software increased by $125,179 thousand. The increase is attributed to software acquired between FY 2000 and FY 2002, which was either improperly recorded, or not recorded at all, in the accounting records until FY 2004. This increase includes $62,000 thousand of software incorrectly reported as equipment and $26,666 thousand incorrectly reported as construction in progress, in addition to new software purchases and software not previously recorded. The majority of the increase is offset by the short service life and subsequent high depreciation values for software. The Army Working Capital Fund (AWCF) is currently identifying all internal use software, as required by Statement of Federal Financial Accounting Standards Number 10.

Construction in Progress – Construction in Progress decreased by $13,527 thousand, or 32 percent. The majority of the decrease in construction in progress was the correction of a posting error. Communications-Electronics Command erroneously posted internal use software as construction in progress in a prior fiscal year. The AWCF identified and corrected this error during 4th Quarter FY 2004.

Other – Other equipment decreased $494 thousand, or 100 percent, between FY 2003 and FY 2004. The balance shown for FY 2003 was an erroneous posting and was corrected in FY 2004.

Note Reference

See Note 1.O, General Plant, Property and Equipment

Note 10.A. Assets Under Capital Lease

As of September 30 (Amounts in thousands)	2004	2003
1. Entity as Lessee, Assets Under Capital Lease:		
A. Land and Buildings	$0	$0
B. Equipment	0	0
C. Other	0	0
D. Accumulated Amortization	0	0
E. Total Capital Leases	$0	$0

2. Description of Lease Arrangements:

3. Other Information:

Corpus Christi Army Depot is a tenant on a Navy installation, but does not maintain a lease with the Navy. Improvements made on these facilities are recorded as leasehold improvements.

Note 11. Liabilities Not Covered by Budgetary Resources

As of September 30 (Amounts in thousands)	2004	2003
1. Intra-governmental Liabilities		
A. Accounts Payable	$0	$0
B. Debt	0	0
C. Environmental Liabilities	0	0
D. Other	50,084	27,824
E. **Total Intra-governmental Liabilities**	$50,084	$27,824
2. Non-Federal Liabilities		
A. Accounts Payable	$0	$0
B. Military Retirement Benefits and Other Employment-Related Actuarial Liabilities	304,976	320,654
C. Environmental Liabilities	0	0
D. Loan Guarantee Liability	0	0
E. Debt Held by Public	0	0
F. Other Liabilities	66,859	0
G. **Total Non-Federal Liabilities**	$371,835	$320,654
3. Total Liabilities Not Covered by Budgetary Resources	$421,919	$348,478
4. Total Liabilities Covered by Budgetary Resources	695,373	1,075,630
5. Total Liabilities	$1,117,292	$1,424,108

Liabilities Not Covered by Budgetary Resources are liabilities incurred by the reporting entity which are not covered by realized budgetary resources as of the balance sheet date.

Liabilities Covered by Budgetary Resources are liabilities incurred by the reporting entity which are covered by realized budget resources as of the balance sheet date. Budgetary resources encompass not only new budget authority, but also other resources available to cover liabilities for specified purposes in a given year. Realized budgetary resources include:

1. New budget authority
2. Spending authority from offsetting collections (credited to an appropriation or fund account)
3. Recoveries of unexpired budget authority through downward adjustments of prior year obligations
4. Unobligated balances of budgetary resources at the beginning of the year or net transfers of prior year balances during the year
5. Permanent indefinite appropriations or borrowing authority, which have been enacted and signed into law as of the balance sheet date, provided that the resources may be apportioned by the Office of Management and Budget without further action by the Congress or without a contingency first having to be met.

Fluctuations and/or Abnormalities

Other Intragovernmental Liabilities increased $22,260 thousand, or 80 percent, from FY 2003 to FY 2004 because of a change in accounting procedures. The portion of the liability that was due in October 2003 was reported as Covered by Budgetary Resources. The current procedure accounts for the portion of the liability due in October 2004 as Not Covered by Budgetary Resources.

Other Non-Federal Liabilities increased from FY 2003 to FY 2004 by $66,859 thousand, or 100 percent, from a mapping change to include Annual Leave as a Not Covered by Budgetary Resources liability. Previously, this liability was reported as Covered by Budgetary Resources.

Other Liabilities Not Covered by Budgetary Resources:
(Amounts in thousands)

	2004	2003
Intragovernmental - Other Liabilities		
FECA Reimbursement to the Dept. of Labor	$50,084	$27,824

Legend:
FECA – Federal Employees Compensation Act

The FECA reimbursement liability is classified as covered or not covered by budgetary resources based on the date the liability is due to be paid. If the liability is due to be paid within one year, it is considered in the rates for the current year and is therefore covered by budgetary resources. If the liability is not due within a year, it is not considered in the rates for the current year and is therefore not covered by budgetary resources. The FECA liability is due in October each year. The covered portion is due in October 2004, while the not covered portion is due in October 2005. Only the Depot Maintenance and Ordnance business areas report a FECA liability because they are host installations responsible for paying Workers' Compensation. The Supply Management business area is made up of selected personnel at other installations, whose FECA liabilities are paid by the Army General Fund.

The FECA liability due in FY 2006 is based on the liability incurred for FY 2005.

Non-Federal Liabilities

Military Retirement Benefits and Other Employment-Related Actuarial Liabilities consist of the FECA actuarial liability.

Note Reference

For additional line item discussion, see:
Note 12, Accounts Payable
Note 15, Other Liabilities
Note 17, Military Retirement Benefits and Other Employment Related Actuarial Liabilities

Note 12. Accounts Payable

As of September 30 (Amounts in thousands)	2004			2003
	Accounts Payable	Interest, Penalties, and Administrative Fees	Total	Total
1. Intra-governmental Payables:	$159,150	N/A	$159,150	$435,586
2. Non-Federal Payables (to the Public):	372,054	0	372,054	342,365
3. Total	$531,204	$0	$531,204	$777,951

4. Other Information:

Intragovernmental Payables - amounts owed to other federal agencies for goods or services ordered and received but not yet paid. Interest, penalties and administrative fees are not applicable to intragovernmental payables.

Non-Federal Payables (to the Public) - payables for debts owed to individuals and entities outside the Federal Government.

Fluctuation and/or Abnormalities

The Army Working Capital Fund (AWCF) Intragovernmental Payables decreased $276,436 thousand, or 63 percent, between FY 2003 and FY 2004. This decrease is primarily due to the FY 2004 AWCF payment of $322,310 thousand in FY 2003 transportation costs to the Defense Logistics Agency.

Other Disclosures

Undistributed disbursements are the difference between disbursements recorded in the activity field records of the AWCF versus those reported by the U.S. Treasury. The DoD policy is to allocate supported undistributed disbursements between intragovernmental and non-federal categories based on the percentage of each category of payables. The AWCF allocated supported undistributed disbursements based on a 12-month review of detail transactions. Unsupported undistributed disbursements are those disbursements reported at the U.S. Treasury for which no supporting voucher exists to post to the appropriate line in the accounting records.

Unsupported undistributed disbursements are recorded in United States Standard General Ledger (USSGL) account 2120, Disbursements in Transit. At the direction of the Office of the Under Secretary of Defense (Comptroller), the AWCF wrote off unsupported undistributed disbursements of $63,287 thousand in FY 2004. The AWCF currently has $2,247 thousand in unsupported undistributed disbursements.

The DoD summary level seller accounts receivable balances were compared to the AWCF payable balances. As a result of this comparison, adjusting entries were entered to decrease the AWCF's intragovernmental payables by $2,290 thousand. In addition, $4,063 thousand of payables within the AWCF were eliminated from the report. For the majority of intragovernmental sales, the AWCF's accounting systems do not capture trading partner data at the transaction level in a manner that facilitates trading partner aggregations. Therefore, the AWCF was unable to reconcile its intragovernmental payables with its trading partners' receivables. The DoD intends to develop long-term systems improvements that will address this issue.

Note Reference

See Note 1.G, Accounting for Intragovernmental Activities

Note 13. Debt

Not applicable.

Note 14. Environmental Liabilities and Disposal Liabilities

Not applicable.

Note 15.A. Other Liabilities

As of September 30 (Amounts in thousands)	2004 Current Liability	2004 Noncurrent Liability	2004 Total	2003 Total
1. Intragovernmental:				
A. Advances from Others	$10,962	$0	$10,962	$32,673
B. Deferred Credits	0	0	0	0
C. Deposit Funds and Suspense Account Liabilities	0	0	0	0
D. Resources Payable to Treasury	0	0	0	0
E. Disbursing Officer Cash	0	0	0	0
F. Non-environmental Disposal Liabilities:				
(1) National Defense PP&E (Non-nuclear)	0	0	0	0
(2) Excess/Obsolete Structures	0	0	0	0
(3) Conventional Munitions Disposal	0	0	0	0
(4) Other	0	0	0	0
G. Accounts Payable-- Cancelled Appropriations	0	0	0	0
H. Judgment Fund Liabilities	0	0	0	0
I. FECA Reimbursement to the Department of Labor	22,260	27,824	50,084	50,462
J. Capital Lease Liability	0	0	0	0
K. Other Liabilities	6,614	0	6,614	11,364
L. Total Intra-governmental Other Liabilities	$39,836	$27,824	$67,660	$94,499
2. Non-Federal:				
A. Accrued Funded Payroll and Benefits	$67,789	$0	$67,789	$85,330
B. Advances from Others	37,206	0	37,206	33,421
C. Deferred Credits	0	0	0	0
D. Loan Guarantee Liability	0	0	0	0
E. Liability for Subsidy Related to Undisbursed Loans	0	0	0	0
F. Deposit Funds and Suspense Accounts	(854)	0	(854)	0
G. Temporary Early Retirement Authority	0	0	0	0
H. Non-environmental Disposal Liabilities:				
(1) National Defense PP&E (Non-nuclear)	0	0	0	0
(2) Excess/Obsolete Structures	0	0	0	0
(3) Conventional Munitions Disposal	0	0	0	0
(4) Other	0	0	0	0
I. Accounts Payable--Cancelled Appropriations	0	0	0	0
J. Accrued Unfunded Annual Leave	66,860	0	66,860	72,592
K. Accrued Entitlement Benefits for Military Retirees and Survivors	0	0	0	0
L. Capital Lease Liability	0	0	0	0
M. Other Liabilities	42,451	0	42,451	39,661
N. Total Non-Federal Other Liabilities	$213,452	$0	$213,452	$231,004
3. Total Other Liabilities:	$253,288	$27,824	$281,112	$325,503

4. Other Information Pertaining to Other Liabilities:

Fluctuations and/or Abnormalities

Total Intragovernmental Other Liabilities decreased $26,839 thousand, or 28 percent, because of the following reasons.

Intragovernmental Advances from others decreased $21,711 thousand, or 66 percent, primarily from FY 2002 orders from the Army General Fund that were collected in advance in FY 2003. These orders were completed and the resulting revenue was recognized in 2004.

Intragovernmental Other Liabilities decreased $4,750 thousand, or 42 percent. The change is a result of decreased employee benefit liabilities as reported by the Office of Personnel Management because of a timing difference between FY 2003 and FY 2004 payroll payments of the last payroll of the fiscal year. The last payroll in FY 2003 was paid on September 18th and the last payroll in FY 2004 was paid on September 30th.

Total Non-Federal Other Liabilities decreased $28,051 thousand, or 12 percent, because of the following reasons.

Accrued Funded Payroll and Benefits decreased $17,541 thousand, or 21 percent, because of a timing difference between FY 2003 and FY 2004 payroll payments of the last payroll of the fiscal year. The last payroll in FY 2003 was paid on September 18th and the last payroll in FY 2004 was paid on September 30th.

Non-Federal Advances from Others increased $3,785 thousand, or 11 percent. The increase is primarily from additional work performed at Anniston Army Depot and Rock Island Arsenal.

Deposit Funds and Suspense Accounts decreased $854 thousand, or 100 percent, as a result of Unsupported Undistributed Collections being moved to the Liability for Deposit Funds, Clearing Accounts, and Undeposited Collections per Attachment 15 of DFAS - Arlington guidance for financial statement preparation.

Other Disclosures

The Federal Employment Compensation Act (FECA) is administered by the Department of Labor (DOL), Office of Workers' Compensation Programs. Workers' Compensation claims are submitted to and approved by the DOL. The DOL pays the claim holders and prepares a chargeback billing to the AWCF. The FECA law, P.L. 93-416, Section 8147, essentially gives agencies two years to pay the chargeback bill, thereby allowing time for the applicable amount to be included in budget submissions. Pursuant to the FECA law, funding should be paid within 30 days. The current liability is payable in October 2004 and the non-current liability is payable in October 2005. Only the Depot Maintenance and Ordnance business areas report a FECA liability because they are host installations responsible for paying Workers' Compensation. The Supply Management business area is made up of selected personnel at other installations, whose FECA liabilities are paid by the Army General Fund.

The Unemployment Benefits Liability bill received from the DOL is not broken out by appropriation. The AWCF does not report an Unemployment Benefits liability. The Army determined that the General Fund is responsible for the entire liability and reports it on the General Fund statements.

Other Liabilities: **(Amounts in Thousands)**

	FY 2004	FY 2003
Intragovernmental - Other Liabilities		
VSIP	$0	$630
CSRS, FERS, FEGLI, FEHB	6,614	10,734
FECA Payable, Past Due	0	0
Total Intragovernmental Other Liabilities	**$6,614**	**$11,364**
Non-Federal –Other Liabilities		
Contract Holdbacks	$32,852	$31,751
Employers Contributions to TSP and Taxes Payable	9,599	7,910
Contingent Liability	0	0
Total Non-Federal Other Liabilities	**$42,451**	**$39,661**
Total Other Liabilities	**$49,065**	**$51,025**

Legend: VSIP – Voluntary Separation Incentive Pay
CSRS – Civil Service Retirement System
FERS – Federal Employees Retirement System
FEGLI – Federal Employees Group Life Insurance
FEHB – Federal Employees Health Benefits
FECA – Federal Employees Compensation Act
TSP – Thrift Savings Plan

Note Reference

For additional line item discussion, see:
Note 1.S, Contingencies and Other Liabilities
Note 11, Liabilities Not Covered by Budgetary Resources
Note 17, Military Retirement Benefits and Other Employment Related Actuarial Liabilities

Note 15.B. Capital Lease Liability

Not applicable.

Note 16. Commitments and Contingencies

Disclosures Related to Commitments and Contingencies:

Relevant Information for Comprehension

Nature of Contingency

The Army Working Capital Fund (AWCF) has other contingent liabilities in which the possibility of loss is considered reasonable. These liabilities are not accrued in the AWCF's financial statements.

As of September 30, 2004, the AWCF does not have any claims considered reasonably possible.

Note Reference

See Note Disclosure 1. S, Contingencies and Other Liabilities

Note 17. Military Retirement Benefits and Other Employment Related Actuarial Liabilities

As of September 30 (Amounts in thousands)	2004 Actuarial Present Value of Projected Plan Benefits	2004 Assumed Interest Rate (%)	2004 (Less: Assets Available to Pay Benefits)	2004 Unfunded Actuarial Liability	2003 Unfunded Actuarial Liability
1. Pension and Health Benefits:					
A. Military Retirement Pensions	$0		$0	$0	$0
B. Military Retirement Health Benefits	0		0	0	0
C. Medicare-Eligible Retiree Benefits	0		0	0	0
D. Total Pension and Health Benefits	$0		$0	$0	$0
2. Other:					
A. FECA	$304,976	4.88	$0	$304,976	$320,654
B. Voluntary Separation Incentive Programs	0		0	0	0
C. DoD Education Benefits Fund	0		0	0	0
D.	0		0	0	0
E. Total Other	$304,976		$0	$304,976	$320,654
3. Total Military Retirement Benefits and Other Employment Related Actuarial Liabilities:	$304,976		$0	$304,976	$320,654

4. Other Information Pertaining to Military Retirement Benefits and Other Employment-Related Actuarial Liabilities:

Actuarial Cost Method Used: The Army's actuarial liability for Workers' compensation benefits is developed by the Department of Labor and provided to the Army at the end of each fiscal year. The liability includes the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases. The liability is determined using a method that utilizes historical benefit payment patterns to predict the ultimate payments.

Assumptions: The projected annual benefit payments are discounted to the present value using the Office of Management and Budget economic assumptions for 10-year U.S. Treasury notes and bonds. Cost of living adjustments and medical inflation factors are applied to the calculation of projected future benefits.

Market Value of Investments in Market-based and Marketable Securities: Not applicable.

Military Retirement Benefits

The Army General Fund pays the Army Working Capital Fund's (AWCF) military retirement benefits.

Federal Employment Compensation Act (FECA)

Only the Depot Maintenance and Ordnance business areas report a FECA liability because they are host installations responsible for paying Workers' Compensation. The Supply Management business area is made up of selected personnel at other installations, whose FECA liabilities are paid by the Army General Fund.

The Office of Personnel Management provides updated Army actuarial liabilities during the 4th Quarter of each fiscal year. The AWCF computes its portion of the total Army actuarial liability based on the percentage of the AWCF's FECA expense to the total Army FECA expense.

Note Reference

For additional line item discussion, see:
Note 11, Liabilities Not Covered by Budgetary Resources
Note 15.A, Other Liabilities

Note 18. Unexpended Appropriations

As of September 30 (Amounts in thousands)	2004	2003
1. Unexpended Appropriations:		
A. Unobligated, Available	$0	$0
B. Unobligated, Unavailable	0	0
C. Unexpended Obligations	53	11,960
D. Total Unexpended Appropriations	$53	$11,960

Fluctuations and/or Abnormalities

Unexpended Obligations decreased $11,907 thousand, or 99 percent, from FY 2003 to FY 2004, as the Army Working Capital Fund received delivery of goods (expended funds) from funds that were obligated in FY 2000.

Relevant Information for Comprehension

Unexpended obligations reported as a component of Unexpended Appropriations includes both Undelivered Orders–Unpaid and Undelivered Orders-Paid only for appropriated funds. This amount is distinct from Change in Budgetary Resources Obligated for Goods, Services, and Benefits Ordered but Not Yet Received of the Statement of Financing, which includes the change during the fiscal year in unexpended obligations against budget authority from all sources.

Note Reference

For additional line item discussion, see:
Note 21.A, Disclosures Related to the Statement of Budgetary Resources

Note 19.A General Disclosures Related to the Statement of Net Cost

Disclosures Related to the Statement of Net Cost

The Consolidated Statement of Net Cost in the Federal Government is unique because its principles are driven by understanding the net cost of programs and/or organizations that the Federal Government supports through appropriations or other means. This statement provides gross and net cost information that can be related to the amount of output or outcome for a given program and/or organization administered by a responsible reporting entity.

While the Army Working Capital Fund (AWCF) activities generally record transactions on an accrual basis, as is required by Federal Generally Accepted Accounting Principles (GAAP), the systems do not always capture actual costs. Information presented on the Consolidated Statement of Net Cost is primarily based on budgetary obligation, disbursements, or collection transactions, as well as information from non-financial feeder systems. The Army is in the process of upgrading its financial and logistical feeder systems to the Logistics Modernization Program (LMP) to address this issue.

Fluctuations and/or Abnormalities

The AWCF's net costs decreased by $1,877,382 thousand, or 361 percent, between 4th Quarter FY 2003 and FY 2004, primarily due to increased sales within the AWCF in support of the contingency missions

Operations Enduring Freedom, Iraqi Freedom, and Noble Eagle. In FY 2004, the AWCF eliminated credit on equipment returns from Operations Iraqi Freedom and Enduring Freedom to compensate for higher current and future repair and replacement costs. However, this increase cannot be seen on the Statement of Net Cost, as the FY 2004 revenue reflects $3,488,555 thousand of revenue within the AWCF that has been eliminated. The FY 2003 Statement of Net Cost reflects $1,473,493 thousand of revenue within the AWCF that has been eliminated. In addition, field reported revenue was reduced by $1,796,859 thousand for Material Return Credits. Field reported Cost of Goods Sold was also reduced by the same amount of the Material Return Credits. Also, a decrease in Gross Costs with the Public contributed to the overall decrease in net costs.

The mapping for the Statement of Net Cost changed in FY 2004. Prior to FY 2004, other gains and losses were netted on the Gross Cost with the Public. In FY 2004, other gains were moved from Gross Cost with the Public to Earned Revenue from the Public. Included in the FY 2004 Earned Revenue from the Public are $4,481,186 thousand in Other Gains. Included in the FY 2004 Gross Costs with the Public are $4,178,155 thousand in Other Losses.

In FY 2004, the AWCF eliminated credit on equipment returns from Operations Iraqi Freedom and Enduring Freedom to compensate for higher current and future repair and replacement costs. This policy change is the primary reason for the net cost decrease. The intragovernmental earned revenue from sales is used to buy or replace inventory and to finance the delivery of future goods and services. The increased sales also translate to increased Intragovernmental Gross Costs and Gross Costs with the Public as the AWCF replenishes inventory.

The fluctuations are as follows:

- Intragovernmental gross costs increased by $196,477 thousand, or 7 percent
- Intragovernmental earned revenue decreased by $1,827,838 thousand, or 18 percent
- Gross costs with the public increased by $827,268 thousand, or 11 percent
- Earned revenue from the public increased by $4,728,965 thousand, or 2,129 percent

During FY 2004, it was discovered that inventory transactions in LMP were causing overstatement of other gains and other losses, impacting the Communication and Electronics Command (CECOM), Tobyhanna Army Depot, and Soldier System Command. To correct these problems, the Defense Finance and Accounting Service (DFAS) prepared adjusting entries to reduce inventory gains with a corresponding offset to the inventory losses. DFAS prepared entries to reduce inventory gains for CECOM of $8,925,078 thousand, Tobyhanna Army Depot of $1,337,129 thousand, and Soldier Systems Command of $95,000 thousand.

In addition, elimination balancing entries to bring the AWCF's buyer-side costs into agreement with the seller-side revenues caused a reclassification of $5,402,494 thousand from Public Gross and Net Costs to Intragovernmental Gross and Net Costs. For the majority of intragovernmental sales, the AWCF's accounting systems do not capture trading partner data at the transaction level in a manner that facilitates trading partner aggregations. Therefore, the AWCF was unable to reconcile its intragovernmental expenses with its trading partners' revenues. The DoD intends to develop long-term systems improvements that will address this issue.

Note Reference

See Note 19.I, Intragovernmental Revenue and Expense

Note 19.B. Gross Cost and Earned Revenue by Budget Functional Classification

Not applicable

Note 19.C. Gross Cost to Generate Intra-governmental Revenue and Earned Revenue (Transactions with Other Federal—Non-DoD—Entities) by Budget Functional Classification

Not applicable

Note 19.D. Imputed Expenses

As of September 30 (Amounts in thousands)	2004	2003
1. Civilian (e.g. CSRS/FERS) Retirement	$56,020	$59,046
2. Civilian Health	74,612	62,086
3. Civilian Life Insurance	189	179
4. Military Retirement Pension	0	0
5. Military Retirement Health	0	0
6. Judgment Fund	0	0
7. Total Imputed Expenses	$130,821	$121,311

8. Other Information

Legend: CSRS - Civil Service Retirement System
FERS - Federal Employees Retirement System

Fluctuations and/or Abnormalities

Total Imputed Expenses increased $9,509 thousand, or 8 percent, from 4th Quarter FY 2003 to 4th Quarter FY 2004. The increase is primarily due to Civilian Health costs which increased $9,536 thousand, or 21 percent, because of pay increases and an increase in the total number of civilian employees. Federal GAAP requires the reporting of government employee benefits. The amounts remitted to the OPM by and for covered employees do not generally cover the actual cost of the benefits those employees will receive after their careers are over. As a consequence, for FY 2004, the AWCF must recognize an imputed cost equal to the difference between the true cost of providing future benefits to its employees and the employer and employee contributions they remit to the OPM.

Note 19.E. Benefit Program Expenses

Not applicable

Note 19. F. Exchange Revenue

Disclosures Related to the Exchange Revenue:

Exchange Revenue arises when a government entity provides goods and services to the public or to another government entity for a price (earned revenue). Exchange revenue includes most user charges other than taxes, such as regulatory user charges. The AWCF reported only exchange revenue in FY 2004.

Note Disclosure

See Note 1.E, Revenues and Other Financing Sources

Note 19.G. Amounts for Foreign Military Sales (FMS) Program Procurements from Contractors

Not applicable.

Note 19.H. Stewardship Assets

Not applicable.

Note 19.I. Intra-governmental Revenue and Expense

Disclosures Related to Intra-governmental Revenue and Expense:

Intragovernmental Revenue

For the majority of buyer-side transactions, the AWCF accounting systems do not capture trading partner data at the transaction level in a manner that facilitates trading partner aggregations. Therefore, the AWCF was unable to reconcile intragovernmental accounts payable balances with its trading partners. The DoD intends to develop long-term system improvements that will address this issue.

Operating Expenses

The DoD summary level seller accounts receivable and revenues were compared to the AWCF's accounts payables and expenses. As a result of this comparison, intragovernmental operating expenses were increased by $5,402,494 thousand with a corresponding decrease of $5,403,252 thousand in non-federal operating expenses in order to balance the AWCF's expenses with the DoD summary level seller revenues.

Note 19.J. Suborganization Program Costs

Not applicable

Note 20. Disclosures Related to the Statement of Changes in Net Position

As of September 30 (Amounts in thousands)	Cumulative Results of Operations 2004	Unexpended Appropriations 2004	Cumulative Results of Operations 2003	Unexpended Appropriations 2003
Prior Period Adjustments Increases (Decreases) to Net Position Beginning Balance:				
A. Changes in Accounting Standards	$0	$0	$0	$0
B. Errors and Omissions in Prior Year Accounting Reports	0	0	0	0
C. Other Prior Period Adjustments	0	0	0	0
D. Total Prior Period Adjustments	$0	$0	$0	$0
2. Imputed Financing:				
A. Civilian CSRS/FERS Retirement	$56,020	$0	$59,046	$0
B. Civilian Health	74,612	0	62,086	0
C. Civilian Life Insurance	189	0	179	0
D. Military Retirement Pension	0	0	0	0
E. Military Retirement Health	0	0	0	0
F. Judgment Fund	0	0	0	0
G. Total Imputed Financing	$130,821	$0	$121,311	$0

3. Other Information:

Legend:

CSRS – Civil Service Retirement System

FERS – Federal Employees Retirement System

Prior Period Adjustments

The Department of the Treasury emphasized the reporting of prior period adjustments for material changes only. The Office of the Under Secretary of Defense (Comptroller) (OSD(C)) and the Defense Finance and Accounting Service (DFAS) guidance also emphasized the position that use of prior period adjustments should be infrequent. Individual entities within the Army Working Capital Fund (AWCF) submitted prior period adjustments, which were subsequently reported on the AR 1307 report. These adjustments did not meet the materiality threshold established for financial statement reporting. These balances were reclassified to accounts that would have been affected if they had occurred in the current year. The net amounts of reclassified prior period adjustments for FY 2004 are as follows: (Amounts in thousands)

Depot Maintenance	($25,840)
Ordnance	1,390
Supply Management	37,725
Total AWCF	**$13,275**

Fluctuations and/or Abnormalities

Appropriations used decreased $35,876 thousand, or 13 percent, from FY 2003 to FY 2004. In FY 2003, the AWCF received $29,700 thousand more in direct appropriations and expended $6,175 thousand more of FY 2000 direct appropriations than in FY 2004.

Budgetary Financing Sources Transfers-in/out without reimbursement changed $1,448,600 thousand, or 100 percent, which reflects the following reprogramming decisions. In FY 2004, Program Budget Decision 614 transferred $41,600 thousand to the Defense Commissary Agency. Also, during the 3rd Quarter, Defense Reprogramming Action FY 04-60 IR transferred $107,000 thousand and FY 04-68 IR transferred $1,050,000 thousand to the Army General Fund. Also, Defense Reprogramming Action FY 04-81 IR transferred $250,000 thousand to the Army General Fund.

Other Budgetary Financing Sources increased by $239,821 thousand, or 375 percent, between FY 2003 and FY 2004 primarily due to the reclassification of $321,764 thousand of Transfers-In Without Reimbursement in FY 2003, versus $37,849 thousand Transfers-Out Without Reimbursement in FY 2004. This represents those transfers in/out without reimbursement without trading partner information that must be reclassified as a gain or loss.

The Other Financing Sources - Transfers-In/Out Without Reimbursement decreased by $908,589 thousand, or 100 percent, from FY 2003 to FY 2004. The FY 2003 amount includes a transfer-in of $918,816 thousand in inventory from the Army General Fund during the implementation of the Single Stock Fund Milestone 3. No inventory transfers were reported for FY 2004.

The Other Resources Other line decreased by $217,064 thousand, or 100 percent. The FY 2003 amount includes an erroneous posting in Material Returns Liability.

Net Cost of Operations decreased from FY 2003 to FY 2004 by $1,887,698 thousand, or 363 percent, due to increased sales in support of the contingency missions Operations Enduring Freedom, Iraqi Freedom, and Noble Eagle.

Appropriations received decreased from FY 2003 to FY 2004 by $29,700 thousand, or 12 percent. In FY 2004, the AWCF received direct appropriations of $105,400 thousand for war reserves and $113,900 thousand for industrial mobilization capacity, totaling $219,300 thousand. The decrease in Appropriations Received from FY 2003 to FY 2004 is due to a net difference of a $100,000 thousand inventory augmentation received in FY 2003, but not in FY 2004, and increases of $53,900 thousand in industrial mobilization capacity and $16,400 thousand in war reserves in FY 2004 over FY 2003.

Note Reference

For Additional Line Item discussion, see:

Note 19, General Disclosures Relating to the Statement of Net Cost
Note 21, Disclosures Related to the Statement of Budgetary Resources

Note 21. Disclosures Related to the Statement of Budgetary Resources

As of September 30 (Amounts in thousands)	2004	2003
1. Net Amount of Budgetary Resources Obligated for Undelivered Orders at the End of the Period	$8,600,534	$6,102,853
2. Available Borrowing and Contract Authority at the End of the Period	$4,549,857	$2,443,489

3. Other Information:

The Army Working Capital Fund (AWCF) reports all obligations as reimbursable per Office of Management and Budget (OMB) circular A-11, Section 83.5.

Primary funding for the AWCF is earned through customer orders, as described in Note 1.C. In addition to revenues earned, appropriations were received and used by the following business areas during FY 2004: (Amounts in thousands)

Business Area	Appropriations Received	Appropriations Obligated
Ordnance	$94,162	$94,162
Depot Maintenance	19,738	19,738
Supply Management	117,307	117,307
Information Services	0	0
Total AWCF	**$231,207**	**$231,207**

In FY 2004, funds were appropriated for war reserves, $105,400 thousand, and industrial mobilization capacity, $113,900 thousand, totaling $219,300 thousand. All FY 2004 appropriations received have been obligated and expended.

Available contract authority as of September 30, 2004, is as follows: (Amounts in thousands)

Business Area	Unused Contract Authority as of September 30, 2003	Contract Authority Realized For FY 2004	Contract Authority Available as of September 30, 2004
Depot Maintenance	$10,663	$6,450	$17,113
Ordnance	7,007	9,575	16,582
Supply Management	2,425,819	2,090,343	4,516,162
Information Services	0	0	0
Total AWCF	**$2,443,489**	**$2,106,368**	**$4,549,857**

Unobligated balances from spending authority from offsetting collections (revenues earned) as of September 30, 2004, are as follows: (Amounts in thousands)

Business Area	Earned	Change in Unfilled Orders	Anticipated	Total Spending Authority from Offsetting Collections
Depot Maintenance	$2,676,243	($112,060)	$0	$2,564,183
Ordnance	876,583	(88,624)	0	787,959
Supply	8,665,919	77,035	0	8,742,954
Information Services	(6,660)	(22,498)	0	(29,158)
Total AWCF	**$12,212,085**	**($146,147)**	**$0**	**$12,065,938**

Fluctuations and/or Abnormalities

The AWCF received direct appropriations of $105,400 thousand for war reserves and $113,900 thousand received for industrial mobilization capacity, totaling $219,300 thousand. The decrease in Appropriations Received from FY 2003 to FY 2004 is due to a net difference of a $100,000 thousand inventory augmentation received in FY 2003, but not in FY 2004 and increases of $53,900 thousand in industrial mobilization capacity and $16,400 thousand in war reserves in FY 2004 over FY 2003.

All business activity increased during FY 2004 over this same period in FY 2003 due to increased reimbursable activity with the Army General Fund, as well as within the AWCF, in support of the contingency missions Operations Enduring Freedom, Iraqi Freedom, and Noble Eagle. Contract authority increased $2,038,741 thousand, or 3,015 percent, primarily to buy spares to support increased maintenance efforts in support of the contingency missions Operations Enduring Freedom, Iraqi Freedom, and Noble Eagle.

Net transfers changed $1,448,600 thousand, or 100 percent, from FY 2003 to FY 2004. During the 2nd Quarter FY 2004, Program Budget Decision 614 transferred $41,600 thousand to the Defense Commissary Agency. Also, during the 3rd Quarter FY 2004, Defense Reprogramming Action FY 04-60 transferred $107,000 thousand and FY 04-68 IR transferred $1,050,000 thousand to the Army General Fund. In 4th Quarter 2004, Defense Reprogramming Action FY 04-81 IR transferred $250,000 thousand to the Army General Fund.

Spending Authority from Offsetting Collections increased $13,547 thousand, or less than 1 percent, in FY 2004. This increase occurred primarily within the Supply Management business area, because of increased demand from the Army General Fund to replenish supplies and repair equipment, as noted below:

Earned - Collected increased by $2,621,557 thousand, or 27 percent, in FY 2004.

Earned - Receivable from Federal Sources decreased by $289,951 thousand, or 123 percent, in FY 2004.

Change in Unfilled Customer Orders – Advance Received increased by $161,993 thousand, or 90 percent, from FY 2003 to FY 2004. The change is due to the repayment in FY 2003 of an advance given by the Army General Fund to supplement cash shortages experienced during FY 2002.

Change in Unfilled Customer Orders – Without Advance from Federal Sources decreased by $2,480,052 thousand, or 105 percent, in FY 2004.

Recoveries of Prior Year Obligations decreased by $88,226 thousand, or 15 percent, from FY 2003 to FY 2004. The decrease is primarily due to the Army Materiel Command performing a review and clean up of unliquidated obligations in FY 2003, prior to the transition to LMP.

Direct Obligations incurred decreased by $249,028 thousand, or 100 percent, from FY 2003 to FY 2004. The decrease is a result of a reporting change. Previously, the AWCF reported obligations as both direct and reimbursable. Beginning 2nd Quarter FY 2004 all obligations are reported as reimbursable per OMB circular A-11, Section 83.5.

Reimbursable obligations increased by $1,683,709 thousand, or 14 percent, primarily in the Supply Management business area due to increased sales in support of the contingency missions Operations Enduring Freedom, Iraqi Freedom, and Noble Eagle.

Unobligated Balance, Apportioned decreased by $563,463 thousand, or 27 percent, in FY 2004, as the AWCF obligated projects in FY 2004 from FY 2003 reimbursable orders.

Accounts Receivable decreased $53,777 thousand, or 10 percent, as a result of the AWCF writing-off $39,041 thousand in unsupported undistributed collections based on guidance from the Office of the Under Secretary of Defense (Comptroller).

Undelivered Orders increased $2,249,580 thousand, or 37 percent, primarily for the Supply Management business area. The increase is due to increased demand in support of the contingency missions Operations Enduring Freedom, Iraqi Freedom, and Noble Eagle.

Accounts Payable decreased $362,509 thousand, or 37 percent. This decrease is due to the AWCF payment in FY 2004 of FY 2003 transportation costs of $322,310 thousand from the Defense Logistics Agency.

Net Outlays increased by $419,274 thousand, or 40 percent, in FY 2004. This is a reflection of the Full Cost Recovery included in the setting of FY 2004 rates and the increased sales in support of the contingency missions Operations Enduring Freedom, Iraqi Freedom, and Noble Eagle. Rates were set to recover all costs in FY 2004, therefore the percentage of collections as compared to disbursements increased over FY 2003.

Other Disclosures

The AWCF does not make eliminating entries in the Statement of Budgetary Resources because the statements are presented as combined and combining and, therefore, are presented as a Disaggregated Statement of Budgetary Resources in the Required Supplementary Information section of the financial statements.

Adjustments in funds that are temporarily not available pursuant to Public Law, and those that are permanently not available, are not included in the Spending Authority From Offsetting Collections and Adjustments line on the Statement of Budgetary Resources or the Spending Authority for Offsetting Collections and Adjustments line on the Statement of Financing.

AWCF had reimbursable obligations for apportionment category B of $14,006,202 thousand and $0 of obligations exempt from apportionment.

The Statement of Budgetary Resources does not eliminate for intragovernmental receivables, nor does it include contractor debt or refunds receivable.

Accounts payable on the Statement of Budgetary Resources includes the employee payroll liability and does not eliminate for intragovernmental payables. The Balance Sheet eliminates for intragovernmental payables and reports the employee payroll liability in Other Liabilities. This results in different balances between the Statement of Budgetary Resources and the Balance Sheet.

The AWCF contains obligation and unliquidated obligation values that were migrated to the LMP at values higher than what was reported in the respective legacy systems at time of migration. This overstatement occurred at the Supply Management activities for the Communication-Electronics Command and Tobyhanna Army Depot. The Defense Finance and Accounting Service and Army Materiel Command are working to reconcile these balances.

Note Reference

For Additional Line Item discussion, see:
Note 1, Significant Accounting Policies
Note 5, Accounts Receivable
Note 12, Accounts Payable
Note 18, Unexpended Appropriations
Note 19, General Disclosures Related to the Statement of Net Cost

Note 22. Disclosures Related to the Statement of Financing

Disclosures Related to the Statement of Financing:

The objective of the Statement of Financing is to allow users to understand the difference between the Statement of Budgetary Resources and the Statement of Net Cost. The statement provides this understanding through a comprehensive reconciliation process.

The Army Working Capital Fund's (AWCF) budgetary data does not agree with its proprietary expenses and assets capitalized. This results in a difference in net cost between the Statement of Net Cost and the Statement of Financing. Resources that finance the acquisition of assets were decreased by $356,731 thousand to bring the statements into agreement. The differences between budgetary and proprietary data for the AWCF were reported as material weaknesses in the FY 2003 AWCF's financial statement report.

Fluctuations and/or Abnormalities

Obligations incurred increased by $1,434,681 thousand, or 11 percent, from FY 2003 and FY 2004 due to increased demand from customers and increased contract authority in support of the contingency missions Operations Enduring Freedom, Iraqi Freedom, and Noble Eagle.

Obligations net of offsetting collections and recoveries increased $1,509,358 thousand, or 2,193 percent, from FY 2003 to FY 2004 due to increased demand from customers and increased contract authority in support of the contingency missions Operations Enduring Freedom, Iraqi Freedom, and Noble Eagle.

The Transfers-In/Out Without Reimbursement decreased by $908,589 thousand, or 100 percent, from FY 2003 to FY 2004. The FY 2003 amount includes a transfer-in of $918,816 thousand in inventory from the Army General Fund during the implementation of the Single Stock Fund Milestone 3. No inventory transfers were reported for FY 2004.

The Budgetary Resources Obligated - Other line decreased by $217,064 thousand, or 100 percent from FY 2003 to FY 2004. The FY 2003 amount includes an erroneous posting in Material Returns Liability.

Change in Undelivered Orders increased $803,752, or 24 percent, from FY 2003 to FY 2004. This is a result of continued increased demand in Supply Management for inventory requisitions.

Change in Unfilled Customer Orders decreased from FY 2003 to FY 2004 by $2,318,058 thousand, or 107 percent. The FY 2003 amount reflected increased operations in anticipation of the contingency missions Operations Enduring Freedom, Iraqi Freedom, and Noble Eagle. The FY 2004 Change in Unfilled Customer Orders reflects a stabilization of operations.

Resources that Fund Expenses Recognized in Prior Periods changed $20,572 thousand, or 744 percent, from FY 2003 to FY 2004. The majority of this change is from a decrease in the Unfunded Leave Liability and a decrease in the FECA liability.

Resources that Finance the Acquisition of Assets decreased by $5,890,330 thousand, or 1,817 percent, from FY 2003 to FY 2004. An accounting procedure change to more accurately report capitalized purchases caused this decrease. Memorandum accounts were added to capture the capitalized costs during the year.

Other resources or adjustments to net obligated resources that do not affect net cost of operations Other increased $6,872 thousand, or 100 percent, from FY 2003 to FY 2004 to bring the Statement of Financing into agreement with the Statement of Budgetary Resources for the Information Services business area.

Increase in Annual Leave Liability decreased by $619 thousand, or 31 percent, from FY 2003 to FY 2004. The Annual Leave reported at the end of FY 2003 showed accruals from June to September only. The additional increase is a result of posting the beginning leave balances that were dropped upon implementation of the Logistics Modernization Program (LMP) in FY 2003.

The Increase in Exchange Revenue Receivable From the Public changed $6,079 thousand, or 100 percent, from FY 2003 to FY 2004. The zero balance in FY 2004 indicates that there was a decrease in total Public Receivables incurred in FY 2004.

Other (+/-) reflects a $16,294 thousand, or 99 percent, decrease from FY 2003 to FY 2004. Decreases in employee benefit liabilities should be recorded on Resources that Fund Expenses Recognized in Prior Periods. The balance reflected for FY 2003 was reported on the Other line.

Depreciation and Amortization decreased by $111,184 thousand, or 57 percent, from FY 2003 to FY 2004 primarily in the Depot Maintenance and Ordnance business areas. The FY 2003 balance includes depreciation expense which was previously reported as unfunded and, therefore, not included on the financial statements.

Revaluation of Assets or Liabilities increased from FY 2003 to FY 2004 by $706,004 thousand, or 157 percent, from increased inventory valuation adjustments for Supply Management activities. The Army and the Defense Finance and Accounting Service continue to monitor inventory values reported by LMP.

Other Cost of Goods Sold increased $5,003,845 thousand, or 100 percent, from FY 2003 to FY 2004. An accounting procedure change to more accurately report cost of goods sold caused this increase. This line was added in FY 2004 and any amounts were previously included on the Resources that finance the acquisition of assets line.

Components Not Requiring or Generating Resources Other Other decreased from FY 2003 to FY 2004 by $440,090 thousand, or 100 percent. The FY 2004 amount reflects the first time use of the Cost Capitalization general ledger account for Tobyhanna Army Depot of $453,005 thousand, Allowance for Uncollectible Accounts Receivable of $12,957 thousand, and a closing entry for Information Services of $6,871 thousand. Information Services business area transferred to the Army General Fund as of October 1, 2003, but some residual balances remain on the books, reported by the Supply Management business area. No allowance for uncollectible accounts receivable was recorded in the past.

Net Cost of Operations decreased in FY 2004 by $1,887,698 thousand, or 363 percent, from FY 2003 to FY 2004 due to increased sales in support of the contingency missions Operations Enduring Freedom, Iraqi Freedom, and Noble Eagle.

Other Disclosures

Transactions within the AWCF have not been eliminated because the statements are presented as combined and combining.

Note Reference

For Additional Line Item discussion, see:
Note 10, General PP&E
Note 11, Liabilities Not Covered by Budgetary Resources
Note 18, Unexpended Appropriations
Note 19, General Disclosures Relating to the Statement of Net Cost
Note 21, Disclosures Related to the Statement of Budgetary Resources

Note 23. Disclosures Related to the Statement of Custodial Activity

Not applicable.

Note 24.A. Other Disclosures

Not applicable

Note 24.B. Other Disclosures

Not applicable

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Department of Defense- Army Working Capital Fund

CONSOLIDATING BALANCE SHEET

As of September 30, 2004 and 2003 ($ in Thousands)

	Depot Maintenance	Supply Management	Information Service
ASSETS (Note 2)			
Intragovernmental:			
Fund Balance with Treasury (Note 3)			
Entity	$128,582	($772,617)	$0
Non-Entity Seized Iraqi Cash	0	0	0
Non-Entity-Other	0	0	0
Investments (Note 4)	0	0	0
Accounts Receivable (Note 5)	150,963	263,272	0
Other Assets (Note 6)	16,900	29,460	0
Total Intragovernmental Assets	$296,445	($479,885)	$0
Cash and Other Monetary Assets (Note 7)	$0	$0	$0
Accounts Receivable (Note 5)	699	10,996	0
Loans Receivable (Note 8)	0	0	0
Inventory and Related Property (Note 9)	240,124	13,620,258	0
General Property, Plant and Equipment (Note 10)	527,153	83,346	0
Investments (Note 4)	0	0	0
Other Assets (Note 6)	48	264,352	0
TOTAL ASSETS	$1,064,469	$13,499,067	$0
LIABILITIES (Note 11)			
Intragovernmental:			
Accounts Payable (Note 12)	$51,536	$93,869	$0
Debt (Note 13)	0	0	0
Environmental Liabilities (Note 14)	0	0	0
Other Liabilities (Note 15 & Note 16)	30,508	53,333	0
Total Intragovernmental Liabilities	$82,044	$147,202	$0
Accounts Payable (Note 12)	$128,715	$193,768	$0
Military Retirement Benefits and Other Employment-Related Actuarial Liabilities (Note 17)	177,507	0	0
Environmental Liabilities (Note 14)	0	0	0
Loan Guarantee Liability (Note 8)	0	0	0
Other Liabilities (Note 15 and Note 16)	93,848	69,131	0
Debt Held by Public	0	0	0
TOTAL LIABILITIES	$482,114	$410,101	$0
NET POSITION			
Unexpended Appropriations (Note 18)	$0	$53	$0
Cumulative Results of Operations	582,355	13,088,913	0
TOTAL NET POSITION	$582,355	$13,088,966	$0
TOTAL LIABILITIES AND NET POSITION	$1,064,469	$13,499,067	$0

Ordnance	Component Level	Combined Total	Eliminations	2004 Consolidated	2003 Consolidated
$42,560	$1,549,938	$948,463	$0	$948,463	$1,548,546
0	0	0	0	0	0
0	0	0	0	0	0
0	0	0	0	0	0
34,752	(4,064)	444,923	0	444,923	411,254
615	(46,896)	79	0	79	329
$77,927	$1,498,978	$1,393,465	$0	$1,393,465	$1,960,129
$0	$0	$0	$0	$0	$0
1,787	0	13,482	0	13,482	31,176
0	0	0	0	0	0
56,290	0	13,916,672	0	13,916,672	12,131,811
288,939	0	899,438	0	899,438	926,751
0	0	0	0	0	0
722	0	265,122	0	265,122	269,877
$425,665	$1,498,978	$16,488,179	$0	$16,488,179	$15,319,744
$20,099	($6,354)	$159,150	$0	$159,150	$435,586
0	0	0	0	0	0
0	0	0	0	0	0
31,474	(47,655)	67,660	0	67,660	94,499
$51,573	($54,009)	$226,810	$0	$226,810	$530,085
$45,034	$4,537	$372,054	$0	$372,054	$342,365
127,469	0	304,976	0	304,976	320,654
0	0	0	0	0	0
0	0	0	0	0	0
51,327	(854)	213,452	0	213,452	231,004
0	0	0	0	0	0
$275,403	($50,326)	$1,117,292	$0	$1,117,292	$1,424,108
$0	$0	$53	$0	$53	$11,960
150,262	1,549,304	15,370,834	0	15,370,834	13,883,676
$150,262	$1,549,304	$15,370,887	$0	$15,370,887	$13,895,636
$425,665	$1,498,978	$16,488,179	$0	$16,488,179	$15,319,744

Department of Defense- Army Working Capital Fund

CONSOLIDATING STATEMENT OF NET COST

As of September 30, 2004 and 2003 ($ in Thousands)

Program Costs	Combined Total	Eliminations	2004 Consolidated	2003 Consolidated
A. Component Level				
Intragovernmental Gross Costs	$2,112,347	$0	$2,112,347	($4,454,511)
(Less: Intragovernmental Earned Revenue)	3,290,147	0	3,290,147	1,476,501
Intragovernmental Net Costs	$5,402,494	$0	$5,402,494	($2,978,010)
Gross Costs With the Public	($5,375,497)	$0	($5,375,497)	$3,013,542
(Less: Earned Revenue From the Public)	0	0	0	0
Net Costs With the Public	($5,375,497)	$0	($5,375,497)	$3,013,542
Total Net Cost	$26,997	$0	$26,997	$35,532
B. Depot Maintenance				
Intragovernmental Gross Costs	$271,082	$0	$271,082	$561,486
(Less: Intragovernmental Earned Revenue)	(2,653,482)	0	(2,653,482)	(1,997,588)
Intragovernmental Net Costs	($2,382,400)	$0	($2,382,400)	($1,436,102)
Gross Costs With the Public	$4,195,038	$0	$4,195,038	$1,532,077
(Less: Earned Revenue From the Public)	(1,917,228)	0	(1,917,228)	(36,285)
Net Costs With the Public	$2,277,810	$0	$2,277,810	$1,495,792
Total Net Cost	($104,590)	$0	($104,590)	$59,690
C. Information Service				
Intragovernmental Gross Costs	$0	$0	$0	$4,278
(Less: Intragovernmental Earned Revenue)	0	0	0	(96,444)
Intragovernmental Net Costs	$0	$0	$0	($92,166)
Gross Costs With the Public	$0	$0	$0	$86,500
(Less: Earned Revenue From the Public)	0	0	0	0
Net Costs With the Public	$0	$0	$0	$86,500
Total Net Cost	$0	$0	$0	($5,666)

D. Ordnance	Combined Total	Eliminations	2004 Consolidated	2003 Consolidated
Intragovernmental Gross Costs	$78,288	$0	$78,288	$54,744
(Less: Intragovernmental Earned Revenue)	(847,632)	0	(847,632)	(687,834)
Intragovernmental Net Costs	($769,344)	$0	($769,344)	($633,090)
Gross Costs With the Public	$1,156,340	$0	$1,156,340	$794,785
(Less: Earned Revenue From the Public)	(223,173)	0	(223,173)	(23,831)
Net Costs With the Public	$933,167	$0	$933,167	$770,954
Total Net Cost	$163,823	$0	$163,823	$137,864
E. Supply Management				
Intragovernmental Gross Costs	$386,277	$0	$386,277	$6,485,520
(Less: Intragovernmental Earned Revenue)	(8,245,086)	0	(8,245,086)	(8,978,526)
Intragovernmental Net Costs	($7,858,809)	$0	($7,858,809)	($2,493,006)
Gross Costs With the Public	$8,185,418	$0	$8,185,418	$1,907,127
(Less: Earned Revenue From the Public)	(2,810,651)	0	(2,810,651)	(161,971)
Net Costs With the Public	$5,374,767	$0	$5,374,767	$1,745,156
Total Net Cost	($2,484,042)	$0	($2,484,042)	($747,850)
F. Total Program Costs				
Intragovernmental Gross Costs	$2,847,994	$0	$2,847,994	$2,651,517
(Less: Intragovernmental Earned Revenue)	(8,456,053)	0	(8,456,053)	(10,283,891)
Intragovernmental Net Costs	($5,608,059)	$0	($5,608,059)	($7,632,374)
Gross Costs With the Public	$8,161,299	$0	$8,161,299	$7,334,031
(Less: Earned Revenue From the Public)	(4,951,052)	0	(4,951,052)	(222,087)
Net Costs With the Public	$3,210,247	$0	$3,210,247	$7,111,944
Total Net Cost	($2,397,812)	$0	($2,397,812)	($520,430)
Cost Not Assigned to Programs	$0	$0	$0	$0
(Less: Earned Revenue Not Attributable to Programs)	0	0	0	0
Net Cost of Operations	($2,397,812)	$0	($2,397,812)	($520,430)

Department of Defense- Army Working Capital Fund

CONSOLIDATING STATEMENT OF CHANGES IN NET POSITION

As of September 30, 2004 and 2003 ($ in Thousands)

	Depot Maintenance	Supply Management	Information Service
CUMULATIVE RESULTS OF OPERATIONS			
Beginning Balances	$338,406	$13,226,131	($739)
Prior period adjustments (+/-)			
Prior Period Adjustments - Restated (+/-)	0	0	0
Beginning Balance, Restated	338,406	13,226,131	(739)
Prior Period Adjustments - Not Restated (+/-)	0	0	0
Beginning Balances, as adjusted	$338,406	$13,226,131	($739)
Budgetary Financing Sources:			
Appropriations received	0	0	0
Appropriations transferred-in/out (+/-)	0	0	0
Other adjustments (rescissions, etc) (+/-)	0	0	0
Appropriations used	19,738	117,307	0
Nonexchange revenue	0	0	0
Donations and forfeitures of cash and cash equivalents	0	0	0
Transfers-in/out without reimbursement (+/-)	0	(1,448,600)	0
Other budgetary financing sources (+/-)	1,701	146,276	0
Other Financing Sources:			
Donations and forfeitures of property	0	0	0
Transfers-in/out without reimbursement (+/-)	33,497	(1,454,505)	739
Imputed financing from costs absorbed by others	84,424	18,263	0
Other (+/-)	0	0	0
Total Financing Sources	$139,360	($2,621,259)	$739
Net Cost of Operations (+/-)	(104,590)	(2,484,042)	0
Ending Balances	$582,356	$13,088,914	$0
UNEXPENDED APPROPRIATIONS			
Beginning Balances	$0	$11,960	$0
Prior period adjustments (+/-)			
Prior Period Adjustments - Restated (+/-)	0	0	0
Beginning Balance, Restated	0	11,960	0
Prior Period Adjustments - Not Restated (+/-)	0	0	0
Beginning Balances, as adjusted	$0	$11,960	$0
Budgetary Financing Sources:			
Appropriations received	19,738	105,400	0
Appropriations transferred-in/out (+/-)	0	0	0
Other adjustments (rescissions, etc) (+/-)	0	0	0
Appropriations used	(19,738)	(117,307)	0
Nonexchange revenue	0	0	0
Donations and forfeitures of cash and cash equivalents	0	0	0
Transfers-in/out without reimbursement (+/-)	0	0	0
Other budgetary financing sources (+/-)	0	0	0
Other Financing Sources:			
Donations and forfeitures of property	0	0	0
Transfers-in/out without reimbursement (+/-)	0	0	0
Imputed financing from costs absorbed by others	0	0	0
Other (+/-)	0	0	0
Total Financing Sources	$0	($11,907)	$0
Net Cost of Operations (+/-)	0	0	0
Ending Balances	$0	$53	$0

Ordnance	Component Level	Combined Total	Eliminations	2004 Consolidated	2003 Consolidated
($2,501)	$322,379	$13,883,676	$0	$13,883,676	$11,913,102
0	0	0	0	0	0
(2,501)	322,379	13,883,676	0	13,883,676	11,913,102
0	0	0	0	0	0
($2,501)	$322,379	$13,883,676	$0	$13,883,676	$11,913,102
0	0	0	0	0	0
0	0	0	0	0	0
0	0	0	0	0	0
94,162	0	231,207	0	231,207	267,083
0	0	0	0	0	0
0	0	0	0	0	0
0	0	(1,448,600)	0	(1,448,600)	0
16,626	11,315	175,918	0	175,918	(63,903)
0	0	0	0	0	0
177,664	1,242,605	0	0	0	908,588
28,134	0	130,821	0	130,821	121,312
0	0	0	0	0	217,064
$316,586	$1,253,920	($910,654)	$0	($910,654)	$1,450,144
163,823	26,997	(2,397,812)	0	(2,397,812)	(520,430)
$150,262	$1,549,302	$15,370,834	$0	$15,370,834	$13,883,676
$0	$0	$11,960	$0	$11,960	$30,043
0	0	0	0	0	0
0	0	11,960	0	11,960	30,043
0	0	0	0	0	0
$0	$0	$11,960	$0	$11,960	$30,043
94,162	0	219,300	0	219,300	249,000
0	0	0	0	0	0
0	0	0	0	0	0
(94,162)	0	(231,207)	0	(231,207)	(267,083)
0	0	0	0	0	0
0	0	0	0	0	0
0	0	0	0	0	0
0	0	0	0	0	0
0	0	0	0	0	0
0	0	0	0	0	0
0	0	0	0	0	0
0	0	0	0	0	0
$0	$0	($11,907)	$0	($11,907)	($18,083)
0	0	0	0	0	0
$0	$0	$53	$0	$53	$11,960

Department of Defense- Army Working Capital Fund

COMBINING STATEMENT OF BUDGETARY RESOURCES

As of September 30, 2004 and 2003 ($ in Thousands)

	Depot Maintenance	Supply Management	Information Service
BUDGETARY FINANCING ACCOUNTS			
BUDGETARY RESOURCES			
Budget Authority:			
Appropriations received	$19,738	$105,400	$0
Borrowing authority	0	0	0
Contract authority	6,450	2,090,343	0
Net transfers (+/-)	0	(1,448,600)	0
Other	0	0	0
Unobligated balance:			
Beginning of period	1,339,455	23,667	14,119
Net transfers, actual (+/-)	0	19,104	(19,104)
Anticipated Transfers Balances	0	0	0
Spending authority from offsetting collections:			
Earned	0	0	0
Collected	2,683,117	8,647,506	(24)
Receivable from Federal sources	(6,875)	18,413	(6,636)
Change in unfilled customer orders	0	0	0
Advance received	(22,752)	8,079	24
Without advance from Federal sources	(89,307)	68,956	(22,522)
Anticipated for the rest of year, without advances	0	0	0
Transfers from trust funds	0	0	0
Subtotal	$2,564,183	$8,742,954	($29,158)
Recoveries of prior year obligations	7,587	452,252	34,143
Temporarily not available pursuant to Public Law	0	0	0
Permanently not available	0	0	0
Total Budgetary Resources	$3,937,413	$9,985,120	$0
STATUS OF BUDGETARY RESOURCES			
Obligations incurred:			
Direct	$0	$0	$0
Reimbursable	3,053,586	9,869,905	0
Subtotal	3,053,586	9,869,905	0
Unobligated balance:			
Apportioned	883,827	115,215	0
Exempt from apportionment	0	0	0
Other available	0	0	0
Unobligated Balances Not Available	0	0	0
Total, Status of Budgetary Resources	$3,937,413	$9,985,120	$0
Relationship of Obligations to Outlays:			
Obligated Balance, Net - beginning of period	($672,329)	$3,034,607	$4,986
Obligated Balance transferred, net (+/-)	0	0	0
Obligated Balance, Net - end of period:			
Accounts receivable	(151,479)	(273,969)	0
Unfilled customer order from Federal sources	(1,102,794)	(2,917,175)	0
Undelivered orders	938,897	7,173,522	0
Accounts payable	233,707	297,510	0
Outlays:			
Disbursements	2,551,521	8,085,003	0
Collections	(2,660,365)	(8,655,586)	0
Subtotal	($108,844)	($570,583)	$0
Less: Offsetting receipts	0	0	0
Net Outlays	($108,844)	($570,583)	$0

Ordnance	Component Level	2004 Combined	2003 Combined
$94,162	$0	$219,300	$249,000
0	0	0	0
9,575	0	2,106,368	67,627
0	0	(1,448,600)	0
0	0	0	0
616,463	99,999	2,093,703	1,708,247
0	0	0	0
0	0	0	0
0	0	0	0
897,075	38,186	12,265,860	9,644,303
(20,492)	(38,186)	(53,776)	236,175
0	0	0	0
(2,597)	0	(17,246)	(179,239)
(86,027)	0	(128,900)	2,351,152
0	0	0	0
0	0	0	0
$787,959	$0	$12,065,938	$12,052,391
5,751	0	499,733	587,959
0	0	0	0
0	0	0	0
$1,513,910	$99,999	$15,536,442	$14,665,224
$0	$0	$0	$249,028
1,019,425	63,286	14,006,202	12,322,493
1,019,425	63,286	14,006,202	12,571,521
494,485	36,714	1,530,241	2,093,704
0	0	0	0
0	(1)	(1)	(1)
0	0	0	0
$1,513,910	$99,999	$15,536,442	$14,665,224
($405,646)	($63,286)	$1,898,332	$918,667
0	0	0	0
(36,300)	(854)	(462,602)	(516,379)
(502,744)	0	(4,522,713)	(4,651,613)
222,235	0	8,334,654	6,085,073
85,277	2,247	618,741	981,250
946,079	36,794	11,619,397	8,416,571
(894,477)	(38,186)	(12,248,614)	(9,465,064)
$51,602	($1,392)	($629,217)	($1,048,493)
0	0	0	0
$51,602	($1,392)	($629,217)	($1,048,493)

Department of Defense- Army Working Capital Fund

COMBINING STATEMENT OF FINANCING

As of September 30, 2004 and 2003 ($ in Thousands)

	Depot Maintenance	Supply Management
Resources Used to Finance Activities:		
Budgetary Resources Obligated		
Obligations incurred	$3,053,586	$9,869,905
Less: Spending authority from offsetting collections and recoveries (-)	(2,571,769)	(9,195,206)
Obligations net of offsetting collections and recoveries	$481,817	$674,699
Less: Offsetting receipts (-)	0	0
Net obligations	$481,817	$674,699
Other Resources		
Donations and forfeitures of property	0	0
Transfers in/out without reimbursement (+/-)	33,497	(1,454,506)
Imputed financing from costs absorbed by others	84,424	18,263
Other (+/-)	0	0
Net other resources used to finance activities	$117,921	($1,436,243)
Total resources used to finance activities	$599,738	($761,544)
Resources Used to Finance Items not Part of the Net Cost of Operations		
Change in budgetary resources obligated for goods, services and benefits ordered but not yet provided		
Undelivered Orders (-)	($491,392)	($1,957,052)
Unfilled Customer Orders	(112,060)	77,035
Resources that fund expenses recognized in prior periods	(12,810)	(2,779)
Budgetary offsetting collections and receipts that do not affect net cost of operations	0	0
Resources that finance the acquisition of assets	(1,238,424)	(4,816,700)
Other resources or adjustments to net obligated resources that do not affect net cost of operations		
Less: Trust or Special Fund Receipts Related to Exchange in the Entity's Budget (-)	0	0
Other (+/-)	(33,497)	1,454,506
Total resources used to finance items not part of the net cost of operations	($1,888,183)	($5,244,990)
Total resources used to finance the net cost of operations	($1,288,445)	($6,006,534)
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:		
Increase in annual leave liability	$0	$0
Increase in environmental and disposal liability	0	0
Upward/Downward reestimates of credit subsidy expense (+/-)	0	0
Increase in exchange revenue receivable from the the public (-)	0	0
Other (+/-)	0	0
Total components of Net Cost of Operations that will require or generate resources in future periods	$0	$0
Components not Requiring or Generating Resources:		
Depreciation and amortization	23,519	41,292
Revaluation of assets or liabilities (+/-)	(39,833)	251,083
Other (+/-)		
Trust Fund Exchange Revenue	0	0
Cost of Goods Sold	1,652,791	3,218,449
Operating Material & Supplies Used	0	0
Other	(452,619)	11,666
Total components of Net Cost of Operations that will not require or generate resources	$1,183,858	$3,522,490
Total components of net cost of operations that will not require or generate resources in the current period	$1,183,858	$3,522,490
Net Cost of Operations	($104,587)	($2,484,044)

Information Service	Ordnance	Component Level	2004 Combined	2003 Combined
$0	$1,019,425	$63,286	$14,006,202	$12,571,521
(4,986)	(793,710)	0	(12,565,671)	(12,640,348)
($4,986)	$225,715	$63,286	$1,440,531	($68,827)
0	0	0	0	0
($4,986)	$225,715	$63,286	$1,440,531	($68,827)
0	0	0	0	0
739	177,664	1,242,606	0	908,589
0	28,134	0	130,821	121,312
0	0	0	0	217,064
$739	$205,798	$1,242,606	$130,821	$1,246,965
($4,247)	$431,513	$1,305,892	$1,571,352	$1,178,138
$20,612	($33,559)	($36,290)	($2,497,681)	($3,301,433)
(22,498)	(88,624)	0	(146,147)	2,171,911
0	(7,748)	0	(23,337)	(2,765)
0	0	0	0	0
0	(159,425)	0	(6,214,549)	(324,219)
0	0	0	0	0
6,133	(177,664)	(1,242,606)	6,872	0
$4,247	($467,020)	($1,278,896)	($8,874,842)	($1,456,506)
$0	($35,507)	$26,996	($7,303,490)	($278,368)
$0	$1,376	$0	$1,376	$1,995
0	0	0	0	0
0	0	0	0	0
0	0	0	0	(6,079)
0	172	0	172	16,466
$0	$1,548	$0	$1,548	$12,382
0	18,098	0	82,909	194,093
0	46,218	0	257,468	(448,537)
0	0	0	0	0
0	132,605	0	5,003,845	0
0	0	0	0	0
0	861	0	(440,092)	0
$0	$197,782	$0	$4,904,130	($254,444)
$0	$199,330	$0	$4,905,678	($242,062)
$0	$163,823	$26,996	($2,397,812)	($520,430)

Department of Defense- Army Working Capital Fund

STATEMENT OF DISAGGREGATED BUDGETARY RESOURCES

As of September 30, 2004 and 2003 ($ in Thousands)

BUDGETARY RESOURCES	Working Capital Funds	2004 Combined	2003 Combined
Budgetary Financing Accounts			
Budget Authority:			
Appropriations received	$219,300	$219,300	$249,000
Borrowing authority	0	0	0
Contract authority	2,106,368	2,106,368	67,627
Net transfers (+/-)	(1,448,600)	(1,448,600)	0
Other	0	0	0
Unobligated balance:			
Beginning of period	2,093,704	2,093,703	1,708,247
Net transfers, actual (+/-)	0	0	0
Anticipated Transfers Balances	0	0	0
Spending authority from offsetting collections:			
Earned	0	0	0
Collected	12,265,860	12,265,860	9,644,303
Receivable from Federal sources	(53,776)	(53,776)	236,175
Change in unfilled customer orders	0	0	0
Advance received	(17,247)	(17,246)	(179,239)
Without advance from Federal sources	(128,900)	(128,900)	2,351,152
Anticipated for the rest of year, without advances	0	0	0
Transfers from trust funds	0	0	0
Subtotal	$12,065,937	$12,065,938	$12,052,391
Recoveries of prior year obligations	499,733	499,733	587,959
Temporarily not available pursuant to Public Law	0	0	0
Permanently not available	0	0	0
Total Budgetary Resources	$15,536,442	$15,536,442	$14,665,224
STATUS OF BUDGETARY RESOURCES			
Obligations incurred:			
Direct	$0	$0	$249,028
Reimbursable	14,006,201	14,006,202	12,322,493
Subtotal	14,006,201	14,006,202	12,571,521
Unobligated balance:			
Apportioned	1,530,241	1,530,241	2,093,704
Exempt from apportionment	0	0	0
Other available	0	(1)	(1)
Unobligated Balances Not Available	0	0	0
Total, Status of Budgetary Resources	$15,536,442	$15,536,442	$14,665,224
Relationship of Obligations to Outlays:			
Obligated Balance, Net - beginning of period	$1,898,332	$1,898,332	$918,667
Obligated Balance transferred, net (+/-)	0	0	0
Obligated Balance, Net - end of period:			
Accounts receivable	(462,602)	(462,602)	(516,379)
Unfilled customer order from Federal sources	(4,522,713)	(4,522,713)	(4,651,613)
Undelivered orders	8,334,654	8,334,654	6,085,073
Accounts payable	618,741	618,741	981,250
Outlays:			
Disbursements	11,619,396	11,619,397	8,416,571
Collections	(12,248,614)	(12,248,614)	(9,465,064)
Subtotal	($629,218)	($629,217)	($1,048,493)
Less: Offsetting receipts	0	0	0
Net Outlays	($629,218)	($629,217)	($1,048,493)

BUDGETARY RESOURCES	Working Capital Funds	2004 Combined	2003 Combined
Non-Budgetary Financing Accounts			
Budget Authority:			
Appropriations received	$0	$0	$0
Borrowing authority	0	0	0
Contract authority	0	0	0
Net transfers (+/-)	0	0	0
Other	0	0	0
Unobligated balance:			
Beginning of period	0	0	0
Net transfers, actual (+/-)	0	0	0
Anticipated Transfers Balances	0	0	0
Spending authority from offsetting collections:			
Earned	0	0	0
Collected	0	0	0
Receivable from Federal sources	0	0	0
Change in unfilled customer orders	0	0	0
Advance received	0	0	0
Without advance from Federal sources	0	0	0
Anticipated for the rest of year, without advances	0	0	0
Transfers from trust funds	0	0	0
Subtotal	$0	$0	$0
Recoveries of prior year obligations	0	0	0
Temporarily not available pursuant to Public Law	0	0	0
Permanently not available	0	0	0
Total Budgetary Resources	$0	$0	$0
STATUS OF BUDGETARY RESOURCES			
Obligations incurred:			
Direct	$0	$0	$0
Reimbursable	0	0	0
Subtotal	0	0	0
Unobligated balance:			
Apportioned	0	0	0
Exempt from apportionment	0	0	0
Other available	0	0	0
Unobligated Balances Not Available	0	0	0
Total, Status of Budgetary Resources	$0	$0	$0
Relationship of Obligations to Outlays:			
Obligated Balance, Net - beginning of period	$0	$0	$0
Obligated Balance transferred, net (+/-)	0	0	0
Obligated Balance, Net - end of period:			
Accounts receivable	0	0	0
Unfilled customer order from Federal sources	0	0	0
Undelivered orders	0	0	0
Accounts payable	0	0	0
Outlays:			
Disbursements	0	0	0
Collections	0	0	0
Subtotal	$0	$0	$0
Less: Offsetting receipts	0	0	0
Net Outlays	$0	$0	$0

Required Supplemental Information - Part A

AT97 - Army Working Capital Fund

Government Transactions from the Consolidating Trial Balance

Schedule, Part A DoD Intragovernmental Asset Balances ($ Amounts in Thousands).	Treasury Index:	Fund Balance with Treasury	Accounts Receivable	Loans Receivable	Investments	Other
Executive Office of the President	11		$0			
Department of Agriculture	12		$62			
Department of Commerce	13		$1			
Department of the Interior	14		$0			
Department of Justice	15		$12			
Navy General Fund	17		$14,767			
Department of State	19		$23			
Department of the Treasury	20	$948,463	$6			
Army General Fund	21		$371,336			$1
Department of Veterans Affairs	36		$8			
General Service Administration	47		$135			
Air Force General Fund	57		$19,595			
Federal Emergency Management Agency	58		$846			
Department of Transportation	69		$523			
Homeland Security	70		$2,851			
Department of Health and Human Services	75		$44			
National Aeronautics and Space Administration	80		$48			
Department of Energy	89		$3			
U.S. Army Corps of Engineers	96		$493			
Other Defense Organizations General Funds	97		$4,951			
Other Defense Organizations Working Capital Funds	97-4930		$18,599			
Navy Working Capital Fund	97-4930.002		$6,320			
Air Force Working Capital Fund	97-4930.003		$4,302			$78
Totals:		**$948,463**	**$444,925**			**$79**

Required Supplemental Information - Part B

AT97 - Army Working Capital Fund

Government Transactions from the Consolidating Trial Balance

Schedule, Part B DoD Intragovernmental entity liabilities ($ Amounts in Thousands).	Treasury Index:	Accounts Payable	Debts/Borrowings From Other Agencies	Other
Department of Labor	16			$50,084
Navy General Fund	17	$8,638		$11
Army General Fund	21	$30,871		$6,092
Office of Personnel Management	24			$6,614
General Service Administration	47			($476)
Air Force General Fund	57	$749		($442)
Homeland Security	70			$6
U.S. Army Corps of Engineers	96			$0
Other Defense Organizations General Funds	97	$125		$24
Other Defense Organizations Working Capital Funds	97-4930	$106,621		$5,720
Navy Working Capital Fund	97-4930.002	$6,832		$15
Air Force Working Capital Fund	97-4930.003	$5,316		$10
Totals:		**$159,152**		**$67,658**

Required Supplemental Information - Part C

AT97 - Army Working Capital Fund

Government Transactions from the Consolidating Trial Balance

Schedule, Part C DoD Intragovernmental revenue and related costs ($ Amounts in Thousands).	Treasury Index:	Earned Revenue
Department of Agriculture	12	$260
Department of Commerce	13	$2
Department of the Interior	14	$42
Department of Justice	15	$301
Navy General Fund	17	$387,139
Department of State	19	$790
Department of the Treasury	20	$398
Army General Fund	21	$7,372,038
Department of Veterans Affairs	36	$8
General Service Administration	47	$608
Air Force General Fund	57	$114,309
Federal Emergency Management Agency	58	$846
Department of Transportation	69	$3,858
Homeland Security	70	$21,387
Department of Health and Human Services	75	$210
National Aeronautics and Space Administration	80	$629
Department of Energy	89	$4
U.S. Army Corps of Engineers	96	$1,318
Other Defense Organizations General Funds	97	$180,207
Other Defense Organizations Working Capital Funds	97-4930	$36,481
Navy Working Capital Fund	97-4930.002	$162,159
Air Force Working Capital Fund	97-4930.003	$173,059
Totals:		**$8,456,053**

Required Supplemental Information - Part E

AT97 - Army Working Capital Fund

Government Transactions from the Consolidating Trial Balance

Schedue, Part E DoD Intragovernmental Non-exchange Revenues ($ Amounts in Thousands).	Treasury Index:	Transfers In	Transfers Out
Army General Fund	21		$1,407,000
Other Defense Organizations Working Capital Funds	97-4930		$41,600
Totals:			**$1,448,600**

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

November 8, 2004

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

SUBJECT: Independent Auditor's Report on the Fiscal Year 2004 Army Working Capital Fund Financial Statements (Report No. D-2005-010)

The Chief Financial Officers Act of 1990, as amended by the Federal Financial Management Act of 1994, requires Federal agency Inspectors General appointed under the Inspector General Act of 1978, as amended, to audit their respective agency's financial statements or determine that "an independent external auditor" should conduct such audits. Pursuant to this statutory authority, the undersigned Inspector General assumed responsibility for auditing the accompanying Army Working Capital Fund Consolidated Balance Sheet as of September 30, 2004 and 2003, the related Consolidated Statement of Net Cost, the Consolidated Statement of Changes in Net Position, the Combined Statement of Budgetary Resources, and the Combined Statement of Financing for the fiscal years then ended.

The financial statements are the responsibility of Army management. The Army is also responsible for implementing effective internal control and for complying with laws and regulations. We are unable to give an opinion on the FY 2004 financial statements of the Army Working Capital Fund 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 the audit.

Disclaimer of Opinion on the Financial Statements

The Assistant Secretary of the Army (Financial Management and Comptroller) acknowledged to us that the financial management and feeder systems that DoD relies on to provide evidence supporting the Army Working Capital Fund financial statements do not comply with Federal financial management system requirements, generally accepted accounting principles, and the U.S. Government Standard General Ledger at the transaction level. Therefore, we did not perform auditing procedures to determine whether material amounts on the financial statements were fairly presented. We did not perform these and other auditing procedures because Section 1008(d) of the FY 2002 National Defense Authorization Act limits the Inspector General of the Department of Defense to perform only audit procedures required by generally accepted government auditing standards that are consistent with the representations made by management. The Army Working Capital Fund has also acknowledged, and prior audits have identified, the material weaknesses listed in the Summary of Internal Control. These material weaknesses also affect the reliability of certain information contained in the annual financial statements—much of which is taken from the same data sources

"A regular Statement and Account of the Receipts and Expenditures of all public Money shall be published from time to time."—Constitution of the United States, Article I, Section 9

as the principal financial statements.[1] As described above, we are unable to express, and we do not express, an opinion on the financial statements and the accompanying information.

Summary of Internal Control

In planning our audit, we considered the Army Working Capital Fund internal control over financial reporting and compliance. We did this to determine our procedures for auditing the financial statements and to comply with Office of Management and Budget 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. However, previously identified reportable conditions,[2] all of which are material, continued to exist in the following areas:

- Financial Management Systems and Processes;
- Inventory and Related Property;
- General Property, Plant, and Equipment;
- Accounting Adjustments;
- Accounts Payable;
- Intragovernmental Eliminations;
- Statement of Net Cost; and
- Statement of Financing.

A material weakness is a condition that precludes the entity's internal control from providing reasonable assurance that misstatements, losses, or noncompliance that are material in relation to the financial statements would be prevented or detected on a timely basis. Our internal control work would not necessarily disclose all material weaknesses. See the Attachment for additional details on material internal control weaknesses.

Summary of Compliance With Laws and Regulations

Our work to determine compliance with selected provisions of applicable laws and regulations related to financial reporting was limited because management acknowledged, and prior audits confirm, that instances of noncompliance continue to exist. The Army is unable to comply with the requirements of the Chief Financial Officers Act of 1990, as amended. The Assistant Secretary of the Army (Financial Management and Comptroller) acknowledged that many of its critical financial management and feeder systems do not comply with the requirements of the Federal Financial Management Information Act of 1996. Therefore, we did not determine whether the Army Working Capital Fund was in compliance with all applicable laws and regulations related to financial reporting. See the Attachment for additional details on compliance with laws and regulations.

[1] The annual financial statements include the principal financial statements, management discussion and analysis, consolidating and combining financial statements, Required Supplementary Stewardship Information, Required Supplementary Information, and Other Accompanying Information.

[2] Reportable conditions are matters coming to the auditor's attention that, in his or her judgment, should be communicated to management because they represent significant deficiencies in the design or operation of internal control, which could adversely affect the organization's ability to initiate, record, process, and report financial data consistent with the assertions of management in financial statements.

Management Responsibility

Management is responsible for:

- preparing the financial statements in conformity with generally accepted accounting principles;
- establishing, maintaining, and assessing internal control to provide reasonable assurance that the broad control objectives of the Federal Managers' Financial Integrity Act of 1982 are met; and
- complying with applicable laws and regulations.

We provided a draft of this report to Army officials who provided no comments to the report.

Joseph E. Schmitz	Paul J. Granetto, CPA
Inspector General	Assistant Inspector General
Department of Defense	Defense Financial Auditing Service

Attachment:
As stated

"A regular Statement and Account of the Receipts and Expenditures of all public Money shall be published from time to time."—Constitution of the United States, Article I, Section 9

Report on Internal Control and Compliance with Laws and Regulations

Internal Control

Management is responsible for implementing effective internal control and for providing reasonable assurance that accounting data are accumulated, recorded, and reported properly 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 because management acknowledged that previously identified reportable conditions, all of which are material, continue to exist. The following financial management deficiencies are indications of material weaknesses in internal control that may adversely affect any decision by the Army that is based, in whole or in part, on information that is inaccurate because of these deficiencies. Financial information reported by the Army Working Capital Fund also may contain misstatements resulting from these deficiencies.

Financial Management Systems and Processes. The systems used for the Army Working Capital Fund are unable to meet all of the requirements for full accrual accounting because the systems were not designed to collect and record financial information, as required by generally accepted accounting principles. Financial and non-financial feeder systems are not integrated and do not contain an audit trail for the proprietary and budgetary accounts. The Army Working Capital Fund derives most of its financial information for major accounts from noncompliant financial systems, such as the Commodity Command Standard System. The Army Working Capital Fund began implementation of the Logistics Modernization Program during FY 2003. However, because of numerous problems, the Army delayed the second round of implementation until the third quarter of FY 2005. The Army Working Capital Fund disclosed financial management system deficiencies in the footnotes to the FY 2004 financial statements. The DoD-wide systemic deficiencies in financial management systems and business processes result in the inability to collect and report financial and performance information that is accurate, reliable, and timely.

Inventory and Related Property. The existing inventory valuation method does not produce an auditable approximation of historical cost. The Army Working Capital Fund uses the latest acquisition cost method of valuing most of its inventory because its legacy inventory systems were designed for materiel management rather than accounting. The systems provide accountability and visibility over inventory items, but do not maintain the historical cost data necessary to comply with Statement of Federal Financial Accounting Standards (SFFAS) No. 3, “Accounting for Inventory and Related Property.” In addition, the systems are unable to produce financial transactions using the U.S. Government Standard General Ledger accounts and neither the Defense Finance and Accounting Service (DFAS) nor the Army reconciled all differences between the accounting records and the logistical records. Instead, they accepted the data from the logistical records and adjusted the accounting records by about $3.4 billion. The Logistics Modernization Program uses the moving average cost method of valuing inventory and the U.S. Government Standard General Ledger accounts to record financial transactions. During the initial deployment phase, Army and DFAS users reported problems associated with duplicate and inaccurate posting of inventory and financial transactions. Further, the Army had not completed physical inventories nor established adequate controls over items in transit.

General Property, Plant, and Equipment. The value of Army Working Capital Fund General Property, Plant, and Equipment is not reliably reported because of the lack of supporting documentation, the failure to correctly compute depreciation, and the failure to fully report value of property in the possession of contractors. Information on the acquisition date and cost was not always available and was sometimes recorded incorrectly. In addition, the Integrated Facilities System, the system that provides real property information to the Defense Property Accountability System, was a noncompliant system. The Integrated Facilities System was not able to calculate depreciated values for real property, preserve previous values by handling both positive and negative numbers, and provide an audit trail of all real property. Systems improvements to address these deficiencies are planned, but have not yet been completed.

Accounting Adjustments. DFAS Indianapolis did not adequately support about $11.5 billion in adjustments to force amounts to agree with other sources of information and records used to prepare the FY 2004 Army Working Capital Fund Financial Statements. An additional $31.6 million in adjustments did not have adequate documentation attached to the journal vouchers to support either the reason for the adjustments or the dollar values. The unsupported adjusting accounting entries presented a material uncertainty regarding the line item balances on the FY 2004 Army Working Capital Fund Financial Statements. These adjustments affected the financial information on all of the statements. DFAS Indianapolis did not always follow the established minimum requirements for documenting journal vouchers to support adjusting accounting entries made to the general ledger accounts.

Accounts Payable. DFAS Indianapolis made significant adjustments to the accounts payable balances to derive the reported balances. DFAS Indianapolis adjusted accounts payable with the public upward by $2.2 million for undistributed disbursements. Also, the Army Working Capital Fund was unable to reconcile intragovernmental accounts payable to the related intragovernmental accounts receivable that generated the payable. As a result, DFAS made $2.3 million in unsupported adjustments to decrease intragovernmental accounts payable to force the amounts to agree with Army trading partners. In addition, accounts payable in the Supply Management activity group were not established in accordance with SFFAS No. 1, "Accounting for Selected Assets and Liabilities," which requires that an accounts payable be established when the entity accepts title to the goods or services. The Army Working Capital Fund recognized accounts payable based on the physical receipt of the goods or services rather than when the Government accepted title to the goods or services. As a result, the Army Working Capital Fund could not ensure that its accounts payable were not materially misstated.

Intragovernmental Eliminations. The inability to reconcile most intragovernmental transactions results in adjustments that cannot be verified. DoD and Army accounting systems were not capable of capturing trading partner data at the transaction level in a manner that facilitated trading partner reconciliations, and DoD guidance did not require adequate support for intragovernmental eliminations. As a result, DoD did not require trading partner reconciliations, but required that buyer-side transaction data be forced to agree with seller-side transaction data without performing proper reconciliations. DFAS Indianapolis made $6.0 billion in adjustments to intragovernmental accounts to force the accounts to agree with the records of Army Working Capital Fund trading partners.

Statement of Net Cost. The Statement of Net Cost was not presented by responsibility segments that were consistent with DoD performance goals and measures. Accounting systems were unable to accurately capture costs for Army Working Capital Fund programs and properly account for intragovernmental transactions and related eliminations. In addition, some of the Army Working Capital Fund's financial data presented on the Statement of Net Cost were based on budgetary transactions.

Statement of Financing. The Army cannot reconcile budgetary obligations to net cost without making unsupported adjustments. The Statement of Financing was prepared on a combined basis, while the Statement of Net Cost was prepared on a consolidated basis.

Compliance With Laws and Regulations

Management is responsible for compliance with existing laws and regulations related to financial reporting. Our work to determine compliance with selected provisions of the applicable laws and regulations was limited because management acknowledged instances of noncompliance, and previously reported instances of noncompliance continue to exist. Therefore, we did not determine whether the Army Working Capital Fund 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 compliance with applicable laws and regulations.

Statutory Financial Management Systems Reporting Requirements. The Army Working Capital Fund is required to comply with the following financial management systems reporting requirements.

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. In addition, the Federal Managers' Financial Integrity Act of 1982 requires the Army to evaluate its systems and to annually report whether those systems are in compliance with applicable requirements. The Chief Financial Officers Act of 1990 requires that each agency develop and maintain an integrated agency accounting and financial management system, including financial reporting and internal control. The system should comply with internal control standards, applicable accounting principles, standards, and requirements, and provide complete, reliable, consistent, and timely information.

The Assistant Secretary of the Army (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, generally accepted accounting principles, and the U.S. Government Standard General Ledger at the transaction level. The Army was also unable to comply with the Chief Financial Officers Act of 1990, which requires agencies to develop and maintain integrated agency accounting and financial systems.

In an attempt to comply with statutory reporting requirements and applicable financial systems requirements, DoD is developing a DoD-wide Business Enterprise Architecture. The architecture will provide a blueprint of the Department's financial management systems and processes to initiate a comprehensive financial management reform effort. Until the architecture is fully developed, the Army Working Capital Fund will be unable to fully comply with the statutory reporting requirements. Therefore, we did not perform tests of compliance for these requirements.

Audit Disclosures

The Assistant Secretary of the Army (Financial Management and Comptroller) acknowledged to us on March 9, 2004, that financial management systems used by the Army Working Capital Fund cannot provide adequate evidence supporting various material amounts on the financial statements.

Our review of internal control was limited to followup work on deficiencies identified in previous audit reports. We primarily focused on the deficiencies related to the material weaknesses reported in the audits of the FY 2003 Army Working Capital Fund Financial Statements.

We performed limited tests of Army Working Capital Fund compliance with laws and regulations that have a direct and material effect on the financial statement information. We did not perform audit work related to the following selected provisions of laws and regulations:

- Anti-Deficiency Act
- Provisions Governing Claims of the United States Government
- Federal Credit Reform Act of 1990
- Pay and Allowance System for Civilian Employees
- Prompt Payment Act

This report does not include recommendations to correct the material internal control weaknesses and instances of noncompliance because previous audit reports contained recommendations for corrective actions.

Civil Works Fund – Management's Discussion & Analysis

Overview

Mission

The Civil Works' mission is constantly evolving to keep pace with the changing needs of the Nation.

Developing and Managing Water Resources

The original Civil Works' mission, as it related to developing and managing water resources, was to support navigation by maintaining and improving water channels. In 1824, legislation authorized the Corps of Engineers (USACE) to improve safety on the Ohio and Mississippi Rivers. In 1909, the Rivers and Harbors Act authorized the consideration of various water uses—including hydroelectric power generation—in the planning, design, and construction of water resource development projects. The Flood Control Act of 1917 established a role for Civil Works in flood damage reduction, and in 1936 the Flood Control Act gave Civil Works the responsibility for providing flood protection for the entire country.

Recreation was added to the Civil Works portfolio by the Flood Control Act of 1944, which authorized the

"The Civil Works' mission is constantly evolving to keep pace with the changing needs of the Nation. Today, those missions fall in four broad areas: water infrastructure, environmental management and restoration, emergency response and assistance, and engineering support and technical services."

provision of recreational facilities at reservoirs. The River and Harbor Flood Control Act expanded this authority in 1962, providing authority to build, where feasible, recreational facilities as part of all water resource development projects.

Another aspect of water resources management is that of water supply. The changing role of the Civil Works Program in water supply has been directed by a series of Water Resources Development Acts. The Water Supply Act of 1958 gave Civil Works the authority to include water storage in both new and existing reservoir projects for municipal and industrial uses at 100 percent non-Federal cost.

Protecting, Restoring, and Managing the Environment

The Rivers and Harbors Act of 1899 required the Corps of Engineers to prevent the obstruction of navigable waterways. As concerns over the environment grew in the late 20th century, the Clean Water Act of 1972 greatly broadened the Corps' responsibility by providing authority over the dredging and filling in of "the waters of the United States," including the country's wetlands. The program's environmental responsibilities were further broadened by new legislation, introduced in 1986, that expanded the Corps' traditional environmental mitigation activities to include the enhancement and restoration of the natural environment at Corps projects and in areas not directly tied to those projects. This legislation made the provision of environmental protection one of the primary missions of the Corps' water resource development activities.

Responding to and Assisting in Disaster Relief

Throughout its history, America has relied upon Civil Works for help in times of national disaster. This help is now provided under two basic authorities: the Flood Control and Coastal Emergency Act (P.L. 84-99, as amended), and the Stafford Disaster and Emergency Assistance Act. Under P.L. 84-99, the Civil Works Program has direct authority to provide emergency assistance during or following flooding events to protect lives, public facilities, and infrastructure. Under the Stafford Act, the program supports the Federal Emergency Management Agency (FEMA) in carrying out the Federal Response Plan, which calls upon 26 Federal departments and agencies to provide coordinated disaster relief and recovery operations. The primary role for Civil Works in emergency relief and recovery operations is to provide public works and engineering support.

Providing Engineering Support and Technical Services

In Titles 10 and 33 of the U.S. Code, Congress expresses its intent that the U.S. Army Corps of Engineers provide services on a reimbursable basis to other Federal entities; state, local, and tribal governments; private firms; and international organizations. Additional authorities to provide services that are applicable to all Federal agencies are provided in Titles 15, 22 and 31. These authorities include providing services to friendly foreign governments.

U.S. Army Corps of Engineers emergency operations vans in Lakeland, FL., oversee hurricane recovery effort.

Civil Works Programs

The Civil Works mission is supported by nine programs through which it accomplishes the four components of its mission. Figure 20 defines the eight programs that receive direct appropriations as well as show funds for executive direction and management for the eight programs. The ninth program, Support for Others, is conducted on a reimbursable basis as outlined in the immediately proceeding paragraph. Each program specifically addresses a single mission component, but all programs may also contribute to one or more of the other mission components.

Navigation

The Navigation program is responsible for providing safe, reliable, efficient, and environmentally sustainable waterborne transportation systems for the movement of commercial goods, and for national security needs. The program seeks to meet this responsibility through a combination of capital improvements and the operation and maintenance of existing infrastructure projects. The Navigation program is vital to the Nation's economic prosperity: 99 percent of America's international trade moves through the program's ports, and 20 percent of American jobs depend to some extent on this trade.

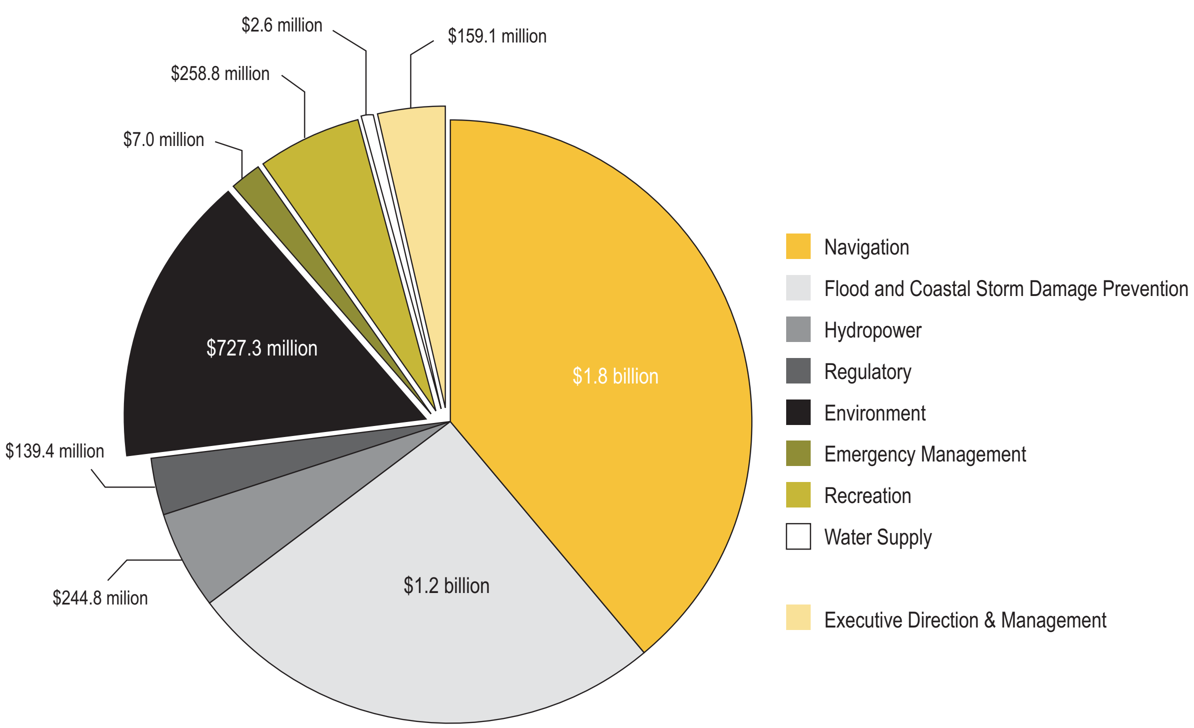
The Corps operates and maintains 25,000 miles of navigable channels and 195 commercial lock and dam sites and is responsible for ports and waterways in 41 states. America's inland waterways provide a highly fuel-efficient mode of transportation, with waterborne shipping able to move freight at more than 500 ton-miles per gallon of fuel, compared to the less than 400 ton-miles per gallon that rail transportation achieves. Use of our waterways rather than rail translates to an annual savings of $7 billion in transportation costs. Every dollar invested in improving our navigation infrastructure results in a better than $3 increase in Gross Domestic Product.

Major Commodities Handled by Civil Works Ports and Waterways in Calendar Year (CY) 2003

Crude Oil	605 million tons
Petroleum Products	474 million tons
Coal	272 million tons
Food/Farm Products	266 million tons

NOTE: Statistics are compiled on a calendar year basis. CY 2004 statistics not available at time of printing.

Figure 20. FY 2004 Civil Works Appropriation by Program



As an example, in May 2004, Civil Works and the Port Authority of New York and New Jersey launched a $1.6 billion project to deepen the channels in the Port of New York and New Jersey to 50 feet. In previous years, the agencies dredged the channels to a depth of 41 feet, and this new project builds upon that work. The project will improve navigational safety and allow the port to accommodate the next generation of cargo ships that can handle more than 8,000 truck-size containers and require deep water to operate. The Port Authority and the Federal Government will share the construction cost.

In fiscal year (FY) 2004, this $1.8 billion program accounted for 40 percent of the Civil Works appropriation.

A container vessel navigates the Kill Van Kull channel as it passes under the Bayonne Bridge, N.J. The Corps has deepened this channel to accommodate modern shipping vessels.

Flood and Coastal Storm Damage Reduction Program

This program is aimed at saving lives and reducing property damage in the event of floods and coastal storms. Civil Works constructed 8,500 miles of levees and dikes, 383 reservoirs, and more than 90 shore protection projects along 240 miles of the Nation's 2,700 miles of shoreline. With the exception of the reservoirs, most of the infrastructure constructed under this program is owned and operated by the sponsoring cities, towns, and agricultural districts.

Average Annual Damage Results for Period 1994 - 2003	
Damaged Suffered	$4.2 billion
Damage Prevented	$15.7 billon

**FY 2004 data were not available at time of printing.*

The Flood and Coastal Storm Damage Reduction program has compiled an impressive record of performance. In the period 1994–2003, floods in unprotected areas caused the United States an average of $4.2 billion yearly in property damage. In the same period, Corps projects in protected areas prevented $15.7 billion in average annual damages. Through FY 2000, the Nation had invested $43.6 billion ($122 billion, adjusted for inflation) in flood damage reduction projects, preventing an estimated $419 billion ($709 billion, adjusted for inflation) of flood damage. Adjusted for inflation, these figures show a return on investment of more than $6.36 in damage prevented for each dollar spent. The program also has helped reduce the number of lives lost annually due to floods from an average of 179 in the decade 1972–1981 to 89 in the period 1991–2000.

As an ever more mobile society moves toward America's coastal regions, protecting the coastline is a matter of increasing Federal interest. The Flood and Coastal Storm Damage Reduction Program seeks the most economical and environmentally sound solutions to achieve this. Most shore protection projects are carried out at the request of local sponsors, as authorized and funded by Congress, and are cost-shared with the state and local governments within whose jurisdiction the project falls. Projects are performed only on publicly accessible beaches and only after thorough studies have determined that there exists a positive benefit-to-cost ratio.

For example, the Corps recently completed a seven-year project that will protect millions of Americans in Los Angeles County. In the early 1990s, the

2,000-square-mile Los Angeles County drainage area was only partially protected from floods. Enormous population growth in the area rendered the existing flood control system inadequate, to the extent that FEMA required residents to hold mandatory flood insurance. Initiated in 1996—at an estimated cost of more than $450 million—the Los Angeles County Drainage Area Project was completed for roughly $200 million, of which Civil Works paid $150 million. The project saw the building of 21 miles of parapet walls, the reinforcement of the back slopes of levees, and the modification or raising of 26 bridges. As a result of these improvements, FEMA eliminated the obligation for flood insurance.

In FY 2004, this $1.2 billion program accounted for 28 percent of the Civil Works appropriations.

Environmental Protection, Restoration, and Management

This evolving and growing business program emphasizes environmental stewardship, ecosystem restoration, mitigation, environmental compliance, and research and development. Responding to the growing national demand for restoration and protection, the program's work takes many forms, ranging from monitoring water quality at dam sites to operating fish hatcheries with the states to restoring the environment at the sites of earlier projects. Since 1998, we have added more than 120,000 acres of aquatic, wetland, and floodplain ecosystems to America's natural habitats.

Kissimmee River C-38 Restoration Project, FL.

One example of work undertaken in FY 2004 is the Kissimmee River project in Florida. In the 1960s, flood control measures reduced this 103-mile river to a 52-mile canal, resulting in a degradation of the natural ecosystem. An ongoing Civil Works project aims to restore 52 miles of the river and 27,000 acres of wetlands, improving water quality and restoring the natural habitat for more than 300 species of fish and wildlife.

Another example is the Corps of Engineers and the Nature Conservancy have agreed to a collaborative effort to improve the management of dams on nine U.S. rivers. The Sustainable Rivers Project will seek to improve dam operations, helping to restore and protect the health of rivers and surrounding natural areas while continuing to meet human needs for services such as flood damage reduction and power generation. The collaborative effort will initially examine the potential to improve operations at 13 dams on nine rivers in nine states.

Ducks, geese, and herons are protected on more than 85,200 acres of Army Corps of Engineers land devoted to wildlife management.

In 1997, the Civil Works Program took over from the Department of Energy the Formerly Utilized Sites Remedial Action program, which mandates the clean-up of former Manhattan Project and Atomic Energy Commission sites. The transfer of this program to Civil Works capitalizes on the Corps experience gained in cleaning up former military sites and hazardous waste sites under the Environmental Protection Agency's Superfund program. Work under the program is ongoing at 46 locations in Missouri, Illinois, Ohio, Maryland, New Jersey, New York, Connecticut, Pennsylvania, and Massachusetts.

In FY 2004, this $727.3 million program accounted for 16 percent of the Civil Works appropriation.

Regulation of Wetlands and Waterways

In accordance with the Rivers and Harbors Act of 1899 (Sec. 10) and the Clean Water Act of 1972 (Sec. 404), as amended, the Army Civil Works

Regulatory Program regulates the discharge of dredged and fill material into waters of the United States, including wetlands. Section 10 applies to navigable waters, while section 404 applies more broadly to waters of the United States, which includes navigable waters, their tributaries, and wetlands.

As part of the permit evaluation process, the Corps complies with the National Environmental Policy Act and other applicable environmental and historic preservation laws. The objective of the program is to protect America's aquatic resources while allowing reasonable use of private property for important economic or infrastructure development on both private and public lands.

The Corps must consider the views of other Federal, tribal, state, and local governments and agencies; interest groups; and the general public when rendering its final permit decisions. The Regulatory program seeks to balance the reasonably foreseeable benefits and detriments of proposed projects, with the goal of making permit decisions that recognize the essential values of aquatic ecosystems to the general public and our national security.

The Corps must make final permit decisions that are not contrary to the public interest, and authorize only those projects that represent the least environmentally damaging practical alternative. The Corps works with project proponents to avoid and minimize impacts to the aquatic environment first. Unavoidable adverse impacts to the aquatic environment must be offset by the implementation of compensatory mitigation projects. Compensatory mitigation projects are designed to restore, enhance, establish, or protect and maintain aquatic functions and values. A critical objective is for the Corps to make efficient and timely permit decisions, providing regulatory consistency and predictability for the regulated public and for all interested parties. In FY 2004, this $139.4 million program accounted for 3 percent of the Civil Works appropriation.

Emergency Management

In a typical year, there are 30 Presidential disaster declarations demanding a response from the Civil Works Program. It is often difficult to know more than a few days in advance when a hurricane or other natural disaster will strike, and in the case of a man-made disaster, as the events of September 11, 2001, showed, there may be no notice at all. To prepare for such events, the Corps has implemented Readiness 2000, a unified and integrated corporate planning project, to raise responsiveness to the highest possible level. Predicting impending disasters can be difficult, but the returns on investment in emergency preparedness can be dramatic.

The Southeastern United States was hit by four major hurricanes in FY 2004. Landfall of these four hurricanes all occurred within a seven-week period in August and September.

- Hurricane Charley – Category 4 – 13 August 2004
- Hurricane Frances – Category 2 – 4 September 2004
- Hurricane Ivan – Category 3 – 16 September 2004
- Hurricane Jeanne –Category 3– 26 September 2004

Four divisions of the Corps of Engineers were affected: South Atlantic Division, Mississippi Valley Division, Great Lakes and Ohio River Division, and North Atlantic Division.

Mississippi Valley Division activated its catastrophic response plans in preparation for a hurricane in New Orleans. Great Lakes and Ohio River Division and North Atlantic Division each responded to significant rainfall as the hurricane weather systems moved through their area of responsibility.

South Atlantic Division responded to all four hurricanes that made landfall within its area of responsibility. The State of Florida was significantly impacted by all four hurricanes. Additionally, Hurricane Jeanne impacted Puerto Rico and Hurricane Ivan impacted Alabama as well as Florida.

The FEMA tasked the Corps of Engineers with response and recovery mission assignments in excess of $630 million. Over 1,700 Corps employees were assigned to support the multiple response and recovery efforts. FEMA-assigned missions included: supply of emergency water and ice; installation of generators for emergency power; provision of temporary roofing and temporary housing; and debris removal. Jacksonville District and Mobile District were responsible for mission execution in the state of Florida. Wilmington District was responsible for mission execution in the state of Alabama.

In FY 2004, this program received new budget authority of $7 million that accounted for a little more than 1.5 percent of the Civil Works new appropriation authority. The program is actually larger than indicated by the FY 2004 appropriation. The $7 million for annual preparedness planning funding is what enables the Corps to respond rapidly and carry out the $630 million reimbursable response and recovery work performed for FEMA along with completing prior year disaster recovery work funded by appropriations carried over into FY 2004.

Hydropower
Some of the Civil Works projects built for navigation and flood control have the additional benefit of providing hydroelectric power. This is in keeping with Civil Works policy and with Congressional direction to maximize public benefits in all projects for all desirable purposes, including power generation. This Civil Works Program operates and maintains 75 power plants, generating about 3 percent of America's total electrical power and 24 percent of the hydroelectric power. Hydropower is a low-cost, renewable power source that produces none of the airborne emissions that contribute to acid rain or the "greenhouse effect," leading many to view it as the least environmentally disruptive source of electric power. As concerns grow about the nation's limited energy resources, the Corps is working to increase hydropower output, efficiency, and reliability by upgrading and modernizing its facilities. Approximately two to three facilities per year are being renovated. For example, the Corps is in the process of installing seven new turbines at the J. Strom Thurmond hydropower plant in South Carolina. The turbines incorporate a new technology called autoventing that will improve dissolved oxygen levels in the water, benefiting fish and other aquatic life on the Savannah River. The $6 million turbine installation is part of a $70 million rehabilitation of the plant.

At the end of every fiscal year, the Corps is required to develop a "Statement of Expenses" for the Corps' hydropower expenses. The statement is broken down by plant, district, and region. These expenses are monitored through regional alliance meetings where Corps customers and stakeholders including the Power Marketing Administrators (PMAs) are represented. Once completed, the Statement of Expenses is audited by an outside contractor and then provided to the PMAs after the completion of each fiscal year. The PMAs use this information to update and adjust their "Power Repayment Study" which analyzes current and future year rates and revenues. The PMAs then collect power receipts (revenues) throughout the year and return the receipts to the Treasury, reflecting either a yearly expense or an amortized expense. The actual summary total of receipts deposited to the Treasury in any given year is reported back to the Corps for inclusion in the Chief Financial Officers (CFO) annual report.

In FY 2004, this $244.8 million program accounted for 5 percent of the Civil Works appropriation. In addition, the Corps received $142.8 million directly from the Booneville Power Administration to finance the cost to operate and maintain Corps-owned hydroelectric power facilities in the Pacific Northwest. In FY 2003, the Federal Power Marketing Administrators returned $1.6 billion to the U.S. Treasury from power sales.

Water Supply
Civil Works has 167 projects with municipal and industrial water supply as an authorized purpose. The projects supply water to 10 million people in 115 cities, including some of America's largest metropolitan areas, such as Washington, D.C., Atlanta, and Dallas–Fort Worth. In arid parts of the country, there are 62 projects that have irrigation as an authorized purpose. Many of these projects serve flood control, navigation, and hydroelectric purposes as well as irrigation.

In FY 2004, this $2.6 million business program accounted for less than 1 percent of the Civil Works appropriation.

Recreation
The Civil Works Recreation program is an important provider of outdoor recreation opportunities. The program operates more than 44,290 recreation sites at 413 projects—mostly lakes. One in ten Americans visits a Civil Works recreation site at least once a year, for a total of over 396 million visits. This is

a significant economic contribution to local areas, because Civil Works recreational sites provide a strong customer base for thousands of on-site and nearby businesses, including resorts, marinas, outfitters, grocery stores, gas stations, and hotels. This supports 600,000 jobs and generates $15 billion in visitor spending annually. There are approximately 500 concessionaires on Civil Works recreation sites, operating services such as marinas, bait shops, and grocery stores, with fixed assets of $1 billion. Corps lands are also leased to nearly 600 state parks, 600 local government parks, and to 420 Boy and Girl Scout camps, church camps, boating clubs, and other organizations that are open to public membership and that have defined goals that are consistent with the Corps' public recreation stewardship responsibilities.

In FY 2004, this $258.8 million business program accounted for 6 percent of the Civil Works appropriation.

Organizational Structure

The Workforce

Civil Works employs almost 24,000 employees including approximately 300 civilians deployed to Iraq and paid with military funds. Civil Works is funded through the Energy and Water Development Appropriation, and executes programs through 8 regional divisions and 38 of the 44 districts of the Corps of Engineers—the remaining 6 districts have only military mission-related work.

Figure 21 shows the division boundaries. Rather than being demarcated by state boundaries, these are defined by watersheds and drainage basins, reflecting the water resources nature of the Civil Works mission.

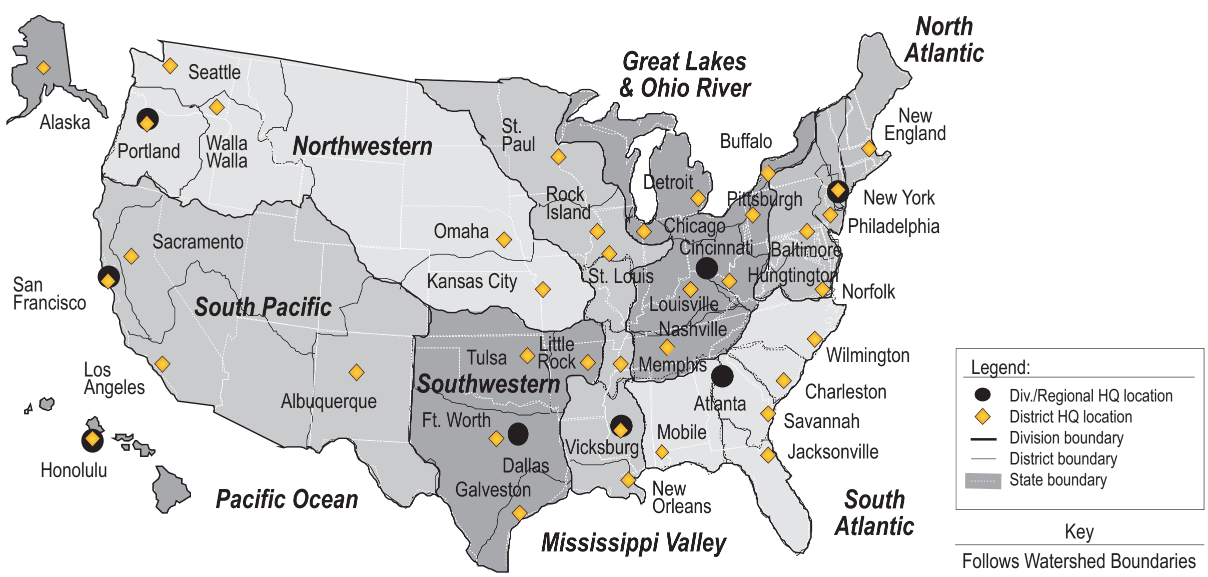
The distribution of Civil Works employees similarly highlights the customer focus of the program: 95 percent of employees work at the district level, reflecting the fact that project management is performed at the district level.

The Civil Works program contracts out to civilian companies all of its construction and approximately 50 percent of its design work. Although Civil Works directly employs almost 24,000 employees including approximately 300 civilians deployed to Iraq and paid with military funds, as many as 150,000 people are indirectly employed in support of its projects. These contractual arrangements have served the Nation well in times of emergency.

The Leadership

Oversight of Civil Works is provided through four levels of authority. As shown in Figure 22, the Assistant Secretary of the Army for Civil Works (ASA (CW)) is appointed by the President and is responsible for Civil Works policy. The Chief of Engineers reports to the ASA (CW) for Civil Works

Figure 21. Civil Works Boundaries

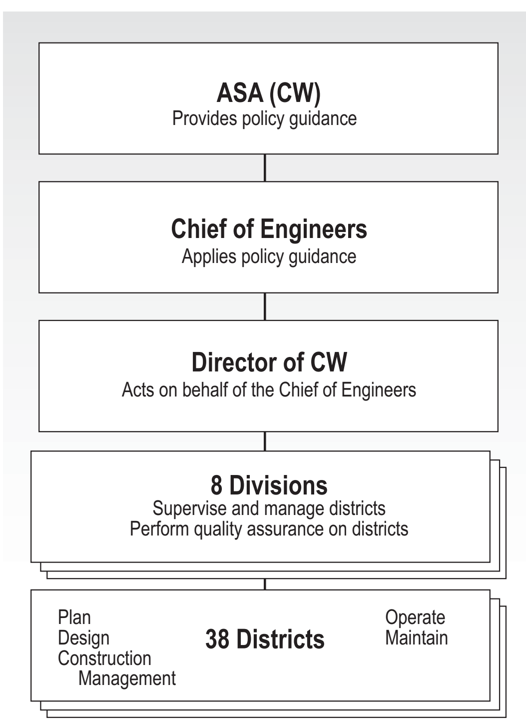


mission accomplishment and in turn delegates most of his responsibilities for managing the various programs to the Director of Civil Works. The Chief of Engineers, through the Director of Civil Works, is responsible for the leadership and management of the program and for ensuring that policies established by the ASA (CW) are applied to all phases of the Civil Works mission.

The divisions, commanded by Division Engineers, are regional offices responsible for the supervision and management of their subordinate districts, including the monitoring and quality assurance of district work.

The districts are the foundation of the Civil Works mission, managing water resource development over a project's life cycle. They conduct planning studies, perform project design, oversee construction by contractors, and manage completed facilities. They also develop decision documents and prepare reports and cost estimates, negotiate agreements, and perform all the day-to-day activities that get the job done. They are the program's face to the nation.

Figure 22. Civil Works Levels of Authority



Civil Works Fund Performance Results

Civil Works directly impacts America's prosperity, competitiveness, quality of life, and environmental stability. Civil Works leaders, accordingly, published a March 2004 strategic plan to identify and answer the Nation's water resources needs, recognizing authorities and funding. Research findings and input from the public, gained through listening sessions, have led the Corps to identify the following five issues as the main national water resource challenges facing the nation:

- Balancing demands for water resource development, in terms of access to and use of those resources, and the preservation of environmental quality
- Repairing damage to the nation's environment from past development
- Addressing the performance and safety implications of an aging water resources infrastructure
- Ensuring the capability to respond to natural disasters
- Minimizing the impact of institutional inhibitors on water resources decisionmaking and management.

To address these challenges, the Corps developed the following five strategic goals. Specific objectives associated with each goal enable the measurement of annual performance toward achievement of the strategic goal:

- Provide sustainable development and integrated management of the Nation's water resources.
- Repair past environmental degradation and prevent future environmental losses.
- Ensure that projects perform to meet authorized purposes and evolving conditions.
- Reduce vulnerabilities and losses to the Nation and the Army from natural and man-made disasters, including terrorism.
- Be a world-class public engineering organization.

Strategic Goals

Strategic Goal 1: Provide Sustainable Development and Integrated Management of the Nation's Water Resources

Through anticipating, identifying, and addressing water resources infrastructure problems and needs, the Army Corps of Engineers Civil Works mission is able to enhance the Nation's economic well-being. By maintaining coastal harbors and inter-coastal waterways, Civil Works strengthens America's ability to export its products to the world and to move those products around the Nation.

To continue to manage our water resources effectively, and to maintain waterway infrastructure, the Civil Works mission applies a consistent program investment objective to the development and management of water resources infrastructure. At the core of this objective are two guiding principles:

- Invest in the navigation program infrastructure when project benefits exceed their costs
- Invest in the flood and coastal storm damage reduction program infrastructure when project benefits exceed their costs.

Performance Measure 1: For investments in navigation projects, the benefit-to-cost ratio at the completion of project construction should at least equal the benefit-to-cost ratio at the time of initial project funding. The performance target for FY 2004 was to achieve a benefit-to-cost ratio at completion within 10 percent of the initial benefit-to-cost ratio.

Performance Result 1: In FY 2004, five navigation projects were budgeted for completion. All five projects were completed and met the performance target with a benefit-to-cost ratio equaling or exceeding the benefit-to-cost estimate used to justify initial project construction funding.

Performance Measure 2: For investments in flood and coastal storm damage reduction projects, the benefit-to-cost ratio at the completion of project construction should at least equal the estimated benefit-to-cost ratio at the time of initial project funding. The performance target for FY 2004 was to achieve a benefit-to-cost ratio at completion within 10 percent of the initial benefit-to-cost ratio.

Performance Result 2: In FY 2004, seven flood and coastal storm projects were budgeted for completion. One project was a dam safety project that was performed based upon a safety justification and not subject to a benefit-to-cost justification logic. Three of the remaining six projects met the performance target with a benefit-to-cost ratio equaling or exceeding the benefit-to-cost estimate used to justify initial project construction funding. The other three projects failed to meet the 10 percent performance target; but all three projects were completed with a positive benefit-to-cost ratio, thereby still validating the initial project investment decision.

Strategic Goal 2: Repair Past Environmental Degradation and Prevent Future Environmental Losses

To accomplish the second strategic goal, Civil Works must anticipate, identify, and address the Nation's needs for the environmental restoration and enhancement of its water resources. Civil Works will work with its partners, including other Federal and state agencies, nongovernmental organizations, and Native American tribes, to develop creative solutions that are both effective and efficient, employing, where appropriate, leading-edge technologies and methodologies.

Civil Works is pursuing the restoration of environmental damages and losses that resulted from past actions where it did not adequately anticipate or take into account the environmental consequences of those actions. It plans to exercise its authority to the fullest extent in support of the ecosystem restoration portion of the Civil Works Program. In addition, it will support the national commitment to wetlands—embodied in the Clean Water Action Plan—by adding to the Nation's environmental resource base through restoration and enhancement projects. It is working to ensure that there is no further net loss of wetlands due to unwise development activity.

The Environment Program also includes a significant environmental stewardship focus at Corps-operated projects. Strategic Goal 3 focuses on ensuring projects perform to meet authorized purposes and evolving conditions. One important aspect of ensuring that projects perform includes assuring that we are good environmental stewards. Accordingly, an environmental program objective under the third strategic goal is to "Ensure healthy and sustainable lands and waters and associated natural resources on Corps lands held in public trust to support multiple purposes."

In addition, the Corps of Engineers has been given responsibility to execute an environmental clean-up program of contaminated sites under the Formerly Utilized Sites Remedial Action Program. Accomplishment of the clean-up program will result in the elimination of potential risks to health and the environment at these high-priority sites.

Success in pursuit of this strategic goal is demonstrated through the performance measures that have been developed for the Environmental and Regulatory business programs.

Environmental

The Environmental program emphasizes environmental stewardship, ecosystem restoration, mitigation, environmental compliance, and research and development. The work undertaken by this program takes many forms, reflecting the growing national demand for restoration and protection.

There are four inter-related program objectives in the March 2004 Civil Works Strategic Plan. The four program objectives are differentiated by program focus, which are restoration, protection, stewardship and remediation. The restoration, stewardship, and remediation program objectives are discussed below. The protection focus is discussed under the Regulatory Program that is also found below, but broken out as a separate program in support of Administration and Congressional oversight.

Table 38. Civil Works-Administered Mitigation Land

	FY 2002	FY 2003	FY 2004
Total acreage designated as Civil Works-administered mitigation land	713,909	625,291	626,373
Mitigation land for which requirements were met (acres)	564,025	566,016	578,076
Percentage of Civil Works-administered mitigation lands for which mitigation requirements were met	79%	91%	92%

Note: The universe of total acreage designated as Civil Works-administered mitigation land shrank by over 88,600 acres from FY 2002 due to two projects with large land holdings being placed in an inactive status and removal of other projects lands misclassified with respect to mitigation requirements.

- Restoration: Invest in mitigation and restoration projects or features to make a positive contribution to the Nation's environmental resources in a cost-effective manner.
- Stewardship: Ensure healthy and sustainable lands and waters and associated natural resources on Corps lands held in public trust to support multiple purposes.
- Protect, preserve, and restore significant ecological resources in accordance with master plans.
- Ensure that the operation of all Civil Works facilities and management of associated lands, including out-granted lands, complies with the environmental requirements of all relevant Federal, State, and local laws and regulations.
- Meet the mitigation requirements of authorizing legislation or applicable Corps decision documents.
- Remediation: Assist in the cleanup of contaminated, hazardous, toxic, and radioactive waste sites as authorized or requested by others.

Performance Measure 1: This is measured by the percentage of Civil Works Environmental program-administered mitigation land that meets the requirements of the authorizing legislation or of the relevant Corps of Engineers decision document. The target for FY 2004 was to meet requirements for 85 percent of mitigation lands. This measure is calculated as a percentage of all designated program-administered mitigation lands that meet mitigation requirements.

Performance Result 1: Table 38 shows that from FY2003 to FY 2004 there was a net increase in acres designated as Civil Works-administered mitigation land. This change is due to the addition of lands in the mitigation inventory and corrections to the data reported in FY 2003. Mitigation requirements were met for 92 percent of Civil Works-administered mitigation land in FY 2004.

Performance Measure 2: The percentage in which Civil Works Stewardship should be engaged in opportunities to participate in recovery plan efforts for federally listed species. The performance target of 95 percent was continued in FY 2004 based upon experience gained with baseline performance measurement and the level of funding appropriated between FY 2002 and FY 2003.

Performance Result 2: Table 39 shows that during FY 2004, the Corps participated in recovery programs for 84 federally listed species, engaging in 533 separate opportunities to benefit these species or their habitat. A total of 306 Corps projects were involved.

Performance Measure 3: This is measured by correcting 100 percent of all significant findings and 70 percent of all major findings annually at Corps projects. A significant finding is a determination that we are not meeting an environmental requirement and that the condition poses, or has a high likelihood of posing, a direct and immediate threat to human health, safety, the environment, or the Civil Works mission. A major finding is a determination that we are not meeting an environmental requirement and that the condition may pose a direct and immediate threat to human health, safety, the environment, or the Civil Works mission. The success rate of correcting significant and major findings is calculated annually.

Performance Result 3: The performance target was exceeded for major findings. During FY 2003, we corrected three of five, or 60 percent (see Table 40), of significant findings. We completed corrections for one significant finding remaining at the end of FY 2002, and two significant findings identified during FY 2003. We implemented provisional corrections for the two remaining significant findings to eliminate the immediate threat to the environment. The Corps anticipates total correction of the two open significant findings in FY 2004 subject to funding availability. The Corps continues to place a high priority on achieving both performance goals in FY 2004; however, results were not available at time of printing.

Regulatory

Civil Works operates a comprehensive regulatory program to protect from overdevelopment the aquatic environment, primarily, but also the navigability of waterways. Management of this program has a related objective of minimizing the time taken to process decisions on requests for permits to work in the waters of the United States. The following program objectives have been established to support the pursuit of the strategic goals of the Civil Works mission:

- Administer the regulatory program in a manner that protects the aquatic environment.
- Administer the regulatory program in a manner that renders fair and reasonable decisions for applicants.
- Administer the regulatory program in a manner that enables efficient decision making.

Performance Measure 1: This is measured by administering the regulatory program in a manner that protects the aquatic environment. The performance target of Civil Works is to realize no net loss of wetlands.

Table 39. Recovery Plan Projects

	FY 2002	FY 2003	FY 2004
Number of opportunities to participate in recovery of federally listed species	509	515	543
Number of opportunities taken	496	504	533
Percentage of opportunities taken to assist in the recovery of Federally listed species	97%	98%	98%

Table 40. Correction of Significant and Major Environmental Findings

	FY 2002	FY 2003	FY 2004
Number of significant findings	10	5	NA[1]
Percentage corrected	70%	60%	NA[1]
Number of major findings	502	471	NA[1]
Percentage corrected	57%	72%	NA[1]

[1] *Data not available at time of printing.*

Table 41. Development and Mitigation of Wetlands

	FY 2002	FY 2003	FY 2004[1]
Wetland acres permitted for development	24,651	21,330	NA[1]
Wetland acres mitigated	57,821	43,379	NA[1]

[1] *Data not available at time of printing.*

Performance Result 1: The performance target was met in FY 2003. Table 41 shows that during FY 2003, 43,379 acres of wetlands were restored, created, enhanced, or preserved, offsetting the 21,330 acres that were lost to permitted development.

Performance Measure 2: This is measured by the number of all permit decisions completed within 60 days, expressed as a percentage of all permit decisions. The target is to complete 85 to 95 percent of all actions within 60 days.

Performance Result 2: FY 2004 performance results were not available at time of publication for Table 42. During FY 2003, 75,771 permit actions, or 88 percent of all permit actions, were completed in 60 days or less. While this figure exceeds the performance target of 85 percent, it remains unchanged from last year's performance. The districts are concentrating on getting the Nationwide and General Permits authorized; this has helped to stabilize overall processing times but is the cause of the downward trend in enforcement and compliance efforts seen since FY 2001.

Performance Measure 3: This is measured by the number of standard permit decisions completed within 120 days, expressed as a percentage of all standard permit decisions. Standard permits are those for larger projects that require extensive review. The performance target is to complete 70 – 80 percent of decisions on standard permits within 120 days.

Performance Result 3: FY 2004 Performance data were not available at time of publication for Table 43. The performance target was not met. During FY 2003, 56 percent of all standard permit actions were completed in fewer than 120 days. FY 2003 performance was down slightly from the last three years, at between 60 percent and 62 percent. The districts are contending with permit applications that are significantly more complex than in past years and that involve lengthy analysis of their potential environmental impacts. Issues related to endangered species, historic properties, water quality, and coastal resources also are adding to permit delays. Furthermore, the general public and the environmental community are becoming much more aware of and involved with the permit process, leading to increased numbers of comments raised in response to every public notice and to a rising trend in legal challenges.

Strategic Goal 3: Ensure that Projects Perform to Meet Authorized Purposes and Evolving Conditions

Civil Works customers, partners, and stakeholders expect delivery of the level of service that is designed into a project, and expect that high quality of service to continue even with changing demands on the project. This third strategic goal was developed to ensure that Civil Works' programs continue to meet customer expectations. This requires particular attention to the quality and performance of our projects, early recognition and analysis of problems, and identification of cost-effective ways to prevent, lessen, or correct any deficiencies.

In addition, Civil Works recognizes that it must continue to provide facilities that meet the needs of diverse and changing user groups. For projects to

Table 42. Permit Actions Completed within 60 Days

	FY 2002	FY 2003	FY 2004
Number of permit actions completed within 60 days	71,652	75,771	NA[1]
Percentage of actions completed within 60 days	88%	88%	NA[1]

[1] *Data not available at time of printing.*

Table 43. Standard Permit Actions Completed within 120 Days

	FY 2002	FY 2003	FY 2004
Number of standard permit actions completed within 120 days	2,536	2,446	NA[1]
Percentage of actions completed within 120 days	61%	56%	NA[1]

[1] *Data not available at time of printing.*

Table 44. Availability of Navigational Infrastructure

Performance Achieved	FY 2002	FY 2003	FY 2004
Actual availability	92%	92%	N/A[1]

[1] *Data not available at time of printing*

deliver the requisite performance and service levels, they must serve the needs of their users. Projects typically are designed to accomplish a particular purpose for a specified lifespan. In order that they continue to meet the changing needs of users, they may have to undergo design changes or may need to be rehabilitated or reconstructed in order to modernize their functions.

The performances of the Navigation, Flood and Coastal Storm Damage Prevention, Hydropower, Recreation, and Water Supply programs reflect the overall success of the Civil Works mission in achieving this strategic goal. The performance of each program is outlined in the following sections.

Navigation

The responsibilities of the Navigation program include the improvement and maintenance of port and harbor channels and of the inland waterways that handle the Nation's maritime commerce. The objective of the program is to operate and manage the navigation infrastructure in order to maintain consistent and acceptable levels of service. One performance measure and two performance indicators are used to gauge the successful pursuit of this objective:

- Availability to commercial traffic of high-use navigation infrastructure (waterways, harbors, and channels)
- Volume of commerce and the operational cost of the fuel-taxed waterways component of the navigation system
- Maintenance, through dredging, of safe and reliable harbors and channels.

Performance Measure: This is measured by the percentage of time program that facilities are open to commercial traffic. The performance target is 90 percent availability.

Performance Indicator 1: This is measured by monitoring the volume of commerce and the operational cost of the fuel-taxed waterways component of the navigation system. FY 2004 performance data were not available at the time of publication as reflected in Table 44.

Performance Result 1: The volume of commerce and the operational cost of the fuel-taxed waterways, shown in Table 45, remained essentially constant in CY 2002 and 2003. CY 2004 was not over at the time of printing, so volume and cost data for CY 2004 are not available.

Performance Indicator 2: The need for dredging of harbors and channels is largely dependent upon acts of nature and factors beyond the control of man. No performance target has therefore been established for the volume of material to be dredged. The depth of material to be dredged and the disposal of dredged material are the two main factors influencing the cost of dredging.

Performance Result 2: Table 46 shows that in FY 2004 performance data were not available at time of publication. In FY 2003, the amount of maintenance dredging decreased by 6.4 percent; and dredging unit costs increased by 14.6 percent.

Flood and Coastal Storm Damage Reduction

There are primarily two ways to reduce flood damage. The first calls for the use of large-scale engineering projects to prevent floodwaters from inundating property, and the second for the modification of property susceptible to flooding, to minimize the risk of damage. Civil Works projects usually use a combination of both approaches. The program objective is to operate and maintain existing Federal infrastructure to ensure that designed levels of protection are realized. A single measure is used to gauge performance in this respect.

Table 45. Volume of Commerce and Operational Cost

	CY 2002	CY 2003	CY 2004
Ton-miles of commerce carried (billions)[1]	266.9	250	NA[2]
Cost per ton-mile	$0.00206	$0.00195	NA[2]

[1] Ton-mile data are reported on a calendar basis. Costs are reported on a fiscal year basis. Ton mile data are reported.

[2] Data not available at time of printing.

Table 46. Volume and Cost of Material Dredged

	FY 2002	FY 2003	FY 2004
Cubic yards removed (millions)	204	191[1]	NA[2]
Cost per cubic yard	$2.73	$3.13[1]	NA[2]

[1] Values reported are for maintenance dredging only. Dredging data related to project construction activity are not covered.

[2] Data not available at time of printing.

Performance Indicator: This is measured by the performance of Civil Works facilities in reducing damage where flooding otherwise would have been experienced.

Performance Result: Table 47 shows that, during FY 2003, the Corps prevented $15.7 billion in flood damages. This can be compared to the 10-year moving average of $19.6 billion that is used to smooth out the significant fluctuations in year-to-year flood damages prevented that are associated with variations in meteorological events.

Hydropower

The Civil Works Program operates 345 hydroelectric power-generating units at 75 multi-purpose reservoirs, providing nearly a quarter of the Nation's total hydropower needs. That is enough energy to serve about 10 million households. Hydropower units can start quickly and adjust rapidly, allowing them to serve a primary role in meeting peak energy demands and energy reserve needs to protect the national power system's reliability and stability. The electricity is distributed by Federal power marketing administrations. To ensure that the Corps of Engineers continues to serve this role, it has established an overall program objective:

- Maintain reliable hydroelectric generation capabilities the at Corps' multi-purpose reservoir projects.

Performance Measure: This is measured by maintaining high reliability of hydroelectric power generated at multi-purpose reservoir projects. The program goal is to keep the forced (unplanned) outage rate at less than 2.3 percent in keeping with industry standards. A lower forced outage rate results in more reliable and less expensive electricity service provided to hydropower customers.

Performance Result: For FY 2004, preliminary data indicate that the Corps of Engineers experienced a forced outage rate of 3.5 percent. This is a slight increase from the outage rates seen for the prior two fiscal years and greater than the target rate of 2.3 percent. Aging equipment and funding levels are two factors that will impact the degree of hydropower reliability in the future. Data by fiscal year are provided in Table 48.

Value to the Nation Performance Indicators: In addition to measuring system reliability, the program also tracks operation system indicators that provide valuable information and trends on system performance. The following indicators are monitored: (1) kilowatt-hours generated to measure total power generation and (2) cost per kilowatt-hour to measure generating efficiency. Annual goals are not set for these indicators because power production is largely dependent upon hydrologic conditions that cannot be managed.

Performance Result: During FY 2004, preliminary data indicate that Corps hydropower facilities produced 67 billion kilowatt-hours of energy at a cost of $.0027 per kilowatt-hour as shown in Table 49. This represents a 4 percent decrease in energy output from FY 2003. Severe drought conditions in the Pacific Northwest are a likely cause of the reduced output, as about two-thirds of the Corps hydropower capacity is located in that region. Energy produced from existing Corps facilities continues to be one of the least expensive sources of electric power.

Table 47. Flood Damages Prevented

(Dollars in billions)	FY 2002	FY 2003	FY 2004
Flood damage prevented	$23.1	$15.7	NA[1]
10-year rolling average	$21.7	$19.6	NA[1]

[1] *Data not available at time of printing*

Table 48. Hydroelectric Power Reliability

	FY 2002	FY 2003	FY 2004
Performance Target (% outage)	4.5	2.3	2.3[1]
Actual reliability (% outage)	3.7	4.7	3.5[1]

[1] *FY 2004 Preliminary Performance data.*

Table 49. Kilowatt Hours Generated

	FY 2002	FY 2003	FY 2004
Kilowatt-hours generated (billions)	69.4	70.0	67.1[1]
Cost per kilowatt-hour	$0.0033	$0.0035	$0.0027[1]

[1] *FY 2004 Preliminary Performance data.*

Recreation
Most Federal lakes were originally built with a single primary purpose. However, public needs and values have changed, and the program has sought to serve the evolving public interest by adapting our reservoirs for multiple uses, provided there is sufficient legislative authority to do so. To support the broader strategic goals of the Civil Works mission and to achieve maximum cost-effectiveness in the provision of outdoor recreation services, Civil Works established the following program objectives:

- Provide outdoor recreation opportunities in an effective and efficient manner at Civil Works-operated water resource projects.
- Provide outdoor recreation opportunities to meet the needs of present and future generations.

Performance Indicator: This is measured by the cost per visitor-day of providing outdoor recreation facilities. The cost per visitor-day is determined by a number of variables. While Civil Works is able to manage the cost of providing recreation facilities, the number of visitors who use these facilities is governed in large part by external factors such as the weather and prevailing economic conditions. Historically, no management performance target has therefore been specified.

Performance Result: FY 2004 performance data were not available at time of printing as shown in Table 50.

Water Supply
Performance measures for this business program have not been fielded.

Strategic Goal 4: Reduce Vulnerabilities and Losses to the Nation and the Army from Natural and Man-Made Disasters, Including Terrorism

By developing and implementing new ways to reduce the risk of flood and storm damage losses, the Civil Works Mission is able to reduce potential flood damage, saving our Nation billions of dollars. Every year, we strive to reduce farther the risks associated with flooding and to increase our responsiveness to natural disasters. The Emergency Management program supports this strategic goal.

Table 50. Recreation Usage

	FY 2002	FY 2003	FY 2004
Visitor-days (millions)	210	212	NA[1]
Cost per visitor-day	$1.37	$1.20	NA[1]

[1] *Data not available at time of printing.*

The Civil Works mission includes a disaster response and recovery program, maintained by the Corps of Engineers under Public Law 84–99 and under the Federal Response Plan in coordination with the FEMA and others. Civil Works response activities are intended to supplement state and local efforts. Disaster preparedness and response capabilities are not limited to water-related disasters, but draw on the engineering skills and management capabilities of the Corps to encompass a broad range of natural disasters and national emergencies.

Through its emergency preparedness planning and disaster response capability, Civil Works can make a significant and direct contribution to national security objectives. Four program strategies support this fourth strategic goal:

- Attain and maintain a high and consistent state of preparedness.
- Provide a rapid, effective, and efficient all-hazards response capability, prepared for deployment anywhere worldwide.
- Provide the leadership to ensure effective and efficient long-term crisis recovery, emphasizing recovery of the Nation’s water resources infrastructure.
- Provide professional emergency management program services to international customers.

Strategic Goal 5: Be a World-Class Public Engineering Organization

A priority of the Corps of Engineers is to maintain a leading-edge technical capability today and into the future. Ensuring the delivery of high-quality and responsive engineering services to America and others requires a solid foundation in a core set of technical skills. To that end, and in anticipation of future requirements, Civil Works has begun to identify the range of expertise needed within the

Corps. It has also begun to identify those critical functions where reserves of talent may be depleted through retirement and attrition. Civil Works maintains the world-class capabilities inherent in its laboratories through capital investment, and it is engaging in research and development to improve operational processes to better address the Nation's water resource problems and opportunities.

Civil Works will leverage core technical capabilities as appropriate by providing engineering-related services to the Department of Defense (DoD) agencies, other Federal agencies, and other authorized entities through the Support for Others program. Overseas, it helps countries enhance their public sector capacities, especially in the management of water, to assist economic development and protect their environments and ecosystems. By assisting legitimate authorities to improve their infrastructure and environments and to ease conditions that potentially can lead to conflict, Civil Works serves to promote democracy, peace, and stability.

To be a world-class technical leader it is imperative to seek continuous improvement in the processes used to meet the customer, partner, and stakeholder needs. The feedback provided by customers and project sponsors is the best indication of how effective Civil Works is in meeting the expectations for the quality, timeliness, and cost-effectiveness of its services. Civil Works will continue to seek that feedback in order to strengthen overall performance and to raise customers' satisfaction.

Analysis of Financial Statements

Throughout FY 2004, the Civil Works Fund continued to improve upon the myriad processes linked to producing auditable financial statements in compliance with the CFO Act of 1990. Within DoD, the USACE Civil Works Fund has been at the forefront in implementing federal financial management reform.

The financial statements were compiled in accordance with guidance issued by the Office of Management and Budget and supplementary guidance provided by DoD. In his letter to the Chief Financial Officer, the IG DoD identified three internal control weaknesses.

The financial statements for the Civil Works Fund are presented in a comparative format, providing financial information for FY 2003 and FY 2004.

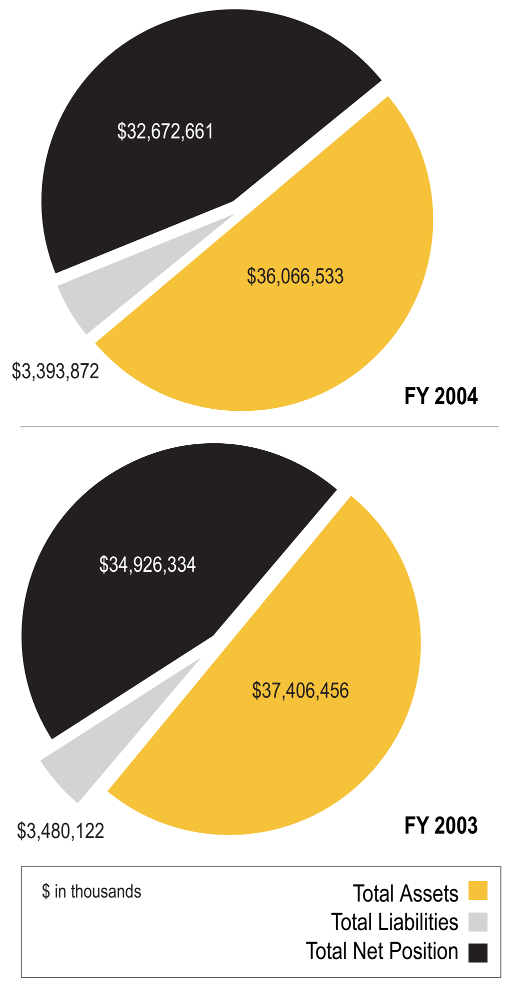
With that in mind, below are the financial highlights of each statement. These highlights focus on significant balances or conditions to help clarify the Civil Work Fund's operations. Additional explanatory information may also be found in the notes that accompany these statements.

Balance Sheet

This statement presents the assets, liabilities, and net position of the Civil Works Fund as of 30 September 2003 and 2004. As shown in Figure 23, the Civil Works assets amounted to $36.1 billion at FY 2004 year-end, over a 6 percent decrease from the previous year. Of the total assets, nearly 79 percent of the dollar value resides in the general property, plant, and equipment accounts. Relative to its total assets, the Civil Works liabilities are quite low, amounting to nearly $3.4 billion; representing a decrease of over $86 million or over 2 percent.

The third major component of the balance sheet is net position. In aggregate, the various elements of the net position section on the balance sheet are also referred to as equity. Equity is the residual interest in the assets of the entity that remains after deducting its liabilities. For FY 2004, the Civil Works Fund net position amounted to $32.7 billion, representing almost a $2.3 billion, or 7 percent, decrease from FY 2003.

Figure 23. Balance Sheet Results



Statement of Net Cost

This statement presents the annual cost of operating the various Civil Works programs. To the extent a program generates revenues, these amounts offset gross costs to arrive at the net cost of operations. For FY 2004, program costs amounted to $9.7 billion, representing a 6 percent decrease from the previous year. Conversely, program revenues increased 22 percent from FY 2003, climbing to $1.6 billion. The increase is primarily attributed to improvements in the Civil Works Fund process of identifying trading partner elimination data for other Corps revenue in the revolving fund. Overall for FY 2004, the Civil Works Fund achieved a 10 percent increase in the net cost of operations, decreasing net costs to $8.1 billion—a nearly $900 million decrease from the previous year.

Statement of Changes in Net Position

This statement presents those accounting items that caused the net position section of the balance sheet to change from the beginning to the end of the reporting period. The Civil Works Fund Net Position at year-end was $32.3 billion, nearly a 6 percent decrease from the previous year.

Statement of Budgetary Resources

This statement provides information on the Civil Works Fund's budgetary financing accounts and the status or remaining balances of those accounts at year-end. This includes information on obligations and outlays or actual cash disbursements for the year.

Statement of Financing

This is a reconciling statement that tracks the relationship between the proprietary accounts and the budgetary accounts of the Civil Works Fund. The Statement of Financing provides data on the total resources provided to the Civil Works Fund during the fiscal year and how those resources were used.

The first section of the statement, *Resources Used to Finance Activities*, shows a total of $4.1 billion. This is the amount for which the Civil Works Fund may have a future liability that would eventually require cash payments.

The second section, *Resources Used to Finance Items not Part of the Net Costs of Operations*, identifies and adjusts budgetary transactions recorded by the Civil Works Fund for changes in the amount of goods, services and benefits ordered but not received, the costs capitalized on the balance sheet, and financing sources that fund costs of earlier periods. For FY 2004, the fund had a negative $253 million in adjustments.

The first two sections are netted together to yield the total resources used to finance the net cost of operations. For FY 2004, total resources used to finance net costs decreased 44 percent over the previous year and amounted to approximately $3.9 billion.

Finally, the third section, *Components of the Net Cost of Operations that will not Require or Generate Resources in the Current Period*, is used to adjust the total resources used to finance the net cost of operations (the net amount of the first and second sections) in order to determine the net cost of operations. Thus, sections one and two are reconciled with section three to yield a net cost of operations of $8.1 billion. This amount ties back to the Statement of Net Cost.

Management Integrity

The Civil Works Program identified three management control weaknesses that were reported to be corrected during FY 2004 in last year's statement of assurance. However, each of the three management control weaknesses remains a weakness going forward to FY 2005. In FY 2004 one new management control weakness was identified. The following is the status of the material weakness:

Open material weaknesses as of September 30, 2003	3
Plus: New material weaknesses identified in FY 2004	1
Less: Material weaknesses corrected in FY 2004	0
Open material weaknesses as of September 30, 2004	4

Weaknesses Identified During FY 2004

The Civil Works Program identified one new management control weakness during FY 2004. The following section provides a brief description of the weakness and the target date for correction.

CFO Property, Plant, and Equipment Issues

Construction in Progress (CIP): During the FY 2002 and FY 2003 audit work, IG DoD projected that $10 billion of the beginning balance for FY 2003 was overstated by $7.8 billion due to expense-type events being erroneously capitalized, (i.e., Bank Stabilization Work, Beach Nourishment, Dredging, Fish Mitigation Work, Reimbursements to Sponsors), untimely transfers to completed projects, non-Federal cost share projects erroneously capitalized, CIP costs that could not be reconciled to source data, and $41 million in negative CIP balances.

Real Property: During FY 2002 and FY 2003 audit work, IG DoD identified seven major issues: (1) Placed in Service Dates, (2) Useful Life, (3) Physical Existence, Impairment, and Usefulness of Assets, (4) Bank Stabilization, (5) Non-Federal Lease Classifications for Building and Other Structures, (6) Supporting Documentation, and (7) Classification of Assts.

The target date for correction of this weakness is 1st Quarter, FY 2005.

Previously Reported Weaknesses

The Civil Works Program reported three weaknesses last year that it had expected to close during FY 2004. Various circumstances prevented this from happening. The following sections provide a brief description of each weakness and the revised target date for correction.

Information Systems Security—Computer System Controls

In October 2000, GAO identified a number of systems control weaknesses at the data processing centers. These weaknesses could allow either hackers or authorized users to improperly modify, disclose, or destroy financial data. Corrective actions to support the assurance of data security, including the reorganization of the Corps of Engineers and funding increases, have been taken to correct these deficiencies. The targeted correction date in last year's statement of assurance was March 2004. The followup on the GAO – Federal Information Systems Controls Audit Manual Audit and followup review/validation actions by IG DoD were delayed. At this time an item with the longest lead time is dependent upon effective actions to relocate a large processing center to a separate facility.

The revised target date for successful correction of this weakness is 4th Quarter, FY 2005.

Subcontracting Plans for Small Business

Procedures for evaluating and negotiating subcontracting plans and for evaluating subcontractor performance are not wholly in compliance with the law as it pertains to small business subcontracting. In August 2002, the Civil Works accepted a Web-based system to track outlays to small businesses under approved subcontracting plans and to track the actual execution of those plans. The system enables subcontractors to enter payments received from their prime contractors monthly, and enables independent validation by the government. Because the system is Web-based, any Civil Works office can review, query, or generate reports on compliance. The system was tested in FY 2003, and full compliance is delayed due to a lack of funds. Incorporation of the system in the Enterprise technology infrastructure for the Army is the strategy being utilized to ensure funding.

The revised target date for successful correction of this weakness is no later than 2nd Quarter, FY 2005.

Information Technology (IT) Capital Planning and Investment Decision Process

Weaknesses in the IT Capital Planning and Investment Decision Process were identified for the selection, control, and evaluation of USACE IT Investments in FY 2001. The Clinger-Cohen Act of 1996 and Army Regulation 25-1 require that Federal agencies institutionalize a USACE IT Capital Planning and Investment Decision Process. This process integrates the programming and budgeting for IT Investments through policies, guidance, and committees that monitor and track these investments through the USACE IT Investment Portfolio. Currently, the process is fragmented and senior-level approval continues to be given to high-visibility projects that have not been through the process. This weakness impacts corporate decisions on the ranking and prioritization of IT Investments and their contribution to the mission of USACE. A number of corrective actions have been completed or partially met while others have been delayed due to ongoing staffing.

The revised target date for successful correction of this weakness is 1st Quarter, FY 2006.

Future Effects of Existing Conditions

The Marine Transportation System

The Marine Transportation System (MTS) consists of 1,000 harbor channels, 25,000 miles of inland, intercoastal, and coastal waterways, and 235 lock chambers. Work done to improve the inland waterways is estimated to yield $5.5 billion in cost savings per year, and improvements to the deep-draft navigation system are estimated to save a further $1.5 billion in transportation costs annually.

The MTS is nearing capacity, however, and demands on it will grow substantially with the projected growth of international and domestic trade—trade is expected to double by 2020 to more than 4 billion tons of cargo annually. This will put great pressure on the system. It also should be noted that few American ports provide the 50 – 55 feet of depth needed by the latest containerships. Many international ports, including Halifax and Vancouver in Canada and Freeport in the Bahamas, already can accommodate such ships, and it is essential that America match them. Civil Works has over the past decade dredged an average of 275 million cubic yards of material per year. This work creates the additional challenge of how to dispose of the dredged material in an economically and environmentally acceptable manner.

Aging Infrastructure

More than 44 percent of America's locks and dams are at least 50 years old, and many locks are now too small to comfortably accommodate modern commercial barges. They are already carrying more tonnage than they were designed to handle, and traffic is forecast to increase 30 percent by 2020. Delays attributable to aged locks already amount to 550,000 hours per year, representing $385 million in increased operating costs. This is eroding America's share of international markets—American farmers already have lost 30 percent of their share of the European market for soybeans to Brazil and Argentina, both of which have invested heavily in inland waterways to reduce costs.

A lock modernization program has been underway since 1986, with $1.7 billion invested to date and an additional $3.4 billion programmed for construction. This, however, is insufficient to support optimum construction schedules. Completion dates for these projects have been set back by between one and five years, considerably increasing costs.

These increasing costs come at a time when investment in water resources is in sharp decline. In 1960, investment in all public infrastructure was 4 percent of the Federal budget. Today, that figure is 2.6 percent. Furthermore, in 1960 water resources received slightly more than 1 percent of all public infrastructure investment; today, they receive less than half a percent. This failure to invest adequately in water infrastructure could pose a serious constraint to America's economic development and competitive advantage in international trade.

Responding to Terrorist Threats

The events of September 11, 2001, changed the thinking about threat management. Everything from drinking water sources to reservoirs and dams is now viewed as a potential target for terrorists. Since the attacks on New York and Washington, D.C., Civil Works has maintained a heightened state of alertness as we seek to protect the Nation's critical infrastructure of water supply, waterborne commerce, and electric power generation.

Assuring the security of this infrastructure will require investment in warning and alert systems, systems to detect and respond to chemical and biological agents, intelligence-gathering and counter-terrorism measures, and emergency management systems. This requires investment in both technology and people. It is essential to institute a program that will comprehensively protect our water supply systems.

Advancing the President's Management Agenda

Strategic Management of Human Capital

It is essential that the USACE develop world-class technical expertise and make the best possible use of its human resources. The Corps of Engineers has long recognized the importance to its mission of its people and, as a result, it has sought through training and by sustaining its workforce to ensure that all mission-essential occupations are appropriately staffed with skilled people.

Aligning the Workforce and Mission

A comprehensive human capital strategy has been developed that is aligned with mission and broad corporate goals.

All employees must understand the Corps' mission and must understand how their work contributes to that mission. Each employee, as part of the larger Corps of Engineers, receives a CD-ROM called the CorpsPath. This provides an overview of the history, mission, and strategic goals of the Corps and provides detailed information on Civil Works business processes as well as on its strategy of knowledge management.

A Mission Essential Task List links performance measurement to mission accomplishment and enables identification of skill gaps in the workforce. The Corps of Engineers has automated this process and is producing a list of individual and organizational training requirements that will, through training and various learning activities, align the workforce and mission. Five Engineer Divisions have adopted the Automated Training Management Program (ATMP), which has the capability of linking individual and organizational training requirements directly to mission. ATMP generates reports that can be used to manage training dollars effectively. An individual development plan is electronically generated as well. A configuration control board has been established in order to review and approve proposed changes and enhancements to ATMP in order to ensure that the program remains uniform throughout the Corps. Individual performance plans are also used to align performance with mission and corporate goals and to increase understanding of the link between each team member's performance and organizational success.

The USACE Learning Advisory Board (LAB) has been established and has operated during the past several years as an advocate for initiatives and activities designed to further align the Civil Works workforce and mission and to transform USACE into a Learning Organization. Co-chaired by a General Officer and the USACE Director of Human Resources, respectively, the LAB is field-based, with representation from all levels within USACE, including Emerging Leaders from various districts. Under the auspices of the LAB, the USACE Learning Organization and Leadership for Learning Doctrines have been developed. The Chief of Engineers chose Learning Organization and Leadership for Learning, respectively, as the focus of the 2002 and 2003 USACE Senior Leadership Conferences. To ensure effective and efficient alignment of the USACE workforce and mission, the LAB has developed, refined and adopted a set of Training Principles to be used in driving workforce development in all areas. Other initiatives of the LAB include ongoing planning for Corps-wide integration of learning organization and leadership for learning doctrines; development of coaching and mentoring communities of practice; development of individual and organization learning assessments; development of a network of university partners; development of a best practices and learning case inventory; and development of a USACE Leadership Development Program template.

A People Committee, chaired by a Senior Executive and with cross-functional membership, has been established and is active in identifying strategic human resources (HR) initiatives, tracking implementation, and measuring progress at our Major Subordinate Commands through the Corps' Command Strategic Review program. HR strategies and initiatives are aligned and developed under the auspices of the USACE Strategic Vision, Campaign Plan, and Human Capital Plans, respectively.

To further support aligning the USACE workforce and mission, the Directorate of HR (DHR) has revised and conducted an orientation program for SES members of the workforce and conducted a USACE-wide HR conference to ensure that all field HR staffs are informed about the USACE PMA for human capital initiatives. Additionally, an important session at the HR conference focused on Strategic Sourcing from three different perspectives: the headquarters Project Office perspective; what Civilian Personnel Advisory Center employees should expect; and labor and employee relations aspects. In addition, DHR established several Project Delivery Teams to focus on redesign and streamlining of the USACE Professional Development Support Center, which designs and delivers Corps-specific technical, professional, and short courses; developed an online USACE Coaching, Counseling, and Mentoring Guide; and identified and executed funding for obtaining access to the Department of Labor Workforce Connections Workforce Productivity Tools that will enable USACE to provide state-of-the art course delivery and learning knowledge management for the benefit of our workforce.

USACE has a customer focus and has allocated its personnel accordingly. As the program is in contact with its customers primarily at the Engineer District level, 95 percent of the workforce is concentrated at district, field office, and resident offices. As part of an effort to improve service to the public, 50 percent of supervisory positions have been eliminated since 1994 in an effort to flatten the organization and increase the percentage of employees directly engaging the customer. A comprehensive review of command functions, business processes, and structure has recently been completed, with implementation scheduled for FY 2004.

Recruiting

The USACE has more than 600 college students enrolled in various intern programs, representing an increase from 1989 to 2001 of 400 percent. The Corps recognizes the need to develop a source of skilled young people to replace an aging workforce. By exposing college students to the work done by the Corps, it is believed that such a source can be developed, and thus we can address anticipated shortages in the workforce as baby boomers reach retirement.

The USACE Human Capital plan includes a comprehensive analysis of the current workforce and projects workforce needs several years into the future based on an analysis of projected turnover and future mission requirements.

The USACE employment website has been reworked to make it more attractive and user-friendly. It now provides more information in which prospective employees would be interested. Recruitment material and advertisements have been updated. A recruiters' handbook has been developed, and training for recruiters has begun.

Training and Learning

To fill and also to limit the occurrence of future skill gaps, the Corps of Engineers must embrace and subsequently embody the attributes and principles of a learning organization. Technology and business practices are continuously evolving: therefore, the Corps has decided to establish a learning network addressing the three areas of technical excellence, business and communications, and leadership. This network will capitalize on USACE Communities of Practice and will create a vibrant knowledge management platform that will bring together discussion of lessons learned, best practices, and knowledge management with training. It will also enable learners to meet with and enjoy the benefits of continuous learning from subject matter experts and enable the further development, refinement, and enhancement of communities of practice within USACE.

Competitive Sourcing

In concordance with the PMA, Civil Works recognizes that some of its employees likely are performing tasks that can be outsourced to the commercial marketplace. Civil Works accordingly has a plan to conduct competitive sourcing studies on approximately 5,700 positions between FY 2004 and FY 2008. This represents 37 percent of authorized Civil Works commercial positions and is in addition to the 58 percent of the Civil Works workload which is already accomplished by its industry partners.

A number of factors need to be considered when identifying the positions that will be opened up for competition. Realization of the full value of outsourcing requires that there be a large number of positions for conversion, that they are of a notably commercial nature, and that they are geographically concentrated. In addition, there is a need to keep a minimum number of Federal positions for each staff function in order that oversight be retained in areas such as financial management, public affairs, and others.

Improved Financial Performance

The USACE is recognized as a leader in the DoD in the area of financial management and continues to upgrade its financial management systems and tools. For example, the Corps has developed a proprietary financial tool known as the Corps of Engineers Financial Management System (CEFMS). Designed and built by the Corps with the aid of external contractors, the system delivers a broad range of functionality. It integrates financial management processes with internal program and project management processes and provides automated linkage to the Department of the Army, DoD, and the OMB.

The Corps invested approximately $76 million in development of CEFMS. The process of implementing the system and gaining its acceptance among the Corps family required a major cultural adjustment, but efforts in this regard have proven extremely successful, and CEFMS is a key component of successful program execution and customer care. The system now serves as a measuring stick for new DoD financial management systems, and provided the basis for development of the Defense Joint Accounting System.

In addition to implementing CEFMS, the Corps has undertaken the challenge of complying with the full requirements of the CFO Act of 1990. With a fully integrated CEFMS and sound business practices, the Corps is positioning itself to be one of the first Army components to receive an unqualified audit opinion.

Expand Electronic Government

Adoption of a wide array of Web-based services has wrought major changes to the Civil Works program's business processes and, in particular, has vastly improved the program's internal and external communications.

Government to Citizen

Civil Works is an active proponent of the Government's drive to reach out to the public through the Internet. Participating in Presidential-level interagency initiatives such as Recreation One-Stop and Geospatial Information One-Stop, Civil Works is making access to information about our services and programs easier for more Americans. In partnership with the U.S. Forest Service, Civil Works also supports the National Recreation Reservation System for the use of public lands and facilities.

To simplify access to the rules governing use of Civil Works lands and waterways, it has eliminated all hard-copy directives and publications (approximately 1,000), placing them instead online in formats suitable for viewing, downloading, and printing. Civil Works is also responsible for nine public reports, and eight of these reports were integrated during FY 2004 into the Operations and Maintenance Business Information Link (OMBIL) with an Internet data collection capability. The remaining report comprises about 60 individual questionnaires that are currently available for download from the web.

Under OMBIL, the regulatory permit process is being streamlined and integrated into a transaction-based web environment. Civil Works is evaluating other means for integrating various types of authorizations and licenses, with the view to improving public access to them and reducing waiting times. Civil Works is also participating in the redesign and horizontal enterprise portal pilot efforts related to the totality of the Corps corporate Web presence.

The Corps strategic-level Communication Committee has identified the revision of the USACE Internet presence as a strategic initiative for this year. A new user-friendly Web page is being developed, and the site is being enhanced with a new search engine and zip code locater. The plan is for the entire Corps eventually to adopt a more corporate presence on the Internet to assist citizens in finding help for the various services we perform.

Government to Business

Civil Works is working to make it easier to do business with the Federal Government. In partnership with the National Institute of Standards and Technology and the Government Accountability Office, Civil Works is working to define the requirements for a public key-based electronic signature capability to replace the proprietary electronic signature capability that currently is used.

Civil Works is a full participant in the Web-based Tri-Service Solicitation Network and sponsors the Electronic Contract Solicitations system, which is a Web-based electronic process for advertising and distributing contract solicitation documents, with linkages to "Army Single Face to Industry" and FedBizOps websites. Civil Works is also DoD's Executive Agent for the Architect-Engineer (A-E) Contractor Administrative Support System and the Construction Contractor Appraisal Support System. These systems manage A-E and construction contractor performance evaluations.

Government to Government (G2G)

The sharing of information among Federal, state, local, and tribal governments and the full integration of that information will contribute to better government for all Americans. The Comprehensive Everglades Restoration Program, a partnership of the Civil Works program with the South Florida Water Management District, is a prime example of interagency and special interest group electronic data sharing through a significant Internet presence (www.evergladesplan.org). Another example, the ENGLink automated system, is the primary integrator of multijurisdictional (local, state, and Federal) data for the support of emergency operations. ENGLink provides real-time, accurate information in the event of a disaster, helping to support collaborative response planning among what may be widely dispersed assets.

OMBIL and the Corps Water Management System aggregate, integrate, and disseminate multiple sources of data in support of hydropower, navigation, environmental stewardship, and flood and coastal storm damage reduction missions that impact local, regional, state, and national interests. The Project Management Business Process (PMBP) program—which will see the development of a one-stop portal enabling customers and stakeholders to access project status information—is also significant in terms of advancing the Corps' G2G services.

Internal Efficiency and Effectiveness

The PMBP program is a significant initiative to streamline the business processes associated with program and project management. It also will support the adoption of best business practices in the delivery of projects to local, state, regional, Federal, and international customers and will facilitate agency budget and performance integration. At the heart of this business re-engineering effort are the adoption of commercial off-the-shelf software, the integration and streamlining of legacy automated systems, and the termination of several stand-alone applications.

The PMBP program will also enhance a common electronic workplace environment that promotes Regional Business Centers, virtual teaming, personalization, and the strategic management of human capital.

Budget and Performance Integration

The President's objective to link performance and budget builds on the Government Performance and Results Act of 1993 and earlier efforts to identify program goals and performance measures and to link them to the budget. The FY 2003 President's Budget was the first to include explicit assessments of program performance and included a performance-linked budget assessment of three Civil Works business programs: Navigation (Inland Waterways portion), Flood and Coastal Storm Damage Reduction, and Environmental Restoration. For the FY 2004 budget, Civil Works added Regulatory, Emergency Management, and Environment programs to the process of linking performance to budget and continued developing new performance measures to further this linkage. More recently, Civil Works completely transformed its FY 2005 and FY 2006 budget development to align it with the eight programs funded through Congressional appropriations. We will place increased emphasis during FY 2005 on fielding new performance measures that are linked the to budget. Progress in implementing this initiative will be reported in the FY 2005 financial statements.

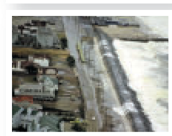
Civil Works Fund Introduction Page Photos

[Large Photo]
Port Mayaca Lock and Dam located on the east side of Lake Okeechobee at the junction with the St. Lucie Canal. The Okeechobee Waterway extends to the Gulf of Mexico using the Caloosahatchee River and to the Atlantic Ocean using the St. Lucie Canal.

[Top Inset Photo]
Clean-up after Hurricane Isabel in Norfolk, VA.

[Middle Inset Photo]
View of Sea Bright, N.J. coastline as a storm attacks the seawall.

[Botton Inset Photo]
Fighting the flood in Fort Wayne, IN.



Civil Works Fund Principal Financial Statements, Notes, and Supplementary Information

Limitations

Limitations of the Financial Statements

The financial statements have been prepared to report the financial position and results of operations for 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 the formats prescribed by the 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.

To the extent possible, the financial statements have been prepared in accordance with federal accounting standards. At times, the Department is unable to implement all elements of the standards due to financial management systems limitations. The Department continues to implement system improvements to address these limitations. There are other instances when the Department's application of the accounting standards is different from the auditor's application of the standards. In those situations, the Department has reviewed the intent of the standard and applied it in a manner that management believes fulfills that intent.

The statements should be read with the realization that they are for a component of the United States Government, a sovereign entity. One implication of this is that the liabilities cannot be liquidated without legislation that provides resources to do so.

Limitations Concerning National Defense Property, Plant and Equipment

The Federal Accounting Standards Advisory Board (FASAB) revised the Statement of Federal Financial Accounting Standards No. 6 to require the capitalization and depreciation of military equipment (formerly National Defense Property, Plant and Equipment/ND PP&E) for fiscal years (FY) 2003 and beyond, and encouraged early implementation

Department of Defense- Department of the Army, Civil Works Fund

CONSOLIDATED BALANCE SHEET

As of September 30, 2004 and 2003 ($ in Thousands)

ASSETS (Note 2)	2004 Consolidated	2003 Consolidated
Intragovernmental:		
Fund Balance with Treasury (Note 3)		
Entity	$2,378,442	$2,588,857
Non-Entity Seized Iraqi Cash	0	0
Non-Entity-Other	8,245	6,865
Investments (Note 4)	2,741,917	2,478,454
Accounts Receivable (Note 5)	520,123	423,774
Other Assets (Note 6)	0	0
Total Intragovernmental Assets	$5,648,727	$5,497,950
Cash and Other Monetary Assets (Note 7)	$1,039	$1,278
Accounts Receivable (Note 5)	1,906,435	1,935,567
Loans Receivable (Note 8)	0	0
Inventory and Related Property (Note 9)	61,815	62,605
General Property, Plant and Equipment (Note 10)	28,448,517	30,909,056
Investments (Note 4)	0	0
Other Assets (Note 6)	0	0
TOTAL ASSETS	$36,066,533	$38,406,456
LIABILITIES (Note 11)		
Intragovernmental:		
Accounts Payable (Note 12)	$103,498	$92,764
Debt (Note 13)	15,367	17,386
Environmental Liabilities (Note 14)	0	0
Other Liabilities (Note 15 & Note 16)	2,058,627	2,096,480
Total Intragovernmental Liabilities	$2,177,492	$2,206,630
Accounts Payable (Note 12)	$570,255	$568,108
Military Retirement Benefits and Other Employment-Related Actuarial Liabilities (Note 17)	0	0
Environmental Liabilities (Note 14)	0	0
Loan Guarantee Liability (Note 8)	0	0
Other Liabilities (Note 15 and Note 16)	646,125	705,384
Debt Held by Public	0	0
TOTAL LIABILITIES	$3,393,872	$3,480,122
NET POSITION		
Unexpended Appropriations (Note 18)	$396,362	$636,846
Cumulative Results of Operations	32,276,299	34,289,488
TOTAL NET POSITION	$32,672,661	$34,926,334
TOTAL LIABILITIES AND NET POSITION	$36,066,533	$38,406,456

Department of Defense- Department of the Army, Civil Works Fund

CONSOLIDATED STATEMENT OF NET COST

As of September 30, 2004 and 2003 ($ in Thousands)

Program Costs	2004 Consolidated	2003 Consolidated
Intragovernmental Gross Costs	$1,020,767	$819,199
(Less: Intragovernmental Earned Revenue)	(1,234,805)	(1,011,769)
Intragovernmental Net Costs	($214,038)	($192,570)
Gross Costs With the Public	$8,658,737	$9,466,972
(Less: Earned Revenue From the Public)	(367,963)	(298,633)
Net Costs With the Public	$8,290,774	$9,168,339
Total Net Cost	$8,076,736	$8,975,769
Cost Not Assigned to Programs	0	0
(Less: Earned Revenue Not Attributable to Programs)	0	0
Net Cost of Operations	$8,076,736	$8,975,769

Department of Defense- Department of the Army, Civil Works Fund

CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION

As of September 30, 2004 and 2003 ($ in Thousands)

CUMULATIVE RESULTS OF OPERATIONS	2004 Consolidated	2003 Consolidated
Beginning Balances	$34,289,488	$39,695,092
Prior period adjustments (+/-)		
Prior Period Adjustments - Restated (+/-)	0	(2,669,485)
Beginning Balance, Restated	34,289,488	37,025,607
Prior Period Adjustments - Not Restated (+/-)	0	0
Beginning Balances, as adjusted	$34,289,488	$37,025,607
Budgetary Financing Sources:		
Appropriations received	0	0
Appropriations transferred-in/out (+/-)	0	0
Other adjustments (rescissions, etc) (+/-)	0	0
Appropriations used	4,079,023	4,323,711
Nonexchange revenue	1,434,495	931,241
Donations and forfeitures of cash and cash equivalents	0	0
Transfers-in/out without reimbursement (+/-)	315,045	863,243
Other budgetary financing sources (+/-)	(3,945)	(32,536)
Other Financing Sources:		
Donations and forfeitures of property	435	4,648
Transfers-in/out without reimbursement (+/-)	(1,632)	(56,344)
Imputed financing from costs absorbed by others	239,548	225,066
Other (+/-)	578	(19,379)
Total Financing Sources	$6,063,547	$6,239,650
Net Cost of Operations (+/-)	8,076,736	8,975,769
Ending Balances	$32,276,299	$34,289,488
UNEXPENDED APPROPRIATIONS		
Beginning Balances	$636,846	$1,064,864
Prior period adjustments (+/-)		
Prior Period Adjustments - Restated (+/-)	0	0
Beginning Balance, Restated	636,846	1,064,864
Prior Period Adjustments - Not Restated (+/-)	0	0
Beginning Balances, as adjusted	$636,846	$1,064,864
Budgetary Financing Sources:		
Appropriations received	3,854,081	4,027,057
Appropriations transferred-in/out (+/-)	18,394	196,111
Other adjustments (rescissions, etc) (+/-)	(33,936)	(344,418)
Appropriations used	(4,079,023)	(4,306,768)
Nonexchange revenue	0	0
Donations and forfeitures of cash and cash equivalents	0	0
Transfers-in/out without reimbursement (+/-)	0	0
Other budgetary financing sources (+/-)	0	0
Other Financing Sources:		
Donations and forfeitures of property	0	0
Transfers-in/out without reimbursement (+/-)	0	0
Imputed financing from costs absorbed by others	0	0
Other (+/-)	0	0
Total Financing Sources	($240,484)	($428,018)
Net Cost of Operations (+/-)	0	0
Ending Balances	$396,362	$636,846

Department of Defense- Department of the Army, Civil Works Fund

COMBINED STATEMENT OF BUDGETARY RESOURCES

As of September 30, 2004 and 2003 ($ in Thousands)

	BUDGETARY FINANCING ACCOUNTS		NON-BUDGETARY FINANCING ACCOUNTS	
BUDGETARY RESOURCES	**2004 Combined**	**2003 Combined**	**2004 Combined**	**2003 Combined**
Budget Authority:				
Appropriations received	$5,141,166	$7,652,893	$0	$0
Borrowing authority	135	0	0	0
Contract authority	0	0	0	0
Net transfers (+/-)	206,924	160,964	0	0
Other	0	0	0	0
Unobligated balance:				
Beginning of period	1,850,226	1,741,013	0	0
Net transfers, actual (+/-)	28,495	0	0	0
Anticipated Transfers Balances	0	0	0	0
Spending authority from offsetting collections:				
Earned	0	0	0	0
Collected	5,212,085	5,065,570	0	0
Receivable from Federal sources	64,104	(74,841)	0	0
Change in unfilled customer orders	0	0	0	0
Advance received	29,660	(16,318)	0	0
Without advance from Federal sources	272,555	262,126	0	0
Anticipated for the rest of year, without advances	0	0	0	0
Transfers from trust funds	0	0	0	0
Subtotal	$5,578,404	$5,236,537	$0	$0
Recoveries of prior year obligations	0	0	0	0
Temporarily not available pursuant to Public Law	(10,000)	0	0	0
Permanently not available	(29,076)	(8,653)	0	0
Total Budgetary Resources	$12,766,274	$14,782,754	$0	$0
STATUS OF BUDGETARY RESOURCES				
Obligations incurred:				
Direct	$5,615,179	$5,516,359	$0	$0
Reimbursable	5,457,815	5,033,749	0	0
Subtotal	$11,072,994	$10,550,108	$0	$0
Unobligated balance:				
Apportioned	1,234,139	1,387,762	0	0
Exempt from apportionment	459,076	2,844,875	0	0
Other available	(1)	0	0	0
Unobligated Balances Not Available	66	9	0	0
Total, Status of Budgetary Resources	$12,766,274	$14,782,754	$0	$0
Relationship of Obligations to Outlays:				
Obligated Balance, Net - beginning of period	$1,007,621	$1,047,323	0	0
Obligated Balance transferred, net (+/-)	0	0	0	0
Obligated Balance, Net - end of period:				
Accounts receivable	(224,704)	(160,601)	0	0
Unfilled customer order from Federal sources	(1,907,809)	(1,635,255)	0	0
Undelivered orders	2,022,902	1,628,915	0	0
Accounts payable	1,148,287	1,174,565	0	0
Outlays:				
Disbursements	10,705,281	10,402,525	0	0
Collections	(5,241,746)	(5,049,251)	0	0
Subtotal	$5,463,535	$5,353,274	$0	$0
Less: Offsetting receipts	(1,592,297)	(904,214)	0	0
Net Outlays	$3,871,238	$4,449,060	$0	$0

Department of Defense- Department of the Army, Civil Works Fund

COMBINED STATEMENT OF FINANCING

As of September 30, 2004 and 2003 ($ in Thousands)

	2004 Combined	2003 Combined
Resources Used to Finance Activities:		
Budgetary Resources Obligated		
Obligations incurred	$11,072,994	$10,550,108
Less: Spending authority from offsetting collections		
and recoveries (-)	(5,578,404)	(5,236,537)
Obligations net of offsetting collections and recoveries	$5,494,590	$5,313,571
Less: Offsetting receipts (-)	(1,592,297)	(904,214)
Net obligations	$3,902,293	$4,409,357
Other Resources		
Donations and forfeitures of property	435	4,648
Transfers in/out without reimbursement (+/-)	(1,632)	(56,344)
Imputed financing from costs absorbed by others	239,548	225,066
Other (+/-)	579	(19,379)
Net other resources used to finance activities	238,930	153,991
Total resources used to finance activities	$4,141,223	$4,563,348
Resources Used to Finance Items not Part of the Net Cost of Operations		
Change in budgetary resources obligated for goods		
services and benefits ordered but not yet provided		
Undelivered Orders (-)	($400,175)	($154,315)
Unfilled Customer Orders	302,216	245,807
Resources that fund expenses recognized in prior periods	(55,278)	0
Budgetary offsetting collections and receipts that		
do not affect net cost of operations	1,592,297	904,695
Resources that finance the acquisition of assets	(1,684,000)	1,399,859
Other resources or adjustments to net obligated resources		
that do not affect net cost of operations		
Less: Trust or Special Fund Receipts Related to Exchange in the Entity's Budget (-	(10,000)	0
Other (+/-)	1,636	0
Total resources used to finance items not part of the net cost of operations	($253,304)	$2,396,046
Total resources used to finance the net cost of operations	$3,887,919	$6,959,394
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		
Increase in annual leave liability	$0	$0
Increase in environmental and disposal liability	0	0
Upward/Downward reestimates of credit subsidy expense (+/-)	0	0
Increase in exchange revenue receivable from the the public (-	0	0
Other (+/-)	50,966	66,422
Total components of Net Cost of Operations that		
will require or generate resources in future periods	$50,966	$66,422
Components not Requiring or Generating Resources		
Depreciation and amortization	2,373,460	447,661
Revaluation of assets or liabilities (+/-)	(822,198)	1,477,630
Other (+/-)		
Trust Fund Exchange Revenue	0	0
Cost of Goods Sold	0	0
Operating Material & Supplies Used	0	0
Other	2,586,589	24,662
Total components of Net Cost of Operations that		
will not require or generate resources	$4,137,851	$1,949,953
Total components of net cost of operations that		
will not require or generate resources in the current period	$4,188,817	$2,016,375
Net Cost of Operations	$8,076,736	$8,975,769

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 U.S. Army Corps of Engineers (USACE) Civil Works, as required by the "Chief Financial Officers (CFO) Act of 1990," expanded by the "Government Management Reform Act (GMRA) of 1994," and other appropriate legislation. The financial statements have been prepared from the books and records of the USACE in accordance with the "Department of Defense Financial Management Regulation (DoDFMR)," the Office of Management and Budget (OMB) Bulletin No. 01-09, "Form and Content of Agency Financial Statements" and, to the extent possible, generally accepted accounting principles (Federal GAAP). USACE financial statements are in addition to the financial reports also prepared by USACE pursuant to OMB directives that are used to monitor and control the USACE's use of budgetary resources.

USACE financial statements are prepared from the consolidation of general ledger financial data reported from the Corps of Engineers Financial System (CEFMS) to the Corps of Engineers Enterprise Management Information System (CEEMIS).

A more detailed explanation of these financial statements elements is provided in the applicable footnote.

1.B. Mission of the Reporting Entity

Some of the missions of USACE include maintaining navigation channels, reducing flooding, assisting during natural disasters and other emergencies and making waterways passable. The financial statements are presented on the accrual basis of accounting as required by federal financial accounting standards.

The asset accounts used to prepare the principal financial statements are categorized as entity/non-entity. Entity accounts consist of resources that the agency has the authority to use, or where management is legally obligated to use funds to meet entity obligations. Non-entity accounts are assets that are held by an entity but are not available for use in the operations of the entity.

USACE Civil Works Program receives Federal funding through annual Energy and Water Development Appropriations Acts. Program funding is also received from non-Federal project sponsors who share in project costs according to formulas established by project authorization acts. A third source of funding comes through the Support for Others Program, which is conducted under reimbursable agreements with Federal agencies.

Entity Accounts:

General Funds	
96X3112	Flood Control, Mississippi River and Tributaries
96X3121	General Investigations
96 3121	General Investigations (fiscal year)
96X3122	Construction, General
96X3123	Operation and Maintenance, General
96X3124	General Expenses
96X3125	Flood Control and Coastal Emergencies
96X3126	Regulatory Program
96X3128	Washington Aqueduct Capital Improvements
96 3129	Payment to the South Dakota Terrestrial Wildlife Habitat Restoration Trust Fund (fiscal year)
96X3130	FUSRAP
96X6094	Advances from the District of Columbia

Revolving Funds

96X4902	Revolving Fund

Special Funds

96X5007	Special Recreation Use Fees
96X5066	Hydraulic Mining in California, Debris
96X5090	Payments to States, Flood Control Act of 1954
96X5125	Maintenance and Operation of Dams and Other Improvements of Navigable Waters
96X5493	Fund for Non-Federal Use of Disposal Facilities

Trust Funds

96X8217	South Dakota Terrestrial Wildlife habitat Restoration Trust Fund
96X8333	Coastal Wetlands Restoration Trust Fund
96 20X8861	Inland Waterways Trust Fund
96X8862	Rivers and Harbors Contributed and Advance Funds
96 20X8863	Harbor Maintenance Trust Fund

Transfer Funds

96 12X1105	State and Private Forestry, Forest Service
96 13X2050	Economic Development Administration
96 14X1039	Construction National Park Service
96 14X5035	Land Acquisition and State Assistance, National Park Service
96 21X2020	OMA, American Samoa Projects
96 69X8083	Federal Aid Highways
96 89X4045	Bonneville Power Administration
96 72 99/00 1021	Development Assistance, Agency for International Development

Non-Entity:

Deposit Funds

96X6500	Advances without Orders from Non-Federal Sources
96X6501	Small Escrow Amounts

Clearing Accounts

96F3875	Budget Clearing Account
96F3880	Unavailable Check Cancellations and Overpayments
96F3885	Undistributed Intergovernmental Payments

Receipt Accounts

960891	Miscellaneous fees for regulatory and judicial services, not otherwise classified
961060	Forfeitures of Unclaimed Money and Property
961099	Fines, Penalties, and Forfeitures Not Otherwise Classified
961435	General Fund Proprietary Interest, Not Otherwise Classified
963220	General Fund Proprietary Receipts. Not Otherwise Classified, All Other
965007	Special Recreation Use Fees
965066	Hydraulic Mining in California
965090	Receipts from leases of lands acquired for flood control, navigation, and allied purposes
965125	Licenses under Federal Power Act, Improvements of navigable water, maintenance and operation of dams, etc., (50%)
965493	User Fees, Fund for Non-Federal Use of Disposal Facilities

Obsolete Accounts

96X3930	96X8868	96 5493
96 13X1450	96 20X8145	
96 14X2301	96F3879	
96 19 00 1082	96F3886	
96 46X0200	960199	
96 47X4542	960869	
96 67X0204	961030	
96 72 00/01 1021	961040	
96 89X0224	961210	
96X6050	961299	
96X6075	961499	
96X6134	962413	
96X6145	962814	
96X6275	963102	
96X6302	965005	
96X6999	96 3124	

1.C. Appropriations and Funds

USACE's appropriations and funds are divided into the general, working capital (revolving funds), trust, special and deposit funds. These appropriations and funds are used to fund and report how the resources have been used in the course of executing USACE missions.

The Civil Works Program receives Federal funding through annual Energy and Water Development Appropriations Acts. Program funding also comes from non-Federal project sponsors who share in project costs according to formulas established by project authorization acts. A third source of funding comes through the Supports for Others Program, which is conducted under reimbursable agreements with Federal agencies.

In 1997, USACE received borrowing authority from the Treasury for the three years 1997 through 1999 to finance capital improvements to the Washington Aqueduct. Appropriation 96X3128 was established to record financial transactions for these capital improvements.

General funds are used for financial transactions arising under congressional appropriations, including personnel, operation and maintenance, research and development, procurement, and construction accounts.

Trust funds represent the receipt and expenditure of funds held in trust by the government for use in carrying out specific purposes or programs in accordance with the terms of the donor, trust agreement, or statute.

Special funds account for receipts of the government that are earmarked for a specific purpose.

Deposit funds generally are used to (1) hold assets for which USACE is acting as an agent or a custodian or whose distribution awaits legal determination, or (2) account for unidentified remittances.

1.D. Basis of Accounting

USACE's transactions are generally recorded on an accrual accounting basis and a budgetary basis as is required by Federal GAAP. Under the accrual method, revenues are recognized when earned and expenses are recognized when a liability is incurred without regard to receipt or payment of cash. Budgetary accounting is accomplished through unique general ledger accounts to facilitate compliance with legal and internal control requirements associated with the use of federal funds.

CEFMS is used at all divisions, districts, centers, laboratories and field offices. CEFMS is a fully automated, comprehensive financial management system that simplifies the management of all aspects of the USACE business, including civil, military, revolving funds and reimbursable activity. The general ledger chart of accounts in CEFMS is substantially compliant with the U.S. Government Standard General Ledger.

In addition, USACE identifies programs based upon the major appropriation groups provided by Congress.

1.E. Revenues and Other Financing Sources

Financing sources for general funds are provided primarily through congressional appropriations that are received on both an annual and a multiyear basis. When authorized, these appropriations are supplemented by revenues generated by sales of goods or services through a reimbursable order process. USACE recognizes revenue as a result of costs incurred or services performed on behalf of other federal agencies and the public. Revenue is recognized when earned under the reimbursable order process.

1.F. Recognition of Expenses

For financial reporting purposes, the DoD policy requires the recognition of operating expenses in the period incurred. Expenditures for capital and other long-term assets are not recognized as expenses in USACE operations until depreciated in the case of PP&E or consumed in the case of OM&S. Net increases or decreases in unexpended appropriations are recognized as a change in the net position.

Certain expenses, such as annual and military leave earned but not taken, are financed in the period when earned.

1.G. Accounting for Intra-governmental Activities

USACE, as an agency of the federal government, interacts with and is dependent upon the financial activities of the federal government as a whole. Therefore, these financial statements do not reflect the results of all financial decisions applicable to USACE as though the agency were a stand alone entity.

USACE's proportionate share of public debt and related expenses of the federal government are not included. Debt issued by the federal government and the related costs are not apportioned to federal agencies. USACE'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.

Financing for the construction of DoD facilities is obtained through budget 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 Department of the Treasury does not allocate such interest costs to the benefiting agencies.

USACE's civilian employees participate in the Civil Service Retirement System (CSRS) and the Federal Employees Retirement Systems (FERS), while military personnel are covered by the Military Retirement System (MRS). Additionally, employees and personnel covered by FERS and MRS also have varying coverage under Social Security. USACE funds a portion of the civilian and military pensions. Reporting civilian pension under CSRS and FERS retirement systems is the responsibility of the Office of Personnel Management (OPM). USACE recognizes an imputed expense for the portion of civilian employee pensions and other retirement benefits funded by the OPM in the Statement of Net Cost, and recognizes corresponding imputed revenue from the civilian employee pensions and other retirement benefits in the Statement of Changes in Net Position.

The Department of Defense reports the assets, funded actuarial liability, and unfunded actuarial liability for the military personnel in the Military Retirement Fund (MRF) financial statements. The Department of Defense recognizes the actuarial liability for the military retirement health benefits in the Other Defense Organization General Fund column of the DoD Agency wide consolidating/combining statements.

To prepare reliable financial statements, transactions occurring between entities within the Department or between two or more federal agencies must be eliminated. USACE is responsible for eliminating transactions between components and activities.

The Department of the Treasury, Financial Management Service (FMS) is responsible for eliminating transactions between the Department and other federal agencies. In September 2000, the Department of the Treasury, FMS issued the "Federal Intragovernmental Transactions Accounting Policies and Procedures Guide." USACE implemented the policies and procedures in this guide related to reconciling intragovernmental assets, liabilities, revenues, and expenses for non-fiduciary transactions. In addition, USACE implemented the policies and procedures contained in the "Intragovernmental Fiduciary Transactions Accounting Guide," as updated by the "Federal Intragovernmental Transactions Accounting Policies and Procedures Guide," issued October 2002, for reconciling intragovernmental transactions. These transactions pertain to investments in Federal securities, borrowings from United States (U.S.) Treasury and the Federal Financing Bank, Federal Employees' Compensation Act transactions with the Department of Labor (DoL), and benefit program transactions with the OPM.

1.H. Transactions with Foreign Governments and International Organizations

Each year, the DoD Components sell defense articles and services to foreign governments and international organizations, primarily under the provision of the "Arms Export Control Act of 1976." Under the provision of the Act, the Department 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. Customers may be required to make payments in advance.

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

USACE's financial resources are maintained in U.S. Treasury accounts. The majority of cash collections, disbursements, and adjustments are processed worldwide at the Defense Finance and Accounting Service (DFAS) and Military Services and the USACE disbursing stations, as well as the Department of State financial service centers. Each disbursing station prepares monthly reports which provide information to the U.S. Treasury on check issues, electronic transfers, interagency transfers and deposits.

In addition, the DFAS centers and the USACE Finance Center submit reports to the Department of the Treasury, by appropriation, on interagency transfers, collections received and disbursements issued. The Department of the Treasury then records this information to the applicable Fund Balance with Treasury (FBWT) account maintained in the Treasury's system. Differences between the USACE recorded balance in the FBWT accounts and Treasury's FBWT accounts sometimes result and are subsequently reconciled. Material disclosures are provided at Note 3. Differences between accounting offices' detail-level records and Treasury's FBWT accounts are disclosed in Note 3, specifically, differences caused by in-transit disbursements and unmatched disbursements (which are not recorded in the accounting offices' detail-level records).

1.J. Foreign Currency

USACE conducts operations overseas. Foreign Currency fluctuations require adjustment to the original obligation amount at the time of payment. These currency fluctuations are not separately identified.

1.K. Accounts Receivable

As presented in the Balance Sheet statement, accounts receivable includes 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 Department 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. Material disclosures are provided at Note 5.

1.L. Loans Receivable

Not applicable.

1.M. Inventories and Related Property

Inventories are reported at approximate historical cost based on a moving weighted average that is based on actual cost divided by quantity. A perpetual record of inventory is maintained in CEFMS to allow for recomputation of the average unit cost as new receipts are recorded.

The related property portion of the amount reported on the Inventory and Related Property line includes operating materials and supplies (OM&S). The OM&S are valued at standard purchase price. For the most part, the Department is using the consumption method of accounting for OM&S, as defined in the SFFAS No. 3, "Accounting for Inventory and Related Property" as material that has not been issued to the end user. Once OM&S is issued, the material is expensed. Material disclosures related to inventory and related property is provided at Note 9.

In addition, past audit results identified uncertainties about the completeness and existence of quantities used to produce the reported values. Material disclosures related to inventory and related property is provided at Note 9.

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

Investments in U. S. Treasury securities are reported at cost, net of unamortized premiums or discounts. Premiums or discounts are amortized into interest income over the term of the investment using the effective interest rate method or other method if similar results are obtained. USACE'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, because in the majority of cases, they are held to maturity. Amounts reported reflect the value of investments in the South Dakota Terrestrial Wildlife Habitat Restoration, Inland Waterways, and Harbor Maintenance Trust Fund accounts, which are managed by the Treasury Department. Material disclosures are provided at Note 4.

1.O. General Property, Plant and Equipment

General property, plant, and equipment (PP&E) assets are capitalized at historical acquisition cost plus capitalized improvements when an asset has a useful life of 2 or more years, and when the acquisition cost is greater than $25,000 with the exception of all buildings and structures related to hydro-power purpose which are capitalized (to include joint cost) regardless of cost. During FY 2003, USACE increased its buildings and structures threshold to $25K (from $0), with the exception previously stated. All Civil Works Buildings and Structures currently capitalized under $25K (excluding Revolving Fund and hydro-power) were expensed in FY 2003 and removed from CEFMS. Starting in FY 2004, all Civil Works Buildings and Structures under $25K were expensed except for hydro-power assets.

All General PP&E, other than land, is depreciated on a straight-line basis. Land is not depreciated.

In FY 2004, USACE, OSD(C), and DoDIG reached an agreement on supporting documentation for Land values to include administrative costs. USACE is in the process of gathering the necessary supporting documentation in accordance with the Memorandum of Agreement signed on 9 June 2004.

When it is in the best interest of the government, USACE provides to contractors government property necessary to complete contract work. Such property is either owned or leased by USACE, or 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, such PP&E is required to be included in the value of General PP&E reported on the USACE Balance Sheet. The Department of Defense completed a study that indicates that the value of General PP&E above the DoD capitalization threshold and not older than the DoD Standard Recovery Periods for depreciation, and that is presently in the possession of contractors, is not material to the Department's financial statements. Regardless, the Department is developing new policies and a contractor reporting process that will provide appropriate General PP&E information for future financial statement reporting purposes. Accordingly, USACE currently reports only government property in the possession of contractors that is maintained in the USACE property systems.

To bring USACE into compliance with federal accounting standards, the Department has issued new property accountability and reporting regulations that require the DoD Components to maintain, in DoD Component 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.

Material disclosures are provided at Note 10.

1.P. Advances and Prepayments

Payments in advance of the receipt of goods and services are recorded as advances or prepayments and reported as an asset on the Balance Sheet. Advances and prepayments are recognized as expenditures and expenses when the related goods and services are received.

1.Q. Leases

Generally, lease payments are for the rental of equipment, space, and operating facilities and are classified as either capital or operating leases. When a lease is essentially equivalent to an installment purchase of property (a capital lease), USACE records the applicable asset and liability if the value equals or exceeds the current DoD capitalization threshold. USACE records the amounts as the lesser of the present value of the rental and other lease payments during the lease term (excluding that portion of the payments representing executory costs paid to the lessor) or the asset's fair value. Leases that do not transfer substantially all of the benefits or risks of ownership are classified as operating leases and recorded as expenses as payments are made over the lease term.

1.R. Other Assets

USACE 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, USACE provides financing payments. One type of financing payment that USACE makes, for real property, is based upon a percentage of completion. In accordance with the SFFAS No. 1, "Accounting for Selected Assets and Liabilities," such payments are treated as construction in process and are reported on the General PP&E line and in Note 10, General PP&E, Net.

In addition, based on the provision of the Federal Acquisition Regulation, USACE makes financing payments under fixed price contracts that are not based on a percentage of completion. USACE reports these financing payments as advances or prepayments in the "Other Assets" line item. USACE treats these payments as advances or prepayments because USACE becomes liable only after the contractor delivers the goods in conformance with the contract terms. If the contractor does not deliver a satisfactory product, USACE is not obligated to reimburse the contractor for its costs and the contractor is liable to repay USACE for the full amount of the advance.

DoD has completed a review of all applicable federal accounting standards; applicable public laws on contract financing; Federal Acquisition Regulation Parts 32, 49, and 52; and the OMB guidance in 5 Code of Federal Regulations Part 1315, "Prompt Payment." DoD concluded that SFFAS No. 1 does not fully or adequately address the subject of progress payment accounting and is considering what further action is appropriate.

1.S. Contingencies and Other Liabilities

The SFFAS No. 5, "Accounting for Liabilities of the Federal Government," defines a contingency as an existing condition, situation, or set of circumstances that involves an uncertainty as to possible gain or loss to USACE. The uncertainty will be resolved when one or more future events occur or fail to occur. A contingency is recognized as a liability when a past event or exchange transaction has occurred, a future loss is probable and the amount of loss 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 that a loss or additional loss will be incurred. Examples of loss contingencies include the collectibility of receivables, pending or threatened litigation, possible claims and assessments. USACE's loss contingencies arising as a result of pending or threatened litigation or claims and assessments occur due to events such as ship and vehicle accidents, property or environmental damages, and contract disputes.

1.T. Accrued Leave

Civilian annual leave and military leave that have been accrued and not used as of the balance sheet date are reported as liabilities. The liability reported at the end of the fiscal year reflects current pay rates.

1.U. Net Position

Net Position consists of unexpended appropriations and cumulative results of operations. Unexpended appropriations represent amounts of authority which are unobligated and have not been rescinded or withdrawn, and amounts obligated but for which legal liabilities for payments have not been incurred.

Cumulative results of operations represent the difference, since inception of an activity, between expenses and losses and financing sources (including appropriations, revenue, and gains). Beginning with FY 1998, this included the cumulative amount of donations and transfers of assets in and out without reimbursement

1.V. Treaties for Use of Foreign Bases

USACE has no existing treaties for use of foreign bases

1.W. Comparative Data

The Financial Statements and accompanying Notes to the Financial Statements report the financial position and results of operations for FY2004. Financial statement fluctuations greater than 2 percent of total assets on the Balance Sheet and/or greater than 10 percent between FY2003 and FY2004 are explained within the Notes to the Financial Statements.

1.X. Unexpended Obligations

USACE records obligations for goods and services that have been ordered but not yet received. No liability for payment has been established in the financial statements because goods/services have yet to be delivered.

1.Y. Problem Disbursements

(Amounts in thousands)	September 2002	September 2003	September 2004
1. Total Problem Disbursements			
Absolute Unmatched Disbursements	$0	$0	$0
Negative Unliquidated Obligations	$0	$0	$0
2. Total In-transit Disbursements, Net	$0	$0	$1,307

Other Information Related to Problem Disbursements and In-transit Disbursements.

USACE had disbursements of $867 thousand that were not reported to Treasury in the Intragovernmental Payment and Collection System (IPAC) until October 2004. The IPAC System cutoff for transactions is five days before month end. There were $440 thousand in deposits at Treasury that were not recorded by USACE until October 2004.

Note 2. Nonentity Assets

As of September 30 (Amounts in thousands)	2004	2003
1. Intragovernmental Assets		
A. Fund Balance with Treasury	$8,245	$6,865
B. Investments	0	0
C. Accounts Receivable	0	0
D. Other Assets	0	0
E. Total Intra-governmental Assets	$8,245	$6,865
2. Non-Federal Assets		
A. Cash and Other Monetary Assets	$1,039	$1,278
B. Accounts Receivable	1,843,102	1,871,575
C. Loans Receivable	0	0
D. Inventory & Related Property	0	0
E. General PP&E	0	0
F. Investments	0	0
G. Other Assets	0	0
H. Total Non-Federal Assets	$1,844,141	$1,872,853
3. Total Non-Entity Assets	$1,852,386	$1,879,718
4. Total Entity Assets	$34,214,147	$36,526,738
5. Total Assets	$36,066,533	$38,406,456

Asset accounts are categorized either as entity or nonentity. Entity accounts consist of resources that the agency has authority to use, or when management is legally obligated to use funds to meet entity obligations. Nonentity assets are assets that are held by an entity, but are not available for use in the operations of the entity.

The schedule format has changed from prior year to comply with Office of Management and Budget Bulletin 01-09.

Composition of Other Nonentity Assets

Intra-governmental Non-Entity Fund Balance with Treasury consists of amounts collected into deposit, suspense and budget clearing accounts.

Cash and Other Monetary Assets is comprised of $4 thousand in change funds for recreation cashiers, $567 thousand in Disbursing Officer’s cash, and $468 thousand in foreign currency, as listed in Note 7.

Non-federal nonentity Accounts Receivable represents all current and non-current receivables due from non-federal sources. Non-entity receivables (net of allowance) include $873,298 thousand in long-term receivables due from state and local municipalities for water storage contracts, $31,683 thousand in current receivables due from state and local municipalities for water storage, $930,140 thousand in accrued Interest Receivable, $1,759 thousand in penalties, fines and Administrative Fees Receivable, $1,400 thousand in

Long-Term Receivable for hydraulic mining, and $4,092 thousand for other miscellaneous receivables. An additional $730 thousand represents the amount due from the leasing of land acquired for flood control purposes. Non-entity receivables are recorded in unavailable receipt accounts and funds will be returned to Treasury when collected. The Allowance for Doubtful Accounts totals $2,883 thousand for non-entity receivables.

Fluctuations

Line 1A. This line contains suspense account items for bid deposits and lease collections totaling $8,245 thousand, an increase of $1,380 thousand. The increase is due to increased lease collections during 4th quarter FY 2004.

Line 2A. The decrease in cash and other monetary assets is due a reduction of outstanding travel advances.

Note Reference

For Additional Line Item discussion, see:
Note 3, Funds Balance With Treasury
Note 4, Investments
Note 5, Accounts Receivable
Note 6, Other Assets
Note 7, Cash and Other Monetary Assets
Note 9, Inventory and Related Property
Note 10, General PP&E, Net

Note 3.A. Fund Balance with Treasury

As of September 30 (Amounts in thousands)	2004	2003
1. Fund Balances		
A. Appropriated Funds	$970,538	$1,127,663
B. Revolving Funds	902,212	990,006
C. Trust Funds	72,121	67,482
D. Other Fund Types	441,816	410,571
E. Total Fund Balances	$2,386,687	$2,595,722
2. Fund Balances Per Treasury Versus Agency		
A. Fund Balance per Treasury	$2,906,916	$2,530,007
B. Fund Balance per USACE	2,386,687	2,595,722
3. Reconciling Amount	$520,229	($65,715)

Fund Balance per USACE includes $70,165 thousand cash reported by Treasury for Inland Waterways and Harbor Maintenance Trust Funds, for which the USACE is identified as the lead agency for reporting.

Fund Balance per USACE includes disbursements of $867 thousand that were not reported to Treasury in the IPAC system until October 2004 and is reflected on the TFS6652 Statement of Differences - Disbursements. Fund Balance per USACE does not include deposits of $440 thousand in CASHLINK and is reflected on the TFS6652 Statement of Differences – Deposits. These were recorded in October 2004.

Fund Balance per Treasury includes $590,393 thousand in receipt accounts. USACE closed receipt accounts per Treasury Financial Management Transmittal Letter S2-04-02, dated September 2004, transaction code F124, but they were included on the Treasury 6655 at 30-Sep-2004.

4. Other Information Related to Fund Balance with Treasury

Fund Balance per USACE includes $16,156 thousand in transfer appropriations that were not reported by the USACE in the Treasury FACTS II System. Those transfer appropriations are reported by the parent agencies on the FMS 2108. The parent agencies are Department of Energy, Department of Transportation, and Department of Commerce. According to the Treasury Financial Manual, Part 2, Chapter 4000, *Federal Agencies' Centralized Trial-Balance System*, paragraph 4030.60, if an allocation transfer is material to the child's financial statements, the child should report the activity relating to the allocation in all of its financial statements, except the Statement of Budgetary Resources. The USACE has determined that these balances are material and have included them in all of our financial statements.

Appropriated Funds includes disbursements in transit for undistributed Intergovernmental Payments and Collections of ($25,577) thousand. These were distributed to the appropriate funds during October 2004.

Other Fund types (nonentity) consist of $8,245 thousand in deposit, suspense and clearing accounts that are not available to finance the USACE's activities. Other Fund Types (entity) consists of $27 thousand in borrowing authority, $408,009 thousand in contributed funds, and $25,534 thousand in the suspense account established to finance Washington Aqueduct operations and are available to finance the USACE's activities.

Entity accounts consist of resources that the agency has the authority to use, or when management is legally obligated to use funds to meet entity obligations. Nonentity accounts are assets that are held by an entity, but are not available for use in the operation of the entity.

There are no restrictions for future use of unobligated balance.

The Fund Balance with Treasury line does not include any amounts for which the Department of the Treasury is willing to accept corrections to cancelled appropriation accounts, in accordance with the Statement of Federal Financial Accounting Standards (SFFAS) No. 1, "Accounting for Selected Assets and Liabilities."

Fluctuations

Appropriated Funds - The decrease in Appropriated Funds is due to $773 thousand in Borrowing Authority that was reported as Appropriated Funds in FY 2003. The Borrowing Authority was reported as Other Funds in FY 2004. USACE currently has a ($24,689) thousand balance in the Flood Control and Coastal Emergencies (96X3125) due to an unprecedented hurricane season with four named storms reaching the continental United States causing significant damage. As the Federal Emergency Management Agency's (FEMA) Emergency Support Function for Engineering, USACE has received over $848,000 thousand in funding authority to perform numerous missions to support those affected by the four hurricanes. Since these missions are funded on a reimbursable basis, USACE was required to finance these large disbursements through their 96X3125 appropriation causing the negative balance. In FY 2005 this negative balance will be reduced as USACE receives collections from FEMA. Appropriated Funds also includes a net of ($25,578) thousand in IPAC transactions recorded in Deposit Funds. The Deposit Funds were recorded as Other Funds in FY2003.

Reconciling Amount - The increase in the Reconciling Amount is due to the Fund Balance per Treasury that includes $590,393 thousand in receipt accounts. USACE closed receipt accounts per Treasury Financial Management Transmittal Letter S2-04-02, dated September 2004, transaction code F124, but it was included on the Treasury 6655 at 30-Sep-2004.

Note Reference

Note Disclosure 1.I. – Significant Accounting Policies for additional discussion on financial reporting requirements and DoD policies governing Funds with the U.S. Treasury.
Note 2 for Entity/Nonentity Accounts
Note 18 for Status of Unexpended Balance.

Note 3.B. Disclosures Related to Suspense/Budget Clearing Accounts

As of September 30 (Amounts in thousands)	September 2002	September 2003	September 2004	(Decrease)/ Increase from FY 2003 - 2004
Account				
F3875	$14,228	$850	$113	($737)
F3880	0	0	(0)	0
F3882	0	0	0	0
F3885	0	0	0	0
F3886	0	0	0	0
Total	$14,228	$850	$113	($737)

The decrease of $737 thousand in Budget Clearing Account F3875 is attributed to funds for Permanent Change in Station (PCS), Homeowners Assistance Program (HAP), and travel that were disbursed to the Internal Revenue Service.

Under the authority of Section 1009 of Public Law 107-314, "Clearance of Certain Transactions Recorded in Treasury Suspense Accounts and Resolution of Certain Check Issue Discrepancies," no funds were written-off from the suspense accounts.

Note 4. Investments

As of September 30 (Amounts in thousands)	2004					2003
	Cost	Amortization Method	Amortized (Premium/ Discount)	Investments, Net	Market Value Disclosure	Investments, Net
1. Intragovernmental Securities:						
A. Marketable	$0		$0	$ 0	$0	$0
B. Non-Marketable, Par Value	0		0	0	0	0
C. Non-Marketable, Market-Based	2,788,938		(60,807)	2,728,131	2,403,145	2,466,771
D. Subtotal	$2,788,938		($60,807)	$2,728,131	$2,403,145	$2,466,771
E. Accrued Interest	$13,786			$13,786	$13,786	$11,683
F. Total Intragovernmental Securities	$2,802,724		($60,807)	$2,741,917	$2,416,931	$2,478,454
2. Other Investments:	$0		0	$0	N/A	$0

3. Other Information:

Investments for the Inland Waterways, Harbor Maintenance, and South Dakota Terrestrial Wildlife Habitat Restoration Trust Funds are reported by the Treasury and included in U.S. Army Corps of Engineers' Financial Statements. Investments include $278,392 thousand in one-day certificates and $2,449,739 thousand in bonds and notes. Total investment amounts include $375,544 thousand in Inland Waterways, $2,302,579 thousand in Harbor Maintenance and $63,793 thousand in the South Dakota Terrestrial Wildlife account.

Investments are held until maturity. As funds are needed to sustain operations, withdrawals are made from the one-day certificate investment account. Provisions are not made for unrealized gains or losses on these securities. The Trust Funds use the same method that conforms to the prevailing practice in the financial community to determine the amortized book value of investments currently held and the related effective interest yield on investments. These calculated yields agree with yields published in the security tables of U.S. Treasury securities.

These types of investments are recorded at cost, net of unamortized premiums or discounts. Premiums or discounts are amortized into interest income over the term of the investment. Investment decisions for these funds are made by the managing entity, in this case the Department of the Treasury.

The Department of the Treasury also provides the investment market value, based on the bid price provided by the Federal Reserve Bank of New York on September 30, 2004.

Note Reference

See Note Disclosure 1.N. – Investments in U. S. Treasury for additional DoD policies governing Investments in U.S. Treasury Securities.
See Note 21A for further discussion of Trust Funds.

Fluctuations

Line 1C. Non-Marketable, Market Based Securities: Investment increase is due to the increase in tax revenues in Trust Funds. Tax revenues are from imports, domestics, excise, foreign trade and passengers. The tax revenues are invested by the Treasury and reported on the financial statements for the Harbor Maintenance and Inland Waterways Trust Funds.

Line 1E. Accrued Interest: The accrued interest on investments also increased due to the increase in investments through tax collections.

Note 5. Accounts Receivable

As of September 30 (Amounts in thousands)	2004 Gross Amount Due	2004 Allowance For Estimated Uncollectibles	2004 Accounts Receivable, Net	2003 Accounts Receivable, Net
1. Intragovernmental Receivables:	$520,123	N/A	$520,123	$423,774
2. Non-Federal Receivables (From the Public):	$1,910,995	($4,560)	$1,906,435	$1,935,567
3. Total Accounts Receivable:	$2,431,118	($4,560)	$2,426,558	$2,359,341

4. Allowance method:

The method of calculating the allowance for estimated uncollectibles is based on the cumulative balance of delinquent public receivables aged in accordance with current USACE policy. The calculation was performed automatically in the Corps of Engineers Financial Management System.

The Code of Federal Regulations (4CFR 101) prohibits the write-off of receivables from another federal agency. As such, no allowance for estimated uncollectible amounts is recognized for these receivables.

5. Other information:

Elimination Adjustments

The Corps was able to compare its Accounts Receivable balances with the Accounts Payable balances of its intragovernmental trading partners. No material differences were identified.

Receivables with Other Federal Agencies (Non-Defense)

Receivable for amounts to be transferred from the Aquatic Resources Trust Fund (Department of Interior) for currently invested balances to the Corps is $25,381 thousand more than at this time last year.

Receivables with National Aeronautics and Space Administration decreased by $10,318 thousand as a result of collections received. Receivables with Federal Emergency Management Agency decreased entirely (by $19,004 thousand) as they were transferred to Department of Homeland Security. Receivables with Department of Homeland Security increased by $79,332 thousand as a result of proper identification of agencies transferred to AT70 trading partner. Some activities previously identified under other agencies are now reported under Department of Homeland Security.

Receivables previously identified as receivables from Treasury (TI 95) have been reclassified to public. The receivables are from District of Columbia Public Schools.

Receivables for amount to be transferred from Inland Waterways Trust Funds (Treasury) are $2,518 thousand more than at this time last year.

Intragovernmental Receivables Over 180 Days

The amount of intragovernmental receivables over 180 days old is $9,606 thousand. No intragovernmental receivables have been submitted to the General Accounting Office for opinion.

Public Receivables Over 180 Days

The amount of public receivables over 180 days old is $73,080 thousand. Receivables with the public include $43,003 thousand in Accrued Interest on Receivables over 180 days old.

Nonfederal Refunds Receivable

The amount of public receivables includes $174 thousand in Refunds Receivable.

Other Disclosures

Public receivables include $32,499 thousand in current and $873,298 thousand in Long-Term Accounts Receivable (principal) associated with water storage contracts, $932,060 thousand in Accrued Interest Receivable, and $1,901 thousand in penalties, fines, and administrative fees receivable. Public receivables also include $1,400 thousand in Long-Term Receivable for hydraulic mining and $736 thousand due from the leasing of land acquired for flood control purposes, and $63,121 thousand due from the D.C. Public Schools and Department of Housing. The remaining $6,048 thousand is for various other Accounts Receivable.

The amount of Public Receivables on the Treasury Report on Receivables Due from the Public is $3,952 thousand more than the balance of public receivables reported on the balance sheet. The difference is attributed to the amount of work-in-progress for $608 thousand less the allowance for estimated uncollectibles of $4,560 thousand not reported on the Treasury Report on Receivables.

Total trust fund receivables for currently invested balances are $362,452 thousand. The breakdown between funds follows. Trust fund receivables for currently invested balances include $352,546 thousand for the Coastal Wetlands Restoration Trust Fund and $9,907 thousand for the Inland Waterways Trust Fund. To accommodate cash management practices, funds will remain invested until needed for disbursement. The budget authority is realized and obligations may be incurred before the actual transfer of funds.

Fluctuations

Line 1. Intra-governmental receivables increased by $96,349 thousand from last year, of which $79,332 thousand was comprised of Federal Emergency Management Agency transactions due to increased activity as a result of hurricanes and disaster relief efforts in Florida and coastal areas.

Note Reference

See Note Disclosure 1.K. - Significant Accounting Policies for additional discussion on financial reporting requirements and DoD policies governing Accounts Receivable.

Note 6. Other Assets

Not applicable

Note Reference

See Note Disclosure 1. R. - Significant Accounting Policies for additional discussion on financial reporting requirements and DoD policies governing Other Assets.

Note 7. Cash and Other Monetary Assets

As of September 30 (Amounts in thousands)	2004	2003
1. Cash	$571	$772
2. Foreign Currency (non-purchased)	468	506
3. Other Monetary Assets	0	0
4. Total Cash, Foreign Currency, & Other Monetary Assets	$1,039	$1,278

5. Other Information Pertaining to Entity Cash & Other Monetary Assets:

Definitions

Cash – The total of cash resources under the control of the Corps which includes coin, paper currency, purchased foreign currency, negotiable instruments, and amounts on deposit in banks and other financial institutions. Cash available for agency use should include petty cash funds and cash held in revolving funds which will not be transferred into the U.S. Government General Fund.

Foreign Currency – Consists of the total U.S. dollar equivalent of non-purchased foreign currencies held in foreign currency fund accounts. Non-purchased foreign currency is limited to the Treasury Index 97X7000 fund account (formerly called FT accounts).

Other Monetary Assets - Includes gold, special drawing rights, and U.S. Reserves in the International Monetary Fund. This category is principally for use by the Department of the Treasury.

Other Corps Disclosures

Cash consists of $567 thousand in Disbursing Officers' Cash and $4 thousand in change funds for recreation cashiers.

The Corps translates foreign currency to U. S. dollars utilizing the Department of the Treasury Prevailing Rate of Exchange. This rate is the most favorable rate that would legally be available to the U. S. Government's acquisition of foreign currency for its official disbursements and accommodation of exchange transactions.

Fluctuations

Cash. The decrease in Disbursing Officers' cash is due to a decrease in travel advances issued.

Note Reference

See Note Disclosure 1. J.- Significant Accounting Policies, for additional discussion on financial reporting requirements and DoD policies governing Foreign Currency.

Note 8. A. Direct Loan and/or Loan Guarantee Programs
Not applicable

Note 8.B. Direct Loans Obligated After FY 1991
Not applicable

Note 8.C. Total Amount of Direct Loans Disbursed
Not applicable

Note 8.D. Subsidy Expense for Post-1991 Direct Loans
Not applicable

Note 8.E. Subsidy Rate for Direct Loans
Not applicable

Note 8.F. Schedule for Reconciling Subsidy Cost Allowance Balances for Post-1991 Direct Loans
Not applicable

Note 8.G. Defaulted Guaranteed Loans from Post-1991 Guarantees
Not applicable

Note 8.H. Guaranteed Loans Outstanding
Not applicable

Note 8.I. Liability for Post-1991 Loan Guarantees, Present Value
Not applicable

Note 8.J. Subsidy Expense for Post-1991 Loan Guarantees
Not applicable

Note 8.K. Subsidy Rate for Loan Guarantees
Not applicable

Note 8.L. Schedule for Reconciling Loan Guarantee Liability Balances for Post-1991 Loan Guarantees
Not applicable

Note 8.M. Administrative Expense
Not applicable

Note 9. Inventory and Related Property

As of September 30 (Amounts in thousands)	2004	2003
1. Inventory, Net (Note 9.A.)	$61,671	$62,570
2. Operating Materials & Supplies, Net (Note 9.B.)	144	35
3. Stockpile Materials, Net (Note 9.C.)	0	0
4. Total	$61,815	$62,605

Note 9.A. Inventory, Net

As of September 30 (Amounts in thousands)	2004 Inventory, Gross Value	2004 Revaluation Allowance	2004 Inventory, Net	2003 Inventory, Net	Valuation Method
1. Inventory Categories:					
A. Available and Purchased for Resale	$88,810	$(47,092)	$41,718	$41,015	O
B. Held for Repair	0	0	0	0	
C. Excess, Obsolete, and Unserviceable	0	0	0	11	
D. Raw Materials	0	0	0	0	
E. Work in Process	19,953	0	19,953	21,544	O
F. Total	$108,763	$(47,092)	$61,671	$62,570	

Legend for Valuation Methods:

Adjusted LAC = Latest Acquisition Cost, adjusted for holding gains and losses
NRV = Net Realizable Value holding gains and losses
O = Other
SP = Standard Price

2. Restrictions of Inventory Use, Sale, or Disposition:

Inventory may be sold to foreign, state and local governments, private parties and contractors in accordance with current policies and guidance or at the direction of the U. S. President.

3. Other Information:

Definitions

Inventory Available and Purchased for Resale includes consumable spare and repair parts and repairable items owned and managed by the Department. Material available and purchased for resale includes material held due to a managerial determination that it should be retained to support military or national contingencies.

Inventory Held for Repair is damaged inventory that requires repair to make suitable for sale. Many of the inventory items are more economical to repair than to procure. In addition, because the Department often relies on weapon systems and machinery no longer in production, the Department 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 scrap materials or items that cannot be economically repaired and are awaiting disposal. Potentially reusable material, presented in previous years as "Excess, Obsolete and Unserviceable," is included in "Held for Use" or "Held for Repair" categories according to its condition.

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. The Work-in-Process designation may also be used to accumulate the amount paid to a contractor under cost reimbursable contracts, including the amount withheld from payment to ensure performance, and the amount paid to other Government plants for accrued costs of end-items of material ordered, but not delivered.

General Composition of Inventory

Inventory is tangible personal property that is (1) held for sale, (2) in the process of production for sale or (3) to be consumed in the production of goods for sale or in the provision of services for a fee. "Inventory held for Current Sale" is that expected to be sold in the normal course of operations. "Excess Inventory" is that which exceeds the demand expected in the normal course of operations and which does not meet management's criteria to be held in reserve for future sale. "Obsolete Inventory" is that which no longer is needed due to changes in technology, laws, customs or operations. "Unserviceable Inventory" is damaged inventory that is more economical to dispose of than to repair. Work in Process includes associated labor, applied overhead and supplies used in the deliver of services.

The inventory data reported on the financial statements is derived from the Corps of Engineers Financial Management System (CEFMS). CEFMS is a comprehensive system that is designed to capture and maintain historical cost data necessary to fully comply with the Statement of Federal Financial Accounting Standards Number 3, "Accounting for Inventory and Related Property."

The inventory valuation method is based on a moving weighted average based on actual cost divided by quantity. A perpetual record of inventory is maintained to allow for recomputation of the average unit cost as new receipts are recorded.

For regulatory discussion on Inventory, Net, see DoD FMR, Volume 6B, chapter 10, paragraph 1011.

Fluctuations

Excess, Obsolete, and Unserviceable - In FY 2003, the amount for Excess, Obsolete and Unserviceable was entered with an incorrect attribute. The amount of Excess, Obsolete, and Unserviceable should have been reported as Available and Purchased for Resale. Based on this, the figure for FY 2003 Excess, Obsolete, and Unserviceable should have been $.00 and Net Inventory Available and Purchased for Resale should have been $41,025,786.86.

Note Reference

See Note Disclosure 1. M. - Significant Accounting Policies for additional discussion on financial reporting requirements and DoD policies governing Inventory and related Property.

Note 9.B. Operating Materials and Supplies, Net

As of September 30
(Amounts in thousands)

1. OM&S Categories:	2004 OM&S Gross Value	2004 Revaluation Allowance	2004 OM&S, Net	2003 OM&S, Net	Valuation Method
A. Held for Use	$144	$0	$144	$35	O
B. Held for Repair	0	0	0	0	
C. Excess, Obsolete, and Unserviceable	0	0	0	0	
D. Total	$144	$0	$144	$ 35	

Legend for Valuation Methods:

Adjusted LAC = Latest Acquisition Cost, adjusted for holding gains and losses
NRV = Net Realizable Value holding gains and losses
O = Other
SP = Standard Price

2. Restrictions on OM&S:

There are no restrictions on operating materials and supplies. The valuation method is based on a moving weighted average based on actual cost divided by quantity.

3. Other Information:

For regulatory discussion on OM&S, see DoD FMR, volume 6B, Chapter 10, paragraph 101108.

Fluctuations

Operating Materials and Supplies - The increase in Operating Materials and Supplies is attributed to an increase in miscellaneous office supplies account at Fort Worth District.

Note Reference

See Note Disclosure 1. M. - Significant Accounting Policies for additional discussion on financial reporting requirements and DoD policies governing Inventory and related Property.

Note 9.C. Stockpile Materials, Net

Not applicable

Note 10. General PP&E, Net

As of September 30 (Amounts in thousands)	2004 Depreciation/ Amortization Method	Service Life	Acquisition Value	(Accumulated Depreciation/ Amortization)	Net Book Value	2003 Prior FY Net Book Value
1. Major Asset Classes:						
A. Land	N/A	N/A	$8,583,779	N/A	$8,583,779	$8,131,547
B. Buildings, Structures, and Facilities	S/L	2 - 100	27,975,596	($11,846,790)	16,128,806	18,280,188
C. Leasehold Improvements	S/L	lease term	26,467	(11,667)	14,800	17,121
D. Software	S/L	2 - 5	66,911	(40,445)	26,466	23,901
E. General Equipment	S/L	5 - 100	1,234,934	(602,094)	632,840	632,726
F. Military Equipment	S/L	Various	0	0	0	0
G. Assets Under Capital Lease [1]	S/L	lease term	0	0	0	0
H. Construction-in-Progress	N/A	N/A	3,018,921	N/A	3,018,921	3,788,250
I. Other			44,963	(2,058)	42,905	35,323
J. Total General PP&E			$40,951,571	($12,503,054)	$28,448,517	$30,909,056

[1]Note 15.B for additional information on Capital Leases

Legend for Valuation Methods:

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

2. Other Information:

General PP&E – Significant Amount of Assets

Intangible assets totaling $2,265,813 thousand were reclassified as land. These costs increased $202,845 thousand in FY2004. These assets are comprised of historical costs associated with the acquisition of land in conjunction with power projects. Costs were originally classified as intangible assets in order to comply with Federal Energy Regulatory Commission guidelines on cost recovery. However, the decision was made that these costs were improperly classified in accordance with SFFAS No. 6, "Accounting for Property, Plant and Equipment," as they were part of the initial acquisitions cost of the land and should have been classified as such. We have also made a reversing entry for current year amortization in our statements to properly reflect the effect of the transfer into land (category 00) where accumulated depreciation is inappropriate. Supporting documentation for $17,353,836 thousand of the $29,000,000 thousand recorded in the Property, Plant and Equipment line is being supported by alternate methods as agreed upon by the Inspector General, Department of Defense and USACE in a 9 June 2004 Memorandum of Agreement. Significant increases in land purchases in Jacksonville, Omaha, Fort Worth and Tulsa Districts include land for Florida Everglades Restoration work in the amount of $33,344 thousand; dam and reservoir spillway embankment work in the amount of $15,566 thousand; reservoir work in Texas in the amount of $48,157 thousand; reservoir work in Oklahoma $20,668 thousand, respectively. The remaining amount is comprised of numerous smaller purchases of land tracts located throughout the United States.

Due to the change in policy (increasing Buildings and Structures threshold), the Corps expensed about 17,760 buildings and structures valued at about $63,261 thousand during FY 2003. The service life for our multiple purpose project assets is derived from guidance provided by the Federal Energy Regulatory Commission based on industry standards. The Power Marketing Administration related assets make up

$7,560,155 thousand of the book value of the Corps Property, Plant and Equipment.

The Corps of Engineers currently operates and maintains 75 hydroelectric power plants, generating about 24 percent of America's hydroelectric power. All power generated by these 75 hydroelectric power plants is transmitted to Power Marketing Authorities (PMA) for distribution to customers across the region. Each fiscal year the Corps prepares a "Statement of Expenses" broken down by plant, District and Region and provides this information to the PMAs to assist in their Power Repayment Study. The PMAs then collect power receipts (revenues) from customers and return the receipts to the Treasury. In FY03, the PMAs returned $1,600 thousand in revenue to the Treasury from power sales.

Corps policy requires all capital improvements to real property, occupied but not owned by the Corps, with a useful life of two or more years and cost of $25 thousand to be capitalized as leasehold improvements.

For regulatory discussion on General PP&E, Net, see DoD FMR, Volume 6B, Chapter 10, paragraph 1012.

Fluctuations

Line1A – USACE recorded a current year increase of $202,845 thousand in intangible assets reclassified to land associated with the power projects. Other significant increases occurred from land purchases in Jacksonville, Omaha, Fort Worth and Tulsa Districts include land for Florida Everglades Restoration work in the amount of $33,344 thousand; dam and reservoir spillway embankment work in the amount of $15,566 thousand; reservoir work in Texas in the amount of $48,157 thousand; reservoir work in Oklahoma $20,668 thousand, respectively.

Line 1B – The majority of the decrease in net book value of Buildings, Structures and Facilities is due to the depreciation adjustments made by the New Orleans, Memphis and Vicksburg districts to fully depreciate all revetments already placed in service which are reported in the Flood Control, Mississippi River and Tributaries Appropriation.

Line 1C – The decrease in net book value of Leasehold Improvements is due an increase in accumulated amortization of $2,300 thousand for LAN and Electronic Document Management System (EDMS) hardware and software at Humphreys Engineering Center Support Activity (HECSA).

Line 1D – The increase in net book value of Software is due to the acquisition of O&M Business Information Link (OMBIL) and Corps of Engineers Water Management System (CWMS) for $10,379 thousand and the amortization of $6,747 thousand that was charged for FY2004 on assets in service (Promis, RMS, REMIS, CEFMS, CWMS and OMBIL) at Headquarters USACE.

Line 1H - The decrease in construction in progress is due to a change in accounting policy in FY 2004 requiring the write-off of non-federal cost share projects as costs are incurred. In the past costs for non-federal cost share projects were capitalized and then transferred to the public at completion by recording a loss.

Line 1I - Other: Other assets consist of assets awaiting disposal. The increase is due to a retirement of a dam at Louisville district.

Note Reference

See Note Disclosure 1.O. - Significant Accounting Policies for additional discussion on financial reporting requirements and DoD policies governing General Property, Plant and Equipment (PP&E).

See Note 20 for further discussion on adjustment for construction-in-progress.

Note 10.A. Assets Under Capital Lease

Not applicable

Note 11. Liabilities Not Covered by Budgetary Resources

As of September 30 (Amounts in thousands)	**2004**	**2003**
1. Intragovernmental Liabilities		
A. Accounts Payable	$0	$0
B. Debt	15,000	16,991
C. Environmental Liabilities	0	0
D. Other	262,233	188,791
E. **Total Intragovernmental Liabilities**	$277,233	$205,782
2. Non-Federal Liabilities		
A. Accounts Payable	$0	$0
B. Military Retirement Benefits and Other Employment-Related Actuarial Liabilities	0	0
C. Environmental Liabilities	0	0
D. Loan Guarantee Liability	0	0
E. Debt Held by Public	0	0
F. Other Liabilities	50,353	62,923
G. **Total Non-Federal Liabilities**	$50,353	$62,923
3. Total Liabilities Not Covered by Budgetary Resources	$327,586	$268,705
4. Total Liabilities Covered by Budgetary Resources	$3,066,286	$3,211,417
5. Total Liabilities	$3,393,872	$3,480,122

Column Format

The DDRS-AFS Note 11 column format changed for FY 2004 to comply with Note 11 column format in OMB Circular 01-09.

Definitions

Liabilities Not Covered by Budgetary Resources

Liabilities that are not considered covered by realized budgetary resources as of the Balance Sheet date. Budgetary resources encompass the following:

- New budget authority.
- Spending authority from offsetting collections (credited to an appropriation or fund account).
- Recoveries of unexpired budget authority through downward adjustments of prior-year obligations.
- Unobligated balances of budgetary resources at the beginning of the year or net transfers of prior-year balances during the year.
- Borrowing authority or permanent indefinite appropriations, which have been enacted and signed into law as of the Balance Sheet date, provided that the resources may be apportioned by the OMB without further action by the Congress or without a contingency first having to be met.

Other Corps Information

Intra-governmental Liabilities – Other includes Workmen's Compensation liabilities in the amount of $43,746 thousand , $65,183 thousand for the offsetting custodial liability to accounts receivable, and judgment fund liabilities in the amount of $153,308 thousand (the amount under the Contract Dispute Act totals $153,305 thousand and the amount under the Notification of Federal Antidiscrimination and Retaliatory Act (NO FEAR) totals $3 thousand).

The Actuarial Liability for Federal Employee's Compensation Act (FECA) is not included. The Department of Labor is unable to furnish a figure for FECA liability specific to the Corps of Engineers.

Non-Federal Liabilities – Other includes $50,353 thousand for contracts with continuation clause.

Total Liabilities Covered by Budgetary Resources: Intragovernmental - Accounts Payable, $103,499 thousand; Debt, $367 thousand; and, Other (FECA, Unearned Revenue-Advances, Deposit Fund, Clearing Accounts and Long Term Receivables), $1,796,393 thousand. Non-Federal – Accounts Payable, $595,831 thousand; and, Other (Contract Holdbacks, FECA, Unearned Revenue-Advances, Deposit Fund, Clearing Account and Contingent Liabilities resulting from casualty losses), $570,196 thousand.

Fluctuations

Intra-governmental Liabilities - Debt: The liability for debt decreases as payments are made to reduce the principal amount.

Intra-governmental Liabilities - Other: This amount increased because Uncollected Custodial Liability totaling $65,183 thousand is reported with Liabilities Not Covered by Budgetary Resources in the 4th Quarter 2004; it was reported with Liabilities Covered by Budgetary Resources in the 4th Quarter 2003. Prior to the 4th Quarter 2004, USACE prepared a journal voucher to move Uncollected Custodial Liability from SGL 2980 to SGL 2990-Other Liabilities per DoDIG direction. There is no longer a restriction on the use of SGL 2980 by the USACE.

Non-Federal Liabilities – Other Liabilities: The decrease in this amount represents the difference between the increase in the unfunded portion of contracts with continuation clauses and the amount of funds received for actual contractual work. The net difference for fiscal year 2004 totals $12,570 thousand.

Note Reference

For additional line item discussion, see:
Note 8, Direct Loans and/or Loan Guarantee Programs
Note 12, Accounts Payable
Note 13, Debt
Note 14, Environmental Restoration Liabilities and Environmental Disposal Liabilities
Note 15, Other Liabilities
Note 16, Commitments and Contingencies
Note 17, Military Retirement Benefits and Other Employment-Related Actuarial Liabilities

Note 12. Accounts Payable

As of September 30 (Amounts in thousands)	2004 Accounts Payable	2004 Interest, Penalties, and Administrative Fees	2004 Total	2003 Total
1. Intragovernmental Payables:	$103,498	N/A	$103,498	$92,764
2. Non-Federal Payables (to the Public):	$570,255	$0	$570,255	$568,108
3. Total	$673,753	$0	$673,753	$660,872

4. Other Information:

Intragovernmental Accounts Payable consists of amounts owed to other federal agencies for goods or services ordered and received but not yet paid. Interest, penalties and administrative fees are not applicable to intragovernmental payables.

The Corps has no known delinquent accounts payable, therefore no amount is reported for interest, penalties, and administrative fees. For the period ending September 30, 2004, the Corps paid $255 thousand in interest, from Civil Works appropriations, on payments subject to the Prompt Payment Act.

The Corps was able to compare its accounts payable balance with the accounts receivable balances of its intra-departmental (DoD) trading partners. No material reconciling differences were identified.

Fluctuations

Intra-governmental Payables: The difference represents an increase in accrued payables.

Note Reference

See Note Disclosure 1.G. - Significant Accounting Policies for additional discussion on financial reporting requirements and DoD policies governing accounting for Intragovernmental Activities.

Note 13. Debt

As of September 30 (Amounts in thousands)	2004 Beginning Balance	2004 Net Borrowings	2004 Ending Balance	2003 Ending Balance
1. Public Debt:				
A. Held by Government Accounts	N/A	N/A	N/A	N/A
B. Held by the Public	N/A	N/A	N/A	N/A
C. Total Public Debt	N/A	N/A	N/A	N/A
2. Agency Debt:				
A. Debt to the Treasury	$17,386	($2,019)	$15,367	$17,386
B. Debt to the Federal Financing Bank	0	0	0	0
C. Debt to Other Federal Agencies	0	0	0	0
D. Total Agency Debt	$17,386	($2,019)	$15,367	$17,386
3. Total Debt:	$17,386	($2,019)	$15,367	$17,386
4. Classification of Debt:				
A. Intragovernmental Debt			$15,367	$17,386
B. Non-Federal Debt			N/A	N/A
C. Total Debt			$15,367	$17,386

5. Other Information:

During fiscal years 1997, 1998 and 1999, the Corps of Engineers executed three promissory notes totaling $75,000 thousand with the Department of the Treasury. Funds provided were used for capital improvements to the Washington Aqueduct. Arlington County, the City of Falls Church, Virginia and the District of Columbia provide funding to repay the debt. Cumulative actual drawdown of the funds has been made from the Treasury in the amount of $74,896 thousand. There were no drawdowns of funds from the Treasury in FY04.

Accrued Interest Payable as of September 30, 2004	+ Principal Repayments FY04	= Net Borrowings FY04
$1,991 thousand	$28 thousand	$2,019 thousand

Total cumulative principal repayments as of September 30, 2004 are $59,895 thousand.
The difference from FY 2003 represents principal repayments towards liquidating the debt.

Note Reference

See Note Disclosure 1. G. - Significant Accounting Policies for additional discussion on financial reporting requirements and DoD policies governing Accounting for Intragovernmental Activities, Public Debt.

See Note 21 for further discussion on the Washington Aqueduct project.

Note 14. Environmental Liabilities and Disposal Liabilities

Not applicable

Note 15.A. Other Liabilities

As of September 30 (Amounts in thousands)	2004 Current Liability	 Noncurrent Liability	 Total	2003 Total
1. Intragovernmental:				
A. Advances from Others	$10,853	$0	$10,853	$10,959
B. Deferred Credits	0	0	0	0
C. Deposit Funds and Suspense Account Liabilities	472	0	472	510
D. Resources Payable to Treasury	0	0	0	0
E. Disbursing Officer Cash	567	0	567	768
F. Nonenvironmental Disposal Liabilities:				
(1) National Defense PP&E (Nonnuclear)	0	0	0	0
(2) Excess/Obsolete Structures	0	0	0	0
(3) Conventional Munitions Disposal	0	0	0	0
(4) Other	0	0	0	0
G. Accounts Payable-- Cancelled Appropriations	0	0	0	0
H . Judgment Fund Liabilities	153,309	0	153,309	145,907
I. FECA Reimbursement to the Department of Labor	17,379	26,366	43,745	42,884
J. Capital Lease Liability	0	0	0	0
K. Other Liabilities	123,788	1,725,893	1,849,681	1,895,452
L. Total Intragovernmental Other Liabilities	$306,368	$1,752,259	$2,058,627	$2,096,480
2. Non-Federal:				
A. Accrued Funded Payroll and Benefits	$358,538	0	358,538	$443,414
B. Advances from Others	139,121	0	139,121	110,265
C. Deferred Credits	0	0	0	0
D. Loan Guarantee Liability	0	0	0	0
E. Liability for Subsidy Related to Undisbursed Loans	0	0	0	0
F. Deposit Funds and Suspense Accounts	9,272	0	9,272	7,060
G. Temporary Early Retirement Authority	0	0	0	0
H. Nonenvironmental Disposal Liabilities:				
(1) National Defense PP&E (Nonnuclear)	0	0	0	0
(2) Excess/Obsolete Structures	0	0	0	0
(3) Conventional Munitions Disposal	0	0	0	0
(4) Other	0	0	0	0
I. Accounts Payable--Cancelled Appropriations	0	0	0	0
J. Accrued Unfunded Annual Leave	0	0	0	0
K. Accrued Entitlement Benefits for Military Retirees and Survivors	0	0	0	0
L. Capital Lease Liability	0	0	0	0
M. Other Liabilities	139,194	0	139,194	144,645
N. Total Non-Federal Other Liabilities	$ 646,125	$ 0	$646,125	$705,384
3. Total Other Liabilities:	$952,493	$1,752,259	$2,704,752	$2,801,864

4. Other Information Pertaining to Other Liabilities:

Line 1.H. The Corps of Engineers Civil Works Directorate has recognized 31 unfunded liabilities arising from Judgment Fund Contract Disputes Act settlement in accordance with the interpretation of Federal Financial Accounting Standards Number 2, Accounting for Treasury Judgment Fund Transactions. The amount reported by the Treasury Department is $154,675 thousand. The difference of $1,370 thousand is due to two claims included in Treasury's total that belong to the Army. The Corps is also reporting a funded liability for $3 thousand under the Notification of Federal Antidiscrimination and Retaliatory Act.

Line 1.I. Federal Employees' Workman's Compensation liability reflects cost of claims incurred for income lost and medical costs for federal civilian employees injured on the job, employees who have incurred a work-related occupational disease, and beneficiaries of employees whose death is attributable to a job-related injury or occupational disease. The claim costs are paid by the Department of Labor in accordance with the Federal Employees' Compensation Act (FECA). USACE will receive a chargeback billing and will process a payment to reimburse the Department of Labor. Until the billing is received and processed, the liability is recorded. Fiscal year 2004 costs of $26,366 thousand are reflected as a non-current liability.

Other Liabilities

Intragovernmental

Line 1.K. Intra-governmental other liabilities (current) includes $11,686 thousand for employer contributions and payroll taxes and $112,102 thousand to offset interest and accounts receivables which, when collected, will be returned to Treasury. Intra-governmental other liabilities (noncurrent) represent future revenue of $1,724,493 thousand from long term water storage and $1,400 thousand from hydraulic mining contracts.

Non-Federal

Line 2.M. Non-federal other liabilities include $39,976 thousand to fund contingent liabilities arising from casualty losses. The amount also includes $48,865 thousand in contract holdbacks on construction-in-progress payments and $50,353 thousand for unfunded liabilities for contracts with continuation clauses. The continuation clause allows contractors to continue work without funds being obligated.

Intragovernmental Reconciliations for Fiduciary Transactions

With respect to the major fiduciary balances with the Office of Personnel Management (OPM) and the Department of Labor (DOL), the Corps was able to reconcile with the OPM and the DOL.

Fluctuations

Line 1.E. The decrease in the liability for Disbursing Officer Cash is attributed to a decrease in receivables related to travel advances.

Line 2.A. The decrease in Accrued Funded Payroll and Benefits is due to two factors. In FY 2003, the accrual included more than $45,212 thousand for the amount of employer contributions and payroll taxes payable. This amount is reported on Line 1.K. Other Liabilities of this note for FY 2004. In FY 2003, the accrual included the amount of the last employee payroll of approximately $23,000 thousand disbursed prior to year-end. The proper accounting entries were not made to reduce the accrual prior to year-end. In FY 2004, the accrual was reduced to reflect the payment of the last employee payroll at year end.

Line 2.B. Advances from Others increased due to an increase in customer orders from the public. A large percent of the increase in customer orders occurred in the New York and Honolulu districts. The New York district received an advance for more than $25,000 thousand for the assessment of security of New York City's public water supply and the Honolulu district received more than $17,000 thousand in advances for variety of local projects.

Line 2.F. The change in Deposit Funds and Suspense Accounts is due to an increase in bid/performance deposits, tax deposits, wire transfers and normal lease collections that were not applied at month end.

Note Reference

See Note Disclosure 1.S.-Significant Accounting Policies for additional discussion on financial reporting requirements and DoD policies governing Contingencies and Other Liabilities.

Note 15.B. Capital Lease Liability

Not applicable

Note 16. Commitments and Contingencies

Disclosures Related to Commitments and Contingencies:

Proprietary contingencies are commonly referred to as contingent liabilities. The Corps of Engineers has 467 cases pending litigation, 461 claims pending in contract claims and appeals, and 273 tort claims in which the relief requested is $3,954,895 thousand or more. The Corps' Legal Counsel is of the opinion that it is "reasonably possible" that the outcome of the litigation will result in a loss.

The Corps is responsible for the Formerly Utilized Remedial Action Program (FUSRAP) which was established to respond to radiological contamination from early U.S. atomic energy and weapons program. This program is funded through Civil Works appropriations. The Corps recognizes future contingent liabilities related to this program but the liability amounts are currently unknown.

Since these cases fail to satisfy the criteria to record a contingent liability in accordance with the Federal Financial Accounting Standard Number 5, Accounting for Liabilities of the Federal Government, no amount is included in our financial statements.

Note Reference

See Note Disclosure 1.S. - Significant Accounting Policies for additional discussion on financial reporting requirements and DoD policies governing Contingencies and Other Liabilities.

Note 17. Military Retirement Benefits and Other Employment Related Actuarial Liabilities

Not applicable

Note 18. Unexpended Appropriations

As of September 30 (Amounts in thousands)	**2004**	**2003**
1. Unexpended Appropriations:		
A. Unobligated, Available	$188,165	$381,759
B. Unobligated, Unavailable	66	8
C. Unexpended Obligations	208,131	255,079
D. Total Unexpended Appropriations	$396,362	$636,846

2. Other Information Pertaining to Unexpended Appropriations:

Definitions

Unexpended appropriations are the amount of budget authority remaining for disbursement against current or future obligations.

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

Unexpended obligations represent funds that have been committed for goods that have not been received or services that have not been performed.

Unobligated, Unavailable represents expired appropriations.

Fluctuations

Unexpended Appropriations - Unobligated, Available: This variance is partially due to a change in reporting appropriations-transfers-in. These transfers-in from the Bonneville Power Administration to the General Funds, and from the Bonneville Power Administration, Federal Aid Highways and National Park Service (Land Acquisition and State Assistance) to the Transfer Funds were treated as Unexpended Appropriations-Transfers-In for the 4th Quarter 2003; they are treated as Nonexpenditure Financing Sources-Transfers-In for the 4th Quarter 2004 and not reported on Note 18. Unexpended Appropriations-Transfers-In reported in the 4th Quarter 2003 were $137,875 thousand for the General Funds and $58,236 thousand for the Transfer Funds. Unexpended Appropriations-Transfers-In reported in the 4th Quarter 2004 are $0 for the General Funds and $18,495 thousand for the Transfer Funds. This is a total reduction of $177,616 thousand.

The remaining variance is due to a decrease in appropriations received in the General Funds.

Unexpended Appropriations - Unobligated, Unavailable: This variance represents an increase in expired appropriations.

Unexpended Appropriations - Unexpended Obligations: This decrease is the result of the change in reporting appropriations-transfers-in and the decrease in appropriations received in the General Funds. Unexpended Obligations decreased by $39,231 thousand for the General Funds and $7,481 thousand for the Transfer Funds.

Note Reference

Note 1.X, Significant Accounting Policies
Note 3.A, Fund Balance with Treasury

Note 19.A General Disclosures Related to the Statement of Net Cost

Disclosures Related to the Statement of Net Cost

Statement of Net Cost

The Consolidated Statement of Net Cost (SoNC) in the federal government is unique because its principles are driven on understanding the net cost of programs and/or organizations that the federal government supports through appropriations or other means. This statement provides gross and net cost information that can be related to the amount of output or outcome for a given program and/or organization administered by a responsible reporting entity.

The amounts presented in the Statement of Net Cost are based on obligations, disbursements and accruals. USACE records transactions on an accrual basis as required by generally accepted accounting principles.

Fluctuations and Abnormalities

Intragovernmental Gross Cost - Intragovernmental Gross Cost changed due to an increase of $19,677 thousand for employee benefit expense for health and life insurance, retirement benefits, workers compensation, and voluntary separation incentive program. Imputed cost for the employee benefits increased $14,482 thousand. Judgment Fund imputed cost increased $836 thousand. The remaining increase is due to continuing improvements in our process of identifying military trading partners for revolving fund labor and facility account transactions. The Corps developed system queries to identify trading partners for costs that are reimbursed by military and other civil appropriations. The increase for Army General Fund was $74,488 thousand. Cost had previously been coded as intra-entity transactions in the elimination process. USACE had significant activity with General Services Administration and Department of Interior with increases in cost of $86,139 thousand and $10,504 thousand, respectively.

Intragovernmental Earned Revenue - The increase is attributed to improvements to our process of identifying trading partner elimination data for other Corps revenue in the revolving fund. The Corps developed system queries to identify trading partners for labor and other transactions reimbursed from military and other civil appropriations. Revenue had previously been included as intra-entity eliminations. There was an increase in activity with Department of Interior for $17,207 thousand, Army General Fund for $91,941 thousand, and Department of Homeland Security of $107,197 thousand. USACE provides support for disaster relief to the Federal Emergency Management Agency, now part of the Department of Homeland Security.

Gross Cost with the Public - The cause of the change in Gross Cost with the Public is due to multiple factors. A decrease in current year expense of $3,651,142 thousand was recorded to reflect the reversal of the amount reported as a prior period adjustment in FY 2003 associated with non-federal cost share projects. USACE has spent much of FY 2004 aggressively working to remove these cost share amounts at transaction level. Current year transactions were recorded in CEFMS for $1,355,950 thousand. The work was on-going on 30 Sep 2004 and USACE has agreed to remove all cost share amounts from the Balance Sheet by the 1st quarter of FY 2005. An adjustment was entered to reflect the remaining amount of $769,763 thousand, not yet expensed. There was an increase of $1,734,889 thousand in depreciation expense primarily in the Mississippi River and Tributaries appropriation. Districts in the Mississippi Valley Division responsible for bank stabilization projects transferred construction in progress to expense for those projects to fully depreciate all revetments that were already in service. The combination of the above events resulted in an overall decrease in cost with the public.

Earned Revenue with the Public – There was an increase in Earned Revenue with the Public because Foreign Military Sales transactions are now recorded as public in accordance with DoD FMR Volume Chapter 3, paragraph 030308. The amount for FY 2004 is $6,777 thousand. Multi-purpose civil works projects on Portland, Omaha, Mobile, Fort Worth and Little Rock Districts recorded an increase in interest during construction of $38,563 thousand. If an asset takes longer than one year to build, then interest during construction is computed and posted as construction in progress cost. The offsetting entry is recorded as other gains. Jacksonville District recorded a substantial increase of $17,603 thousand in earned revenue for environmental restoration work.

Note 19.B. Gross Cost and Earned Revenue by Budget Functional Classification

Not applicable

Note 19.C. Gross Cost to Generate Intra-governmental Revenue and Earned Revenue (Transactions with Other Federal—Non-DoD—Entities) by Budget Functional Classification

Not applicable

Note 19.D. Imputed Expenses

As of September 30 (Amounts in thousands)	2004	2003
1. Civilian (e.g.,CSRS/FERS) Retirement	$102,108	$106,317
2. Civilian Health	125,990	108,142
3. Civilian Life Insurance	392	385
4. Military Retirement Pension	0	0
5. Military Retirement Health	0	0
6. Judgment Fund	11,058	10,222
7. Total Imputed Expenses	$239,548	$225,066

8. Other Information

Line 2. An overall increase in health benefit premium prices lead to an increase in the USACE portion of benefit costs.

Line 6. There were new dispute cases submitted to Treasury for payment from the Judgment Fund, which resulted in an increase in Judgment Fund expense.

Note 19.E. Benefit Program Expenses

Not applicable

Note 19. F. Exchange Revenue

Disclosures Related to the Exchange Revenue:

Exchange revenue arises when a government entity provides goods and services to the public or to another government entity for a price, "earned revenue'. Exchange revenue includes most user charges other than taxes, i.e., regulatory user charges.

Goods and services provided through reimbursable programs to the public or another U.S. government entity (Intra-Corps, Intra-DoD, or other Federal Government entity) are provided at cost. Such reimbursable sales are reported as earned revenues. Costs are equal to the amount reported as earned.

For regulatory discussion on Exchange Revenue, see DoD FMR, Volume 6B, Chapter 10, paragraph 102120.

Note 19.G. Amounts for Foreign Military Sales (FMS) Program Procurements from Contractors

Not applicable

Note 19.H. Stewardship Assets

Not applicable

Note 19.I. Intra-governmental Revenue and Expense

Disclosures Related to Intra-governmental Revenue and Expense:

The Corps of Engineers Financial Management System (CEFMS) captures trading partner data at the transaction level in a manner that facilitates trading partner reconciliation and elimination entries. There were no material reconciling differences.

Note 19.J. Suborganization Program Costs

Not applicable

Note 20. Disclosures Related to the Statement of Changes in Net Position

As of September 30 (Amounts in thousands)	Cumulative Results of Operations 2004	Unexpended Appropriations 2004	Cumulative Results of Operations 2003	Unexpended Appropriations 2003
1. Prior Period Adjustments Increases (Decreases) to Net Position Beginning Balance:				
A. Changes in Accounting Standards	$0	$0	$0	$0
B. Errors and Omissions in Prior Year Accounting Reports	0	0	(2,669,485)	0
C. Other Prior Period Adjustments	0	0	0	0
D. Total Prior Period Adjustments	$0	$0	($2,669,485)	$0
2. Imputed Financing:				
A. Civilian CSRS/FERS Retirement	$102,108	$0	$106,317	$0
B. Civilian Health	125,990	0	108,142	0
C. Civilian Life Insurance	392	0	385	0
D. Military Retirement Pension	0	0	0	0
E. Military Retirement Health	0	0	0	0
F. Judgment Fund	11,058	0	10,222	0
G. Total Imputed Financing	$239,548	$0	$225,066	$0

3. Other Information:

Other Corps Disclosures

Taxes and Other Nonexchange Revenue include $960,544 thousand in tax collections and $60,300 thousand in interest income deposited into the trust fund accounts. Excise taxes totaling $90,845 thousand were deposited into the Inland Waterways Trust Fund. Taxes totaling $869,699 thousand were collected and deposited into The Harbor Maintenance Trust Fund. These taxes were derived from:

Tax on Foreign Trade	$109,341 thousand
Tax on Imports	694,884 thousand
Tax on Passengers	6,708 thousand
Tax on Domestics	56,588 thousand
Tax on Exports	2,178 thousand

Transfers-in include $10 million transferred into the South Dakota Terrestrial Wildlife Restoration Trust Fund; $117,262 thousand transferred into the Inland Waterways Trust Fund from Treasury and recorded by the Corps; $630,944 thousand in budget authority transferred into the Harbor Maintenance Trust Fund from Treasury; and $59,023 thousand in budget authority transferred into the Coastal Wetlands Restoration Trust Fund from the Aquatic Resource Trust Fund. Additional monies were transferred into the Corps' General Fund. The breakdown is as follows: $51 thousand was transferred from the US Geological Survey, $30 thousand was transferred from the US Fish and Wildlife Service, $7 thousand was transferred from the National Park Service, $35 thousand was transferred from Bonneville Power Administration and $2,095 thousand was transferred from the Western Area Power Administration.

Transfers-out to other governmental agencies include $14,273 thousand to the Saint Lawrence Seaway Development Corporation from the Harbor Maintenance Trust Fund. Additional transfers from the General Fund were transferred as follows: $165 thousand was transferred to the National Park Service, $835 thousand was transferred to the US Forestry Service, $744 thousand was transferred to the Tennessee Valley Authority,

$211 thousand was transferred to the Non-Corps, US Navy Public Works, $52 thousand was transferred to the Non-Corps, US Army Public Works, $168 thousand was transferred to the US Fish and Wildlife, $39 thousand was transferred to the USDI Bureau of Indian Affairs and $6 thousand was transferred to the Department of Interior.

Fluctuations

Footnotes:

Line 2B. Imputed Financing – Civilian Health: Overall pay rate increased due to the annual cost of living raise. Civilian health benefits increased because overall pay rates increased. The health benefits are a percentage of the payroll.

Line 2F. Imputed Financing – Judgment Fund: The amount of Judgment Fund claims paid by Treasury increased by $836 thousand.

Statement of Changes in Net Position

Cumulative Results of Operations:

Line 1. Results of Operations – Beginning Balances: Cost share and other construction in progress projects, totaling $3,130,400 thousand, were transferred to the public and recorded as a loss in the fourth quarter of FY 2003. Also, a prior period adjustment (restated) of $2,669,485 thousand, was done in the fourth quarter of FY 2003 for non-federal cost share projects. The loss and prior period adjustments closed into results of operations and rolled forward to FY 2004.

Line 2. Prior Period Adjustments: An adjustment of $2,669,485 thousand was done in the fourth quarter of FY 2003, to remove construction in progress, for non-federal cost share projects. There is no prior period adjustment in FY 2004.

Line 4E. Budgetary Financing Sources – Nonexchange revenue: There are several factors that have contributed to the overall increase in nonexchange revenue. First, the $116,630 thousand increase in the Trust Funds account is due to fluctuation in taxes and interest. The Corps is the lead agency for reporting Inland Waterways and Harbor Maintenance Trust Funds. Second, the $413,651 increase in the Contributed Fund account is due to new reporting procedures in recording Contributed Fund receipts. CEFMS was recording the transactions as appropriations received and updated SGL 3100 series. According to Treasury proforma entry A186, the transactions should be recorded in the SGL 5900 other revenue.

Line 4G. Budgetary Financing Sources – Transfers-in/out: The overall $548,200 thousand net decrease to Transfers-in/out without reimbursement is due to changes in reporting procedures for Contributed, General and Transfer Funds. Contributed Funds now records appropriated receipts as other revenue based on Treasury proforma entry A186. The $183,368 thousand recorded in the Transfer Fund account and the $74,089 thousand recorded in the General Fund account, for the fourth quarter of 2004, are due to a change in reporting procedures for appropriations that no longer update GLAC 3100.

Line 4H. Budgetary Financing Sources – Other budgetary financing sources: The overall change in other budgetary financing sources is due to a change in reporting procedures for General, Revolving and Transfer Funds. General and Revolving Funds now record GLACs 7190 and 7290 with a Fin26 attribute to update the Statement of Financing instead of the Change in Net Position. However, General Funds has a $39,606 thousand decrease and Revolving Fund has a $8,963 thousand increase in the losses on disposition of assets account. The $7,137 thousand recorded in the Transfer Fund account, for the fourth quarter of 2004, is due to a change in reporting procedures for Transfer appropriations that no longer updates GLAC 3100.

Line 5A. Other Financing Sources – Donations and forfeitures of property: There was an overall decrease in donations and forfeitures of property for the third quarter of FY 2004. The negative balance, in Revolving

Fund, is due to property recorded with an incorrect work item class code, in the fourth quarter of FY 2003 at the Buffalo District, which was corrected during the second quarter FY 2004.

Line 5B. Other Financing Sources – Transfers-in/out without reimbursement: The most significant changes for Transfers-in/out without reimbursements were with Borrowing Authority, General, Transfer and Trust Funds. Borrowing Authority had a decrease in transfers-out for $61,014 thousand. General Funds had a net increase in transfers-in/out for $31,774 thousand; Transfer Funds had a net increase in transfers-in/out for $15,571 thousand and Trust Funds had a net increase in Transfers-in/out for $15,006 thousand.

Line 5D. Other Financing Sources – Other: The overall decrease in Other Changes in Net Position is due to a change in the accounting treatment for collections in the General Fund Proprietary Interest Receipt Account during the fourth quarter of FY 2003. Due to this change a contra revenue account was established. No contra revenue amount was reported for the fourth quarter of FY 2003 for this appropriation.

There was also a decrease in Borrowing Authority, by $6,661 thousand, which is due to a reduction in the amount of loan repayments made to Treasury for improvements to the Washington Aqueduct.

Unexpended Appropriations

Lines 1 & 2B. Beginning Balance and Prior period adjustments: This is due to the change in recording the amount of appropriated receipts from available receipt accounts to the expenditure accounts. In prior years, these amounts in Special and Contributed Funds have been recorded as appropriations received, which updated unexpended appropriations. According to Treasury proforma entry A184, these amounts are to be recorded as transfers-in. Transfers-in do not update unexpended appropriations. An adjustment was made to remove the unexpended balances in Special Funds ($78 thousand) and Contributed Funds ($342,591 thousand) and report as transfers-in.

Line 4B. Budgetary Financing Sources – Appropriations transferred-in/out: The overall decrease is due to a decrease in the amount of net appropriations transfers from the Transfer Funds by $39,841 thousand. Also, General Funds now records transfers-in from Bonneville Power Administration to GLAC 5755 Non-expenditure Financing Sources-transfers-in. General Funds, however, did have a decrease in net appropriations transferred-in from Bonneville Power Administration for $63,786 thousand.

Line 4C. Budgetary Financing Sources – Other adjustments (rescissions, etc): The overall decrease to other adjustments is due to several factors. First, there were rescissions in the USACE Pollution Control and Abatement (FUSRAP) account for $826 thousand, and $26,259 thousand in the General Fund account. Second, Contributed Funds, for FY03, recorded $342,591 thousand in receipts as appropriations received which updated SGL 3100. The credit should have been recorded in SGL 5740 according to Treasury Proforma entry A184. USACE previously recorded SF1151 transfers in our Transfer Funds as appropriations transferred account 3102. We learned that this was in error, based on the appropriation the funds were transferred from, and that we should be recording a transfer-in using SGL 5755. We used the adjustment account to remove beginning balances associated with prior year transfers in 3100 for $7,137 thousand.

Note Reference

See Note 10 for further discussion of the construction in progress adjustment.

For Regulatory Disclosure Related to The Statement of Changes in Net Position” see, Department of Defense Financial Management Regulation, Volume 6B, Chapter 10, paragraph 1022.

Note 21. Disclosures Related to the Statement of Budgetary Resources

As of September 30 (Amounts in thousands)	2004	2003
1. Net Amount of Budgetary Resources Obligated for Undelivered Orders at the End of the Period	$1,628,052	$1,407,415
2. Available Borrowing and Contract Authority at the End of the Period	30,445	31,840

3. Other Information:

Intra-entity Transactions

The Statement of Budgetary Resources (SBR) does not include intra-entity transactions because the statements are presented as combined and combining.

Apportionment Categories

The amount of direct and reimbursable obligations incurred against amounts apportioned under Category A in the SBR includes: $5,570,977 thousand for direct; $44,201 thousand for direct obligations exempt from apportionment; $5,456,291 thousand for reimbursable obligations; and $1,525 thousand for reimbursable obligations exempt from apportionment. The Corps has no apportionments under Category B.

Undelivered Orders

Undelivered Orders presented in the SBR includes Undelivered Orders-Unpaid for both direct and reimbursable funds.

Borrowing Authority

Borrowing authority is for capital improvements to the Washington Aqueduct. Funding to repay the debt is provided by Arlington County, Virginia; Falls Church, Virginia; and the District of Columbia. Borrowing authority expired at the end of fiscal year 2003. Borrowing authority converted to cash was not correctly recorded for fiscal years 2000 and 2001. Adjustment has been made this quarter to reflect this correction. The available borrowing authority reported on Line 2 does not reflect this adjustment.

Current Year to Prior Year Reconciliation

The difference on Line 2 of Current Year to Prior Year is due to a beginning balance change by Treasury. Treasury manages the investment portion of the Inland Waterways and Harbor Maintenance Trust Funds. The Corps is the lead agency for reporting these trust funds. We receive financial statements from Treasury to incorporate into our statements. During the 4th quarter, Treasury had changed the beginning balances for unobligated funds to unavailable for obligation.

Fluctuations

Line 1 Note 21 reflects a variance due to more undelivered orders in FY2004. The largest increase is $145,964 thousand in General Funds and $146,108 thousand in Trust Funds.

SBR Fluctuations

Budget Authority: Appropriations received and net transfers reflect a variance due to the way Treasury is recording the investment portion of Trust Funds (see Current Year to Prior Year Recon above). Net Transfers also reflect a variance due to the recording of receipt and transfer of funds (net zero) that were not recorded on this line before and an increase of $125,031 thousand in additional funding from Transfer Funds. Borrowing authority reflects a variance due to a correction of $135 thousand to the CEFMS database to reconcile cash to Treasury.

Unobligated Balance: Net transfers reflect a variance due to the recording of funds from Department of Interior as prior year funding vice current year funding based on guidance from Department of Interior.

Spending Authority from Offsetting Collections: Increase in receivable from Federal sources is due to an increase of $143,197 thousand in General Funds and a decrease of $4,319 thousand in Revolving Fund. Change in unfilled customer orders, advance received, reflects an increase of $34,951 thousand in General Funds and an increase of $11,017 thousand in Revolving Fund.

Temporarily not Available Pursuant to Public Law: Variance is due to the beginning balance change by Treasury for South Dakota Terrestrial Wildlife. Receipts unavailable for obligation upon collection was changed to receipts and appropriation temporarily precluded from obligation which populates this line vice appropriations received.

Permanently not Available: Reflects a variance due to a change in recording budget authority recissions. In FY2003, recissions of $30,095 thousand were recorded as a reduction to appropriations received vice Budgetary Resources permanently not available. A difference of $6,661 thousand is due to the repayment of debt in Borrowing Authority.

Unobligated Balance: Apportioned reflects a decrease of $147,719 thousand due to a change in recording unobligated balance of transfers in from Transfer Appropriations derived from a special or trust fund. These funds are considered exempt from apportionment. They were recorded as apportioned prior to 4th quarter FY2004. The large variance in exempt from apportionment is due the change in Treasury's recording of the investment portion of the Corps Trust Funds (see current year to prior year reconciliation above).

Unobligated Balance not Available: Increase of $57 thousand is due to expired funds in the General Investigation Appropriation.

Obligated Balance, Net – End of Period: Variance in accounts receivable is due to a decrease in accounts receivable of $8,249 thousand in Revolving Fund, an increase of $72,282 thousand in General Funds and an increase of $71 thousand in FUSRAP. The change in unfilled customer orders from Federal sources is due to an increase of $273,911 thousand in General Funds. Undelivered orders

reflects a variance due to an increase of $22,440 thousand in Contributed Funds, $145,964 thousand in General Funds, $76,441 thousand in Revolving Fund, $2,938 thousand in Transfer Funds and $146,108 thousand in Trust Funds.

Offsetting Receipts: The increase is primarily due to the reporting of Distributed Offsetting Receipts totaling $571,453 thousand in Contributed, General and Special Funds. Prior to 4th quarter FY2004, these funds were recorded as other revenue. There was also an increase in tax collections and interest revenue of $116,630 thousand in Trust funds from prior year.

Note 22. Disclosures Related to the Statement of Financing

Disclosures Related to the Statement of Financing:

Intra-entity transactions have not been eliminated because the Statement of Financing is presented as combined and combining.

Resources Used to Finance Activities:

Less: Offsetting receipts: The increase in offsetting receipts is due primarily to the reporting of Distributed Offsetting Receipts totaling $571,453 thousand in the Contributed, General and Special Funds on Line 4. Distributed Offsetting Receipts in these fund accounts were not reported on Line 4 in the past. There was also an increase in tax collections and interest revenue of $116,630 thousand in the Trust Funds from the prior year.

Donations and forfeitures of property: The decrease in Donations and forfeitures of property is due to a decrease in asset donations during the current fiscal year.

Transfers in/out without reimbursement: The decrease in the net amount of asset transfers-out is due to a decrease in transfers out to other government agencies. The largest change was for transfers-out to the Department of Interior which dropped from $56,649 thousand in FY 2003 to $378 thousand in FY 2004.

Other: The reporting of Distributed Offsetting Receipts and the contra revenue account changed this quarter. Distributed Offsetting Receipts for the General and Special Funds are now reported on Line 4 rather than Line 9. The amount of the contra revenue account for the distributed offsetting receipts has also been deleted from Line 9.

The decrease is also due to the decrease in the amount of collections from local governments used to repay the loan to Treasury for improvements to the Washington Aqueduct. Collections from local governments decreased from $8,653 thousand to $1,991 thousand from FY 2003 to FY2004.

Resources Used to Finance Items not Part of the Cost of Operations:

Undelivered Orders: The increase in undelivered orders occurred primarily in the Coastal Wetlands Trust Fund, Flood Control and Coastal Emergencies Appropriation and the Revolving Fund. The increase in the Flood Control and Coastal Emergency Appropriation is due to the hurricanes in the South Atlantic Region. The increase in the Revolving Funds is associated with the new Gulf Region Division in Iraq.

Unfilled Customer Orders: The change is due primarily to an increase in unfilled customer orders without advances in the Flood Control and Coastal Emergencies Appropriation in the South Atlantic Division due to the hurricanes in that area.

Resources that fund expenses recognized in prior periods: The amount reported on Line 13 includes the change in future funded expense for contracts with continuation clauses, unfunded judgment fund expense and employer contributions to employee benefits programs not requiring current year budgetary authority. The change in future funded expense was not reported on Line 13 in FY 2003.

Budgetary offsetting collections and receipts that do not affect net cost of operations: The increase is due to the reporting of $571,453 thousand in Distributed Offsetting Receipts on this line for the Contributed, Special and General Funds to offset the amount of offsetting receipts reported on Line 4. Distributed Offsetting Receipts for these funds were not reported on this line in the past. Tax collections and interest revenue in the Trust Funds have been reported on this line in the past. Trust fund revenue increased by $116,630 thousand this year.

Resources that finance the acquisition of assets: The change in resources that finance the acquisition of assets is due primarily to the change in reporting current year asset purchases during FY2004. Prior to FY2004 the amount reported on this line included asset transfers and other revaluations of assets. These amounts are now excluded from line 15 and reported on lines 16 or 26. At this time the true variance in current year asset purchases cannot be determined due to this change in reporting requirements.

Other resources or adjustments to net obligated resources that do not affect net cost of operations – Less: Trust or Special Fund Receipts Related to Exchange in the Entity's Budget: The increase is due to the reporting of the expenditure transfer from the General Fund to the South Dakota Terrestrial Wildlife Habitat Restoration Trust Fund as a transfer-out in FY2004. The FY2003 transfer to the trust fund was recorded as an expense and was not recorded on the statement of financing.

Other resources or adjustments to net obligated resources that do not affect net cost of operations – Less: Other: This is the net amount of asset transfers-out. Net asset transfers were included in Line 15 in prior periods.

Other: The change is mostly attributed to the decrease in future funded expense for contracts with a continuation clause.

Components of the Net Cost of Operations that will not Require or Generate Resources in the Current Period:

Depreciation and amortization: The increase in depreciation expense is due primarily to the depreciation adjustments made by the New Orleans, Memphis and Vicksburg districts to fully depreciate all revetments already placed in service reported in the Flood Control, Mississippi River and Tributaries Appropriation.

Revaluation of assets or liabilities: The change in the amount on Line 26 is due to two factors. In FY 2003 the amount reported on this line included adjustments for $981,667 thousand to write off current year costs that had been capitalized as construction in progress for non federal cost share projects, an adjustment for $255,555 thousand to record the loss for two failed fish mitigation studies and $240,460 thousand for asset transfers to the public. In FY 2004 the adjustment for $981,667 to record the write-off of capitalized current year costs for non-federal cost share projects was reversed. This reversal represents almost 85 percent of the variance. The non-federal cost share projects were written-off to operating expense rather than loss on disposition of assets in the Corps' accounting system this year.

The second factor is the change in reporting requirements for the amount of resources that finance current year purchases reported on Line 15. In prior periods the amount reported on Line 15 was the total change in assets including asset gains and losses and transfers-in and out. In accordance with DFAS policy, Line 15 now includes only asset purchases during the fiscal year. Therefore, we are now reporting asset gains and losses on Line 26.

Other: The change is due to an increase in other expenses not requiring budgetary resources related to the write-off of capitalized non-federal cost share projects.

Note 23. Disclosures Related to the Statement of Custodial Activity

Disclosures Related to the Statement of Custodial Activity:

This Statement is prepared at the Department of Defense level only.

Note 24.A. Other Disclosures

Not applicable

Note 24.B. Other Disclosures

Not applicable.

Department of Defense- Department of the Army, Civil Works Fund

CONSOLIDATING BALANCE SHEET

As of September 30, 2004 and 2003 ($ in Thousands)

ASSETS (Note 2)	**Special Funds**	**Trust Funds**	**Transfer Funds**
Intragovernmental:			
Fund Balance with Treasury (Note 3)			
Entity	$2,972	$72,121	$45,067
Non-Entity Seized Iraqi Cash	0	0	0
Non-Entity-Other	0	0	0
Investments (Note 4)	0	2,741,917	0
Accounts Receivable (Note 5)	0	362,451	35,650
Other Assets (Note 6)	0	0	0
Total Intragovernmental Assets	$2,972	$3,176,489	$80,717
Cash and Other Monetary Assets (Note 7)	$0	$0	$0
Accounts Receivable (Note 5)	2,222	0	0
Loans Receivable (Note 8)	0	0	0
Inventory and Related Property (Note 9)	0	0	195
General Property, Plant and Equipment (Note 10)	2,068	673,197	271,480
Investments (Note 4)	0	0	0
Other Assets (Note 6)	0	0	0
TOTAL ASSETS	$7,262	$3,849,686	$352,392
LIABILITIES (Note 11)			
Intragovernmental:			
Accounts Payable (Note 12)	$280	$10,207	$1,350
Debt (Note 13)	0	0	0
Environmental Liabilities (Note 14)	0	0	0
Other Liabilities (Note 15 & Note 16)	2,222	6,000	0
Total Intragovernmental Liabilities	$2,502	$16,207	$1,350
Accounts Payable (Note 12)	$480	$9,201	$13,902
Military Retirement Benefits and Other Employment-Related Actuarial Liabilities (Note 17)	0	0	0
Environmental Liabilities (Note 14)	0	0	0
Loan Guarantee Liability (Note 8)	0	0	0
Other Liabilities (Note 15 and Note 16)	3	677	2,952
Debt Held by Public	0	0	0
TOTAL LIABILITIES	$2,985	$26,085	$18,204
NET POSITION			
Unexpended Appropriations (Note 18)	$0	$0	$23,515
Cumulative Results of Operations	4,277	3,823,601	310,673
TOTAL NET POSITION	$4,277	$3,823,601	$334,188
TOTAL LIABILITIES AND NET POSITION	$7,262	$3,849,686	$352,392

Borrowing Authority	Revolving Funds	Contributed Funds	General Funds	FUSRAP
$27	$902,212	$408,009	$917,110	$30,924
0	0	0	0	0
0	0	0	8,245	0
0	0	0	0	0
(1)	2,168	0	121,122	0
0	0	0	2,140	0
$26	$904,380	$408,009	$1,048,617	$30,924
$0	$0	$0	$1,039	$0
0	424	66	1,903,723	0
0	0	0	0	0
0	50,420	0	11,200	0
7,634	847,826	16,003	26,630,309	0
0	0	0	0	0
0	0	0	0	0
$7,660	$1,803,050	$424,078	$29,594,888	$30,924
$0	$46,053	$720	$45,996	$159
15,367	0	0	0	0
0	0	0	0	0
0	15,769	2,636	2,034,140	0
$15,367	$61,822	$3,356	$2,080,136	$159
$0	$75,497	$19,836	$425,099	$26,240
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
1	464,635	4,097	173,608	152
0	0	0	0	0
$15,368	$601,954	$27,289	$2,678,843	$26,551
$0	$0	$0	$368,474	$4,373
(7,708)	1,201,096	396,789	26,547,571	0
($7,708)	$1,201,096	$396,789	$26,916,045	$4,373
$7,660	$1,803,050	$424,078	$29,594,888	$30,924

Department of Defense- Department of the Army, Civil Works Fund

CONSOLIDATING BALANCE SHEET

As of September 30, 2004 and 2003 ($ in Thousands)

ASSETS (Note 2)	Combined Total	Eliminations	2004 Consolidated	2003 Consolidated
Intragovernmental:				
Fund Balance with Treasury (Note 3)				
Entity	$2,378,442	$0	$2,378,442	$2,588,857
Non-Entity Seized Iraqi Cash	0	0	0	0
Non-Entity-Other	8,245	0	8,245	6,865
Investments (Note 4)	2,741,917	0	2,741,917	2,478,454
Accounts Receivable (Note 5)	521,390	1,267	520,123	423,774
Other Assets (Note 6)	2,140	2,140	0	0
Total Intragovernmental Assets	$5,652,134	$3,407	$5,648,727	$5,497,950
Cash and Other Monetary Assets (Note 7)	$1,039	$0	$1,039	$1,278
Accounts Receivable (Note 5)	1,906,435	0	1,906,435	1,935,567
Loans Receivable (Note 8)	0	0	0	0
Inventory and Related Property (Note 9)	61,815	0	61,815	62,605
General Property, Plant and Equipment (Note 10)	28,448,517	0	28,448,517	30,909,056
Investments (Note 4)	0	0	0	0
Other Assets (Note 6)	0	0	0	0
TOTAL ASSETS	$36,069,940	$3,407	$36,066,533	$38,406,456
LIABILITIES (Note 11)				
Intragovernmental:				
Accounts Payable (Note 12)	$104,765	$1,267	$103,498	$92,764
Debt (Note 13)	15,367	0	15,367	17,386
Environmental Liabilities (Note 14)	0	0	0	0
Other Liabilities (Note 15 & Note 16)	2,060,767	2,140	2,058,627	2,096,480
Total Intragovernmental Liabilities	$2,180,899	$3,407	$2,177,492	$2,206,630
Accounts Payable (Note 12)	$570,255	$0	$570,255	$568,108
Military Retirement Benefits and Other Employment-Related Actuarial Liabilities (Note 17)	0	0	0	0
Environmental Liabilities (Note 14)	0	0	0	0
Loan Guarantee Liability (Note 8)	0	0	0	0
Other Liabilities (Note 15 and Note 16)	646,125	0	646,125	705,384
Debt Held by Public	0	0	0	0
TOTAL LIABILITIES	$3,397,279	$3,407	$3,393,872	$3,480,122
NET POSITION				
Unexpended Appropriations (Note 18)	$396,362	$0	$396,362	$636,846
Cumulative Results of Operations	32,276,299	0	32,276,299	34,289,488
TOTAL NET POSITION	$32,672,661	$0	$32,672,661	$34,926,334
TOTAL LIABILITIES AND NET POSITION	$36,069,940	$3,407	$36,066,533	$38,406,456

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Department of Defense- Department of the Army, Civil Works Fund

CONSOLIDATING STATEMENT OF NET COST

As of September 30, 2004 and 2003 ($ in Thousands)

	Combined Total	Eliminations	2004 Consolidated	2003 Consolidated
Program Costs				
A. Borrowing Authority				
Intragovernmental Gross Costs	$258	$17	$241	$237
(Less: Intragovernmental Earned Revenue)	0	0	0	0
Intragovernmental Net Costs	$258	$17	$241	$237
Gross Costs With the Public	$2,110	$0	$2,110	$8,626
(Less: Earned Revenue From the Public)	(2,261)	0	(2,261)	(9,049)
Net Costs With the Public	($151)	$0	($151)	($423)
Total Net Cost	$107	$17	$90	($186)
B. Contributed Funds	0			
Intragovernmental Gross Costs	$39,030	$28,047	$10,983	$7,465
(Less: Intragovernmental Earned Revenue)	(50)	(50)	0	0
Intragovernmental Net Costs	$38,980	$27,997	$10,983	$7,465
Gross Costs With the Public	$336,036	$0	$336,036	$900,965
(Less: Earned Revenue From the Public)	(1)	0	(1)	(10)
Net Costs With the Public	$336,035	$0	$336,035	$900,955
Total Net Cost	$375,015	$27,997	$347,018	$908,420
C. FUSRAP				
Intragovernmental Gross Costs	$17,150	$14,640	$2,510	$2,524
(Less: Intragovernmental Earned Revenue)	0	0	0	0
Intragovernmental Net Costs	$17,150	$14,640	$2,510	$2,524
Gross Costs With the Public	$122,458	$0	$122,458	$137,757
(Less: Earned Revenue From the Public)	0	0	0	0
Net Costs With the Public	$122,458	$0	$122,458	$137,757
Total Net Cost	$139,608	$14,640	$124,968	$140,281
D. General Funds				
Intragovernmental Gross Costs	$1,341,876	$1,044,329	$297,547	$265,020
(Less: Intragovernmental Earned Revenue)	(638,482)	(29,089)	(609,393)	(479,499)
Intragovernmental Net Costs	$703,394	$1,015,240	($311,846)	($214,479)
Gross Costs With the Public	$6,063,017	$0	$6,063,017	$6,314,004
(Less: Earned Revenue From the Public)	(281,571)	0	(281,571)	(264,819)
Net Costs With the Public	$5,781,446	$0	$5,781,446	$6,049,185
Total Net Cost	$6,484,840	$1,015,240	$5,469,600	$5,834,706

	Combined Total	Eliminations	2004 Consolidated	2003 Consolidated
F. Special Funds				
Intragovernmental Gross Costs	$855	$541	$314	$136
(Less: Intragovernmental Earned Revenue)	0	0	0	0
Intragovernmental Net Costs	$855	$541	$314	$136
Gross Costs With the Public	$12,850	$0	$12,850	$11,212
(Less: Earned Revenue From the Public)	0	0	0	0
Net Costs With the Public	$12,850	$0	$12,850	$11,212
Total Net Cost	$13,705	$541	$13,164	$11,348
G. Transfer Funds				
Intragovernmental Gross Costs	$31,541	$25,570	$5,971	$2,999
(Less: Intragovernmental Earned Revenue)	0	0	0	0
Intragovernmental Net Costs	$31,541	$25,570	$5,971	$2,999
Gross Costs With the Public	$35,596	$0	$35,596	$70,313
(Less: Earned Revenue From the Public)	(5,610)	0	(5,610)	0
Net Costs With the Public	$29,986	$0	$29,986	$70,313
Total Net Cost	$61,527	$25,570	$35,957	$73,312
H. Trust Funds	0			
Intragovernmental Gross Costs	$31,605	$8,549	$23,056	$25,734
(Less: Intragovernmental Earned Revenue)	0	0	0	0
Intragovernmental Net Costs	$31,605	$8,549	$23,056	$25,734
Gross Costs With the Public	$694,248	$0	$694,248	$644,898
(Less: Earned Revenue From the Public)	0	0	0	0
Net Costs With the Public	$694,248	$0	$694,248	$644,898
Total Net Cost	$725,853	$8,549	$717,304	$670,632
I. Total Program Costs	0			
Intragovernmental Gross Costs	$2,144,474	$1,123,707	$1,020,767	$819,199
(Less: Intragovernmental Earned Revenue)	(2,358,513)	(1,123,708)	(1,234,805)	(1,011,769)
Intragovernmental Net Costs	($214,039)	($1)	($214,038)	($192,570)
Gross Costs With the Public	$8,658,737	$0	$8,658,737	$9,466,972
(Less: Earned Revenue From the Public)	(367,963)	0	(367,963)	(298,633)
Net Costs With the Public	$8,290,774	$0	$8,290,774	$9,168,339
Total Net Cost	$8,076,735	($1)	$8,076,736	$8,975,769
Cost Not Assigned to Programs	0	0	0	0
(Less:Earned Revenue Not Attributable to Programs)	0	0	0	0
Net Cost of Operations	$8,076,735	($1)	$8,076,736	$8,975,769

Department of Defense- Department of the Army, Civil Works Fund

CONSOLIDATING STATEMENT OF CHANGES IN NET POSITION

As of September 30, 2004 and 2003 ($ in Thousands)

CUMULATIVE RESULTS OF OPERATIONS	Special Funds	Trust Funds	Transfer Funds
Beginning Balances	$2,540	$3,578,769	$188,444
Prior period adjustments (+/-)			
Prior Period Adjustments - Restated (+/-)	0	0	0
Beginning Balance, Restated	2,540	3,578,769	188,444
Prior Period Adjustments - Not Restated (+/-)	0	0	0
Beginning Balances, as adjusted	$2,540	$3,578,769	$188,444
Budgetary Financing Sources:			
Appropriations received	0	0	0
Appropriations transferred-in/out (+/-)	0	0	0
Other adjustments (rescissions, etc) (+/-)	0	0	0
Appropriations used	0	0	20,148
Nonexchange revenue	0	1,020,844	0
Donations and forfeitures of cash and cash equivalents	0	0	0
Transfers-in/out without reimbursement (+/-)	15,820	51,768	183,368
Other budgetary financing sources (+/-)	0	0	7,137
Other Financing Sources:			
Donations and forfeitures of property	0	0	0
Transfers-in/out without reimbursement (+/-)	(378)	(101,927)	(26,897)
Imputed financing from costs absorbed by others	0	0	0
Other (+/-)	0	0	0
Total Financing Sources	$15,442	$970,685	$183,756
Net Cost of Operations (+/-)	13,705	725,853	61,527
Ending Balances	$4,277	$3,823,601	$310,673

UNEXPENDED APPROPRIATIONS	Special Funds	Trust Funds	Transfer Funds
Beginning Balances	$0	$0	$32,406
Prior period adjustments (+/-)			
Prior Period Adjustments - Restated (+/-)	0	0	0
Beginning Balance, Restated	0	0	32,406
Prior Period Adjustments - Not Restated (+/-)	0	0	0
Beginning Balances, as adjusted	$0	$0	$32,406
Budgetary Financing Sources:			
Appropriations received	0	0	0
Appropriations transferred-in/out (+/-)	0	0	18,394
Other adjustments (rescissions, etc) (+/-)	0	0	(7,137)
Appropriations used	0	0	(20,148)
Nonexchange revenue	0	0	0
Donations and forfeitures of cash and cash equivalents	0	0	0
Transfers-in/out without reimbursement (+/-)	0	0	0
Other budgetary financing sources (+/-)	0	0	0
Other Financing Sources:			
Donations and forfeitures of property	0	0	0
Transfers-in/out without reimbursement (+/-)	0	0	0
Imputed financing from costs absorbed by others	0	0	0
Other (+/-)	0	0	0
Total Financing Sources	$0	$0	($8,891)
Net Cost of Operations (+/-)	0	0	0
Ending Balances	$0	$0	$23,515

Borrowing Authority	Revolving Funds	Contributed Funds	General Funds	FUSRAP
($8,368)	$1,260,998	$367,889	$28,899,179	$37
0	0	0	0	0
(8,368)	1,260,998	367,889	28,899,179	37
0	0	0	0	0
($8,368)	$1,260,998	$367,889	$28,899,179	$37
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	3,919,304	139,571
0	0	413,651	0	0
0	0	0	0	0
0	0	0	64,089	0
0	(10,635)	0	(447)	0
0	(99)	0	534	0
(1,223)	(1,578)	(9,736)	140,107	0
0	228,490	0	11,058	0
1,991	0	0	(1,413)	0
$768	$216,178	$403,915	$4,133,232	$139,571
107	276,080	375,015	6,484,840	139,608
($7,707)	$1,201,096	$396,789	$26,547,571	$0
$0	$0	$0	$599,670	$4,770
0	0	0	0	0
0	0	0	599,670	4,770
0	0	0	0	0
$0	$0	$0	$599,670	$4,770
0	0	0	3,714,081	140,000
0	0	0	0	0
0	0	0	(25,973)	(826)
0	0	0	(3,919,304)	(139,571)
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
$0	$0	$0	($231,196)	($397)
0	0	0	0	0
$0	$0	$0	$368,474	$4,373

Department of Defense- Department of the Army, Civil Works Fund

CONSOLIDATING STATEMENT OF CHANGES IN NET POSITION

As of September 30, 2004 and 2003 ($ in Thousands)

CUMULATIVE RESULTS OF OPERATIONS	Combined Total	Eliminations
Beginning Balances	$34,289,488	$0
Prior period adjustments (+/-)		
Prior Period Adjustments - Restated (+/-)	0	0
Beginning Balance, Restated	34,289,488	0
Prior Period Adjustments - Not Restated (+/-)	0	0
Beginning Balances, as adjusted	$34,289,488	$0
Budgetary Financing Sources:		
Appropriations received	0	0
Appropriations transferred-in/out (+/-)	0	0
Other adjustments (rescissions, etc) (+/-)	0	0
Appropriations used	4,079,023	0
Nonexchange revenue	1,434,495	0
Donations and forfeitures of cash and cash equivalents	0	0
Transfers-in/out without reimbursement (+/-)	315,045	0
Other budgetary financing sources (+/-)	(3,945)	0
Other Financing Sources:		
Donations and forfeitures of property	435	0
Transfers-in/out without reimbursement (+/-)	(1,632)	0
Imputed financing from costs absorbed by others	239,548	0
Other (+/-)	578	0
Total Financing Sources	$6,063,547	$0
Net Cost of Operations (+/-)	8,076,735	(1)
Ending Balances	$32,276,300	$1
UNEXPENDED APPROPRIATIONS		
Beginning Balances	$636,846	$0
Prior period adjustments (+/-)		
Prior Period Adjustments - Restated (+/-)	0	0
Beginning Balance, Restated	636,846	0
Prior Period Adjustments - Not Restated (+/-)	0	0
Beginning Balances, as adjusted	$636,846	$0
Budgetary Financing Sources:		
Appropriations received	3,854,081	0
Appropriations transferred-in/out (+/-)	18,394	0
Other adjustments (rescissions, etc) (+/-)	(33,936)	0
Appropriations used	(4,079,023)	0
Nonexchange revenue	0	0
Donations and forfeitures of cash and cash equivalents	0	0
Transfers-in/out without reimbursement (+/-)	0	0
Other budgetary financing sources (+/-)	0	0
Other Financing Sources:		
Donations and forfeitures of property	0	0
Transfers-in/out without reimbursement (+/-)	0	0
Imputed financing from costs absorbed by others	0	0
Other (+/-)	0	0
Total Financing Sources	($240,484)	$0
Net Cost of Operations (+/-)	0	0
Ending Balances	$396,362	$0

2004 Consolidated	2003 Consolidated
$34,289,488	$39,695,092
0	(2,669,485)
34,289,488	37,025,607
0	0
$34,289,488	$37,025,607
0	0
0	0
0	0
4,079,023	4,323,711
1,434,495	931,241
0	0
315,045	863,243
(3,945)	(32,536)
435	4,648
(1,632)	(56,344)
239,548	225,066
578	(19,379)
$6,063,547	$6,239,650
8,076,736	8,975,769
$32,276,299	$34,289,488
$636,846	$1,064,864
0	0
636,846	1,064,864
0	0
$636,846	$1,064,864
3,854,081	4,027,057
18,394	196,111
(33,936)	(344,418)
(4,079,023)	(4,306,768)
0	0
0	0
0	0
0	0
0	0
0	0
0	0
0	0
($240,484)	($428,018)
0	0
$396,362	$636,846

Department of Defense- Department of the Army, Civil Works Fund

COMBINING STATEMENT OF BUDGETARY RESOURCES

As of September 30, 2004 and 2003 ($ in Thousands)

BUDGETARY FINANCING ACCOUNTS	Special Funds	Trust Funds	Transfer Funds	Borrowing Authority
BUDGETARY RESOURCES				
Budget Authority:				
Appropriations received	$56,251	$817,249	$0	$0
Borrowing authority	0	0	0	135
Contract authority	0	0	0	0
Net transfers (+/-)	(40,432)	0	173,267	0
Other	0	0	0	0
Unobligated balance:				
Beginning of period	36	208,348	21,310	(380)
Net transfers, actual (+/-)	0	0	28,495	0
Anticipated Transfers Balances	0	0	0	0
Spending authority from offsetting collections:				
Earned	0	0	0	0
Collected	0	0	10	2,261
Receivable from Federal sources	0	0	0	0
Change in unfilled customer orders	0	0	0	0
Advance received	0	0	0	1
Without advance from Federal sources	0	0	11	0
Anticipated for the rest of year, without advances	0	0	0	0
Transfers from trust funds	0	0	0	0
Subtotal	$0	$0	$21	$2,262
Recoveries of prior year obligations	0	0	0	0
Temporarily not available pursuant to Public Law	0	(10,000)	0	0
Permanently not available	0	0	0	(1,991)
Total Budgetary Resources	$15,855	$1,015,597	$223,093	$26
STATUS OF BUDGETARY RESOURCES				
Obligations incurred:				
Direct	$15,794	$926,253	$175,594	$99
Reimbursable	0	0	10	269
Subtotal	15,794	926,253	175,604	368
Unobligated balance:				
Apportioned	62	0	19,892	0
Exempt from apportionment	0	89,344	27,589	(342)
Other available	(1)	0	0	0
Unobligated Balances Not Available	0	0	8	0
Total, Status of Budgetary Resources	$15,855	$1,015,597	$223,093	$26
Relationship of Obligations to Outlays:				
Obligated Balance, Net - beginning of period	$3,039	$127,939	$18,994	$890
Obligated Balance transferred, net (+/-)	0	0	0	0
Obligated Balance, Net - end of period:				
Accounts receivable	0	0	0	0
Unfilled customer order from Federal sources	0	0	(11)	0
Undelivered orders	2,147	264,884	15,035	2
Accounts payable	763	10,179	18,205	367
Outlays:				
Disbursements	15,922	779,128	161,359	889
Collections	0	0	(10)	(2,262)
Subtotal	$15,922	$779,128	$161,349	($1,373)
Less: Offsetting receipts	(47,914)	(1,020,844)	0	0
Net Outlays	($31,992)	($241,716)	$161,349	($1,373)

Revolving Funds	Contributed Funds	General Funds	FUSRAP	2004 Combined	2003 Combined
$0	$413,585	$3,714,081	$140,000	$5,141,166	$7,652,893
0	0	0	0	135	0
0	0	0	0	0	0
0	0	74,089	0	206,924	160,964
0	0	0	0	0	0
81,068	261,803	1,275,601	2,440	1,850,226	1,741,013
0	0	0	0	28,495	0
0	0	0	0	0	0
0	0	0	0	0	0
4,044,756	187	1,161,272	3,599	5,212,085	5,065,570
(8,249)	0	72,282	71	64,104	(74,841)
0	0	0	0	0	0
(1,984)	(1)	31,644	0	29,660	(16,318)
(1,112)	8	273,911	(263)	272,555	262,126
0	0	0	0	0	0
0	0	0	0	0	0
$4,033,411	$194	$1,539,109	$3,407	$5,578,404	$5,236,537
0	0	0	0	0	0
0	0	0	0	(10,000)	0
0	0	(26,259)	(826)	(29,076)	(8,653)
$4,114,479	$675,582	$6,576,621	$145,021	$12,766,274	$14,782,754
$0	$415,458	$3,942,646	$139,335	$5,615,179	$5,516,359
4,110,926	186	1,342,990	3,434	5,457,815	5,033,749
4,110,926	415,644	5,285,636	142,769	11,072,994	10,550,108
0	0	1,211,933	2,252	1,234,139	1,387,762
3,552	259,938	78,995	0	459,076	2,844,875
1	0	(1)	0	(1)	0
0	0	58	0	66	9
$4,114,479	$675,582	$6,576,621	$145,021	$12,766,274	$14,782,754
$908,939	$126,649	($212,219)	$33,390	$1,007,621	$1,047,323
0	0	0	0	0	0
(13,340)	0	(211,289)	(75)	(224,704)	(160,601)
(37,206)	(63)	(1,868,987)	(1,542)	(1,907,809)	(1,635,255)
445,315	123,483	1,168,372	3,664	2,022,902	1,628,915
503,891	24,651	563,605	26,626	1,148,287	1,174,565
4,130,567	394,213	5,075,524	147,679	10,705,281	10,402,525
(4,042,773)	(186)	(1,192,916)	(3,599)	(5,241,746)	(5,049,251)
$87,794	$394,027	$3,882,608	$144,080	$5,463,535	$5,353,274
0	(413,585)	(109,954)	0	(1,592,297)	(904,214)
$87,794	($19,558)	$3,772,654	$144,080	$3,871,238	$4,449,060

Department of Defense- Department of the Army, Civil Works Fund

COMBINING STATEMENT OF FINANCING

As of September 30, 2004 and 2003 ($ in Thousands)

Resources Used to Finance Activities:	**Special Funds**	**Trust Funds**	**Transfer Funds**
Budgetary Resources Obligated			
Obligations incurred	$15,794	$926,253	$175,604
Less: Spending authority from offsetting collections and recoveries (-)	0	0	(21)
Obligations net of offsetting collections and recoveries	$15,794	$926,253	$175,583
Less: Offsetting receipts (-)	(47,914)	(1,020,844)	0
Net obligations	($32,120)	($94,591)	$175,583
Other Resources			
Donations and forfeitures of property	0	0	0
Transfers in/out without reimbursement (+/-)	(378)	(101,927)	(26,897)
Imputed financing from costs absorbed by others	0	0	0
Other (+/-)	0	0	0
Net other resources used to finance activities	($378)	($101,927)	($26,897)
Total resources used to finance activities	($32,498)	($196,518)	$148,686
Resources Used to Finance Items not Part			
Change in budgetary resources obligated for goods, services and benefits ordered but not yet provided			
Undelivered Orders (-)	$269	($146,108)	($3,938)
Unfilled Customer Orders	0	0	11
Resources that fund expenses recognized in prior periods	(1,102)	(10,647)	0
Budgetary offsetting collections and receipts that do not affect net cost of operations	47,914	1,020,844	0
Resources that finance the acquisition of assets	(1,269)	(110,982)	(114,596)
Other resources or adjustments to net obligated resources that do not affect net cost of operations			
Less: Trust or Special Fund Receipts Related to Exchange in the Entity's Budget (-)	0	0	0
Other (+/-)	377	101,928	26,897
Total resources used to finance items not part of the net cost of operations	$46,189	$855,035	($91,626)
Total resources used to finance the net cost of operations	$13,691	$658,517	$57,060
Components of the Net Cost of Operations that will			
Components Requiring or Generating Resources in Future Period:			
Increase in annual leave liability	$0	$0	$0
Increase in environmental and disposal liability	0	0	0
Upward/Downward reestimates of credit subsidy expense (+/-)	0	0	0
Increase in exchange revenue receivable from the the public (-)	0	0	0
Other (+/-)	0	0	0
Total components of Net Cost of Operations that will require or generate resources in future periods	$0	$0	$0
Components not Requiring or Generating Resources:			
Depreciation and amortization	28	1,816	2,453
Revaluation of assets or liabilities (+/-)	0	54	2,014
Other (+/-)			
Trust Fund Exchange Revenue	0	0	0
Cost of Goods Sold	0	0	0
Operating Material & Supplies Used	0	0	0
Other	(14)	65,466	0
Total components of Net Cost of Operations that will not require or generate resources	$14	$67,336	$4,467
Total components of net cost of operations that will not require or generate resources in the current period	$14	$67,336	$4,467
Net Cost of Operations	$13,705	$725,853	$61,527

Borrowing Authority	Revolving Funds	Contributed Funds	General Funds	FUSRAP	2004 Combined	2003 Combined
$368	$4,110,926	$415,644	$5,285,636	$142,769	$11,072,994	$10,550,108
(2,262)	(4,033,411)	(194)	(1,539,109)	(3,407)	(5,578,404)	(5,236,537)
($1,894)	$77,515	$415,450	$3,746,527	$139,362	$5,494,590	$5,313,571
0	0	(413,585)	(109,954)	0	(1,592,297)	(904,214)
($1,894)	$77,515	$1,865	$3,636,573	$139,362	$3,902,293	$4,409,357
0	(99)	0	534	0	435	4,648
(1,223)	(1,578)	(9,736)	140,107	0	(1,632)	(56,344)
0	228,490	0	11,058	0	239,548	225,066
1,991	0	0	(1,412)	0	579	(19,379)
$768	$226,813	($9,736)	$150,287	$0	$238,930	$153,991
($1,126)	$304,328	($7,871)	$3,786,860	$139,362	$4,141,223	$4,563,348
$162	($81,227)	($22,440)	($147,365)	$472	($400,175)	($154,315)
1	(3,095)	7	305,555	(263)	302,216	245,807
0	0	(4,564)	(38,965)	0	(55,278)	0
0	0	413,585	109,954	0	1,592,297	904,695
(153)	(51,232)	(208,523)	(1,197,245)	0	(1,684,000)	1,399,859
0	0	0	(10,000)	0	(10,000)	0
1,223	1,578	9,738	(140,105)	0	1,636	0
$1,233	($133,976)	$187,803	($1,118,171)	$209	($253,304)	$2,396,046
$107	$170,352	$179,932	$2,668,689	$139,571	$3,887,919	$6,959,394
$0	$0	$0	$0	$0	$0	$0
0	0	0	0	0	0	0
0	0	0	0	0	0	0
0	0	0	0	0	0	0
0	50,105	0	861	0	50,966	66,422
$0	$50,105	$0	$861	$0	$50,966	$66,422
0	52,356	428	2,316,379	0	2,373,460	447,661
0	3,228	(202,518)	(624,976)	0	(822,198)	1,477,630
0	0	0	0	0	0	0
0	0	0	0	0	0	0
0	0	0	0	0	0	0
0	39	397,174	2,123,887	37	2,586,589	24,662
$0	$55,623	$195,084	$3,815,290	$37	$4,137,851	$1,949,953
$0	$105,728	$195,084	$3,816,151	$37	$4,188,817	$2,016,375
$107	$276,080	$375,016	$6,484,840	$139,608	$8,076,736	$8,975,769

Required Supplementary Stewardship Information

Federal Mission Property, Plant and Equipment

Yearly Investment in Federal Mission Property, Plant and Equipment
For Fiscal Year Ended September 30, 2004
(In Millions of Dollars)

(a) Categories	(b) FY2000	(c) FY2001	(d) FY2002	(e) FY2003	(f) FY2004
1. Bank Stabilization Projects	nr	nr	nr	nr	$74
TOTAL:					$74

Narrative Statement:

Investments in Federal Mission Property, Plant and Equipment refer to those expenses incurred by USACE for the protection of the riverbanks of the Mississippi River and other navigable waterways inside the continental United States. Stabilization and protection of the riverbanks are important to the flood control and navigation plans, serving to protect flood control features and to insure the desired alignment of the river's navigation channel. Stabilizing the riverbanks and channels provide an efficient navigation alignment, increase the flood-carrying capacity of the river, and or protection of the levees system to include the tributary basin improvements for major drainage. The process by which this is accomplished is by; cutoffs (shortening the river and reducing flood heights), revetment (controlling the river's meandering), dikes (directing the flow), and improvement dredging (realigning the river/channel).

Notes:

1. For FY 2000 – 2003 USACE does not have historical data as this is our first reporting of Federal Mission Property, Plant and Equipment in the Required Supplementary Stewardship Information section of the financial statements. (nr = Nonreporting)

2. After major floods in 1882, 1912, 1913 and 1927 the Flood Control Act of 1928 was signed which committed the federal government to a definite program of flood control. This legislation authorized the Mississippi River and Tributaries Project, the nation's first comprehensive flood control and navigation act.

3. Investments 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 Accounting Standards requirements.

Heritage Assets

For Fiscal Year Ended September 2004

(a)	(b) Measurement Quantity	(c) As of 10/01/03	(d) Additions	(e) Deletions	(f) As of 9/30/04
Museums	Each	1			1
Monuments & Memorials	Each	1			1
Cemeteries	Sites	0			0
Archeological Sites	Sites	129	13		142
Buildings & Structure	Each	327	21		348
Major Collections	Each	1			1

Narrative Statement

USACE administers the Lake Superior Marine Museum as part of the Operations and Maintenance Mission of the Detroit District. This museum has gone inadvertently unreported in previous submittals on USACE Heritage Assets.

We have one (1) Major Collection, that being the collection of historical memorabilia, historic artifacts and records managed by the Headquarters, U.S. Army Corps of Engineers Office of History.

Other than multipurpose heritage assets, heritage assets are not material to the mission of the U. S. Army Corps of Engineers. Disclosures pertinent to multipurpose heritage assets are contained in the financial statements.

Heritage assets classified as Land are special land plots containing archaeological sites as listed on the National Register of Historic Places or eligible to be listed.

Heritage assets on display are assumed to be in adequate condition for display purposes, consistent with their origins, unless otherwise noted. Reported heritage assets are free of material conditions that are counter to safeguarding, adequately protecting, and properly managing those assets; they have not materially degraded while under the care of the U. S. Army Corps of Engineers. The existence of most of the un-categorized heritage assets is informally known to be adequate for display purposes, however, the condition of many un-categorized assets are unknown.

Cemeteries and Archeological Sites are archeological properties listed on or eligible for, the National Register of Historic Places. These archeological assets cover almost the entire range of human occupation of the Continental United States beginning with the Kennewick Man Discovery Site in Washington State, dating to approximately 10,000 years before present, to archeological remains of early European-American settlements such as Fort Independence in Georgia. Of the 13 new additions, 12 were individual site nominations to the National Register of Historic Places and 1 Multiple Property Nomination for the John H. Kerr Reservoir, Wilmington District.

Buildings and Structures include a range of historic resources from a covered bridge in Sacramento District to early farming structures in Savannah District. It also includes some non-traditional structures such as a snag boat that operated on the Mississippi River. The 21 new additions were submitted by the Rock Island District for the Upper Mississippi River and Illinois Waterway Projects.

Nonfederal Physical Property

Yearly Investment in State and Local Governments
For Fiscal Years FY 2000 through FY 2004
(In Millions of Dollars)

(a) Categories	(b) FY2000	(c) FY2001	(d) FY2002	(e) FY2003	(f) FY2004
Transferred Assets:					
1. Federal Mission Related	nr	nr	nr	nr	$4,429
Funded Assets:					
2. Federal Mission Related	nr	nr	nr	nr	0
TOTAL:					$4,429

Narrative Statement:

Investments in Nonfederal Property refers to those expenses incurred by USACE for the purchase, construction or major renovation of physical property owned by State and Local Governments, including major additions and replacements; the purchase of major equipment; and the purchase of improvement of other physical assets. The authority to enter into cost share agreements with nonfederal sponsors is governed under numerous Water Resources Development Acts starting with the Act of 1992.

Notes:

1. For FY 2000 – 2003 USACE does not have historical data as this is our first reporting of Nonfederal Physical Property in the Required Supplementary Stewardship Information section of the financial statements. (nr = Nonreporting)

2. Under numerous authorities USACE provides design, build and construction services/management for the missions of commercial navigation, flood/storm damage reduction, hydropower, regulatory, environmental, recreation and water supply.

3. Investments 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 Accounting Standards requirements.

General Property, Plant and Equipment

Real Property Deferred Maintenance Amounts
As of September 30, 2004

(a)	(b)
Property Type/Major Class	
1. Real Property	
A. Buildings	
B. Structures	$883,000,000
2. Total	$883,000,000

Narrative Statement: Deferred maintenance at Civil Works water resources projects operated and maintained by the U.S. Army Corps of Engineers was determined through the budget development process whereby operations managers identify the operation and maintenance (O&M) needs at each project in the Civil Works inventory. O&M needs are based on inspections of project Features, engineering analyses and historical experience.

Department of Defense- Department of the Army, Civil Works Fund

STATEMENT OF DISAGGREGATED BUDGETARY RESOURCES

As of September 30, 2004 and 2003 ($ in Thousands)

BUDGETARY RESOURCES	**Civil Works**	**2004 Combined**	**2003 Combined**
Budgetary Financing Accounts			
Budget Authority:			
Appropriations received	$5,141,165	$5,141,166	$7,652,893
Borrowing authority	135	135	0
Contract authority	0	0	0
Net transfers (+/-)	206,924	206,924	160,964
Other	0	0	0
Unobligated balance:			
Beginning of period	1,850,227	1,850,226	1,741,013
Net transfers, actual (+/-)	28,495	28,495	0
Anticipated Transfers Balances	0	0	0
Spending authority from offsetting collections:			
Earned	0	0	0
Collected	5,212,085	5,212,085	5,065,570
Receivable from Federal sources	64,103	64,104	(74,841)
Change in unfilled customer orders	0	0	0
Advance received	29,660	29,660	(16,318)
Without advance from Federal sources	272,556	272,555	262,126
Anticipated for the rest of year, without advances	0	0	0
Transfers from trust funds	0	0	0
Subtotal	$5,578,404	$5,578,404	$5,236,537
Recoveries of prior year obligations	0	0	0
Temporarily not available pursuant to Public Law	(10,000)	(10,000)	0
Permanently not available	(29,076)	(29,076)	(8,653)
Total Budgetary Resources	$12,766,274	$12,766,274	$14,782,754

Department of Defense- Department of the Army, Civil Works Fund

STATEMENT OF DISAGGREGATED BUDGETARY RESOURCES

As of September 30, 2004 and 2003 ($ in Thousands)

STATUS OF BUDGETARY RESOURCES	Civil Works	2004 Combined	2003 Combined
Non-Budgetary Financing Accounts			
Obligations incurred:			
Direct	$5,615,177	$5,615,179	$5,516,359
Reimbursable	5,457,816	5,457,815	5,033,749
Subtotal	$11,072,993	$11,072,994	$10,550,108
Unobligated balance:			
Apportioned	1,234,138	1,234,139	1,387,762
Exempt from apportionment	459,076	459,076	2,844,875
Other available	0	(1)	0
Unobligated Balances Not Available	66	66	9
Total, Status of Budgetary Resources	$12,766,273	$12,766,274	$14,782,754
Relationship of Obligations to Outlays:			
Obligated Balance, Net ? beginning of period	$1,007,622	$1,007,621	$1,047,323
Obligated Balance transferred, net (+/-)	0	0	0
Obligated Balance, Net ? end of period:			
Accounts receivable	(224,704)	(224,704)	(160,601)
Unfilled customer order from Federal sources	(1,907,810)	(1,907,809)	(1,635,255)
Undelivered orders	2,022,903	2,022,902	1,628,915
Accounts payable	1,148,288	1,148,287	1,174,565
Outlays:			
Disbursements	$10,705,282	$10,705,281	$10,402,525
Collections	(5,241,745)	(5,241,746)	(5,049,251)
Subtotal	$5,463,537	$5,463,535	$5,353,274
Less: Offsetting receipts	(1,592,297)	(1,592,297)	(904,214)
Net Outlays	$3,871,240	$3,871,238	$4,449,060

Required Supplemental Information - Part A
AT96 - U.S. Army Corps of Engineers

Government Transactions from the Consolidating Trial Balance

Schedule, Part A DoD Intragovernmental Asset Balances. ($ Amounts in Thousands).	Treasury Index:	Fund Balance with Treasury	Accounts Receivable	Loans Receivable	Investments	Other
Unidentifiable Federal Agency Entity (Other than DoD entities)	0		$88			
The Judiciary	10		$20			
Department of Agriculture	12		$996			
Department of Commerce	13		$140			
Department of the Interior	14		$353,489			
Department of Justice	15		$1,201			
Department of Labor	16		$1			
Navy General Fund	17		$147			
United States Postal Service	18		$17			
Department of State	19		$1,170			
Department of the Treasury	20	$2,386,688	$65		$2,741,917	
Army General Fund	21		$848			
Office of Personnel Management	24		$4			
Social Security Administration	28		$1			
Nuclear Regulatory Commission	31		$1			
Smithsonian Institution	33		$1,598			
Department of Veterans Affairs	36		$18			
Government Printing Office	4		$1			
U.S. Equal Employment Opportunity Commission	45		$4			
Appalachian Regional Commission	46		$43			
General Service Administration	47		$8			
National Science Foundation	49		$100			
Air Force General Fund	57		$43			
Railroad Retirement Board	60		$2			
National Labor Relations Board	63		$329			
Environmental Protection Agency	68		$29,229			
Department of Transportation	69		$3,541			
Homeland Security	70		$80,010			
Agency for International Development	72		$1,813			
Small Business Administration	73		$7			
Department of Health and Human Services	75		$484			
National Aeronautics and Space Administration	80		$84			
Department of Housing and Urban Development	86		$32			
Department of Energy	89		$34,412			
Department of Education	91		$4			
Independent Agencies	95		$15			
Other Defense Organizations General Funds	97		$71			
Other Defense Organizations Working Capital Funds	97-4930		$3			
Army Working Capital Fund	97-4930.001					$0
The General Fund of the Treasury	99		$9,907			
Architect of the Capitol			$176			
Totals:		**$2,386,688**	**$520,122**		**$2,741,917**	**$0**

Required Supplemental Information - Part B

AT96 - U.S. Army Corps of Engineers

Government Transactions from the Consolidating Trial Balance

Schedule, Part B DoD Intragovernmental entity liabilities. ($ Amounts in Thousands)	Treasury Index:	Accounts Payable	Debts/Borrowings From Other Agencies	Other
The Judiciary	10	$15		
Department of Agriculture	12	$908		$6
Department of Commerce	13	$8,855		$433
Department of the Interior	14	$16,431		$1,027
Department of Justice	15	$472		$129
Department of Labor	16	$45		$43,746
Navy General Fund	17	$1,657		
United States Postal Service	18			$1
Department of State	19	$719		$98
Department of the Treasury	20	$1,235	$15,367	$153,381
Army General Fund	21	$6,604		$98
Office of Personnel Management	24	$73		$11,686
Library of Congress	3	$98		
Department of Veterans Affairs	36	$510		
Government Printing Office	4	$66		
Appalachian Regional Commission	46	$8		
General Service Administration	47	$31,728		$60
National Science Foundation	49	$137		
Air Force General Fund	57	$55		
Tennessee Valley Authority	64	$1,560		$36
Environmental Protection Agency	68	$181		
Department of Transportation	69	$430		
Homeland Security	70	$6,334		$24
Small Business Administration	73			$1
Department of Health and Human Services	75	$364		$57
Department of Housing and Urban Development	86			$3,060
Department of Energy	89	$2,187		$5,115
Department of Education	91	$70		$635
Federal Mediation and Conciliation Services	93	$8		
Independent Agencies	95	$2		
Other Defense Organizations General Funds	97	$351		
Other Defense Organizations Working Capital Funds	97-4930	$11,702		
Army Working Capital Fund	97-4930.001	$493		
Navy Working Capital Fund	97-4930.002	$270		
Air Force Working Capital Fund	97-4930.003	$25		
The General Fund of the Treasury	99	$9,907		$1,839,034
Totals:		**$103,500**	**$15,367**	**$2,058,627**

Required Supplemental Information - Part C

AT96 - U.S. Army Corps of Engineers

Government Transactions from the Consolidating Trial Balance

Schedule, Part C DoD Intragovernmental revenue and related costs. ($ Amounts in Thousands)	Treasury Index:	Earned Revenue
Unidentifiable Federal Agency Entity (Other than DoD entities)	0	$88
The Judiciary	10	$34
Department of Agriculture	12	$9,393
Department of Commerce	13	$3,247
Department of the Interior	14	$77,181
Department of Justice	15	$14,219
Department of Labor	16	$97
Navy General Fund	17	$10,276
United States Postal Service	18	$65
Department of State	19	$7,915
Department of the Treasury	20	$230
Army General Fund	21	$526,886
Social Security Administration	28	$5
Nuclear Regulatory Commission	31	$197
Smithsonian Institution	33	$11,033
Department of Veterans Affairs	36	$2,390
Government Printing Office	4	$1
U.S. Equal Employment Opportunity Commission	45	$5
General Service Administration	47	$356
National Science Foundation	49	$1,576
General Accounting Office	5	$375
Air Force General Fund	57	$52,227
Railroad Retirement Board	60	$5
National Labor Relations Board	63	$2
Tennessee Valley Authority	64	$670
Environmental Protection Agency	68	$109,146
Department of Transportation	69	$27,907
Homeland Security	70	$241,440
Agency for International Development	72	$23,992
Small Business Administration	73	$7
American Battle Monuments	74	$8
Department of Health and Human Services	75	$6,055
National Aeronautics and Space Administration	80	$44,353
Department of Housing and Urban Development	86	$237
National Archives and Records Administration	88	$1
Department of Energy	89	$22,207
Department of Education	91	$27
Independent Agencies	95	$1,242
Other Defense Organizations General Funds	97	$35,726
Other Defense Organizations Working Capital Funds	97-4930	$105
Navy Working Capital Fund	97-4930.002	$1
Architect of the Capitol		$3,881
Totals:		**$1,234,808**

Required Supplemental Information - Part E

AT96 - U.S. Army Corps of Engineers

Government Transactions from the Consolidating Trial Balance

Schedue, Part E DoD Intragovernmental Non-exchange Revenues ($ Amounts in Thousands)	Treasury Index:	Transfers In	Transfers Out
Department of Agriculture	12		$835
Department of Commerce	13		$64
Department of the Interior	14	$69,111	$378
Army General Fund	21	$78	$331
General Service Administration	47		$23
Tennessee Valley Authority	64		$1,881
Department of Transportation	69	$2,850	
Homeland Security	70		$204
Department of Energy	89	$246,738	
Other Defense Organizations General Funds	97	$0	
Navy Working Capital Fund	97-4930.002		$211
The General Fund of the Treasury	99	$774,025	$775,461
Totals:		**$1,092,802**	**$779,388**

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

November 8, 2004

MEMORANDUM FOR COMMANDER, U.S. ARMY CORPS OF ENGINEERS

SUBJECT: Independent Auditor's Report on the Fiscal Year 2004 U.S. Army Corps of Engineers, Civil Works, Financial Statements (Report No. D-2005-016)

The Chief Financial Officers (CFO) Act of 1990, as amended by the Federal Financial Management Act of 1994, requires Federal agency Inspectors General appointed under the Inspector General Act of 1978, as amended, to audit their respective agencies' financial statements or determine that "an independent external auditor" should conduct such audits. Pursuant to this statutory authority, the undersigned Inspector General assumed responsibility for auditing the accompanying U.S. Army Corps of Engineers, Civil Works, (USACE) Consolidated Balance Sheet as of September 30, 2004 and 2003, the related Consolidated Statement of Net Cost, the Consolidated Statement of Changes in Net Position, the Combined Statement of Budgetary Resources, and the Combined Statement of Financing for the fiscal years then ended.

The financial statements are the responsibility of USACE management. USACE is also responsible for implementing effective internal control and for complying with laws and regulations. We are unable to give an opinion on the USACE Fiscal Year 2004 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 the audit.

Disclaimer of Opinion on the Financial Statements

USACE acknowledged to us that the USACE FY 2004 Financial Statements may not be fairly presented in conformity with Federal accounting standards. We provided USACE with numerous audit findings, for which USACE is in the process of completing the necessary corrective actions.

Based on the inability of management to assert that the financial statements are free from material error, and based on the deficiencies acknowledged by management, we did not perform auditing procedures to determine whether material amounts on the financial statements were fairly presented. We did not perform these and other auditing procedures because Section 1008(d) of the FY 2002 National Defense Authorization Act limits the Inspector General of the Department of Defense to perform only audit procedures required by generally accepted government auditing standards that are consistent with the representations made by management. USACE acknowledged, and prior audits identified the material weaknesses listed in the Summary of Internal Control.

"A regular Statement and Account of the Receipts and Expenditures of all public Money shall be published from time to time."—Constitution of the United States, Article I, Section 9

These material weaknesses also affect the reliability of certain information contained in the annual financial statements—much of which is taken from the same data sources as the principal financial statements. As described above, we are unable to express, and we do not express, an opinion on the financial statements[1] and the accompanying information.

Summary of Internal Control

In planning our audit, we considered USACE internal control over financial reporting and compliance. We did this to determine our procedures for auditing the financial statements and to comply with Office of Management and Budget (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. However, previously identified reportable conditions,[2] some of which are material, continued to exist in the following areas:

- Financial Management Systems;
- General Property, Plant, and Equipment; and
- Accounts Payable.

A material weakness is a condition that precludes the entity's internal control from providing reasonable assurance that misstatements, losses, or noncompliance that are material in relation to the financial statements would be prevented or detected on a timely basis. Our internal control work would not necessarily disclose all material weaknesses. See the Attachment for additional details on material internal control weaknesses.

Summary of Compliance with Laws and Regulations

Our work to determine compliance with selected provisions of applicable laws and regulations related to financial reporting was limited because management acknowledged, and prior audits confirm, that instances of noncompliance continue to exist. USACE acknowledged to us that the financial management systems do not fully comply with Federal financial management systems requirements, applicable Federal accounting standards, and the U.S. Government Standard General Ledger (USSGL) at the transaction level, as required under the Federal Financial Management Improvement Act (FFMIA) of 1996. In previously issued audit reports, the Government Accountability Office (GAO) and U.S. Army Audit Agency (AAA) noted instances of noncompliance with:

- Federal Manager's Financial Integrity Act (FMFIA) of 1982;
- OMB Circular A 123, "Management Accountability and Control;"
- OMB Circular A 130, "Management of Federal Information Resources;" and
- OMB Circular A 127, "Federal Management Systems."

Therefore, we did not determine whether USACE was in compliance with all applicable laws and regulations related to financial reporting. See the Attachment for additional details on compliance with laws and regulations.

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[1] The annual financial statements include the principal financial statements, management discussion and analysis, consolidating and combining financial statements, Required Supplementary Stewardship Information, Required Supplementary Information, and Other Accompanying Information.

[2] Reportable conditions are matters coming to the auditor's attention that, in his or her judgment, should be communicated to management because they represent significant deficiencies in the design or operation of internal control, which could adversely affect the organization's ability to initiate, record, process, and report financial data consistent with the assertions of management in financial statements.

Management Responsibility

Management is responsible for:

- preparing the financial statements in conformity with generally accepted accounting principles;
- establishing, maintaining, and assessing internal control to provide reasonable assurance that the broad control objectives of FMFIA are met; and
- complying with applicable laws and regulations.

Joseph E. Schmitz
Inspector General
Department of Defense

Paul J. Granetto, CPA
Assistant Inspector General
Defense Financial Auditing Service

Attachment:
As stated

"A regular Statement and Account of the Receipts and Expenditures of all public Money shall be published from time to time."—Constitution of the United States, Article I, Section 9

Report on Internal Control and Compliance with Laws and Regulations

Internal Control

Management is responsible for implementing effective internal control and for providing reasonable assurance that accounting data are accumulated, recorded, and reported properly and that assets are safeguarded against misappropriation and abuse. Our objective was not to, and we do not, express an opinion on internal control over financial reporting. However, management acknowledged that previously identified reportable conditions continue to exist. In accordance with Section 1008(d) of the FY 2002 National Defense Authorization Act, OIG DoD did not perform sufficient internal control testing to determine to what degree the weaknesses continue to exist.

The following financial management deficiencies[3] are indications of material weaknesses or reportable conditions in internal control that may adversely affect any decision by USACE that is based, in whole or in part, on information that is inaccurate because of these deficiencies. Financial information reported by USACE also may contain misstatements resulting from these deficiencies.

Financial Management Systems. The Corps of Engineers Financial Management System (CEFMS) did not process and summarize all accounting transactions in accordance with the USSGL. USACE did not have a process in place to ensure that the CEFMS general ledger correlations were promptly updated, or that deficiencies were corrected.

USACE did not have effective controls to ensure accounting information transferred from the Corps of Engineers Enterprise Management Information System (CEEMIS) to the Defense Departmental Reporting System – Automated Financial Statements (DDRS-AFS) was reliable. USACE made undocumented adjustments because DoD policy and Federal system requirements for making accounting adjustments were not adequately implemented. As a result, the financial information imported into DDRS-AFS and used to prepare the USACE financial statements was unreliable.

General Property, Plant, and Equipment. As discussed in our FY 2003 financial statement disclaimer opinion, internal controls were not adequate because USACE guidance was not consistently implemented and strictly enforced. Existence issues for buildings and other structures continue. Also, the rights to some structures may not have been properly recorded and treated as capital leases.

Accounts Payable. As discussed in our FY 2003 financial statement disclaimer opinion, internal control testing identified departures from generally accepted accounting principles to include misclassification of general ledger accounts when making accounting journal entries for Accounts Payable.

Compliance with Laws and Regulations

Management is responsible for compliance with existing laws and regulations related to financial reporting. Our work to determine compliance with selected provisions of the applicable laws and regulations was limited because management acknowledged instances of noncompliance continue to exist. Therefore, we did not determine whether USACE 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 compliance with applicable laws and regulations.

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[3] Described in greater detail in previous IG DoD reports.

Financial Management Systems. USACE is required to comply with financial management systems reporting requirements.

- The Federal Mangers' Financial Integrity Act of 1982 requires agencies to evaluate the systems and to annually report whether those systems are in compliance with applicable requirements. When systems are not in compliance, the statement must include a report of internal accounting and administrative control material weaknesses and plans and a schedule for correcting the material weaknesses.
- OMB Circular A-123, revised June 21, 1995, requires agencies and individual Federal managers to take systematic and proactive measures to: assess the adequacy of management controls in Federal programs and operations, identify needed improvements, take corresponding corrective actions, and report annually on management controls.
- OMB Circular A-130, Appendix III, establishes a minimum set of controls to be included in Federal automated information security programs, assigns Federal agency responsibilities for the security of automated information, and links agency information security programs and agency management control systems established in accordance with OMB Circular A-123. Agencies should implement and maintain their automated security programs to ensure that adequate security is provided for all agency information collected, processed, transmitted, stored, or disseminated in general support systems and major applications.
- OMB Circular A-127, revised July 23, 1993, requires agencies to develop, operate, evaluate, and report on financial management systems. It also requires that financial management systems provide complete, reliable, consistent, timely, and useful information.

USACE acknowledged that its financial management systems do not fully comply with Federal financial management systems requirements, applicable Federal accounting standards, and the USSGL at the transaction level, as required under FFMIA. According to GAO and AAA prior audit reports, USACE did not fully comply with the FMFIA and OMB Circulars A-123 and A-130 requirements to protect the integrity of its financial management systems, identify needed improvements, and take corresponding corrective actions. During FY 2004, OIG DoD reviewed previously identified GAO and AAA deficiencies related to general and application controls. Our audit work concluded that USACE had not fully implemented all of the GAO and AAA recommendations. The continued CEFMS general and application computer control vulnerabilities impair the ability of USACE to ensure reliability, confidentiality, and availability of financial and sensitive data, as required by OMB Circular A 127.

Audit Disclosures

USACE acknowledged to us on September 20, 2004, that the USACE financial management systems cannot provide adequate evidence supporting various material amounts on the financial statements. Therefore, we did not conduct audit work related to Accounts Payable.

This report does not include recommendations to correct the material internal control weaknesses and instances of noncompliance because previous audit reports contained recommendations for corrective actions.

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