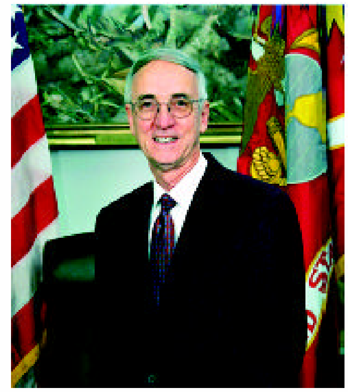
Department of the Navy

Annual Financial Report

Fiscal Year 2004

Table of Contents



THE SECRETARY OF THE NAVY
WASHINGTON, D.C. 20350-1000

2 November 2004

Today, as has been the case throughout our Nation's history, the Navy and Marine Corps team answers the President's call to duty by being the first on station with staying power. Operating on the front lines of the Global War on Terrorism, our naval expeditionary forces have displayed extraordinary strategic agility and operational flexibility. To continue to answer the call and maintain our warfighting effectiveness, we are leveraging our investments, adopting innovative organizational concepts, and instilling best business practices both afloat and ashore.

To improve our warfighting capabilities and sustain maritime superiority afloat, we have adopted several new concepts and practices. Fleet Response Plan is a new paradigm in naval operational availability that leverages our naval forces to produce combat ready forces on short notice to support our Nation's objectives. Under the Fleet Response Plan, the Navy can provide significant combat power with six Carrier Strike Groups in less than 30 days, and two more groups within three months in response to a national emergency or crisis. This capability gives us great flexibility and optimizes use of national assets. The Marine Corps Strategy 21 supports the development of enhanced strategic agility, operational reach, and tactical flexibility that enables joint allied and coalition operations. These capabilities provide the Combatant Commanders the ability to respond quickly across the complex spectrum of crises and conflicts.

Ashore, our Training Resource Strategy provides high quality training to our deploying combat forces. It has resulted in more training options, increased productive training days, and reduced pre-deployment training transit time. To standardize management processes and further leverage our investment in the shore establishment, Navy shore installations were aligned under the Commander, Navy Installations Command. This organizational change will enable better decisions regarding the investment of limited funds in our shore establishment. Both the Navy and Marine Corps are aggressively reviewing the way that supporting services are provided to our combat forces. We are converting to civilian or contract service delivery where it makes good sense, thus freeing military manpower for more effective use.

As we pursue these and other related initiatives to transform the Department, fiscal accountability is paramount. The Navy is actively supporting the Department of Defense's goal of achieving a clean audit opinion. We support that goal and have made financial accounting improvements a priority. As testament to our continuing commitment to fiscal accountability, I am pleased to present the Department of the Navy Fiscal Year 2004 Annual Financial Report.

Gordon England

The Assistant Secretary of the Navy
(FINANCIAL MANAGEMENT AND COMPTROLLER)
1000 NAVY PENTAGON
WASHINGTON, D.C. 20350-1000

November 2004

I am pleased to present the Department of the Navy's Fiscal Year 2004 Annual Financial Report. Improvements in the Department's stewardship of public resources are reflected in this year's report.

As the Department of the Navy continues to provide Congress and the public with relevant, reliable, and timely financial information, and strives for favorable audit opinions, accountability becomes even more important as we prosecute the Global War on Terrorism and support the nation's defense needs. The Department's Financial Improvement Plan will help us achieve our goal.

The Financial Improvement Plan identifies actions and timeframes for correcting financial management deficiencies in the Department and will result in further improvements in the Principal Statements and notes presented in this Annual Financial Report. Measurements of success have also been built into this plan. Our financial improvement efforts focus on maintaining a highly skilled workforce; standardizing and transforming business processes; and maintaining and aligning systems with the Department of Defense Business Management Modernization Program. This effort must and will succeed.

I am proud of the Department of the Navy's progress thus far, and the enthusiasm exhibited by all communities that support the business processes that provide our war fighters with the resources and financial intelligence to succeed. We must sustain this momentum, leverage lessons learned, and move forward with transformational initiatives.

Robert L. Panek
Acting

Department of the Navy

Management's Discussion and Analysis

"The very best organizations are the most efficient organizations."

-- The Honorable Gordon R. England, Secretary of the Navy, March 2004

Introduction

The Department of the Navy (DON) is one of the most visible organizations in the world. With service members and civilian employees in geographically dispersed locations, the spotlight on our contributions and our sacrifices never dims. The contributions and sacrifices of our Navy-Marine Corps Team in prosecuting the Global War on Terrorism have been significant to the overall success of U.S. military forces. As a Nation, we are blessed to have a 228-year legacy where magnificent men and women volunteer as Sailors and Marines to protect and defend America. The contributions and sacrifices of our civilian workforce have been instrumental in supporting our Navy-Marine Corps Team. These experienced and dedicated craftspeople, researchers, supply and maintenance specialists, computer experts, service providers, and their managers are an essential part of our total naval force concept.

As we continue to prosecute the Global War on Terrorism, DON remains focused on improving effectiveness to gain efficiency, facilitating our transformation in force management, combat and technological capabilities, and business management. The discussion that follows focuses on our achievements in each area of the DON Balanced Scorecard: People, Combat Capability, Technology Insertion, and Improved Business Practices.

Our People

The Department of the Navy (DON) remains committed to taking care of its people. As reflected in the Secretary of the Navy's priority objectives for fiscal year (FY) 2004, DON is pursuing a strategy that enhances the quality of service and life of our Sailors and Marines and that shapes and streamlines our military and civilian workforce. Below is a synopsis of our achievements in the areas of Quality of Service, Quality of Life, and Human Resource Management.

"Sailors and Marines - along with our civilian workforce - remain the strong and steady foundation of our Naval capabilities."

-- The Honorable Gordon R. England,
Secretary of the Navy, March 2004

Quality of Service

United States Navy	United States Marine Corps
The **Navy** shall be organized, trained, and equipped primarily for prompt and sustained combat incident to operations at sea. It is responsible for the preparation of naval forces necessary for the effective prosecution of war except as otherwise assigned and, in accordance with integrated joint mobilization plans, for the peacetime components of the Navy to meet the needs of war. *(Section 5062, Title 10, U.S. Code)* **Founded 13 October 1775**	The **Marine Corps** shall be organized, trained, and equipped to provide fleet marine forces of combined arms, together with supporting air components, for service with the fleet in the seizure or defense of advanced naval bases and for the conduct of such land operations as may be essential to the prosecution of a naval campaign. *(Section 5063, Title 10, U.S. Code)* **Founded 10 November 1775**

Sailing into New York Harbor, Sailors and Marines "man the rails" aboard the USS IWO JIMA (LHD 7).

DON developed a Training Resource Strategy to provide high quality training to its deploying combat forces. The training of high technology forces in modern warfare has shifted to a stateside network of existing ranges and installations. Fully implemented, the Training Resource Strategy has resulted in more training options, reduced pre-deployment training transit time, and has increased productive training days. The USS ENTERPRISE was the first Carrier Strike Group to deploy under the Training Resource Strategy, utilizing six training ranges. The Training Resource Strategy supports the Fleet Response Plan and will be used to respond quickly to surge requirements by delivering and bringing to bear a capable fighting force. (A discussion of the Fleet Response Plan follows in the next section, "Our Combat Capability.")

In January 2004, DON participated in the first in a series of Joint National Training Capability exercises. These exercises linked a Marine Corps Combined Arms Exercise with live Close Air Support sorties, a Navy Stand-off Land Attack Missile Exercise, an Army rotation at the National Training Center, and an Air Force Air Warrior Exercise. The Marine Corps will be actively involved in future Joint National Training Capability exercises, including Combined Arms Exercises, Marine Aviation Weapons, and Tactics Squadron-1 evolution's scheduled for FY 2005.

QUALITY OF LIFE

DON works to improve the quality of life for Sailors and Marines and their families in order to continue the success of the all volunteer force. Quality of life programs and services available to service members and their families include the Fleet and Family Support Center and Marine Corps Community Services OneSource. The Fleet and Family Support Center provides free operational, mobility and counseling support to all service members, single or married, including activated Reservists, retiree's and Department of Defense (DoD) civilians overseas. The Center has enhanced delivery of services by dispatching Return and Reunion teams to sea and adding online features such as the DoD's new Navy OneSource information and referral system. Similarly, the Marine Corps implemented Marine Corps Community Services OneSource, a DoD-funded pilot program that provides around-the-clock information and referral services to Marines and their families before, during, and after deployments. Marine Corps Community Services OneSource is especially useful to activated Marine Reserves and their families as they negotiate the requirements and procedures associated with utilization of military programs such as TRICARE and other benefit services.

Additionally, DON remains committed to improving living conditions for Sailors and Marines, and their families. With an increased emphasis on public-private ventures and an increase in Basic Allowance for Housing, DON remains on track to eliminate inadequate housing by FY 2007.

Human Resource Management

DON has made several fleet and shore organizational changes that have shown great potential in maximizing the way forces can be employed and supported. One of these changes is alignment of Navy shore installations under a single Major Command - Commander, Navy Installations. This alignment will enable DON to implement common support practices and make better decisions about where to invest limited funds.

Additionally, DON is restructuring its active and reserve forces under the Active Reserve Integration initiative. This initiative will fully integrate the naval reserve force with the active force in an effort to create a more cohesive, surge-ready force. This "one fleet" perspective is the most effective, efficient use of resources because it matches capabilities with requirements for optimum performance. DON expects the realization of Active Reserve Integration to result in increased warfighting wholeness for the current Navy-Marine Corps Team and the team of the next generation.

The FY 2004 National Defense Authorization Act authorized DoD to establish a new human resources management system for DoD civilians known as the National Security Personnel System. This legislation provides flexibility in the hiring and management of civilian workers and links pay to mission accomplishment and performance. The National Security Personnel System will be implemented over a three-year period. DON will participate in the first pilot scheduled to commence at fiscal year-end 2005.

US Marines assigned to the 22nd Marine Expeditionary Unit, Special Operations Capable, conduct physical training on the flight deck of the USS WASP (LHD 1).

Our Combat Capability

"Innovative capabilities will result in profound increases in military power, maintaining the Navy and Marine Corps Team as the preeminent global Naval power."

-- The Honorable Gordon R. England, Secretary of the Navy, March 2004

The Department of the Navy (DON) has embraced a transformational, capabilities-based approach to forming the Navy-Marine Corps Team of tomorrow. Two transformational initiatives underway are the Fleet Response Plan and Tactical Aircraft Integration.

Fleet Response Plan

The Fleet Response Plan, implemented in fiscal year (FY) 2004, represents a new paradigm in force readiness. Under the old paradigm, the Navy sought to achieve the highest levels of readiness for forward-deployed units. While a number of forward-deployed units were at peak readiness, the majority of ships and associated units were not deployed and thus at a point in their Inter-Deployment Readiness Cycle that made it difficult and expensive to meet the rapid surge requirements of a crisis, conflict, or Homeland Defense mission. In contrast, under the Fleet Response Plan, the Navy's goal is to develop and sustain significant, surge-ready combat capabilities through the use of Carrier Strike Groups, Expeditionary Strike Groups, and Surface Strike Groups. Under the "six-plus-two" concept, the Navy will organize and sustain six Carrier Strike Groups capable of deploying within 30 days to support global contingency operations; and an additional two Carrier Strike Groups ready to deploy within 90 days to reinforce or rotate with forces, continue presence operations in other parts of the world, or support military action in other crises. Overall, the Fleet Response Plan provides a framework in which the Navy can balance unprecedented combat capability and readiness with the prudent use of resources.

"Summer Pulse '04"

"Summer Pulse '04" was the Navy's first test of the Fleet Response Plan. During July and August 2004, seven Carrier Strike Groups successfully deployed and operated in five theaters with other U.S. allied and coalition forces. The near-simultaneous deployment of these Carrier Strike Groups provided the Navy and the Joint Combatant Commanders an opportunity to exercise the Fleet Response Plan while maintaining the ability to respond to crises around the globe, enhance regional security and relationships, meet Combatant Commander requirements (including forward presence), and demonstrate a commitment to allies and coalition partners. The success of this exercise reflects the effectiveness and efficiencies associated with DON's investment in readiness and improved productivity.

Signalman communicates with the guided missile destroyer USS CURTIS WILBER (DDG 54) in the Kitty Hawk Carrier Strike Group in Summer Pulse 2004.

TACTICAL AIRCRAFT INTEGRATION

DON continues to implement the Tactical Aircraft Integration plan to create a leaner, more efficient naval strike-fighter force. Success factors of this plan include global sourcing and level readiness. Global sourcing is the ability to task any non-deployed DON squadron to either Navy's or Marine Corps' missions, allowing for a reduction in force structure. Level readiness is the ability to apply the proper resources to training, maintenance, and modernization, ensuring that the smaller force is always capable of responding to the needs of the Navy-Marine Corps Team and the nation. Additionally, support of readiness accounts, modernization programs, and replacement of the F/A-18 and AV-8B with the Short Takeoff and Vertical Landing Joint Strike Fighter will ensure the potential promised by this integration. Overall, Tactical Aircraft Integration retains the Navy-Marine Corps Team's warfighting potential and brings DON a step closer to the flexible sea-based force envisioned for the future.

OUR TECHNOLOGY INSERTION

> *"…our Naval forces have been able to project overwhelming combat power because they are technologically superior. We continue to sustain a robust RDT&E effort as we transform the Navy and Marine Corps to the next generation of combat systems."*
>
> -- The Honorable Gordon R. England, Secretary of the Navy, March 2004

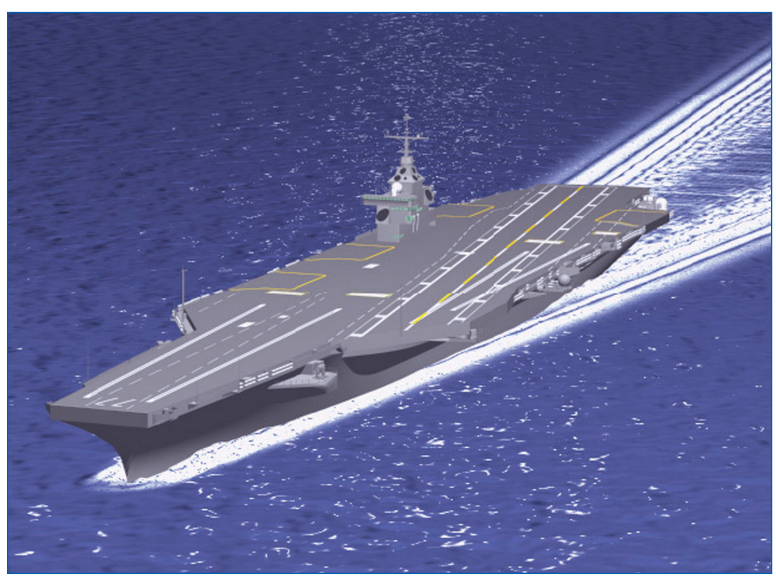
The transformation of our naval forces through innovative operational concepts and the application of appropriate technologies leverage our enduring capabilities for projecting sustainable, immediately deployable, joint combat power. Two focal areas for naval technological transformation include ship programs and Marine Corps aviation and ground equipment, as discussed below. These focal areas are representative examples of naval technological transformation and therefore are part of a broader list of naval transformation priorities.

SHIP PROGRAMS

The Department of the Navy (DON) continues to address the requirement for the acquisition, modernization, and recapitalization of the world's preeminent surface fleet. Continuing to integrate emerging technologies, DON will ensure that tomorrow's fleet will remain on the cutting edge. Two of DON's transformational surface programs include the CVN-21 and the Littoral Combat Ship.

CVN-21

CVN-21 will be a transformational 21st century ship and the future centerpiece of the Carrier Strike Group. It will have a new electrical generation and distribution system, an electro-magnetic aircraft launching system, a new and enlarged flight deck, weapons and material handling improvements, and a smaller crew.



Artist's conception of the CVN-21.

Littoral Combat Ship

The Littoral Combat Ship is a new breed of U.S. Navy warship that will be a critical component of tomorrow's Carrier Strike Groups and Expeditionary Strike Groups. The Navy envisions this ship to be a fast, agile, and affordable surface combatant capable of operating against anti-access, asymmetric threats in littoral (i.e., the transition areas between the sea and land). The Navy plans detailed design and construction of the first Littoral Combat Ship in FY 2005.

Marine Corps Aviation and Ground Equipment

The Marine Corps is committed to transforming tactical and operational capabilities that will provide a critical joint competency for assuring access and projecting naval power. Representative examples of new systems that will enhance the already potent combat power of the Marine Air Ground Task Force are the MV-22 Osprey, Short Take Off and Vertical Landing Joint Strike Fighter, and Expeditionary Fighting Vehicle.

Members of 3rd Battalion, 3rd Marine Regiment, Combat Assault Company advance to offensive positions during exercise Rim of the Pacific (RIMPAC) 2004.

MV-22 Osprey

The MV-22 Osprey remains a priority among Marine Corps aviation acquisitions. While fulfilling the critical Marine Corps medium lift requirement, the MV-22 Osprey's increased range, speed, payload, and survivability will generate truly transformational tactical and operational capabilities. The MV-22 Osprey will replace the Marine Corps' aging fleets of CH-46E Sea Knight and CH-53D Sea Stallion helicopters.

Short Take Off and Vertical Landing Joint Strike Fighter

The Short Take Off and Vertical Landing Joint Strike Fighter will be a single engine, stealth, supersonic aircraft, designed to replace the aging Marine Corps’ AV-8B and F/A-18 fleets. This strike-fighter will combine the basing flexibility of the AV-8B with the multi-role capabilities, speed, and maneuverability of the F/A-18 to fulfill both the air-to-ground and air-to-air requirements of the Marine Corps.

Expeditionary Fighting Vehicle

The Expeditionary Fighting Vehicle will provide Marine Corps surface assault elements the requisite operational and tactical mobility to exploit fleeting opportunities in the fluid operational environment of the future. Designed to be off-loaded by ships located beyond the enemy's visual horizon, the Expeditionary Fighting Vehicle will be capable of carrying a Marine rifle squad at speeds in excess of 20 nautical miles per hour even in rough seas. Production representative vehicle procurement occurred in FY 2003 and will deliver in FY 2005. Initial operational capability will be reached in FY 2008.

A Lighter Amphibious Resupply Cargo (LARC) checks the water level prior to the disembarking members of 3rd Battalion, 3rd Marine Regiment, Combat Assault Company.

Our Improved Business Practices

> *"[Our] continuous improvement initiatives enable us to increase our combat capabilities with the expectation that we become more efficient…at a reduced cost of doing business."*
>
> -- The Honorable Gordon R. England, Secretary of the Navy, March 2004

The breadth of our financial resources requires a steadfast commitment to fiscal accountability and to incorporating efficient and effective business practices throughout the Department of the Navy (DON). To illustrate the relative scope of our financial resources, DON would rank among the 15 largest U.S. corporations on the Fortune 500™ list for total assets. In fiscal year (FY) 2004, DON reported total assets of $321 billion (i.e., combined total dollars of FY 2004 DON General Fund and Navy Working Capital Fund assets). (See FY 2004 DON General Fund and Navy Working Capital Fund consolidated balance sheets in this report.) The following are a few examples of our commitment to improving business and financial management throughout DON.

The golden anchor is proudly displayed by the guided missile cruiser USS LAKE ERIE (CG 70) and reflects the ship's high retention rate.

DON Financial Improvement Program

DON is finalizing development of a Financial Improvement Program that supports DON and Department of Defense (DoD) goals to produce relevant, reliable, and timely financial information. The cornerstone of this program is the DON Financial Improvement Plan (formerly, the Mid-Range Financial Improvement Plan). DON is continuously refining the plan to incorporate executable tasks and timeframes for correcting deficiencies in DON General Fund and Navy Working Capital Fund financial statement line items. This plan, as well as the financial improvement plans of the other Services, will be used to facilitate progress toward a favorable audit opinion on the FY 2007 DoD-wide financial statements.

Similarly, DON has established an audit committee that will interface with the federal and private sector audit communities to ensure that DON financial statements are ready for audit. Additionally, DON is coordinating its financial improvement efforts with the DoD Business Modernization and Systems Integration office – the program management office for the DoD Business Management Modernization Program. This coordination ensures DON compliance with business process and system requirements established and maintained under this DoD program.

Global Combat Support System-Marine Corps

The Global Combat Support System-Marine Corps is part of the Global Combat Support System (GCSS), a DoD - sponsored information technology program, designed to streamline DoD logistics and combat service support processes. GCSS-Marine Corps will be based upon a logistics operational architecture that will facilitate integration of current Marine Corps supply, logistics, distribution, and financial processes. Integration of these processes will enable data and information to be shared across the Marine Corps enterprise and with other Services and agencies. Components of this architecture include, but are not limited to:

- A web-based portal that provides a single point of entry for product and service acquisitions, and

- A logistics functionality that supports Marine Air Ground Task Force command and control (C2) processes.

Initial operational capability of the GCSS-Marine Corps is scheduled for FY 2005.

The Los Angeles-class attack submarine USS HAMPTON (SSN 767) surfaces at the North Pole.

Convergence of Enterprise Resource Planning Pilots

In FY 2004, the Navy component of DON continued to successfully operate four Enterprise Resource Planning (ERP) system pilots – a financial management initiative to streamline Navy business processes. These Navy ERP system pilots are:

- SIGMA (Program Management under the DON General Fund and Navy Working Capital Fund);
- CABRILLO (Warfare Center Management under the Navy Working Capital Fund only);
- SMART (Aviation Supply and Maintenance under the DON General Fund and Navy Working Capital Fund); and
- NEMAIS (Regional Ship Maintenance under the DON General Fund and Navy Working Capital Fund).

A sailor from the guided missile destroyer USS ROSS (DDG 71) throws a line to the pier.

These system pilots use commercial off-the-shelf software approved and certified by the Joint Financial Management Improvement Program. Additionally, under the auspices of the converged ERP program office, the Navy component of DON continued efforts to collapse these ERP system pilots into one solution. The Converged ERP Program will be the key enabler for Sea Enterprise, the flagship effort for transforming required business processes and generating enterprise-wide efficiency savings to support the planned recapitalization of naval forces. Benefits of the converged ERP system include, but are not limited to:

- Improved logistics ashore and afloat, thereby increasing fleet combat readiness;
- End-to-end supply chain integration; and
- Cost reductions and improved performance of business operations for acquisition, budget, procurement, workforce management, and decision-making.

Initial operational capability of the converged ERP system is planned for the third quarter of FY 2006.

Strategic Management

Introduction

The Department of the Navy (DON) remains committed to accomplishing its mission in a way that delivers the best value to the Nation and reflects accountability for results. To this end, DON has consolidated the objectives and performance management goals of the President's Management Agenda with the four tenets of Department of Defense (DoD) risk management – Force Management Risk, Operational Risk, Future Challenges Risk, and Institutional Risk – to form a balanced scorecard for risk management. These four tenets of risk management align with the four perspectives of the DON Balanced Scorecard – People, Combat Capability, Technology Insertion, and Improved Business Practices. This alignment provides DON with an efficient approach to measuring, evaluating, and improving strategic performance consistent with the goals of defense policy and the President's Management Agenda. (A copy of the President's Management Agenda and the Quadrennial Defense Review, which includes a discussion of the four DoD risk tenets, is available at the respective websites of the Office of Management and Budget (http://www.whitehouse.gov/omb) and Defenselink (http://www.defenselink.mil)).

Mission of the Department of the Navy:

- Control and maintain freedom of the seas
- Project power beyond the sea
- Influence events and advance U.S. interests across the full spectrum of military operations

U.S. Marines assigned to Combat Service Support Group Three, role play, as opposition forces observe amphibious assault vehicles deploying from amphibious dock landing ship USS RUSHMORE (LSD 47), during the operational phase of exercise Rim of the Pacific 2004.

PERFORMANCE RESULTS: FY 2004 v. FY 2003

The DON strategic goals and related performance results shown below are representative examples from the balanced scorecard for risk management. To view this balanced scorecard in its entirety, see the website of the Assistant Secretary of the Navy (Financial Management and Comptroller), Office of Budget (http://navweb.secnav.navy.mil).

FORCE MANAGEMENT RISK

Strategic Goal 1: Ensure Sustainable Military Tempo

DON must be able to provide and maintain ready forces necessary to support military operations at any tempo. In FY 2004, DON sustained a force structure necessary to meet deployment requirements of the Global War on Terrorism and other military operations. As displayed in the table below, total military end strength (i.e., combined total of Navy and Marine Corps, active and reserve) decreased by two percent during FY 2004.

Strategic Goal 2: Maintain Reasonable Force Costs

DON continues to strive toward a leaner, more efficient organization so that it can best address its warfighting and recapitalization requirements. One way DON strives to improve operational efficiency is workforce reduction. In FY 2004, DON reduced civilian full-time equivalent workyears (i.e., how DON tracks the civilian workforce) by approximately one percent. (See table below)

Force Management Risk

DON Strategic Goal	Performance Measure	Performance Results	
		FY 2004	FY 2003 *
Ensure Sustainable Military Tempo	**Military End Strength**		
	Active, Navy	373,800	382,235
	Active, Marine Corps	175,000	177,779
	Reserve, Navy	85,900	88,156
	Reserve, Marine Corps	39,600	41,046
Maintain Reasonable Force Costs	**Civilian Full-Time Equivalent Workyears**		
	Navy	179,935	180,032
	Marine Corps	16,878	17,921

**Results derived from FY 2005 President's Budget.*

OPERATIONAL RISK

Strategic Goal 1: Ensure Force Levels

Projecting power from the sea is critical to the security of the United States and its interests abroad. DON remains focused on the Navy-Marine Corps Team's ability to fulfill deployment requirements for U.S. and related international defense missions. In FY 2004, the total number of battle force ships and Marine Corps land forces decreased by nearly two and three percent, respectively (see table below).

Strategic Goal 2: Ensure Force Readiness

The Global War on Terrorism requires that naval forces operate differently, to be more ready and responsive. The Fleet Response Plan has been designed to accomplish these objectives. As displayed in the table below, the number of Navy and Marine Corps personnel on deployment decreased by approximately two percent in FY 2004. However, modifications in readiness thresholds resulted in a 12 percent decrease in monthly flying hours of active crew, and a 24 percent decrease in steaming days per quarter for active force ships.

Operational Risk			
DON Strategic Goal	**Performance Measure**	**Performance Results**	
		FY 2004	**FY 2003 ***
Ensure Force Levels	**Battle Force Ships**		
	Aircraft Carriers	12	12
	Fleet Ballistic Missile Submarines	14	16
	Guided Missile Submarines	4	2
	Surface Combatants	103	106
	Nuclear Attack Submarines	53	54
	Amphibious Warfare Ships	35	36
	Combat Logistics Ships	34	34
	Mine Warfare Ships	17	17
	Support Ships	19	19
	Number of Marine Corps Land Forces		
	Marine Expeditionary Forces	3	3
	Marine Expeditionary Brigades	4	4
	Battalions	69	72
Ensure Force Readiness	Navy / Marine Corps Personnel Readiness Ratings	38,015	38,655
	Monthly Flying Hours Per Crew Ratio (Active)	19.3	22.1
	Active Steaming Days Per Quarter	51.0	67.3

**Results derived from FY 2005 President's Budget.*

Future Challenges Risk

Strategic Goal: Define and Develop Transformational Capabilities

DON remains focused on naval transformational capabilities. A key component of naval transformation is research and development. Representative examples of research and development platforms include:

- Joint Strike Fighter - a family of aircraft that meets the needs of the U.S. Navy, U.S. Marine Corps, U.S. Air Force, and allies.
- DD(X) - a family of advanced multi-mission warships capable of long-range firepower in support of forces ashore.
- V-22 - a joint aircraft program designed to meet the amphibious/vertical assault needs of the Marine Corps and the strike rescue needs of the Navy, and to supplement special mission aircraft.

The table below presents FY 2003 and FY 2004 funding for these research and development platforms.

Future Challenges Risk			
DON Strategic Goal	**Performance Measure**	**Performance Results**	
		FY 2004	**FY 2003 ***
Define and Develop Transformational Capabilities	**Major Platform Research and Development**		
	Joint Strike Fighter	$2,091M	$1,662M
	DD(X)	$1,025M	$ 668M
	V-22	$ 367M	$ 387M

**Results derived from FY 2005 President's Budget.*

Marines, assigned to 3rd Battalion, 3rd Marine Regiment, approach a landing zone for extraction.

INSTITUTIONAL RISK

Strategic Goal 1: Streamline Decision Processes, Drive Financial Management and Acquisition Excellence

This strategic goal distills the business transformation initiative underway in DoD. DON remains committed to business transformation, as exemplified by its information technology initiative, the Navy Marine Corps Intranet (NMCI), and its financial management initiative, the Enterprise Resource Planning system pilots. The table below presents FY 2003 and FY 2004 comparative data for the number of NMCI seats cutover, and the reduction of applications from implementation of the Enterprise Resource Planning system pilots. The number of NMCI seats cutover (i.e., installed on a user's desk top) is cumulative. Therefore, 201,270 seats have been cutover as of FY 2004 representing increased connectivity to NMCI throughout DON. The number of applications reduced through implementation of the Enterprise Resource Planning system pilots remain unchanged in FY 2004.

Strategic Goal 2: Improve Readiness and Quality of Key Facilities

Among key facilities slated for improvement are housing units for Sailors and Marines, and their families. With an increased emphasis on public-private ventures, DON remains on track to eliminate inadequate housing by FY 2007. (See table below)

Institutional Risk

DON Strategic Goal	Performance Measure	Performance Results	
		FY 2004	FY 2003 *
Streamline Decision Processes, Drive Financial Management and Acquisition Excellence	Number of Navy Marine Corps Intranet Seats Cut Over	201,270	109,602
	Implement Enterprise Resource Planning - Number of Applications Reduced	70	70
Improve Readiness and Quality of Key Facilities	Number of Privatization Projects/Units	3,493	9,549

**Results derived from FY 2005 President's Budget.*

Management Integrity

Commanders and managers throughout the Department of the Navy (DON) must ensure the integrity of their programs and operations. Part of this responsibility entails compliance with applicable laws and regulations. Two applicable statutes include the Federal Managers' Financial Integrity Act of 1982 and the Improper Payments Information Act of 2002. Under this statute, DON must present improper payments information in the annual report, beginning with fiscal year (FY) 2004. A discussion of both statutes and their applicability to DON appears below.

Federal Managers' Financial Integrity Act of 1982

As required by implementing guidance from the Office of Management and Budget and the Department of Defense, under the Federal Managers' Financial Integrity Act of 1982, DON must evaluate its system of internal accounting and administrative controls (i.e., management controls) on an annual basis. The objective of this evaluation is to determine whether reasonable assurance exists that:

- obligations and costs are in compliance with applicable laws;
- funds, property, and other assets are safeguarded against waste, loss, unauthorized use, or misappropriation; and
- revenues and expenditures applicable to agency operations are properly recorded and accounted for to permit the preparation of reliable accounting, financial, and statistical reports and to maintain accountability over assets.

A Marine secures razor wire while setting up camp during Exercise Bearing Duel '04.

For FY 2004, DON issued a qualified statement of assurance, citing material weaknesses in management controls. Specifically, DON's system of internal accounting and administrative controls in effect during the 12-month period ending June 30, 2004, taken as a whole, provides reasonable assurance that DON can execute its mission effectively and protect its critical assets, with the exception of material weaknesses reported. The basis for reasonable assurance includes an established control environment, continued emphasis on risk assessment, specific control activities, continuous communication and flow of information, and monitoring performed by both command management and the audit/inspection community. Additionally, the effective execution of missions during recent military actions confirms the strength of DON's management controls. To view the FY 2004 statement of assurance in its entirety, see the website for the Assistant Secretary of the Navy (Financial Management and Comptroller), Office of Financial Operations (http://www.fmo.navy.mil/MCP/soa_index.htm).

Improper Payments Information Act of 2002

A component of the President's Management Agenda is the initiative to reduce improper payments. Improper payments are those which should not have been made or that were made in incorrect amounts under statutory, contractual, administrative, or other legally applicable requirements. Examples of improper payments include overpayments, underpayments, duplicate payments, and payments for services not received.

DON programs and activities susceptible to erroneous payments are those for which DON has the responsibility for entitlement computation and/or disbursement of government funds. Examples include DON Personnel Support Activities and Detachment, which are responsible for the entitlement computation for some travel payments; and DON Disbursing Officers aboard ships and at other isolated locations, which are responsible for disbursement of government funds. Note that the Defense Finance and Accounting Service provides the vast majority of DON's entitlement computation and disbursement functions.

As required by implementing guidance from the Office of Management and Budget under the Improper Payments Information Act of 2002, DON identified $700 thousand of improper payments in FY 2004. This amount is significantly less than the Office of Management and Budget threshold of $10 million. Consequently, for the programs for which DON has entitlement computation and/or disbursement responsibility, we have instituted internal controls designed to mitigate the occurrence of improper payments in future fiscal years.

Reporting Results

For financial reporting purposes, the Department of the Navy (DON) is organized into two reporting entities: DON General Fund and Navy Working Capital Fund. Each entity has its own set of financial statements and related notes (see Principal Statements and Notes in this report). In terms of assets, the General Fund accounts for 92 percent and the Navy Working Capital Fund accounts for 8 percent of DON fiscal year (FY) 2004 Total Assets. DON has been producing DON General Fund financial statements since FY 1996, and Navy Working Capital Fund financial statements since FY 1991. Below is a discussion of each entity, including FY 2004 performance.

DON General Fund

The DON General Fund supports overall Department operations. Direct appropriations from Congress comprise the DON General Fund account structure. Examples of DON General Fund appropriation types are:

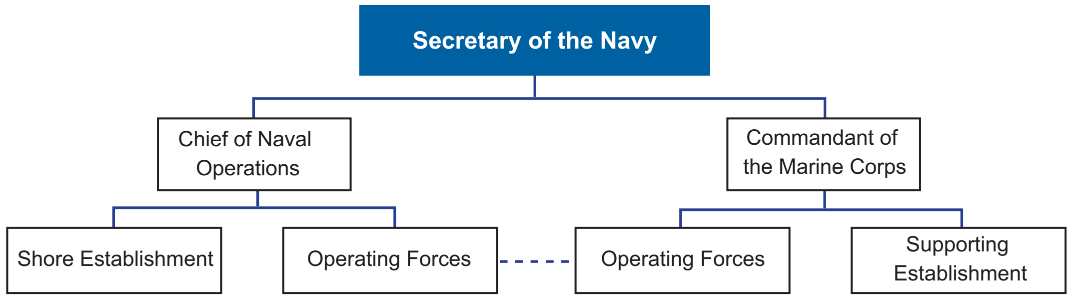
- Military Personnel;
- Operation and Maintenance;
- Procurement;
- Research, Development, Test and Evaluation;
- Military Construction; and
- Family Housing.

For a complete list of DON General Fund appropriations, see "General Fund Other Accompanying Information" in this report.

Major Commands

DON is comprised a joint warfighting team: U.S. Navy and U.S. Marine Corps. Both services have numerous major commands that operate under the authority and responsibility of a Commander or other designated official who has similar authority and responsibility. Each major command has a defined mission that supports the overall DON mission and generally supports a network of subordinate commands.

For purposes of our discussion, Navy major commands can be grouped into three categories: Secretariat, Shore Establishment, and Operating Forces. The Shore Establishment and Operating Forces operate under the purview of the Chief of Naval Operations. Similarly, the Supporting Establishment and Operating Forces of the Marine Corps organization operate under the purview of the Commandant of the Marine Corps. See organization chart on page 28. (To view the DON organization in its entirety, see the respective Navy and Marine Corps websites (http://www.navy.mil and http://www.usmc.mil).)



Due to the breadth of the DON organization and space limitations of this report, we have included representative examples of Navy major commands below. Included with these examples are the mission and end strength of each Navy major command. Mission and end strength of the Marine Corps follow in the next section, "Marine Corps Organization."

SECRETARIAT

Assistant for Administration to the Under Secretary of the Navy

Mission: To provide timely and responsive management and customer services to the Secretariat, staff offices, field activities, and supported organizations in order to enable them to effectively execute goals.

FY 2004 End Strength:
Military personnel: 990
Civilian personnel: 4,255

Office of Naval Research

(Office of Naval Research operates under the Chief of Naval Research, Assistant Secretary of the Navy (Research, Development, and Acquisition).)

Mission: To coordinate, execute, and promote science and technology programs of the U.S. Navy and Marine Corps through schools, universities, government laboratories, and nonprofit and for-profit organizations; to provide technical advice to the Chief of Naval Operations and the Secretary of the Navy; and work with industry to improve technology manufacturing processes.

FY 2004 End Strength:
Military personnel: 18
Civilian personnel: 2,937

Operating Forces

Commander, U.S. Fleet Forces

(Commander, U.S. Fleet Forces has dual responsibility as Commander, U.S. Atlantic Fleet.)

Mission: To fully organize, train, maintain, equip, and man active and reserve naval forces in support of the Unified Command Plan; develop and articulate authoritative Fleet-coordinated readiness and warfighting requirements; establish and implement Fleet-coordinated and integrated standards and policies for Fleet units; execute assigned readiness and personnel accounts to develop required levels of Fleet readiness; and explore transformational concepts.

FY 2004 End Strength:
Military personnel: 126,621
Civilian personnel: 7,085

Commander, U.S. Pacific Fleet

Mission: To support the U.S. Pacific Command's theater strategy, and to provide interoperable, trained and combat-ready naval forces to the U.S. Pacific Command and other U.S. Unified Commanders.

FY 2004 End Strength:
Military personnel: 106,925
Civilian personnel: 18,597

Commander, U.S. Naval Forces Europe

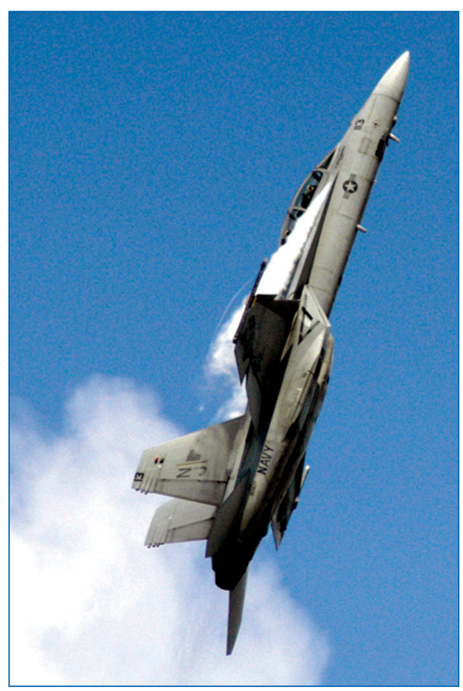
Mission: To execute missions assigned by Commander U.S. European Command, and perform U.S. Navy functions assigned by the Chief of Naval Operations; maintain and employ ready forces to conduct the full range of military operations unilaterally or in concert with coalition partners; enhance trans-Atlantic security through support of the North Atlantic Treaty Organization; promote regional stability; counter terrorism; and enhance U.S. interests in the European theater.

FY 2004 End Strength:
Military personnel: 1,924
Civilian personnel: 171

Commander, Naval Reserve Force

Mission: To provide mission-capable units and individuals to the Navy-Marine Corps Team throughout the full range of operations from peace to war.

FY 2004 End Strength:
Military personnel: 8,878
Civilian personnel: 487



A U.S. Navy F/A-18F Super Hornet, performs at Air Show on Andrews Air Force Base, Clinton, MD.

SHORE ESTABLISHMENT

Commander, Navy Installations

Mission: To enable and enhance Navy combat power by providing the most effective and efficient shore services and support.

FY 2004 End Strength:
Military personnel: 25,522
Civilian personnel: 26,171

Naval Sea Systems Command

Mission: To keep America's Navy #1 in the world by providing the Navy operationally superior and affordable ships, systems, and ordnance throughout their lifecycle…for today, tomorrow, and the Navy after next.

FY 2004 End Strength:
Military personnel: 2,063
Civilian personnel: 36,125

Naval Air Systems Command

Mission: To provide sustainment (current readiness), systems acquisition (future readiness), decision support; and to make the Navy more capable, ready, and affordable in a joint environment.

FY 2004 End Strength:
Military personnel: 2,669
Civilian personnel: 24,718

Space and Naval Warfare Systems Command

Mission: To provide the warfighter with knowledge superiority by developing, delivering, and maintaining effective, capable and integrated command, control, communications, computer, intelligence and surveillance systems.

FY 2004 End Strength:
Military personnel: 484
Civilian personnel: 7,188

Naval Facilities Engineering Command

Mission: To manage the planning, design, construction, contingency engineering, real estate, environmental, and public works support for U. S. Navy shore facilities around the world; to provide the Navy's forces with the operating, expeditionary, support and training bases they need.

FY 2004 End Strength:
Military personnel: 633
Civilian personnel:13,930

Naval Supply Systems Command

Mission: To provide Navy, Marine Corps, Joint and Allied Forces quality supplies and services on a timely basis with "One Touch Supply."

FY 2004 End Strength:
Military personnel: 446
Civilian personnel: 7,661

Strategic Systems Programs

Mission: To serve our nation by providing credible and affordable sea-based deterrent missile systems.

FY 2004 End Strength:
Military personnel: 457
Civilian personnel: 774

Bureau of Medicine and Surgery

Mission: To provide a comprehensive healthcare delivery system of shore-based treatment facilities and operating forces of the Navy and Marine Corps; and ensure the provision of medical and dental care and services for Navy and Marine Corps personnel, other uniformed services personnel, and eligible beneficiaries authorized by law or regulation.

FY 2004 End Strength:
Military personnel: 31,272
Civilian personnel: 11,402

Navy Personnel Command

Mission: To support the needs of the Navy by providing the Fleet with the right person in the right place at the right time; to satisfy our Sailors' personal goals and improve their quality of life by providing them with meaningful and rewarding career opportunities; to promote and retain the best; and to ensure fair and equitable treatment of all hands, by all hands, at all times.

FY 2004 End Strength:
Military personnel: 10,047
Civilian personnel: 1,466

Naval Education and Training Command

Mission: To educate and train those who serve, providing the tools and opportunities which enable life-long learning, professional and personal growth and development, ensuring fleet readiness and mission accomplishment; to perform such other functions and tasks assigned by higher authority; and to serve as the sole command for individual training and education, and as the Principal Advisor to the Chief of Naval Operations and the Commander, U.S. Fleet Forces Command on training and education related matters.

FY 2004 End Strength:
Military personnel: 16,457
Civilian personnel: 4,287

Naval Security Group Command

Mission: To exploit, defend and attack information for our naval forces and nation.

FY 2004 End Strength:
Military personnel: 6,979
Civilian personnel: 514

Office of Naval Intelligence

Mission: To provide national-level maritime intelligence support to our customers including the joint warfighters, the Department of the Navy, national decision-makers, joint operational commanders, shore-based and theater tactical elements of the Navy and Marine Corps, and foreign partners; to support the acquisition process through scientific and technical analysis of naval weapons systems; and to support nontraditional maritime intelligence missions.

FY 2004 End Strength:
Military personnel: 948
Civilian personnel: 1,194

Field Support Activity

(Field Support Activity provides direct support to the Chief of Naval Operations.)

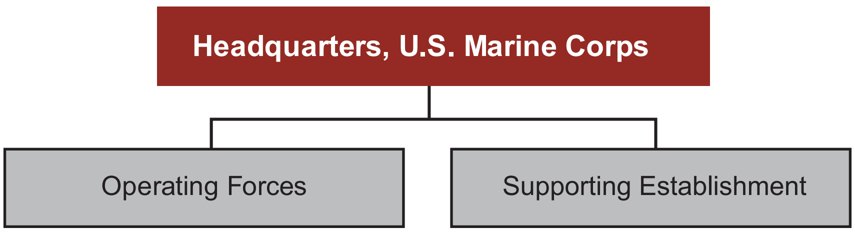
Mission: To initiate action in matters pertaining to the provision of funds, manpower, and facilities to assigned unified commands, Navy headquarters and activities; and to evaluate the utilization of such resources and initiate or recommend appropriate corrective action.

FY 2004 End Strength:
Military personnel: 11,145
Civilian personnel: 2,923

Marine Corps Organization

Mission: To provide Fleet Marine Forces with combined arms capabilities, including integrated aviation and logistical elements, for service as part of a naval expeditionary force.

FY 2004 End Strength:
Military personnel: 177,480
Civilian personnel: 17,028



Airman signals a CH-53D Sea Stallion preparing to land aboard the amphibious assault ship USS TARAWA (LHA 1),, which was one of many U.S. ships participating in exercise Rim of the Pacific (RIMPAC) 2004.

FY 2004 OVERVIEW OF PERFORMANCE

Implementation of the DON Financial Improvement Plan and the Under Secretary of Defense (Comptroller) (USD(C)) Financial Improvement Initiative has driven progress in the area of the DON General Fund. Highlights of our progress in FY 2004 include:

- Completion of assertion process for the Investments line item on the DON General Fund Consolidated Balance Sheet;
- Issuance of Accounts Receivable guidance related to the timely collection of delinquent receivables;
- Development of Accounts Payable Workshops to facilitate implementation of Command-level Accounts Payable strategy; and
- Initiation of actions to produce and distribute consolidated DON General Fund trial balances for each DON Major Command, including Marine Corps.

Our financial performance relative to the FY 2004 DON General Fund Consolidated Balance Sheet and Combined Statement of Budgetary Resources appears below.

Asset Composition

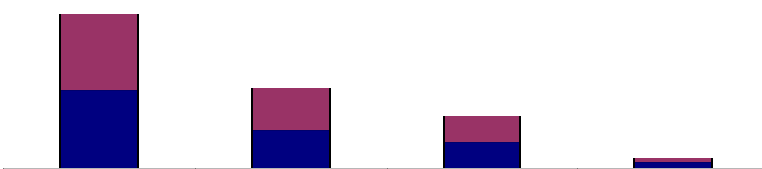
In FY 2004, Total Assets decreased by two percent. The overall decrease in Total Assets is primarily attributed to Intragovernmental Accounts Receivable. Specifically, DON reported a decrease of $246,160 thousand (or, 50 percent) in Intragovernmental Accounts Receivables in FY 2004 when compared to FY 2003. This decrease is a result of implementing the Under Secretary of Defense (Comptroller) memo of June 20, 2003, that directed the military departments to establish a goal to close out or collect all over-aged receivables by December 31, 2003. In addition, the trading partner/elimination process with other Federal agencies and DoD organizations contributed to this decrease. Similarly, DON reported a 14 percent decrease in Non-Federal Accounts Receivable. The majority of this decrease is attributed to decreases within the Operation and Maintenance, Navy and Military Personnel, Navy appropriations. (See DON General Fund Notes to the Principal Statements, Note 5, for more information.)

Other significant changes in line items comprising Total Assets are as follows:

<u>Other Assets</u>. DON reported a 45 percent increase in Intragovernmental Other Assets, and a 19 percent decrease in Non-Federal Other Assets in FY 2004. The increase in the intragovernmental balance is attributed to the trading partner/elimination process. The decrease in the non-federal balance is attributed to outstanding contract financing payments within the Aircraft Procurement Program. (See DON General Fund Notes to the Principal Statements, Note 6, for more information.)

Cash and Other Monetary Assets. DON reported a 17 percent decrease in this line item for FY 2004. This decrease is a result of the draw down related to Operation Iraqi Freedom and subsequent events. (See DON General Fund Notes to the Principal Statements, Note 7, for more information.)

Asset Composition: FY 2003 v. FY 2004
($ in Thousands)



	General PP&E	Fund Balance	Inventory*	Other**
FY 2004	$151,679,503	$81,874,818	$53,340,667	$8,888,157
FY 2003	$158,407,450	$78,191,653	$53,611,634	$10,540,281

**includes operating materials and supplies, held for use*
***comprised of investments, accounts receivable, other assets, and cash and other monetary assets*

Accounts Receivable Metric

As part of the Under Secretary of Defense (Comptroller) (USD(C)) Financial Indicators Program, DON must track the total amount of delinquent Intragovermental and Public Accounts Receivable. Accounts Receivable is deemed "delinquent" when payment has not been received within 30 days of the date specified in the initial demand letter (Department of Defense Financial Management Regulation, Volume 4, Chapter 3, paragraph 030205). The purpose of the metric is to ensure proper stewardship over public funds and cash management.

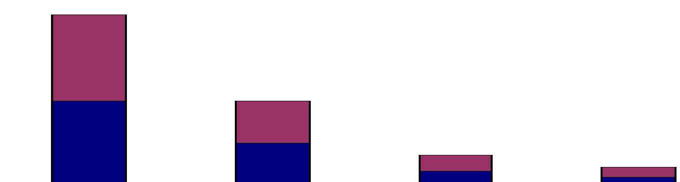
USD(C) has established a Department of Defense-wide goal of 25 percent reduction against the total amount of delinquent Intragovernmental and Public Accounts Receivable. For FY 2004, DON achieved this goal.

A U.S. Marine Corps MV-22 Osprey lands aboard the amphibious assault ship USS BATAAN (LHD 5).

Liability Composition

In FY 2004, Total Liabilities increased by three percent. The overall increase in Total Liabilities is attributed to Intragovernmental Accounts Payable. Specifically, DON reported an increase of $402,583 thousand (or, 39 percent) in FY 2004 when compared with FY 2003. The increase is the result of the varying needs and execution requirements of DON as well as the trading partner/intragovernmental elimination process. Additionally, DON reported a 20 percent decrease in Non-Federal Accounts Payable in FY 2004. This decrease is attributed to DON business process and policy changes. (See DON General Fund Notes to the Principal Statements, Note 12, for more information.)

Liability Composition: FY 2003 v. FY 2004
($ in Thousands)



	Environmental Liabilities	Other Liabilities*	Accounts Payable*	Military Retirement
FY 2004	$16,031,979	$8,005,628	$2,832,624	$1,575,815
FY 2003	$15,614,424	$7,645,875	$2,777,555	$1,589,971

**includes intragovernmental debt*

Budgetary Resources, Obligations, and Outlays

In FY 2004, DON reported the following on the DON General Fund Combined Statement of Budgetary Resources:

- $159,183 million, Total Budgetary Resources,
- $141,155 million, Total Obligations Incurred, and
- $119,193 million, Total Outlays.

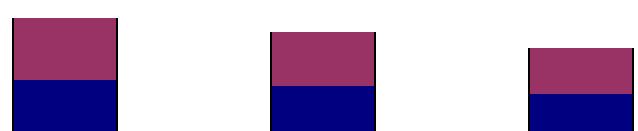
A discussion of these reported budgetary amounts appears below.

Total Budgetary Resources. A primary component of budgetary resources is budget authority (i.e., authority provided by law to enter into financial obligations that will result in immediate or future outlays involving federal government funds). In FY 2004, DON reported $124,374 million in budget authority (or 78 percent of Total Budgetary Resources). FY 2004 budget authority represents an increase (i.e., less than one percent) from FY 2003 due to continuing efforts to accomplish overall DON mission. Note that Marine Corps initiated a process improvement to capture prior year recoveries in FY 2004.

Total Obligations Incurred. Obligations incurred represent amounts of orders placed, contracts awarded, services received, and similar transactions during a given period that will require payments during the same or future period. Obligations incurred by DON in FY 2004 (i.e., $141,155 million) represent an increase of six percent from FY 2003. This increase is primarily the result of increased funding for procurement accounts.

Total Outlays. Outlays occur when a federal agency issues checks, disburses cash, or electronically transfers funds to liquidate an obligation. Outlays also occur when interest on the Treasury debt held by the public accrues; the federal government issues bonds, notes, or other cash-equivalent instruments; or a direct or guaranteed loan is disbursed. Outlays reported by DON in FY 2004 (i.e., $119,193 million) represent an increase of six percent from FY 2003. This increase is the result of increased funding for procurement and research and development accounts.

Total Budgetary Resources, Obligations Incurred, Outlays: FY 2003 v. FY 2004



	Budgetary Resources	Obligations Incurred	Outlays
FY 2004	$159,182,848	$141,154,852	$119,192,659
FY 2003	$147,273,067	$132,577,831	$112,318,319

Navy Working Capital Fund

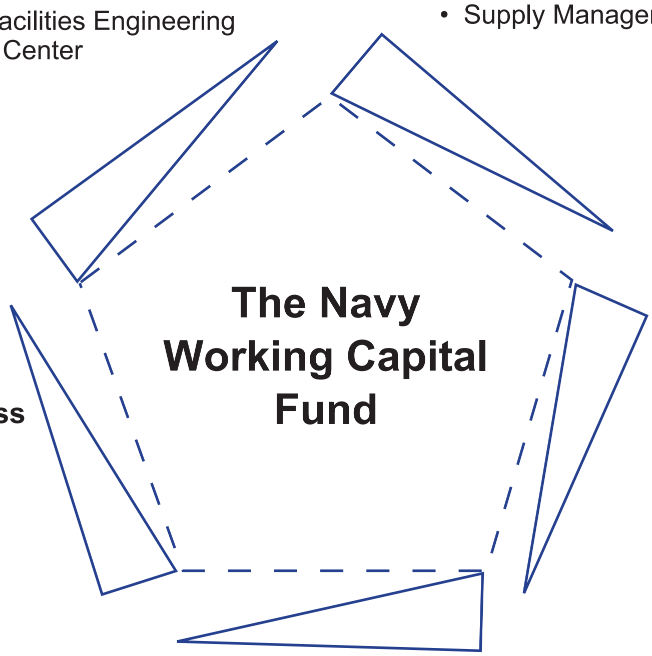
The Navy Working Capital Fund (NWCF) is a revolving fund established to meet the diverse requirements of the Navy and Marine Corps operating forces. Under the revolving fund concept, an appropriation or transfer of funds finances the initial cost of goods and services. Reimbursements from a customer's appropriated account replenish the initial working capital and permit continuing operations without further appropriation by Congress. Unlike profit-oriented businesses, the goal of the revolving fund is to break even over time.

NWCF Business Areas

Included in the NWCF are five business areas comprised of one or more activities. NWCF activities stabilize the price of goods and services in their budget to protect customers from unforeseen fluctuations. Each NWCF activity is comprised of civilian and/or military personnel and has a defined mission that supports the overall Department of the Navy mission.

Base Support Business Area
- Public Works Centers
- Naval Facilities Engineering Service Center

Supply Management Business Area
- Supply Management - Navy
- Supply Management - Marine Corps



Transportation Business Area
- Military Sealift Command

Depot Maintenance Business Area
- Naval Shipyards
- Aviation Depots
- Marine Corps Depots

Research & Development Business Area
- Naval Research Laboratory
- Naval Surface Warfare Center
- Naval Undersea Warfare Center
- Naval Air Warfare Center
- Space & Naval Warfare Systems Centers

Supply Management

The Supply Management business area consists of Navy and Marine Corps components, which operate under the purview of their respective Commands: Naval Supply Systems Command and Marine Corps Logistics Command. In FY 2004, total actual end strength (i.e., civilian and military personnel) for the Supply Management business area was 6,430. However, Supply Management-Navy anticipates end strength to change in FY 2005 and FY 2006, as a result of planned strategic sourcing efforts at the Fleet and Industrial Supply Centers, the Naval Supply Information Systems Activity, and the Naval Inventory Control Point. Similarly, Supply Management-Marine Corps expects end strength to decrease in FY 2005.

Supply Management, Navy

Mission: To provide Navy, Marine Corps, Joint and Allied Forces quality supplies and services on a timely basis with "One Touch Supply."

Supply Management, Marine Corps

Mission: To perform inventory management functions that result in sale of consumable and reparable items to support both the Department of Defense and other government agencies.

Depot Maintenance

The Depot Maintenance business area consists of Naval Shipyards, Aviation Depots, and Marine Corps Depots, all of which operate under the purview of their respective commands: Naval Sea Systems Command, Naval Air Systems Command, and Marine Corps Logistics Command. In FY 2004, total actual end strength (i.e., civilian and military personnel) for the Depot Maintenance business area was 24,558. (See chart for actual FY 2004 end strength by activity groups.)

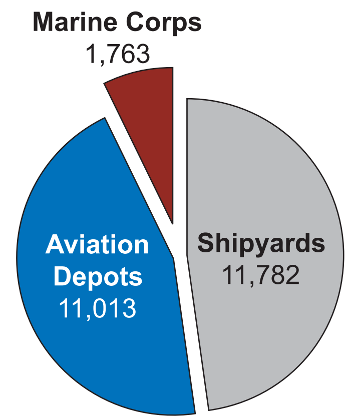
In subsequent fiscal years, the Depot Maintenance business area anticipates end strength to change. Specifically, Naval Shipyards expect evolving workload requirements and process efficiencies to affect civilian end strength and workyears. Aviation Depots expect civilian end strength and workyears to decrease based on projected use of contractor labor and workload fluctuations. In contrast, Marine Corps Depots anticipate end strength to increase in FY 2005 to accommodate additional workload for repairing combat-damaged equipment and weapons systems used in the Global War on Terrorism. However, based on projected workload for FY 2007, Marine Corps Depots expect to reduce the permanent workforce through voluntary separation incentives and to release the temporary employees hired to support unplanned workload increases in prior fiscal years.

Depot Maintenance, Shipyards

Mission: To provide logistics support for assigned ships and service craft; perform authorized work in connection with construction, overhaul, repair, alteration, drydocking and outfitting of ships and craft as assigned; perform design, manufacturing, refit and restoration, research and development and test work, and provide services and material to other activities and units as directed by competent authority.

Depot Maintenance

FY 2004 Actual End Strength by Activity Groups



Depot Maintenance, Aviation

Mission: To provide responsive worldwide maintenance, engineering, and logistics support to the Fleet and ensure a core industrial resource base essential for mobilization; repair aircraft, engines, and components, and manufacture parts and assemblies; provide engineering services in the development of hardware design changes, and furnish technical and other professional services on maintenance and logistics problems.

Depot Maintenance, Marine Corps

Mission: To provide the quality products and responsive maintenance support services required to maintain a core industrial base in support of mobilization, surge and reconstitution requirements.

Research and Development

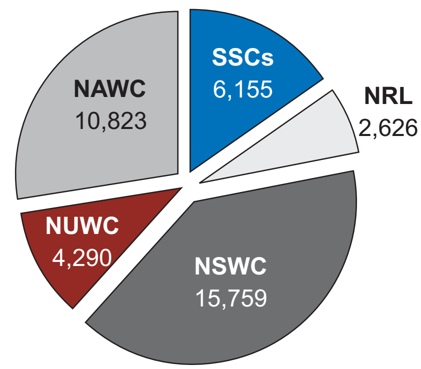
The Research and Development business area consists of the Naval Research Laboratory and four Naval Warfare Centers, all of which operate under the purview of their respective Commands. In FY 2004, total actual end strength (i.e., civilian and military personnel) for the Research and Development business area was 39,653. (See chart for actual FY 2004 end strength by activity group.) To compensate for the projected loss of retired personnel in subsequent fiscal years, the Space and Naval Warfare Systems Centers plan to continue workforce revitalization through recruitment and retention of talented C4ISR (Command, Control, Communications, Computers, Intelligence, Surveillance, and Reconnaissance) professionals.

NAVAL RESEARCH LABORATORY

Mission: To operate the Navy's full spectrum corporate laboratory, conducting a broadly based multidisciplinary program of scientific research and advanced technological development directed toward maritime applications of new and improved materials, techniques, equipment, systems and ocean, atmospheric, and space sciences and related technologies.

Research and Development

FY 2004 Actual End Strength by Activity Group



NAVAL SURFACE WARFARE CENTER

Mission: To operate the Navy's full spectrum research, development, test and evaluation, engineering and fleet support center for ship hull, mechanical, and electrical systems, surface combat systems, coastal warfare systems, and other offensive and defensive systems associated with surface warfare.

NAVAL UNDERSEA WARFARE CENTER

Mission: To operate the Navy's full spectrum research, development, test and evaluation, engineering and fleet support center for submarines, autonomous underwater systems, and offensive and defensive weapons systems associated with undersea warfare.

NAVAL AIR WARFARE CENTER

Aircraft Division

Mission: To operate the Navy's principal research, development, test and evaluation, engineering, and fleet support activity for naval aircraft engines, avionics, and aircraft support systems and ship/shore/air operations.

Weapons Division

Mission: To operate as the Navy's full spectrum research, development, test and evaluation in-service engineering center for air warfare weapons systems (except anti-submarine warfare systems), missiles and missile subsystems, aircraft weapons integration, and assigned airborne electronic warfare systems; and as the Department of the Navy's air, land, and sea test ranges.

SPACE AND NAVAL WARFARE SYSTEMS CENTERS

Mission: To operate the Navy's full spectrum research, development, test and evaluation, engineering, and fleet support centers for command, control, and communication systems and ocean surveillance and the integration of those systems that overarch multiple platforms.

Transportation

The Transportation business area is comprised of the Military Sealift Command, which has dual reporting responsibilities to DON (as a NWCF activity group), and to the U.S. Transportation Command.

Military Sealift Command

Mission: To provide ocean transportation of equipment, fuel, supplies and ammunition to sustain U.S. forces worldwide during peacetime and in war for as long as operational requirements dictate.

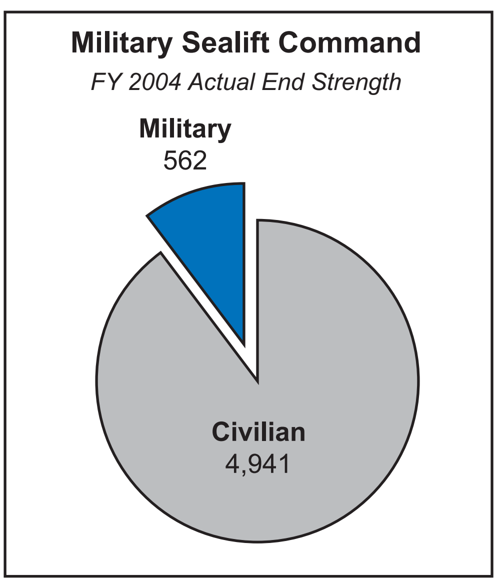
The Military Sealift Command supports three separate and distinct ship programs:

- Naval Fleet Auxiliary Force - provides fuel, food, ammunition, spare parts and other supplies, enabling the Navy fleet to operate at the highest possible operating tempo. In July 2004, Naval Fleet Auxiliary Force East merged with Military Sealift Command Atlantic and Combat Logistics Squadron Two to become the Sealift Logistics Command Atlantic.

- Special Mission Ships - provide oceanographic and hydrographic surveys, underwater surveillance, missile flight data collection and tracking, acoustic research and submarine support, and other support for Department of Defense sponsors.

- Afloat Pre-Positioning Force Ships-Navy - provide military equipment and supplies for a contingency forward deployed in key ocean areas before it is needed.

In FY 2004, total actual end strength (i.e., civilian and military personnel) for the Military Sealift Command was 5,503 (see chart). In FY 2006 and FY 2007, the Military Sealift Command expects an increase in afloat civilian/civilian mariner end strength, as a result of additional ships augmenting the Naval Fleet Auxiliary Force.



The guided missile frigate USS JOHN L. HALL (FFG 32) departs for sea in preparation for PANAMAX 2004

Base Support

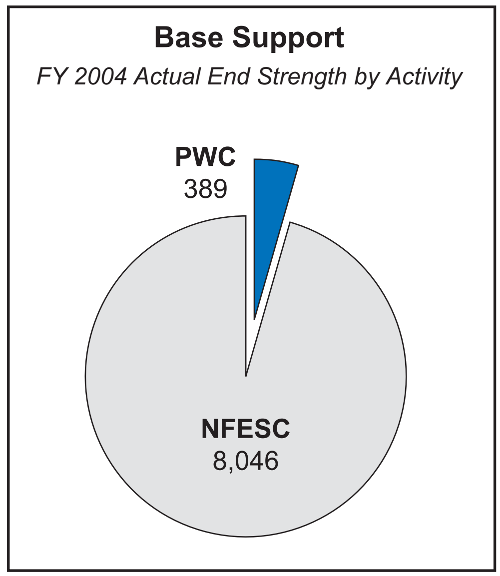
The Base Support business area consists of eight Public Works Centers and the Naval Facilities Engineering Service Center, which operate under the purview of the Naval Facilities Engineering Command. In FY 2004, Public Works Centers transferred functional support of Navy shore installations to Commander, Navy Installations, and established detachment at various Naval Surface and Naval Air Warfare Centers. Additionally, Public Works Center Pensacola became a detachment of Public Works Center Jacksonville, reducing the total number of centers from nine to eight.

Public Works Center

Mission: To provide Navy, tenant Department of Defense, and tenant federal clients with quality public works support and services, including utilities services, facilities maintenance, transportation support, engineering services, environmental services, and shore facilities planning support.

Naval Facilities Engineering Services Center

Mission: To deliver quality products and services in Energy and Utilities, Amphibious and Expeditionary Systems, Environment, Shore, Ocean, and Waterfront Facilities.



In FY 2004, total actual end strength (i.e., civilian and military personnel) for the Base Support business area was 8,435. (See chart for actual FY 2004 end strength by activity.) Public Works Centers anticipate a decrease in civilian end strength and workyears in subsequent fiscal years due to reorganizations, outsourcing, and workload reductions.

The conventional aircraft carrier USS KITTY HAWK (CV 63) combat systems department conducts a Close-In Weapons System (CIWS) pre-action calibration on CIWS Mount 24.

FY 2004 OVERVIEW OF PERFORMANCE

Implementation of the DON Financial Improvement Plan and the Under Secretary of Defense (Comptroller) (USD(C)) Financial Improvement Initiative has begun in the NWCF area. Specifically, the Assistant Secretary of the Navy (Financial Management and Comptroller) plans to initiate the assertion process for NWCF Personal Property, Accounts Receivable, and Debt in the first quarter, FY 2005.

PROGRAM PERFORMANCE

Supply Management

Supply Management, Navy. Since 1998, Supply Management, Navy has used average customer wait time to improve customer support. FY 2004 goals for average customer wait time for aviation and maritime supplies were 7.5 days and 18.8 days, respectively. As of June 30, 2004, Supply Management, Navy remained on track to achieve their fiscal year-end goals: the actual average customer wait time for aviation and maritime supplies was 7.9 days and 19.9 days, respectively.

Supply Management, Marine Corps. The availability of spare parts is an essential performance metric to warfighting customers. Accordingly, the Supply Management business area establishes goals and continuously monitors results so that corrective actions can be taken, when necessary, to maximize performance outputs. In FY 2004, Supply Management, Marine Corps established a goal of 85 percent for supply chain channel performance.

Depot Maintenance

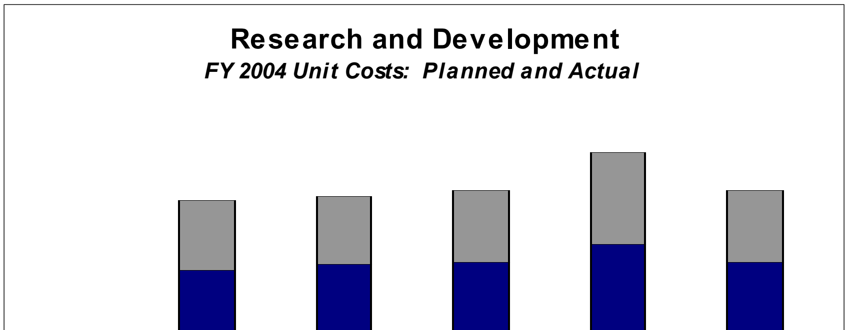
Depot Maintenance, Shipyards. The shipyards remain committed to productivity improvement. One measure of productivity is the direct labor indicator, expressed in part as a percentage of total direct labor man hours and overhead. In FY 2004, shipyards exceeded their direct labor goal of 67.9 percent, reporting an actual result of 68.2 percent of total direct and overhead hours.

Depot Maintenance, Aviation. Aviation depots, such as NAVAIR Depot Jacksonville, continue to focus on business efficiencies. In the third quarter of FY 2004, NAVAIR Depot Jacksonville produced 11,156 components, reducing component physical work-in-process by 21 percent. Additionally, NAVAIR Depot Jacksonville sold F/A-18 Sequence JX40 out of PMI2 seven days ahead of schedule. This particular airframe was converted to the Blue Angel configuration.

Depot Maintenance, Marine Corps. Schedule conformance improved in FY 2004 as the workforce positioned for the workload influx associated with the Global War on Terrorism. Depot Maintenance, Marine Corps advanced toward their 100 percent goal through management initiatives aimed at increasing and improving productivity yield through continued implementation of the Theory of Constraints. Similarly, Marine Corps maintenance centers remained focused on refining and expanding implementation of the Theory of Constraints and the application of Lean Thinking to eliminate inefficiencies in shop-level procedures.

Research and Development

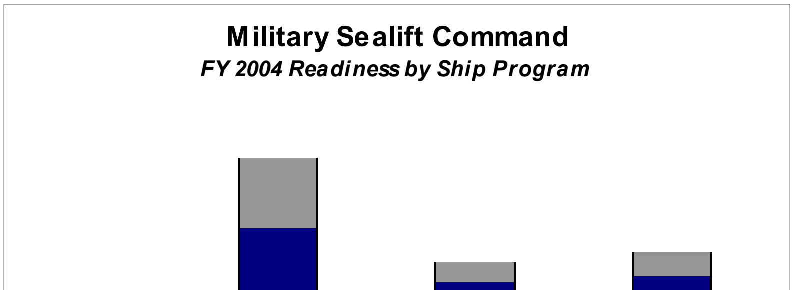
The span of Research and Development (R&D) activities' products and services is broad and diverse. The primary measure of performance for the R&D activities is cost per direct labor hour, calculated as direct labor (civilian and military labor plus overhead) divided by direct labor hours. This financial indicator measures cost effectiveness in mission performance. The chart below presents FY 2004 planned and actual cost per direct labor hour for each R&D activity.



	NAWC	NSWC	NUWC	NRL	SSC
Actual	$80.51	$79.39	$82.39	$106.02	$83.79
Planned	$74.73	$80.49	$83.67	$103.65	$83.60

Transportation

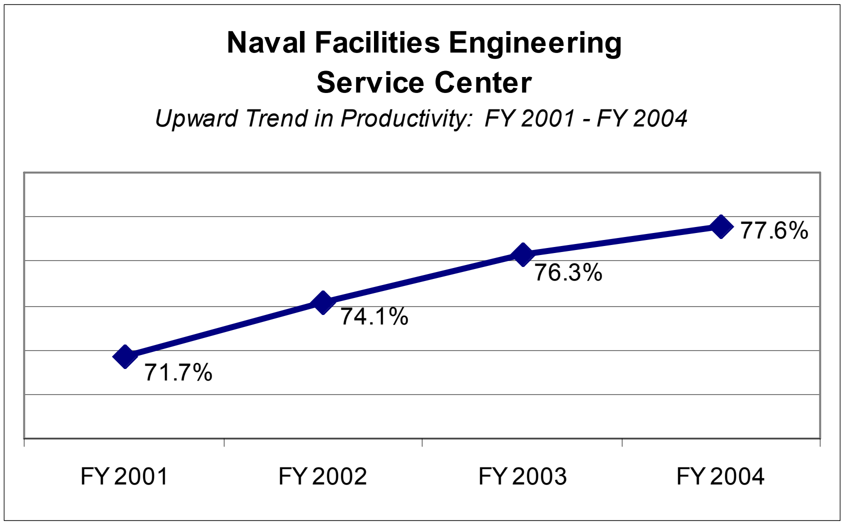
To ensure mobility of combat-ready naval forces, it is critical that the Military Sealift Command meet its readiness goals. The Military Sealift Command bases readiness on "goal days," calculated as the number of days ships are available to perform a mission multiplied by the number of ships in the program. In FY 2004, the Military Sealift Command exceeded 100 percent readiness in the Afloat Pre-positioning Force Ships-Navy (APF- N) Program (see chart). This achievement is attributed primarily to the activation of the USNS CAPE JOHN (T-AK 5022) and USNS CAPE GIBSON (T-AK 5051) Ready Reserve Force ships during the first quarter of FY 2004. In the Special Mission Ships (SMS) Program, the Military Sealift Command achieved 99.8 percent readiness due in part to an unplanned deactivation of the USNS CAPABLE (T-AGOS 16) in September 2004. In their Naval Fleet Auxiliary Force (NFAF) Program, the Military Sealift Command achieved 96.7 percent readiness, reflecting the workload decrease for Harbor Tugs operating in Norfolk and San Diego and the delayed activation of the USNS BRIDGE (T-AOE 10).



	NFAF: 96.7%	APF-N: 101.6%	SMS: 99.8%
Actual Days	23,126	6,322	8,032
Goal Days	23,912	6,222	8,052

Base Support

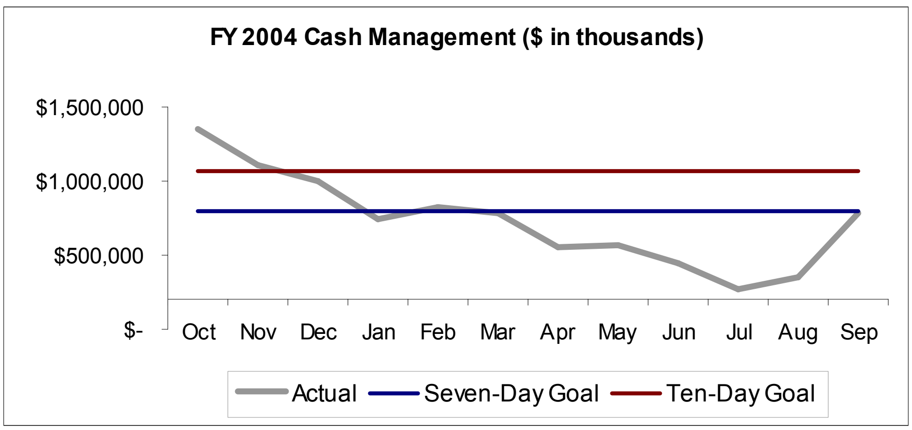
As their workload increases, and manual processes are automated, Naval Facilities Engineering Services Center continues an upward trend in productivity in FY 2004 (see chart).



FINANCIAL PERFORMANCE

Cash Management

Working Capital Fund cash is managed at the Departmental level. The Department of Defense Financial Management Regulation requires Working Capital Fund cash levels be maintained at seven to ten days of operational costs, and be sufficient to meet six months of capital outlays. For FY 2004, the seven-day cash requirement was $792 million and the ten-day requirement was $1,063 million (see chart below). Based on the relatively large beginning balance of $1,827 million, DON structured its FY 2004 budget with a disbursement of $448 million from NWCF cash to the Operation and Maintenance, Navy appropriation. Early in the fiscal year, Congress and the Office of the Secretary of Defense authorized additional transfers of $88 million. These transfers, along with anticipated outlays in the Supply Management Business Area, resulted in a projected year-end balance of $901 million. During FY 2004, actual cash levels tracked closely with the projected plan except for an unanticipated transfer of $200 million directed by the Department of Defense in June 2004 to help finance the Global War on Terrorism. This last transfer is the primary reason the actual cash balance finished approximately $223 million below the projected level of $901 million.



Net Cost of Operations

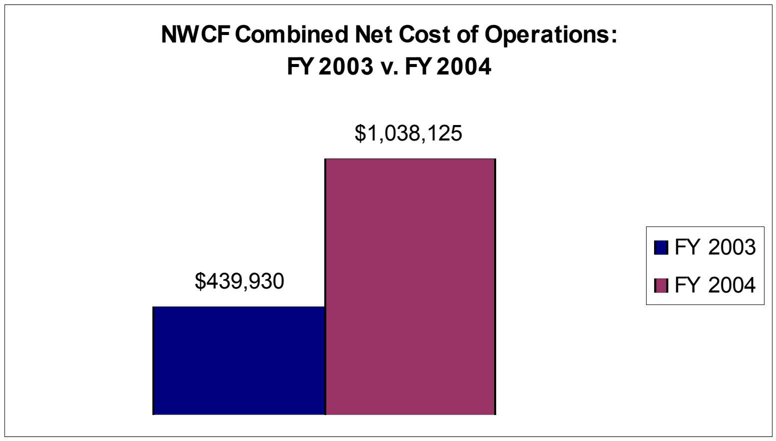
The NWCF Consolidating Statement of Net Cost present earned revenue and program costs by business area. The total net cost presented is calculated as the sum of:

- Intragovernmental Net Costs (i.e., intragovernmental gross costs less intragovernmental earned revenue), and

- Net Costs With the Public (i.e., gross costs with the public less revenue with the public).

NWCF net cost of operations is based on the combined total net cost for the business areas, or "Total Net Program Costs," after adjustments for any costs not assigned to programs or earned revenue not attributable to programs. In FY 2003 and FY 2004, there were no adjustments required for costs not assigned to programs and earned revenue.

In FY 2004, the combined total net cost for the NWCF business areas - Supply Management, Depot Maintenance, Research and Development, Transportation, Base Support - NWCF ordnance and component level was $1,038,125 thousand.



Note: Totals above also include net cost of operations for NWCF ordnance and component level.

The Nimitz-class aircraft carrier USS JOHN C. STENNIS (CVN 74).

Net Cost of Operations By NWCF Business Area

NWCF Business Area	FY 2004 $ (000)	FY 2003 $ (000)
Supply Management		
Program Costs	$ 6,870,512	$ 8,456,945
Less: Earned Revenue	6,106,967	6,895,749
Net Cost of Operations	**$ 763,545**	**$ 1,561,196**
Depot Maintenance		
Program Costs	$ 1,942,893	$ 5,192,971
Less: Earned Revenue	4,788,820	5,346,593
Net Cost of Operations	**$ (2,845,927)**	**$ (153,622)**
Research and Development		
Program Costs	$ 10,296,517	$ 9,573,205
Less: Earned Revenue	10,259,846	9,585,868
Net Cost of Operations	**$ 36,671**	**$ (12,663)**
Transportation		
Program Costs	$ 1,777,196	$ 1,789,147
Less: Earned Revenue	1,792,429	1,844,089
Net Cost of Operations	**$ (15,233)**	**$ (54,942)**
Base Support		
Program Costs	$ 1,581,392	$ 1,569,729
Less: Earned Revenue	1,602,991	1,584,722
Net Cost of Operations	**$ (21,599)**	**$ (14,993)**

An F-18C Hornet from Fighter Attack Squadron Three Seven

Conclusion

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).

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. These statements are in addition to the financial reports used to monitor and control budgetary resources which are prepared from the same books and records.

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 U.S. Government, a sovereign entity. One implication of this is that the liabilities cannot be liquidated without legislation that provides resources to do so.

USNS CAMDEN (T-AOE 2) prepares to receive USS NIMITZ (CVN 68) alongside for a replenishment at sea.

Sailors man the rails aboard the Navy's newest and most advanced Arleigh Burke-class guided missile destroyer USS CHUNG-HOON (DDG 93).

Department of the Navy

General Fund Principal Statements

Principal Statements

The FY 2004 Department of the Navy, General Fund Principal Financial Statements and related notes are presented in the format prescribed by the Department of Defense Financial Management Regulation 7000.14, Volume 6B. The statements and related notes summarize financial information for individual funds and accounts within the General Fund for the fiscal year ending September 30, 2004, and are presented on a comparative basis with information previously reported for the fiscal year ending September 30, 2003.

The following statements are included in the Department of the Navy, General Fund Principal Statements:

- Consolidated Balance Sheet
- Consolidated Statement of Net Cost
- Consolidated Statement of Changes in Net Position
- Combined Statement of Budgetary Resources
- Combined Statement of Financing

The Principal Statements and related notes have been prepared to report financial position pursuant to the requirements of the Chief Financial Officers Act of 1990, as amended by the Government Management Reform Act of 1994.

The accompanying notes should be considered an integral part of the Principal Statements.

Department of Defense
Department of the Navy
CONSOLIDATED BALANCE SHEET
As of September 30, 2004 and 2003
($ in thousands)

		2004 Consolidated		2003 Consolidated Restated
ASSETS (Note 2)				
Intragovernmental:				
Fund Balance with Treasury (Note 3)				
Entity	$	81,874,818	$	78,191,653
Non-Entity Seized Iraqi Cash		0		0
Non-Entity - Other		219,095		223,225
Investments (Note 4)		9,457		9,801
Accounts Receivable (Note 5)		250,703		496,863
Other Assets (Note 6)		272,723		187,865
Total Intragovernmental Assets	$	82,626,796	$	79,109,407
Cash and Other Monetary Assets (Note 7)	$	234,865	$	282,995
Accounts Receivable (Note 5)		2,895,966		3,382,133
Loans Receivable (Note 8)		0		0
Inventory and Related Property (Note 9)		53,340,667		53,611,634
General Property, Plant and Equipment (Note 10)		151,679,503		158,407,450
Investments (Note 4)		0		0
Other Assets (Note 6)		5,000,348		6,180,624
TOTAL ASSETS	$	295,778,145	$	300,974,243
LIABILITIES (Note 11)				
Intragovernmental:				
Accounts Payable (Note 12)	$	1,437,616	$	1,035,033
Debt (Note 13)		0		0
Environmental Liabilities (Note 14)		0		0
Other Liabilities (Note 15 & Note 16)		3,984,802		3,859,913
Total Intragovernmental Liabilities	$	5,422,418	$	4,894,946
Accounts Payable (Note 12)	$	1,395,008	$	1,742,522
Military Retirement Benefits and Other Employment-Related Actuarial Liabilities (Note 17)		1,575,815		1,589,971
Environmental Liabilities (Note 14)		16,031,979		15,614,424
Loan Guarantee Liability (Note 8)		0		0
Other Liabilities (Note 15 and Note 16)		4,020,826		3,785,962
Debt Held by Public (Note 13)		0		0
TOTAL LIABILITIES	$	28,446,046	$	27,627,825
NET POSITION				
Unexpended Appropriations (Note 18)	$	79,161,774	$	76,694,928
Cumulative Results of Operations		188,170,325		196,651,490
TOTAL NET POSITION	$	267,332,099	$	273,346,418
TOTAL LIABILITIES AND NET POSITION	$	295,778,145	$	300,974,243

The accompanying notes are an integral part of these statements.

Department of Defense
Department of the Navy
CONSOLIDATED STATEMENT OF NET COST
For the years ended September 30, 2004 and 2003
($ in thousands)

	2004 Consolidated	2003 Consolidated
Program Costs		
Intragovernmental Gross Costs	$ 39,171,720	$ 35,142,574
(Less: Intragovernmental Earned Revenue)	(3,272,860)	(3,186,968)
Intragovernmental Net Costs	$ 35,898,860	$ 31,955,606
Gross Costs With the Public	$ 96,846,251	$ 81,168,783
(Less: Earned Revenue From the Public)	(3,302,708)	(1,919,696)
Net Costs With the Public	$ 93,543,543	$ 79,249,087
Total Net Cost	$ 129,442,403	$ 111,204,693
Costs Not Assigned to Programs	0	0
(Less: Earned Revenue Not Attributable to Programs)	0	0
Net Cost of Operations	$ 129,442,403	$ 111,204,693

The accompanying notes are an integral part of these statements.

Department of Defense
Department of the Navy
CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION
For the years ended September 30, 2004 and 2003
($ in thousands)

	2004 Consolidated	2003 Consolidated Restated
Cumulative Results of Operations		
Beginning Balances	$ 222,565,239	$ 44,169,672
Prior period adjustments (+/-)		
Prior Period Adjustments - Restated (+/-)	(25,913,750)	0
Beginning Balance, Restated	$ 196,651,489	$ 44,169,672
Prior Period Adjustments - Not Restated (+/-)	0	152,557,286
Beginning Balances, as adjusted	$ 196,651,489	$ 196,726,958
Budgetary Financing Sources:		
Appropriations Received	$ 0	$ 0
Appropriations transferred in/out (+/-)	0	0
Other adjustments (rescissions, etc) (+/-)	0	0
Appropriations used	120,198,147	110,567,740
Nonexchange revenue	0	0
Donations and forfeitures of cash and cash equivalents	0	0
Transfers in/out without reimbursement (+/-)	166,000	0
Other budgetary financing sources (+/-)	0	0
Other Financing Sources:		
Donations and forfeitures of property	0	0
Transfers in/out without reimbursement (+/-)	11,883	51,765
Imputed financing from costs absorbed by others	585,209	509,719
Other (+/-)	0	0
Total Financing Sources	$ 120,961,239	$ 111,129,224
Net Cost of Operations (+/-)	$ 129,442,403	$ 111,204,693
Ending Balances	$ 188,170,325	$ 196,651,489

The accompanying notes are an integral part of these statements.

Department of Defense
Department of the Navy
CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION
For the years ended September 30, 2004 and 2003
($ in thousands)

		2004 Consolidated		2003 Consolidated Restated
Unexpended Appropriations				
Beginning Balances	$	50,781,179	$	64,774,328
Prior period adjustments (+/-)				
Prior Period Adjustments - Restated (+/-)		25,913,750		0
Beginning Balance, Restated	$	76,694,929	$	64,774,328
Prior Period Adjustments - Not Restated (+/-)		0		0
Beginning Balances, as adjusted	$	76,694,929	$	64,774,328
Budgetary Financing Sources:				
Appropriations Received	$	123,917,983	$	122,132,688
Appropriations transferred in/out (+/-)		455,059		1,810,288
Other adjustments (rescissions, etc) (+/-)		(1,708,050)		(1,454,635)
Appropriations used		(120,198,147)		(110,567,740)
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	$	2,466,845	$	11,920,601
Net Cost of Operations (+/-)	$	0	$	0
Ending Balances	$	79,161,774	$	76,694,929

The accompanying notes are an integral part of these statements.

Department of Defense
Department of the Navy
COMBINED STATEMENT OF BUDGETARY RESOURCES
For the years ended September 30, 2004 and 2003
($ in thousands)

	2004 Combined Budgetary Financing Accounts	2003 Combined Budgetary Financing Accounts
BUDGETARY RESOURCES		
Budget Authority:		
Appropriations Received	$ 123,948,477	$ 122,169,428
Borrowing Authority	0	0
Contract Authority	0	739
Net transfers (+/-)	425,109	1,662,142
Other	0	0
Unobligated Balance:		
Beginning of period	14,695,238	11,908,983
Net transfers, actual (+/-)	195,950	145,546
Anticipated Transfers Balances	0	0
Spending Authority from Offsetting Collections:		
Earned	0	0
Collected	7,706,650	6,792,556
Receivable from Federal sources	(360,284)	(1,211,532)
Change in unfilled customer orders	0	0
Advances received	56,010	(59,842)
Without advance from Federal sources	467,506	308,282
Anticipated for the rest of year, without advances	0	0
Transfers from trust funds	0	0
Subtotal	$ 7,869,882	$ 5,829,464
Recoveries of prior year obligations	$ 13,756,981	$ 7,009,339
Temporarily not available pursuant to Public Law	0	0
Permanently not available	(1,708,789)	(1,452,574)
Total Budgetary Resources	$ 159,182,848	$ 147,273,067
STATUS OF BUDGETARY RESOURCES		
Obligations Incurred:		
Direct	$ 132,268,522	$ 124,497,950
Reimbursable	8,886,330	8,079,881
Subtotal	$ 141,154,852	$ 132,577,831
Unobligated balance:		
Apportioned	$ 13,973,108	$ 13,697,001
Exempt from apportionment	0	0
Other available	0	0
Unobligated Balances Not Available	4,054,888	998,235
Total, Status of Budgetary Resources	$ 159,182,848	$ 147,273,067

The accompanying notes are an integral part of these statements.

Department of Defense
Department of the Navy
COMBINED STATEMENT OF BUDGETARY RESOURCES
For the years ended September 30, 2004 and 2003
($ in thousands)

	2004 Combined Budgetary Financing Accounts	2003 Combined Budgetary Financing Accounts
RELATIONSHIP OF OBLIGATIONS TO OUTLAYS:		
Obligated Balance, Net-beginning of period	$ 63,520,894	$ 56,100,186
Obligated Balance transferred, net (+/-)	0	0
Obligated Balance, net-end of period:		
Accounts Receivable	(537,560)	(897,842)
Unfilled customer order from Federal sources	(2,802,982)	(2,335,476)
Undelivered Orders	63,723,755	63,419,000
Accounts Payable	3,473,010	3,335,213
Outlays:		
Disbursements	126,955,319	119,051,033
Collections	(7,762,660)	(6,732,714)
Subtotal	$ 119,192,659	$ 112,318,319
Less: Offsetting receipts	(115,027)	(246,802)
Net Outlays	$ 119,077,632	$ 112,071,517

The accompanying notes are an integral part of these statements.

Department of Defense
Department of the Navy
COMBINED STATEMENT OF FINANCING
For the years ended September 30, 2004 and 2003
($ in thousands)

	2004 Combined	2003 Combined
Resources Used to Finance Activities:		
Budgetary Resources Obligated		
Obligations Incurred	$ 141,154,852	$ 132,577,831
Less: Spending Authority from offsetting collections and recoveries (-)	(21,626,865)	(12,838,803)
Obligations net of offsetting collections and recoveries	$ 119,527,987	$ 119,739,028
Less: Offsetting receipts (-)	(115,027)	(246,802)
Net obligations	$ 119,412,960	$ 119,492,226
Other Resources		
Donations and forfeitures of property	0	0
Transfers in/out without reimbursement (+/-)	11,883	51,765
Imputed financing from costs absorbed by others	585,209	509,719
Other (+/-)	0	0
Net other resources used to finance activities	$ 597,092	$ 561,484
Total resources used to finance activities	$ 120,010,052	$ 120,053,710
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 (-)	$ 1,796,210	$ (3,213,420)
Unfilled Customer Orders	523,516	248,440
Resources that fund expenses recognized in prior periods	(115,122)	(31,284)
Budgetary offsetting collections and receipts that do not affect Net Cost of Operations	0	0
Resources that finance the acquisition of assets	(12,412,218)	(26,444,222)
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 budget (-)	0	0
Other (+/-)	(11,883)	0
Total resources used to finance items not part of the Net Cost of Operations	$ (10,219,497)	$ (29,440,486)
Total resources used to finance the Net Cost of Operations	$ 109,790,555	$ 90,613,224

The accompanying notes are an integral part of these statements.

Department of Defense
Department of the Navy
COMBINED STATEMENT OF FINANCING
For the years ended September 30, 2004 and 2003
($ in thousands)

	2004 Combined	2003 Combined
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 Periods:		
Increase in annual leave liability	$ 188,260	$ 0
Increase in environmental and disposal liability	427,489	0
Upward/Downward reestimates of credit subsidy expense	0	0
Increase in exchange revenue receivable from the public (-)	0	0
Other (+/-)	193,243	428,344
Total components of Net Cost of Operations that will require or generate resources in future periods	$ 808,992	$ 428,344
Components not Requiring or Generating Resources:		
Depreciation and amortization	$ 17,475,862	$ 16,936,476
Revaluation of assets and liabilities (+/-)	1,114,040	3,203,729
Other (+/-)		
Trust Fund Exchange Revenue	(30,297)	0
Cost of Goods Sold	0	0
Operating Material & Supplies Used	270,967	0
Other	12,284	22,920
Total components of Net Cost of Operations that will not require or generate resources	$ 18,842,856	$ 20,163,125
Total components of Net Cost of Operations that will not require or generate resources in the current period	$ 19,651,848	$ 20,591,469
Net Cost of Operations	$ 129,442,403	$ 111,204,693

The accompanying notes are an integral part of these statements.

Department of the Navy

General Fund Notes to the Principal Statements

Note 1. Significant Accounting Policies

1.A. Basis of Presentation

These financial statements have been prepared to report the financial position and results of operations of the Department of the Navy (DON), 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 DON in accordance with the "Department of Defense Financial Management Regulation" (DoD FMR), the 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 DON is responsible; except that information relative to classified assets, programs, and operations has been excluded from the statement or otherwise aggregated and reported in such a manner that it is no longer classified. In addition to the DON financial statements, and pursuant to OMB directives, financial reports are also prepared by the DON that are used to monitor and control the DON's use of budgetary resources.

The DON is unable to fully implement all elements of Federal GAAP and the OMB Bulletin No. 01-09 due to limitations of its financial management processes and systems, including feeder systems and processes. Reported values and information for the DON's major asset and liability categories are derived largely from feeder systems, such as inventory systems and logistic 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 DON cannot currently implement every aspect of Federal GAAP and OMB Bulletin No. 01-09. The DON continues to implement process and system improvements addressing the limitation of its financial and feeder systems. A more detailed explanation of these financial statement elements is provided in the applicable note.

Fiscal Year (FY) 2004 represents the ninth year that the DON has prepared audited financial statements as required by the CFO Act and the GMRA.

1.B. Mission of the Reporting Entity

The DON was created on April 30 1798 by an act of Congress (I Stat. 533; 5 U.S.C. 411-12). The overall mission of DoD, as stated in the FY 2002 Annual Defense Report, is to assure allies and friends, dissuade future military competition, deter threats and coercion against U.S. interests, and defeating adversaries if deterrence fails.

1.C. Appropriations and Funds

The DON's appropriations and funds are divided into the general, 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 DON's missions.

<u>General funds</u> are used for financial transactions arising under Congressional appropriations, including personnel, operation and maintenance, research and development, procurement, and construction accounts.

<u>Revolving funds</u> 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 National Defense Sealift Fund is the DON's only revolving fund.

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 the DON is acting as an agent or a custodian or whose distribution awaits legal determination, or (2) account for unidentified remittances.

The asset accounts used to prepare the statements are categorized as either entity or 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.

Entity Accounts:

General Funds

17X0380	Coastal Defense Augmentation, Navy
17 0703	Family Housing Construction, Navy and Marine Corps
17 0735	Family Housing, Navy and Maine Corps (Operations and Maintenance)
17X0810	Environmental Restoration, Navy
17 1105	Military Personnel, Marine Corps
17 1106	Operation and Maintenance, Marine Corps
17 1107	Operation and Maintenance, Marine Corps Reserve
17 1108	Reserve Personnel, Marine Corps
17 1109	Procurement, Marine Corps
17 1205	Military Construction, Navy
17 1235	Military Construction, Naval Reserve
17X1236	Payments to Kaho Olawe Island Conveyance, Remediation, and Environmental Restoration Fund, Navy
17 1319	Research, Development, Test, and Evaluation, Navy
17 1405	Reserve Personnel, Navy
17 1453	Military Personnel, Navy
17 1506	Aircraft Procurement, Navy
17 1507	Weapons Procurement, Navy
17 1508	Procurement of Ammunition, Navy and Marine Corps
17 1611	Shipbuilding and Conversion, Navy
17 1804	Operation and Maintenance, Navy
17 1806	Operation and Maintenance, Navy Reserve
17 1810	Other Procurement, Navy

Revolving Funds

17 4557	National Defense Sealift Fund, Navy

Trust Funds

17X8716	Department of the Navy General Gift Fund
17X8723	Ship Stores Profits, Navy
17X8733	United States Naval Academy Gift and Museum Fund

Special Funds

17X5095	Wildlife Conservation, Military Reservations, Navy
17X5185	Kaho Olawe Island Conveyance, Remediation, and Environmental Restoration Fund, Navy
17X5429	Rossmoor Liquidating Trust Settlement Account

Non Entity Accounts:

17 3XXX	Receipt Accounts
17X6XXX	Deposit Funds

1.D. Basis of Accounting

The DON generally records transactions on a budgetary basis and not an accrual accounting basis as is required by Federal GAAP. For FY 2004, DON's financial management systems are unable to meet all of the requirements for full accrual accounting. Many of the DON's financial and 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. The DON has undertaken efforts to determine the actions required to bring its financial and 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 United States Government Standard General Ledger (USSGL). Until such time as all of the DON's financial and feeder systems and processes are updated to collect and report financial information as required by Federal GAAP, the DON's financial data will be based on budgetary transactions (obligations, disbursements, and collections), and transactions from feeder systems, adjusted for known accruals of major items such as payroll expenses, accounts payable, and environmental liabilities. However, when possible, the financial statements are presented on the accrual basis of accounting as required. One example of information presented on the budgetary basis is the data on the Statement on Net Cost. Much of this information is based on obligations and disbursements and may not always represent accrued costs.

In addition, the DON identifies programs based upon the major appropriation groups provided by Congress. The DON is in the process of reviewing available data and attempting to develop a cost reporting methodology that balances the need for cost information required by the Statement of Federal Financial Accounting Standard (SFFAS) No. 4, "Managerial Cost Accounting Concepts and Standards for the Federal Government," with the need to keep the financial statements from being overly voluminous.

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 DON 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 DON does not include non-monetary support provided by U.S. Allies for common defense in 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 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 in port. DoD is reviewing these types of financing and costs 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 generally accepted accounting principles. 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, DON policy requires the recognition of operating expenses in the period incurred. However, because the DON's financial and 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 DON's 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 the net position. Certain expenses, such as annual and military leave earned but not taken, are financed in the period in which payment is made.

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

1.G. Accounting for Intragovernmental Activities

The DON, 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 DON as though the agency was a stand-alone entity.

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

Financing for the construction of DoD facilities is obtained through 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.

The DON'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 DON 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). The DON 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.

DoD reports the assets, funded actuarial liability, and unfunded actuarial liability for the military personnel in the Military Retirement Fund (MRF) financial statements. DoD 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 components or activities within the DON must be eliminated. However, the DON, as well as the majority of the federal government, cannot consistently and accurately identify all intragovernmental transactions by customer. The Defense Finance and

Accounting Services (DFAS) is responsible for eliminating transactions between components or activities of the DON. For FYs 1999 and beyond seller entities within 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 Department of the Treasury, Financial Management Services (FMS) is responsible for eliminating transactions between the Department and other federal agencies. In September 2004, the FMS issued the "Federal Intragovernmental Transactions Accounting Policies Guide." The Department 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 DON, 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 (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 provisions of the "Arms Export Control Act of 1976." Under the provisions of this Act, DoD has authority to sell defense articles and services to foreign countries and international organizations, generally at no profit or loss to the U.S. Government. Customers may be required to make payments in advance.

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

The DON'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 U. S. Army Corps 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 DON's recorded balance in the FBWT accounts and Treasury's FBWT accounts sometimes result and are subsequently reconciled. Material disclosures are provided at Note 3.

1.J. Foreign Currency

The DON conducts a significant portion of its operations overseas. The Congress established a special account to handle the gains and losses from foreign currency transactions for five general fund appropriations (Operations and Maintenance, Military Personnel, Military Construction, Family Housing Operations and Maintenance, and Family Housing Construction.) The gains and losses are computed as the variance between the exchange rate current at the date of payment and a budget rate established at the beginning of each fiscal year. Foreign currency fluctuations related to other appropriations require 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

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 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 National Defense Property, Plant, and Equipment) also includes items, which will now be classified as Operating Materials and Supplies (OM&S).

The DON uses the Latest Acquisition Cost method as its inventory systems were designed for material management rather than accounting purposes. The systems provide accountability for and visibility over inventory items. The systems do not maintain the historical cost data necessary to comply with the SFFAS No. 3, "Accounting for Inventory Related Property." Neither can they directly produce financial transactions using the USSGL, as required by the Federal Financial Management Improvement Act of 1996 (P.L. 104-208). DoD is transitioning to a Moving Average Cost methodology for valuing inventory and OM&S that when fully implemented will allow the DON 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 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 DoD holds material based on military need and support for contingencies. Therefore, the DON does not attempt to account separately for items held for current or future use.

Related property includes OM&S and stockpile materials. The OM&S, including munitions not held for sale, are valued at standard purchase price. The DoD uses the consumption method of accounting for OM&S, for the most part, expensing material when it is issued to the end user. Where current systems cannot fully support the consumption method, the DON uses the purchase method - that is, expended when purchased. The DON 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.

DoD implemented new policy in FY 2002 to account for condemned material (only) as "Excess, Obsolete, and Unserviceable." The net value of condemned material is zero, because the costs of disposal are greater than the potential scrap value. Material that can be potentially redistributed, presented in previous years as "Excess, Obsolete, and Unserviceable," is included in the "Held for Use" or "Held for Repair" categories according to its condition.

In addition, past audit results identified uncertainties about the completeness and existence of quantities used to produce the reported values. Material disclosure related to inventory and related property is provided at Note 9.

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

For the Trust Funds, investments in U.S. Treasury securities are reported at cost, net of unamortized premiums or discounts. Premium or discounts are amortized into interest income over the term of the investment using the effective interest rate method or other methods if similar results are obtained. The DON's intent is to hold investments to maturity; unless they are needed to finance claims or otherwise sustain operations. Consequently, a provision is not made for unrealized gains or losses on these securities.

The DON invests in non-marketable securities. The two types of non-marketable securities are par value and market based Intragovernmental securities. The Bureau of Public Debt issues non-marketable Par Value Intragovernmental Securities. Non-marketable, Market Based Intragovernmental Securities mimic marketable securities, but are not traded publicly. See Note 4 for material disclosures.

1.O. General Property, Plant and 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 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.

General PP&E, exclusive of Military Equipment, is 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 and Military Equipment, is depreciated on a straight-line basis. Land is not depreciated.

When it is in the best interest of the government, the DON provides government property to contractors when deemed necessary to complete contracted work. Such property is either owned or leased by the DON, 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 DON'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 DON currently reports only government property in the possession of contractors that is maintained in the DON'S property systems.

To bring the DoD into fuller compliance with federal accounting standards, 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 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 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) the DON records the applicable asset and liability if the value equals or exceeds the current DoD capitalization threshold. The DON 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 assets fair value. The DON 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 DON 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

DON 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 DON provides financing payments for certain contracts. One type of financing payment that the DON 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-Progress 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 (FAR), the DON makes financing payments under fixed price contracts that are not based on a percentage of completion. The DON reports these financing payments as advances or prepayments in the “Other Assets” line item. The DON treats these payments as advances or prepayment because the DON 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 DON is not obligated to reimburse the contractor for its costs and the contractor is liable to repay the DON for the full amount of the advance.

DoD has completed a review of all applicable federal accounting standards; applicable public laws on contract financing; FAR 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. 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. The DON’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 DON's assets. This type of liability has two components-- nonenvironmental and environmental. Recognition of an anticipated environmental disposal liability begins when the asset is placed into service, consistent with SFFAS No. 6, "Accounting for Property, Plant, and Equipment." Based upon the DON's policies and consistent with SFFAS No.5 "Accounting for Liabilities of Federal Government," a nonenvironmental disposal liability is recognized for an asset when management makes a decision to dispose of the asset. The Department has agreed to the recognition of nonenvironmental disposal liability for nuclear powered assets when the asset is placed in service. Such amounts are developed in conjunction with and not easily identifiable separately from environmental disposal costs. Material disclosures are provided at Notes 14 and 15.

1.T. Accrued Leave

Civilian annual leave and military leave that has 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. Unexpended appropriations also represent amounts obligated for which legal liabilities for payments have not yet 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

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 the Department. 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 10 percent between FY 2003 and FY 2004 are explained within the Notes to the Financial Statements.

1.X. Unexpended Obligations

The DON 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 and services not yet delivered.

1.Y. Problem Disbursements

Disclosures Related to Problem Disbursements, In-transit Disbursements

As of September 30,	2002	2003	2004	(Decrease)/Increase from 2003 to 2004
(Amounts in thousands)				
1. Total Problem Disbursements				
A. Absolute Unmatched Disbursements	$ 352,000	$ 144,000	$ 183,570	$ 39,570
B. Negative Unliquidated Obligations	41,000	42,000	32,110	(9,890)
2. Total In-transit Disbursements, Net	$ 51,551	$ (11,621)	$ (23,714)	$ (12,093)

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 posted in an accounting system.

UMDs, NULOs, and In-transit Disbursements, Net represent disbursements of DON funds that have been reported by a disbursing station to the Department of the Treasury but have not yet been precisely matched against the specific source obligation giving rise to the disbursements. For the most part, these payments have been made using available funds and are based on valid receiving reports for goods and services delivered under valid contracts.

The elimination of both Problem Disbursements and In-transits is one of the highest financial management priorities of the OUSD(C). Problem Disbursements and In-transits represent a significant financial management concern since: (1) accuracy of accounting reports is affected; (2) availability of funds is more difficult to determine; and (3) the required research and resolution process becomes much more labor intensive as the age of the problem disbursements increase. As a result, the DON has efforts underway to improve the systems and to resolve all previous problem disbursements and process all in-transit disbursements.

1.Z. Data Collection Approach

The DON financial statements include information from both financial systems and feeder systems. The Defense Finance Accounting Service, Cleveland (DFAS-CL) and Kansas City (DFAS-KC) collect the financial system information and incorporate it into the financial statements. The DON collects financial information from feeder systems through a data call process and submits it to DFAS-CL & KC for incorporation into the financial statements. For FY 2004, the DON utilized a web-based data collection instrument (DCI) that captures all required financial information from feeder systems for the General Fund (GF) statements. This is the sixth year DON has used the DCI to collect information from feeder systems. The DON DCI identifies the information requirements to the source provider, provides an audit trail, and integrates into the financial statement preparation process.

NOTE 2. NON-ENTITY ASSETS

As of September 30,		2004		2003
(Amounts in thousands)				
1. Intragovernmental Assets:				
A. Fund Balance with Treasury	$	219,095	$	223,225
B. Investments		0		0
C. Accounts Receivable		0		0
D. Other Assets		0		0
E. Total Intragovernmental Assets	$	219,095	$	223,225
2. Non-Federal Assets:				
A. Cash and Other Monetary Assets	$	234,865	$	282,995
B. Accounts Receivable		2,755,331		2,642,167
C. Loans Receivable		0		0
D. Inventory & Related Property		0		0
E. General Property, Plant and Equipment		0		0
F. Investments		0		0
G. Other Assets		0		0
H. Total Non-Federal Assets	$	2,990,196	$	2,925,162
3. Total Non-Entity Assets	$	3,209,291	$	3,148,387
4. Total Entity Assets	$	292,568,854	$	297,825,856
5. Total Assets	$	295,778,145	$	300,974,243

6. Other Information Related to Non-Entity and Entity Assets:

Fluctuation and/or Abnormalities

Non-Entity Assets.

The DON reported a decrease of $ 48,130 thousand, 17 percent, in Cash and Other Monetary Assets in FY 2004 when compared with FY 2003. The Disbursing Officers had more cash on hand in FY 2003 because of Operation Iraqi Freedom and subsequent events. In addition, the ATM at Sea and Navy Cash programs have contributed to the decrease of Cash and Monetary Assets.

Explanation of fluctuations for Entity Assets is included in the note for that particular asset. See notes 3-10.

Definitions

Assets are categorized as:

Entity accounts – Resources that the DON has the authority to use, or when management is legally obligated to use funds to meet entity obligations.

Non-Entity accounts - Assets held by an entity, but are not available for use in the operations of the entity.

Other Disclosures

Non-Entity Assets. As of year-end FY 2004, DON holds $ 3,209,291 thousand Non-Entity assets. These assets are not available for use by the DON in its day-to-day operations but the DON maintains stewardship accountability and responsibility to report. There are three categories of significant non-entity assets held by the DON: (1) the Intragovernmental Fund Balance with Treasury, (2) the Nonfederal Cash and Other Monetary Assets, and (3) the Nonfederal Accounts Receivable.

Non-Entity Nonfederal Accounts Receivable (public). As of year-end FY 2004, Non-Entity Nonfederal Accounts Receivable contains $1,333,494 thousand (principal) in advance payments made to contractors and $1,128,742 thousand in associated accrued interest that remain in litigation. These balances are being reported in Non-Entity Accounts Receivable since the original appropriation year has been cancelled, and any funds collected as a result of this litigation would go to the Department of Treasury and not be available for the DON's use in normal operations. See Note 5 for additional information.

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 Loans and/or Loan Guarantee Programs
- Note 9, Inventory and Related Property, Net
- Note 10, General Property, Plant, and Equipment (PP&E), Net

For regulatory discussion on Non-Entity and Entity Assets, see Department of Defense Financial Management Regulation, Volume 6B, Chapter 10, paragraph 1004.

Note 3.A. Fund Balance with Treasury

As of September 30,	2004	2003
(Amounts in thousands)		
1. Fund Balances:		
A. Appropriated Funds	$ 79,826,096	$ 76,290,090
B. Revolving Funds	2,024,355	1,779,963
C. Trust Funds	18,245	18,877
D. Other Fund Types	225,217	325,947
E. Total Fund Balances	$ 82,093,913	$ 78,414,877
2. Fund Balances Per Treasury Versus Agency:		
A. Fund Balance per Treasury	$ 83,080,322	$ 78,414,877
B. Fund Balance per DON	82,093,913	78,414,877
3. Reconciling Amount	$ 986,409	$ 0

4. Explanation of Reconciliation Amount:

(Amounts in thousands)

Receipt accounts unavailable to DON	$	48,315
Invalid program years		455
Cancelling years		937,639
Total Reconciling Amount	$	986,409

Fund Balance Per Treasury Calculation

(Amounts in thousands)

Undisbursed Appropriation Account Trial Balance (FMS 6654)	$	83,005,320
Receipt Account Trial Balance (FMS 6655 - IAS 613)		123,925
Less: 6655 Trust Funds Balances included in 6654		(30,343)
Less: 6655 Special Funds Balances included in 6654		(18,580)
Fund Balance Per Treasury	$	83,080,322

The Financial Management Services (FMS) 6653, which is the Undisbursed Appropriation Account Ledger, includes the current month's transactions and cumulative balances for any appropriation that had financial activity during the month. FMS 6653 is systematically interfaced with the Standard Accounting and Reporting System (STARS) for posting expenditure transactions. FMS 6654, which is the Undisbursed Appropriation Account Trial Balance, includes any activity and the cumulative balances for all appropriations regardless of whether they had activity for the month. Since the FMS 6654 is all-inclusive, this report is used to calculate FBWT. FMS 6655 is the Receipt Account Trial Balance.

5. Other Information Related to Fund Balance with Treasury:

Fluctuation and/or Abnormalities

Fund Balance with the Treasury is the total of entity accounts that the DON has the authority to use and non-entity accounts that are held by the DON but are not available for use in operations. The DON reported an increase of $3,679,036 thousand, 5 percent, in FY 2004 when compared with FY 2003.

The only DON Revolving Fund is the National Defense Sealift Fund, Navy. The increase of $244,392 thousand, 14 percent, in FY 2004 when compared with FY 2003 is a result of increased business activity for movement of goods and services over the sea-lanes.

Other Fund Types (Line 1.D), DON reported a decrease of $100,730 thousand, 31 percent, in FY 2004 when compared with FY 2003. The majority of the decrease is the result of the cancelled transactions in the suspense accounts as described below.

Other Disclosures

To deal with reconciliation of check issue discrepancies and deposit differences that are aged 90 days or greater the following actions are being taken: (1) follow-up action with disbursing officers on the status of their resolving transactions listed on their statement of differences; (2) weekly teleconferences with the field sites and site visits; and (3) improving training.

Deposits.
Deposit Statements of Difference result when the deposit amount reported by the Disbursing Office on its monthly Statement of Accountability submission to the Department of the Treasury does not equal the amount of deposit information reported by the banking network to the Department of the Treasury for the monthly period.

Intragovernmental Payments and Collections.
The Intragovernmental Payment and Collections (IPAC) Statements of Difference result when the amount reported by the Disbursing Office on its monthly Statement of Accountability report to the Department of the Treasury does not equal the amount of the details reported through the Treasury's IPAC system which is one of the major components of the Government On-Line Accounting Link System II (GOALS II). The IPAC application's primary purpose is to provide a standardized interagency fund transfer mechanism for Federal Program Agencies (FPAs). IPAC facilitates the intragovernmental transfer of funds, with descriptive data from one FPA to another.

Reference

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

For regulatory discussion on Fund Balance with Treasury, see Department of Defense Financial Management Regulation, Volume 6B, Chapter 10, paragraph 100501.

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

As of September 30,	2002	2003	2004	(Decrease)/ Increase from FY 2003 to 2004
(Amount in thousands)				
Account				
F3875	$ (112,731)	$ (262,678)	$ (253,211)	$ 9,467
F3880	(2,510)	(3,631)	2,453	6,084
F3882	(23,965)	(4,172)	(37,698)	(33,526)
F3885	(445,921)	(412,370)	(133,156)	279,214
F3886	(622)	(2)	9	11
Total	$ (585,749)	$ (682,853)	$ (421,603)	$ 261,250

Other Information Related to Suspense/Budget Clearing Accounts:
The DON, in conjunction with DFAS, has made a concerted effort to reduce balances in the suspense and budget clearing accounts that are disclosed in this note. However, the balances fluctuate during the year based on current activity. Additionally, the DON is establishing policies and procedures to ensure accurate and consistent use of these accounts. On September 30th of each fiscal year, all of the un-cleared suspense/budget clearing account balances are reduced to zero (as required by the Department of Treasury and DoD FMR Volume 3 Chapter 11 guidance) by transferring the balances to the predominate appropriation accounts. On October 1st of the following year, the un-cleared suspense/clearing account balances are reestablished.

The suspense accounts F3875/3885/3886 temporarily hold collections or disbursements until they can be assigned or identified to the proper appropriation. Each suspense account represents a specific source of transactions, i.e. Disbursing Officer's (DO) suspense (F3875), Interfund/IPAC (F3885), and Payroll (TSP) (F3886) suspense.

Clearance of Treasury Account Transactions.

Public Law 107-314, HR4546, Section 1009, "Clearance of Certain Transactions Recorded in Treasury Suspense Accounts and Resolution of Certain Check Issuance Discrepancies" issued December 2, 2002 allows for the cancellation of certain transactions. In order for transactions to qualify for cancellation, there must have been efforts made to locate documentation necessary to identify the appropriation to be charged or credited. In accordance with the above legislation, the following amounts were written off from the DON suspense accounts during FY 2004:

(Amounts in thousands)

17 F 3885	$ 348,022 Net	$ 354,558 Absolute
17 F 3875	36,446 Net	225,296 Absolute
17 F 3880	9,244 Net	9,244 Absolute

Note 4. Investments

As of September 30,	2004					2003
	Cost	Amortization Method	Amortized (Premium/ Discount)	Investments, Net	Market Value Disclosure	Investments, Net
(Amounts in thousands)						
1. Intragovernmental Securities						
A. Marketable	$ 0	N/A	$ 0	$ 0	$ 0	$ 0
B. Non-Marketable, Par Value	0	N/A	0	0	0	0
C. Non-Marketable, Market-Based	9,432	N/A	(23)	9,409	9,409	9,706
D. Subtotal	$ 9,432		$ (23)	$ 9,409	$ 9,409	$ 9,706
E. Accrued Interest	48		0	48	48	95
F. Total Intragovernmental Securities	$ 9,480		$ (23)	$ 9,457	$ 9,457	$ 9,801

2. Other Investments: None

3. Other Information Related to Investments:

Fluctuation and/or Abnormalities

The DON reported a decrease of $47 thousand, 49 percent, in accrued interest in FY 2004 compared with FY 2003. This is due to the decrease in the interest rates during FY 2004. The interest rate for February, June and August 2004 was 2.125, 1.75, and 2.00 percent, respectively. The average interest rate was 2.17 percent for this period.

Other Disclosures
The two DON Trust Funds holding interest-bearing securities are the Naval Academy General Gift Fund and the Navy General Gift Fund, which have a total Investment net value of $9,457 thousand (including $48 thousand of accrued interest.) These investments are Non-Marketable Market-Based securities reported at cost, net of amortized premiums and discounts.

Reference

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

For regulatory discussion on Investments, see Department of Defense Financial Management Regulation, Volume 6B, Chapter 10, paragraph 1006.

Note 5. Accounts Receivable

As of September 30,	2004			2003
	Gross Amount Due	Allowance For Estimated Uncollectibles	Accounts Receivable, Net	Accounts Receivable, Net
(Amounts in thousands)				
1. Intragovernmental Receivables:	$ 250,703	N/A	$ 250,703	$ 496,863
2. Non-Federal Receivables (From the Public):	$ 3,203,625	$ (307,659)	$ 2,895,966	$ 3,382,133
3. Total Accounts Receivable:	$ 3,454,328	$ (307,659)	$ 3,146,669	$ 3,878,996

4. Other Information Related to Accounts Receivables:

Fluctuation and/or Abnormalities
Intragovernmental Receivables.
The DON reported a decrease of $246,160 thousand, 50 percent, in Intragovernmental Receivables in FY 2004 when compared to FY 2003. The decrease is a result of implementing the Under Secretary of Defense (Comptroller) memo of June 20, 2003, that directed the military departments to establish a goal to close out or collect all over-aged receivables by December 31, 2003. The DON established a plan of action and continues to aggressively implement the direction of the memo. In addition, the trading partner/elimination process with other Federal agencies (level one trading partner) and other organizations within DoD (level two trading partner) also contributed to the decrease of intragovernmental accounts receivable. The majority of the decrease, $91,298 thousand, is with Navy Working Capital Fund, $80,793 thousand with Other Defense Organizations General Funds, and $57,922 thousand with Other Defense Organization Working Capital Fund, and $16,430 thousand with Executive Office of the President.

Non-Federal Receivables.

The DON reported a decrease of $486,167 thousand, 14 percent, in Non-Federal Receivables in FY 2004 when compared to FY 2003. The decrease in the Entity Receivables is $599,329 thousand. The majority of the decrease is within Operation and Maintenance, Navy in the amount of $418,881 thousand and Military Personnel, Navy in the amount of $116,175 thousand. The total decrease is offset by the increase in Non-Entity Receivables in Contract Debt System (CDS)/Mechanization of Contract Administration Services (MOCAS) in the amount of $126,586 thousand.

Allowance Method

The allowance method for Nonfederal Receivables (From the Public) is determined in the following methodology: For all program groups except Military Personnel appropriations, the DON estimates for the entity accounts receivable allowance is 3 percent. The entity accounts receivable allowance for Military Personnel is estimated to be 14 percent. Each estimate is based on write-offs of accounts receivable over the last three-year period. The non-entity accounts receivable allowance was established at 50 percent excluding interest receivables pertaining to pending litigation.

Intragovernmental Accounts Receivable Adjustments

Allocation of Undistributed Collections.

Undistributed collections are allocated between federal and non-federal categories based on the percentage of federal and non-federal Accounts Receivable as submitted in the field level general ledgers. This allocation was suggested as appropriate in a DFAS Arlington memorandum dated October 4, 2000, which required disclosure to the audit community of the applicable methodology used to allocate undistributed. For FY 2004, $1,296,264 thousand in undistributed collections were allocated to accounts receivable. This amount represents a $195,741 thousand or 13% decrease from FY 2003.

Elimination Adjustments.

The DON's accounting systems do not consistently capture trading partner data at the transaction level in a manner that facilitates trading partner aggregations. Therefore, the DON was unable to reconcile intragovernmental accounts receivable balances with its trading partners. Through the ongoing Business Management Modernization Program (BMMP), the Department intends to develop long-term systems improvements that will capture the data necessary to perform reconciliations.

Intrafund transactions are eliminated based upon trading partner information obtained from the Bureau of Naval Personnel (BUPERS), Standard Accounting and Reporting System – Field Level (STARS-FL), and the Standard Accounting and Reporting System – Headquarters Module (STARS-HQ). The elimination data obtained from these systems included seller appropriation, grantor (buyer) appropriation, grantor subhead, grantor code, reimbursable source code, accounts receivable, revenue, unearned revenue, and amount collected.

Other Disclosures

Non-Federal Receivables (from the Public) includes Non-Entity Non-Federal Account Receivables and Entity Non-Federal Account Receivables.

Non-Entity Non-Federal Accounts Receivables (from the Public) includes the following:

(Amounts in thousands)	As of September 30, 2004
Contract Litigation Principal and Interest	$2,462,236
Defense Debt Management System (DDMS)	20,297
CDS/MOCAS system debts	372,582
Civilian Pay (DCPS) debt	2,940
In-service Debt & Other Debt	66,475
JAG	4,138
Penalties, Fines and Admin. Fees and Interest	119,570
Gross Non-Entity Non-Federal A/R	$3,048,238
Less Allowance	(292,908)
Nonentity Non-Federal Receivables, Net	$2,755,330
Entity Non-Federal Receivables, Net	140,636
Non-Federal Receivables (From the Public), Net	$2,895,966

The contract litigation includes principal of $1,333,494 thousand, and accrued interest receivable of $1,128,742 thousand. Interest receivable increased $52,951 thousand from FY 2003.

Other Debt represents foreign military sales and services DON has provided to the public.

Abnormal Account Balances.

Abnormal Accounts Receivable balances may occur for two primary reasons: 1) the application of undistributed collections and 2) as a result of the intragovernmental transaction elimination process. DFAS Arlington has provided guidance in a memorandum dated March 1, 2001 to record accruals, for financial statement presentation purposes, to correct abnormal balances resulting from these conditions.

In accordance with the DoD FMR, Volume 6B, Chapter 13, adjustments are recorded, at the appropriation level, to bring the DON's intragovernmental accounts receivable into agreement with its trading partners' intragovernmental accounts payable.

Reference

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

For regulatory discussion on Accounts Receivable, see Department of Defense Financial Management Regulation, Volume 6B, Chapter 10, paragraph 1007.

Note 6. Other Assets

As of September 30,	2004	2003
(Amounts in thousands)		
1. Intragovernmental Other Assets:		
A. Advances and Prepayments	$ 272,723	$ 187,865
B. Other Assets	0	0
C. Total Intra-governmental Other Assets	$ 272,723	$ 187,865
2. Non-Federal Other Assets:		
A. Outstanding Contract Financing Payments	$ 4,694,420	$ 5,809,610
B. Other Assets (With the Public)	305,928	371,014
C. Total Non-Federal Other Assets	$ 5,000,348	$ 6,180,624
3. Total Other Assets:	$ 5,273,071	$ 6,368,489

4. Other Information Related to Other Assets:

Fluctuation and/or Abnormalities

Intragovernmental Other Assets.

The DON reported an increase of $84,858 thousand, 45 percent, in Intragovernmental Other Assets, Advances and Prepayment in FY 2004 when compared with FY 2003. The balances reported are determined by the intragovernmental elimination process as submitted by DON's trading partners. In processing the elimination data, increase to Advances and Prepayments are recorded to compensate for the unresolved differences. The majority of the increase is with the following trading partners: Department of Interior $177,407 thousand; Air Force General Fund $69,510 thousand. The increase is offset by the decrease in Navy Working Capital Fund of $130,165 thousand; Other Defense Organizations Working Capital Fund of $29,842 thousand; and Air Force Working Capital Fund of $7,356 thousand.

Non-Federal Other Assets.

DON reported a decrease of $1,115,190 thousand, 19 percent, in Outstanding Contract Financing Payment in FY 2004 when compared with FY 2003. The majority of the decrease, $1,295,246 thousand, is within the Aircraft Procurement Program. New contracts within the Aircraft program are being written as performance based contracts, and this business process change has reduced the amount of outstanding contract financing payments. This decrease is offset by the increase in Weapons Procurement of $317,069 thousand. DON also reported a decrease of $65,086 thousand, 18 percent, in Other Assets (With the Public) in FY 2004 when compared with FY 2003. The decrease is a result of fewer outstanding progress payments as previously issued Marine Corps contracts are being fulfilled.

Other Disclosures

Advances and Prepayment.

The buyer-side advances to others amounts were adjusted to agree with seller-side advances from others on the books of other DoD reporting entities. Additionally, the buyer-side prepayment balances were adjusted to agree with seller-side deferred credits on the books of other DoD reporting entities.

Outstanding Contract Financing Payments.
The DON has reported outstanding financing payments for fixed price contracts as an advance and prepayment, because under the terms of the fixed price contracts, the DON 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 DON is not obligated to reimburse the contractor for its costs and the contractor is liable to repay the DON for the full amount of the outstanding contract financing payments. DoD is completing its review of all applicable federal accounting standards; applicable public laws on contract financing; FAR Parts 32,48, and 52; and the OMB guidance in 5 CFR Part 1315, “Prompt Payment.” The DON has concluded that the SFFAS No. 1, “Accounting for Selected Assets and Liabilities” does not fully or adequately addresses the subject of progress payment accounting and is considering what further action is appropriate.

The following table displays the Outstanding Contract Financing Payments attributed by program:

(Amounts in thousands)	As of September 30, 2004
Aircraft Procurement	$2,914,923
Shipbuilding and Conversion	558,521
Weapons Procurement	710,807
Other Procurement	487,214
Other (O&M, RDT&E)	22,955
Total	$4,694,420

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,	2004	2003
(Amounts in thousands)		
1. Cash	$ 232,946	$ 224,881
2. Foreign Currency (non-purchased)	1,919	58,114
3. Other Monetary Assets	0	0
4. Total Cash, Foreign Currency, & Other Monetary Assets	$ 234,865	$ 282,995

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

Fluctuation and/or Abnormalities
The DON reported a decrease of $56,195 thousand, 97 percent, in Foreign Currency in FY 2004 compared with FY 2003. This was offset by a slight increase in Cash held by Disbursing Officers of $8,065 thousand. The overall decrease in Cash and Other Monetary Assets is a result of the draw down related to Operation Iraqi Freedom and subsequent events.

Definitions
Cash - the total of cash resources under the control of the DON, 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.

Restriction on Cash - all cash and other monetary assets reported are classified as non-entity, which means that the assets are not available for the DON's use in normal operations.

Other Disclosures
Cash and Foreign Currency reported consists primarily of cash held by Disbursing Officers to carry out their payment, collection, and foreign currency accommodation exchange mission. The primary source of the amounts reported is the Standard Form 1219, Statement of Accountability reported by DoD Disbursing Officers.

The DON 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 disbursement and accommodation of exchange transactions.

Reference

See Note Disclosure 1.J. – Significant Accounting Policies for additional discussion on financial reporting requirements and DoD policies governing Foreign Currency.

For regulatory discussion on Cash and Other Monetary Assets, see Department of Defense Financial Management Regulation, Volume 6B, Chapter 10, paragraph 1009.

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

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

   Military Housing Privatization Initiative

2. Other Information:
   The Military Housing Privatization Initiative (MHPI) fosters a mutually beneficial relationship between the DoD and the private sector. For the DoD, the MHPI results in the construction of more housing built to market standards, at a lower cost than through the military construction process. Commercial construction (Private Sector) is faster and less costly than military construction and significantly stretches and leverages the DoD's limited housing funds. The MHPI also provides protection against specific risks, such as base closure or member deployment, for the private sector partner.

An analysis of loans receivables, loan guarantees, the liability for loan guarantees, and the nature and amounts of the subsidy and administrative costs associated with the direct loans and loan guarantees is provided in the following sections of this note.

DoD operates a loan guarantee program authorized by the National Defense Authorization Act for FY 1996, Public Law 104-106 Stat. 186 Section 2801, includes a series of powerful authorities that allow DoD to work with the private sector to renovate military housing. DoD's goals are to:

- Obtain private capital to leverage government dollars,
- Make efficient use of limited resources, and
- Use a variety of private sector approaches to build and renovate military housing faster and at a lower cost to American taxpayers.

The Act also provides DoD with a variety of authorities to obtain private sector financing and expertise to improve military housing. DoD uses these authorities individually, or in combination. They include:

- Guarantees, both loan and rental
- Conveyance/leasing of existing property and facilities
- Differential lease payments
- Investments, both limited partnerships and stock/bond ownership
- Direct loans

In addition, the "Federal Credit Reform Act of 1990" governs all amended direct loan obligations and loan guarantee commitments made after FY 1991 resulting in direct loans or loan guarantees.

- Direct loans - are reported net of allowance for subsidy at present value, and
- Loan Guarantee Liabilities - are reported at present value.

Reference

For regulatory discussion on Direct Loans and Loan Guarantee, see Department of Defense Financial Management Regulation, Volume 6B, Chapter 10, paragraph 1010.

Note 9. Inventory and Related Property

As of September 30,	2004	2003
(Amounts in thousands)		
1. Inventory, Net (Note 9.A.)	$ 0	$ 0
2. Operating Materials & Supplies, Net (Note 9.B.)	53,340,667	53,611,634
3. Stockpile Materials, Net (Note 9.C.)	0	0
4. Total	$ 53,340,667	$ 53,611,634

Note 9.A. Inventory, Net

Not Applicable

NOTE 9.B. OPERATING MATERIALS AND SUPPLIES, NET

As of September 30,	2004			2003	
	OM&S Gross Value	Revaluation Allowance	OM&S, Net	OM&S, Net	Valuation Method
(Amounts in thousands)					
1. OM&S Categories:					
A. Held for Use	$ 49,608,556	$ 0	$ 49,608,556	$ 49,948,473	LAC, SP, AC, O
B. Held for Repair	6,042,959	(2,310,848)	3,732,111	3,663,161	LAC, SP, AC, O
C. Excess, Obsolete, and Unserviceable	1,191,493	(1,191,493)	0	0	LAC, SP, AC, O
D. Total	$ 56,843,008	$ (3,502,341)	$ 53,340,667	$ 53,611,634	

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 on OM&S: None

3. Other Information Related to OM&S:

Fluctuation and/or Abnormalities

No fluctuation and/or abnormalities need to be explained.

Information Related to Operating Materials and Supplies, Net

General Composition of Operating Materials and Supplies (OM&S).

OM&S includes spare and repair parts, ammunition, conventional missiles, torpedoes, aircraft configuration pods, and centrally managed aircraft engines. The general composition of OM&S is as follows:

(Amounts in thousands)	September 30, 2004
Ammunition and Munitions	$32,406,277
Appropriation Purchase Account (APA) Principal End Item	8,818,403
Sponsor Owned Material	9,024,008
APA Secondary Inventory	1,127,908
Real-time Reutilization Asset Management (RRAM)	1,525,591
Other	438,480
Total	$53,340,667

Balances.

In addition to the account balances shown in Table 9.B., the Statement of Federal Financial Accounting Standards (SFFAS) No. 3 "Accounting For Inventory and Related Property" requires disclosure of the amount of OM&S held for "Future Use." This information is not captured by current OM&S systems which were designed for material management rather than accounting purposes. However, the DON estimates that $16,633,878 thousand of the OM&S Held for Use will be used more than 24 months after the end of FY 2004.

Decision Criteria For Identifying The Category To Which Operating Materials And Supplies Are Assigned.

In order to standardize reporting of the categories Held for Use, Held for Repair, and Excess, Obsolete, Unserviceable, DON implemented the Under Secretary of Defense (Comptroller) (USD(C)) condition code crosswalk as defined in the memorandum "Accounting for Excess, Unserviceable, and Obsolete Inventory and Operating Materials and Supplies" dated August 12, 2002. In addition, a September 15, 2002, USD(C) memo amended the condition code crosswalk to include code "V" in the Excess, Obsolete, Unserviceable category. OM&S was reported as follows:

OM&S Category	Condition Codes
Held for Use	A, B, C, D
Held for Repair	E, F, G, J, K, L, M, N, R
Excess,Obsolete, Unserviceable	P, H, S, V

Valuation Method for OM&S.

In July, 2001, the OUSD(C) issued a memo requiring Moving Average Cost (MAC) as the approved valuation method for Inventory Held for Sale and Operating Materials and Supplies. "Each Military Department and Defense Agency responsible for material amounts of inventory or operating materials and supplies shall implement the moving average cost valuation method as systems are renovated or replaced." The DON is participating in the DoD Business Management Modernization Program that is currently reviewing and designing the Business Enterprise Architecture (BEA). The BEA provides for a master plan that includes guidance on transition plan strategy concepts, considerations, processes, and principles. MAC will be implemented as systems are renovated or replaced. Until then, the DON continues to value OM&S using different valuation methodologies such as standard purchase price or actual cost. These valuation methodologies vary by system.

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

Generally, the value of the DON's GFM and CAM in the hands of contractors is not included in the OM&S values reported above. 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 already in other existing logistics systems.

Other Disclosures

Ammunition and Munitions.

Ammunition and Munitions are maintained and valued in the Conventional Ammunition Integrated Management System (CAIMS).

APA Principal End Items.
Principal End Items includes OM&S items such as shipboard hull, mechanical and electronic equipment, and uninstalled aircraft engines. Principal End Items are items of such importance that central inventory control is required. They normally possess one of the following characteristics: (a) essential for combat or training; (b) high dollar value; (c) difficult to procure or produce; or (d) critical basic materials or components.

Sponsor Owned Material (SOM).
SOM is defined as "programmatic material required in support of Program Manager mission requirements for production, life cycle maintenance, and installation of systems and equipment consistent with the mission charter. The material usage may involve, but is not limited to: item fabrication, assembly, testing, manufacture, development, repair, or research and development."

Real-time Reutilization Asset Management (RRAM).
Material maintained and valued in RRAM is considered excess to the owner, but may not be excess to the Navy. Standard price is used to value all stock-numbered items. Part-numbered items are valued by best available information.

Other Operating Materials & Supplies.
Other OM&S totaled $438,480 thousand as of September 30, 2004. This consists primarily of $383,310 thousand in Fleet Hospitals and War Reserves, and $38,773 thousand material in the possession of the U.S. Coast Guard.

Reference

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

For regulatory discussion on OM&S, see Department of Defense Financial Management Regulation, Volume 6B, Chapter 10, paragraph 101107.

Note 9.C. Stockpile Materials, Net
Not Applicable

Note 10. General PP&E, Net

As of September 30,	2004					2003
	Depreciation/ Amortization Method	Service Life	Acquisition Value	(Accumulated Depreciation/ Amortization)	Net Book Value	Net Book Value
(Amounts in thousands)						
1. Major Asset Classes:						
A. Land	N/A	N/A	$ 567,889	N/A	$ 567,889	$ 603,961
B. Buildings, Structures, and Facilities	S/L	20 - 40	32,912,222	$ (20,058,447)	12,853,775	21,007,724
C. Leasehold Improvements	S/L	lease term	231	(21)	210	0
D. Software	S/L	2-5 Or 10	3,071	(1,122)	1,949	423
E. General Equipment	S/L	5 Or 10	2,596,057	(2,078,308)	517,749	133,239,341
F. Military Equipment	S/L	Various	427,160,000	(293,030,000)	134,130,000	0
G. Assets Under Capital Lease [1]	S/L	lease term	432	(230)	202	146
H. Construction-in-Progress	N/A	N/A	3,607,729	N/A	3,607,729	3,555,856
I. Other			0	0	0	0
J. Total General PP&E			$ 466,847,631	$ (315,168,128)	$ 151,679,503	$ 158,407,451

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

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

2. Other Information Related to General PP&E, Net:

Fluctuation and/or Abnormalities

Building, Structures, and Facilities.

The DON reported a decrease of $8,153,949 thousand, 39 percent, in the net book value of buildings, structures, and facilities in FY 2004 when compared with FY 2003. The reason for the decrease in net book value is an increase in accumulated depreciation. While testing and changing the query methodology for the depreciation module in Internet Naval Facility Asset Database Store (iNFADS), it was discovered that the methodology was not recognizing the depreciation of capitalized improvements for those buildings, structures, and facilities whose initial cost was fully depreciated. The cost of the capitalized improvements was in the reported book value of the DON real property and was captured by the iNFADS query. Since the DON initiated the OUSD(C) policy of separately identifying and depreciating capitalized improvements in FY 1999, the depreciation for the capitalized improvements records was not captured in the query methodology. The correction was made during 1st Quarter FY 2004. The revised query methodology now recognizes the depreciation expense for those fully depreciated buildings, structures, and facilities that have capitalized improvements associated with them. Therefore, this change to the query methodology resulted in an increase in accumulated depreciation and a decrease to the net book value. Other changes associated with the new query and validation of iNFADS database records also contributed to the overall increase in accumulated depreciation. A total of $6,369,029 thousand of the accumulated depreciation contributed to the majority of the decrease in the Building, Structures, and Facilities.

Leasehold Improvements.
For FY 2004, the DON recognized $210 thousand, net, in Leasehold Improvements. This recognition is part of the DON Financial Improvement Plan. Therefore, this is a 100 percent increase in FY 2004 when compared with FY 2003.

Software.
The DON reported an increase of $1,526 thousand, 361 percent, in Software in FY 2004 when compared with FY 2003. The increase is a result of migrating DON activities to the Defense Property Accountability System (DPAS) in FY 2004. Among the assets migrated are capitalized software and therefore the increase.

General Equipment.
For FY 2003, Net Book Value of $132,660,000 thousand of Military Equipment was not reported as a separate line item, but was reported in General Equipment Line.

Excluding the Military Equipment, the DON reported a decrease of $61,592 thousand, 11 percent, in General Equipment in FY 2004 when compared with FY 2003. Among the decrease, $46,252 thousand is a result of realignment of DON activities and the transfer out and disposal of remaining equipment from these locations.

Assets Under Capital Lease.
The DON reported a increase of $56 thousand, 38 percent, in Assets Under Capital Lease in FY 2004 when compared with FY 2003. The increase is a result of migrating DON activities to Defense Property Accountability System (DPAS) in FY 2004.

Information Related to General PP&E, Net
Military Equipment.
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, establishes generally accepted accounting principles 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.

DoD has determined that it is not practicable to accumulate the information needed to value military equipment in accordance with generally accepted accounting principles. The Department is working to revise its accounting processes and systems to support the informational needs of management and compliance with generally accepted accounting principles. In the interim, the Department will base the value of military equipment for financial statement presentation purposes on data provided by the Bureau of Economic Analysis (BEA), Department of Commerce.

The data provided by BEA consist of investment and net book value data for 84 groups of equipment such as aircraft, ships and combat vehicles. The Department adjusts 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 Department of Defense budget, expenditure, and delivery data to calculate the Department’s annual investment in equipment, after recognizing any equipment transfers or war losses. BEA revised its Fiscal Year 2003 estimate. Previous BEA estimates were based, in part, on projections because source data was not available. The revised estimate for Fiscal Year 2003 is based on updated and more complete source data.

Further, the revised estimate reflects changes in the methods and data BEA uses to project 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 included in the updated estimate was new data that showed that governments purchased a smaller proportion of the domestic supply of software than had previously been estimated.

For the DON, the BEA analysis provided for an Acquisition value of $427,160,000 thousand for military equipment, less an Accumulated Depreciation value of $293,030,000 thousand giving a Net Book Value of $134,130,000 thousand for military equipment as of FY 2004.

Property in the Possession of Contractors.
The value of the DON's General PP&E real property in the possession of contractors is included in the values reported above for the Major Asset Classes of Land and Buildings, Structures, and Facilities. The value of General PP&E personal property (Major Asset Classes of Software and Equipment) does not include all of the General PP&E above the DoD capitalization threshold in the possession of contractors. The net book amount of such property is immaterial in relation to the total General PP&E net book value. Per the DoD FMR Volume 6B Chapter 10, DON is not supplementing General PP&E information with values from the Defense Contract Management Agency's CPMS (DD Form 1662) database. In accordance with an approved strategy with OMB, the GAO and the Inspector General, DoD, the DoD is developing new policies and a contractor reporting process to capture General PP&E information for future reporting purposes for compliance with Federal GAAP.

Other Disclosures
Real Property.
The Internet Naval Facility Asset Database Store (iNFADS) is used to report on real property values for financial statement reporting purposes.

Leasehold Improvements.
No leasehold improvements were reported for FY 2003, because the DON's real property system does not track leasehold improvements as a separate component of a building's total value. However, the DON is in the process of surveying commands to determine the value of leasehold improvements and began recognizing those values in FY 2004.

Software.
The DON uses the Defense Property Accountability System (DPAS) to capture costs associated with Internal Use Software.

Construction-in-Progress (CIP).
CIP balances were obtained from the Facilities Information System (FIS).

Preponderant Use.
Per the DoD FMR, Volume 4, Chapter 6, legal ownership is not always the determinant factor when establishing which DoD Component recognizes a particular General PP&E asset for accounting and reporting purposes. If the following four criteria are met, the preponderant user should report the property regardless of legal ownership or funding source:

- The asset embodies a probable future benefit;
- The DoD Component that reports the asset obtains the benefit and controls access to the benefit inherent in the asset;
- The transaction or event giving the Component the right to, and control over, the benefit has already occurred; and
- The predominantly used assets, taken as a whole, are material to the Component's financial statements.

During the course of FY 2004, the DON continued to identify properties whose preponderant users are other DoD Components. Until the Department is able to reconcile with the DoD Components the listing of properties and values, the DON will disclose in this note. Those entities utilizing material amounts of DON owned property are as follows (dollar values include both acquisition value and improvements meeting the capitalization threshold):

(Amounts in thousands)	FY 2004
Defense Commissary Agency (DeCA)	$50,412
DoD Schools	39,142
Defense Logistics Agency (DLA)	21,616

Reference

See Note Disclosure 1.O. – Significant Accounting Policies for additional discussion on financial reporting requirements and DoD policies governing General PP&E.

For regulatory discussion on General PP&E, see Department of Defense Financial Management Regulation, Volume 6B, Chapter 10, paragraph 1012.

Note 10.A. Assets Under Capital Lease

As of September 30,	2004	2003
(Amounts in thousands)		
1. Entity as Lessee, Assets Under Capital Lease:		
A. Land and Buildings	$ 0	$ 0
B. Equipment	432	206
C. Other	0	0
D. Accumulated Amortization	(230)	(60)
E. Total Capital Leases	$ 202	$ 146

2. **Description of Lease Arrangements:**
   Leased assets consist primarily of personal property reported via the DPAS system. Disclosures pertaining to future payments due are provided at Note 15.

3. **Other Information Related to Assets Under Capital Lease:**

Fluctuation and/or Abnormalities
The DON reported an increase of $56 thousand, 38 percent, in Net Equipment Leases in FY 2004 when compared with FY 2003. The increase is a result of migrating several DON activities to DPAS in FY 2004. Prior to the use of the DPAS by these activities, these individual capital leases liabilities were not reported.

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,	2004	2003
(Amounts in thousands)		
1. Intragovernmental Liabilities:		
A. Accounts Payable	$ 0	$ 0
B. Debt	0	0
C. Environmental Liabilities	0	0
D. Other	3,438,795	3,305,048
E. Total Intragovernmental Liabilities	$ 3,438,795	$ 3,305,048
2. Non-Federal Liabilities:		
A. Accounts Payable	$ 89,472	$ 0
B. Military Retirement Benefits and Other Employment-Related Actuarial Liabilities	1,575,816	1,589,971
C. Environmental Liabilities	16,031,979	15,614,424
D. Loan Guarantee Liability	0	0
E. Debt Held by the Public	0	0
F. Other Liabilities	3,478,823	3,298,340
G. Total Non-Federal Liabilities	$ 21,176,090	$ 20,502,735
3. Total Liabilities Not Covered by Budgetary Resources:	$ 24,614,885	$ 23,807,783
4. Total Liabilities Covered by Budgetary Resources:	3,831,161	3,820,042
5. Total Liabilities	$ 28,446,046	$ 27,627,825

6. Other Information Related to Liabilities Not Covered by Budgetary Resources:

Fluctuation and/or Abnormalities

Canceled years accounts payable were re-mapped from Non-Federal Other Liabilities to Non-Federal accounts payable as directed by Treasury guidance. The prior year amount was not re-mapped in the footnote at the time of completion of the statements. This resulted in an increase of $89,472 thousand, 100 percent in Accounts Payable in FY 2004 when compared with FY 2003 for this line item. However, cancelled payable actually increased by $66,234 thousand, or 285 percent in FY 2004.

An explanation of fluctuations and abnormalities for Total Liabilities Covered by Budgetary Resources is included in the specific note for that liability. See notes 12-17.

Definitions

- Liabilities Covered by Budgetary Resources are those that are incurred by the reporting entity that are covered by realized budgetary 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, and
(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 OMB without further action by the Congress or without a contingency first having to be met.

- Conversely, Liabilities Not Covered by Budgetary Resources are those liabilities which are not considered covered by realized budgetary resources as of the balance sheet date. Budgetary Authority to satisfy these liabilities is expected to be provided in a future Defense Appropriations Act. When that future budgetary authority is provided, these respective liabilities will be recorded as Covered by Budgetary Resources with an associated funded expense. To prevent overstatement on the Balance Sheet and Statement of Net Cost, the liabilities previously recorded as Not Covered by Budgetary Resources and the associated unfunded expenses are reversed.

Other Disclosures

Intragovernmental Liabilities – Other (Not covered by Budgetary Resources) (line 1.D.) includes the following:

(Amounts in thousands)	As of September 30, 2004
FECA	$565,885
Unemployment	75,204
Judgment Fund	41,833
DOD Education Trust	472
Liabilities to Treasury	2,755,401
Total	$3,438,795

Judgment Fund.

Beginning in FY 2003 and continuing into FY 2004, the DON has made substantial progress in identifying and resolving Judgment Fund liabilities. Amounts recorded in the DON General Fund Judgment Fund include those that may be applicable to the Navy Working Capital Fund. This methodology is necessary, as current Department of Justice reports do not distinguish between the two reporting entities. Reporting the Judgment Fund is in compliance with OUSD(C) guidance to resolve any outstanding debt due to the Department of Treasury. The DON is in the process of working with the appropriate Major Commands to obtain documentation that supports the amounts that have been remitted to Department of Treasury, or provide the necessary funding to liquidate the liabilities. DON is working with the Department of Treasury to validate the amounts recorded in this account. FY 2004, the DON reported $41,833 thousand as the outstanding Judgment Fund liability. Of this amount, $41,547 thousand is attributed to Navy Contract Dispute Act (CDA); $107 thousand is attributed to Marine Corps CDA; and $179 thousand for the Notification and Federal Employee Antidiscrimination and Retaliation Act (No FEAR). However, there is $66 thousand for No FEAR Act in dispute and has not been recorded.

Liability to Treasury.

Unliquidated progress payments and associated accrued interest receivables for contractor debt is reported as an unfunded liability to Department of the Treasury. Collections on this debt will be due and payable to Treasury as the appropriations are in a cancelled status. See Note 5 for further disclosure.

Nonfederal Liabilities – Other (Not covered by Budgetary Resources) (Line 2.F.) includes the following:

(Amounts in thousands)	As of September 30, 2004
Annual Leave	$2,463,860
Capital Lease Liabilities	202
Military Equipment (Non-nuclear Nonenvironmental Disposal Liabilities)	565,796
Disposal Liabilities for Excess/Obsolete Structures	343,324
Contract Incentive	105,641
Total	$3,478,823

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 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 12. ACCOUNTS PAYABLE

As of September 30,	2004			2003
	Accounts Payable	Interest, Penalties, and Administrative Fees	Total	Total
(Amounts in thousands)				
1. Intragovernmental Payables:	$ 1,437,616	N/A	$ 1,437,616	$ 1,035,033
2. Non-Federal Payables (to the Public):	1,395,008	0	1,395,008	1,742,522
3. Total	$ 2,832,624	$ 0	$ 2,832,624	$ 2,777,555

4. Other Information Related to Accounts Payable:

Fluctuation and/or Abnormalities
Intragovernmental Account Payables increased $402,583 thousand, 39 percent, in FY 2004 when compared with FY 2003. The varying needs and execution requirements of the DON generally caused fluctuations in the intragovernmental payables. Additionally, trading partner/ intragovernmental elimination process affected the intragoverenemental Accounts Payable line. In FY 2004, in concert with the greater DoD level 1 trading partner improvement effort, DON recorded the following Accounts Payable with other Federal Agencies (level 1 trading partner): General Service Administration $226,749 thousand; Department of Energy $107,944 thousand; and Homeland Security $17,766 thousand. There was also a change in Accounts Payable with some of the organizations within DoD (level 2 trading partner). There was a change within Navy Working Capital Fund in the amount of $147,738 thousand and $39,107 thousand with Other Defense Organization General Funds. The increase is offset by the decrease with Other Defense Organizations Working Capital Fund of $175,710 thousand.

DON reported a decrease of $347,514 thousand, 20 percent, in Non-Federal Accounts Payable in FY 2004 when compared with FY 2003. Among other events, the Marine Corps instituted a business process change in the Military Pay account using a new interface file that matches pay records with corresponding accounts payable records. This process change resulted in a reduction of $380,000 thousand. Among offsets, liabilities for Cancelled Accounts are now recorded as Accounts Payable rather than Other Liabilities. This change in reporting policy added $89,472 thousand to reported balances.

Definitions
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.

Non-Federal Payables (to the Public) - are payments to nonfederal government entities and individuals.

Undistributed Disbursements.

Undistributed Disbursements are the difference between disbursements recorded at the detailed level to a specific obligation or payable in the activity field records versus those reported by the Department of the Treasury via the reconciled DD 1329 and DD 1400. This should agree with the undistributed disbursements reported on monthly accounting reports (SF 133/DD 1002). Generally, timing issues between systems cause undistributed disbursements. In-transit disbursements are payments that have been made by other agencies, entities, or systems that have not yet been recorded in the DON's accounting records. For FY 2004, total undistributed disbursements were $4,396,148 thousand. This amount represents a $201,756 thousand or 5 percent increase from FY 2003.

Intragovernmental Elimination.

Regarding inter-agency purchases; DON accounting systems do not capture trading partner data at the transaction level in a manner that facilitates trading partner aggregations. Therefore, the DON was unable to fully reconcile intragovernmental accounts payable to the related intragovernmental accounts receivable, on another agencies' records that generated the payable.

Therefore, the DoD summary level seller accounts receivables were compared to the DON's accounts payable. An adjustment was posted to the DON'S accounts payable based on the comparison with the accounts receivable of the DoD Components providing goods and services to the DON.

DoD 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 after-the-fact reconciliation cannot be accomplished with existing or foreseeable resources. In the interim, DFAS is leading an effort to identify alternative means of capturing and recognizing buyer side trading partner data.

Other Disclosures

Abnormal Account Balances.

Abnormal Accounts Payable balances may occur because 1) the DON does not consistently record Accounts Payable upon receipt and acceptance of goods and services; 2) the application of undistributed disbursements; and 3) as a result of the intragovernmental transaction elimination process. Per DoD FMR Vol. 6B, Ch. 13, when an abnormal balance is created, an adjustment to Accounts Payable and Expenses should be made accordingly to recognize the shortfall.

Intragovernmental elimination adjustments are recorded at the component level, to bring the DON's intragovernmental accounts payable into agreement with its trading partners' intragovernmental accounts receivable. These elimination process adjustments may also result in abnormal accounts payable.

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

Not Applicable.

NOTE 14. ENVIRONMENTAL LIABILITIES AND DISPOSAL LIABILITIES

As of September 30,	2004			2003
	Current Liability	Noncurrent Liability	Total	Total
(Amounts in thousands)				
1. Environmental Liabilities - Non Federal				
A. Accrued Environmental Restoration (DERP funded) Costs:				
1. Active Installations--Environmental Restoration (ER)	$ 503,393	$ 2,338,069	$ 2,841,462	$ 3,132,127
2. Active Installations--ER for Closed Ranges	22,029	560,972	583,001	341,266
3. Formerly Used Defense Sites (FUDS) – ER	0	0	0	0
4. FUDS--ER for Transferred Ranges	0	0	0	0
B. Other Accrued Environmental Costs (Non-DERP funds)				
1. Active Installations--Environmental Corrective Action	0	0	0	0
2. Active Installations—Environmental Closure Requirements	0	0	0	0
3. Active Installations--Environ.Response at Active Ranges	0	0	0	0
4. Other	0	0	0	0
C. Base Realignment and Closure (BRAC)				
1. BRAC Installations--Environmental Restoration (ER)	446,732	663,920	1,110,652	1,155,946
2. BRAC Installations--ER for Transferring Ranges	5,762	50,019	55,781	15,551
3. BRAC Installations--Environmental Corrective Action	0	0	0	0
4. Other	0	0	0	0
D. Environmental Disposal for Weapons Systems Programs				
1. Nuclear Powered Aircraft Carriers	0	5,693,000	5,693,000	5,565,000
2. Nuclear Powered Submarines	42,400	5,146,300	5,188,700	4,888,900
3. Other Nuclear Powered Ships	86,500	201,000	287,500	269,100
4. Other National Defense Weapons Systems	5,790	266,093	271,883	246,534
5. Chemical Weapons Disposal Program	0	0	0	0
6. Other	0	0	0	0
2. Total Environmental Liabilities:	$ 1,112,606	$ 14,919,373	$ 16,031,979	$ 15,614,424

3. Other Information Related to Environmental Liabilities:

Fluctuation and/or Abnormalities

Accrued Environmental Restoration (DERP funded) Costs.

The DON reported a net increase of $241,735 thousand, 71 percent, for Active Installations ER for Closed Ranges in FY 2004 when compared to FY 2003. Of the total increase, $33,500 thousand is due to adding 10 new unexploded ordnance (UXO) sites at Concord and Seal Beach, CA; $76,000 thousand increase for Vieques, Puerto Rico; $19,000 thousand increase in Cost to Complete (CTC) based on findings from Preliminary Assessments; $88,000 thousand increase in CTC due to addition of Munitions Response Program support and adjustment for inflation; $30,000 thousand increase for CTC for Site Investigation at Marine Corps sites; and $5,500 thousand for program growth. The program increases were offset by $12,097 thousand for cleanup efforts.

Base Realignment and Closure (BRAC).
The DON reported an increase of $40,230 thousand, 259 percent, in FY 2004 when compared to FY 2003. Of the increase, $36,300 thousand is due to the sites moving from ER program to ER for Transferring Ranges.

Environmental Disposal for Weapon Systems.
Other National Defense Weapons Systems – The DON reported an overall increase of $25,349 thousand, 10 percent, in FY 2004 when compared to FY 2003. The increase is related to an estimate for the disposal of Trident Missile Motors.

Information Related to Environmental Liabilities
Accrued Environmental Restoration (DERP Funded) Cost Liabilities.
For FY 2004, the DON estimated and reported $3,424,463 thousand for environmental restoration liabilities. This amount is comprised of $2,841,462 thousand in Active Installations - Environmental Restoration (ER) liabilities and $583,001 thousand in Active Installations – ER for Closed Ranges liabilities, which represents UXO. The DoD FMR, Volume 6B, Chapter 10 requires that "any estimate produced must be based on site specific information and use cost models validated in accordance with DoD Instruction 5000.61." The DON is supporting this requirement by continuing to validate its range inventory as well as by pursuing the process of obtaining valid cost estimates for each range.

Other Accrued Environmental Costs (Non-DERP funds).
The DON developed guidance for the DON Major Commands to use as they begin to identify site data and develop estimates for the DON's "ongoing" operations. The DON continued review of program areas such as solid waste management unit cleanup, landfill closure, permitted facilities, removal, replacement, retrofill, and/or disposal of PCB transformers, underground storage tank remedial investigation and closure. For these areas the DON has identified an estimated total liability of $288,215 thousand in FY 2004. However, the DON is currently not reporting this amount within the General Fund financial statements until the Major Commands are able to identify all the site data and complete the estimates for the Non-DERP costs. The DON plans to start reporting the Other Accrued Environmental Costs (Non-DERP) within the financial statements beginning with FY 2006.

Base Realignment and Closure (BRAC).
For FY 2004, the DON estimated and reported $1,166,433 thousand for BRAC funded environmental restoration liabilities. This amount includes $1,110,652 thousand for environmental restoration (ER) and $55,781 thousand for ER transferring ranges, which includes military munitions, chemical residues from military munitions, and munitions scrap at locations on or associated with a military range on a BRAC installation.

Environmental Disposal for Weapons Systems Programs.
The DON reported an environmental disposal liability for Weapons Systems Programs of $11,441,083 thousand in FY 2004. This amount includes nuclear powered aircraft carriers of $5,693,000 thousand, nuclear powered submarines of $5,188,700 thousand, other nuclear powered ships of $287,500 thousand and other national defense weapons systems of $271,883 thousand.

Methodology Used to Estimate Environmental Liabilities

Accrued Environmental Restoration (DERP Funded) Costs.

Active Installations – Environmental Restoration (ER): Accrued restoration (cleanup) liabilities represent the cost to correct past environmental areas that are funded under the Defense Environmental Restoration Program in accordance with "Management Guidance for the DERP," and "Accrued Environmental Restoration (Cleanup) Liabilities," Chapter 14 of Volume 4 of the DoD FMR. These liabilities relate to PP&E, including acquired land and Stewardship Land, as those major asset categories are described in Chapter 6 of Volume 4 of the DoD FMR. Environmental restoration activities may be conducted at operating installations, at FUDS, at Closed, Transferred, and Transferring Ranges. Environmental restoration measurements involve the use of cost estimates that consider, on a current cost basis, the anticipated costs of the level of effort required to affect the restoration, as well as applicable legal and/or regulatory requirements. Program management and support costs are included in the estimates. The estimates are based on the DON's cost-to-complete (CTC) module of the DON Normalization of Data System (NORM). Certification of the CTC module was completed early in FY 2002. Such cost estimates are based on the current technology available. Site inventory and estimated cost data prepared for the DERP report to the Congress was used by the DON as the baseline for environmental restoration (cleanup) liability measurement (i.e., the current cost to acquire the required services). The Accrued Environmental Restoration (Cleanup) Costs do not include the costs of environmental compliance, pollution prevention, conservation activities, contamination or spills associated with current operations, or treaty obligations, all of which are accounted for as part of ongoing operations. The Department of the Navy's Environmental Restoration (ER,N) Program includes 3,692 clean-up sites while those installations covered by Base Realignment and Closure (BRAC) funding includes 1,057 clean-up sites.

Active Installations – Environmental Restoration For Closed Ranges: This represents the environmental liabilities associated with the identification, investigation and removal and remedial actions to address environmental contamination at ranges that were closed prior to September 30, 2002. The contamination may include munitions, chemical residues from military munitions and munitions scrap at ranges on active installations that pose a threat to human health or the environment. The amount reported is the portion of the liability that can be estimated based on site level investigations and characterizations. The estimate produced is based on site-specific information and use cost models validated in accordance with DoD Instruction 5000.61. Total liabilities (cost-to-complete) are not estimated until there is sufficient site-specific data available to estimate the total liability. Beginning in FY 2001, the Department began an inventory of closed ranges and transferring ranges under the Military Munitions Response Program (MMRP) or UXO program. The inventory was completed September 2002 and contains 208 closed ranges at active installations and 19 transferring ranges at BRAC sites.

Information regarding changes

Survey data of the Department of the Navy Environmental Restoration Program cost estimate changes for sites that had over 10 percent change or $500 thousand indicates diverse reasons for change in estimates. The reasons for changes include estimation changes (26 percent), regulatory changes (60 percent), and technical changes (15 percent). Reasons for changes in estimation are as follows: cost-to-complete (CTC) overlooked or previously unknown, better site characterization with sampling, cost avoidance rerun CTC, re-estimation based on different assumptions and/or escalation, and re-estimation of costs based on lessons learned. Reasons for changes in the regulatory area include: addition of range rule/munitions requirements, additional or extended long-term monitoring requirements or 5 year reviews, no further action agreement with regulator, and risk based corrective action. Reasons for changes in the technical area include: additional contamination level reduction with sampling, additional or extended remedial action operation, additional sites and incomplete site data, and changes in technical solutions.

Reference

The following is a summary of significant laws that affect the Department's conduct of environmental policy and regulations.

The National Environmental Policy Act (NEPA) of 1970 requires the Department to consider the environmental impacts of proposed actions in the decision making process. Per DON regulations, the action proponent will determine the level or amount of NEPA documentation required. The Resource Conservation and Recovery Act (RCRA) of 1976 as amended by the Hazardous and Solid Waste Amendments of 1984 (HSWA), was the first comprehensive federal effort to deal with safe disposal of all types of hazardous wastes, and provides for "cradle to grave" tracking of hazardous wastes. Permits are required for treatment, storage or disposal. Requirements for underground storage tanks (USTs) are also contained in RCRA.

The Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA), commonly referred to as the Superfund legislation, provided for Federal agencies authority to respond to the release or the substantial threat of release of hazardous substances into the environment. CERCLA was amended several times; one of the amendments was the Community Environmental Response Facilitation Act of 1992. The Department must identify real property on each facility that is not contaminated and that offers the greatest opportunity for expedited reuse and redevelopment. When property is transferred, BRAC or non-BRAC, the Department is still responsible for any remediation or corrective action or any response action found to be necessary after the transfer.

For the nuclear powered aircraft carriers, submarines, and other nuclear ships, the following significant laws affect the Department's conduct of environmental policy and regulations. The Atomic Energy Act of 1954, as amended, assures the proper management of source, special nuclear, and byproduct material. As in all cases with nuclear power, the Department coordinates all actions with the Department of Energy. The Nuclear Waste Policy Act of 1982 required all owners and generators of high-level nuclear waste and spent nuclear fuel, to pay their respective shares of the full cost of the program. Finally, the Low Level Radioactive Waste Policy Amendments Act of 1986 provides for the safe and efficient management of low-level radioactive waste.

For additional information concerning applicable laws and regulations, methodology for assigning estimated cleanup costs, and description of sites and technology used for cleanup consult the "FY 2002 Defense Environmental Restoration Program Annual Report to Congress."

For regulatory discussion on Environmental Liabilities, see Department of Defense Financial Management Regulation, Volume 6B, Chapter 10, paragraph 1016.

NOTE 15.A. OTHER LIABILITIES

As of September 30,	2004 Current Liability	2004 Noncurrent Liability	2004 Total	2003 Total
(Amounts in thousands)				
1. Intragovernmental:				
A. Advances from Others	$ 0	$ 0	$ 0	$ 0
B. Deferred Credits	0	0	0	0
C. Deposit Funds and Suspense Account Liabilities	256,784	0	256,784	223,225
D. Resources Payable to Treasury	0	0	0	0
E. Disbursing Officer Cash	234,866	0	234,866	282,996
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	41,833	0	41,833	49,157
I. FECA Reimbursement to the Department of Labor	245,461	320,423	565,884	562,105
J. Capital Lease Liability	0	0	0	0
K. Other Liabilities	2,885,435	0	2,885,435	2,742,430
L. Total Intragovernmental Other Liabilities	$ 3,664,379	$ 320,423	$ 3,984,802	$ 3,859,913
2. Non-Federal:				
A. Accrued Funded Payroll and Benefits	$ 414,999	$ 0	$ 414,999	$ 394,706
B. Advances from Others	0	0	0	0
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	699	0	699	2,933
H. Nonenvironmental Disposal Liabilities:				
(1) National Defense PP&E (Nonnuclear)	0	565,796	565,796	574,916
(2) Excess/Obsolete Structures	53,707	289,617	343,324	324,270
(3) Conventional Munitions Disposal	0	0	0	0
(4) Other	0	0	0	0
I. Accounts Payable--Cancelled Appropriations	0	0	0	23,238
J. Accrued Unfunded Annual Leave	2,463,860	0	2,463,860	2,269,191
K. Accrued Entitlement Benefits for Military Retirees and Survivors	0	0	0	0
L. Capital Lease Liability	202	0	202	146
M. Other Liabilities	150,592	81,355	231,947	196,562
N. Total Non-Federal Other Liabilities	$ 3,084,059	$ 936,768	$ 4,020,827	$ 3,785,962
3. Total Other Liabilities:	$ 6,748,438	$ 1,257,191	$ 8,005,629	$ 7,645,875

4. Other Information Pertaining to Other Liabilities:

Fluctuation and/or Abnormalities

Intragovernmental Other Liabilities.

The DON reported an increase of $33,559 thousand, 15 percent, in Deposit Funds and Suspense Account Liabilities (Line 1C) in FY 2004 when compared with FY 2003. The increase is due to implementing the Treasury and OUSD(C) policy on disbursement balances in the non-entity accounts. The disbursement balance was previously classified in USSGL 2400, Liability for Deposit Funds, Clearing Accounts, and Undeposited Collections, and now is recorded in USSGL 2120, Disbursements in Transit. The DON also reported a decrease of $48,130 thousand, 17 percent, in Disbursing Officer Cash (Line 1E) in FY 2004 when compared to FY 2003. It is the result of the draw down from Operation Iraqi Freedom and subsequent events.

The expansion of the ATM at Sea and Navy Cash programs in FY 2004 also contributed to the decrease of Disbursing Officer Cash as Disbursing Officers do not need as much cash on hand. In addition, the DON reported a decrease of $7,324 thousand, 15 percent, in the Judgment Fund Liabilities (Line 1H) in FY 2004. The decrease is due to the aggressive effort of the DON to reconcile and resolve claims under the Contracts Dispute Act.

Nonfederal Other Liabilities.

The DON also reported a decrease of $2,234 thousand, 76 percent, in Temporary Early Retirement Authority in FY 2004. Some DON commands did not update the Status of Funds in 4th Quarter FY 2003 and corrective action was taken in FY 2004. Accounts Payable – Cancelled Appropriations decreased $23,238 thousand, 100 percent for this line item, in FY 2004 due to a policy change that requires reclassifying it as Accounts Payable. However, cancelled payables actually increased by $66,234 thousand, or 285 percent in FY 2004. DON is reviewing the process of recording and liquidating cancelled appropriation liabilities. Capital Leases Liability increased $56 thousand, 38 percent, in the FY 2004 is due to the migration of DON activities to the Defense Property Accountability System (DPAS) in FY 2004. In addition, Other Liabilities increased $35,385 thousand, 18 percent, due to an increase of $36,324 thousand in Contract Holdbacks with the majority in Aircraft Procurement.

Other Disclosures

Intragovernmental Other Liabilities:

Judgment Fund (Line1.H).

The DON must reimburse the Department of the Treasury for payments made from the Judgment Fund on its behalf. These payments are a result of claims being resolved under the Contracts Dispute Act. Great strides have been made in reconciling and identifying the outstanding Judgment Fund Liability. Since FY 2003, the DON has reduced the Judgment Fund from $49,157 thousand to $41,833 thousand.

In addition, the Notification of Federal Antidiscrimination and Retaliatory Act (No FEAR) was implemented on October 1, 2003. This law requires all agencies to reimburse the Judgment Fund for cases covered by the No FEAR Act. For FY 2004, the DON reported $179 thousand for No FEAR Act liabilities. However, there is $66 thousand for the No FEAR Act in dispute and has not been recorded.

Other Liabilities (Line 1.K.) includes the following:

(Amounts in thousands)	As of September 30, 2004
Liability to Treasury & Others	$2,757,397
Unemployment	75,204
Employment Benefit	52,834
Total Intragovernmental Other Liabilities	$2,885,435

With respect to the major fiduciary balances, the DON must reconcile with the DOL and OPM. In FY 2004, the DON reported the following Intragovernmental Fiduciary liabilities: $565,884 thousand in FECA, $75,204 thousand in Unemployment, $52,834 thousand in Employment Benefit, and $41,833 thousand in Judgment Fund.

Nonfederal Other Liabilities:

Nonenvironmental Disposal Liability Disclosure.
The DON recognizes the nonenvironmental disposal liability for nuclear powered assets when the asset is initially placed in service. The nonenvironmental costs are included with the environmental disposal costs and reported in Note 14. However, the $565,796 thousand reported is estimated nonenvironmental disposal liability for conventional military equipment.

Excess/Obsolete Structures (Line 2.H.2).
The reported amount of $343,324 thousand is an estimate of disposing excess/obsolete structures at active installations.

Other Liabilities (Line 2.M.) includes $126,306 thousand Contract Holdbacks, $105,641 thousand Contract Incentives.

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

As of September 30,	2004				2003
	Asset Category				
	Land and Buildings	Equipment	Other	Total	Total
(Amounts in thousands)					
1. Future Payments Due:					
A. Fiscal Year 2005	$ 0	$ 202	$ 0	$ 202	$ 146
B. Fiscal Year 2006	0	0	0	0	0
C. Fiscal Year 2007	0	0	0	0	0
D. Fiscal Year 2008	0	0	0	0	0
E. Fiscal Year 2009	0	0	0	0	0
F. After 5 Years	0	0	0	0	0
G. Total Future Lease Payments Due	$ 0	$ 202	$ 0	$ 202	$ 146
H. Less: Imputed Interest Executory Costs	0	0	0	0	0
I. Net Capital Lease Liability	$ 0	$ 202	$ 0	$ 202	$ 146
2. Capital Lease Liabilities Covered by Budgetary Resources:				$ 0	$ 0
3. Capital Lease Liabilities Not Covered by Budgetary Resources:				$ 202	$ 146

4. Other Information Related to Capital Lease Liability:

Fluctuation and/or Abnormalities

The DON reported $56 thousand, 38 percent, increase in Capital Lease Liability in FY 2004 compared with FY 2003. The increase is due to the migration of DON activities to DPAS in FY 2004. Prior to the use of DPAS by these activities, these individual capital lease liabilities were not reported.

Other Disclosures

The liabilities associated with capital leases are captured in legacy systems and are not consistently recorded in the accounting system. The DON has recognized a liability equal to the net value of the assets (i.e. gross value less accumulated amortization). The resulting liability was recorded as a payment due in FY 2004. The proper breakout of future payments to appropriate years will be done when a process for capturing lease liabilities is implemented.

Reference

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

For regulatory discussion on Capital Lease Liability, see Department of Defense Financial Management Regulation, Volume 6B, Chapter 10, paragraph 1017.

Note 16. Commitments and Contingencies

Information Related to Commitments and Contingencies

The Department of the Navy is a party in various administrative proceedings and legal actions which may ultimately result in settlements or decisions adverse to the Federal Government. These proceedings and actions arise in the normal course of operations and their ultimate disposition is unknown. In the event of an adverse judgment against the Government, some of the liabilities may be payable from the Judgment Fund. Others may be payable from the Department's resources, either directly or by reimbursement to the Judgment Fund. Based on information currently available, however, it is management's opinion that the expected outcome of these matters, individually or in the aggregate, will not have a material adverse effect on the Department.

For fiscal years 2003 and 2004, the materiality threshold for reporting litigation, claims, or assessments was $16.7 million and $33.3 million, respectively. The amounts set forth above for civil and environmental litigation, claims, and assessments represent the aggregate of the amounts of claims, litigation or assessments considered to be significant for reporting purposes based on the established materiality thresholds. These amounts represent the maximum amounts of any potential liability of the Government based on the amounts claimed. Management does not consider it to be at all likely that the Government will be liable for such maximum amounts.

The DON reported a total of 29 cases in FY 2004 that met the materiality threshold. However, DON legal counsel is unable to express an opinion concerning the likely outcome of these cases.

Reference

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

For regulatory discussion on Commitments and Contingencies, see Department of Defense Financial Management Regulation, Volume 6B, Chapter 10, paragraph 1018.

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

As of September 30,	2004				2003
	Actuarial Present Value of Projected Plan Benefits	Assumed Interest Rate (%)	(Less: Assets Available to Pay Benefits)	Unfunded Actuarial Liability	Unfunded Actuarial Liability
(Amount in Thousands)					
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	$ 1,575,815		$ 0	$ 1,575,815	$ 1,589,971
B. Voluntary Separation Incentive Programs	0		0	0	0
C. DoD Educational Benefits Fund	0		0	0	0
D. Total Other	$ 1,575,815		$ 0	$ 1,575,815	$ 1,589,971
3. Total Military Retirement Benefits and Other Employment Related Actuarial Liabilities:	$ 1,575,815		$ 0	$ 1,575,815	$ 1,589,971

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

Military Retirement Pensions.

The portion of the military retirement benefits actuarial liability applicable to the DON is reported on the financial statements of the Military Retirement Fund (MRF).

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 DON is reported only on the DoD Agency-wide financial statements.

Federal Employees Compensation Act (FECA).

Actuarial Cost Method Used and Assumptions:
The DON's actuarial liability for workers' compensation benefits is developed by DOL and provided to DON at the end of each fiscal year. The liability for future workers' compensation (FWC) benefits includes the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases, plus a component for incurred but not reported claims. The liability is determined using a method that utilizes historical benefit payment patterns related to a specific incurred period to predict the ultimate payments related to that period. Consistent with past practice, these projected annual benefit payments have been discounted to present value using the Office of Management and Budgets economic assumptions for 10-year Treasury notes and bonds. Interest rate assumptions utilized for discounting were as follows:

FY 2004
4.883 percent in Year 1
5.235 percent in Year 2 and thereafter

To provide more specifically for the effects of inflation on the liability for future workers' compensation benefits, wage inflation factors (cost of living adjustments or COLAs) and medical inflation factors (consumer price index medical or CPIMs) were applied to the calculation of projected future benefits. These factors were also used to adjust the methodology's historical payments to current year constant dollars.

The compensation COLAs and CPIMs used in the projections for various charge back years (CBY) were as follows:

CBY	COLA	CPIM
2005	2.03%	4.14%
2006	2.73%	3.96%
2007	2.40%	3.98%
2008	2.40%	3.99%
2009+	2.40%	4.02%

The model's resulting projections were analyzed to insure that the estimates were reliable. The analysis was based on two tests: (1) a comparison of the percentage change in the liability amount by agency to the percentage change in the actual payments, and (2) a comparison of the ratio of the estimated liability to the actual payment of the beginning year calculated for the current projection to the liability-payment ratio calculated for the prior projection.

The estimate was allocated between General Fund and Navy Working Capital Fund using a percentage based on the number of civilian employees taken from the Navy Budget Tracking System. The following table, as of March 31, 2004, details the numbers used in support of the allocation:

	Personnel	Allocation %
DON General Fund	111,166	57%
Navy Working Capital Fund	82,712	43%
Total	193,878	100%

Voluntary Separation Incentive (VSI) Program.
The Voluntary Separation Incentive (VSI) Fund (recorded on the books of the Department of the Treasury) is used to accumulate funds to finance, on an actuarially sound basis, the liabilities DoD incurred under this program. The VSI benefit is an annual annuity paid to members who have separated under this program, and is paid for a period of time equal to twice the members' years of service.

DoD Education Benefits Fund.
The DoD Education Benefits Fund is designed to accumulate funds for the educational programs described under Title 10 United States Code, section 2006. This program promotes the recruitment and retention of members for the All-Volunteer Forces program and the Total Force Concept of the Armed Forces and aids in the readjustment of members of the Armed Forces to civilian life after separation from military service.

Reference

For regulatory discussion on Military Retirement Benefits and Other Employee Related Actuarial Liabilities, see Department of Defense Financial Management Regulation, Volume 6B, Chapter 10, paragraph 1019.

NOTE 18. UNEXPENDED APPROPRIATIONS

As of September 30,	2004	2003
(Amounts in thousands)		
1. Unexpended Appropriations:		
A. Unobligated, Available	$ 12,741,747	$ 28,083,485
B. Unobligated, Unavailable	4,054,888	998,235
C. Unexpended Obligations	62,365,139	47,613,208
D. Total Unexpended Appropriations	$ 79,161,774	$ 76,694,928

2. Other Information Pertaining to Unexpended Appropriations:

Fluctuation and/or Abnormalities
The Unobligated, Available and the Unexpended Obligations lines for FY 2004 when compared with FY 2003 does not provide for a meaningful comparison. Due to a prior period adjustment and the restatement of the FY 2003 column, it is not practical to compare FY 2004 to FY 2003 for these lines. The DON reported an increase of $3,056,653 thousand, 306 percent in Unobligated, Unavailable (Line 1B) in FY 2004 when compared with FY 2003. The reason for the significant increase in Unobligated, Unavailable is a result of receipt of supplemental appropriations (Title IX of the FY 2005 DoD Appropriations Act (P.L. 108-287)) that provided for FY 2004/FY 2005 additional funding.

Other Disclosures
Unobligated, Unavailable includes annual funds that are subject to the quarterly apportionment rule. They will become available in subsequent periods as they are apportioned. The amounts below reflect supplemental appropriations that will be made available in FY 2005. Below is a summary of funds subject to subsequent period apportionment:

Apportioned, Subsequent Periods:	Unobligated, Unavailable Funds
(Amounts in thousands)	
Military Personnel	$269,400
Operations and Maintenance	2,032,000
Procurement	61,800
Total	$2,363,200
Expired Years Authority	1,691,688
Unobligated, Unavailable	$4,054,888

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

Fluctuation and/or Abnormalities
The DON reported an increase of $18,237,710 thousand, 16 percent, in the Net Cost of Operations in FY 2004 when compared to FY 2003. The Procurement area showed a fluctuation in FY 2004 when compared with FY 2003 of $14,808,038 thousand, 86 percent, and Military Construction costs increased by $7,053,236 thousand, 653 percent. On a comparative basis, the major factor affecting the Procurement area was the FY 2003 capitalization of Military Equipment that reduced operating expenses by $20,440,000 thousand in FY 2003. The major factor affecting the Military Construction area was a correction to depreciation expense in FY 2004 related to Real Property and associated Capitalized Improvements. See Note 10 for a further explanation of the depreciation change.

Intragovernmental Gross Costs increased by $4,029,146 thousand, 11 percent, in FY 2004 when compared to FY 2003 with an increase in Intragovernmental Earned Revenue of $85,892 thousand, 3 percent. Intragovernmental Gross Costs are adjusted for trading partner submissions at the Component level, as trading partner submissions for payables and expense do not identify the DON Appropriations or associated Programs. The increase in Intragovernmental Earned Revenue is spread over several governmental agencies with these increases offset by immaterial decreases with several of the agencies. Significant increases in Intragovernmental Revenue were $917,991 thousand with Navy Working Capital Fund and $67,732 thousand with Air Force General Fund.

Similarly, Gross Costs with the Public increased $15,677,468 thousand, 19 percent, in FY 2004 when compared with FY 2003 and is coupled with an increase in Earned Revenue from the Public of $1,383,012 thousand, 72 percent. The increase in Gross Costs with the Public is a result of an increase in depreciation costs as a result of recognizing Military Equipment in FY 2003 and continuing into FY 2004 and an increase in depreciation costs for buildings, structures, and utilities resulting from changes to the depreciation module of Internet Naval Facility Association Database Store (iNFADS). These cost increases are explained in detail in Note 10.

A factor that impacted the increase on DON's Earned Revenue from the Public was the re-mapping of USSGL 7190 (Other Gains) to Earned Revenue from the Public.

Other 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 Statement of Net Cost (SoNC) are based on obligations and disbursements and therefore may not in all cases report actual accrued costs. The DON generally records transactions on a cash basis and not an accrual basis as is required by Federal GAAP. Therefore, the DON systems do not consistently capture actual costs. As such, information presented in the SoNC is based on budgetary obligations, disbursements, and collection transactions, as well as non-financial feeder systems; then adjusted to record known accruals for major items such as payroll expenses, accounts payable, and environmental liabilities.

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

Not Applicable.

Note 19.C. Gross Cost to Generate Intragovernmental 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,	2004	2003
(Amount in thousands)		
1. Civilian (e.g.,CSRS/FERS) Retirement	$ 247,413	$ 231,585
2. Civilian Health	296,631	232,822
3. Civilian Life Insurance	1,020	904
4. Military Retirement Pension	0	0
5. Military Retirement Health	0	0
6. Judgment Fund	40,145	44,408
7. Total Imputed Expenses	$ 585,209	$ 509,719

8. Other Information Related to Imputed Expense:

The DON financial statements have recognized an imputed expense for civilian employee pensions, life insurance, and health benefits in the Statement of Net Cost. Imputed expenses for employee benefits were calculated using cost factors provided by OPM applied against gross basic pay for all categories of civilian service employees. The gross basic pay amounts were extracted directly from the Defense Civilian Pay System (DCPS).

Note 19.E. Benefit Program Expenses
Not Applicable.

Note 19. F. Exchange Revenue
Not Applicable.

Note 19.G. Amounts for Foreign Military Sales (FMS) Program Procurements from Contractors
Not Applicable.

Note 19.H. Stewardship Assets
Stewardship assets include Heritage Assets, Stewardship Land, Non-Federal Physical Property, and Investments in Research and Development. The current year cost of acquiring, constructing, improving, reconstructing, or renovating stewardship assets are included in the Statement of Net Cost.

Note 19.I. Intragovernmental Revenue and Expense
The majority of DON accounting systems do not consistently capture trading partner data at the transaction level in a manner that facilitates trading partner aggregations. Therefore, DON was unable to reconcile intragovernmental revenue balances with its trading partners. DoD 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 after-the-fact reconciliation can not be accomplished with existing or foreseeable resources.

Note 19.J. Suborganization Program Costs
Not Applicable.

NOTE 20. DISCLOSURES RELATED TO THE STATEMENT OF CHANGES IN NET POSITION

As of September 30,		Cumulative Results of Operations 2004		Unexpended Appropriations 2004		Cumulative Results of Operations 2003		Unexpended Appropriations 2003
(Amounts in thousands)								
1. Prior Period Adjustments Increases (Decreases) to Net Position Beginning Balance:								
A. Changes in Accounting Standards	$	0	$	0	$	152,557,286	$	0
B. Errors and Omissions in Prior Year		(25,913,750)		25,913,750		0		0
C. Other Prior Period Adjustments		0		0		0		0
D. Total Prior Period Adjustments	$	(25,913,750)	$	25,913,750	$	152,557,286	$	0
2. Imputed Financing:								
A. Civilian CSRS/FERS Retirement	$	247,413	$	0	$	231,585	$	0
B. Civilian Health		296,631		0		232,822		0
C. Civilian Life Insurance		1,020		0		904		0
D. Military Retirement Pension		0		0		0		0
E. Military Retirement Health		0		0		0		0
F. Judgment Fund		40,145		0		44,408		0
G. Total Imputed Financing	$	585,209	$	0	$	509,719	$	0

3. Other Information:

Other Disclosures

Errors and Omissions in Prior Year Accounting Reports.

Two prior period adjustments were recorded to the DON financial statements and were recognized as errors and omissions per Statement of Federal Financial Accounting Standards (SFFAS) No. 21, "Reporting Corrections of Errors and Changes in Accounting Principles." The errors occurred in the 4th Quarter FY 2003 financial statements. The overall impact of the prior period adjustments warrants the restatement of the FY 2004 DON financial statements for comparative purposes. These adjustments will affect the following financial statements for restatement in the fourth quarter: Balance Sheet (Net Position section) and the Statement of Changes in Net Position. The prior period adjustments were categorized as follows:

	Cumulative Results of Operations	Unexpended Appropriations
Error in reporting Appropriations Used	($25,913,750)	$25,913,750

The errors involved the inclusion of disbursement and collection amounts in Appropriations Used, accounts (USSGL 3107 and USSGL 5700) both of which are mapped to the Statement of Changes in Net Position: 3107 to Unexpended Appropriations, and 5700 to Cumulative Results of Operations.

Imputed Financing.

The DON financial statements have recognized an imputed financing source for civilian employee pensions, life insurance, and health benefits in the Statement of Net Cost. Imputed financing sources for employee benefits were calculated using cost factors provided by OPM applied against gross basic pay for all categories of civilian service employees. The gross basic pay amounts were extracted directly from the Defense Civilian Pay System (DCPS).

Judgment Fund.
Treasury provided information related to amounts paid for Judgment Fund liabilities under the Contracts Dispute Act and the Notification of Federal Antidiscrimination and Retaliatory Act (No FEAR Act) on behalf of the DON, which the DON is required to repay. Judgment Fund payments made out of the following Treasury appropriations do not require reimbursement and therefore represent imputed financing to the DON: 20X1740 and 20X1742. Only those payments made from Treasury appropriation 20X1743, and that portion of 20X1741 that is related to the No FEAR Act are required to be repaid by DON.

Note 21. Disclosures Related to the Statement of Budgetary Resources

As of September 30,	2004	2003
(Amounts in thousands)		
1. Net Amount of Budgetary Resources Obligated for Undelivered Orders at the End of the Period	$ 63,059,730	$ 64,855,940
2. Available Borrowing and Contract Authority at the End of the Period	0	739

3. Other Information Related to the Statement of Budgetary Resources:

The Net Amount of Budgetary Resources Obligated for Undelivered Orders in this note only represents USSGL 4801, Undelivered Orders – Obligations, Unpaid. However, the amount represented on the Statement of Budgetary Resources, line 14 C not only includes USSGL 4801, Undelivered Orders – Obligations, Unpaid but also USSGL 4802, Undelivered Orders – Obligations, Prepaid/Advanced.

The difference of $30,494 thousand between the SBR Appropriations Received when compared with the Statement of Change of Net Position (SOCNP) Appropriations Received is due to the Trust Funds not being included in the Appropriations Received line of the SOCNP.

Other Disclosures
Obligations Incurred includes $132,268,522 thousand Direct Obligations and $8,886,330 thousand Reimbursable Obligations.

Included in the DON FY 2004 Statement of Budgetary Resources is a $448,000 thousand transaction from the Navy Working Capital Fund (NWCF). This transaction was recorded using a Voucher For Transfers Between Appropriations and/or Funds (SF1080) and is not reflected as a part of Net Transfers on the Statement of Budgetary Resources. The SF1080 transaction with the NWCF was made in accordance with the Department of the Navy's FY 2004 President's Budget.

Due to accounting system deficiencies, intragovernmental transactions were not eliminated for the presentation of a Consolidated Statement of Budgetary Resources (SBR).

In FY 2004, DoD treated Foreign Military Sales (FMS) Trust Fund transactions as nonfederal, and were presented as such in the Balance Sheet (BS) and the Statement of Net Cost. Accounts Receivable and Revenues related to FMS are recognized in the SBR. Therefore, reconciling differences exist between the SBR and the BS. OUSD(C) Accounting Policy is currently researching the issue to determine the proper treatment of FMS Trust Fund transactions to ensure proper reporting.

DON has two permanent, indefinite appropriations.

National Defense Sealift Fund:
The National Defense Sealift Fund (NDSF) is operated under the authority of 10 U.S. Code 2218, which provides for the construction (including design of vessels), purchase, alteration, and conversion of Department of Defense (DOD) sealift vessels; operation, maintenance, and lease or charter of DOD vessels for national defense purposes; installation and maintenance of defense features for national defense purposes on privately owned and operated vessels that are constructed in the United States and documented under the laws of the United States; research and development relating to national defense sealift; and expenses for maintaining the National Defense Reserve Fleet (NDRF) including the acquisition, alteration or conversion of vessels built in U.S. shipyards for the NDRF. In FY 2004, $5,000 thousand was transferred from the NDSF to the Military Personnel, Marine Corps appropriation.

Environmental Restoration, Navy:
Environmental Restoration, Navy (ER, N) is a transfer account that funds environmental restoration, reduction and recycling of hazardous waste, removal of unsafe buildings and debris, and similar purposes. Funds are to remain available until transferred, and remain available for the same purpose and same time period as the appropriations to which transferred. In FY 2004, $254,929 thousand was transferred from ER, N to the Operations and Maintenance, Navy appropriation.

Note 22. Disclosures Related to the Statement of Financing

Fluctuation and/or Abnormalities
Budgetary data is not in agreement with proprietary expenses and assets capitalized. This fact causes a difference in net cost between the Statement of Net Cost and the Statement of Financing. Adjustments are posted to the Statement of Financing for these differences.

Other Disclosures
The increase of resources that finance the acquisition of assets is primarily due to the implementation of SFFAS No. 23 “Eliminating the Category of National Defense Property, Plant, and Equipment.” Correspondingly, there is also an increase in the reported depreciation for the military equipment.

The Statement of Financing is presented as combined or combining statements rather than consolidated statements due to intragovernmental transactions not being eliminated. Adjustments in funds which are temporarily not available pursuant to Public Law, and those that are permanently not available (included in the “Adjustments” line on the Statement of Budgetary Resources), are not included in “Spending Authority From Offsetting Collections and Adjustments” line on the Statement of Budgetary Resources or on the Statement of Financing.

The Statement of Financing was expanded to further articulate and detail the relationship between new obligations from budgetary accounting and net cost of operations from proprietary accounting.

Note 23. Disclosures Related to the Statement of Custodial Activity
Not Applicable

Note 24.A. Other Disclosures

1. Entity as Lessee - Operating Leases

As of September 30,	2004				2003
(Amounts in thousands)					
Future Payments Due:	Land and Buildings	Equipment	Other	Total	Total
Fiscal Year					
2005	$ 59,965	$ 0	$ 0	$ 59,965	$ 15,596
2006	64,693	0	0	64,693	15,474
2007	66,276	0	0	66,276	17,469
2008	66,569	0	0	66,569	17,559
2009	66,861	0	0	66,861	17,571
After 5 Years	0	0	0	0	0
Total Future Lease Payments Due	$ 324,364	$ 0	$ 0	$ 324,364	$ 83,669

Fluctuations and/of Abnormalities
The DON reported an increase of $240,695 thousand, 288 percent, in Operating Leases Future Payment in FY 2004 when compared to FY 2003. The increase is due to better data collection efforts throughout the Navy shore establishment.

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 a payment of funds.

Operating Lease - A lease which does not transfer substantially all the benefits and risk of ownership. Payments should be charged to expense over the lease term as it becomes payable.

Other Disclosure
The value for lease information is derived from the DON data collection process. This process only provides summary levels values at this time.

Note 24.B. Other Disclosures
Not Applicable.

Department of the Navy

General Fund Supporting Consolidating/Combining Statements

Department of Defense
Department of the Navy
CONSOLIDATING BALANCE SHEET
As of September 30, 2004 and 2003
($ in thousands)

	Navy	Marine Corps
ASSETS (Note 2)		
Intragovernmental:		
Fund Balance with Treasury (Note 3)		
Entity	$ 75,047,363	$ 6,827,455
Non-Entity Seized Iraqi Cash	0	0
Non-Entity-Other	219,095	0
Investments (Note 4)	9,457	0
Accounts Receivable (Note 5)	211,008	59,418
Other Assets (Note 6)	269,589	3,134
Total Intragovernmental Assets	$ 75,756,512	$ 6,890,007
Cash and Other Monetary Assets (Note 7)	$ 126,338	$ 108,527
Accounts Receivable (Note 5)	2,885,043	10,923
Loans Receivable (Note 8)	0	0
Inventory and Related Property (Note 9)	52,862,678	477,989
General Property, Plant and Equipment (Note 10)	148,266,586	3,412,917
Investments (Note 4)	0	0
Other Assets (Note 6)	4,824,249	176,099
TOTAL ASSETS	$ 284,721,406	$ 11,076,462
LIABILITIES (Note 11)		
Intragovernmental:		
Accounts Payable (Note 12)	$ 1,303,589	$ 153,750
Debt (Note 13)	0	0
Environmental Liabilities (Note 14)	0	0
Other Liabilities (Note 15 & Note 16)	3,784,884	199,918
Total Intragovernmental Liabilities	$ 5,088,473	$ 353,668
Accounts Payable (Note 12)	$ 1,016,008	$ 379,000
Military Retirement Benefits and Other Employment-Related Actuarial Liabilities (Note 17)	1,359,036	216,779
Environmental Liabilities (Note 14)	16,031,979	0
Loan Guarantee Liability (Note 8)	0	0
Other Liabilities (Note 15 and Note 16)	3,488,967	531,859
Debt Held by Public	0	0
TOTAL LIABILITIES	$ 26,984,463	$ 1,481,306
NET POSITION		
Unexpended Appropriations (Note 18)	$ 72,627,291	$ 6,534,483
Cumulative Results of Operations	185,109,652	3,060,673
TOTAL NET POSITION	$ 257,736,943	$ 9,595,156
TOTAL LIABILITIES AND NET POSITION	$ 284,721,406	$ 11,076,462

Department of Defense
Department of the Navy
CONSOLIDATING BALANCE SHEET
As of September 30, 2004 and 2003
($ in thousands)

ASSETS (Note 2)	Combined Total	Eliminations	2004 Consolidated	2003 Consolidated Restated
Intragovernmental:				
Fund Balance with Treasury (Note 3)				
Entity	$ 81,874,818	$ 0	$ 81,874,818	$ 78,191,653
Non-Entity Seized Iraqi Cash	0	0	0	0
Non-Entity-Other	219,095	0	219,095	223,225
Investments (Note 4)	9,457	0	9,457	9,801
Accounts Receivable (Note 5)	270,426	19,723	250,703	496,863
Other Assets (Note 6)	272,723	0	272,723	187,865
Total Intragovernmental Assets	$ 82,646,519	$ 19,723	$ 82,626,796	$ 79,109,407
Cash and Other Monetary Assets (Note 7)	$ 234,865	$ 0	$ 234,865	$ 282,995
Accounts Receivable (Note 5)	2,895,966	0	2,895,966	3,382,133
Loans Receivable (Note 8)	0	0	0	0
Inventory and Related Property (Note 9)	53,340,667	0	53,340,667	53,611,634
General Property, Plant and Equipment (Note 10)	151,679,503	0	151,679,503	158,407,450
Investments (Note 4)	0	0	0	0
	5,000,348	0	5,000,348	6,180,624
TOTAL ASSETS	$ 295,797,868	$ 19,723	$ 295,778,145	$ 300,974,243
LIABILITIES (Note 11)				
Intragovernmental:				
Accounts Payable (Note 12)	$ 1,457,339	$ 19,723	$ 1,437,616	$ 1,035,033
Debt (Note 13)	0	0	0	0
Environmental Liabilities (Note 14)	0	0	0	0
Other Liabilities (Note 15 & Note 16)	3,984,802	0	3,984,802	3,859,913
Total Intragovernmental Liabilities	$ 5,442,141	$ 19,723	$ 5,422,418	$ 4,894,946
Accounts Payable (Note 12)	$ 1,395,008	$ 0	$ 1,395,008	$ 1,742,522
Military Retirement Benefits and Other Employment-Related Actuarial Liabilities (Note 17)	1,575,815	0	1,575,815	1,589,971
Environmental Liabilities (Note 14)	16,031,979	0	16,031,979	15,614,424
Loan Guarantee Liability (Note 8)	0	0	0	0
Other Liabilities (Note 15 and Note 16)	4,020,826	0	4,020,826	3,785,962
Debt Held by Public	0	0	0	0
TOTAL LIABILITIES	$ 28,465,769	$ 19,723	$ 28,446,046	$ 27,627,825
NET POSITION				
Unexpended Appropriations (Note 18)	$ 79,161,774	$ 0	$ 79,161,774	$ 76,694,928
Cumulative Results of Operations	188,170,325	0	188,170,325	196,651,490
TOTAL NET POSITION	$ 267,332,099	$ 0	$ 267,332,099	$ 273,346,418
TOTAL LIABILITIES AND NET POSITION	$ 295,797,868	$ 19,723	$ 295,778,145	$ 300,974,243

Department of Defense
Department of the Navy
CONSOLIDATING STATEMENT OF NET COST
For the years ended September 30, 2004 and 2003
($ in thousands)

	Navy	Marine Corps
Program Costs		
Military Personnel		
Intragovernmental Gross Costs	$ 5,157,236	$ 2,241,253
(Less Intragovernmental Earned Revenue)	(397,452)	(20,074)
Intragovernmental Net Costs	$ 4,759,784	$ 2,221,179
Gross Costs With the Public	$ 20,934,864	$ 8,069,582
(Less: Earned Revenue From the Public)	0	0
Net Costs With the Public	$ 20,934,864	$ 8,069,582
Net Program Cost	$ 25,694,648	$ 10,290,761
Operations and Maintenance		
Intragovernmental Gross Costs	$ 1,581,078	$ 281,615
(Less Intragovernmental Earned Revenue)	(4,774,111)	(392,144)
Intragovernmental Net Costs	$ (3,193,033)	$ (110,529)
Gross Costs With the Public	$ 38,784,464	$ 5,345,293
(Less: Earned Revenue From the Public)	(47,276)	0
Net Costs With the Public	$ 38,737,188	$ 5,345,293
Net Program Cost	$ 35,544,155	$ 5,234,764
Procurement		
Intragovernmental Gross Costs	$ 0	$ 550
(Less Intragovernmental Earned Revenue)	(765,188)	(2,035)
Intragovernmental Net Costs	$ (765,188)	$ (1,485)
Gross Costs With the Public	$ 30,116,666	$ 2,983,589
(Less: Earned Revenue From the Public)	0	(248,999)
Net Costs With the Public	$ 30,116,666	$ 2,734,590
Net Program Cost	$ 29,351,478	$ 2,733,105
Research, Development, Test & Evaluation		
Intragovernmental Gross Costs	$ 0	$ 0
(Less Intragovernmental Earned Revenue)	(307,534)	0
Intragovernmental Net Costs	$ (307,534)	$ 0
Gross Costs With the Public	$ 14,466,658	$ 0
(Less: Earned Revenue From the Public)	0	0
Net Costs With the Public	$ 14,466,658	$ 0
Net Program Cost	$ 14,159,124	$ 0

Department of Defense
Department of the Navy
CONSOLIDATING STATEMENT OF NET COST
For the years ended September 30, 2004 and 2003
($ in thousands)

	Combined Total	Eliminations	2004 Consolidated	2003 Consolidated
Program Costs				
Military Personnel				
Intragovernmental Gross Costs	$ 7,398,489	$ 0	$ 7,398,489	$ 12,135,559
(Less Intragovernmental Earned Revenue)	(417,526)	0	(417,526)	(69,149)
Intragovernmental Net Costs	$ 6,980,963	$ 0	$ 6,980,963	$ 12,066,410
Gross Costs With the Public	$ 29,004,446	$ 0	$ 29,004,446	$ 24,509,847
(Less: Earned Revenue From the Public)	0	0	0	(281,482)
Net Costs With the Public	$ 29,004,446	$ 0	$ 29,004,446	$ 24,228,365
Net Program Cost	$ 35,985,409	$ 0	$ 35,985,409	$ 36,294,775
Operations and Maintenance				
Intragovernmental Gross Costs	$ 1,862,693	$ 0	$ 1,862,693	$ 16,783,901
(Less Intragovernmental Earned Revenue)	(5,166,255)	0	(5,166,255)	(2,605,019)
Intragovernmental Net Costs	$ (3,303,562)	$ 0	$ (3,303,562)	$ 14,178,882
Gross Costs With the Public	$ 44,129,757	$ 0	$ 44,129,757	$ 28,690,542
(Less: Earned Revenue From the Public)	(47,276)	0	(47,276)	(1,036,745)
Net Costs With the Public	$ 44,082,481	$ 0	$ 44,082,481	$ 27,653,797
Net Program Cost	$ 40,778,919	$ 0	$ 40,778,919	$ 41,832,679
Procurement				
Intragovernmental Gross Costs	$ 550	$ 0	$ 550	$ 3,966,807
(Less Intragovernmental Earned Revenue)	(767,223)	0	(767,223)	(886,640)
Intragovernmental Net Costs	$ (766,673)	$ 0	$ (766,673)	$ 3,080,167
Gross Costs With the Public	$ 33,100,255	$ 0	$ 33,100,255	$ 14,507,061
(Less: Earned Revenue From the Public)	(248,999)	0	(248,999)	(310,683)
Net Costs With the Public	$ 32,851,256	$ 0	$ 32,851,256	$ 14,196,378
Net Program Cost	$ 32,084,583	$ 0	$ 32,084,583	$ 17,276,545
Research, Development, Test & Evaluation				
Intragovernmental Gross Costs	$ 0	$ 0	$ 0	$ 993,892
(Less Intragovernmental Earned Revenue)	(307,534)	0	(307,534)	(237,506)
Intragovernmental Net Costs	$ (307,534)	$ 0	$ (307,534)	$ 756,386
Gross Costs With the Public	$ 14,466,658	$ 0	$ 14,466,658	$ 11,418,578
(Less: Earned Revenue From the Public)	0	0	0	(4,122)
Net Costs With the Public	$ 14,466,658	$ 0	$ 14,466,658	$ 11,414,456
Net Program Cost	$ 14,159,124	$ 0	$ 14,159,124	$ 12,170,842

Department of Defense
Navy Working Capital Fund
CONSOLIDATING STATEMENT OF NET COST
For the years ended September 30, 2004 and 2003
($ in thousands)

	Navy	Marine Corps
Program Costs		
Military Construction/Family Housing		
Intragovernmental Gross Costs	$ 0	$ 0
(Less Intragovernmental Earned Revenue)	(741,184)	0
Intragovernmental Net Costs	$ (741,184)	$ 0
Gross Costs With the Public	$ 8,910,371	$ 0
(Less: Earned Revenue From the Public)	(35,329)	0
Net Costs With the Public	$ 8,875,042	$ 0
Net Program Cost	$ 8,133,858	$ 0
Other		
Intragovernmental Gross Costs	$ 27,763,610	$ 2,364,592
(Less Intragovernmental Earned Revenue)	3,714,298	194,350
Intragovernmental Net Costs	$ 31,477,908	$ 2,558,942
Gross Costs With the Public	$ (30,308,974)	$ (2,456,262)
(Less: Earned Revenue From the Public)	(2,863,533)	(107,571)
Net Costs With the Public	$ (33,172,507)	$ (2,563,833)
Net Program Cost	$ (1,694,599)	$ (4,891)
Total Program Costs		
Intragovernmental Gross Costs	$ 34,501,924	$ 4,888,010
(Less Intragovernmental Earned Revenue)	(3,271,171)	(219,903)
Intragovernmental Net Costs	$ 31,230,753	$ 4,668,107
Gross Costs With the Public	$ 82,904,049	$ 13,942,202
(Less: Earned Revenue From the Public)	(2,946,138)	(356,570)
Net Costs With the Public	$ 79,957,911	$ 13,585,632
Net Program Cost	$ 111,188,664	$ 18,253,739
Costs Not Assigned to Programs	0	0
(Less: Earned Revenue Not Attributable to Programs)	0	0
Net Cost of Operations	$ 111,188,664	$ 18,253,739

Department of Defense
Department of the Navy
CONSOLIDATING STATEMENT OF NET COST
For the years ended September 30, 2004 and 2003
($ in thousands)

	Combined Total	Eliminations	2004 Consolidated	2003 Consolidated
Program Costs				
Military Construction/Family Housing				
Intragovernmental Gross Costs	$ 0	$ 0	$ 0	$ 204,387
(Less Intragovernmental Earned Revenue)	(741,184)	0	(741,184)	(124,381)
Intragovernmental Net Costs	$ (741,184)	$ 0	$ (741,184)	$ 80,006
Gross Costs With the Public	$ 8,910,371	$ 0	$ 8,910,371	$ 1,370,505
(Less: Earned Revenue From the Public)	(35,329)	0	(35,329)	(369,889)
Net Costs With the Public	$ 8,875,042	$ 0	$ 8,875,042	$ 1,000,616
Net Program Cost	$ 8,133,858	$ 0	$ 8,133,858	$ 1,080,622
Other				
Intragovernmental Gross Costs	$ 30,128,202	$ 218,214	$ 29,909,988	$ 1,058,028
(Less Intragovernmental Earned Revenue)	3,908,648	(218,214)	4,126,862	735,727
Intragovernmental Net Costs	$ 34,036,850	$ 0	$ 34,036,850	$ 1,793,755
Gross Costs With the Public	$ (32,765,236)	$ 0	$ (32,765,236)	$ 672,250
(Less: Earned Revenue From the Public)	(2,971,104)	0	(2,971,104)	83,225
Net Costs With the Public	$ (35,736,340)	$ 0	$ (35,736,340)	$ 755,475
Net Program Cost	$ (1,699,490)	$ 0	$ (1,699,490)	$ 2,549,230
Total Program Costs				
Intragovernmental Gross Costs	$ 39,389,934	$ 218,214	$ 39,171,720	$ 35,142,574
(Less Intragovernmental Earned Revenue)	(3,491,074)	(218,214)	(3,272,860)	(3,186,968)
Intragovernmental Net Costs	$ 35,898,860	$ 0	$ 35,898,860	$ 31,955,606
Gross Costs With the Public	$ 96,846,251	$ 0	$ 96,846,251	$ 81,168,783
(Less: Earned Revenue From the Public)	(3,302,708)	0	(3,302,708)	(1,919,696)
Net Costs With the Public	$ 93,543,543	$ 0	$ 93,543,543	$ 79,249,087
Net Program Cost	$ 129,442,403	$ 0	$ 129,442,403	$ 111,204,693
Costs Not Assigned to Programs	0	0	0	0
(Less: Earned Revenue Not Attributable to Programs)	0	0	0	0
Net Cost of Operations	$ 129,442,403	$ 0	$ 129,442,403	$ 111,204,693

Department of Defense
Department of the Navy
CONSOLIDATING STATEMENT OF CHANGES IN NET POSITION
For the years ended September 30, 2004 and 2003
($ in thousands)

	Navy	Marine Corps
Cumulative Results of Operations		
Beginning Balances	$ 217,746,444	$ 4,818,795
Prior period adjustments (+/-)		
Prior Period Adjustments- Restated (+/-)	(25,913,750)	0
Beginning Balance- Restated	$ 191,832,694	$ 4,818,795
Prior Period Adjustments- Not Restated (+/-)	0	0
Beginning Balances, as adjusted	$ 191,832,694	$ 4,818,795
Budgetary Financing Sources:		
Appropriations Received	$ 0	$ 0
Appropriations transferred in/out (+/-)	0	0
Other adjustments (rescissions, etc) (+/-)	0	0
Appropriations used	103,759,488	16,438,659
Nonexchange revenue	0	0
Donations and forfeitures of cash and cash equivalents	0	0
Transfers in/out without reimbursement (+/-)	166,000	0
Other budgetary financing sources (+/-)	0	0
Other Financing Sources:		
Donations and forfeitures of property	0	0
Transfers in/out without reimbursement (+/-)	16,775	(4,892)
Imputed financing from costs absorbed by others	523,359	61,850
Other (+/-)	0	0
Total Financing Sources	$ 104,465,622	$ 16,495,617
Net Cost of Operations (+/-)	$ 111,188,664	$ 18,253,739
Ending Balances	$ 185,109,652	$ 3,060,673
Unexpended Appropriations		
Beginning Balances	$ 46,963,736	$ 3,817,443
Prior period adjustments (+/-)		
Prior Period Adjustments- Restated (+/-)	25,913,750	0
Beginning Balance- Restated	$ 72,877,486	$ 3,817,443
Prior Period Adjustments- Not Restated (+/-)	0	0
Beginning Balances, as adjusted	$ 72,877,486	$ 3,817,443
Budgetary Financing Sources:		
Appropriations Received	$ 105,443,972	$ 18,474,011
Appropriations transferred in/out (+/-)	(327,024)	782,083
Other adjustments (rescissions, etc) (+/-)	(1,607,655)	(100,395)
Appropriations used	(103,759,488)	(16,438,659)
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	$ (250,195)	$ 2,717,040
Net Cost of Operations (+/-)	$ 0	$ 0
Ending Balances	$ 72,627,291	$ 6,534,483

Department of Defense
Department of the Navy
CONSOLIDATING STATEMENT OF CHANGES IN NET POSITION
For the years ended September 30, 2004 and 2003
($ in thousands)

	Combined Total	Eliminations	2004 Consolidated	2003 Consolidated Restated
Cumulative Results of Operations				
Beginning Balances	$ 222,565,239	$ 0	$ 222,565,239	$ 44,169,672
Prior period adjustments (+/-)				
Prior Period Adjustments- Restated (+/-)	$ (25,913,750)	$ 0	$ (25,913,750)	$ 0
Beginning Balance- Restated	196,651,489	0	196,651,489	44,169,672
Prior Period Adjustments- Not Restated (+/-)	0	0	0	152,557,286
Beginning Balances, as adjusted	$ 196,651,489	$ 0	$ 196,651,489	$ 196,726,958
Budgetary Financing Sources:				
Appropriations Received	$ 0	$ 0	$ 0	$ 0
Appropriations transferred in/out (+/-)	0	0	0	0
Other adjustments (rescissions, etc) (+/-)	0	0	0	0
Appropriations used	120,198,147	0	120,198,147	110,567,740
Nonexchange revenue	0	0	0	0
Donations and forfeitures of cash and cash equivalents	0	0	0	0
Transfers in/out without reimbursement (+/-)	166,000	0	166,000	0
Other budgetary financing sources (+/-)	0	0	0	0
Other Financing Sources:				
Donations and forfeitures of property	0	0	0	0
Transfers in/out without reimbursement (+/-)	11,883	0	11,883	51,765
Imputed financing from costs absorbed by others	585,209	0	585,209	509,719
Other (+/-)	0	0	0	0
Total Financing Sources	$ 120,961,239	$ 0	$ 120,961,239	$ 111,129,224
Net Cost of Operations (+/-)	$ 129,442,403	$ 0	$ 129,442,403	$ 111,204,693
Ending Balances	$ 188,170,325	$ 0	$ 188,170,325	$ 196,651,489
Unexpended Appropriations				
Beginning Balances	$ 50,781,179	$ 0	$ 50,781,179	$ 64,774,328
Prior period adjustments (+/-)				
Prior Period Adjustments- Restated (+/-)	25,913,750	0	25,913,750	0
Beginning Balance- Restated	$ 76,694,929	$ 0	$ 76,694,929	$ 0
Prior Period Adjustments- Not Restated (+/-)	0	0	0	0
Beginning Balances, as adjusted	$ 76,694,929	$ 0	$ 76,694,929	$ 64,774,328
Budgetary Financing Sources:				
Appropriations Received	$ 123,917,983	$ 0	$ 123,917,983	$ 122,132,688
Appropriations transferred in/out (+/-)	455,059	0	455,059	1,810,288
Other adjustments (rescissions, etc) (+/-)	(1,708,050)	0	(1,708,050)	(1,454,635)
Appropriations used	(120,198,147)	0	(120,198,147)	(110,567,740)
Nonexchange revenue	0	0	0	0
Donations and forfeitures of cash and cash equivalents	0	0	0	0
Transfers in/out without reimbursement (+/-)	0	0	0	0
Other budgetary financing sources (+/-)	0	0	0	0
Other Financing Sources:				
Donations and forfeitures of property	0	0	0	0
Transfers in/out without reimbursement (+/-)	0	0	0	0
Imputed financing from costs absorbed by others	0	0	0	0
Other (+/-)	0	0	0	0
Total Financing Sources	$ 2,466,845	$ 0	$ 2,466,845	$ 11,920,601
Net Cost of Operations (+/-)	$ 0	$ 0	$ 0	$ 0
Ending Balances	$ 79,161,774	$ 0	$ 79,161,774	$ 76,694,929

Department of Defense
Department of the Navy
COMBINING STATEMENT OF BUDGETARY RESOURCES
For the years ended September 30, 2004 and 2003
($ in thousands)

BUDGETARY FINANCING ACCOUNTS

	Navy	Marine Corps	2004 Combined	2003 Combined
BUDGETARY RESOURCES				
Budget Authority:				
Appropriations Received	$ 105,474,466	$ 18,474,011	$ 123,948,477	$ 122,169,428
Borrowing Authority	0	0	0	0
Contract Authority	0	0	0	739
Net transfers (+/-)	(252,259)	677,368	425,109	1,662,142
Other	0	0	0	0
Unobligated Balance:				
Beginning of period	14,108,219	587,019	14,695,238	11,908,983
Net transfers, actual (+/-)	91,235	104,715	195,950	145,546
Anticipated Transfers Balances	0	0	0	0
Spending Authority from Offsetting Collections:				
Earned				
Collected	7,327,335	379,315	7,706,650	6,792,556
Receivable from Federal sources	(395,222)	34,938	(360,284)	(1,211,532)
Change in unfilled customer orders				
Advances received	56,010	0	56,010	(59,842)
Without advance from Federal sources	457,066	10,440	467,506	308,282
Anticipated for the rest of year, without advances	0	0	0	0
Transfers from trust funds	0	0	0	0
Subtotal	$ 7,445,189	$ 424,693	$ 7,869,882	$ 5,829,464
Recoveries of prior year obligations	$ 6,708,443	$ 7,048,538	$ 13,756,981	$ 7,009,339
Temporarily not available pursuant to Public Law	0	0	0	0
Permanently not available	(1,608,394)	(100,395)	(1,708,789)	(1,452,574)
Total Budgetary Resources	$ 131,966,899	$ 27,215,949	$ 159,182,848	$ 147,273,067

Department of Defense
Department of the Navy
COMBINING STATEMENT OF BUDGETARY RESOURCES
For the years ended September 30, 2004 and 2003
($ in thousands)

BUDGETARY FINANCING ACCOUNTS

	Navy	Marine Corps	2004 Combined	2003 Combined
STATUS OF BUDGETARY RESOURCES				
Obligations Incurred:				
Direct	$ 108,067,166	$ 24,201,356	$ 132,268,522	$ 124,497,950
Reimbursable	8,332,062	554,268	8,886,330	8,079,881
Subtotal	$ 116,399,228	$ 24,755,624	$ 141,154,852	$ 132,577,831
Unobligated balance:				
Apportioned	$ 13,683,673	$ 289,435	$ 13,973,108	$ 13,697,001
Exempt from apportionment	0	0	0	0
Other available	0	0	0	0
Unobligated Balances Not Available	1,883,998	2,170,890	4,054,888	998,235
Total, Status of Budgetary Resources	$ 131,966,899	$ 27,215,949	$ 159,182,848	$ 147,273,067
RELATIONSHIP OF OBLIGATIONS TO OUTLAYS:				
Obligated Balance, Net-beginning of period	$ 59,338,256	$ 4,182,638	$ 63,520,894	$ 56,100,186
Obligated Balance transferred, net (+/-)	0	0	0	0
Obligated Balance, net-end of period:				
Accounts Receivable	(440,504)	(97,056)	(537,560)	(897,842)
Unfilled customer order from Federal sources	(2,672,247)	(130,735)	(2,802,982)	(2,335,476)
Undelivered Orders	59,698,095	4,025,660	63,723,755	63,419,000
Accounts Payable	2,903,749	569,261	3,473,010	3,335,212
Outlays:				
Disbursements	109,478,103	17,477,216	126,955,319	119,051,033
Collections	(7,383,345)	(379,315)	(7,762,660)	(6,732,714)
Subtotal	$ 102,094,758	$ 17,097,901	$ 119,192,659	$ 112,318,319
Less: Offsetting receipts	$ (115,027)	$ 0	$ (115,027)	$ (246,802)
Net Outlays	$ 101,979,731	$ 17,097,901	$ 119,077,632	$ 112,071,517

Department of Defense
Department of the Navy
COMBINING STATEMENT OF FINANCING
For the years ended September 30, 2004 and 2003
($ in thousands)

	Navy	Marine Corps	2004 Combined	2003 Combined
Resources Used to Finance Activities:				
Budgetary Resources Obligated				
Obligations Incurred	$ 116,399,228	$ 24,755,624	$ 141,154,852	$ 132,577,831
Less: Spending Authority from offsetting collections and recoveries (-)	(14,153,633)	(7,473,232)	(21,626,865)	(12,838,803)
Obligations net of offsetting collections and recoveries	$ 102,245,595	$ 17,282,392	$ 119,527,987	$ 119,739,028
Less: Offsetting receipts (-)	(115,027)	0	(115,027)	(246,802)
Net obligations	$ 102,130,568	$ 17,282,392	$ 119,412,960	$ 119,492,226
Other Resources				
Donations and forfeitures of property	0	0	0	0
Transfers in/out without reimbursement (+/-)	16,775	(4,892)	11,883	51,765
Imputed financing from costs absorbed by others	523,359	61,850	585,209	509,719
Other (+/-)	0	0	0	0
Net other resources used to finance activities	$ 540,134	$ 56,958	$ 597,092	$ 561,484
Total resources used to finance activities	$ 102,670,702	$ 17,339,350	$ 120,010,052	$ 120,053,710
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 (-)	$ 2,650,383	$ (854,173)	$ 1,796,210	$ (3,213,420)
Unfilled Customer Orders	513,076	10,440	523,516	248,440
Resources that fund expenses recognized in prior periods	(104,796)	(10,326)	(115,122)	(31,284)
Budgetary offsetting collections and receipts that do not affect Net Cost of Operations	0	0	0	0
Resources that finance the acquisition of assets	(12,412,218)	0	(12,412,218)	(26,444,222)
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	0
Other (+/-)	(16,775)	4,892	(11,883)	0
Total resources used to finance items not part of the Net Cost of Operations	$ (9,370,330)	$ (849,167)	$ (10,219,497)	$ (29,440,486)
Total resources used to finance the Net Cost of Operations	$ 93,300,372	$ 16,490,183	$ 109,790,555	$ 90,613,224

Department of Defense
Department of the Navy
COMBINING STATEMENT OF FINANCING
For the years ended September 30, 2004 and 2003
($ in thousands)

	Navy	Marine Corps	2004 Combined	2003 Combined
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 Periods:				
Increase in annual leave liability	$ 188,260	$ 0	$ 188,260	$ 0
Increase in environmental and disposal liability	427,489	0	427,489	0
Upward/Downward reestimates of credit subsidy expense (+/-)	0	0	0	0
Increase in exchange revenue receivable from the public (-)	0	0	0	0
Other (+/-)	10,245	182,998	193,243	428,344
Total components of Net Cost of Operations that will require or generate resources in future periods	$ 625,994	$ 182,998	$ 808,992	$ 428,344
Components not Requiring or Generating Resources:				
Depreciation and amortization	$ 15,721,991	$ 1,753,871	$ 17,475,862	$ 16,936,476
Revaluation of assets and liabilities (+/-)	1,367,930	(253,890)	1,114,040	3,203,729
Other (+/-)				
Trust Fund Exchange Revenue	(30,297)	0	(30,297)	0
Cost of Goods Sold	0	0	0	0
Operating Materials and Supplies Used	234,481	36,486	270,967	0
Other	(31,808)	44,092	12,284	22,920
Total components of Net Cost of Operations that will not require or generate resources	$ 17,262,297	$ 1,580,559	$ 18,842,856	$ 20,163,125
Total components of Net Cost of Operations that will not require or generate resources in the current period	$ 17,888,291	$ 1,763,557	$ 19,651,848	$ 20,591,469
Net Cost of Operations	$ 111,188,663	$ 18,253,740	$ 129,442,403	$ 111,204,693

Department of the Navy

General Fund Required Supplementary Stewardship Information

MILITARY EQUIPMENT

Narrative Statement

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. Therefore, RSSI reporting of military equipment has been terminated.

HERITAGE ASSETS

For Fiscal Year Ended September 30, 2004

(a)	(b) Measurement Quantity	(c) As of 10/01/03	(d) Additions	(e) Deletions	(f) As of 9/30/04
Museums	Each	27	0	0	27
Monuments & Memorials	Each	511	37	26	522
Cemeteries	Sites	58	1	0	59
Archeological Sites	Sites	23,262	0	0	23,262
Buildings and Structures	Each	9,092	0	0	9,092
Major Collections (See Supplemental Reporting)	Each				

Narrative Statement

The Department of the Navy (DON) is required to report Heritage Assets in accordance with the following public laws:

- 10 USC 2721
- USC 483(b)
- Antiquities Act of 1906
- Historic Sites Act of 1935
- USC 470 National Historic Preservation Act of 1966
- National Environmental Policy Act of 1969
- American Indian Religious Freedom Act of 1978
- Archeological Resources Protection Act of 1979
- Native American Graves Protection & Repatriation Act of 1990
- Presidential Memorandum for Heads of Executive Departments and Agencies: Government to Government Relations with Native American Tribal Governments Act of 1994
- 36 CFR 79 - Curation of Federally Owned and Administered Archeological Collections

In general, the DON defines Heritage Assets as items that are unique for one or more of the following reasons: historical or natural significance; cultural, educational or artistic importance, or significant architectural characteristics.

Explanation for adjustments, additions, and deletions.

In FY 2004 adjustments to museums, cemeteries and monuments were made to reflect assets acquired in prior years that were not previously reported.

Accurate inventory data for archaeological artifacts, archaeological sites, and buildings and structures are pending full implementation of tracking systems, notably iNFADS and DONHAMS, and related use of historic property data elements for buildings and structures.

Process used to define assets as Heritage Assets. The processes used to define items as having heritage significance varies between categories and type of assets being evaluated. Subject matter experts, including historians and curators, play a significant role in the definition process in addition to other criteria such as listing on the National Register of Historic Places. In all cases, a myriad of federal statutes, service regulations, and other guidelines mandate heritage significance or provide guidance in its determination.

Multi-Use Heritage Assets. Per DoD FMR Volume 6B, Multi-Use Heritage Assets are reported both as Heritage Assets on the RSSI and on the Balance Sheet.

Information Pertaining to the Condition of DON Heritage Assets. The methodology used to report the condition of the heritage assets was a combination of visual assessment of the objects, historic value to the DON collection, and general display and storage standards for historic collections. The overall condition of the collection objects is good.

Museums
Museums are buildings, places, or institutions devoted to the acquisition, conservation, study, exhibition, and educational interpretation of objects having scientific, historical, or artistic value.

Monuments and Memorials
Monuments and Memorials have significant monetary and/or historical value to the DON.

Cemeteries
Cemeteries are government owned burial grounds of which gravesites of prominent historical figures are located.

Archeological Sites
Archeological Sites are lands on which items of significance are located.

Buildings and Structures
Buildings and Structures are listed on or determined eligible for listing on the National Register of Historic Places, including Multi-use Heritage Assets. Criteria for evaluating National Register eligibility of these sites may be referenced at 36 CFR 60.4.

Supplemental Reporting. In addition to the data presented in the table above, the following supplemental information was reported as of 9/30/04:

Category	Measurement Quantity	As of 10/01/03	Additions	Deletions	As of 9/30/04
Archeological Artifacts	Cubic Feet	13,749	0	0	13,749
Archival	Linear Feet	96,222	751	2,757	94,216
Artwork	Item	37,380	567	0	37,947
Historical Artifacts	Item	1,114,407	10,712	2	1,125,117

Archival
The FY 2003 ending balance was adjusted downward by 30,404 resulting in an FY 2004 beginning balance of 96,222. This adjustment reflects the correction of an error in the prior reporting period.

Stewardship Land

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

(a) Land Use	(b) As of 10/01/03	(c) Additions	(d) Deletions	(e) As of 9/30/04
1. Mission	2,021	5	0	2,026
2. Parks & Historic Sites	0	0	0	0
Totals	2,021	5	0	2,026

Narrative Statement
The DON followed the definition of Stewardship Land per DoD Guidance to include Public Domain, Land Set Aside, and Donated Land. The iNFADS was used to derive acres for Stewardship Land. Within the definition of Stewardship Land, land can be further defined as improved, semi-improved and other categories of land.

Non-Federal Physical Property

The Department of the Navy does not fund this type of Activity.

Investments in Research and Development

For Fiscal Years 2000 through 2004
(In Millions of Dollars)

(a) Categories	(b) FY00	(c) FY01	(d) FY02	(e) FY03	(f) FY04
1. Basic Research	$345	$383	$378	$399	$431
2. Applied Research	538	597	647	743	686
3. Development					
Advanced Technology Development	607	738	779	836	967
Advanced Component Development And Prototypes	2,216	2,418	2,415	2,536	2,361
System Development and Demonstration	2,225	2,086	2,836	4,200	6,115
Research, Development, Test, and Evaluation Management Support	750	782	838	797	906
Operational Systems Development	2,047	2,266	2,417	2,385	1,820
Total	$8,728	$9,270	$10,310	$11,896	$13,286

Narrative Statement

Investments in Research and Development

Investment values included in this Report are based on Research and Development (R&D) outlays (expenditures). Outlays are used because current DON systems are unable to fully capture and summarize costs in accordance with FASAB standards.

A. Basic Research

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 fuller knowledge or understanding of the subject under study. Major outputs are scientific studies and research papers.

The following are two representative program examples for the Basic Research category.

Converting Waste Heat Into Electricity

The excess heat produced in everything from microelectronics to large ship engines is generally thought of as a problem for engineers to solve. A new scientific leap discovered in semiconductor technology funded by the Office of Naval Research could put that troublesome heat to good use. Funded through a Multi-University Research Initiative (MURI), a Michigan State group has developed a fundamental understanding of the chemical properties needed to create the ideal material with high electrical conductivity but low thermal conductivity. The group has found the right combination of ultrapure lead, antimony, silver, and tellurium for a material (called LAST) that is significantly more efficient for high temperature power generation than existing thermoelectric materials. The secret to the new material's efficiency seems to be in the nanostructures within it that impede the flow of heat by introducing internal boundaries.

NOAA and U.S. Navy Uncover Secrets of Lost Civil War Submarine USS Alligator

The U.S. Department of Commerce's National Oceanic and Atmospheric Administration (NOAA) and the U.S. Navy's Office of Naval Research (ONR) have joined forces to uncover the secrets of a technological marvel of the Civil War era akin to the USS *Monitor* and the CSS *Hunley*: the USS *Alligator*. Launched in 1862, the *Alligator* was the U.S. Navy's first submarine. While the vessel represented a significant leap forward in naval engineering, complete information about its design and fate has been elusive. Recently, NOAA and ONR released findings that help fill large gaps in the history of the all-but-forgotten Union submarine, including details about the *Alligator's* inventor, innovative features and its loss in April 1863.

NOAA and ONR initiated the *Alligator* Project in 2002 in an effort to shed new light on America's maritime heritage. In October 2003, at a special symposium, NOAA and ONR brought together experts in naval history, maritime archaeology, oceanography, engineering and ocean exploration to exchange information about the *Alligator* and discuss the possibility of locating and recovering this historic vessel.

B. Applied Research

Applied Research is the systematic study to gain knowledge or understanding necessary for determining the means by which a recognized and specific need may be met. It is the practical application of such knowledge or understanding for the purpose of meeting a recognized need. This research points toward specific military needs with a view toward developing and evaluating the feasibility and practicability of proposed solutions and determining their parameters. 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 nonsystem specific development efforts.

The following are two representative program examples for the Applied Research category.

Free-Electron Laser Reaches 10 Kilowatts

The Free-Electron Laser (FEL), supported by the Office of Naval Research and located at the U.S. Department of Energy's Thomas Jefferson National Accelerator Facility, achieved 10 kilowatts of infrared laser light in late July, making it the most powerful tunable laser in the world. The recently upgraded laser's new capabilities will enhance defense and manufacturing technologies, and support advanced studies of chemistry, physics, biology, and more.

The FEL program began as the One-Kilowatt Demonstration FEL, which broke power records and made its mark as the world's brightest high average power laser. It delivered 2.1 kilowatts (kW) of infrared light, more than twice it was initially designed to achieve, before it was taken offline in November 2001 for an upgrade to 10 kW. The FEL provides intense beams of laser light that can be tuned to a precise wavelength, and which are more powerful than beams from a conventional laser. Conventional lasers are limited in the wavelength of light they emit by the source of the electrons (such as a gas or crystal) used within the laser.

ONR manages the FEL development effort in cooperation with the Naval Sea Systems Command (NAVSEA) Directed Energy and Electric Weapons Office. ONR is also funding the operation and optimization of the 10 kW FEL, and has several experiments slated to begin in early fall 2004. The Navy intends on using the lessons learned from the development of the 10 kW FEL to begin design and construction of a 100 kW FEL over the next four years. Eventually, the Navy plans on moving the 100 kW laser to an over water test site, and scaling the power up to megawatt levels.

"Brain-Based" Control for Unmanned Vehicles

This summer at the Naval Undersea Warfare Center in Newport, RI, a mobile autonomous research vehicle (MARV) fitted with an agile "brain-based" controller attempted to smoothly and quietly maneuver itself in and out of a docking tube. This tricky feat could be critical to future missions in which Unmanned Underwater Vehicles might carry out missions too dangerous for humans.

ONR's project sponsor reported that the controller, developed jointly by Russia's Nizhny Novgorod State University and Institute for Applied Sciences and New York University Medical School, mimics the part of the human brain that controls balance and limb movement, known as the olivo-cerebellar system. The controller can be used to replicate not only the human body's ability to carry out complex maneuvers but also, for example, the wing control of birds and insects as they adjust their angles of flight. In the case of the MARV, the controller will manipulate the movements of high-lift actuators that change the direction and speed of the vehicle's motion. This capability could be exploited both by autonomous military and commercial systems that require highly precise movement control.

C. Development

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. Advance Technology Development is the systematic use of the knowledge or understanding gained from research directed toward proof of technological feasibility and assessment of operational and producibility rather than the development of hardware for service use. Employs demonstration activities intended to prove or test a technology or method.

2. Advanced Component Development and Prototypes evaluates integrated technologies in as realistic an operating environment as possible to assess the performance or cost reduction potential of advanced

technology. Programs in this phase are generally system specific. Major outputs of Advanced Component Development and Prototype are hardware and software components, or complete weapon systems, ready for operational and developmental testing and field use.

3. System Development and Demonstration concludes the program or project and prepares it for production. It consists primarily of preproduction efforts, such as logistics and repair studies. Major outputs are weapons systems finalized for complete operational and development testing.

4. 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 analyzes in support of the R&D program.

5. Operational Systems Development is concerned with development projects in support of programs or upgrades still in engineering and manufacturing development, which have received approval for production, for which production funds have been budgeted in subsequent fiscal years.

The following are two representative program examples for the Development category.

Clearing Antennas for Better Communication

In August, the Office of Naval Research tested a concept that aims to bring down the number of antennas used for receiving and transmitting radio-frequency (RF) signals because each antenna requires a costly support system, and the antennas interfere with one another.

The advanced multi-function radio frequency concept, or AMRF-C, is developing electronic modules and software to enable a limited number of transmit and receive antennas to handle multiple communications, radar, and electronic warfare (EW) functions. The goal is to halt the proliferation of so-called "stovepipes"-systems tailored for a single function such as super-high-frequency satellite communications or extremely low-frequency submarine contacts. Specialized computers, power hookups, and maintenance support for each antenna means higher costs, and risks, when they fail. The dissimilar antennas can interfere with one another or other ship systems, and degrade performance, thereby forcing ships to limit strictly the operations of certain RF systems when others are needed.

Hybrids on the High Sea; Fuel Cells for Future Ships

As hybrid electric cars become more commonplace on America's highways, the Navy is working to bring hybrid electric ships to the high seas. The Office of Naval Research (ONR) is developing innovative propulsion systems based on new fuel-cell technology for efficient generation of electrical power-and greater design flexibility-for future ships.

To ensure a relatively quick transition to this promising technology, ONR is funding development of a method to extract hydrogen from diesel fuel. A diesel reforming system would take advantage of the relative low cost of the fuel and the Navy's established infrastructure for buying, storing, and transporting it.

ONR is testing a 500-kilowatt diesel fuel reformer, or "integrated fuel processor," that is compatible with a proton exchange membrane (PEM) fuel cell, at the Department of Energy Idaho National Engineering and Environmental Laboratory in Idaho Falls. The testing will continue to prove out the reforming process. ONR is also looking at design approaches to reduce the size of the processor, which consists of an arrangement of valves, water-gas shift reactors, an oxidizer, and other components, so that it won't take up too much space on a Navy ship.

Department of the Navy

General Fund Required Supplementary Information

Department of Defense
Department of the Navy
DISAGGREGATED STATEMENT OF BUDGETARY RESOURCES
For the years ended September 30, 2004 and 2003
($ in thousands)

	Other	Research, Development, Test & Evaluation	Operation and Maintenance	Procurement
BUDGETARY FINANCING ACCOUNTS				
BUDGETARY RESOURCES				
Budget Authority				
Appropriations Received	$ 323,507	$ 15,140,383	$ 38,835,051	$ 31,533,801
Borrowing Authority	0	0	0	0
Contract Authority	0	0	0	0
Net transfers (+/-)	(254,929)	(83,036)	689,364	(176,811)
Other	0	0	0	0
Unobligated Balance:				
Beginning of period	100,536	1,422,855	858,590	11,221,811
Net transfers, actual (+/-)	0	7,500	118,953	203,208
Anticipated Transfers Balances	0	0	0	0
Spending Authority from Offsetting Collections:				
Earned				
Collected	0	308,474	5,198,785	1,023,564
Receivable from Federal sources	0	1,715	(94,312)	(256,342)
Change in unfilled customer orders				
Advances received	0	0	61,782	0
Without advance from Federal sources	0	263,623	12,972	154,176
Anticipated for the rest of year, without advances	0	0	0	0
Transfers from trust funds	0	0	0	0
Subtotal	$ 0	$ 573,812	$ 5,179,227	$ 921,398
Recoveries of prior year obligations	$ 1,058	$ 750,964	$ 2,926,779	$ 4,003,086
Temporarily not available pursuant to Public Law	0	0	0	0
Permanently not available	(1,963)	(205,340)	(732,515)	(520,019)
Total Budgetary Resources	$ 168,209	$ 17,607,138	$ 47,875,449	$ 47,186,474
STATUS OF BUDGETARY RESOURCES				
Obligations Incurred				
Direct	$ (22,618,778)	$ 15,667,733	$ 53,145,441	$ 41,032,035
Reimbursable	22,762,495	(236,177)	(8,201,287)	(5,319,061)
Subtotal	$ 143,717	$ 15,431,556	$ 44,944,154	$ 35,712,974
Unobligated balance				
Apportioned	$ 24,492	$ 2,031,771	$ 127,502	$ 10,863,766
Exempt from apportionment	0	0	0	0
Other available	0	0	0	0
Unobligated Balances Not Available	0	143,812	2,803,794	609,734
Total, Status of Budgetary Resources	$ 168,209	$ 17,607,139	$ 47,875,450	$ 47,186,474
RELATIONSHIP OF OBLIGATIONS TO OUTLAYS:				
Obligated Balance, Net-beginning of period:	$ 102,743	$ 6,135,287	$ 15,805,153	$ 37,672,898
Obligated Balance transferred, net (+/-)	0	0	0	0
Obligated Balance, net-end of period:				
Accounts Receivable	$ 0	$ (3,842)	$ (218,866)	$ (133,595)
Unfilled customer order from Federal sources	0	(283,282)	(1,855,180)	(11,204)
Undelivered Orders	(840,309)	6,392,738	15,825,519	39,395,853
Accounts Payable	906,061	1	211,325	1,217,804
OUTLAYS:				
Disbursements	$ 179,649	$ 14,444,925	$ 43,941,070	$ 29,016,095
Collections	0	(308,474)	(5,260,567)	(1,023,564)
Subtotal	$ 179,649	$ 14,136,451	$ 38,680,503	$ 27,992,531
Less: Offsetting receipts	(115,027)	0	0	0
Net Outlays	$ 64,622	$ 14,136,451	$ 38,680,503	$ 27,992,531

Department of Defense
Department of the Navy
DISAGGREGATED STATEMENT OF BUDGETARY RESOURCES
For the years ended September 30, 2004 and 2003
($ in thousands)

	Military Personnel	Military Construction/ Family Housing	2004 Combined	2003 Combined
BUDGETARY FINANCING ACCOUNTS				
BUDGETARY RESOURCES				
Budget Authority				
Appropriations Received	$ 36,602,056	$ 1,513,679	$ 123,948,477	$ 122,169,428
Borrowing Authority	0	0	0	0
Contract Authority	0	0	0	739
Net transfers (+/-)	242,821	7,700	425,109	1,662,142
Other	0	0	0	0
Unobligated Balance:				
Beginning of period	177,408	914,037	14,695,238	11,908,983
Net transfers, actual (+/-)	(114,161)	(19,550)	195,950	145,546
Anticipated Transfers Balances	0	0	0	0
Spending Authority from Offsetting Collections:				
Earned				
Collected	463,167	712,659	7,706,650	6,792,556
Receivable from Federal sources	(45,641)	34,296	(360,284)	(1,211,532)
Change in unfilled customer orders				
Advances received	0	(5,771)	56,010	(59,842)
Without advance from Federal sources	323	36,413	467,506	308,282
Anticipated for the rest of year, without advances	0	0	0	0
Transfers from trust funds	0	0	0	0
Subtotal	$ 417,849	$ 777,597	$ 7,869,882	$ 5,829,464
Recoveries of prior year obligations	$ 6,056,640	$ 18,454	$ 13,756,981	$ 7,009,339
Temporarily not available pursuant to Public Law	0	0	0	0
Permanently not available	(137,391)	(111,560)	(1,708,789)	(1,452,574)
Total Budgetary Resources	$ 43,245,222	$ 3,100,357	$ 159,182,848	$ 147,273,067
STATUS OF BUDGETARY RESOURCES				
Obligations Incurred				
Direct	$ 44,089,514	$ 952,578	$ 132,268,522	$ 124,497,950
Reimbursable	(1,320,441)	1,200,802	8,886,330	8,079,881
Subtotal	$ 42,769,073	$ 2,153,380	$ 141,154,852	$ 132,577,831
Unobligated balance				
Apportioned	$ 9,215	$ 916,363	$ 13,973,107	$ 13,697,001
Exempt from apportionment	0	0	0	0
Other available	0	0	1	0
Unobligated Balances Not Available	466,934	30,614	4,054,888	998,235
Total, Status of Budgetary Resources	$ 43,245,222	$ 3,100,357	$ 159,182,848	$ 147,273,067
RELATIONSHIP OF OBLIGATIONS TO OUTLAYS:				
Obligated Balance, Net-beginning of period:	$ 2,100,639	$ 1,704,174	$ 63,520,894	$ 56,100,186
Obligated Balance transferred, net (+/-)	0	0	0	0
Obligated Balance, net-end of period:				
Accounts Receivable	$ (53,914)	$ (127,342)	$ (537,560)	$ (897,842)
Unfilled customer order from Federal sources	631	(653,946)	(2,802,982)	(2,335,476)
Undelivered Orders	909,797	2,040,156	63,723,755	63,419,000
Accounts Payable	907,837	229,981	3,473,010	3,335,213
OUTLAYS:				
Disbursements	$ 37,094,039	$ 2,279,541	$ 126,955,319	$ 119,051,033
Collections	(463,167)	(706,888)	(7,762,660)	(6,732,714)
Subtotal	$ 36,630,872	$ 1,572,653	$ 119,192,659	$ 112,318,319
Less: Offsetting receipts	0	0	(115,027)	(246,802)
Net Outlays	$ 36,630,872	$ 1,572,653	$ 119,077,632	$ 112,071,517

DON General Property, Plant, and Equipment

Real Property Deferred Annual Sustainment and Restoration Tables
As of September 30, 2004
($ in Millions)

Annual Sustainment FY 2004			
	Required	**Actual**	**Difference**
Navy	1,283	795	488
Marine Corps	553	529	24
Building, Structures, and Utilities	1,836	1,324	512

Annual Deferred Sustainment Trend				
	FY 2001	**FY 2002**	**FY 2003**	**FY 2004**
Navy	-	-	-	488
Marine Corps	-	-	-	24
Building, Structures, and Utilities	501	40	346	512

Restoration and Modernization Requirements			
	End FY 2003	**End FY 2004**	**Change**
Navy			
Marine Corps			
Building, Structures, and Utilities	-	-	-

Narrative Statement:

Fiscal Year 2004 represents the third year in which the Facility Sustainment Model (FSM) was utilized. Deferred amounts were calculated in accordance with the methodology provided by DoD Financial Management Regulation, Volume 6B, Chapter 12. The output of the Facility Sustainment Model continues to undergo quality checks to ensure its accuracy. Accordingly, requirements for each fiscal year are prepared with a more updated and accurate version of the model.

In FY 2004, FSM version 4.0 was used for programming and budgeting facilities sustainment.

This year represents the first year that separate breakout of Navy and Marine Corps sustainment amounts can be provided.

The Department of the Navy General Fund has no material amounts of deferred sustainment for the General Property, Plant, and Equipment categories of Personal Property, Heritage Assets, or Stewardship Land.

Military Equipment

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

Major Type	Amount
1. Aircraft	$ 98,885
2. Ships	97,642
3. Missiles	66,444
4. Combat Vehicles	40,193
5. Other Weapons Systems	143,964
6. Total	$ 447,128

Narrative Statement:

Aircraft Deferred Maintenance

There are four sub-categories, which comprise aircraft, deferred maintenance: airframe rework and maintenance (active and reserve), engine rework and maintenance (active and reserve), component repair and software maintenance. The airframe rework deferred maintenance calculation reflects executable unfunded requirements, which represent aircraft that failed Aircraft Service Period Adjustment (ASPA) or reached fixed Period End Date (PED) at year-end. The engine rework deferred maintenance calculation reflects year-end actual requirements minus actual funded units. Component repair deferred maintenance cost represents the difference between the validated requirement and funding. Aircraft deferred maintenance reflects only executable deferred maintenance. Unexecutable deferred maintenance is not reported for airframe rework, engine rework and component repair, nor is it collected.

The Depot maintenance is currently being performed under both the Standard Depot Level Maintenance (SDLM) and Integrated Maintenance Concept (IMC) programs. Currently, the C-130, E-2C, EA-6B, F/A-14, F/A-18, H-60, UH-1N, and S-3 aircraft programs have been incorporated under the IMC concept. The IMC concept uses Planned Maintenance Intervals (PMI), performing more frequent depot maintenance, with smaller work packages, thereby reducing out of service time. The goal of this program is to improve readiness while reducing operating and support costs. Commander, Naval Air Systems Command's (COMNAVAIRSYSCOM) Industrial Strategy is to maintain the minimum level of organic capacity, consistent with force levels, that is necessary to sustain peacetime readiness and maintain fighting surge capability. COMNAVAIRSYSCOM works in partnership with private industry to make maximum use of industry's production capabilities and for non-core related aviation depot level maintenance.

Ship Deferred Maintenance

Fleet Type Commanders provided deferred Ship Maintenance data. Data was collected from the Current Ships' Maintenance Plan (CSMP) database, which captures maintenance actions at all levels (organizational, intermediate, depot) for active and reserve ships. Only depot level deferred maintenance has been provided in this report. This includes maintenance actions that were deferred from actual depot maintenance work packages as well as maintenance actions that were deferred prior to inclusion in a work package due to fiscal, operational, or capacity constraints. Although there is a significant amount of deferred maintenance actions, there are no ships that fall into the category of "unacceptable operating condition". Any ship that would be at risk of being in unacceptable operating condition would receive priority for maintenance funding to maintain acceptable operating condition.

Missile Maintenance
Four categories are used to determine missile maintenance: missiles, tactical missiles, software maintenance, and other. Deferred maintenance is defined as the difference between the total weapon maintenance requirement as determined by requirements modeling processes and the weapon maintenance that is funded in accordance with the annual budget controls for the Missile Maintenance program. The maintenance requirements model projects the quantity of missiles and missile components per weapon system that are required to be maintained (reworked) annually.

Combat Vehicles
The combat vehicles category is for vehicle overhaul for the active and reserve Marine Corps.

Other Weapons System
The "Other Weapons System" category is comprised of ordnance, end item maintenance for support equipment, camera equipment, landing aids, calibration equipment, air traffic control equipment, target systems, expeditionary airfield equipment, special weapons, target maintenance, and repair of repairables. Three categories define ordnance maintenance: ordnance maintenance, software maintenance and other. Although the various programs vary in the methodology in defining requirements, all programs define deferred maintenance as the difference between requirements and funding.

Software Maintenance
Software maintenance requirements and deferred maintenance for aircraft, missiles and other equipment are determined using the same methodology and, therefore will not be addressed separately for each Military Equipment Deferred Maintenance reporting categories. Software maintenance includes the operational and system test software that runs in the airborne avionics systems (e.g., mission computer, display computer, radar) and the software that runs the ground based support lab's used to perform software sustainment (e.g., compilers, editors, simulation, configuration management). The deferred maintenance reported for the execution year are those requirements below the funding threshold and up to, but not exceeding, the capacity of the Software Support Activity (SSA) in that particular fiscal year. There may be deferred requirements that exceed the capacity of the SSA, but these are not reported in the Exhibit OP-30 for the execution year, but rather identified as an out year requirement.

Schedule, Part A DoD Intra-governmental Asset Balances *($ Amounts in Thousands)*	Treasury Index	Fund Balance with Treasury	Accounts Receivable	Loans Receivable	Investments	Other
Government Printing Office	4		$ 10			
The Judiciary	10		22			
Department of Commerce	13		1,975			
Department of the Interior	14		271			$ 177,407
Department of Justice	15		3,136			
Department of Labor	16		73			59
United States Postal Service	18		14			
Department of State	19		3,924			
Department of the Treasury	20	$ 82,093,913	1,496		$ 9,481	
Department of the Army	21		38,049			154
Nuclear Regulatory Commission	31		38			
Department of Veterans Affairs	36		13			
General Services Administration	47		3,480			
National Science Foundation	49		563			212
Department of the Air Force	57		15,358			75,516
Federal Emergency Management Agency	58		139			
Environmental Protection Agency	68					1,077
Department of Transportation	69		385			2,643
Homeland Security	70		6,461			
Department of Health and Human Services	75		92			24
National Aeronautics and Space Administration	80		9,629			395
Department of Housing and Urban Development	86		9			
Department of Energy	89		401			1,144
Department of Education	91		167			
US Army Corps of Engineers	96		1,657			
Other Defense Organizations General Funds	97		67,507			4
Other Defense Organizations Working Capital Funds	97-4930		30,396			14,010
Army Working Capital Fund	97-4930.001		8,638			11
Navy Working Capital Fund	97-4930.002		56,800			
Air Force Working Capital Fund	97-4930.003					66
Totals might not match reports.	**Totals**	$ 82,093,913	$ 250,703	$ 0	$ 9,481	$ 272,722

Schedule, Part B DoD Intra-governmental Entity Liabilities *($ Amounts in Thousands)*	Treasury Index	Accounts Payable	Debts/Borrowings From Other Agencies	Other
Library of Congress	3	$ 12		
Department of Agriculture	12	550		
Department of the Interior	14	15,441		
Department of Justice	15	17		
Department of Labor	16			$ 642,613
Department of State	19	14,306		
Department of the Treasury	20	47		41,833
Department of the Army	21	59,749		
Office of Personnel Management	24	1		52,834
Federal Communications Commission	27	438		
Nuclear Regulatory Commission	31	44		
Department of Veterans Affairs	36	6,676		
General Services Administration	47	226,749		
National Science Foundation	49	913		
Department of the Air Force	57	4,792		
Tennessee Valley Authority	64	813		
Environmental Protection Agency	68	426		
Department of Transportation	69	-		
Homeland Security	70	17,766		
Department of Health and Human Services	75	44		
National Aeronautics and Space Administration	80	4,370		
Department of Energy	89	107,944		
US Army Corps of Engineers	96	147		
Other Defense Organizations General Funds	97	52,967		472
Other Defense Organizations Working Capital Funds	97-4930	336,552		
Army Working Capital Fund	97-4930.001	14,767		
Navy Working Capital Fund	97-4930.002	568,385		
Air Force Working Capital Fund	97-4930.003	3,701		
The General Fund of the Treasury	99			3,247,050
Totals might not match reports.	**Totals:**	**$ 1,437,617**	**$ 0**	**$ 3,984,802**

Schedule, Part C DoD Intragovernmental revenue and related costs *($ Amounts in Thousands)*	Treasury Index	Earned Revenue
Government Printing Office	4	$ 41
Executive Office of the President	11	73,227
Department of Agriculture	12	24,068
Department of Commerce	13	19,578
Department of the Interior	14	618
Department of Justice	15	17,855
Department of Labor	16	2
United States Postal Service	18	9
Department of State	19	40,740
Department of the Treasury	20	8,966
Department of the Army	21	208,864
Nuclear Regulatory Commission	31	345
Department of Veterans Affairs	36	227
General Service Administration	47	1,377
National Science Foundation	49	2,003
Department of the Air Force	57	201,169
Federal Emergency Management Agency	58	682
Department of Transportation	69	4,081
Homeland Security	70	45,702
Agency for International Development	72	1
Small Business Administration	73	(2)
Department of Health and Human Services	75	465
National Aeronautics and Space Administration	80	17,820
Department of Housing and Urban Development	86	7,798
Department of Energy	89	8,568
Department of Education	91	1,142
US Army Corps of Engineers	96	3,282
Other Defense Organizations General Funds	97	800,104
Other Defense Organizations Working Capital Funds	97-4930	190,129
Army Working Capital Fund	97-4930.001	40,394
Navy Working Capital Fund	97-4930.002	1,423,377
Air Force Working Capital Fund	97-4930.003	-
DoD Medicare-Eligible Retiree Health Care Fund		130,228
Total might not match reports.	**Total:**	**$ 3,272,860**

Schedule, Part E DoD Intragovernmental non-exchange revenues			
($ Amounts in Thousands)	**Treasury Index**	**Transfers In**	**Transfers Out**
Department of the Air Force	57	$ (2,809)	0
Other Defense Organizations General Funds	97	14,489	0
Other Defense Organizations Working Capital Funds	97-4930	121,026	0
Navy Working Capital Fund	97-4930.002	45,177	0
Total might not match reports.	**Total**	$ 177,883	0

Department of the Navy

General Fund Other Accompanying Information

Appropriations, Funds, and Accounts Included in the Principal Statements

Entity Accounts:

General Funds

17X0380	Coastal Defense Augmentation, Navy
17 0703	Family Housing Construction, Navy and Marine Corps
17 0735	Family Housing, Navy and Marine Corps (Operations and Maintenance)
17X0810	Environmental Restoration, Navy
17 1105	Military Personnel, Marine Corps
17 1106	Operation and Maintenance, Marine Corps
17 1107	Operation and Maintenance, Marine Corps Reserve
17 1108	Reserve Personnel, Marine Corps
17 1109	Procurement, Marine Corps
17 1205	Military Construction, Navy
17 1235	Military Construction, Naval Reserve
17X1236	Payments to Kaho Olawe Island Conveyance, Remediation, and Environmental Restoration Fund, Navy
17 1319	Research, Development, Test, and Evaluation, Navy
17 1405	Reserve Personnel, Navy
17 1453	Military Personnel, Navy
17 1506	Aircraft Procurement, Navy
17 1507	Weapons Procurement, Navy
17 1508	Procurement of Ammunition, Navy and Marine Corps
17 1611	Shipbuilding and Conversion, Navy
17 1804	Operation and Maintenance, Navy
17 1806	Operation and Maintenance, Navy Reserve
17 1810	Other Procurement, Navy

Revolving Funds

17 4557	National Defense Sealift Fund, Navy

Trust Funds

17X8716	Department of the Navy General Gift Fund
17X8723	Ship Stores Profits, Navy
17X8733	United States Naval Academy Gift and Museum Fund

Special Funds

17X5095	Wildlife Conservation, Military Reservations, Navy
17X5185	Kaho Olawe Island Conveyance, Remediation, and Environmental Restoration Fund,
17X5429	Rossmoor Liquidating Trust Settlement Account

Non Entity Accounts:

17 3XXX	Receipt Accounts
17X6XXX	Deposit Funds

Department of the Navy

Navy Working Capital Fund Principal Statements

Principal Statements

The FY 2004 Navy Working Capital Fund Principal Financial Statements and related notes are presented in the format prescribed by the Department of Defense Financial Management Regulation 7000.14, Volume 6B. The statements and related notes summarize financial information for individual activity groups and activities within the Navy Working Capital Fund for the fiscal year ending September 30, 2004, and are presented on a comparative basis with information previously reported for the fiscal year ending September 30, 2003.

The following statements are included in the Navy Working Capital Fund Principal Statements:

- Consolidated Balance Sheet
- Consolidated Statement of Net Cost
- Consolidated Statement of Changes in Net Position
- Combined Statement of Budgetary Resources
- Combined Statement of Financing

The Principal Statements and related notes have been prepared to report financial position pursuant to the requirements of the Chief Financial Officers Act of 1990, as amended by the Government Management Reform Act of 1994.

The accompanying notes should be considered an integral part of the Principal Statements.

Department of Defense
Navy Working Capital Fund
CONSOLIDATED BALANCE SHEET
As of September 30, 2004 and 2003
($ in thousands)

	2004 Consolidated	2003 Consolidated Restated
ASSETS (Note 2)		
Intragovernmental:		
Fund Balance with Treasury (Note 3)		
Entity	$ 861,243	$ 1,827,646
Non-Entity Seized Iraqi Cash	0	0
Non-Entity - Other	0	0
Investments (Note 4)	0	0
Accounts Receivable (Note 5)	857,519	582,773
Other Assets (Note 6)	15	10,392
Total Intragovernmental Assets	$ 1,718,777	$ 2,420,811
Cash and Other Monetary Assets (Note 7)	$ 0	$ 0
Accounts Receivable (Note 5)	26,190	111,775
Loans Receivable (Note 8)	0	0
Inventory and Related Property (Note 9)	19,239,192	18,256,128
General Property, Plant and Equipment (Note 10)	3,895,542	4,323,910
Investments (Note 4)	0	0
Other Assets (Note 6)	717,191	868,808
TOTAL ASSETS	$ 25,596,892	$ 25,981,432
LIABILITIES (Note 11)		
Intragovernmental:		
Accounts Payable (Note 12)	$ 243,982	$ 313,786
Debt (Note 13)	506,278	615,648
Environmental Liabilities (Note 14)	0	0
Other Liabilities (Note 15 & Note 16)	114,851	289,268
Total Intragovernmental Liabilities	$ 865,111	$ 1,218,702
Accounts Payable (Note 12)	$ 1,862,567	$ 2,102,870
Military Retirement Benefits and Other Employment-Related Actuarial Liabilities (Note 17)	1,168,225	1,409,853
Environmental Liabilities (Note 14)	0	0
Loan Guarantee Liability (Note 8)	0	0
Other Liabilities (Note 15 and Note 16)	5,679,116	4,157,892
Debt Held by Public (Note 13)	0	0
TOTAL LIABILITIES	$ 9,575,019	$ 8,889,317
NET POSITION		
Unexpended Appropriations (Note 18)	$ 0	$ 0
Cumulative Results of Operations	16,021,873	17,092,115
TOTAL NET POSITION	$ 16,021,873	$ 17,092,115
TOTAL LIABILITIES AND NET POSITION	$ 25,596,892	$ 25,981,432

The accompanying notes are an integral part of these statements.

Department of Defense
Navy Working Capital Fund
CONSOLIDATED STATEMENT OF NET COST
For the years ended September 30, 2004 and 2003
($ in thousands)

		2004 Consolidated		2003 Consolidated
Program Costs				
Intragovernmental Gross Costs	$	5,434,981	$	5,422,250
(Less: Intragovernmental Earned Revenue)		(21,698,935)		(21,871,864)
Intragovernmental Net Costs	$	(16,263,954)	$	(16,449,614)
Gross Costs With the Public	$	17,915,614		17,656,253
(Less: Earned Revenue From the Public)		(613,535)		(766,709)
Net Costs With the Public	$	17,302,079	$	16,889,544
Total Net Cost	$	1,038,125	$	439,930
Costs Not Assigned to Programs		0		0
(Less: Earned Revenue Not Attributable to Programs)		0		0
Net Cost of Operations	$	1,038,125	$	439,930

The accompanying notes are an integral part of these statements.

Department of Defense
Navy Working Capital Fund
CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION
For the years ended September 30, 2004 and 2003
($ in thousands)

	Cumulative Results of Operations 2004 Consolidated	Cumulative Results of Operations 2003 Consolidated Restated
Beginning Balances	$ 18,136,830	$ 18,006,706
Prior period adjustments (+/-)	0	0
Prior period adjustments - restated (+/-)	(1,044,715)	(1,044,715)
Beginning Balance, Restated	17,092,115	16,961,991
Prior period adjustments - not restated (+/-)	0	0
Beginning Balances, as adjusted	$ 17,092,115	$ 16,961,991
Budgetary Financing Sources:		
Appropriations Received	$ 0	$ 40,200
Appropriations transferred in/out (+/-)	0	0
Other adjustments (rescissions, etc) (+/-)	0	0
Appropriations used	130,446	(40,200)
Nonexchange revenue	0	0
Donations and forfeitures of cash and cash equivalents	0	0
Transfers in/out without reimbursement (+/-)	(287,800)	0
Other budgetary financing sources (+/-)	(419,775)	0
Other Financing Sources:		
Donations and forfeitures of property	0	0
Transfers in/out without reimbursement (+/-)	126	(13,527)
Imputed financing from costs absorbed by others	544,886	543,381
Other (+/-)	0	0
Total Financing Sources	$ (32,117)	$ 570,054
Net Cost of Operations (+/-)	$ 1,038,125	$ 439,930
Ending Balances	$ 16,021,873	$ 17,092,115

The accompanying notes are an integral part of these statements.

Department of Defense
Navy Working Capital Fund
CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION
For the years ended September 30, 2004 and 2003
($ in thousands)

	Unexpended Appropriations 2004 Consolidated	Unexpended Appropriations 2003 Consolidated Restated
Beginning Balances	$ 0	$ 0
Prior period adjustments (+/-)	0	0
Prior period adjustments, restated (+/-)	0	0
Beginning Balance, Restated	0	0
Prior period adjustments, not restated	0	0
Beginning Balances, as adjusted	$ 0	$ 0
Budgetary Financing Sources:		
Appropriations Received	$ 130,446	$ 40,200
Appropriations transferred in/out (+/-)	0	0
Other adjustments (rescissions, etc) (+/-)	0	0
Appropriations used	(130,446)	(40,200)
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	$ 0	$ 0
Net Cost of Operations (+/-)	$ 0	$ 0
Ending Balances	$ 0	$ 0

The accompanying notes are an integral part of these statements.

Department of Defense
Navy Working Capital Fund
COMBINED STATEMENT OF BUDGETARY RESOURCES
For the years ended September 30, 2004 and 2003
($ in thousands)

	2004 Combined Budgetary Financing Accounts	2003 Combined Budgetary Financing Accounts
BUDGETARY RESOURCES		
Budget Authority:		
Appropriations Received	$ 130,446	$ 40,200
Borrowing Authority	0	0
Contract Authority	355,172	558,144
Net transfers (+/-)	0	0
Other	0	0
Unobligated Balance:		
Beginning of period	4,513,325	4,117,221
Net transfers, actual (+/-)	(287,800)	(30,200)
Anticipated Transfers Balances	0	0
Spending Authority from Offsetting Collections:		
Earned		
Collected	23,926,810	25,585,547
Receivable from Federal sources	249,344	(432,227)
Change in unfilled customer orders		
Advances received	90,067	178,239
Without advance from Federal sources	(1,724,666)	1,964,175
Anticipated for the rest of year, without advances	0	0
Transfers from trust funds	0	0
Subtotal	$ 22,541,555	$ 27,295,734
Recoveries of prior year obligations	$ 0	$ 0
Temporarily not available pursuant to Public Law	0	0
Permanently not available	(186,529)	(204,140)
Total Budgetary Resources	$ 27,066,169	$ 31,776,959
STATUS OF BUDGETARY RESOURCES		
Obligations Incurred:		
Direct	$ 0	$ 0
Reimbursable	24,316,448	27,263,631
Subtotal	$ 24,316,448	$ 27,263,631
Unobligated Balance:		
Apportioned	$ 2,650,776	$ 4,632,115
Exempt from apportionment	0	0
Other available	0	2
Unobligated Balances Not Available	98,945	(118,789)
Total, Status of Budgetary Resources	$ 27,066,169	$ 31,776,959

The accompanying notes are an integral part of these statements.

Department of Defense
Navy Working Capital Fund
COMBINED STATEMENT OF BUDGETARY RESOURCES
For the years ended September 30, 2004 and 2003
($ in thousands)

	2004 Combined Budgetary Financing Accounts	2003 Combined Budgetary Financing Accounts
RELATIONSHIP OF OBLIGATIONS TO OUTLAYS:		
Obligated Balance, Net-beginning of period	$ 3,274,114	$ 2,985,762
Obligated Balance transferred, net (+/-)	0	0
Obligated Balance, Net-end of period:		
Accounts Receivable	(590,442)	(341,097)
Unfilled customer orders from Federal sources	(7,031,461)	(8,756,130)
Undelivered Orders	6,892,059	7,998,442
Accounts Payable	4,968,550	4,372,899
Outlays:		
Disbursements	24,827,178	25,443,332
Collections	(24,016,876)	(25,763,785)
Subtotal	$ 810,302	$ (320,453)
Less: Offsetting receipts	0	0
Net Outlays	$ 810,302	$ (320,453)

The accompanying notes are an integral part of these statements.

Department of Defense
Navy Working Capital Fund
COMBINED STATEMENT OF FINANCING
For the years ended September 30, 2004 and 2003
($ in thousands)

	2004 Combined	2003 Combined
Resources Used to Finance Activities:		
Budgetary Resources Obligated		
Obligations Incurred	$ 24,316,448	$ 27,263,631
Less: Spending Authority from offsetting collections and recoveries (-)	(22,541,554)	(27,295,734)
Obligations net of offsetting collections and recoveries	$ 1,774,894	$ (32,103)
Less: Offsetting receipts (-)	0	0
Net obligations	$ 1,774,894	$ (32,103)
Other Resources		
Donations and forfeitures of property	0	0
Transfers in/out without reimbursement (+/-)	125	(13,527)
Imputed financing from costs absorbed by others	544,886	543,381
Other (+/-)	0	0
Net other resources used to finance activities	$ 545,011	$ 529,854
Total resources used to finance activities	$ 2,319,905	$ 497,751
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 (-)	$ 1,142,521	$ (703,528)
Unfilled Customer Orders	(1,634,601)	2,142,413
Resources that fund expenses recognized in prior periods	(241,627)	0
Budgetary offsetting collections and receipts that do not affect Net Cost of Operations	0	8
Resources that finance the acquisition of assets	(5,045,185)	(1,899,644)
Other resources or adjustments to net obligated resources that do not affect Net Cost of Operations	0	0
Less: Trust or Special Fund receipts related to exchange in the entity's budget (-)	0	0
Other (+/-)	(125)	0
Total resources used to finance items not part of the Net Cost of Operations	$ (5,779,017)	$ (460,751)
Total resources used to finance the Net Cost of Operations	$ (3,459,112)	$ 37,000

The accompanying notes are an integral part of these statements.

Department of Defense
Navy Working Capital Fund
COMBINED STATEMENT OF FINANCING
For the years ended September 30, 2004 and 2003
($ in thousands)

	2004 Combined	2003 Combined
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 Periods:		
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 public (-)	0	0
Other (+/-)	0	83,927
Total components of Net Cost of Operations that will require or generate resources in future periods	$ 0	$ 83,927
Components not Requiring or Generating Resources:		
Depreciation and amortization	$ 255,203	$ 243,755
Revaluation of assets and liabilities (+/-)	42,924	74,973
Other (+/-)		
Trust Fund Exchange Revenue	0	0
Cost of Goods Sold	4,160,738	0
Operating Material & Supplies Used	0	0
Other	38,372	275
Total components of Net Cost of Operations that will not require or generate resources	$ 4,497,237	$ 319,003
Total components of Net Cost of Operations that will not generate resources in the current period	$ 4,497,237	$ 402,930
Net Cost of Operations	$ 1,038,125	$ 439,930

The accompanying notes are an integral part of these statements.

Department of the Navy

Navy Working Capital Fund

Notes to the Principal Statements

Note 1. Significant Accounting Policies

1.A. Basis of Presentation

These financial statements have been prepared to report the financial position and results of operations of the Navy Working Capital Fund (NWCF), as required by the Chief Financial Officers (CFO) 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 NWCF 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 Principals (GAAP). The accompanying financial statements account for all resources for which the NWCF is responsible except that information relative to classified assets, programs, and operations which have been excluded from the statement or otherwise aggregated and reported in such a manner that it is no longer classified. The NWCF financial statements are in addition to the financial reports also prepared by the NWCF pursuant to OMB directives that are used to monitor and control the NWCF use of budgetary resources.

The NWCF is unable to fully implement all elements of Federal GAAP and OMB Bulletin No. 01-09 due to limitations of its financial management processes and systems, including feeder systems and processes. Reported values and information for NWCF major asset and liability categories are derived in part from feeder systems, such as inventory systems 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. The NWCF continues to implement process and system improvements addressing the limitation of its financial and feeder systems. A more detailed explanation of these financial statement elements is provided in the applicable note.

1.B. Mission of the Reporting Entity

The overall mission of the Department of the Navy (DON) is to organize, train, and equip forces to deter aggression and, if necessary, defeat aggressors of the United States and its allies. The NWCF provides goods, services, and infrastructure to DON and other DoD customers to help ensure our military forces are mobile, ready, and have the most advanced technology.

The NWCF has prepared annual financial statements pursuant to the CFO Act of 1990, as amended, for the past fourteen years. The Act requires that financial statements be prepared and audited for each revolving fund and account that performed substantial commercial functions, such as those performed by the NWCF.

The NWCF financial statements include all activities previously financed through the Navy Industrial Fund and DON Stock Fund. DoD converted these activities to the Defense Business Operations Fund (DBOF) in October 1991. In December 1996, Under Secretary of Defense (Comptroller) replaced the DBOF with four working capital funds, one of which is the NWCF. This action did not change the previous organizational reporting structure.

1.C. Appropriations and Funds

The DON's appropriations and funds are divided into 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 DON's missions.

The NWCF (a revolving fund) received its initial working capital through an appropriation or a transfer of resources from existing appropriations or funds and used 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 NWCF 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 NWCF generally records transactions on an accrual accounting basis as required by Federal GAAP. However, some of the NWCF's financial and feeder systems and processes are not designed to collect and record financial information on the full accrual accounting basis. The NWCF has undertaken efforts to determine the actions required to bring all of its financial and feeder systems and processes into compliance with all elements of Federal GAAP.

In addition, the NWCF identifies programs based upon the major appropriation groups provided by Congress. The NWCF is in the process of reviewing available data and attempting to develop a cost reporting methodology that balances the need for cost information required by the Statements of Federal Financial Accounting Standards (SFFAS) No. 4, "Managerial Cost Accounting Concepts and Standards for the Federal Government," with the need to keep the financial statements from being overly voluminous.

1.E. Revenues and Other Financing Sources

Revenue is recognized according to the percentage of completion method for depot maintenance activity groups. Research and Development activity groups recognize revenue according to the percentage of completion method or as actual costs are incurred and billed. Revenue is recognized when an inventory item is sold for supply management activities and at the time service is rendered for base support activities. Revenue for the transportation activity group is recognized on either a reimbursable or per diem basis, that is, revenue is recognized when earned. The preponderance of per diem projects are billed and collected in the month services are rendered. In the case of reimbursables, some per diems and point-to-point voyages, the revenue is accrued in the month services are rendered and collection is made the following month.

The NWCF 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, where U.S. troops are stationed, or where the U.S. fleet is in a port. 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 the recognition of operating expenses in the period incurred. However, because the NWCF's financial and 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 contracts. Expenditures for capital and other long-term assets are not recognized as expenses in the NWCF's 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 the net position.

Operating expenses were adjusted as a result of the elimination of balances between DoD Components. See Note 19.I Intragovernmental Revenue and Expense, for disclosure of adjustment amounts.

1.G. Accounting for Intragovernmental Activities

The NWCF, 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 NWCF as though the agency was a stand-alone entity.

The DON'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 NWCF financial statements, therefore, do not report any portion of the federal government public debt or interest thereon, nor do the statements report the source of public financing whether from issuance of debt or tax revenues.

Financing for the construction of DON 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.

The NWCF'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. The NWCF 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). The NWCF 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 NWCF must be eliminated. However, the NWCF 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 NWCF. For FY 1999 and beyond, seller entities within the Department 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 Department of the Treasury, Financial Management Service is responsible for eliminating transactions between the Department of Defense or Navy and other federal agencies. In September 2000, the Financial Management Service issued the "Federal Intragovernmental Transactions Accounting Policies and Procedures Guide." The Department 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 NWCF, 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 (U.S.) Treasury and the Federal Financing Bank, Federal Employees' Compensation Act transactions with the Department of Labor, and benefit program transactions with the OPM.

1.H. Transactions with Foreign Governments and International Organizations
Each year, DoD 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 this Act, DoD has authority to sell defense articles and services to foreign countries and international organizations, generally at no profit or loss to the U.S. Government. Customers may be required to make payments in advance.

1.I. Funds with the U.S. Treasury
The NWCF financial resources are maintained in U.S. Treasury accounts. Cash collections, disbursements, and adjustments are processed worldwide at DFAS, Military Services, and the U.S. Army Corps 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, 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 NWCF recorded balance in the FBWT accounts and Treasury's FBWT accounts sometimes result and are subsequently reconciled. Material disclosures are provided at Note 3.

1.J. Foreign Currency
Not Applicable.

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. Allowances for uncollectible accounts due from the public are based upon analysis of collection experience by fund type. DoD does not recognize an allowance for estimated uncollectible amounts from other federal agencies. Claims against another federal agency are to be resolved between the agencies. Material disclosures are provided in Note 5.

1.L. Loans Receivable.
Not Applicable.

1.M. Inventories and Related Property
Effective FY 2003, Statement of Federal Financial Accounting Standards 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). The standard renames National Defense Property, Plant, and Equipment to military equipment, classifies military equipment 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 also includes items, which will now be classified as Operating Materials and Supplies. Military equipment is reported on the books of the DON General Fund.

The majority of the NWCF inventories are reported at approximate historical cost using Latest Acquisition Cost (LAC) adjusted for holding gains and losses. The remaining inventory is valued using Moving Average Cost (MAC). The NWCF 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 the historical cost data necessary to comply with the SFFAS No. 3, "Accounting for Inventory and Related Property." Neither can they directly produce financial transactions using the U.S. Standard General Ledger (USSGL), as required by the Federal Financial Management Improvement Act of 1996 (P.L. 104-208). DoD is transitioning to a MAC methodology for valuing inventory that when fully implemented will allow the NWCF 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 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 DoD holds material based on military need and support for contingencies.

Related property includes Operating Materials and Supplies (OM&S) and stockpile materials. The OM&S, including munitions not held for sale, are valued at standard purchase price. The NWCF uses various methods of accounting for OM&S.

The DoD policy is to account for condemned material (only) as "Excess, Obsolete, and Unserviceable." The net value of condemned material is zero, because the costs of disposal are greater than the potential scrap value. Material that can be potentially redistributed, presented in previous years as "Excess, Obsolete, and Unserviceable," is included in the "Held for Use" or "Held for Repair" categories according to its condition.

In FY 2003, DoD adopted the use of an allowance to reflect impaired assets, i.e. Inventory Held for Repair. Previously, the DoD financial statements have presented its impaired assets at other than historical cost. The NWCF will implement the allowance method in conjunction with the transition to MAC.

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 at Note 9.

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

Not Applicable.

1.O. General Property, Plant and Equipment

Effective FY 2003, 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). The standard renames National Defense Property, Plant, and Equipment to military equipment, classifies military equipment 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. Military equipment is reported on the books of the Department of the Navy General Fund.

General PP&E assets and any improvements to the asset are capitalized at historical acquisition cost when the asset has a useful life of two or more years, and when the acquisition cost equals or exceeds the DoD capitalization threshold of $100 thousand. Improvement costs over the DoD capitalization threshold of $100 thousand 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.

General PP&E has been capitalized and reported on the NWCF financial statements using the following DoD capitalization thresholds: FY 1996 though FY 2004 - $100 thousand; FY 1995 - $50 thousand; FY 1994 - $25 thousand; and FY 1993 - $15 thousand.

For NWCF 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. Military Equipment, Heritage Assets and Stewardship Land owned or maintained on a NWCF installation are reported in the Supplemental Stewardship Report of the applicable Military Department. To prevent duplicate reporting of the same Heritage Assets within DON, the total number of DON-wide Heritage Assets are reported in the Required Supplementary Stewardship Information of the Annual Audited Financial Statements of the DON General Funds (Treasury Index 17).

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 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), the NWCF records the applicable asset and liability if the value equals or exceeds the current DoD capitalization threshold. The NWCF 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 assets fair value. The NWCF 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 NWCF 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 NWCF 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 NWCF provides financing payments. One type of financing payment that the NWCF 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 (FAR), the NWCF makes financing payments under fixed price contracts that are not based on a percentage of completion. The NWCF reports these financing payments as advances or prepayments in the "Other Assets" line item. The NWCF treats these payments as advances or prepayments because the NWCF 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 NWCF is not obligated to reimburse the contractor for its costs and the contractor is liable to repay the NWCF 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 FAR 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 NWCF. 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. The NWCF's loss contingencies arising as a result of pending or threatened litigation or claims and assessments occur due to events such as property 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 (CRO). Unexpended appropriations represent amounts of authority which are unobligated and have not been rescinded or withdrawn. Unexpended appropriations also represent amounts obligated but for which legal liabilities for payments have not been incurred.

CRO for the NWCF represents the excess/loss 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
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. The DoD capital assets overseas are purchased with appropriated funds; however, title to land and improvements is 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 the Department. 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 irretrievable 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 NWCF 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.

1.Y. Problem Disbursements

As of (Amounts in thousands)	Sep-02	Sep-03	Sep-04	Decrease/Increase from 2003 to 2004
1. Total Problem Disbursements				
A. Absolute Unmatched Disbursements	$166,500	$88,748	$56,910	($31,838)
B. Negative Unliquidated Obligations	0	0	0	0
2. Total In-Transit Disbursements, Net	$0	$0	$0	$0

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 represent the net value of disbursements and collections made by a DoD disbursing activity on behalf of an accountable activity but not yet posted in an accounting system.

The NWCF had a problem disbursement absolute amount and net amount of $56,910 thousand and $35,225 thousand, respectively. NWCF problem disbursements continue to decrease from the prior years largely due to improving system functionality and business processes. Additional emphasis on further reducing NWCF problem disbursements has resulted in corresponding efforts to analyze and improve DFAS processes, and determine solutions to reduce current inflow and their root causes.

UMDs, NULOs, and In-transit Disbursement, Net represent disbursements of the NWCF funds that have been reported by a disbursing station to the Department of the Treasury, but have not yet been precisely matched against the specific source obligation giving rise to the disbursements. For the most part, these payments have been made using available funds and are based on valid receiving reports for goods and services delivered under valid contracts.

The elimination of both Problem Disbursements and In-transits is one of the highest financial management priorities of the OUSD(C). Problem Disbursements and In-transits represent a significant financial management concern since: (1) accuracy of accounting reports is affected; (2) availability of funds is more difficult to determine; and (3) the required research and resolution process becomes much more labor intensive as the age of the problem disbursements increase. As a result the NWCF has efforts underway to improve the systems and to resolve all previous problem disbursements.

NOTE 2. NON-ENTITY ASSETS

As of September 30,	2004	2003
(Amounts in thousands)		
1. Intra-governmental Assets:		
A. Fund Balance with Treasury	$ 0	$ 0
B. Investments	0	0
C. Accounts Receivable	0	0
D. Other Assets	0	0
E. Total Intra-governmental Assets	$ 0	$ 0
2. Non-Federal Assets:		
A. Cash and Other Monetary Assets	$ 0	$ 0
B. Accounts Receivable	5,141	11,617
C. Loans Receivable	0	0
D. Inventory & Related Property	0	0
E. General Property, Plant and Equipment	0	0
F. Investments	0	0
G. Other Assets	0	0
H. Total Non-Federal Assets	$ 5,141	$ 11,617
3. Total Non-Entity Assets	$ 5,141	$ 11,617
4. Total Entity Assets	$ 25,591,751	$ 25,969,815
5. Total Assets	$ 25,596,892	$ 25,981,432

6. Other Information Related to Non-entity and Entity Assets:

Fluctuations and/or Abnormalities

The decrease of $6,476 thousand, 56 percent, in non-federal accounts receivable is the result of reduced outstanding interest, penalties, fines, and administrative fees.

Definitions

Asset accounts are either categorized as entity or 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, e.g., accounts payable. Non-entity accounts are assets that are held by an entity, but are not available for use in the operations of the entity, for example, interest, penalties and fines, as an agent of the Department of the Treasury.

Composition of Non-entity Assets

The $5,141 thousand included in non-entity non-federal accounts receivable represents interest, penalties, fines, & administrative fees. These fees do not belong to the Navy Working Capital Fund and will be submitted to the Department of the Treasury.

Other Disclosures Related to Non-entity Assets
No further disclosures required.

Note Reference

For regulatory discussion on Non-entity Assets, See Department of Defense Financial Management Regulation, Volume 6B, Chapter 10, paragraph 1004.

Note 3.A. Fund Balance with Treasury

As of September 30,	2004	2003
(Amounts in thousands)		
1. Fund Balances:		
A. Appropriated Funds	$ 0	$ 0
B. Revolving Funds	861,243	1,827,646
C. Trust Funds	0	0
D. Other Fund Types	0	0
E. Total Fund Balances	$ 861,243	$ 1,827,646
2. Fund Balances Per Treasury Versus Agency:		
A. Fund Balance per Treasury	$ 861,243	$ 1,827,646
B. Fund Balance per NWCF	861,243	1,827,646
3. Reconciling Amount	$ 0	$ 0

4. Explanation of Reconciliation Amount:
None.

5. Information Related to Fund Balance with Treasury:

Fluctuations and/or Abnormalities
Fund Balance with Treasury (FBWT) had a net decrease of $966,403 thousand, 53 percent, from FY 2003 to FY 2004. The majority of the decreases (over 80 percent) are attributed to: $810,000 thousand decrease in net outlays which is attributable to a disbursement of $448,000 thousand to the Navy General Fund in FY 2004. This transfer to the Navy General Fund was made in accordance with the Department of the Navy's (DON) FY 2004 President's Budget; the Naval Shipyards had a net decrease of $94,636 thousand because the budgeted stabilized billing rate for FY 2004 was lower than the FY 2003 billing rate. The Navy Supply Management had a net decrease in net outlays of $447,545 thousand which was attributed to the increase in disbursements that was the result of liquidating accounts payable in FY 2004.

Composition of Fund Balance with Treasury

The FBWT of $861,243 thousand reflects the FY 2003 ending balance of $1,827,646 thousand plus FY 2004 collections, disbursements, and other cash transactions recorded in the Navy Working Capital Fund (NWCF) Treasury sub-limit 97X4930.002. The following table details the amounts recorded as of September 30, 2004.

(Amounts in thousands)

Net Prior Year Adjustments	$	0
Collections	$	24,016,877
Disbursements	$	(24,718,258)
Other Cash Transactions, Net	$	(265,021)

The following table provides a breakout of Other Cash Transactions, Net:

(Amounts in thousands)

Activity		
Navy Supply Management	Appropriations Received	$ 130,446
Ordnance-Seal Beach	PBD 419 Cash Transfer	(42,800)
Transportation	Principal Payment to FFB	(107,667)
Navy Component	Public Law 108-87	(245,000)
Total		$ (265,021)

A direct appropriation of $130,446 thousand was provided to the NWCF Supply Management Activity through the allocation of the Department of Defense (DoD) Appropriations Act of 2004.
Program Budget Decision 419 transferred $42,800 thousand for the residual accounting from NWCF Ordnance activity group, which became part of the General Fund in FY 2000.

The principal payment of $107,667 thousand to the Federal Financing Bank relates to an outstanding debt principal amount reported by the Transportation Activity Group. See Note 6 for additional disclosures.

As outlined in Office of the Under Secretary of Defense memorandum of December 9, 2003, a direct appropriation was provided to the Defense Working Capital Fund in the DoD Appropriations Act, 2004, P.L. 108-87, Title V. Program Budget Decision 624, dated December 1, 2003 provided those funds to Navy Supply Management.

Intragovernmental Payment and Collection (IPAC)

IPAC differences are reconcilable differences that represent amounts recorded by Treasury but not reported by the organization. IPAC differences for the DON cannot be differentiated between NWCF and General Funds. Therefore, no IPAC differences are being reported for the NWCF. All amounts, if applicable, will be reported on the Department of the Navy General Fund statement.

Other Disclosures Related to Fund Balance with Treasury

No further disclosures required.

Note Reference

See Note Disclosure 1.I., Significant Accounting Policies, for additional discussion on financial reporting requirements and DoD policies governing Funds with the U.S. Treasury.

For regulatory discussion on Fund Balance with Treasury, See DoD Financial Management Regulation, Volume 6B, Chapter 10, paragraph 100501.

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

Information Related to Suspense/Budget Clearing Accounts:
The NWCF Suspense/Budget Clearing Accounts are being reported under Navy General Funds, Index 17.

Note 4. Investments
Not Applicable.

Note 5. Accounts Receivable

As of September 30,	2004			2003
	Gross Amount Due	Allowance For Estimated Uncollectibles	Accounts Receivable, Net	Accounts Receivable, Net
(Amounts in thousands)				
1. Intra-governmental Receivables:	$ 857,519	N/A	$ 857,519	$ 582,773
2. Non-Federal Receivables (From the Public):	$ 26,198	$ (8)	$ 26,190	$ 111,775
3. Total Accounts Receivable:	$ 883,717	$ (8)	$ 883,709	$ 694,548

4. Other Information Related to Accounts Receivable:

Fluctuations and/or Abnormalities
Intra-governmental accounts receivable increased $274,746 thousand, 47 percent, from FY 2003 to FY 2004. This increase is mainly attributed to the increase of $352,938 thousand of supported undistributed collections. The Navy Supply Management business area had a decrease of $48,357 thousand for the reduction in undistributed collections that were applied/matched to the accounts receivable. Transportation business area had a decrease of $44,940 thousand that was attributed to the Global War on Terrorism (GWOT). Normally, the Military Sealift Command (MSC) bills and collects accounts receivables for the majority of its recurring customers in the same month, but as the GWOT was initiated, MSC had an increase in new customers, and at first was unable to bill and collect in the same month, which resulted in a higher than normal FY 2003 year-end balance. The Depot Maintenance Aviation had a decrease of $66,703 thousand from the collection of outstanding customer bills, which had been recorded in FY 2003 and liquidated in FY 2004.

Other activity groups' undistributed collections were impacted because of the shortened reporting period for year-end, which prohibited the processing of some of the Daily Expenditure Files through September 30, 2004.

Non-federal Accounts Receivable decreased $85,585 thousand, 77 percent, from FY 2003 to FY 2004. The decrease of Non-federal Accounts Receivable in the amount of $91,458 thousand is predominantly attributed to the changes from FY 2003 to FY 2004 listed below:

(Amount in thousands)		
Foreign Military Sales reclass JV	$	(24,314)
MOCAS JV		30,175
Combined Changes for Undistributed Supported /Unsupported		85,597
Total	$	91,458

A posting logic flaw in the Material Financial Control System for the Supply Management business area continues from FY 2003. Progress has been made, however additional problems have surfaced; thus creating a lower than anticipated balance in the Allowance for Estimated Uncollectibles. In addition, the Industrial Fund's business processes will be changed as a result of the DON Financial Improvement Plan requiring them to record an allowance.

Throughout the NWCF activities, a more aggressive role has been taken within the activities working in conjunction with their DFAS partners, to clear delinquent aged accounts receivables.

Allowance Method

The Statement of Federal Financial Accounting Standards No. 1 and the Department of Defense (DoD) Financial Management Regulation require that federal agencies establish an allowance for uncollectible accounts receivable non-federal accounts. This account has been established within the Navy Working Capital Fund (NWCF). This amount is low, as the NWCF requires an advance deposit from all non-federal entities prior to the commencement of work. Therefore, an assumption is made that the amount of uncollectible accounts should be negligible. The allowance amount represents a percentage of the total that was billed after the total project cost has been adjusted to reflect the advance deposit.

Allocation of Undistributed Collections

The DoD policy is to allocate supported undistributed collections between federal and non-federal categories based on the percentage of federal and non-federal accounts receivable. Supported undistributed collections in the amount of $352,938 thousand were applied against accounts receivable. (The allocation of supported undistributed did not result in an abnormal balance or allocations greater than 10 percent of the accounts receivable balance.) The NWCF allocates its unsupported undistributed collections in U. S. Standard General Ledger account 2400, Liability for Deposit Funds, Clearing Accounts, and Undeposited Collections. This treatment recognizes that the potential exists that some of these unsupported undistributed collections do not belong to the NWCF and will have to be paid to the appropriate fund holder.

Trading Partner Data

The NWCF's accounting systems do not capture trading partner data at the transaction level in a manner that facilitates trading partner aggregations. Therefore, the NWCF is unable to reconcile intragovernmental accounts receivable balances with most trading partners. Through the Business Management Modernization Program, DoD intends to develop long-term systems improvements that will capture the data necessary to perform reconciliations. The DON is also working on short-term solutions to gather the required information as outlined in the DON Financial Improvement Plan.

Accounts Receivable Greater than 180 days

The amount of non-federal and intragovernmental receivables over 180-days old is $20,515 thousand and $19,052 thousand, respectively.

Non-federal Refunds Receivable
The total amount of non-federal refund receivables does not exceed 10 percent of the non-federal accounts receivable, net amount on the Balance Sheet.

Other Disclosures Related to Accounts Receivable
No further disclosures required.

Note Reference
For additional discussion on financial reporting requirements and DoD policies governing Trading Partner Data and Accounts Receivable, see Notes 1.G. and 1.K, Significant Accounting Policies, respectively.

For regulatory discussion on Accounts Receivable, See Department of Defense Financial Management Regulation, Volume 6B, Chapter 10, paragraph 1007.

NOTE 6. OTHER ASSETS

As of September 30,	2004	2003
(Amounts in thousands)		
1. Intra-governmental Other Assets:		
A. Advances and Prepayments	$ 15	$ 10,392
B. Other Assets	0	0
C. Total Intra-governmental Other Assets	$ 15	$ 10,392
2. Non-Federal Other Assets:		
A. Outstanding Contract Financing Payments	$ 0	$ 0
B. Other Assets (With the Public)	717,191	868,808
C. Total Non-Federal Other Assets	$ 717,191	$ 868,808
3. Total Other Assets:	$ 717,206	$ 879,200

4. Other Information Related to Other Assets:

Fluctuations and/or Abnormalities
Intragovernmental Other Assets, Advances and Prepayments, decreased $10,376 thousand, 99 percent from FY 2003 to FY 2004. This variance was the result of elimination adjustments to reflect the balances reported on the seller's books (other Department of Defense (DoD)) in September 2003. For FY 2004, these eliminations were not necessary to facilitate the DoD and federal-wide consolidation process, which is discussed in Note 1.

Non-Federal Other Assets (Other Assets With the Public) decreased $151,616 thousand, 18 percent, which is primarily attributed to the change in the outstanding principal balance of the Maritime Prepositioning Ships (MPS) loan in the amount of $107,861 thousand.

Advances and Prepayments
In FY 2003, the buyer-side advances to others account balances were adjusted to agree with seller-side advances from others account balances as reported on the books of other DoD reporting entities. Additionally, the buyer-side prepayment balances were adjusted to agree with seller-side deferred credits as reported on the books of other DoD reporting entities for FY 2003 only.

Composition of Non-Federal Other Assets
Non-Federal Other Assets (Other Assets With the Public) includes prepayments made by Navy Supply Management; revenue earned but not billed by Depot Maintenance, Shipyards; and deferred charges, advances, and unallocated costs.

Other Disclosures Related to Other Assets
None.

Note Reference
See Note 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
Not Applicable.

Note 8. A. Direct Loan and/or Loan Guarantee Programs
Not Applicable.

Note 9. Inventory and Related Property

As of September 30,	2004	2003
(Amounts in thousands)		
1. Inventory, Net (Note 9.A.)	$ 18,505,475	$ 17,519,382
2. Operating Materials & Supplies, Net (Note 9.B.)	733,717	736,746
3. Stockpile Materials, Net (Note 9.C.)	0	0
4. Total	$ 19,239,192	$ 18,256,128

NOTE 9.A. INVENTORY, NET

As of September 30,	2004 Inventory, Gross Value	2004 Revaluation Allowance	2004 Inventory, Net	2003 Inventory, Net	Valuation Method
(Amounts in thousands)					
1. Inventory Categories:					
A. Available and Purchased for Resale	$ 22,561,554	$ (18,421,542)	$ 4,140,012	$ 3,319,295	O
B. Held for Repair	13,520,824	372,350	13,893,174	13,242,934	O
C. Excess, Obsolete, and Unserviceable	708,360	(708,360)	0	0	SP
D. Raw Materials	0	0	0	0	
E. Work in Process	472,289	0	472,289	957,153	AC
F. Total	$ 37,263,027	$ (18,757,552)	$ 18,505,475	$ 17,519,382	

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: None

3. Other Information:

Fluctuations and/or Abnormalities

Inventory Available and Purchased for Resale is a net increase of $820,716 thousand, 25 percent, from FY 2003 to FY 2004. The Cost of Goods Sold (COGS) model prior period adjustment, $534,077 thousand, was reclassified to the inventory allowance account, thereby decreasing the inventory allowance which resulted in an increase in inventory. In addition, Navy Supply Management had a reduction in purchases at cost in FY 2004 for approximately $300,000 thousand.

The Material Financial Control System (MFCS) posting logic is incorrect and caused an abnormal balance in other liabilities, the Navy Supply Management business area's Other Supply Offices, had $568,567 thousand reclassified to the inventory allowance account to more accurately reflect Navy Supply Management's financial position and correct the posting logic.

Work in Process decreased $484,861 thousand, 51 percent, from FY 2003 to FY 2004 due to aggressive clearing of backlogged work in process. The majority of this decrease is a result of Depot Maintenance, Aviation, $175,529 thousand; Naval Air Warfare Center, decrease of $231,196 thousand, and Naval Surface Warfare Center, decrease of $38,734 thousand. Due to Puget Sound Naval Shipyard becoming mission funded in FY 2004, the shipyards work in process decreased $31,387 thousand.

The abnormal value of the allowance account for Inventory Held for Repair in the amount of ($372,350) thousand was caused by increased disposal of inventory held for the Inactive Inventory Investment Program. This program held material above requirements for potential market and recoupment of investment funds for a predetermined amount of time. Once the time expired, the inventory was disposed.

Changes in Accounting Methods

Navy Supply Management started implementation of SMART, an Enterprise Resource Planning (ERP) System in FY 2003. The inventory capitalized into ERP is valued at Moving Average Cost (MAC). Under the MAC inventory valuation method, the "per item" inventory value can change upon each new purchase.

Valuation Methods

The valuation method O (Other) included in the numeric note table above for inventory categories Available and Purchased for Resale and Held for Repair were provided because the amounts reported are valued at both Latest Acquisition Cost (LAC) and MAC. A breakout of these amounts by valuation method is as follows:

(Amounts in thousands)	
Inventory Available and Purchased for Resale, Net	
Latest Acquisition Cost	$3,359,312
Moving Average Cost	780,700
Total	$4,140,012
Inventory Held for Repair, Net	
Latest Acquisition Cost	$13,397,093
Moving Average Cost	496,081
Total	$13,893,174

Restrictions of Inventory Use, Sale, or Disposition

Generally, there are no restrictions with regard to the use, sale, or disposition to applicable Department of Defense (DoD) activities and personnel. Other than certain safety and war reserve levels, inventory may be sold to foreign, state and local governments, private parties and contractors in accordance with DoD and the Department of the Navy (DON) policies and guidance or at the direction of the President.

Composition of Inventory

Except for the Work in Process, all Inventory categories shown in the table above apply to the Supply Management Activities only.

Inventory Categories. Inventory represents 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 Available and Purchase for Resale includes consumable spare and repair parts and repairable items owned and managed by the DON. In some cases, the consumable and repairable items are managed by other Military Services, such as the Defense Logistics Agency or the General Services Administration. 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. Federal Accounting Standards require disclosure of the amount of Inventory Held for "Future Sale". The Navy Working Capital Fund estimates there is currently no Inventory Held for Future Sale reported for FY 2004 in Inventory Held for Sale, Net.

Included in Line 1.A., Inventory Available and Purchased for Resale, is an amount of $156,925 thousand for War Reserve Material for Navy Supply Management. Marine Corps Supply Management currently has no War Reserve Material.

Inventory Held for Repair is 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 DON often relies on weapon systems and machinery no longer in production, the DON supports a process that encourages the repair and rebuilding of certain items. This repair cycle is an essential part of 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. The DON does not anticipate recovering any significant costs as a result of final disposal of these items. Therefore, Excess, Obsolete, and Unserviceable inventory will reflect a net realizably value of zero.

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 billing 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.

Inventory Work in Process

Work in process at Depot Maintenance activities and Research and Development activities of approximately $120,004 thousand and $352,286 thousand, respectively, is included as inventory Work in Process in Note 9.A. These amounts are reported in inventory because the U.S. Government Standard General Ledger (USSGL) does not provide a separate account for Work in Process. This amount represents work that has been completed, expenses incurred, and waiting to be billed to the customer.

Other Disclosures Related to Inventory

The general ledger values in the accounting system do not reconcile with the supporting detail records in the Navy segment of the Supply Management Activity logistics system. Navy Supply Management has determined that program changes must be made to MFCS to correct systemic posting problems, which contribute to a reconciling difference between the systems. Twenty-four System Change Requests have been prepared and submitted. Once approved and executed, final adjustments will be made to inventory and financial systems to align the data.

Note Reference

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

For regulatory discussion on Inventory, Net, see Department of Defense Financial Management Regulation, Volume 6B, Chapter 10, paragraph 1011.

Note 9.B. Operating Materials and Supplies, Net

As of September 30,	2004 OM&S Gross Value	2004 Revaluation Allowance	2004 OM&S, Net	2003 OM&S, Net	Valuation Method
(Amounts in thousands)					
1. OM&S Categories:					
A. Held for Use	$ 733,717	$ 0	$ 733,717	$ 736,746	O
B. Held for Repair	0	0	0	0	
C. Excess, Obsolete, and Unserviceable	0	0	0	0	
D. Total	$ 733,717	$ 0	$ 733,717	$ 736,746	

Legend for Valuation Methods:

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

2. Restrictions on OM&S: None

3. Other Information Related to OM&S:

Fluctuations and/or Abnormalities
No further disclosures required.

Restrictions on OM&S
Generally, there are no restrictions with regard to the use, sale, or disposition of OM&S applicable the Department of Defense (DoD) activities.

Composition of OM&S
OM&S Held for Use represents property that is consumed during normal operations and includes consumable spare and repair parts for use on customer work by various activities. The items are recorded using different methodologies including actual, weighted-average and historical cost. Federal Accounting Standards requires disclosure of the amount of OM&S Held for "Future Use". The Navy Working Capital Fund estimates that $13,674 thousand of the OM&S Held for Use, Net will be for future use. There is no management or valuation difference between the two categories.

Government Furnished Material (GFM) and Contractor Acquired Material (CAM)
Generally, the values of the NWCF's GFM and CAM in the hands of contractors are not included in the OM&S values reported above. 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 already in other existing logistics systems.

Other Disclosures Related to OM&S
No further disclosures required.

Note Reference

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

For regulatory discussion on OM&S, Net, see Department of Defense Financial Management Regulation, Volume 6B, Chapter 10, paragraph 101107.

Note 9.C. Stockpile Materials, Net

Not Applicable.

Note 10. General PP&E, Net

As of September 30,	2004					2003
	Depreciation/ Amortization Method	Service Life	Acquisition Value	(Accumulated Depreciation/ Amortization)	Net Book Value	Prior FY Net Book Value
(Amounts in thousands)						
1. Major Asset Classes:						
A. Land	N/A	N/A	$ 50,740	N/A	$ 50,740	$ 63,711
B. Buildings, Structures, and Facilities	S/L	20 Or 40	5,780,915	$ (3,727,618)	2,053,297	2,496,894
C. Leasehold Improvements	S/L	lease term	302	(164)	138	169
D. Software	S/L	2-5 Or 10	414,331	(200,236)	214,095	106,935
E. Equipment	S/L	5 Or 10	3,354,530	(2,471,542)	882,988	921,981
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	682,665	N/A	682,665	730,671
I. Other			11,619	0	11,619	3,549
J. Total General PP&E			$ 10,295,102	$ (6,399,560)	$ 3,895,542	$ 4,323,910

[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 Related to General PP&E, Net:

Fluctuations and/or Abnormalities

Land decreased $12,972 thousand, 20 percent. The Naval Air Warfare Centers (NAWCs) became a tenant of Commander, Naval Installation (CNI), as of October 1, 2003, resulting in the transfer of land to CNI, which caused a decrease of $11,563 thousand. The Naval Undersea Warfare Center (NUWC) had a decrease of $646 thousand because of a transfer of land to CNI also.

Buildings, Structures, and Facilities decreased $443,596 thousand, 17.8 percent from FY 2003 to FY 2004. The majority of the decrease is a result of the NAWC decrease of $327,565 thousand and the NUWC decrease of $76,040 thousand transfer of assets to CNI.

Leasehold Improvements decreased $31 thousand, 18 percent, due to increased depreciation in the Transportation Business Area.

Software increased $107,160 thousand, 100 percent, from FY 2003 to FY 2004. The increase is primarily attributed to an increase in the Depot Maintenance Aviation business areas as a result of its Enterprise Resource Planning (ERP), System configuration Management Information System, Naval Air Systems Command (NAVAIR) Depot Maintenance System and the Depot Maintenance System becoming operational in FY 2004.

GPP&E Other increased $8,070 thousand, 227 percent, from FY 2003 to FY 2004 due to property awaiting disposal. With the implementation of ERP, this is the book value of the Defense Industrial Financial Management System (DIFMS) that is no longer being depreciated.

Military Equipment
Military equipment is reported on the books of the Department of Navy General Fund.

Fully Depreciated Assets
The acquisition value of fully depreciated assets reported in the Balance Sheet amount to $3,325,566 thousand as of September 30, 2004.

Outside of the Continental United States (OCONUS) GPP&E
Included in the Major Asset Classes disclosed in Note 10 are assets located OCONUS. As of September 30, 2004 the amount of OCONUS was $322,816 thousand.

Contractor Held GPP&E
For those activities with GPP&E real property in the possession of contractors, the value of this real property is included in the values reported for the Major Asset Classes of Buildings, Structures, and Facilities. The value of personal property in Major Asset Classes of Automated Data Processing Software and Equipment does not include all of the GPP&E in the possession of contractors. The net book amount of such property is immaterial in relation to the total GPP&E net book value. In accordance with an approved strategy with the Office of Management and Budget, the General Accounting Office, and the Inspector General Department of Defense, the Department of Defense is developing new policies and a contractor reporting process to capture GPP&E information for future reporting purposes for compliance with federal-wide accounting standards.

Other Disclosures Related to GPP&E
For the Naval Supply Systems Command, the value of GPP&E is potentially overstated. Implementation of the Defense Property Accounting System (DPAS) has recorded all plant, property, and equipment since its inception in October 1999. The value of equipment is overstated in the Central Database (CDB) due to a lack of an interface between the source system, DPAS and the Defense Business Management System (DBMS). Additionally, the GPP&E that was resident in the CDB prior to October 1999 remains in the CDB. The amounts reported in the CDB appear on the balance sheet, but potentially overstate the true value of the GPP&E. Navy Supply Management plans to initiate the interface with DPAS and DBMS, for equipment, during the first quarter of FY 2005. There are initiatives underway to identify corrective actions for the reporting of land, buildings, and software during FY 2005. This deficiency has been noted in the DON Financial Improvement Plan.

Note Reference
See Note 1.O., Significant Accounting Policies, for additional discussion on financial reporting requirements and the Department of Defense (DoD) policies governing GPP&E.

For regulatory discussion on GPP&E, Net, see Department of Defense Financial Management Regulation, Volume 6B, Chapter 10, paragraph 1012.

Note 10.A. Assets Under Capital Lease

Information Related to Assets Under Capital Lease:
The Navy Working Capital Fund has no assets under capital lease.

Other Disclosures Related to Assets Under Capital Lease
No further disclosures required.

Note References
See Note 1.Q., Significant Accounting Policies, for additional discussion on financial reporting requirements and the DoD policies governing Leases.

Note 11. Liabilities Not Covered by Budgetary Resources

As of September 30,	2004	2003
(Amounts in thousands)		
1. Intra-governmental Liabilities:		
A. Accounts Payable	$ 0	$ 0
B. Debt	0	0
C. Environmental Liabilities	0	0
D. Other	5,141	11,617
E. Total Intra-governmental Liabilities	$ 5,141	$ 11,617
2. Non-Federal Liabilities:		
A. Accounts Payable	$ 0	$ 0
B. Military Retirement Benefits and Other Employment-Related Actuarial Liabilities	1,168,225	1,409,853
C. Environmental Liabilities	0	0
D. Loan Guarantee Liability	0	0
E. Debt Held by Public	0	0
F. Other Liabilities	0	0
G. Total Non-Federal Liabilities	$ 1,168,225	$ 1,409,853
3. Total Liabilities Not Covered by Budgetary Resources	$ 1,173,366	$ 1,421,470
4. Total Liabilities Covered by Budgetary Resources	$ 8,401,653	$ 7,467,848
5. Total Liabilities	$ 9,575,019	$ 8,889,318

Fluctuations and/or Abnormalities
The decrease of $6,476 thousand, 55 percent, in other intragovernmental liabilities is the result of reduced outstanding refunds receivable and interest.

The decrease of $241,628 thousand, 17 percent, in Military Retirement Benefits and Other Employment-Related Actuarial Liabilities is based on the amount received from the Department of Labor.

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

The Intragovernmental Liabilities, Other amount of $5,141 thousand represents interest, penalties, fines & administrative fees. These fees do not belong to the Navy Working Capital Fund and will be distributed directly to the Department of the Treasury.

Other Disclosures Related to Liabilities Not Covered by Budgetary Resources
The $1,168,225 thousand included in Military Retirement Benefits and Other Employment-Related Actuarial Liabilities represents Federal Employees' Compensation Act liabilities.

Note Reference
For additional line item discussion, see Note 12, Accounts Payable; Note 15, Other Liabilities; Note 16, Commitments and Contingencies; and Note 17, Military Retirement Benefits and Other Employment Related Actuarial Liabilities.

Note 12. Accounts Payable

As of September 30,	2004			2003
	Accounts Payable	Interest, Penalties, and Administrative Fees	Total	Total
(Amounts in thousands)				
1. Intra-governmental Payables:	$ 243,982	N/A	$ 243,982	$ 313,786
2. Non-Federal Payables (to the Public):	$ 1,862,567	$ 0	$ 1,862,567	$ 2,102,870
3. Total	$ 2,106,549	$ 0	$ 2,106,549	$ 2,416,656

4. Other Information Related to Accounts Payable:

Fluctuations and/or Abnormalities
Intragovernmental Accounts Payable had a net decrease of $69,804 thousand, 22 percent, from FY 2003 to FY 2004. The decrease is attributed to the Component business area that had a total decrease of $400,775 thousand of which a net decrease of $257,016 thousand reflects an accounts payable adjustment that moved unsupported undistributed disbursements to disbursements in transit; a net decrease of $122,149 thousand reflects an adjustment to accounts payable that reclassified intragovernmental to public and a decrease of $21,611 thousand that is attributed to eliminations.

There was an increase of $333,902 thousand in accounts payable that was attributed to the Ordnance business area of $119,474 thousand. This increase was offset by undistributed disbursements and the continual clearing of residual accounts in this business area; the Naval Air Warfare Center's (NAWC's) increase of $121,160 thousand related to the implementation of SIGMA Enterprise Resource Planning (ERP) System. During the NAWC's implementation, undistributed disbursements were higher in FY 2003. With the system being fully operational, the problems encountered in FY 2003 have been corrected in FY 2004 and the proper balances are reflected. Navy Supply Management increased $140,217 thousand, which was attributed to the increase in supplies ordered during FY 2004 and the decrease of undistributed disbursements. See below for discussion on the composition and allocation of undistributed disbursements.

In February 2003, the Department of Defense (DoD) Appropriations Act authorized the Navy Working Capital Fund (NWCF) Cash Balance and Rate Stabilization Adjustment for the Ordnance activity group for $120,000 thousand that decreased accounts payable because a Voucher for Transfers between Appropriations and/or Funds was used and this transaction created an undistributed disbursement. Navy Supply Management increased $140,217 thousand because of the activity at the field level accounts payable records. Space and Naval Warfare System Center had a decrease of $73,673 thousand. The majority of the undistributed disbursements represent Mechanization of Contract Administration Services (MOCAS) payments, which had not liquidated. NAWC increased $121,160 thousand due to delayed processing of the Daily Expenditure File in September 2004, which created an undistributed disbursement.

Approximately 85-90 percent of Intragovernmental Other Liabilities includes the Industrial Fund's contract accruals. Contract accruals are the costs of contractual services rendered by either commercial or government organizations, which are accrued over the anticipated life of each service contract. Accruals are rolled-up in the accounting system as Other Liabilities and should be adjusted based on paid vouchers. The Department of the Navy (DON) Financial Improvement Plan is addressing the accounting deficiencies of not posting contract accruals as accounts payable. The NWCF will continue to reflect abnormal accounts payable until the solution is implemented.

Other activity groups' undistributed collections were impacted because of the shortened reporting period for year-end, which prohibited the processing of some of the Daily Expenditure Files through September 30, 2004.

Non-Federal Accounts Payable decreased $240,303 thousand, 11 percent, from FY 2003 to FY 2004. Net adjustments were made in the Component business area which were attributed to a net decrease of $148,349 thousand which was moved from unsupported undistributed disbursements to disbursements in transit (other liabilities); a net increase in the amount of $122,149 thousand was reclassified payables from intragovernmental to non-federal in order to reconcile trading partner data. The remaining $221,780 thousand decrease is related to the Naval Surface Warfare Center. This decrease was caused by a new business practice of running cash daily and the clean up of old accounts payables. The Transportation business area decreased because they were able to resolve outstanding unmatched disbursements during FY 2004.

Definitions

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. Non-Federal payables are payments to non-federal government entities (to the public).

Undistributed Disbursements

Undistributed disbursements are the difference between disbursements/collections recorded at the transaction level to a specific obligation, payable, or receivable in the activity field records as opposed to those reported by the U.S. Treasury via the reconciled DD1329 and DD1400. The total undistributed disbursement amounts displayed in this note should agree with the undistributed amounts reported on the accounting reports (SF133/AR(M)1307). In-transit payments are payments that have been made for other agencies or entities that have not been recorded in their accounting records. These payments are applied to each entity's outstanding accounts payable balance at year-end.

Allocation of Undistributed Disbursements

The DoD policy is to allocate supported undistributed disbursements between federal and nonfederal categories based on the percentage of Federal and Nonfederal accounts payable. Supported undistributed disbursements in the amount of $237,294 thousand were applied against Accounts Payable. Unsupported undistributed disbursements should be recorded in U.S. Standard General Ledger (USSGL) account 2120, Disbursements in Transit. The NWCF reclassified $604,251 thousand to in-transit payments.

Composition of Undistributed Disbursements

The majority of the undistributed disbursements represent MOCAS payments, which have not been liquidated. MOCAS payments represent those payments made to contractors for materials or services that are greater than $2,500 dollars. Accruals are made when the service is performed and remains in this account until the provider submits an invoice for payment. Therefore, if a copy of the invoice is not received by the NWCF activity prior to the Defense Finance and Accounting Service making payment, the payment will go to undistributed disbursements. The amounts accrued to cover the anticipated materials and services are captured as Contract Accruals on the Other Accrued Expense line (Note 15.A., Other Liabilities, Nonfederal: Other Liabilities) and are not considered an accounts payable.

Note 3 describes a $448,000 thousand disbursement to the Navy General Fund. This transfer to the Navy General Fund was made in accordance with the Department of the Navy's FY 2004 President's Budget resulting in an undistributed disbursement in the Component business area that was also applied to accounts payable.

Trading Partner Data

For the majority of intra-agency sales, NWCF accounting systems do not capture trading partner data at the transaction level in a manner that facilitates trading partner aggregations. Therefore, the NWCF was unable to reconcile the majority of its intragovernmental accounts payable to the related intragovernmental accounts receivable that generated the payable. Through an ongoing Business Management Modernization Program, the DoD intends to develop long-term systems improvements that will capture the data necessary to perform reconciliations. The DON has outlined some processes for review and implementation in the DON Financial Improvement Plan, which should provide some near-term solutions.

Eliminating Adjustments

The DoD summary level seller accounts receivables were compared to NWCF accounts payable. An adjustment was posted to the NWCF accounts payable based on the comparison with the accounts receivable of the DoD Components providing goods and services to the NWCF. As required, adjustments were made to reclassify accounts payable from Federal to Public.

Other Disclosures Related to Accounts Payable

The NWCF also disbursed $448,000 thousand to the Navy General Fund in April 2004 in accordance with the Department of the Navy's FY 2004 President's Budget, which also created an undistributed disbursement in the Component business area.

Note Reference

See Note 1.G., Significant Accounting Policies, for additional discussion on financial reporting requirements and DoD policies governing Trading Partner Data and Eliminating Adjustments.

Note 13. Debt

As of September 30,	2004 Beginning Balance	2004 Net Borrowings	2004 Ending Balance	2003 Ending Balance
(Amounts in thousands)				
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	$ 0	$ 0	$ 0	$ 0
B. Debt to the Federal Financing Bank	615,648	(109,370)	506,278	615,648
C. Debt to Other Federal Agencies	0	0	0	0
D. Total Agency Debt	$ 615,648	$ (109,370)	$ 506,278	$ 615,648
3. Total Debt:	$ 615,648	$ (109,370)	$ 506,278	$ 615,648
4. Classification of Debt:				
A. Intragovernmental Debt			$ 506,278	$ 615,648
B. Non-Federal Debt			N/A	N/A
C. Total Debt			$ 506,278	$ 615,648
5. Other Information				

Fluctuations and/or Abnormalities

Intragovernmental Debt decreased $109,370 thousand, 18 percent, from FY 2003 to FY 2004 as a result of the reduction of the outstanding debt principal and interest amount reported for the Transportation Activity Group.

Other Information Related to Debt

The Afloat Propositioning Force - Navy (APF-N) program, with Congressional approval, provides ships for Time Charter to meet requirements not available in the marketplace. These ships are built or converted by private Interim Vessel Owners using private, non-government financing obtained from various banking institutions. There were no payments made by the government during the building/conversion phase. APF-N Time Charters are for five years with four option renewal periods of five years each, for a total of 25 years. At the end of the contract, each ship returns to the vessels owner.

The Federal Financing Bank (FFB) is one of the institutions that provided loans to the vessel owners. The FFB is reporting a debt in the amount of $506,278 thousand which represents an outstanding principal balance of $498,583 thousand and accrued interest payable of $7,695 thousand for the Transportation activity group. This information is being presented in error as the transportation activity group does not owe this debt to the FFB. This debt is a public debt owed by the private vessel owners. In order to simplify the payments to the FFB and to meet its requirements, the FFB cross-disburses the semi-annual principal and interest payments directly from the Navy Working Capital Fund (NWCF). This is done instead of having the Military Sealift Command (MSC) make Capital Hire payments to the vessel owners, who would in turn make its loan obligation payments to the FFB.

The direction of the vessel owner to have the government make payments directly to a bank, in this case the FFB, is not an uncommon practice, and mirrors other Time Charters where payment is assigned directly to a bank. This occurred when the ownership of these vessels was transferred to private vessel owners; however, the FFB when establishing the loan coded the loan as a government debt.

As required by the Under Secretary of Defense (Comptroller) memorandum of January 22, 1999, MSC is correctly recording these payments as an operating expense. However, the outstanding debt principal amount is reported in the NWCF Balance Sheet as an Other Asset to reconcile with the amount reported by the FFB through the trading partner elimination process. The misclassification by the FFB has generated this long-standing reporting problem. See Note 6 for additional disclosures.

As required by the Department of Defense Appropriations Act passed in December 1985, 10 percent of the fifth year termination value of the vessels must be obligated from Operation and Maintenance, Navy funds. This was completed as each vessel was delivered.

Note References

See Note 3, Fund Balance with Treasury and Note 6, Other Assets, for additional discussion on the Debt to the Federal Financing Bank.

For regulatory discussion on Debt, Net, see Department of Defense Financial Management Regulation, Volume 6B, Chapter 10, paragraph 1015.

Note 14. Environmental Liabilities and Disposal Liabilities

Not Applicable.

NOTE 15.A. OTHER LIABILITIE

As of September 30,	2004 Current Liability	2004 Noncurrent Liability	2004 Total	2003 Total
(Amounts in thousands)				
1. Intragovernmental:				
A. Advances from Others	$ 72,509	$ 0	$ 72,509	$ 239,595
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. 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. Judgement Fund Liabilities	0	0	0	0
I. FECA Reimbursement to the Department of Labor	0	0	0	0
J. Capital Lease Liability	0	0	0	0
K. Other Liabilities	42,342	0	42,342	49,673
L. Total Intragovernmental Other Liabilities	$ 114,851	$ 0	$ 114,851	$ 289,268
2. Non-Federal:				
A. Accrued Funded Payroll and Benefits	$ 746,226	$ 0	$ 746,226	$ 726,494
B. Advances from Others	477,383	0	477,383	194,779
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	341,793	0	341,793	235,588
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	4,113,706	8	4,113,714	3,001,030
N. Total Non-Federal Other Liabilities	$ 5,679,108	$ 8	$ 5,679,116	$ 4,157,891
3. Total Other Liabilities:	$ 5,793,959	$ 8	$ 5,793,967	$ 4,447,159

4. Other Information Pertaining to Other Liabilities:

Fluctuations and/or Abnormalities

On the balance sheet, Intragovernmental Other Liabilities decreased $174,416 thousand, 60 percent, from FY 2003 to FY 2004. The Component business area reflects a decrease of $162,608 thousand, which includes an adjustment of $277,020 thousand for buyer side eliminations.

Approximately 85-90 percent of Intragovernmental Other Liabilities includes the Industrial Fund's contract accruals. Contract accruals are the costs of contractual services rendered by either commercial or government organizations, which are accrued over the anticipated life of each service contract. Accruals are rolled-up in the accounting system as Other Liabilities and should be adjusted based on paid vouchers. The Department of the Navy (DON) Financial Improvement Plan is addressing the accounting deficiencies of not posting contract accruals as accounts payable. The Navy Working Capital Fund (NWCF) will continue to reflect the abnormal accounts payable and other liabilities until the solution is implemented.

Non-Federal Accounts Receivable decreased from FY 2003 to FY 2004 in the amount of $6,476 thousand or 55 percent as a result of reduced outstanding refunds receivable and interest reported in Mechanization of Contract Administration Services, (MOCAS).

In addition the increase is attributed to Depot Maintenance Shipyards growth in Advances for Revenue Recognition, which have been cross-walked within the Department of Defense Reporting System to Advances from Others. Specified projects at the Naval Shipyards are funded using fixed price versus the reimbursable method. This amount actually represents the difference between what the activity billed the customer and that which it actually earned as determined by what was physically accomplished on the job. Preliminary analysis indicates this amount would be more appropriately posted to Progress Payments - Work in Progress. A review of this amount will be included in the Department of the Navy Financial Improvement Plan.

Non-Federal Other Liabilities increased $1,521,225 thousand, 37 percent, from FY 2003 to FY 2004. The Component business area had an increase of $333,432 thousand that was attributed to Non-Federal Advances from Others which increased $282,604 thousand, 145 percent, from FY 2003 to FY 2004. This amount is primarily attributable to a reclassification in the Component business area in the amount of $277,020 thousand, to adjust for trading partner data. The $1,044,000 thousand that was included FY 2003 was reclassified as a prior year adjustment. Also, the Navy Supply Management business area had an increase of $1,306,495 thousand due to the reclassification of $568,567 thousand abnormal balance and an increase of $676,000 thousand in depot level reparable carcass returns.

Composition of Other Liabilities

Intragovernmental Other Liabilities represents liabilities of $42,342 thousand for fringe benefits and the Voluntary Separation Incentive Program.

Non-federal Deposit Funds and Suspense Account Liabilities increased $106,205 thousand, 45 percent, which include amounts for unsupported undistributed collections.

Non-federal Other Liabilities includes amounts that are significant portions of the total liabilities presented in the NWCF balance sheet. A breakout of the major components of Non-federal Other Liabilities follows:

a. Accrual of Contractual Services represents an accrued liability for direct work performed by contractors or material and supplies purchased for a direct order in which a request for payment has not been received. The accrual is based on the level of effort performed for the direct order on a monthly basis.

b. Depot Level Repairable Carcass Return Liability represents the value of returned depot level repairable carcasses that have been received by an accountable activity from an end-use activity but for which an issue has not yet been processed.

c. Other Liabilities includes a $(1,044,715) thousand allocation of unsupported undistributed disbursements. This allocation was based on the Defense Finance and Accounting Service memorandum dated October 10, 1997, which directed the allocation of undistributed disbursements to the DoD Military Services from their Defense Working Capital Fund corporate account. During FY 2004, the $1,044,715 thousand was treated as a prior period adjustment.

The remainder of the Other Liabilities amount consists of Progress Payments, which show the balance of payments taken for accrued costs charged to Work in Process or the value of material procured and held for specific orders received from customers within the DoD.

Intragovernmental Reconciliation for Fiduciary Transactions with Department of Labor (DOL)
With respect to the major fiduciary balances, the NWCF was able to reconcile with the DOL.

Other Disclosures Related to Other Liabilities
No further disclosures required.

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

Note 15.B. Capital Lease Liability

Information Related to Capital Lease Liability:
The NWCF has no capital lease liability.

Other Disclosures Related to Capital Lease Liability
No further disclosures required.

Note Reference
See Note 1.Q., Significant Accounting Policies, for additional discussion on financial reporting requirements and the DoD policies governing Leases.

For regulatory discussion on Capital Lease Liability, see Department of Defense Financial Management Regulation, Volume 6B, Chapter 10, paragraph 1017.

Note 16. Commitments and Contingencies

Information Related to Commitments and Contingencies:
The Navy Working Capital Fund (NWCF) is a party in various administrative proceedings and legal actions that may ultimately result in settlements or decisions adverse to the Federal Government. These proceedings and actions arise in the normal course of operations and their ultimate disposition is unknown. In the event of an adverse judgment against the Government, some of the liabilities may be payable from the Judgment Fund. Others may be payable from the Department's resources, either directly or by reimbursement to the Judgment Fund. Based on information currently available, however, it is management's opinion that the expected outcome of these matters, individually or in the aggregate, will not have a material adverse effect on the Department.

For fiscal years 2003 and 2004, the materiality threshold for reporting litigation, claims, or assessments was $5.8 million and $3.5 million, respectively. The amounts set forth above for civil and environmental litigation, claims, and assessments represent the aggregate of the amounts of claims, litigation or assessments considered to be significant for reporting purposes based on the established materiality thresholds. These amounts represent the maximum amounts of any potential liability of the Government based on the amounts claimed. Management does not consider it to be at all likely that the Government will be liable for such maximum amounts.

The NWCF reported a total amount of 10 cases in FY 2004. However, the Department of the Navy (DON) is unable to express an opinion concerning the likely outcome of these cases.

Reference

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

For regulatory discussion on Commitments and Contingencies, see Department of Defense Financial Management Regulation, Volume 6B, Chapter 10, paragraph 1018.

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

As of September 30,	2004				2003
	Actuarial Present Value of Projected Plan Benefits	Assumed Interest Rate (%)	(Less: Assets Available to Pay Benefits)	Unfunded Actuarial Liability	Unfunded Actuarial Liability
(Amount in Thousands)					
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	$ 1,168,225	4.883%	$ 0	$ 1,168,225	$ 1,409,853
B. Voluntary Separation Incentive Programs	0		0	0	0
C. DoD Educational Benefits Fund	0		0	0	0
D. Total Other	$ 1,168,225		$ 0	$ 1,168,225	$ 1,409,853
3. Total Military Retirement Benefits and Other Employment Related Actuarial Liabilities:	$ 1,168,225		$ 0	$ 1,168,225	$ 1,409,853

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

Actuarial Cost Method Used:

The Department of the Navy (DON) actuarial liability for workers' compensation benefits is developed by the Department of Labor (DOL) and provided to the DON at the end of each fiscal year. The liability is distributed between the Navy Working Capital Fund (NWCF) and DON General Fund based upon the number of civilian employees funded in each entity as reported in the Navy Budget Tracking System. 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 Budgets (OMB'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. The interest rate assumptions used in the discount calculations were as follows as of September 30, 2004:

4.883 percent in year 1,
5.235 percent in year 2 and thereafter

Market Value of Investments in Market-based and Marketable Securities:
Not Applicable.

Note 18. Unexpended Appropriations
Not Applicable.

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

Disclosures Related to the Statement of Net Cost:

Fluctuations and/or Abnormalities
The overall increase of $598,195 thousand, 136 percent, was attributed to the Component business area reclassifying expenses from intragovernmental to non-federal in order to adjust the trading partner data received from other federal reporting entities. The Statement of Net Cost reflects the circumstances and general business conditions of the Activities of the Navy Working Capital Fund (NWCF). In FY 2004, the business conditions of the NWCF included: reduction in new orders and workload changes; restraints on overhead; transition of Puget Sound Naval Shipyard out of NWCF; deferred maintenance and stabilized rate adjustments.

The goal of the Net Cost of Operations is to maintain an income and expense account that comes close to break even. It is not the goal of the U.S. Government to make a profit.

Composition of Statement of Net Cost
The NWCF generally records transactions on an accrual basis as required by federal generally accepted accounting principles. Information presented on the Statement of Net Cost represents the net result of post-closing adjustments and eliminating entries made in compiling and consolidating the NWCF financial statements. These entries significantly affected the reported amounts of Intragovernmental Program Cost, Program Cost with the Public, Earned Revenue and Net Program Cost. The post-closing adjustments were made in order to increase or decrease certain NWCF account balances reported as of September 30, 2004 to ensure agreement with related balances reported by other Department of Defense (DoD) activities and other federal reporting entities. Eliminating entries are required adjustments made as part of the financial process. This process enables the matching of trading partner data recorded at each financial statement consolidation level -- the NWCF, DoD and Federal Government levels.

Other Disclosures Related to the Statement of Net Cost

The Statement of Net Cost was impacted by recording a Prior Period Adjustment in the amount of $103,258 thousand as a current year transaction in accordance with the federal accounting standards. See Note 20 for further disclosures.

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

Not Applicable.

Note 19.C. Gross Cost to Generate Intragovernmental 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,	2004	2003
(Amount in thousands)		
1. Civilian (e.g.,CSRS/FERS) Retirement	$ 243,406	$ 270,127
2. Civilian Health	300,500	272,241
3. Civilian Life Insurance	980	1,013
4. Military Retirement Pension	0	0
5. Military Retirement Health	0	0
6. Judgment Fund	0	0
7. Total Imputed Expenses	$ 544,886	$ 543,381

8. Other Information

Related to Imputed Expense:

The NWCF financial statements have recognized an imputed expense for civilian employee pensions, life insurance, and health benefits in the Statement of Net Cost. Imputed expenses for employee benefits were calculated using cost factors provided by the Office of Personnel Management (OPM) applied against gross basic pay for all categories of civilian service employees. The gross basic pay amounts were extracted directly from the Defense Civilian Pay System (DCPS). Judgment Fund claims are reported in the Navy General Fund statements and notes.

Other Disclosures Related to Imputed Expenses

No further disclosures required.

Note 19.E. Benefit Program Expenses

Not Applicable.

Note 19. F. Exchange Revenue

Disclosures related to the Exchange Revenue:

Definition
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.

Other Disclosures Related to Exchange Revenue
No further disclosures required.

Note Reference
For regulatory discussion on Exchange Revenue, see Department of Defense Financial Management Regulation, 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. Intragovernmental Revenue and Expense

Disclosures Related to Intergovernmental Revenue and Expense:
Intragovernmental Revenue. The Navy Working Capital Fund (NWCF) accounting systems do not capture trading partner data at the transaction level in a manner that facilitates trading partner aggregations. Therefore, the NWCF was unable to reconcile intragovernmental revenue balances with the majority of its trading partners. Action has been taken to reconcile some of the smaller accounts manually. Through an ongoing Business Management Modernization Program (BMMP), the Department of Defense (DoD) intends to develop long-term systems improvements that will capture the data necessary to perform reconciliations.

Intragovernmental Operating Expenses
The NWCF operating expenses were adjusted based on a comparison between the NWCF's accounts payable and the DoD summary level seller accounts receivable. Adjustments were posted to accounts payable and operating expenses to reflect the following reported balances: other trading partners; Federal Financing Bank (FFB) payments for debt; interest, penalties, fines & administrative fees data call; and resolution of abnormal accounts payables in accordance with current guidance. The operating expenses of the NWCF were adjusted downward in the net amount of $905,726 thousand.

The Office of Management and Budget (OMB) has established a working group to review the current business practices in place to capture the data exchanged between federal agencies and to determine what changes need to be incorporated. The Department of the Navy (DON) has representation on the Office of the Under Secretary of Defense (Comptroller) group, which is working directly with OMB to ensure that all aspects (e.g., financial, logistics and security) of DoD are given full consideration. Based on the large volume of intragovernmental transactions that occur, this project is a major undertaking and will take several years to complete with the ultimate goal of having this process totally automated.

Other Disclosures Related to Exchange Revenue
No further disclosures required.

Note 19.J. Suborganization Program Costs
Not Applicable.

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

As of September 30,	Cumulative Results of Operations 2004	Unexpended Appropriations 2004	Cumulative Results of Operations 2003	Unexpended Appropriations 2003
(Amounts in thousands)				
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	0	0
C. Other Prior Period Adjustments	(1,044,715)	0	(1,044,715)	0
D. Total Prior Period Adjustments	$ (1,044,715)	$ 0	$ (1,044,715)	$ 0
2. Imputed Financing:				
A. Civilian CSRS/FERS Retirement	$ 243,406	$ 0	$ 270,127	$ 0
B. Civilian Health	300,500	0	272,241	0
C. Civilian Life Insurance	980	0	1,013	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	$ 544,886	$ 0	$ 543,381	$ 0

3. Other Information:

Fluctuations and/or Abnormalities
In FY 1995, the Department of the Navy received $1,044,715 thousand in undistributed Net Outlays from the Office of the Secretary of Defense corporate account. This value was adjusted to the Navy Working Capital Fund (NWCF) Component business area.

Composition of Statement of Changes in Net Position
During FY 2004, the $1,044,715 thousand was treated as a prior period adjustment. NWCF activities capture prior period adjustments in their accounting systems. Adjustments in the amount of $103,258 thousand were reclassified to current year operations because their individual values did not meet the material threshold outlined in the OUSD(C) memo of June 8, 2003.

Based on Office of the Under Secretary of Defense (OUSD) (C) direction, amounts generated as prior period adjustments within the Cost of Goods Sold model were moved to inventory allowance accounts. The amounts are as follows:

(Amount in thousands)	FY 2004	FY 2003
Navy Supply Management	$ (533,848)	$ (951,964)
Marine Corps Supply Management	$ (229)	$ 178,768

The Other Budgetary Financing Sources line on the Statement of Changes in Net Position includes $258,002 thousand for amounts reclassified to Other Gains or Other Losses from Transfers-In and Transfers-Out. Transfers-In amounts are required to agree with Transfers-Out amounts received from seller-side data.

Imputed Financing

The amounts remitted to the Office of Personnel Management (OPM) by and for employees covered by the Civil Service Retirement System, Federal Employee Retirement System, Federal Employees Health Benefits Program and the Federal Employee Group Life Insurance Program do not fully cover the Government's cost to provide these benefits. An imputed cost is recognized as the difference between the Government's cost of providing these benefits to the employees and contributions made by and for them. The OPM provides the cost factors to the Defense Finance and Accounting Service (DFAS) for computation of imputed financing cost. The DFAS provides the costs to OUSD(Personnel and Readiness) for validation. Approved imputed costs are provided to the reporting components for inclusion in their financial statements.

Note 21. Disclosures Related to the Statement of Budgetary Resources

As of September 30,	2004	2003
(Amounts in thousands)		
1. Net Amount of Budgetary Resources Obligated for Undelivered Orders at the End of the Period	$ 6,901,108	$ 8,043,629
2. Available Borrowing and Contract Authority at the End of the Period	6,156,853	5,880,543

3. Other Information:

Fluctuations and/or Abnormalities

None.

Information Related to the Statement of Budgetary Resources:

The Statement of Budgetary Resources (SBR) is an image of the monthly Report on Budget Execution (Standard Form (SF) 133). These reports should be produced using budgetary accounts. However, the Navy Working Capital Fund (NWCF) uses proprietary accounts because its financial accounting systems were not designed to produce budgetary accounting data. The Department of the Navy (DON) and the Defense Finance and Accounting Service (DFAS) continue with the implementation of new accounting systems designed to produce both proprietary and budgetary reports and use the U.S. Standard General Ledger (USSGL). The Defense Industrial Financial Management System (DIFMS) has been fully implemented at all Research and Development (R&D) activities that were scheduled for conversion. R&D activity Space and Naval Warfare

Systems Command, San Diego has successfully implemented the Enterprise Resource Planning (ERP) System (Cabrillo) thus moving off DIFMS. Also, the Naval Air Warfare Centers (NAWCs) have moved from DIFMS to their ERP (SIGMA). The ERPs are programmed to complete the SBR at the activity level. The Defense Working Capital Fund Accounting System (DWAS) implementation continues to be implemented at the Base Support Activities.

As of September 30, 2004, the SBR does not measure the NWCF's budget execution against budgetary resources. Budgetary resources are recorded in the accounting records and reported on the basis of customer orders received and contract authority invoked. On these reports, the spending authority from offsetting collections during the period of execution is based upon the approved President's Budget estimate of anticipated customer orders. Further, there are system deficiencies that have been identified, which are being addressed in the DON Financial Improvement Plan.

For the SBR, Supply Management's revenue is defined as gross sales less credit returns. For the balance sheet, revenue does not include credit returns because the inventory valuation model considers credit returns as inventory allowances. The difference in "meanings" causes variances in the reports. On these budgetary reports, the net outlays (collections and disbursements) year to date are reported based on the amounts reported to the U.S. Treasury.

As of September 30, 2004, the differences between the U.S. Treasury and the NWCF activity ledgers have been minimal, and the cause is related to timing or the type of transactions. The differences are recorded as undistributed disbursements and collections on the departmental reports. While there may be no impact upon the U.S. Treasury balance, the above differences have created distortions in the accounts receivable and accounts payable from a budgetary reporting perspective on the SBR. Also, problems with undistributed collections and disbursements have created abnormal balances for accounts receivable and accounts payable on the SBR.

Intra-entity Transactions

The 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 categories A, B, and exempt from apportionment as required by OMB Bulletin 01-09 are as follows:

(Amounts in Thousands)			
Obligations Incurred – Direct	Line 8A	$	0
Obligations Incurred – Reimbursable	Line 8B	$	24,316,447
Exempt from apportionment -	Line 9B	$	0

Undelivered Orders

Undelivered Orders presented in the SBR includes Undelivered Orders-Unpaid for reimbursable funds.

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 line on the SBR or the Spending Authority for Offsetting Collections line on the Statement of Financing.

Other Disclosures Related to the Statement of Budgetary Resources
No further disclosures required.

Note 22. Disclosures Related to the Statement of Financing

Disclosures Related to the Statement of Financing:
The Statement of Financing is designed to provide information on the total resources used by an entity, to explain how those resources were used to finance orders for goods and services not yet delivered, to acquire assets and liabilities, and to fund the entity's net cost of operations. It is designed to report the differences and facilitate the reconciliation of accrual-based amounts used in the Statement of Net Cost and obligation-based amounts used in the Statement of Budgetary Resources. The computations and presentation of items in the Statement of Financing demonstrate that the budgetary and proprietary information in an entity's financial management system is in agreement.

The Defense Finance and Accounting Service (DFAS) Navy Working Capital Fund (NWCF) accounting systems and Navy Enterprise Resource Planning (ERP), include budgetary accounts. However some of the legacy NWCF accounting systems do not. As a result, the Statement of Budgetary Resources (SBR) is generated by DFAS using data extracted from the proprietary accounts.

The detailed level of information required to appropriately complete the SBR is being developed for those activities that cannot provide the data due to system deficiencies. Due to the system deficiencies, the Statement of Financing line, Resources that Finance the Acquisition of Assets, was adjusted upward by $2,209,934 thousand.

Intra-entity transactions have not been eliminated because statements are presented as combined and combining.

Other Disclosures Related to the Statement of Financing
No further disclosures required.

Note 23. Disclosures Related to the Statement of Custodial Activity
Not Applicable.

Note 24.A. Other Disclosures

Entity as Lessee - Operating Leases

As of September 30,	2004				2003
(Amounts in thousands)					
Future Payments Due:	Land and Buildings	Equipment	Other	Total	Total
Fiscal Year					
2005	$ 0	$ 0	$ 0	$ 0	$ 511
2006	0	0	0	0	0
2007	0	0	0	0	0
2008	0	0	0	0	0
2009	0	0	0	0	0
After 5 Years	0	0	0	0	0
Total Future Lease Payments Due	$ 0	$ 0	$ 0	$ 0	$ 511

Fluctuations and/or Abnormalities

The Military Sealift Command (MSC) had an operating lease for a corporate data center, which commenced December 1, 1999 for a lease period of one year with three option years. MSC exercised the final option to buy the equipment prior to the end of FY 2004 in the amount of $494 thousand.

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 a payment of funds.

Operating Lease - A lease which does not transfer substantially all the benefits and risks of ownership. Payments should be charged to expense over the lease term as it becomes payable.

Land and Building Leases consist of:

Description of Leases:

None.

Equipment Leases consist of:

None.

Other Leases consist of:

None.

Note 24.B. Other Disclosures

Not Applicable.

Department of the Navy

Navy Working Capital Fund Supporting Consolidating/Combining Statements

Department of Defense
Navy Working Capital Fund
CONSOLIDATING BALANCE SHEET
As of September 30, 2004 and 2003
($ in thousands)

	Depot Maintenance, Shipyards	Depot Maintenance, Aviation	Depot Maintenance, Marine Corps	Ordnance
ASSETS (Note 2)				
Intragovernmental:				
Fund Balance with Treasury (Note 3)				
Entity	$ 390,127	$ 59,035	$ (33,400)	$ 31,211
Non-Entity Seized Iraqi Cash	0	0	0	0
Non-Entity - Other	0	0	0	0
Investments (Note 4)	0	0	0	0
Accounts Receivable (Note 5)	12,622	77,089	13,051	1
Other Assets (Note 6)	0	0	12	0
Total Intragovernmental Assets	$ 402,749	$ 136,124	$ (20,337)	$ 31,212
Cash and Other Monetary Assets (Note 7)	$ 0	$ 0	$ 0	$ 0
Accounts Receivable (Note 5)	170	345	168	0
Loans Receivable (Note 8)	0	0	0	0
Inventory and Related Property (Note 9)	194,782	482,857	75,509	0
General Property, Plant and Equipment (Note 10)	660,252	349,981	51,708	140
Investments (Note 4)	0	0	0	0
Other Assets (Note 6)	74,319	2,724	0	0
TOTAL ASSETS	$ 1,332,272	$ 972,031	$ 107,048	$ 31,352
LIABILITIES (Note 11)				
Intragovernmental:				
Accounts Payable (Note 12)	$ 17,340	$ 232,530	$ 35,558	$ 5,655
Debt (Note 13)	0	0	0	0
Environmental Liabilities (Note 14)	0	0	0	0
Other Liabilities (Note 15 & Note 16)	49,084	4,798	8,691	0
Total Intragovernmental Liabilities	$ 66,424	$ 237,328	$ 44,249	$ 5,655
Accounts Payable (Note 12)	$ 48,666	$ 27,190	$ 9,863	$ 4,641
Military Retirement Benefits and Other Employment-Related Actuarial Liabilities (Note 17)	0	0	22,365	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)	270,258	276,612	5,621	8,182
Debt Held by Public (Note 13)	0	0	0	0
TOTAL LIABILITIES	$ 385,348	$ 541,130	$ 82,098	$ 18,478
NET POSITION				
Unexpended Appropriations (Note 18)	$ 0	$ 0	$ 0	$ 0
Cumulative Results of Operations	946,924	430,901	24,950	12,874
TOTAL NET POSITION	$ 946,924	$ 430,901	$ 24,950	$ 12,874
TOTAL LIABILITIES AND NET POSITION	$ 1,332,272	$ 972,031	$ 107,048	$ 31,352

Department of Defense
Navy Working Capital Fund
CONSOLIDATING BALANCE SHEET
As of September 30, 2004 and 2003
($ in thousands)

	Transportation	Base Support	Research & Development	Supply Management
ASSETS (Note 2)				
Intragovernmental:				
Fund Balance with Treasury (Note 3)				
Entity	$ 286,324	$ 178,398	$ 1,131,923	$ (943,264)
Non-Entity Seized Iraqi Cash	0	0	0	0
Non-Entity - Other	0	0	0	0
Investments (Note 4)	0	0	0	0
Accounts Receivable (Note 5)	98,318	156,404	40,962	180,053
Other Assets (Note 6)	0	0	(52)	0
Total Intragovernmental Assets	$ 384,642	$ 334,802	$ 1,172,833	$ (763,211)
Cash and Other Monetary Assets (Note 7)	$ 0	$ 0	$ 0	$ 0
Accounts Receivable (Note 5)	260	22,077	58,385	(37,657)
Loans Receivable (Note 8)	0	0	0	0
Inventory and Related Property (Note 9)	3,359	25,965	423,534	18,033,186
General Property, Plant and Equipment (Note 10)	44,085	669,697	1,562,410	557,269
Investments (Note 4)	0	0	0	0
Other Assets (Note 6)	499,745	1,320	22,745	116,393
TOTAL ASSETS	$ 932,091	$ 1,053,861	$ 3,239,907	$ 17,905,980
LIABILITIES (Note 11)				
Intragovernmental:				
Accounts Payable (Note 12)	$ 58,011	$ 31,593	$ (104,113)	$ 607,304
Debt (Note 13)	506,278	0	0	0
Environmental Liabilities (Note 14)	0	0	0	0
Other Liabilities (Note 15 & Note 16)	3,092	4,339	202,063	55,888
Total Intragovernmental Liabilities	$ 567,381	$ 35,932	$ 97,950	$ 663,192
Accounts Payable (Note 12)	$ 340,937	$ 160,902	$ 728,336	$ 514,214
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)	49,533	117,179	2,260,277	2,137,570
Debt Held by Public (Note 13)	0	0	0	0
TOTAL LIABILITIES	$ 957,851	$ 314,013	$ 3,086,563	$ 3,314,976
NET POSITION				
Unexpended Appropriations (Note 18)	$ 0	$ 0	$ 0	$ 0
Cumulative Results of Operations	(25,760)	739,848	153,344	14,591,004
TOTAL NET POSITION	$ (25,760)	$ 739,848	$ 153,344	$ 14,591,004
TOTAL LIABILITIES AND NET POSITION	$ 932,091	$ 1,053,861	$ 3,239,907	$ 17,905,980

Department of Defense
Navy Working Capital Fund
CONSOLIDATING BALANCE SHEET
As of September 30, 2004 and 2003
($ in thousands)

	Component Level	Combined Total	Eliminations
ASSETS (Note 2)			
Intragovernmental:			
Fund Balance with Treasury (Note 3)			
Entity	$ (239,111)	$ 861,243	$ 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)	279,019	857,519	0
Other Assets (Note 6)	55	15	0
Total Intragovernmental Assets	$ 39,963	$ 1,718,777	$ 0
Cash and Other Monetary Assets (Note 7)	$ 0	$ 0	$ 0
Accounts Receivable (Note 5)	(17,558)	26,190	0
Loans Receivable (Note 8)	0	0	0
Inventory and Related Property (Note 9)	0	19,239,192	0
General Property, Plant and Equipment (Note 10)	0	3,895,542	0
Investments (Note 4)	0	0	0
Other Assets (Note 6)	(55)	717,191	0
TOTAL ASSETS	$ 22,350	$ 25,596,892	$ 0
LIABILITIES (Note 11)			
Intragovernmental:			
Accounts Payable (Note 12)	$ (639,896)	$ 243,982	$ 0
Debt (Note 13)	0	506,278	0
Environmental Liabilities (Note 14)	0	0	0
Other Liabilities (Note 15 & Note 16)	(213,104)	114,851	0
Total Intragovernmental Liabilities	$ (853,000)	$ 865,111	$ 0
Accounts Payable (Note 12)	$ 27,818	$ 1,862,567	$ 0
Military Retirement Benefits and Other			0
Employment-Related Actuarial Liabilities (Note 17)	1,145,860	1,168,225	
Environmental Liabilities (Note 14)	0	0	0
Loan Guarantee Liability (Note 8)	0	0	0
Other Liabilities (Note 15 and Note 16)	553,884	5,679,116	0
Debt Held by Public (Note 13)	0	0	0
TOTAL LIABILITIES	$ 874,562	$ 9,575,019	$ 0
NET POSITION			
Unexpended Appropriations (Note 18)	$ 0	$ 0	$ 0
Cumulative Results of Operations	(852,212)	16,021,873	0
TOTAL NET POSITION	$ (852,212)	$ 16,021,873	$ 0
TOTAL LIABILITIES AND NET POSITION	$ 22,350	$ 25,596,892	$ 0

Department of Defense
Navy Working Capital Fund
CONSOLIDATING BALANCE SHEET
As of September 30, 2004 and 2003
($ in thousands)

	2004 Consolidated	2003 Consolidated
ASSETS (Note 2)		
Intragovernmental:		
Fund Balance with Treasury (Note 3)		
Entity	$ 861,243	$ 1,827,646
Non-Entity Seized Iraqi Cash	0	0
Non-Entity - Other	0	0
Investments (Note 4)	0	0
Accounts Receivable (Note 5)	857,519	582,773
Other Assets (Note 6)	15	10,392
Total Intragovernmental Assets	$ 1,718,777	$ 2,420,811
Cash and Other Monetary Assets (Note 7)	$ 0	$ 0
Accounts Receivable (Note 5)	26,190	111,775
Loans Receivable (Note 8)	0	0
Inventory and Related Property (Note 9)	19,239,192	18,256,128
General Property, Plant and Equipment (Note 10)	3,895,542	4,323,910
Investments (Note 4)	0	0
Other Assets (Note 6)	717,191	868,808
TOTAL ASSETS	$ 25,596,892	$ 25,981,432
LIABILITIES (Note 11)		
Intragovernmental:		
Accounts Payable (Note 12)	$ 243,982	$ 313,786
Debt (Note 13)	506,278	615,648
Environmental Liabilities (Note 14)	0	0
Other Liabilities (Note 15 & Note 16)	114,851	289,268
Total Intragovernmental Liabilities	$ 865,111	$ 1,218,702
Accounts Payable (Note 12)	$ 1,862,567	$ 2,102,870
Military Retirement Benefits and Other Employment-Related Actuarial Liabilities (Note 17)	1,168,225	1,409,853
Environmental Liabilities (Note 14)	0	0
Loan Guarantee Liability (Note 8)	0	0
Other Liabilities (Note 15 and Note 16)	5,679,116	4,157,892
Debt Held by Public (Note 13)	0	0
TOTAL LIABILITIES	$ 9,575,019	$ 8,889,317
NET POSITION		
Unexpended Appropriations (Note 18)	$ 0	$ 0
Cumulative Results of Operations	16,021,873	17,092,115
TOTAL NET POSITION	$ 16,021,873	$ 17,092,115
TOTAL LIABILITIES AND NET POSITION	$ 25,596,892	$ 25,981,432

Department of Defense
Navy Working Capital Fund
CONSOLIDATING STATEMENT OF NET COST
For the years ended September 30, 2004 and 2003
($ in thousands)

	2004 Total	Eliminations	2004 Consolidated	2003 Consolidated
Program Costs				
Base Support				
Intragovernmental Gross Costs	$ 985,405	$ 0	$ 985,405	$ 1,008,827
(Less Intragovernmental Earned Revenue)	(1,602,991)	0	(1,602,991)	(1,584,722)
Intragovernmental Net Costs	$ (617,586)	$ 0	$ (617,586)	$ (575,895)
Gross Costs With the Public	$ 595,987	0	595,987	560,902
(Less: Earned Revenue From the Public)	0	0	0	0
Net Costs With the Public	$ 595,987	$ 0	$ 595,987	$ 560,902
Net Program Cost	$ (21,599)	$ 0	$ (21,599)	$ (14,993)
Component Level				
Intragovernmental Gross Costs	$ (4,319,029)	$ 0	$ (4,319,029)	$ (5,265,821)
(Less Intragovernmental Earned Revenue)	2,777,999	0	2,777,999	3,370,279
Intragovernmental Net Costs	$ (1,541,030)	$ 0	$ (1,541,030)	$ (1,895,542)
Gross Costs With the Public	$ 2,311,441	0	2,311,441	1,763,338
(Less: Earned Revenue From the Public)	(539,417)	0	(539,417)	(750,905)
Net Costs With the Public	$ 1,772,024	$ 0	$ 1,772,024	$ 1,012,433
Net Program Cost	$ 230,994	$ 0	$ 230,994	$ (883,109)
Depot Maintenance, Aviation				
Intragovernmental Gross Costs	$ 1,179,235	$ 0	$ 1,179,235	$ 1,333,506
(Less Intragovernmental Earned Revenue)	(2,218,932)	0	(2,218,932)	(2,355,599)
Intragovernmental Net Costs	$ (1,039,697)	$ 0	$ (1,039,697)	$ (1,022,093)
Gross Costs With the Public	$ 1,032,649	0	1,032,649	945,884
(Less: Earned Revenue From the Public)	0	0	0	(12,226)
Net Costs With the Public	$ 1,032,649	$ 0	$ 1,032,649	$ 933,658
Net Program Cost	$ (7,048)	$ 0	$ (7,048)	$ (88,435)
Depot Maintenance, Marine Corps				
Intragovernmental Gross Costs	$ 331,518	$ 0	$ 331,518	$ 20,163
(Less Intragovernmental Earned Revenue)	(324,480)	0	(324,480)	(224,548)
Intragovernmental Net Costs	$ 7,038	$ 0	$ 7,038	$ (204,385)
Gross Costs With the Public	$ (11,652)	0	(11,652)	222,057
(Less: Earned Revenue From the Public)	(3,927)	0	(3,927)	(3,578)
Net Costs With the Public	$ (15,579)	$ 0	$ (15,579)	$ 218,479
Net Program Cost	$ (8,541)	$ 0	$ (8,541)	$ 14,094

Department of Defense
Navy Working Capital Fund
CONSOLIDATING STATEMENT OF NET COST
For the years ended September 30, 2004 and 2003
($ in thousands)

	2004 Total	Eliminations	2004 Consolidated	2003 Consolidated
Program Costs				
Depot Maintenance, Shipyards				
Intragovernmental Gross Costs	$ 826,312	$ 0	$ 826,312	$ 1,019,640
(Less Intragovernmental Earned Revenue)	(2,241,481)	0	(2,241,481)	(2,750,642)
Intragovernmental Net Costs	$ (1,415,169)	$ 0	$ (1,415,169)	$ (1,731,002)
Gross Costs With the Public	$ 1,482,587	0	1,482,587	1,650,127
(Less: Earned Revenue From the Public)	0	0	0	0
Net Costs With the Public	$ 1,482,587	$ 0	$ 1,482,587	$ 1,650,127
Net Program Cost	$ 67,418	$ 0	$ 67,418	$ (80,875)
Ordnance				
Intragovernmental Gross Costs	$ (8,104)	$ 0	$ (8,104)	$ 71
(Less Intragovernmental Earned Revenue)	1	0	1	(926)
Intragovernmental Net Costs	$ (8,103)	$ 0	$ (8,103)	$ (855)
Gross Costs With the Public	$ 21	0	21	512
(Less: Earned Revenue From the Public)	0	0	0	0
Net Costs With the Public	$ 21	$ 0	$ 21	$ 512
Net Program Cost	$ (8,082)	$ 0	$ (8,082)	$ (343)
Transportation				
Intragovernmental Gross Costs	$ 439,176	$ 0	$ 439,176	$ 1,299,609
(Less Intragovernmental Earned Revenue)	(1,792,429)	0	(1,792,429)	(1,844,089)
Intragovernmental Net Costs	$ (1,353,253)	$ 0	$ (1,353,253)	$ (544,480)
Gross Costs With the Public	$ 1,338,020	0	1,338,020	489,538
(Less: Earned Revenue From the Public)	0	0	0	0
Net Costs With the Public	$ 1,338,020	$ 0	$ 1,338,020	$ 489,538
Net Program Cost	$ (15,233)	$ 0	$ (15,233)	$ (54,942)
Research & Development				
Intragovernmental Gross Costs	$ 5,854,980	$ 0	$ 5,854,980	$ 5,822,619
(Less Intragovernmental Earned Revenue)	(10,260,468)	0	(10,260,468)	(9,585,868)
Intragovernmental Net Costs	$ (4,405,488)	$ 0	$ (4,405,488)	$ (3,763,249)
Gross Costs With the Public	$ 4,441,537	0	4,441,537	3,750,586
(Less: Earned Revenue From the Public)	622	0	622	0
Net Costs With the Public	$ 4,442,159	$ 0	$ 4,442,159	$ 3,750,586
Net Program Cost	$ 36,671	$ 0	$ 36,671	$ (12,663)

Department of Defense
Navy Working Capital Fund
CONSOLIDATING STATEMENT OF NET COST
For the years ended September 30, 2004 and 2003
($ in thousands)

	2004 Total	Eliminations	2004 Consolidated	2003 Consolidated
Program Costs				
Supply Management				
Intragovernmental Gross Costs	$ 145,488	$ 0	$ 145,488	$ 183,636
(Less Intragovernmental Earned Revenue)	(6,036,154)	0	(6,036,154)	(6,895,749)
Intragovernmental Net Costs	$ (5,890,666)	$ 0	$ (5,890,666)	$ (6,712,113)
Gross Costs With the Public	$ 6,725,024	0	6,725,024	8,273,309
(Less: Earned Revenue From the Public)	(70,813)	0	(70,813)	0
Net Costs With the Public	$ 6,654,211	$ 0	$ 6,654,211	$ 8,273,309
Net Program Cost	$ 763,545	$ 0	$ 763,545	$ 1,561,196
Total Program Costs				
Intragovernmental Gross Costs	$ 5,434,981	$ 0	$ 5,434,981	$ 5,422,250
(Less Intragovernmental Earned Revenue)	(21,698,935)	0	(21,698,935)	(21,871,864)
Intragovernmental Net Costs	$ (16,263,954)	$ 0	$ (16,263,954)	$ (16,449,614)
Gross Costs With the Public	$ 17,915,614	0	17,915,614	17,656,253
(Less: Earned Revenue From the Public)	(613,535)	0	(613,535)	(766,709)
Net Costs With the Public	$ 17,302,079	$ 0	$ 17,302,079	$ 16,889,544
Net Program Cost	$ 1,038,125	$ 0	$ 1,038,125	$ 439,930
Costs Not Assigned to Programs	0	0	0	0
(Less: Earned Revenue Not Attributable to Programs)	0	0	0	0
Net Cost of Operations	$ 1,038,125	$ 0	$ 1,038,125	$ 439,930

Department of Defense
Navy Working Capital Fund
CONSOLIDATING STATEMENT OF CHANGES IN NET POSITION
For the years ended September 30, 2004 and 2003
($ in thousands)

	Depot Maintenance, Shipyards	Depot Maintenance, Aviation	Depot Maintenance, Marine Corps	Ordnance
Cumulative Results of Operations				
Beginning Balances	$ 1,053,728	$ 420,294	$ 58,480	$ 167,592
Prior period adjustments (+/-)				
Prior Period Adjustments - Restated (+/-)	0	0	0	0
Beginning Balance, Restated	1,053,728	420,294	58,480	167,592
Prior Period Adjustments - Not Restated (+/-)	(911)	0	0	
Beginning Balances, as adjusted	$ 1,052,817	$ 420,294	$ 58,480	$ 167,592
Budgetary Financing Sources:				
Appropriations Received	$ 0	$ 0	$ 0	$ 0
Appropriations transferred in/out (+/-)	0	0	0	0
Other adjustments (rescissions, etc) (+/-)	0	0	0	0
Appropriations used	0	0	0	0
Nonexchange revenue	0	0	0	0
Donations and forfeitures of cash and cash equivalents	0	0	0	0
Transfers in/out without reimbursement (+/-)	0	0	0	(42,800)
Other budgetary financing sources (+/-)	0	0	0	0
Other Financing Sources:				
Donations and forfeitures of property	0	0	0	0
Transfers in/out without reimbursement (+/-)	(38,474)	3,559	(50,573)	(120,000)
Imputed financing from costs absorbed by others	0	0	8,501	0
Other (+/-)	0	0	0	0
Total Financing Sources	$ (38,474)	$ 3,559	$ (42,072)	$ (162,800)
Net Cost of Operations (+/-)	$ 67,418	$ (7,048)	$ (8,541)	$ (8,082)
Ending Balances	$ 946,925	$ 430,901	$ 24,949	$ 12,874
Unexpended Appropriations				
Beginning Balances	$ 0	$ 0	$ 0	$ 0
Prior period adjustments (+/-)	0	0	0	0
Beginning Balances, as adjusted	$ 0	$ 0	$ 0	$ 0
Budgetary Financing Sources:				
Appropriations Received	$ 0	$ 0	$ 0	$ 0
Appropriations transferred in/out (+/-)	0	0	0	0
Other adjustments (rescissions, etc) (+/-)	0	0	0	0
Appropriations used	0	0	0	0
Nonexchange revenue	0	0	0	0
Donations and forfeitures of cash and cash equivalents	0	0	0	0
Transfers in/out without reimbursement (+/-)	0	0	0	0
Other budgetary financing sources (+/-)	0	0	0	0
Other Financing Sources:				
Donations and forfeitures of property	0	0	0	0
Transfers in/out without reimbursement (+/-)	0	0	0	0
Imputed financing from costs absorbed by others	0	0	0	0
Other (+/-)	0	0	0	0
Total Financing Sources	$ 0	$ 0	$ 0	$ 0
Net Cost of Operations (+/-)	$ 0	$ 0	$ 0	$ 0
Ending Balances	$ 0	$ 0	$ 0	$ 0

Department of Defense
Navy Working Capital Fund
CONSOLIDATING STATEMENT OF CHANGES IN NET POSITION
For the years ended September 30, 2004 and 2003
($ in thousands)

	Transportation	Base Support	Research & Development	Supply Management
Cumulative Results of Operations				
Beginning Balances	$ (40,575)	$ 743,193	$ 554,407	$ 15,914,791
Prior period adjustments (+/-)				
Prior Period Adjustments - Restated (+/-)	0	0	0	0
Beginning Balance, Restated	(40,575)	743,193	554,407	15,914,791
Prior Period Adjustments - Not Restated (+/-)	0	10	0	(102,357)
Beginning Balances, as adjusted	$ (40,575)	$ 743,203	$ 554,407	$ 15,812,434
Budgetary Financing Sources:				
Appropriations Received	$ 0	$ 0	$ 0	$ 0
Appropriations transferred in/out (+/-)	0	0	0	0
Other adjustments (rescissions, etc) (+/-)	0	0	40,524	0
Appropriations used	0	0	0	130,446
Nonexchange revenue	0	0	0	0
Donations and forfeitures of cash and cash equivalents	0	0	0	0
Transfers in/out without reimbursement (+/-)	0	0	0	45,184
Other budgetary financing sources (+/-)	0	0	0	0
Other Financing Sources:				
Donations and forfeitures of property	0	0	0	0
Transfers in/out without reimbursement (+/-)	(419)	(24,954)	(404,916)	(633,515)
Imputed financing from costs absorbed by others	0	0	0	
Other (+/-)	0	0	0	0
Total Financing Sources	$ (419)	$ (24,954)	$ (364,392)	$ (457,885)
Net Cost of Operations (+/-)	$ (15,233)	$ (21,599)	$ 36,671	$ 763,545
Ending Balances	$ (25,761)	739,848	153,344	14,591,004
Unexpended Appropriations				
Beginning Balances	$ 0	$ 0	$ 0	$ 0
Prior period adjustments (+/-)	0	0	0	0
Beginning Balances, as adjusted	$ 0	$ 0	$ 0	$ 0
Budgetary Financing Sources:				
Appropriations Received	$ 0	$ 0	$ 0	$ 130,446
Appropriations transferred in/out (+/-)	0	0	0	0
Other adjustments (rescissions, etc) (+/-)	0	0	0	0
Appropriations used	0	0	0	(130,446)
Nonexchange revenue	0	0	0	0
Donations and forfeitures of cash and cash equivalents	0	0	0	0
Transfers in/out without reimbursement (+/-)	0	0	0	0
Other budgetary financing sources (+/-)	0	0	0	0
Other Financing Sources:				
Donations and forfeitures of property	0	0	0	0
Transfers in/out without reimbursement (+/-)	0	0	0	0
Imputed financing from costs absorbed by others	0	0	0	0
Other (+/-)	0	0	0	0
Total Financing Sources	$ 0	$ 0	$ 0	$ 0
Net Cost of Operations (+/-)	$ 0	$ 0	$ 0	$ 0
Ending Balances	$ 0	$ 0	$ 0	$ 0

Department of Defense
Navy Working Capital Fund
CONSOLIDATING STATEMENT OF CHANGES IN NET POSITION
For the years ended September 30, 2004 and 2003
($ in thousands)

	Component Level	Combined Total	Eliminations
Cumulative Results of Operations			
Beginning Balances	$ (735,080)	$ 18,136,830	$ 0
Prior period adjustments (+/-)			
Prior Period Adjustments - Restated (+/-)	(1,044,715)	(1,044,715)	
Beginning Balance, Restated	(1,779,795)	17,092,115	
Prior Period Adjustments - Not Restated (+/-)	103,258	0	0
Beginning Balances, as adjusted	$ (1,676,537)	$ 17,092,115	$ 0
Budgetary Financing Sources:			
Appropriations Received	$ 0	$ 0	$ 0
Appropriations transferred in/out (+/-)	0	0	0
Other adjustments (rescissions, etc) (+/-)	(40,524)	0	0
Appropriations used	0	130,446	0
Nonexchange revenue	0	0	0
Donations and forfeitures of cash and cash equivalents	0	0	0
Transfers in/out without reimbursement (+/-)	(290,184)	(287,800)	0
Other budgetary financing sources (+/-)	(419,775)	(419,775)	0
Other Financing Sources:			
Donations and forfeitures of property	0	0	0
Transfers in/out without reimbursement (+/-)	1,269,418	126	0
Imputed financing from costs absorbed by others	536,385	544,886	0
Other (+/-)	0	0	0
Total Financing Sources	$ 1,055,320	$ (32,117)	$ 0
Net Cost of Operations (+/-)	$ 230,994	$ 1,038,125	$ 0
Ending Balances	$ (852,211)	$ 16,021,873	$ 0
Unexpended Appropriations			
Beginning Balances	$ 0	$ 0	$ 0
Prior period adjustments (+/-)	0	0	0
Beginning Balances, as adjusted	$ 0	$ 0	$ 0
Budgetary Financing Sources:			
Appropriations Received	$ 0	$ 130,446	$ 0
Appropriations transferred in/out (+/-)	0	0	0
Other adjustments (rescissions, etc) (+/-)	0	0	0
Appropriations used	0	(130,446)	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	$ 0	$ 0
Net Cost of Operations (+/-)	$ 0	$ 0	$ 0
Ending Balances	$ 0	$ 0	$ 0

Department of Defense
Navy Working Capital Fund
CONSOLIDATING STATEMENT OF CHANGES IN NET POSITION
For the years ended September 30, 2004 and 2003
($ in thousands)

		2004 Consolidated		2003 Consolidated
Cumulative Results of Operations				
Beginning Balances	$	18,136,830	$	18,006,706
Prior period adjustments (+/-)				
Prior Period Adjustments - Restated (+/-)		(1,044,715)		(1,044,715)
Beginning Balance, Restated		17,092,115		16,961,991
Prior Period Adjustments - Not Restated (+/-)		0		0
Beginning Balances, as adjusted	$	17,092,115		16,961,991
Budgetary Financing Sources:				
Appropriations Received	$	0		0
Appropriations transferred in/out (+/-)		0		0
Other adjustments (rescissions, etc) (+/-)		0		0
Appropriations used		130,446		40,200
Nonexchange revenue		0		0
Donations and forfeitures of cash and cash equivalents		0		0
Transfers in/out without reimbursement (+/-)		(287,800)		0
Other budgetary financing sources (+/-)		(419,775)		0
Other Financing Sources:				
Donations and forfeitures of property		0		0
Transfers in/out without reimbursement (+/-)		126		(13,527)
Imputed financing from costs absorbed by others		544,886		543,381
Other (+/-)		0		0
Total Financing Sources	$	(32,117)		570,054
Net Cost of Operations (+/-)	$	1,038,125		439,930
Ending Balances	$	16,021,873	$	17,092,115
Unexpended Appropriations				
Beginning Balances	$	0	$	0
Prior period adjustments (+/-)		0		0
Beginning Balances, as adjusted	$	0	$	0
Budgetary Financing Sources:				
Appropriations Received	$	130,446	$	40,200
Appropriations transferred in/out (+/-)		0		0
Other adjustments (rescissions, etc) (+/-)		0		0
Appropriations used		(130,446)		(40,200)
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	$	0	$	0
Net Cost of Operations (+/-)	$	0	$	0
Ending Balances	$	0	$	0

Department of Defense
Navy Working Capital Fund
COMBINING STATEMENT OF BUDGETARY RESOURCES
For the years ended September 30, 2004 and 2003
($ in thousands)

BUDGETARY FINANCING ACCOUNTS

	Depot Maintenance, Shipyards	Depot Maintenance, Aviation	Depot Maintenance, Marine Corps
BUDGETARY RESOURCES			
Budget Authority:			
Appropriations Received	$ 0	$ 0	$ 0
Borrowing Authority	0	0	0
Contract Authority	22,162	58,804	3,881
Net transfers (+/-)	0	0	0
Other	0	0	0
Unobligated Balance:			
Beginning of period	1,280,688	977,482	119,505
Net transfers, actual (+/-)	0	0	0
Anticipated Transfers Balances	0	0	0
Spending Authority from Offsetting Collections:			
Earned			
Collected	2,326,063	1,988,051	335,370
Receivable from Federal sources	2,778	(66,997)	(7,118)
Change in unfilled customer orders			
Advances received	(82,519)	5,535	617
Without advance from Federal sources	(1,014,455)	(309,249)	33,454
Anticipated for the rest of year, without advances	0	0	0
Transfers from trust funds	0	0	0
Subtotal	$ 1,231,867	$ 1,617,340	$ 362,323
Recoveries of prior year obligations	0	$ 0	$ 0
Temporarily not available pursuant to Public Law	0	0	0
Permanently not available	(4,020)	(36,282)	0
Total Budgetary Resources	$ 2,530,697	$ 2,617,344	$ 485,709

Department of Defense
Navy Working Capital Fund
COMBINING STATEMENT OF BUDGETARY RESOURCES
For the years ended September 30, 2004 and 2003
($ in thousands)

BUDGETARY FINANCING ACCOUNTS

	Depot Maintenance, Shipyards	Depot Maintenance, Aviation	Depot Maintenance, Marine Corps
STATUS OF BUDGETARY RESOURCES			
Obligations Incurred:			
Direct	$ 0	$ 0	$ 0
Reimbursable	2,162,146	1,712,449	337,336
Subtotal	$ 2,162,146	$ 1,712,449	$ 337,336
Unobligated balance:			
Apportioned	$ 368,551	904,894	148,373
Exempt from apportionment	0	0	0
Other available	0	1	0
Unobligated Balances Not Available	0	0	0
Total, Status of Budgetary Resources	$ 2,530,697	$ 2,617,344	$ 485,709
RELATIONSHIP OF OBLIGATIONS TO OUTLAYS:			
Obligated Balance, Net-beginning of period	$ (604,825)	$ (50,372)	$ (99,183)
Obligated Balance transferred, net (+/-)	0	0	0
Obligated Balance, net-end of period:			
Accounts Receivable	(11,508)	(74,443)	(13,218)
Unfilled customer order from Federal sources	(491,963)	(601,970)	(167,210)
Undelivered Orders	403,252	163,963	43,145
Accounts Payable	331,036	529,991	59,116
Outlays:			
Disbursements	2,338,181	2,020,783	289,984
Collections	(2,243,544)	(1,993,586)	(335,987)
Subtotal	$ 94,637	$ 27,197	$ (46,003)
Less: Offsetting receipts	0	0	0
Net Outlays	$ 94,637	$ 27,197	$ (46,003)

Department of Defense
Navy Working Capital Fund
COMBINING STATEMENT OF BUDGETARY RESOURCES
For the years ended September 30, 2004 and 2003
($ in thousands)

BUDGETARY FINANCING ACCOUNTS

	Ordnance	Transportation	Base Support
BUDGETARY RESOURCES			
Budget Authority:			
Appropriations Received	$ 0	$ 0	$ 0
Borrowing Authority	0	0	0
Contract Authority	0	13,100	19,063
Net transfers (+/-)	0	0	0
Other	0	0	0
Unobligated Balance:			
Beginning of period	210,328	210,634	237,706
Net transfers, actual (+/-)	(42,800)	0	0
Anticipated Transfers Balances	0	0	0
Spending Authority from Offsetting Collections:			
Earned			
Collected	410	1,837,235	1,642,345
Receivable from Federal sources	(825)	(44,940)	(22,486)
Change in unfilled customer orders			
Advances received	0	0	(19,893)
Without advance from Federal sources	(15,027)	(27,326)	(13,143)
Anticipated for the rest of year, without advances	0	0	0
Transfers from trust funds	0	0	0
Subtotal	$ (15,442)	$ 1,764,969	$ 1,586,823
Recoveries of prior year obligations	$ 0	$ 0	$ 0
Temporarily not available pursuant to Public Law	0	0	0
Permanently not available	0	(108,143)	(1,424)
Total Budgetary Resources	$ 152,086	$ 1,880,560	$ 1,842,168

Department of Defense
Navy Working Capital Fund
COMBINING STATEMENT OF BUDGETARY RESOURCES
For the years ended September 30, 2004 and 2003
($ in thousands)

BUDGETARY FINANCING ACCOUNTS

	Ordnance	Transportation	Base Support
STATUS OF BUDGETARY RESOURCES			
Obligations Incurred:			
Direct	$ 0	$ 0	$ 0
Reimbursable	104,513	1,689,098	1,499,704
Subtotal	$ 104,513	$ 1,689,098	$ 1,499,704
Unobligated balance:			
Apportioned	$ 47,573	191,462	342,464
Exempt from apportionment	0	0	0
Other available	0	0	0
Unobligated Balances Not Available	0	0	0
Total, Status of Budgetary Resources	$ 152,086	$ 1,880,560	$ 1,842,168
RELATIONSHIP OF OBLIGATIONS TO OUTLAYS:			
Obligated Balance, Net-beginning of period	$ (101,338)	$ 195,619	$ 122,306
Obligated Balance transferred, net (+/-)	0	0	0
Obligated Balance, net-end of period:			
Accounts Receivable	(2)	(98,318)	(121,518)
Unfilled customer order from Federal sources	0	(130,904)	(238,925)
Undelivered Orders	442	26,874	66,342
Accounts Payable	18,478	459,267	294,781
Outlays:			
Disbursements	108	1,700,064	1,656,960
Collections	(410)	(1,837,235)	(1,622,451)
Subtotal	$ (302)	$ (137,171)	$ 34,509
Less: Offsetting receipts	0	0	0
Net Outlays	$ (302)	$ (137,171)	$ 34,509

Department of Defense
Navy Working Capital Fund
COMBINING STATEMENT OF BUDGETARY RESOURCES
For the years ended September 30, 2004 and 2003
($ in thousands)

BUDGETARY FINANCING ACCOUNTS

	Research & Development	Supply Management	Component Level
BUDGETARY RESOURCES			
Budget Authority:			
Appropriations Received	$ 0	$ 130,446	$ 0
Borrowing Authority	0	0	0
Contract Authority	125,500	112,662	0
Net transfers (+/-)	0	0	0
Other	0	0	0
Unobligated Balance:			
Beginning of period	1,035,504	37,363	404,115
Net transfers, actual (+/-)	0	0	(245,000)
Anticipated Transfers Balances	0	0	0
Spending Authority from Offsetting Collections:			
Earned			
Collected	10,119,066	5,882,342	(204,072)
Receivable from Federal sources	48,721	27,582	312,629
Change in unfilled customer orders			
Advances received	186,327	0	0
Without advance from Federal sources	(153,892)	(225,028)	0
Anticipated for the rest of year, without advances	0	0	0
Transfers from trust funds	0	0	0
Subtotal	$ 10,200,222	$ 5,684,896	$ 108,557
Recoveries of prior year obligations	$ 0	$ 0	$ 0
Temporarily not available pursuant to Public Law	0	0	0
Permanently not available	(22,722)	(13,938)	0
Total Budgetary Resources	$ 11,338,504	$ 5,951,429	$ 267,672

Department of Defense
Navy Working Capital Fund
COMBINING STATEMENT OF BUDGETARY RESOURCES
For the years ended September 30, 2004 and 2003
($ in thousands)

BUDGETARY FINANCING ACCOUNTS

	Research & Development	Supply Management	Component Level
STATUS OF BUDGETARY RESOURCES			
Obligations Incurred:			
Direct	$ 0	$ 0	$ 0
Reimbursable	9,942,870	5,700,391	1,167,941
Subtotal	$ 9,942,870	$ 5,700,391	$ 1,167,941
Unobligated balance:			
Apportioned	$ 1,395,633	152,093	(900,267)
Exempt from apportionment	0	0	0
Other available	1	0	(2)
Unobligated Balances Not Available	0	98,945	0
Total, Status of Budgetary Resources	$ 11,338,504	$ 5,951,429	$ 267,672
RELATIONSHIP OF OBLIGATIONS TO OUTLAYS:			
Obligated Balance, Net-beginning of period	$ 147,391	$ 4,517,578	$ (853,062)
Obligated Balance transferred, net (+/-)	0	0	0
Obligated Balance, net-end of period:			
Accounts Receivable	(34,971)	(244,746)	8,282
Unfilled customer order from Federal sources	(4,659,151)	(741,338)	0
Undelivered Orders	2,234,203	3,953,838	0
Accounts Payable	2,678,205	1,138,718	(541,042)
Outlays:			
Disbursements	9,977,146	6,308,943	535,009
Collections	(10,305,393)	(5,882,342)	204,072
Subtotal	$ (328,247)	$ 426,601	$ 739,081
Less: Offsetting receipts	0	0	0
Net Outlays	$ (328,247)	$ 426,601	$ 739,081

Department of Defense
Navy Working Capital Fund
COMBINING STATEMENT OF BUDGETARY RESOURCES
For the years ended September 30, 2004 and 2003
($ in thousands)

BUDGETARY FINANCING ACCOUNTS

	2004 Combined	2003 Combined
BUDGETARY RESOURCES		
Budget Authority:		
Appropriations Received	$ 130,446	$ 40,200
Borrowing Authority	0	0
Contract Authority	355,172	558,144
Net transfers (+/-)	0	0
Other	0	0
Unobligated Balance:		
Beginning of period	4,513,325	4,117,221
Net transfers, actual (+/-)	(287,800)	(30,200)
Anticipated Transfers Balances	0	0
Spending Authority from Offsetting Collections:		
Earned		
Collected	23,926,810	25,585,547
Receivable from Federal sources	249,344	(432,227)
Change in unfilled customer orders		
Advances received	90,067	178,239
Without advance from Federal sources	(1,724,666)	1,964,175
Anticipated for the rest of year, without advances	0	0
Transfers from trust funds	0	0
Subtotal	$ 22,541,555	$ 27,295,734
Recoveries of prior year obligations	$ 0	$ 0
Temporarily not available pursuant to Public Law	0	0
Permanently not available	(186,529)	(204,140)
Total Budgetary Resources	$ 27,066,169	$ 31,776,959

Department of Defense
Navy Working Capital Fund
COMBINING STATEMENT OF BUDGETARY RESOURCES
For the years ended September 30, 2004 and 2003
($ in thousands)

BUDGETARY FINANCING ACCOUNTS

	2004 Combined	2003 Combined
STATUS OF BUDGETARY RESOURCES		
Obligations Incurred:		
Direct	$ 0	$ 0
Reimbursable	24,316,448	27,263,631
Subtotal	$ 24,316,448	27,263,631
Unobligated balance:		
Apportioned	$ 2,650,776	4,632,115
Exempt from apportionment	0	0
Other available	0	2
Unobligated Balances Not Available	98,945	(118,789)
Total, Status of Budgetary Resources	$ 27,066,169	$ 31,776,959
RELATIONSHIP OF OBLIGATIONS TO OUTLAYS:		
Obligated Balance, Net-beginning of period	$ 3,274,114	$ 2,985,762
Obligated Balance transferred, net (+/-)	0	0
Obligated Balance, net-end of period:		
Accounts Receivable	(590,442)	(341,097)
Unfilled customer order from Federal sources	(7,031,461)	(8,756,130)
Undelivered Orders	6,892,059	7,998,442
Accounts Payable	4,968,550	4,372,899
Outlays:		
Disbursements	24,827,178	25,443,332
Collections	(24,016,876)	(25,763,785)
Subtotal	$ 810,302	(320,453)
Less: Offsetting receipts	0	0
Net Outlays	$ 810,302	$ (320,453)

Department of Defense
Navy Working Capital Fund
COMBINING STATEMENT OF FINANCING
For the years ended September 30, 2004 and 2003
($ in thousands)

	Depot Maintenance, Shipyards	Depot Maintenance, Aviation	Depot Maintenance, Marine Corps
Resources Used to Finance Activities:			
Budgetary Resources Obligated			
Obligations Incurred	$ 2,162,146	$ 1,712,449	$ 337,336
Less: Spending Authority from offsetting collections and recoveries (-)	(1,231,867)	(1,617,340)	(362,323)
Obligations net of offsetting collections and recoveries	$ 930,279	$ 95,109	$ (24,987)
Less: Offsetting receipts (-)	0	0	0
Net obligations	$ 930,279	$ 95,109	$ (24,987)
Other Resources			
Donations and forfeitures of property	0	0	0
Transfers in/out without reimbursement (+/-)	(38,474)	3,559	(50,573)
Imputed financing from costs absorbed by others	0	0	8,501
Other (+/-)	0	0	0
Net other resources used to finance activities	$ (38,474)	$ 3,559	$ (42,072)
Total resources used to finance activities	$ 891,805	$ 98,668	$ (67,059)
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 (-)	$ 195,479	$ 10,446	$ (7,818)
Unfilled Customer Orders	(1,096,974)	(303,714)	34,070
Resources that fund expenses recognized in prior periods	0	0	(703)
Budgetary offsetting collections and receipts that do not affect Net Cost of Operations	0	0	0
Resources that finance the acquisition of assets	(10,084)	(37,302)	(20,888)
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 (+/-)	38,474	(3,559)	50,573
Total resources used to finance items not part of the Net Cost of Operations	$ (873,105)	$ (334,129)	$ 55,234
Total resources used to finance the Net Cost of Operations	$ 18,700	$ (235,461)	$ (11,825)

Department of Defense
Navy Working Capital Fund
COMBINING STATEMENT OF FINANCING
For the years ended September 30, 2004 and 2003
($ in thousands)

	Depot Maintenance, Shipyards	Depot Maintenance, Aviation	Depot Maintenance, Marine Corps
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 Periods:			
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 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	$ 22,827	$ 41,747	$ 3,644
Revaluation of assets and liabilities (+/-)	0	0	0
Other (+/-)			
Trust Fund Exchange Revenue	0	0	0
Cost of Goods Sold	25,893	181,545	(363)
Operating Material & Supplies Used	0	0	0
Other	0	5,121	3
Total components of Net Cost of Operations that will not require or generate resources	$ 48,720	$ 228,413	$ 3,284
Total components of Net Cost of Operations that will not require or generate resources in the current period	$ 48,720	$ 228,413	$ 3,284
Net Cost of Operations	$ 67,420	$ (7,048)	$ (8,541)

Department of Defense
Navy Working Capital Fund
COMBINING STATEMENT OF FINANCING
For the years ended September 30, 2004 and 2003
($ in thousands)

	Ordnance	Transportation	Base Support
Resources Used to Finance Activities:			
Budgetary Resources Obligated			
Obligations Incurred	$ 104,513	$ 1,689,098	$ 1,499,704
Less: Spending Authority from offsetting collections and recoveries (-)	15,442	(1,764,969)	(1,586,822)
Obligations net of offsetting collections and recoveries	$ 119,955	$ (75,871)	$ (87,118)
Less: Offsetting receipts (-)	0	0	0
Net obligations	$ 119,955	$ (75,871)	$ (87,118)
Other Resources			
Donations and forfeitures of property	0	0	0
Transfers in/out without reimbursement (+/-)	(120,000)	(419)	(24,954)
Imputed financing from costs absorbed by others	0	0	0
Other (+/-)	0	0	0
Net other resources used to finance activities	$ (120,000)	$ (419)	$ (24,954)
Total resources used to finance activities	$ (45)	$ (76,290)	$ (112,072)
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 (-)	$ 6,129	$ (44,176)	$ 104,662
Unfilled Customer Orders	(15,027)	(27,326)	(33,037)
Resources that fund expenses recognized in prior periods	0	0	0
Budgetary offsetting collections and receipts that do not affect Net Cost of Operations	0	0	0
Resources that finance the acquisition of assets	(119,139)	126,786	(25,643)
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 (+/-)	120,000	419	24,954
Total resources used to finance items not part of the Net Cost of Operations	$ (8,037)	$ 55,703	$ 70,936
Total resources used to finance the Net Cost of Operations	$ (8,082)	$ (20,587)	$ (41,136)

Department of Defense
Navy Working Capital Fund
COMBINING STATEMENT OF FINANCING
For the years ended September 30, 2004 and 2003
($ in thousands)

	Ordnance	Transportation	Base Support
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 Periods:			
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 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	$ 0	$ 5,353	$ 17,562
Revaluation of assets and liabilities (+/-)	0	0	0
Other (+/-)			
Trust Fund Exchange Revenue	0	0	0
Cost of Goods Sold	0	0	0
Operating Material & Supplies Used	0	0	0
Other	0	0	1,976
Total components of Net Cost of Operations that will not require or generate resources	$ 0	$ 5,353	$ 19,538
Total components of Net Cost of Operations that will not require or generate resources in the current period	$ 0	$ 5,353	$ 19,538
Net Cost of Operations	$ (8,082)	$ (15,234)	$ (21,598)

Department of Defense
Navy Working Capital Fund
COMBINING STATEMENT OF FINANCING
For the years ended September 30, 2004 and 2003
($ in thousands)

	Research & Development	Supply Management	Component Level
Resources Used to Finance Activities:			
Budgetary Resources Obligated			
Obligations Incurred	$ 9,942,870	$ 5,700,391	$ 1,167,941
Less: Spending Authority from offsetting collections and recoveries (-)	(10,200,222)	(5,684,896)	(108,557)
Obligations net of offsetting collections and recoveries	$ (257,352)	$ 15,495	$ 1,059,384
Less: Offsetting receipts (-)	0	0	0
Net obligations	$ (257,352)	$ 15,495	$ 1,059,384
Other Resources			
Donations and forfeitures of property	0	0	0
Transfers in/out without reimbursement (+/-)	(404,916)	(633,515)	1,269,417
Imputed financing from costs absorbed by others	0	0	536,385
Other (+/-)	0	0	0
Net other resources used to finance activities	$ (404,916)	$ (633,515)	$ 1,805,802
Total resources used to finance activities	$ (662,268)	$ (618,020)	$ 2,865,186
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 (-)	$ 9,349	$ 831,337	$ 37,113
Unfilled Customer Orders	32,435	(225,028)	0
Resources that fund expenses recognized in prior periods	0	0	(240,924)
Budgetary offsetting collections and receipts that do not affect Net Cost of Operations	0	0	0
Resources that finance the acquisition of assets	(193,861)	(3,644,614)	(1,120,440)
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 (+/-)	445,440	633,515	(1,309,941)
Total resources used to finance items not part of the Net Cost of Operations	$ 293,363	$ (2,404,790)	$ (2,634,192)
Total resources used to finance the Net Cost of Operations	$ (368,905)	$ (3,022,810)	$ 230,994

Department of Defense
Navy Working Capital Fund
COMBINING STATEMENT OF FINANCING
For the years ended September 30, 2004 and 2003
($ in thousands)

	Research & Development	Supply Management	Component Level
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 Periods:			
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 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	$
Components not Requiring or Generating Resources:			
Depreciation and amortization	$ 155,364	$ 8,760	$ 0
Revaluation of assets and liabilities (+/-)	0	42,926	(2)
Other (+/-)			
Trust Fund Exchange Revenue	0	0	0
Cost of Goods Sold	250,212	3,703,451	0
Operating Material & Supplies Used	0	0	0
Other	0	31,272	0
Total components of Net Cost of Operations that will not require or generate resources	$ 405,576	$ 3,786,355	$ (2)
Total components of Net Cost of Operations that will not require or generate resources in the current period	$ 405,576	$ 3,786,355	$ (2)
Net Cost of Operations	$ 36,671	$ 763,545	$ 230,992

Department of Defense
Navy Working Capital Fund
COMBINING STATEMENT OF FINANCING
For the years ended September 30, 2004 and 2003
($ in thousands)

	2004 Combined	2003 Combined
Resources Used to Finance Activities:		
Budgetary Resources Obligated		
Obligations Incurred	$ 24,316,448	$ 27,263,631
Less: Spending Authority from offsetting collections and recoveries (-)	(22,541,554)	(27,295,734)
Obligations net of offsetting collections and recoveries	$ 1,774,894	$ (32,103)
Less: Offsetting receipts (-)	0	0
Net obligations	$ 1,774,894	$ (32,103)
Other Resources		
Donations and forfeitures of property	0	0
Transfers in/out without reimbursement (+/-)	125	(13,527)
Imputed financing from costs absorbed by others	544,886	543,381
Other (+/-)	0	0
Net other resources used to finance activities	$ 545,011	$ 529,854
Total resources used to finance activities	$ 2,319,905	$ 497,751
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 (-)	$ 1,142,521	$ (703,528)
Unfilled Customer Orders	(1,634,601)	2,142,413
Resources that fund expenses recognized in prior periods	(241,627)	0
Budgetary offsetting collections and receipts that do not affect Net Cost of Operations	0	8
Resources that finance the acquisition of assets	(5,045,185)	(1,899,644)
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 (+/-)	(125)	0
Total resources used to finance items not part of the Net Cost of Operations	$ (5,779,017)	$ (460,751)
Total resources used to finance the Net Cost of Operations	$ (3,459,112)	$ 37,000

Department of Defense
Navy Working Capital Fund
COMBINING STATEMENT OF FINANCING
For the years ended September 30, 2004 and 2003
($ in thousands)

	2004 Combined	2003 Combined
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 Periods:		
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 public (-)	0	0
Other (+/-)	0	83,927
Total components of Net Cost of Operations that will require or generate resources in future periods	$ 0	$ 83,927
Components not Requiring or Generating Resources:		
Depreciation and amortization	$ 255,203	$ 243,755
Revaluation of assets and liabilities (+/-)	42,924	74,973
Other (+/-)		
Trust Fund Exchange Revenue	0	0
Cost of Goods Sold	4,160,738	0
Operating Material & Supplies Used	0	0
Other	38,732	275
Total components of Net Cost of Operations that will not require or generate resources	$ 4,497,237	$ 319,003
Total components of Net Cost of Operations that will not require or generate resources in the current period	$ 4,497,237	$ 402,930
Net Cost of Operations	$ 1,038,125	$ 439,930

Department of the Navy

Navy Working Capital Fund Required Supplementary Information

Navy Working Capital Fund
Required Supplementary Information

Navy Working Capital Fund
General Property, Plant, and Equipment
Real Property Deferred Annual Sustainment and Restoration Tables
As of September 30, 2004
($ in Millions)

Annual Sustainment FY 2004			
	Required	**Actual**	**Difference**
Navy	$ 230	$ 230	0
Marine Corps	5	5	0
Building, Structures, and Utilities	$ 235	$ 235	0

Annual Deferred Sustainment Trend				
	FY 2001	**FY 2002**	**FY 2003**	**FY 2004**
Navy	-	-	-	0
Marine Corps	-	-	-	0
Building, Structures, and Utilities	$ 72	0	0	0

Restoration and Modernization Requirements			
	End FY 2003	**End FY 2004**	**Change**
Navy	-	-	0
Marine Corps	-	-	0
Building, Structures, and Utilities	0	0	0

Narrative Statement:
Fiscal Year 2004 represents the third year in which the Facility Sustainment Model (FSM) was utilized. Deferred amounts were calculated in accordance with the methodology provided by DoD Financial Management Regulation, Volume 6B, Chapter 12. The output of the Facility Sustainment Model continues to undergo quality checks to ensure its accuracy. Accordingly, requirements for each fiscal year are prepared with a more updated and accurate version of the model.

In FY 2004, FSM version 4.0 was used for programming and budgeting facilities sustainment.

This year represents the first year that separate breakout of Navy and Marine Corps sustainment amounts can be provided.

Presently, final execution figures for NWCF are not available. The amounts shown on this table reflect the budgeted amounts and will be updated as soon as execution data is available.

The NWCF has no material amounts of deferred sustainment for the General Property, Plant, and Equipment categories of Personal Property, Heritage Assets, or Stewardship Land.

Schedule, Part A DoD Intra-governmental Asset Balances. *($ Amounts in Thousands)*	Treasury Index	Fund Balance with Treasury	Accounts Receivable	Loans Receivable	Investments	Other
Architect of the Capitol	01		11			
Library of Congress	03		-			
Government Printing Office	04		126			
General Accounting Office	05		-			
The Judiciary	10		-			
Executive Office of the President	11		53			
Department of Agriculture	12		219			
Department of Commerce	13		1,209			
Department of the Interior	14		375			
Department of Justice	15		1,192			
Department of Labor	16		-			
Department of the Navy	17		568,385			
United States Postal Service	18		57			
Department of State	19		4,956			
Department of the Treasury	20	861,243	3,990			
Department of the Army	21		33,598			
Resolution Trust Corporation	22		-			
Office of Personnel Management	24		1			
Federal Communications Commission	27		-			
Social Security Administration	28		-			
Federal Trade Commission	29		38			
Nuclear Regulatory Commission	31		26			
Smithsonian Institution	33		-			
Department of Veterans Affairs	36		182			
Pennsylvania Avenue Development Corp	42		-			
General Service Administration	47		1,822			
National Science Foundation	49		37			
Advisory Commission on Intergovernmental Relations	55		3			
Department of the Air Force	57		60,640			
National Foundation on the Arts and the Humanities	59		10			
Consumer Product Safety Commission	61		2			
Tennessee Valley Authority	64		8			
Environmental Protection Agency	68		625			
Department of Transportation	69		7,791			
Depatment of Homeland Security	70		20,808			
Small Business Administration	73		1,156			
Department of Health and Human Services	75		1,727			
National Aeronautics and Space Administration	80		5,915			
Export-Import Bank of the United States	83		37			
Department of Energy	89		2,315			
Selective Service System	90		31			
Department of Education	91		5			
Independent Agencies	95		272			
Corps of Engineers, Civil	96		270			
Other Defense Organizations General Funds	97		124,765			
Other Defense Organizations Working Capital Funds	97-4930		3,864			
Army Working Capital Fund	97-4930.001		6,832			15
Air Force Working Capital Fund	97-4930.003		4,163			
	Totals:	$ 861,243	$ 857,516	$ -	$ -	$ 15

Note: Totals might not match the amounts shown on the Principal Statements.

Schedule, Part B DoD Intragovernmental entity liabilities. *($ Amounts in Thousands)*	**Treasury Index:**	**Accounts Payable**	**Debts/Borrowings From Other Agencies**	**Other**
Department of Agriculture	12	6		
Department of Commerce	13	71		
Department of the Interior	14	(143)		
Department of Justice	15	5		
Department of Labor	16	54		
Depatment of the Navy	17	56,800		
United States Postal Service	18	976		
Department of the Treasury	20	132	506,278	
Office of Personnel Management	24	36,228		37,201
Federal Communications Commission	27	3,028		
Department of Veterans Affairs	36	0		
Government Printing Office	4	1		
General Service Administration	47	1,426		
National Science Foundation	49	951		
Air Force General Fund	57	1,507		
Depatment of Homeland Security	70	50		72,510
National Aeronautics and Space Administration	80	884		
Department of Energy	89	24		
Other Defense Organizations General Funds	97	2,152		
Other Defense Organizations Working Capital Funds	97-4930	124,187		
Defense Working Capital Fund, Army	97-4930.001	6,320		
Defense Working Capital Fund, Airforce	97-4930.003	9,320		
The General Fund of the Treasury	99			5,141
	Totals:	**$ 243,979**	**$ 506,278**	**$ 114,852**

Note: Totals might not match the amounts shown on the Principal Statements.

Schedule, Part C DoD Intragovernmental revenue and related costs. *($ Amounts in Thousands)*	**Treasury Index:**	**Earned Revenue**
Architect of the Capitol	01	$ 792
Library of Congress	03	921
Government Printing Office	04	162
The Judiciary	10	-
Executive Office of the President	11	2,057
Department of Agriculture	12	14,975
Department of Commerce	13	10,144
Department of the Interior	14	2,394
Department of Justice	15	104,170
Department of Labor	16	716
Department of the Navy	17	18,912,132
United States Postal Service	18	98
Department of State	19	16,974
Department of the Treasury	20	8,636
Department of the Army	21	288,024
Resolution Trust Corporation	22	20
Office of Personnel Management	24	61
Federal Communications Commission	27	(2)
Social Security Administration	28	106
Federal Trade Commission	29	420
Nuclear Regulatory Commission	31	1,536
Smithsonian Institution	33	739
Department of Veterans Affairs	36	1,255
Pennsylvania Avenue Development Corporation	42	169
General Services Administration	47	2,213
National Science Foundation	49	14,483
Advisory Commission on Intergovernmental Relations	55	269
Department of the Air Force	57	525,513
Federal Emergency Management Agency	58	822
Consumer Product Safety Commission	61	12
Tennessee Valley Authority	64	105
Environmental Protection Agency	68	1,932
Department of Transportation	69	19,158
Department of Homeland Security	70	104,975
Agency for International Development	72	16,267
Small Business Administration	73	16
Department of Health and Human Services	75	14,581
Independent Agencies	76	-
National Aeronautics and Space Administration	80	52,883
Export-Import Bank of the United States	83	137
Department of Energy	89	31,563
Selective Service System	90	75
Department of Education	91	28
Independent Agencies	95	131
Corps of Engineers, Civil	96	206
Other Defense Organizations General Fund	97	1,167,947
Department of Defense Working Capital Funds	97-4930	78,260
Defense Working Capital Fund, Army	97-4930.001	67,181
Defense Working Capital Fund, Air Force	97-4930.003	233,845
The General Fund of the Treasury	99	(5,141)
	Total	$ 21,693,791

Note: Totals might not match the amounts shown on the Principal Statements.

Required Supplemental Information - Part E *($ Amounts in Thousands)*	**Treasury Index:**	**Transfers In**	**Transfers Out**
Navy General Fund	17		$ 45,177
Army General Fund	21		$ 200,000
US Army Corps of Engineers	96	$ 211	
Other Defense Organizations General Funds	97		$ 0
Other Defense Organizations Working Capital Funds	97-4930	$ 92	$ 42,800
Totals might not match reports	Totals:	$ 303	$ 287,977

Note: Totals might not match the amounts shown on the Principal Statements.

Department of the Navy

Navy Working Capital Fund Other Accompanying Information

Appropriations, Funds, and Accounts Included in the Financial Statements

Reporting Entity

Navy Working Capital Fund

Fund/Account Treasury Symbol and Title:

97X4930 002

Navy Working Capital Fund Activity Group Treasury Symbol and Title:

97X4930.NA1*	Depot Maintenance-Shipyards
97X4930.NA2*	Depot Maintenance-Aviation
97X4930.NA4*	Depot Maintenance- Other (Marine Corps)
97X4930.NA3* a	Ordnance
97X4930.ND*	Transportation
97X4930.NE* *	Base Support
97X4930.NH**	Research and Development
97X4930.NC**	Supply Management

Notes

* - The "*" represents alpha or numeric characters which identify an activity or reporting segment of the activity group.

a - The Ordnance activity group became a part of the DON General Fund in FY 2000. The Ordnance information included in this report represents residual NWCF accounting for this group.

Department of the Navy

Audit Opinions

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

November 8, 2004

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

SUBJECT: Independent Auditor's Report on the Fiscal Year 2004 Department of the Navy General Fund Financial Statements (Report No. D-2005-013)

The Chief Financial Officers Act of 1990, as amended, requires the Inspector General of the Department of Defense to audit the accompanying Department of the Navy 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; and the Combined Statement of Financing for the fiscal years then ended. The financial statements are the responsibility of the Department of the Navy management. The Department of the Navy 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 Department of the Navy 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 Navy (Financial Management and Comptroller) acknowledged to us that material deficiencies in the Department of the Navy financial statements still exist. 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 Department of the Navy 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 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.

[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.

Summary of Internal Control

In planning our audit, we considered the Department of the Navy's 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:

- Accounting and Financial Management Systems;
- Fund Balance with Treasury;
- Accounts Receivable;
- Inventory and Related Property;
- General Property, Plant, and Equipment;
- Accounts Payable;
- Environmental Liabilities; and
- Problem Disbursements.

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 Assistant Secretary of the Navy (Financial Management and Comptroller) acknowledged to us that critical financial management and feeder systems do not comply with Federal financial systems requirements, Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level, as required under the Federal Financial Management Improvement Act (FFMIA) of 1996. Therefore, we did not determine whether the Department of the Navy 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.

---

[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 (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

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. The purpos 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 Department of the Navy that is based, in whole or in part, on information that is inaccurate because of these deficiencies. Financial information reported by the Department of the Navy also may contain misstatements resulting from these deficiencies.

Accounting and Financial Management Systems. The Department of the Navy financial systems deficiencies include the inability to implement elements of Generally Accepted Accounting Principles (GAAP), and inadequately implement the U.S. Government Standard General Ledger. Also, adjusting entries were needed to correct errors caused by differences between accounting systems.

Fund Balance with Treasury. Inaccurate or missing fund accounting codes have resulted in unmatched disbursements and collections; the use of suspense and budget clearing accounts; deposits-in transit; check discrepancies; undistributed disbursements, collections, and abnormal balances; and an inability to reconcile the Department of the Navy records with the Department of the Treasury records.

Accounts Receivable. Intragovernmental accounts receivable may be overstated becaus of outstanding over aged reimbursable work orders. Seller side trading partner data are neither captured nor maintained at a transaction level detail, or may be missing or incomplete because of system deficiencies. Accounts receivable balances with the public may not be complete or accurate because of system and procedural problems. An inadequate audit trail exists because of unmatched and undistributed collections being posted to accounts receivable at a summary level based on percentages.

Inventory and Related Property. The legacy systems currently being used do not maintain the historical cost data necessary to comply with Statement of Federal Financial Accounting Standards Number 3, "Accounting for Inventory and Related Property." In addition, completeness issues exist because these legacy systems were not designed to ensure that all of the inventory items are included in the values reported on the Balance Sheet. Also, some commands have not used the consumption method for expensing Operating Materials and Supplies (OM&S). Some commands are unable to report OM& at the detailed transaction level and only maintain beginning and ending balances.

General Property, Plant, and Equipment. Completeness issues associated with recognizing internal use software and leasehold improvements still exist. Trading partne data for capitalizing assets may not always be recorded. Statement of Federal Financial Accounting Standards No. 23, "Eliminating the Category National Defense Property Plan and Equipment," has not been fully implemented.

Accounts Payable. Intragovernmental accounts payable such as MILSTRIP, fuel payables, and non-PowerTrack transportation charges are not being recorded timely, completely, or accurately. There is a lack of sufficient systems, processes, and data to support reconciliation of buyer-side trading partner information. Accounts payable with the public are not being recorded timely, completely, or accurately in all cases. Some existing procedures create abnormal balances.

Environmental Liabilities. Non-Defense Environmental Restoration Program liabilities are not currently being reported and therefore the line is not ready for audit.

Problem Disbursements. Inaccurate or missing fund accounting codes have resulted in unmatched disbursements and collections requiring use of suspense accounts. The suspense accounts cause difficulty in reconciling Department of the Navy fund records with Treasury's records.

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 Department of the Navy 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.

Financial Management Systems. The Department of the Navy is required to comply with financial management systems reporting requirements. For example, the Federal Financial Management Improvement Act of 1996 requires the Department of the Navy to establish and maintain financial management systems that comply substantially with the Federal financial management system 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 Department of the Navy to evaluate the systems and to annually report whether those systems are in compliance with applicable requirements. The Chief Financial Officers Act of 1990 requires the DoD to prepare a 5-year Financial Management Plan describing activities that DoD will conduct during the next 5 years to improve financial management.

The Department of the Navy acknowledged that many of its critical financial management and feeder systems do not comply substantially with the Federal financial management systems requirements, applicable Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level. In an attempt to comply with statutory reporting requirements and applicable financial system requirements, DoD is developing a DoD-wide Business Enterprise Architecture. The architecture will provide a blue print of the Department's financial management systems and processes to initiate a comprehensive financial management reform effort. Until the architecture is fully developed, the Department of the Navy 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 Navy (Financial Management and Comptroller) acknowledged to us on February 18, 2004, that the Navy General Fund financial management systems cannot provide adequate evidence supporting various material amounts on the financial statements. Therefore, we did not conduct audit work related to deficiencies identified during previous audits of the Department of the Navy.

In addition, we did not perform audit work related to the following selected provisions of laws and regulations: the Antideficiency Act, the Prompt Payment Act, and the Federal Credit Reform 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.

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

November 8, 2004

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

SUBJECT: Independent Auditor's Report on the Fiscal Year 2004 Department of the Navy Working Capital Fund Financial Statements (Report No. D-2005-012)

The Chief Financial Officers Act of 1990, as amended, requires the Inspector General of the Department of Defense to audit the accompanying Department of the Navy 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 the Department of the Navy management. The Department of the Navy 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 Department of the Navy 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 Navy (Financial Management and Comptroller) acknowledged to us that material deficiencies in the Department of the Navy Working Capital Fund financial statements still exist. 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 Department of the Navy 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 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.

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

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

Summary of Internal Control

In planning our audit, we considered the Department of the Navy 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:

- Accounting and Financial Management Systems;
- Fund Balance with Treasury;
- Accounts Receivable;
- Inventory and Related Property;
- 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. The Assistant Secretary of the Navy (Financial Management and Comptroller) acknowledged to us that critical financial management and feeder systems do not comply with Federal Financial systems requirements, Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level, as required under the Federal Financial Management Improvement Act (FFMIA) of 1996. Therefore, we did not determine whether the Department of the Navy 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.

[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 (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

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. The 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 Department of the Navy that is based, in whole or in part, on information that is inaccurate because of these deficiencies. Financial information reported by the Department of the Navy also may contain misstatements resulting from these deficiencies.

Accounting and Financial Management Systems. The Department of the Navy financial systems deficiencies include the inability to implement elements of Generally Accepted Accounting Principles (GAAP), and inadequately implement the U.S. Government Standard General Ledger. Also, adjusting entries were needed to correct errors caused by differences between accounting systems.

Fund Balance with Treasury. Reconciliations are not consistently being completed between the Department of the Navy Working Capital Fund cash account and the Treasury cash account. In addition, the lack of a direct system interface between the Financial Reporting Systems and other financial systems causes unmatched collections and disbursements.

Accounts Receivable. Recognition and collection of public accounts receivables for contract overpayments, travel advances, and employee debt are not always recorded. In addition, subsidiary records are not reconciled to their corresponding general ledger on a regular basis. Furthermore, trading partner adjustments posted to intragovernmental accounts receivables are not supported by detailed transactions.

Inventory and Related Property. Supply Management activities do not comply with GAAP because Navy records inventories at the latest acquisition cost. Currently, adequate data, processes, and methodologies do not exist to convert Navy inventory to approximations of historical cost.

General Property, Plant, and Equipment. The Supply Management Business Area is not properly recording their assets and depreciation within their accounting systems. In addition, buyer side trading partner information is not currently being captured and reported.

Accounts Payable. Insufficient or inconsistent reconciliations and lack of direct system interfaces cause matching difficulties, undistributed disbursements, and the inability to capture trading partner 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 noncompliance, and previously reported instances of noncompliance continue to exist. Therefore, we did not determine whether the Department of the Navy 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.

Financial Management Systems. The Department of the Navy is required to comply with financial management systems reporting requirements. For example, the Federal Financial Management Improvement Act of 1996 requires the Department of the Navy to establish and maintain financial management systems that comply substantially with the Federal financial management system 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 Department of the Navy to evaluate the systems and to annually report whether those systems are in compliance with applicable requirements. The Chief Financial Officers Act of 1990 requires DoD to prepare a 5-year Financial Management Plan describing activities that DoD will conduct during the next 5 years to improve financial management.

The Department of the Navy acknowledged that many of its critical financial management and feeder systems do not comply substantially with the Federal financial management systems requirements, applicable Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level. 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 Department of the Navy 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 Navy (Financial Management and Comptroller) acknowledged to us on February 18, 2004, that the Department of the Navy Working Capital Fund financial management systems cannot provide adequate evidence supporting various material amounts on the financial statements. Therefore, we did not conduct audit work related to deficiencies identified during previous audits of the Department of the Navy.

In addition, we did not perform audit work related to the following selected provisions of laws and regulations: the Antideficiency Act, the Prompt Payment Act, and the Federal Credit Reform 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.