

**Department of Defense**  
**Department of the Navy**  
**CONSOLIDATED BALANCE SHEET**  
**As of March 31, 2005 and 2004**

	<b>2005 Consolidated</b>	<b>2004 Consolidated</b>
<b>1. ASSETS (Note 2)</b>		
A. Intragovernmental:		
1. Fund Balance with Treasury (Note 3)		
a. Entity	\$ 141,818,737,619.08	\$ 142,066,040,383.76
b. Non-Entity Seized Iraqi Cash	0.00	0.00
c. Non-Entity-Other	184,937,232.06	(675,402,496.84)
2. Investments (Note 4)	9,450,908.20	9,701,230.77
3. Accounts Receivable (Note 5)	202,899,862.47	249,400,749.15
4. Other Assets (Note 6)	749,116,746.84	220,672,343.29
5. Total Intragovernmental Assets	<u>\$ 142,965,142,368.65</u>	<u>\$ 141,870,412,210.13</u>
B. Cash and Other Monetary Assets (Note 7)	\$ 289,290,572.12	\$ 206,388,714.52
C. Accounts Receivable (Note 5)	3,000,204,870.89	2,986,837,013.14
D. Loans Receivable (Note 8)	0.00	0.00
E. Inventory and Related Property (Note 9)	54,289,581,665.19	52,425,162,007.29
F. General Property, Plant and Equipment (Note 10)	155,226,067,926.32	153,212,012,265.21
G. Investments (Note 4)	0.00	0.00
H. Other Assets (Note 6)	7,637,553,850.73	6,987,012,859.63
<b>2. TOTAL ASSETS</b>	<u><u>\$ 363,407,841,253.90</u></u>	<u><u>\$ 357,687,825,069.92</u></u>
<b>3. LIABILITIES (Note 11)</b>		
A. Intragovernmental:		
1. Accounts Payable (Note 12)	\$ 1,422,173,563.55	\$ 943,065,979.00
2. Debt (Note 13)	0.00	0.00
3. Other Liabilities (Note 15 & Note 16)	3,709,653,229.96	3,675,991,118.52
4. Total Intragovernmental Liabilities	<u>\$ 5,131,826,793.51</u>	<u>\$ 4,619,057,097.52</u>
B. Accounts Payable (Note 12)	\$ 1,824,198,461.96	\$ 724,047,880.86
C. Military Retirement Benefits and Other Employment-Related Actuarial Liabilities (Note 17)	1,575,815,538.46	1,589,970,895.43
D. Environmental Liabilities (Note 14)	17,023,297,742.25	16,193,938,302.25
E. Loan Guarantee Liability (Note 8)	0.00	0.00
F. Other Liabilities (Note 15 & Note 16)	3,807,388,756.29	3,675,134,074.46
<b>4. TOTAL LIABILITIES</b>	<u>\$ 29,362,527,292.47</u>	<u>\$ 26,802,148,250.52</u>
<b>5. NET POSITION</b>		
A. Unexpended Appropriations	\$ 139,777,358,140.31	\$ 140,338,826,936.22
B. Cumulative Results of Operations	194,267,955,821.12	190,546,849,883.18
<b>6. TOTAL NET POSITION</b>	<u>\$ 334,045,313,961.43</u>	<u>\$ 330,885,676,819.40</u>
<b>7. TOTAL LIABILITIES AND NET POSITION</b>	<u><u>\$ 363,407,841,253.90</u></u>	<u><u>\$ 357,687,825,069.92</u></u>

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CONSOLIDATED STATEMENT OF NET COST

For the periods ended March 31, 2005 and 2004

	2005 Consolidated	2004 Consolidated
<b>1. Program Costs</b>		
A. Intragovernmental Gross Costs	\$ 18,991,693,850.41	\$ 16,569,006,530.81
B. (Less: Intragovernmental Earned Revenue)	(1,052,864,242.47)	(763,974,034.09)
C. Intragovernmental Net Costs	\$ 17,938,829,607.94	\$ 15,805,032,496.72
D. Gross Costs With the Public	38,509,605,929.00	49,044,522,388.67
E. (Less: Earned Revenue From the Public)	(2,683,350,278.89)	(1,336,585,952.23)
F. Net Costs With the Public	\$ 35,826,255,650.11	\$ 47,707,936,436.44
G. Total Net Cost	\$ 53,765,085,258.05	\$ 63,512,968,933.16
<b>2. Cost Not Assigned to Programs</b>	0.00	0.00
<b>3. (Less: Earned Revenue Not Attributable to Programs)</b>	0.00	0.00
<b>4. Net Cost of Operations</b>	\$ 53,765,085,258.05	\$ 63,512,968,933.16

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**CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION**

For the periods ended March 31, 2005 and 2004

	2005 Consolidated	2004 Consolidated
<b>CUMULATIVE RESULTS OF OPERATIONS</b>		
<b>1. Beginning Balances</b>	\$ 188,170,325,142.74	\$ 222,565,238,626.33
<b>2. Prior period adjustments (+/-)</b>		
2.A. Prior Period Adjustments - Restated (+/-)	0.00	(25,913,749,160.94)
2.B. Beginning Balance, Restated	188,170,325,142.74	196,651,489,465.39
2.C. Prior Period Adjustments - Not Restated (+/-)	0.00	0.00
<b>3. Beginning Balances, as adjusted</b>	188,170,325,142.74	196,651,489,465.39
<b>4. Budgetary Financing Sources:</b>		
4.A. Appropriations received	0.00	0.00
4.B. Appropriations transferred-in/out (+/-)	0.00	0.00
4.C. Other adjustments (rescissions, etc) (+/-)	0.00	0.00
4.D. Appropriations used	59,562,496,373.24	57,121,931,191.31
4.E. Nonexchange revenue	92,243.52	0.00
4.F. Donations and forfeitures of cash and cash equivalents	16,631,952.63	0.00
4.G. Transfers-in/out without reimbursement (+/-)	0.00	0.00
4.H. Other budgetary financing sources (+/-)	0.00	0.00
<b>5. Other Financing Sources:</b>		
5.A. Donations and forfeitures of property	0.00	0.00
5.B. Transfers-in/out without reimbursement (+/-)	0.00	1,452,368.49
5.C. Imputed financing from costs absorbed by others	283,495,367.04	284,945,791.15
5.D. Other (+/-)	0.00	0.00
<b>6. Total Financing Sources</b>	59,862,715,936.43	57,408,329,350.95
<b>7. Net Cost of Operations (+/-)</b>	53,765,085,258.05	63,512,968,933.16
<b>8. Ending Balances</b>	\$ 194,267,955,821.12	\$ 190,546,849,883.18

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**CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION**

For the periods ended March 31, 2005 and 2004

	2005 Consolidated	2004 Consolidated
<b>UNEXPENDED APPROPRIATIONS</b>		
<b>1. Beginning Balances</b>	\$ 79,161,773,513.55	\$ 50,781,178,966.59
<b>2. Prior period adjustments (+/-)</b>		
2.A. Prior Period Adjustments - Restated (+/-)	0.00	25,913,749,160.94
2.B. Beginning Balance, Restated	79,161,773,513.55	76,694,928,127.53
2.C. Prior Period Adjustments - Not Restated (+/-)	0.00	0.00
<b>3. Beginning Balances, as adjusted</b>	79,161,773,513.55	76,694,928,127.53
<b>4. Budgetary Financing Sources:</b>		
4.A. Appropriations received	120,682,229,000.00	121,307,583,000.00
4.B. Appropriations transferred-in/out (+/-)	246,998,000.00	177,668,000.00
4.C. Other adjustments (rescissions, etc) (+/-)	(751,146,000.00)	(719,421,000.00)
4.D. Appropriations used	(59,562,496,373.24)	(57,121,931,191.31)
4.E. Nonexchange revenue	0.00	0.00
4.F. Donations and forfeitures of cash and cash equivalents	0.00	0.00
4.G. Transfers -in/out without reimbursement (+/-)	0.00	0.00
4.H. Other budgetary financing sources (+/-)	0.00	0.00
<b>5. Other Financing Sources:</b>		
5.A. Donations and forfeitures of property	0.00	0.00
5.B. Transfers -in/out without reimbursement (+/-)	0.00	0.00
5.C. Imputed financing from costs absorbed by others	0.00	0.00
5.D. Other (+/-)	0.00	0.00
<b>6. Total Financing Sources</b>	60,615,584,626.76	63,643,898,808.69
<b>7. Net Cost of Operations (+/-)</b>		
<b>8. Ending Balances</b>	\$ 139,777,358,140.31	\$ 140,338,826,936.22

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**COMBINED STATEMENT OF BUDGETARY RESOURCES**  
 For the periods ended March 31, 2005 and 2004

	2005 Combined	2004 Combined
<b>BUDGETARY FINANCING ACCOUNTS</b>		
<b>BUDGETARY RESOURCES</b>		
1. Budget Authority:		
1a. Appropriations received	\$ 120,699,015,912.58	\$ 121,325,054,443.59
1b. Borrowing authority	0.00	0.00
1c. Contract authority	0.00	0.00
1d. Net transfers (+/-)	(24,623,000.00)	5,195,000.00
1e. Other	159,886.00	149,060.15
2. Unobligated balance:		
2a. Beginning of period	18,027,995,386.41	14,695,236,688.97
2b. Net transfers, actual (+/-)	271,621,000.00	172,473,000.00
2c. Anticipated Transfers balances	0.00	0.00
3. Spending authority from offsetting collections:		
3a. Earned	0.00	0.00
1. Collected	4,164,610,963.95	3,546,714,109.88
2. Receivable from Federal sources	647,805,049.73	(72,053,704.67)
3b. Change in unfilled customer orders	0.00	0.00
1. Advance received	58,332,859.74	19,526,256.88
2. Without advance from Federal sources	2,472,405,258.91	2,294,923,295.27
3c. Anticipated for the rest of year, without advances	0.00	172,820,151.90
3d. Previously unavailable	0.00	0.00
3e. Transfers from trust funds	0.00	0.00
3f. Subtotal	<u>7,343,154,132.33</u>	<u>5,961,930,109.26</u>
4. Recoveries of prior year obligations	7,444,905,194.80	10,439,564,835.52
5. Temporarily not available pursuant to Public Law	0.00	0.00
6. Permanently not available	(751,146,000.00)	(719,421,000.00)
<b>7. Total Budgetary Resources</b>	<u><u>\$ 153,011,082,512.12</u></u>	<u><u>\$ 151,880,182,137.49</u></u>

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**COMBINED STATEMENT OF BUDGETARY RESOURCES**  
For the periods ended March 31, 2005 and 2004

	2005 Combined	2004 Combined
<b>STATUS OF BUDGETARY RESOURCES</b>		
8. Obligations incurred:		
8a. Direct	\$ 87,114,221,793.60	\$ 86,922,799,860.35
8b. Reimbursable	5,300,984,571.36	1,913,597,839.80
8c. Subtotal	<u>92,415,206,364.96</u>	<u>88,836,397,700.15</u>
9. Unobligated balance:		
9a. Apportioned	57,493,635,515.16	30,242,436,481.25
9b. Exempt from apportionment	0.00	0.00
9c. Other available	0.00	0.00
10. Unobligated Balances Not Available	3,102,240,632.00	32,801,347,956.09
<b>11. Total, Status of Budgetary Resources</b>	<u><u>\$ 153,011,082,512.12</u></u>	<u><u>\$ 151,880,182,137.49</u></u>
<b>RELATIONSHIP OF OBLIGATIONS TO OUTLAYS:</b>		
12. Obligated Balance, Net - beginning of period	\$ 63,856,223,651.09	\$ 63,520,894,155.09
13. Obligated Balance transferred, net (+/-)	0.00	0.00
14. Obligated Balance, Net - end of period:		
14a. Accounts receivable	(1,185,364,062.11)	(825,788,893.47)
14b. Unfilled customer order from Federal sources	(5,275,386,911.52)	(4,630,398,857.13)
14c. Undelivered orders	83,328,958,752.24	81,614,758,792.46
14d. Accounts payable	4,486,994,493.71	3,025,889,718.08
15. Outlays:		
15a. Disbursements	64,351,112,240.29	60,510,396,669.18
15b. Collections	(4,222,943,823.69)	(3,566,240,366.76)
15c. Subtotal	<u>60,128,168,416.60</u>	<u>56,944,156,302.42</u>
16. Less: Offsetting receipts	(39,125,005.33)	(27,459,870.55)
<b>17. Net Outlays</b>	<u><u>\$ 60,089,043,411.27</u></u>	<u><u>\$ 56,916,696,431.87</u></u>

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**COMBINED STATEMENT OF BUDGETARY RESOURCES**  
 For the periods ended March 31, 2005 and 2004

	2005 Combined	2004 Combined
<b>NONBUDGETARY FINANCING ACCOUNTS</b>		
<b>BUDGETARY RESOURCES</b>		
1. Budget Authority:		
1a. Appropriations received	\$ 0.00	\$ 0.00
1b. Borrowing authority	0.00	0.00
1c. Contract authority	0.00	0.00
1d. Net transfers (+/-)	0.00	0.00
1e. Other	0.00	0.00
2. Unobligated balance:		
2a. Beginning of period	0.00	0.00
2b. Net transfers, actual (+/-)	0.00	0.00
2c. Anticipated Transfers balances	0.00	0.00
3. Spending authority from offsetting collections:		
3a. Earned	0.00	0.00
1. Collected	0.00	0.00
2. Receivable from Federal sources	0.00	0.00
3b. Change in unfilled customer orders	0.00	0.00
1. Advance received	0.00	0.00
2. Without advance from Federal sources	0.00	0.00
3c. Anticipated for the rest of year, without advances	0.00	0.00
3d. Previously unavailable	0.00	0.00
3e. Transfers from trust funds	0.00	0.00
3f. Subtotal	0.00	0.00
4. Recoveries of prior year obligations	0.00	0.00
5. Temporarily not available pursuant to Public Law	0.00	0.00
6. Permanently not available	0.00	0.00
<b>7. Total Budgetary Resources</b>	<b>\$ 0.00</b>	<b>\$ 0.00</b>

**Department of Defense**  
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**COMBINED STATEMENT OF BUDGETARY RESOURCES**  
**For the periods ended March 31, 2005 and 2004**

	<b>2005 Combined</b>	<b>2004 Combined</b>
<b>STATUS OF BUDGETARY RESOURCES</b>		
8. Obligations incurred:		
8a. Direct	\$ 0.00	\$ 0.00
8b. Reimbursable	0.00	0.00
8c. Subtotal	<u>0.00</u>	<u>0.00</u>
9. Unobligated balance:		
9a. Apportioned	0.00	0.00
9b. Exempt from apportionment	0.00	0.00
9c. Other available	0.00	0.00
10. Unobligated Balances Not Available	0.00	0.00
<b>11. Total, Status of Budgetary Resources</b>	<u><u>\$ 0.00</u></u>	<u><u>\$ 0.00</u></u>
<b>RELATIONSHIP OF OBLIGATIONS TO OUTLAYS:</b>		
12. Obligated Balance, Net - beginning of period	\$ 0.00	\$ 0.00
13. Obligated Balance transferred, net (+/-)	0.00	0.00
14. Obligated Balance, Net - end of period:		
14a. Accounts receivable	0.00	0.00
14b. Unfilled customer order from Federal sources	0.00	0.00
14c. Undelivered orders	0.00	0.00
14d. Accounts payable	0.00	0.00
15. Outlays:		
15a. Disbursements	0.00	0.00
15b. Collections	0.00	0.00
15c. Subtotal	<u>0.00</u>	<u>0.00</u>
16. Less: Offsetting receipts	0.00	0.00
<b>17. Net Outlays</b>	<u><u>\$ 0.00</u></u>	<u><u>\$ 0.00</u></u>



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**COMBINED STATEMENT OF FINANCING**  
 For the periods ended March 31, 2005 and 2004

	<b>2005 Combined</b>	<b>2004 Combined</b>
<b>Resources Used to Finance Activities:</b>		
Budgetary Resources Obligated		
1. Obligations incurred	\$ 92,415,206,364.96	\$ 88,836,397,700.15
2. Less: Spending authority from offsetting collections and recoveries (-)	(14,788,059,327.13)	(16,228,674,792.88)
3. Obligations net of offsetting collections and recoveries	77,627,147,037.83	72,607,722,907.27
4. Less: Offsetting receipts (-)	(39,125,005.33)	(27,459,870.55)
5. Net obligations	77,588,022,032.50	72,580,263,036.72
Other Resources		
6. Donations and forfeitures of property	0.00	0.00
7. Transfers in/out without reimbursement (+/-)	0.00	1,452,368.49
8. Imputed financing from costs absorbed by others	283,495,367.04	284,945,791.15
9. Other (+/-)	0.00	0.00
10. Net other resources used to finance activities	283,495,367.04	286,398,159.64
<b>11. Total resources used to finance activities</b>	<b>77,871,517,399.54</b>	<b>72,866,661,196.36</b>
<b>Resources Used to Finance Items not Part of the Net Cost of Operations</b>		
12. Change in budgetary resources obligated for goods, services and benefits ordered but not yet provided		
12a. Undelivered Orders (-)	(23,849,997,957.36)	(18,038,029,658.63)
12b. Unfilled Customer Orders	2,530,738,118.65	2,314,449,552.15
13. Resources that fund expenses recognized in prior periods	(130,748,555.11)	(95,270,211.06)
14. Budgetary offsetting collections and receipts that do not affect net cost of operations	0.00	0.00
15. Resources that finance the acquisition of assets	(7,601,764,370.78)	(12,148,563,314.09)
16. Other resources or adjustments to net obligated resources that do not affect net cost of operations		
16a. Less: Trust or Special Fund Receipts Related to	0.00	0.00
16b. Other (+/-)	0.00	(1,452,368.49)
<b>17. Total resources used to finance items not part of the net cost of operations</b>	<b>(29,051,772,764.60)</b>	<b>(27,968,866,000.12)</b>
<b>18. Total resources used to finance the net cost of operations</b>	<b>48,819,744,634.94</b>	<b>44,897,795,196.24</b>

Department of Defense

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**COMBINED STATEMENT OF FINANCING**

For the periods ended March 31, 2005 and 2004

	<b>2005 Combined</b>	<b>2004 Combined</b>
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<b>Components of the Net Cost of Operations that will not Require or Generate Resources in the Current Period:</b>		
Components Requiring or Generating Resources in Future Period:		
19. Increase in annual leave liability	0.00	(23,781,806.91)
20. Increase in environmental and disposal liability	920,369,064.79	587,318,623.72
21. Upward/Downward reestimates of credit subsidy expense (+/-)	0.00	0.00
22. Increase in exchange revenue receivable from the public (-)	0.00	0.00
23. Other (+/-)	6,719,123.48	179,508,066.53
24. Total components of Net Cost of Operations that will require or generate resources in future periods	<hr/> 927,088,188.27	<hr/> 743,044,883.34
Components not Requiring or Generating Resources:		
25. Depreciation and amortization	6,179,820,865.79	14,952,553,938.00
26. Revaluation of assets or liabilities (+/-)	(1,196,386,194.37)	1,724,336,147.71
27. Other (+/-)		
27a. Trust Fund Exchange Revenue	0.00	(17,476,438.59)
27b. Cost of Goods Sold	0.00	0.00
27c. Operating Material & Supplies Used	(948,914,378.33)	93,443,099.47
27d. Other	(16,267,858.25)	1,119,272,106.99
28. Total components of Net Cost of Operations that will not require or generate resources	<hr/> 4,018,252,434.84	<hr/> 17,872,128,853.58
<b>29. Total components of net cost of operations that will not require or generate resources in the current period</b>	<hr/> 4,945,340,623.11	<hr/> 18,615,173,736.92
<b>30. Net Cost of Operations</b>	<hr/> <hr/> 53,765,085,258.05	<hr/> <hr/> 63,512,968,933.16

**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) 2005 represents the tenth 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 is to organize, train, and equip armed forces to deter aggression and, if necessary, defeat aggressors against the United States and its allies.

### **1.C. Appropriations and Funds**

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

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

Revolving funds receive their initial working capital through an appropriation or a transfer of resources from existing appropriations or funds and use those capital resources to finance the initial cost of products and services. Financial resources to replenish the initial working capital and to permit continuing operations are generated by the acceptance of customer orders. 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 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

Navy GF

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

**Budget Clearing Accounts**

17X3XXX Suspense Accounts (except those listed in Non-Entity below)

**Non-Entity Accounts:**

17X3882 Military Thrift Savings Plan  
17X3886 Civilian Thrift Savings Plan  
17X3041 Recoveries Under the Foreign Military Sales Program  
17X3210 General Fund Proprietary Receipts  
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 2005, 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 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, the 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

#### **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 DoD and other federal agencies. In September 2004, the FMS issued the "Federal Intragovernmental Transactions Accounting Policies Guide." The DON 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 Department of the 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 Department of the 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 Department of the 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. DON 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 and 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, expensed 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. Premiums 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, no provision is 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.

### **1.0. General Property, Plant and Equipment**

Effective October 1, 2002, 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). 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 must also be capitalized. DON depreciates all General PP&E, other than land, 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 asset's 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—non-environmental 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 non-environmental 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 non-environmental 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 2nd Quarter, FY 2005. Financial statement fluctuations greater than 2 percent of total assets on the Balance Sheet and/or greater than 10 percent between 2nd Quarter, FY 2005 and 2nd Quarter, 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. Undistributed Disbursements and Collections**

Undistributed disbursements and collections represent the difference between disbursements and collections matched at the transaction level to a specific obligation, payable, or receivable in the activity field records as opposed to those reported by the U.S. Treasury. These amounts should agree with the undistributed amounts reported on the departmental accounting reports.

The Department of Defense policy is to allocate supported undistributed disbursements and collections between federal and nonfederal categories based on the percentage of Federal and nonfederal accounts payable and accounts receivable. Unsupported undistributed disbursements are recorded in accounts payable. Unsupported undistributed collections are recorded in other liabilities. The DON follows this procedure.

#### **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 2005, 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 seventh 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.

<b>Note 2.</b>	<b>Nonentity Assets</b>
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As of March 31	2005	2004
<b>1. Intragovernmental Assets</b>		
A. Fund Balance with Treasury	\$ 184,937,232.06	\$ (675,402,496.84)
B. Investments	0.00	0.00
C. Accounts Receivable	0.00	0.00
D. Other Assets	0.00	0.00
E. Total Intragovernmental Assets	\$ 184,937,232.06	\$ (675,402,496.84)
<b>2. Nonfederal Assets</b>		
A. Cash and Other Monetary Assets	\$ 289,290,572.12	\$ 206,388,714.52
B. Accounts Receivable	2,666,054,314.93	2,706,518,370.00
C. Loans Receivable	0.00	0.00
D. Inventory & Related Property	0.00	0.00
E. General PP&E	0.00	0.00
F. Investments	0.00	0.00
G. Other Assets	0.00	0.00
H. Total Nonfederal Assets	\$ 2,955,344,887.05	\$ 2,912,907,084.52
<b>3. Total Nonentity Assets</b>	\$ 3,140,282,119.11	\$ 2,237,504,587.68
<b>4. Total Entity Assets</b>	\$ 360,267,559,134.79	\$ 355,450,320,482.24
<b>5. Total Assets</b>	\$ 363,407,841,253.90	\$ 357,687,825,069.92

**Fluctuation and/or Abnormalities**Intragovernmental Assets.

Fund Balance with Treasury (Line 1.A): DON reported an increase of \$860,340 thousand, 127 percent, in 2<sup>nd</sup> Quarter FY 2005. Nonentity Fund Balance with Treasury was affected by a reclassification of the majority of 3000 series Treasury Suspense accounts from Nonentity to Entity. This reclassification was done to bring DON's categorization of the Suspense accounts into alignment with DoD's treatment. The reclassification had a net effect of \$296,530 thousand. Had the reclassification not occurred, the reported balance of \$184,937 thousand would have been -\$111,593 thousand. Remaining in Nonentity are the 6000 series Deposit accounts which hold items such as withheld state and local taxes and payroll savings allotments and several of the 3000 series. See Note 1C for a complete listing of the entity and nonentity account symbols.

Non-Federal Assets

Cash and Other Monetary Assets (Line 2.A): DON reported an increase of \$82,902 thousand, 40 percent, in 2<sup>nd</sup> Quarter FY 2005. The majority of the increase in the Cash and Other Monetary Assets line is attributed to an increase of \$78,743 thousand in foreign currency held by the Marine Corps Expeditionary Forces, Camp Lejeune, due to deposits into their Limited Deposit Account for deployment and mission requirements.



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

## **Information Related to Non-Entity Assets**

### **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 2<sup>nd</sup> Quarter FY 2005, DON holds \$3,140,282 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 Non-federal Cash and Other Monetary Assets, and (3) the Non-federal Accounts Receivable.

#### Non-Entity Non-federal Accounts Receivable (Public).

As of 2<sup>nd</sup> Quarter 2005, non-entity non-federal accounts receivable contains principal of \$1,333,494 thousand in advance payments made to contractors that remains in litigation and \$1,158,245 thousand in associated accrued interest. 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 the 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.

<b>Note 3.</b>	<b>Fund Balance with Treasury</b>
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As of March 31	2005	2004
<b>1. Fund Balances</b>		
A. Appropriated Funds	\$ 139,102,982,926.18	\$ 139,416,331,899.70
B. Revolving Funds	2,993,027,834.54	2,560,063,699.92
C. Trust Funds	15,525,434.48	19,528,713.86
D. Special Funds	0.00	0.00
E. Other Fund Types	(107,861,344.06)	(605,286,426.56)
F. Total Fund Balances	<u>\$ 142,003,674,851.14</u>	<u>\$ 141,390,637,886.92</u>
<b>2. Fund Balances Per Treasury Versus Agency</b>		
A. Fund Balance per Treasury	\$ 142,052,167,827.45	\$ 141,425,681,885.56
B. Fund Balance per DON	<u>142,003,674,851.14</u>	<u>141,390,637,886.92</u>
<b>3. Reconciling Amount</b>	<u>\$ 48,492,976.31</u>	<u>\$ 35,043,998.64</u>

**Explanation of Reconciliation Amount:**

Receipt Accounts in Treasury unavailable to DON	\$50,567,193.88
Invalid program years recorded in DON	<u>(2,074,217.57)</u>
Total Reconciling Amount	<u>\$48,492,976.31</u>

**Fund Balance Per Treasury Calculation**

Undisbursed Appropriation Account Trial Balance (FMS 6654)	\$142,024,250,516.02
Receipt Account Trial Balance (FMS 6655 – IAS 613)	44,704,224.01
Less: 6655 Trust Funds Balances included in 6654	(16,717,798.58)
Less: 6655 Special Funds Balances included in 6654	<u>(69,114.00)</u>
Fund Balance Per Treasury	<u>\$142,052,167,827.45</u>

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.

## **4. Other Information**

### **Fluctuation and/or Abnormalities**

The only DON Revolving Fund (Line 1B) is the National Defense Sealift Fund, Navy. The increase of \$432,964 thousand, 17 percent, is a result of additional funding to cover the increase in approved stabilized rates for the Surge Program and the hospital ship program, and for construction of combat logistics ships.

The Trust Fund balance (Line 1C) decreased \$4,003 thousand, 20 percent, primarily due to a construction project capital outlay at the Naval Academy.

Other Fund types (Line 1E) increased by \$497,425 thousand, 82 percent. Included in this line are the Treasury Suspense and Clearing accounts. There were substantial efforts to clear negative balances, primarily in Disbursing Officers suspense account 3885 and Interfund/IPAC suspense account 3875.

### **Information Related to Fund Balance with Treasury**

#### **Other Disclosures**

##### Check Issue Discrepancies.

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 Differences.

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.

See Note 2, Non-Entity Assets for further discussions on Fund Balance with Treasury.

Navy GF

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

## Status of Fund Balance with Treasury

As of March 31	2005	2004
<b>1. Unobligated Balance</b>		
A. Available	\$ 57,493,315,743.16	\$ 60,701,417,209.05
B. Unavailable	3,102,240,632.00	2,169,248,956.09
<b>2. Obligated Balance not yet Disbursed</b>	\$ 81,345,801,807.70	\$ 79,174,091,403.54
<b>3. Total</b>	\$ 141,941,358,182.86	\$ 142,044,757,568.68

### Other Information Related to Status of Fund Balance with Treasury

#### Fluctuation and/or Abnormalities

Unobligated, Unavailable represents budget authority that is expired and not generally available for new obligations. Unobligated, Unavailable (Line 1.B) increased \$932,992 thousand, 43 percent, from 2<sup>nd</sup> Quarter FY 2004. Research and Development increased \$636,004 thousand, Operations and Maintenance increased \$503,452 thousand, while Procurement decreased \$267,146 thousand.

#### Other Disclosures

Unobligated, Available includes annual funds that are subject to the quarterly apportionment rule. They will become available for obligation in subsequent periods as they are apportioned. Below is a summary of funds subject to subsequent period apportionment:

Apportioned, Subsequent Periods:	Amounts
Military Personnel	\$17,116,284,001.00
Operations and Maintenance	12,124,797,000.00
Total	\$29,241,081,001.00

## Disclosures Related to Suspense/Budget Clearing Accounts

As of March 31	2003	2004	2005	(Decrease)/ Increase from FY 2004 - 2005
<b>Account</b>				
F3875	\$ (270,040,892.20)	\$ (356,118,675.16)	\$ (189,609,497.55)	166,509,177.61
F3880	(19,988,090.35)	(5,759,224.19)	12,648,365.39	18,407,589.58
F3882	(2,063,934.10)	(12,865,867.33)	38,076,560.25	50,942,427.58
F3885	(450,247,394.46)	(427,274,183.64)	(119,568,748.65)	307,705,434.99
F3886	383.13	3,502.38	3,521.58	19.20
<b>Total</b>	<b>\$ (742,339,927.98)</b>	<b>\$ (802,014,447.94)</b>	<b>\$ (258,449,798.98)</b>	<b>543,564,648.96</b>

### Other Disclosures

#### Other Information Related to Suspense/Budget Clearing Account.

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.

Thus far in FY 2005, \$95,601 thousand net and \$135,426 thousand absolute value were cancelled in accordance with this legislation.

### Definitions

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

**Note References**

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.

See Footnote 2 for further discussions on Other Fund Balance Types.

## Disclosures Related to Problem Disbursements and In-Transit Disbursements

As of March 31	2003	2004	2005	(Decrease)/ Increase from FY 2004 - 2005
<b>1. Total Problem Disbursements, Absolute Value</b>				
A. Unmatched Disbursements (UMDS)	\$ 548,000,000.00	\$ 882,540,000.00	\$ 3,094,012,000.00	\$ 2,211,472,000.00
B. Negative Unliquidated Obligations (NULO)	45,000,000.00	47,100,000.00	37,940,000.00	(9,160,000.00)
<b>2. Total In-transit Disbursements, Net</b>	\$ 94,433,000.00	\$ 88,898,000.00	\$ 589,129,000.00	\$ 500,231,000.00

### Definitions

#### Unmatched Disbursements.

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

#### Negative Unliquidated Obligations.

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-Transit Disbursements, Net.

In-Transit Disbursements, Net 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. In 2<sup>nd</sup> Quarter FY 2005, DFAS-Cleveland commenced reporting of In-Transits Disbursements, Net by the distinct reporting entities of DON General Fund with \$589,129 thousand, Navy Working Capital Fund with (\$64,898) thousand, and Other Defense Organizations, General Fund with \$6,828 thousand. Previously, all DFAS-Cleveland network In-transits were reported under the DON General Fund. Of the \$589,129 thousand reported for DON General Fund, \$408,227 thousand or 69% is over 30 days old.

### Other Disclosures

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.

In 2<sup>nd</sup> Quarter FY 2005, DFAS-Cleveland expanded the scope of the definition of a UMD. Formerly, transactions that had not yet reached an accounting station were defined as undistributed. Now these transactions are being defined as an UMD. This change in practice is the primary driver behind the \$2,211,472 thousand increase reported in UMDs.

<b>Note 4.</b>	<b>Investments and Related Interest</b>
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As of March 31	2005				2004	
	Par Value/Cost	Amortization Method	Unamortized (Premium/Discount)	Investments, Net	Market Value Disclosure	Investments, Net
<b>1. Intragovernmental Securities</b>						
A. Non-Marketable, Market-Based	\$ 9,392,100.00		\$ 8,364.62	\$ 9,400,464.62	\$ 9,400,464.62	\$ 9,630,082.40
B. Accrued Interest	50,443.58			50,443.58	50,443.58	71,148.37
C. Total Intragovernmental Securities	<u>\$ 9,442,543.58</u>		<u>\$ 8,364.62</u>	<u>\$ 9,450,908.20</u>	<u>\$ 9,450,908.20</u>	<u>\$ 9,701,230.77</u>
<b>2. Other Investments</b>	<u>\$ 0.00</u>		<u>0.00</u>	<u>0.00</u>	<u>N/A</u>	<u>\$ 0.00</u>

**Fluctuation and/or Abnormalities**

The DON reported a decrease of \$20 thousand, 29 percent, in interest in 2<sup>nd</sup> Quarter FY 2005. There are two reasons for the decrease; use of trust fund assets for a construction project capital outlay, coupled with the majority of the reduced principal being reinvested at lower rates of interest ranging between 1.65 percent to 1.80 percent.

**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 \$9,451 thousand (including \$50 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.

<b>Note 5.</b>	<b>Accounts Receivable</b>
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As of March 31	2005			2004
	Gross Amount Due	Allowance For Estimated Uncollectibles	Accounts Receivable, Net	Accounts Receivable, Net
<b>1. Intragovernmental Receivables</b>	\$ 202,899,862.47	N/A	\$ 202,899,862.47	\$ 249,400,749.15
<b>2. Nonfederal Receivables (From the Public)</b>	\$ 3,010,743,437.78	\$ (10,538,566.89)	\$ 3,000,204,870.89	\$ 2,986,837,013.14
<b>3. Total Accounts Receivable</b>	\$ 3,213,643,300.25	\$ (10,538,566.89)	\$ 3,203,104,733.36	\$ 3,236,237,762.29

**Fluctuation and/or Abnormalities**Intragovernmental Receivables.

The DON reported a decrease of \$46,501 thousand, 19 percent, in intragovernmental receivables in 2<sup>nd</sup> Quarter, FY 2005.

The DON General Fund (GF) acts as a seller of goods and services to other Federal agencies (they are DON GF's Level One trading partners) and other organizations within DoD (they are DON GF's Level Two trading partners). Receipt of customer orders, the resulting billing of receivables, and the collection of those receivables from other agencies, does not consistently follow a predictable pattern. This revenue cycle is subject to the business conditions and requirements of DON's trading partners. The value of accounts receivable is also subject to the processes used for billing and collection.

Decrease- The majority of the decrease was with the following trading partners:

<u>Trading Partner</u>	<u>Level</u>	<u>Amounts (in thousands)</u>
Air Force General Fund	Two	\$19,527
Navy Working Capital Fund	Two	17,298
Other Defense Organizations Working Capital Fund	Two	14,233

Nonfederal Receivables.

No variance needed to be explained.

**Information Related to Accounts Receivable****Allowance Method**

Based upon an extensive analysis of historic Treasury Report on Receivables (TROR) data, DON revised the methodology for determining the allowance for estimated uncollectible accounts receivable in 1<sup>st</sup> Quarter, FY 2005. For comparison purposes, had the prior methodology been used in 2<sup>nd</sup> Quarter FY 2005, the allowance would have been \$100,808 thousand instead of the reported \$10,539 thousand.

## **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 2<sup>nd</sup> Quarter, FY 2005 \$388,566 thousand in undistributed collections was allocated to accounts receivable.

### 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. The Intragovernmental Transaction system (IGTS) is one solution being designed to address the Trading Partner elimination issue.

Intrafund transactions are eliminated based upon trading partner information obtained from the Naval Personnel Command, the 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:

	<u>As of March 31, 2005</u>
Contract Litigation Principal and Interest	\$ 2,491,739,013.56
Defense Debt Management System (DDMS)	21,600,567.00
CDS/MOCAS system debts	(53,250,980.00)
Civilian Pay (DCPS) debt	3,326,456.00
In-service Debt & Other Debt	85,651,589.00
JAG	1,496,809.00
Penalties, Fines and Admin. Fees and Interest	123,629,875.60
Gross Non-entity Non-Federal A/R	<u>2,674,193,330.16</u>
Less Allowance	<u>(8,139,015.23)</u>
Non-entity Non-Federal Receivables, Net	2,666,054,314.93
Entity Non-Federal Receivables, Net	334,150,555.96
Non-Federal Receivables (From the Public), Net	<u><u>\$ 3,000,204,870.89</u></u>

The contract litigation includes principal of \$1,333,494 thousand, and accrued interest receivable of \$1,158,245 thousand. Interest receivable increased \$58,322 thousand from FY 2004.

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

Definitions of debt system acronyms:

CDS is the Contractor Debt System that manages debts owed by contractors.

MOCAS is the Mechanization of Contract Administration System that manages debts owed by contractors.

JAG is the Judge Advocate General's Office. JAG is responsible for certain military personnel related debts.

DCPS is the Defense Civilian Payroll System. DCPS has certain civilian payroll related debts.

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.

See Note Disclosure 1.Y - Undistributed Disbursements and Collections for the definition of Undistributed Collection.

<b>Note 6.</b>	<b>Other Assets</b>
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As of March 31	2005	2004
<b>1. Intragovernmental Other Assets</b>		
A. Advances and Prepayments	\$ 749,116,746.84	\$ 220,672,343.29
B. Total Intragovernmental Other Assets	\$ 749,116,746.84	\$ 220,672,343.29
<b>2. Nonfederal Other Assets</b>		
A. Outstanding Contract Financing Payments	\$ 7,271,016,884.02	\$ 6,677,496,923.79
B. Other Assets (With the Public)	366,536,966.71	309,515,935.84
C. Total Nonfederal Other Assets	\$ 7,637,553,850.73	\$ 6,987,012,859.63
<b>3. Total Other Assets</b>	\$ 8,386,670,597.57	\$ 7,207,685,202.92

**Fluctuation and/or Abnormalities**Intragovernmental Other Assets.

The DON reported a increase of \$528,444 thousand, 240 percent, in Advances and Prepayments, (Line 1.A), in 2<sup>nd</sup> Quarter, FY 2005. The balances reported are determined by the intragovernmental elimination process as submitted by DON's trading partners. In processing the elimination data, increases to Advances and Prepayments are recorded to compensate for the unresolved differences when needed. Furthermore, using historical data as a baseline, DON recorded an overall Level One estimate for advances in the amount of \$301,318 thousand.

Increase - The majority of the increase was with the following trading partners:

<u>Trading Partner</u>	<u>Level</u>	<u>Amounts (in thousands)</u>
Department of Interior	One	\$185,506
Navy Working Capital Fund	Two	155,780
Department of Transportation	One	98,720
Air Force General Fund	Two	67,901

Non-Federal Other Assets.

DON reported an increase of \$57,021 thousand, 18 percent, in Other Assets (With the Public) (Line 2.B.) in 2<sup>nd</sup> Quarter, FY 2005. The following are the programs that contributed to the increases:

<u>Category</u>	<u>Amounts (in thousands)</u>
Travel/PCS Advances	\$27,005
Marine Corps Procurement	29,192

Travel and Permanent Change of Station (PCS) advances are returning to more normal, pre-Operation Iraqi Freedom levels, and the increase in Marine Corps Procurement advances to contractors represents execution of supplemental funding.

## Information Related to Other Assets

### Other Disclosures

#### Intragovernmental Other Assets - 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 (Level Two trading partners). Additionally, the buyer-side prepayment balances were adjusted to agree with seller-side deferred credits on the books of other DoD reporting entities. Advances and prepayments to Other Federal Agencies (Level One trading partners) were estimated since the DON accounting systems cannot identify buyer side. The estimates were based upon historical trading partner data obtained from the Intragovernmental Review and Analysis System (IRAS).

#### Non-Federal Other Assets - 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.

The following table displays the Outstanding Contract Financing Payments attributed by program. Of note for the 2<sup>nd</sup> Quarter, FY 2005 is an increase of \$270,033 thousand, 42 percent, in the Weapons Procurement account related to the requirement to replenish stocks of weapons and ammunitions.

	As of March 31, 2005
Aircraft Procurement	\$4,995,015,676.69
Shipbuilding and Conversion	594,702,543.68
Weapons Procurement	910,653,699.30
Other Procurement	691,631,276.30
Other (O&M, RDT&E)	79,013,688.05
Total	<u>\$7,271,016,884.02</u>

### 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.

<b>Note 7.</b>	<b>Cash and Other Monetary Assets</b>
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As of March 31	2005	2004
1. Cash	\$ 209,790,581.21	\$ 205,631,941.74
2. Foreign Currency (non-purchased)	79,499,990.91	756,772.78
3. Total Cash, Foreign Currency, & Other Monetary Assets	\$ 289,290,572.12	\$ 206,388,714.52

**Fluctuation and/or Abnormalities**

Foreign Currency (Line 2): The DON reported an increase of \$78,743 thousand, 10,405 percent, in 2<sup>nd</sup> Quarter, FY 2005. The majority of the increase is the result of the Marine Corps Expeditionary Forces, Camp Lejeune, depositing money into their Limited Deposit Account for deployment and mission requirements.

**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**



Navy GF

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.

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

As of March 31

**Direct Loan and/or Loan Guarantee Programs** The entity operates the following direct loan and/or Loan guarantee program(s)  
Military Housing Privatization Initiative

### **Other Information Related to Direct Loan and/or Loan Guarantee Programs.**

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.

Navy GF

**Reference**

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

## Direct Loans Obligated After FY 1991

As of March 31

	2005	2004
Loan Programs		
<b>Military Housing Privatization Initiative</b>		
A. Loans Receivable Gross	\$ 0.00	\$ 0.00
B. Interest Receivable	0.00	0.00
C. Foreclosed Property	0.00	0.00
D. Allowance for Subsidy Cost (Present Value)	0.00	0.00
E. Value of Assets Related to Direct Loans	\$ 0.00	\$ 0.00
<b>Total Loans Receivable</b>	<b>\$ 0.00</b>	<b>\$ 0.00</b>

**Total Amount of Direct Loans Disbursed**

As of March 31

2005

2004

**Direct Loan Programs**

Military Housing Privatization Initiative

\$	0.00	\$	0.00
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**Total**

\$	0.00	\$	0.00
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## Subsidy Expense for Post-1991 Direct Loans

As of March 31

2005	Interest Differential	Defaults	Fees	Other	Total
<b>1. New Direct Loans Disbursed:</b> Military Housing Privatization Initiative	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
2004	Interest Differential	Defaults	Fees	Other	Total
<b>2. New Direct Loans Disbursed:</b> Military Housing Privatization Initiative	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
2005	Modifications	Interest Rate Reestimates	Technical Reestimates	Total Reestimates	Total
<b>3. Direct Loan Modifications and Reestimates:</b> Military Housing Privatization Initiative	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
2004	Modifications	Interest Rate Reestimates	Technical Reestimates	Total Reestimates	Total
<b>4. Direct Loan Modifications and Reestimates:</b> Military Housing Privatization Initiative	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
<hr/>					
		2005	2004		
<b>5. Total Direct Loan Subsidy Expense:</b> Military Housing Privatization Initiative	\$ 0.00	\$ 0.00	\$ 0.00		

## Subsidy Rate for Direct Loans

As of March 31	Interest Differential	Defaults	Fees	Other	Total
Military Housing Privatization Initiative	0.00%	0.00%	0.00%	0.00%	0.00%

## Schedule for Reconciling Subsidy Cost Allowance Balances for Post-1991 Direct Loans

As of March 31

	2005	2004
<b>1. Beginning Balance of the Subsidy Cost Allowance</b>	\$ 0.00	\$ 0.00
<b>2. Add: Subsidy Expense for Direct Loans Disbursed during the Reporting Years by Component</b>		
A. Interest Rate Differential Costs	\$ 0.00	\$ 0.00
B. Default Costs (Net of Recoveries)	0.00	0.00
C. Fees and Other Collections	0.00	0.00
D. Other Subsidy Costs	0.00	0.00
<b>E. Total of the above Subsidy Expense Components</b>	<b>\$ 0.00</b>	<b>\$ 0.00</b>
<b>3. Adjustments</b>		
A. Loan Modifications	\$ 0.00	\$ 0.00
B. Fees Received	0.00	0.00
C. Foreclosed Property Acquired	0.00	0.00
D. Loans Written Off	0.00	0.00
E. Subsidy Allowance Amortization	0.00	0.00
F. Other	0.00	0.00
<b>G. Total of the above Adjustment Components</b>	<b>\$ 0.00</b>	<b>\$ 0.00</b>
<b>4. Ending Balance of the Subsidy Cost Allowance before Re-estimates</b>	<b>\$ 0.00</b>	<b>\$ 0.00</b>
<b>5. Add or Subtract Subsidy Re-estimates by Component</b>		
A. Interest Rate Re-estimate	\$ 0.00	\$ 0.00
B. Technical/default Re-estimate	0.00	0.00
<b>C. Total of the above Re-estimate Components</b>	<b>\$ 0.00</b>	<b>\$ 0.00</b>
<b>6. Ending Balance of the Subsidy Cost Allowance</b>	<b>\$ 0.00</b>	<b>\$ 0.00</b>



## Defaulted Guaranteed Loans from Post-1991 Guarantees

As of March 31

	2005	2004
<b>Loan Guarantee Program(s)</b>		
<b>1. Military Housing Privatization Initiative</b>		
A. Defaulted Guaranteed Loans Receivable, Gross	\$ 0.00	\$ 0.00
B. Interest Receivable	0.00	0.00
C. Foreclosed Property	0.00	0.00
D. Allowance for Subsidy Cost (Present Value)	0.00	0.00
E. Value of Assets Related to Defaulted Guaranteed Loans Receivable	\$ 0.00	\$ 0.00
<b>2. Armament Retooling &amp; Manufacturing Support Initiative</b>		
A. Defaulted Guaranteed Loans Receivable, Gross	\$ 0.00	\$ 0.00
B. Interest Receivable	0.00	0.00
C. Foreclosed Property	0.00	0.00
D. Allowance for Subsidy Cost (Present Value)	0.00	0.00
E. Value of Assets Related to Defaulted Guaranteed Loans Receivable	\$ 0.00	\$ 0.00
<b>3. Total Value of Assets Related to Defaulted Guaranteed Loans Receivable</b>	\$ 0.00	\$ 0.00

<b>Guaranteed Loans Outstanding</b>		
As of March 31	Outstanding Principal, Guaranteed Loans, Face Value	Amount of Outstanding Principal Guaranteed
<b>Guaranteed Loans Outstanding</b>		
1. Military Housing Privatization Initiative	\$ 0.00	\$ 0.00
2. Armament Retooling & Manufacturing Support Initiative	\$ 0.00	\$ 0.00
<b>3. Total</b>	<b>\$ 0.00</b>	<b>\$ 0.00</b>
<b>2005</b>		
<b>New Guaranteed Loans Disbursed</b>		
1. Military Housing Privatization Initiative	\$ 0.00	\$ 0.00
2. Armament Retooling & Manufacturing Support Initiative	\$ 0.00	\$ 0.00
<b>3. Total</b>	<b>\$ 0.00</b>	<b>\$ 0.00</b>
<b>2004</b>		
<b>New Guaranteed Loans Disbursed</b>		
1. Military Housing Privatization Initiative	\$ 0.00	\$ 0.00
2. Armament Retooling & Manufacturing Support Initiative	\$ 0.00	\$ 0.00
<b>3. Total</b>	<b>\$ 0.00</b>	<b>\$ 0.00</b>

**Liability for Post-1991 Loan Guarantees, Present Value**

As of March 31

	2005	2004
<b>Loan Guarantee Program</b>		
1. Military Housing Privatization Initiative	\$ 0.00	\$ 0.00
2. Armament Retooling & Manufacturing Support Initiative	0.00	0.00
<b>3. Total</b>	<b>\$ 0.00</b>	<b>\$ 0.00</b>

## Subsidy Expense for Post-1991 Loan Guarantees

As of March 31

2005	Interest Differential	Defaults	Fees	Other	Total
<b>1. New Loan Guarantees</b>					
<b>Disbursed:</b>					
Military Housing Privatization Initiative	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
Armament Retooling & Manufacturing Support Initiative	0.00	0.00	0.00	0.00	0.00
Total	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
2004	Interest Differential	Defaults	Fees	Other	Total
<b>2. New Loan Guarantees</b>					
<b>Disbursed:</b>					
Military Housing Privatization Initiative	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
Armament Retooling & Manufacturing Support Initiative	0.00	0.00	0.00	0.00	0.00
Total	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
2005	Modifications	Interest Rate Reestimates	Technical Reestimates	Total Reestimates	Total
<b>3. Modifications and Reestimates:</b>					
Military Housing Privatization Initiative	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
Armament Retooling & Manufacturing Support Initiative	0.00	0.00	0.00	0.00	0.00
Total	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
2004	Modifications	Interest Rate Reestimates	Technical Reestimates	Total Reestimates	Total
<b>4. Modifications and Reestimates:</b>					
Military Housing Privatization Initiative	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
Armament Retooling & Manufacturing Support Initiative	0.00	0.00	0.00	0.00	0.00
Total	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
2005	2004				
<b>5. Total Loan Guarantee:</b>					
Military Housing Privatization Initiative	\$ 0.00	\$ 0.00			
Armament Retooling & Manufacturing Support Initiative	0.00	0.00			
Total	\$ 0.00	\$ 0.00			

## Subsidy Rate for Loan Guarantees

	Interest Supplements	Defaults	Fees and other Collections	Other	Total
<b>Loan Guarantees:</b>					
1. Military Housing Privatization Initiative	0.00%	0.00%	0.00%	0.00%	0.00%
2. Armament Retooling & Manufacturing Support Initiative	0.00%	0.00%	0.00%	0.00%	0.00%

## Schedule for Reconciling Loan Guarantee Liability Balances for Post-1991 Loan Guarantees

As of March 31

	2005	2004
<b>1. Beginning Balance of the Loan Guarantee Liability</b>	\$ 0.00	\$ 0.00
<b>2. Add: Subsidy Expense for Guaranteed Loans Disbursed during the Reporting Years by Component</b>		
A. Interest Supplement Costs	\$ 0.00	\$ 0.00
B. Default Costs (Net of Recoveries)	0.00	0.00
C. Fees and Other Collections	0.00	0.00
D. Other Subsidy Costs	0.00	0.00
<b>E. Total of the above Subsidy Expense Components</b>	\$ 0.00	\$ 0.00
<b>3. Adjustments</b>		
A. Loan Guarantee Modifications	\$ 0.00	\$ 0.00
B. Fees Received	0.00	0.00
C. Interest Supplements Paid	0.00	0.00
D. Foreclosed Property and Loans Acquired	0.00	0.00
E. Claim Payments to Lenders	0.00	0.00
F. Interest Accumulation on the Liability Balance	0.00	0.00
G. Other	0.00	0.00
<b>H. Total of the above Adjustments</b>	\$ 0.00	\$ 0.00
<b>4. Ending Balance of the Loan Guarantee Liability before Re-estimates</b>	\$ 0.00	\$ 0.00
<b>5. Add or Subtract Subsidy Re-estimates by Component</b>		
A. Interest Rate Re-estimate	0.00	0.00
B. Technical/default Re-estimate	0.00	0.00
<b>C. Total of the above Re-estimate Components</b>	\$ 0.00	\$ 0.00
<b>6. Ending Balance of the Loan Guarantee Liability</b>	\$ 0.00	\$ 0.00

**Administrative Expense**

As of March 31

	2005	2004
<b>1. Direct Loans</b>		
Military Housing Privatization Initiative	\$ 0.00	\$ 0.00
Total	\$ 0.00	\$ 0.00
<b>2. Loan Guarantees</b>		
Military Housing Privatization Initiative	\$ 0.00	\$ 0.00
Armament Retooling & Manufacturing Support Initiative	0.00	0.00
Total	\$ 0.00	\$ 0.00

<b>Note 9.</b>	<b>Inventory and Related Property</b>
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As of March 31	2005	2004
<b>1. Inventory, Net</b>	\$ 0.00	\$ 0.00
<b>2. Operating Materials &amp; Supplies, Net</b>	54,289,581,665.19	52,425,162,007.29
<b>3. Stockpile Materials, Net</b>	0.00	0.00
<b>4. Total</b>	<u>\$ 54,289,581,665.19</u>	<u>\$ 52,425,162,007.29</u>



## Inventory, Net

As of March 31

	2005			2004		Valuation Method
	Inventory, Gross Value	Revaluation Allowance	Inventory, Net	Inventory, Net		
<b>1. Inventory Categories</b>						
A. Available and Purchased for Resale	\$ 0.00	\$ 0.00	0.00	\$ 0.00	0.00	
B. Held for Repair	0.00	0.00	0.00	0.00	0.00	
C. Excess, Obsolete, and Unserviceable	0.00	0.00	0.00	0.00	0.00	
D. Raw Materials	0.00	0.00	0.00	0.00	0.00	
E. Work in Process	0.00	0.00	0.00	0.00	0.00	
F. Total	\$ 0.00	\$ 0.00	0.00	\$ 0.00	0.00	

### 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

**Operating Materials and Supplies, Net**

As of March 31

	2005			2004	Valuation Method
	OM&S Gross Value	Revaluation Allowance	OM&S, Net	OM&S, Net	
<b>1. OM&amp;S Categories</b>					
A. Held for Use	\$ 50,019,038,710.77	\$ 0.00	\$ 50,019,038,710.77	\$ 49,392,540,112.95	LAC,SP, AC, O
B. Held for Repair	6,400,817,818.59	(2,130,274,864.17)	4,270,542,954.42	3,032,621,894.34	LAC,SP, AC, O
C. Excess, Obsolete, and Unserviceable	1,241,673,351.44	(1,241,673,351.44)	0.00	0.00	LAC,SP, AC, O
D. Total	\$ 57,661,529,880.80	\$ (3,371,948,215.61)	\$ 54,289,581,665.19	\$ 52,425,162,007.29	

**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

**Fluctuation and/or Abnormalities**

OM&S, Held for Repair (Line 1.B): The DON reported an increase of \$1,237,921 thousand, 41 percent, in 2<sup>nd</sup> Quarter, FY. The following shows the composition of this amount:

- \$1,129,613 thousand was due to price adjustments, condition code adjustments, gains and losses in physical inventory and
- \$893,449 thousand was due to transfers in.
- The total increase was offset by a \$317,284 thousand increase in transfers out and a \$315,066 thousand decrease in revaluation allowance.

**Information Related to Operating Material 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:

	As of March 31, 2005
Ammunition and Munitions	\$32,943,867,982.04
Appropriation Purchase Account (APA) Principal End Item	8,683,196,561.89
Sponsor Owned Material	9,576,050,813.37
APA Secondary Inventory	1,143,299,526.77
Real-time Reutilization Asset Management (RRAM)	1,524,078,194.30
Other	419,088,586.82
Total	<u>\$54,289,581,665.19</u>

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.

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, the condition code crosswalk was amended to include code “V” in the Excess, Obsolete, Unserviceable category in September 2002. 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.

On July 6, 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 “programmatically 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 \$419,088 thousand as of March 31, 2005. This consists primarily of \$365,436 thousand in Fleet Hospitals and War Reserves and \$41,513 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.

## Stockpile Materials, Net

As of March 31

	2005			2004		Valuation Method
	Stockpile Materials Amount	Allowance for Gains (Losses)	Stockpile Materials, Net	Stockpile Materials, Net		
<b>1. Stockpile Materials Categories</b>						
A. Held for Sale	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00	0.00	
B. Held in Reserve for Future Sale	0.00	0.00	0.00	0.00	0.00	
C. Total	<u>\$ 0.00</u>	<u>\$ 0.00</u>	<u>\$ 0.00</u>	<u>\$ 0.00</u>	<u>0.00</u>	

### Legend for Valuation Methods:

LAC= Latest Acquisition Cost  
 SP= Standard Price  
 AC= Actual Cost

NRV = Net Realizable Value  
 O = Other

**Note 10. General PP&E, Net**

As of March 31	2005					2004
	Depreciation/ Amortization Method	Service Life	Acquisition Value	(Accumulated Depreciation/ Amortization)	Net Book Value	Prior FY Net Book Value
<b>1. Major Asset Classes</b>						
A. Land	N/A	N/A	\$ 621,050,020.00	N/A	\$ 621,050,020.00	\$ 540,885,887.00
B. Buildings, Structures, and Facilities	S/L	20 Or 40	33,986,113,207.00	\$ (20,112,631,686.95)	13,873,481,520.05	12,976,063,644.64
C. Leasehold Improvements	S/L	lease term	231,200.00	(20,760.00)	210,440.00	210,440.00
D. Software	S/L	2-5 Or 10	3,070,660.44	(2,728,144.63)	342,515.81	776,964.83
E. General Equipment	S/L	5 or 10	2,641,198,114.87	(2,142,466,196.40)	498,731,918.47	546,623,708.60
F. Military Equipment	S/L	Various	435,690,000,000.00	(299,090,000,000.00)	136,600,000,000.00	135,340,000,000.00
G. Assets Under Capital Lease	S/L	lease term	106,944.00	(101,596.80)	5,347.20	135,406.00
H. Construction-in-Progress	N/A	N/A	3,632,246,164.79	N/A	3,632,246,164.79	3,807,316,214.14
I. Other			0.00	0.00	0.00	0.00
<b>2. Total General PP&amp;E</b>			<b>\$ 476,574,016,311.10</b>	<b>\$ (321,347,948,384.78)</b>	<b>\$ 155,226,067,926.32</b>	<b>\$ 153,212,012,265.21</b>

<sup>1</sup> Note 15 for additional information on Capital Leases

**Legend for Valuation Methods:**

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

**Fluctuation and/or Abnormalities**Land.

The DON reported an increase of \$80,164 thousand, 15 percent, in Land in 2<sup>nd</sup> Quarter, FY 2005. Two factors that contributed to the increase are as follows:

- The ongoing effort to validate the Internet Naval Facility Asset Database Store (iNFADS).
- Capturing land rights and condemned land that was not previously being captured.

Software.

The DON reported a decrease of \$434 thousand, 56 percent, in Software in 2<sup>nd</sup> Quarter, FY 2005. It is caused by the increase of accumulated depreciation of \$1,068 thousand. When one major command was converted to Defense Property Accountability System (DPAS) during FY 2004, the associated accumulated depreciation was not recorded during the conversion. The decrease in net asset value caused by the accumulated depreciation is offset by the increase in gross asset value of \$634 thousand due to the migration of DON activities to the DPAS in FY 2004. Among the assets migrated are capitalized software and therefore the increase.

Assets Under Capital Lease.

The DON reported a decrease of \$130 thousand, 96 percent, in Equipment Leases, net in 2<sup>nd</sup> Quarter, FY 2005. This reflects the ongoing effort to validate Equipment Leases in the DPAS database and the expiration of leases.

**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.

The Department has determined that it is not practicable at this time to accumulate from internal records the information necessary to value military equipment in accordance with generally accepted accounting principles, because the Department is currently 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. 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. 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.

For the DON, the BEA analysis provided for an Acquisition value of \$435,690,000 thousand for military equipment, less an Accumulated Depreciation value of \$299,090,000 thousand giving a Net Book Value of \$136,600,000 thousand for military equipment as of 2<sup>nd</sup> Quarter, FY 2005.

#### 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) provides real property values for financial statement reporting purposes.

##### Leasehold Improvements.

The DON's real property system (iNFADS) 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 2<sup>nd</sup> Quarter FY 2004.

##### Software.

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

##### Construction-in-Progress (CIP).

Navy GF

CIP balances were obtained from the Facilities Information System (FIS). Construction performed for the benefit of non-DON customers, such as Air Force, is not included in DON CIP balances.

#### 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.

#### **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.



## Assets Under Capital Lease

As of March 31	2005	2004
<b>1. Entity as Lessee, Assets Under Capital Lease</b>		
A. Land and Buildings	\$ 0.00	\$ 0.00
B. Equipment	106,944.00	205,680.00
C. Other	0.00	0.00
D. Accumulated Amortization	(101,596.80)	(70,274.00)
E. Total Capital Leases	\$ 5,347.20	\$ 135,406.00

### 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 a decrease of \$130 thousand, 96 percent, in Equipment Leases, net in 2<sup>nd</sup> Quarter, FY 2005. This reflects the ongoing effort to validate Equipment Leases in the DPAS database and the expiration of leases.

#### Reference

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

<b>Note 11.</b>	<b>Liabilities Not Covered by Budgetary Resources</b>
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As of March 31	2005	2004
<b>1. Intragovernmental Liabilities</b>		
A. Accounts Payable	\$ 0.00	\$ 0.00
B. Debt	0.00	0.00
C. Other	3,193,750,335.65	3,281,158,113.56
<b>D. Total Intragovernmental Liabilities</b>	<b>\$ 3,193,750,335.65</b>	<b>\$ 3,281,158,113.56</b>
<b>2. Nonfederal Liabilities</b>		
A. Accounts Payable	\$ 89,472,623.49	\$ 0.00
B. Military Retirement Benefits and Other Employment-Related Actuarial Liabilities	1,575,815,538.46	1,589,970,895.43
C. Environmental Liabilities	17,023,297,742.25	16,193,938,302.25
D. Loan Guarantee Liability	0.00	0.00
E. Other Liabilities	3,439,630,694.51	3,454,912,795.40
<b>F. Total Nonfederal Liabilities</b>	<b>\$ 22,128,216,598.71</b>	<b>\$ 21,238,821,993.08</b>
<b>3. Total Liabilities Not Covered by Budgetary Resources</b>	<b>\$ 25,321,966,934.36</b>	<b>\$ 24,519,980,106.64</b>
<b>4. Total Liabilities Covered by Budgetary Resources</b>	<b>\$ 4,040,560,358.11</b>	<b>\$ 2,282,168,143.88</b>
<b>5. Total Liabilities</b>	<b>\$ 29,362,527,292.47</b>	<b>\$ 26,802,148,250.52</b>
<b>6. Other Information Related to Liabilities Not Covered by Budgetary Resources</b>		

**Fluctuation and/or Abnormalities**Intragovernmental Liabilities.

No fluctuation and/or abnormalities need to be explained.

Non-Federal Liabilities.

Accounts Payable (Line 2.A) Cancelled 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. This resulted in 100% increase in Non-federal Accounts Payable in 2<sup>nd</sup> Quarter, FY 2005.

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, which 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.C.) includes the following:

	As of March 31, 2005
Federal Employees Compensation Act (FECA)	\$ 446,009,064.60
Unemployment	81,598,321.74
Liabilities to Treasury	2,666,142,949.31
Total	\$ 3,193,750,335.65

Liabilities to Treasury.

Unliquidated progress payments and associated accrued interest receivables for contractor debt in litigation 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.

Non-Federal Liabilities – Other (Not covered by Budgetary Resources) (Line 2.E.) includes the following:

	As of March 31, 2005
Annual Leave	\$ 2,471,051,808.48
Capital Lease Liabilities	5,347.20
Military Equipment – Non-nuclear Non- Environmental Disposal Liabilities	590,418,056.81
Disposal Liabilities for Excess/Obsolete Structures	289,478,000.00
Contract Incentives	88,677,482.02
Total	<u>\$3,439,630,694.51</u>

**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

<b>Note 12.</b>	<b>Accounts Payable</b>
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As of March 31	2005			2004
	Accounts Payable	Interest, Penalties, and Administrative Fees	Total	Total
<b>1. Intragovernmental Payables</b>	\$ 1,422,173,563.55	\$ N/A	\$ 1,422,173,563.55	\$ 943,065,979.00
<b>2. Non-Federal Payables (to the Public)</b>	1,824,198,461.96	0.00	1,824,198,461.96	724,047,880.86
<b>3. Total</b>	<u>\$ 3,246,372,025.51</u>	<u>\$ 0.00</u>	<u>\$ 3,246,372,025.51</u>	<u>\$ 1,667,113,859.86</u>

**4. Other Information Related to Accounts Payable****Fluctuation and/or Abnormalities**Intragovernmental Payables.

The DON reported an increase of \$479,108 thousand, 51 percent, in intragovernmental payables in 2<sup>nd</sup> Quarter, FY 2005. These balances are largely driven by the trading partner process. Using historical data as a baseline, DON recorded an overall Level One estimate for payables in the amount of \$421,141 thousand.

Increase- the majority of the increase was with the following trading partners:

<u>Intragovernmental Entities</u>	<u>Level</u>	<u>Amounts (in thousands)</u>
General Service Administration	One	\$201,210
Department of Energy	One	129,541
Navy Working Capital Fund	Two	170,319

Decrease- the increases above were offset by a decrease with the following trading partner:

<u>Intragovernmental Entities</u>	<u>Level</u>	<u>Amount (in thousands)</u>
Other Defense Organizations	Two	\$214,038
Working Capital Funds		

To implement new Treasury guidance, Judgment Fund Liabilities were recorded in USSGL 2110 starting 1<sup>st</sup> Quarter, FY 2005, and USSGL 2110 account is mapped to Note 12 rather than Note 15. This change in policy added \$46,438 thousand to reported balances in Intragovernmental Payables.

Non-Federal Payables.

DON reported an increase of \$1,100,151 thousand, 152 percent, in Non-Federal Accounts Payable in 2<sup>nd</sup> Quarter, FY 2005.

A decrease in the debit value of the Non-entity Suspense Account disbursement balances contributed \$521,764 thousand to the increase in Non-Federal Accounts Payable.

In 3<sup>rd</sup> Quarter FY 2004, the Marine Corps instituted business process changes in the Military Pay account using a new interface file to record payables for military pay transactions. The interface then matches pay records with corresponding accounts payable records. With this process change, public accounts payable are recognized promptly and subsequently liquidated when payroll is issued. This process change added \$347,486 thousand to 2<sup>nd</sup> Quarter FY 2005 accounts payable. Also for the Marine Corps, execution of the FY 2004/2005 supplemental funding added \$337,400 thousand to reported Non-Federal Accounts Payable.

In addition, liabilities for Cancelled Accounts are now recorded as Accounts Payable rather than Other Liabilities. This change in policy added \$89,473 thousand to reported balances.

The following table summarizes the causes of the increases in Non-Federal Payables:

<u>Causes of the increases in Payables</u>	<u>Amounts (in thousands)</u>
Decrease in Non-entity Suspense Account	\$521,764
Marine Corps Military Pay – process change	347,486
Marine Corps supplemental execution	337,400
Cancelled Accounts – process change	89,473

These increases were offset by other normal fluctuations.

### **Definitions**

#### Intragovernmental Accounts Payable.

It 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).

They are payments to non-federal government entities and individuals.

### **Informations Related to Accounts Payable**

#### 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 2<sup>nd</sup> Quarter, FY 2005, total undistributed disbursements were \$2,433,080 thousand.

### 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 DoDFMR 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.

#### Judgment Fund Liabilities.

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 over the past several years. Since FY 2004, the DON has reduced the Judgment Fund from \$47,000 thousand to \$46,308 thousand. In addition, the Notification of Federal Antidiscrimination and Retaliatory Act (No FEAR) was implemented on Oct 1, 2003. This law requires all agencies to reimburse the Judgment Fund for cases covered by the No FEAR Act. For FY 2005, the DON reported \$130 thousand for No FEAR Act liabilities.

### **Reference**

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

<b>Note 13.</b>	<b>Debt</b>
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As of March 31	2005			2004	
	Beginning Balance	Net Borrowings	Ending Balance	Ending Balance	
<b>1. Agency Debt</b>					
A. Debt to the Treasury	\$ 0.00	\$ 0.00	\$ 0.00	\$	0.00
B. Debt to the Federal Financing Bank	0.00	0.00	0.00		0.00
C. Total Agency Debt	\$ 0.00	\$ 0.00	\$ 0.00	\$	0.00
<b>2. Total Debt</b>	\$ 0.00	\$ 0.00	\$ 0.00	\$	0.00

### 3. Other Information Related to Debt

#### Reference

See Note Disclosure 1.G. – Significant Accounting Policies for additional discussion on financial reporting requirements and DoD policies governing Accounting for Intragovernmental Activities, Public Debt.

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



<b>Note 14.</b>	<b>Environmental Liabilities and Disposal Liabilities</b>
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As of March 31	2005			2004
	Current Liability	Noncurrent Liability	Total	Total
<b>1. Environmental Liabilities – Non Federal</b>				
A. Accrued Environmental Restoration (DERP funded) Costs:				
1. Active Installations-- Environmental Restoration (ER)	\$ 393,221,000.00	\$ 2,321,830,000.00	\$ 2,715,051,000.00	\$ 3,181,330,000.00
2. Active Installations--ER for Closed Ranges	19,980,000.00	515,424,000.00	535,404,000.00	467,426,000.00
3. Formerly Used Defense Sites (FUDS) -- ER	0.00	0.00	0.00	0.00
4. FUDS--ER for Transferred Ranges	0.00	0.00	0.00	0.00
B. Other Accrued Environmental Costs (Non-DERP funds)				
1. Active Installations-- Environmental Corrective Action	0.00	0.00	0.00	0.00
2. Active Installations-- Environmental Closure Requirements	0.00	0.00	0.00	0.00
3. Active Installations-- Environ.Response at Active Ranges	0.00	0.00	0.00	0.00
4. Other	0.00	0.00	0.00	0.00
C. Base Realignment and Closure (BRAC)				
1. BRAC Installations-- Environmental Restoration (ER)	272,881,000.00	764,264,000.00	1,037,145,000.00	1,092,835,000.00
2. BRAC Installations--ER for Transferring Ranges	3,671,000.00	56,721,000.00	60,392,000.00	57,850,000.00
3. BRAC Installations-- Environmental Corrective Action	0.00	0.00	0.00	0.00
4. Other	0.00	0.00	0.00	0.00
D. Environmental Disposal for Weapons Systems Programs				
1. Nuclear Powered Aircraft Carriers	0.00	6,426,100,000.00	6,426,100,000.00	5,693,000,000.00
2. Nuclear Powered Submarines	0.00	5,765,600,000.00	5,765,600,000.00	5,172,400,000.00
3. Other Nuclear Powered Ships	0.00	223,900,000.00	223,900,000.00	287,500,000.00
4. Other National Defense Weapons Systems	3,641,500.00	256,064,242.25	259,705,742.25	241,597,302.25
5. Chemical Weapons Disposal Program	0.00	0.00	0.00	0.00
6. Other	0.00	0.00	0.00	0.00
<b>2. Total Environmental Liabilities:</b>	<b>\$ 693,394,500.00</b>	<b>\$ 16,329,903,242.25</b>	<b>\$ 17,023,297,742.25</b>	<b>\$ 16,193,938,302.25</b>

**3. Other Information Related to Environmental Liabilities****Fluctuation and/or Abnormalities**Accrued Environmental Restoration (DERP funded) Costs.

Active Installations Environmental Restoration (ER) (Line 1.A.1): The DON reported a net decrease of \$466,279 thousand, 15 percent, in 2<sup>nd</sup> Quarter, FY 2005. The majority of the decrease is attributed to the following factors:

- DERP program execution of \$230,371 thousand increased as a result of additional environmental sites being cleaned up.

- \$24,000 thousand is active sites moved to Base Realignment and Closure (BRAC).
- The remaining balance was revaluation of the Cost to Complete (CTC) estimates of the DERP sites.

Active Installations ER for Closed Ranges (Line 1.A.2): The DON reported a net increase of \$67,978 thousand, 15 percent, in 2<sup>nd</sup> Quarter, FY 2005. The majority of the increase is attributed to the following factors:

- An \$80,000 thousand increase in support for salary, Defense and State Memorandum of Agreement and site investigation costs.
- An increase of \$30,000 in the site investigation at Marine Corps installations.
- This increase was offset by a decrease of \$37,267 thousand in the net change to CTC estimates and a decrease of \$8,173 thousand in expenditures for the period.

#### Environmental Disposal for Weapon Systems.

Nuclear Powered Aircraft Carriers (line 1.D.1): The DON reported an overall increase of \$733,100 thousand, 13 percent, in 2<sup>nd</sup> Quarter, FY 2005. Two factors attributed to the increase in the liability estimate: (1) an increase in the labor rates; and (2) an increase in the cost of materials used in doing the disposal. The source for labor rates and cost of materials is the annual escalation guidance.

Nuclear Powered Submarines (Line 1.D.2): The DON reported an overall increase of \$593,200 thousand, 11 percent, in 2<sup>nd</sup> Quarter, FY 2005. Two factors attributed to the increase in the liability estimate: (1) an increase in the labor rates; and (2) an increase in the cost of materials used in doing the disposal. The source for labor rates and cost of materials is the annual escalation guidance.

Other Nuclear Powered Ships (Line 1.D.3): The DON reported an overall decrease of \$63,600 thousand, 22 percent in 2<sup>nd</sup> Quarter, FY 2005. Two factors attributed to the decrease in the liability estimate: (1) annual review of estimates resulted in decreases in the estimates; and (2) overall disposal program execution.

#### **Information Related to Environmental Liabilities**

##### Accrued Environmental Restoration (DERP Funded) Cost Liabilities.

For 2<sup>nd</sup> Quarter, FY 2005, the DON estimated and reported \$3,250,455 thousand for environmental restoration liabilities. This amount is comprised of \$2,715,051 thousand in Active Installations - Environmental Restoration (ER) liabilities and \$535,404 thousand in Active Installations – ER for Closed Ranges liabilities, which represents Unexploited Ordnance (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 a preliminary total liability of \$258,232 thousand in 2<sup>nd</sup> Quarter, FY 2005; 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 is currently conducting a pilot to define a methodology for identifying and reporting Non-DERP Environmental Liabilities. This pilot is part of the DON Financial Improvement Program.

### Base Realignment and Closure (BRAC).

For 2<sup>nd</sup> Quarter, FY 2005, the DON estimated and reported \$1,097,537 thousand for BRAC funded environmental restoration liabilities. This amount includes \$1,037,145 thousand for environmental restoration (ER) and \$60,392 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 \$12,675,306 thousand in 2<sup>nd</sup> Quarter, FY 2005. This amount includes nuclear powered aircraft carriers of \$6,426,100 thousand, nuclear powered submarines of \$5,765,600 thousand, other nuclear powered ships of \$223,900 thousand and other national defense weapons systems of \$259,705 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 DON Report for FY's 2004-2008, "Strong Environmental Partners; Our Community, Our Navy", July 2004.

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

## Note 15. Other Liabilities

As of March 31	2005			2004
	Current Liability	Noncurrent Liability	Total	Total
<b>1. Intragovernmental</b>				
A. Advances from Others	\$ 31,447,000.00	\$ 0.00	\$ 31,447,000.00	\$ 32,557,000.00
B. Deposit Funds and Suspense Account Liabilities	146,857,150.23	0.00	146,857,150.23	104,811,262.53
C. Disbursing Officer Cash	289,290,572.12	0.00	289,290,572.12	206,388,714.52
D. Judgment Fund Liabilities	0.00	0.00	0.00	46,999,752.39
E. FECA Reimbursement to the Department of Labor	245,145,141.40	200,863,923.20	446,009,064.60	443,928,831.73
F. Other Liabilities	2,796,049,443.01	0.00	2,796,049,443.01	2,841,305,557.35
<b>G. Total Intragovernmental Other Liabilities</b>	<b>\$ 3,508,789,306.76</b>	<b>\$ 200,863,923.20</b>	<b>\$ 3,709,653,229.96</b>	<b>\$ 3,675,991,118.52</b>
<b>2. Nonfederal</b>				
A. Accrued Funded Payroll and Benefits	\$ 252,317,002.72	\$ 0.00	\$ 252,317,002.72	\$ 92,390,475.79
B. Advances from Others	0.00	0.00	0.00	0.00
C. Deferred Credits	0.00	0.00	0.00	0.00
D. Deposit Funds and Suspense Accounts	0.00	0.00	0.00	0.00
E. Temporary Early Retirement Authority	0.00	0.00	0.00	885,173.87
F. Nonenvironmental Disposal Liabilities				
(1) National Defense PP&E (Nonnuclear)	0.00	590,418,056.81	590,418,056.81	576,686,000.81
(2) Excess/Obsolete Structures	53,581,000.00	235,897,000.00	289,478,000.00	333,065,000.00
(3) Conventional Munitions Disposal	0.00	0.00	0.00	0.00
(4) Other	0.00	0.00	0.00	0.00
G. Accrued Unfunded Annual Leave	2,471,051,808.48	0.00	2,471,051,808.48	2,351,596,779.22
H. Capital Lease Liability	5,347.20	0.00	5,347.20	135,406.00
I. Other Liabilities	153,885,541.08	50,233,000.00	204,118,541.08	320,375,238.77
<b>J. Total Nonfederal Other Liabilities</b>	<b>\$ 2,930,840,699.48</b>	<b>\$ 876,548,056.81</b>	<b>\$ 3,807,388,756.29</b>	<b>\$ 3,675,134,074.46</b>
<b>3. Total Other Liabilities</b>	<b>\$ 6,439,630,006.24</b>	<b>\$ 1,077,411,980.01</b>	<b>\$ 7,517,041,986.25</b>	<b>\$ 7,351,125,192.98</b>

## 4. Other Information

### Fluctuation and/or Abnormalities

#### Intragovernmental Other Liabilities.

Deposit Funds and Suspense Account Liabilities (Line 1.B): The DON reported an increase of \$42,046 thousand, 40 percent, in 2<sup>nd</sup> Quarter, FY 2005. The increase is attributed primarily to timing issues in the Pay of the Marine

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Corps account and the Withheld State and Local Taxes account. Also impacting this line is a USD (C) policy change requiring classification of Suspense account disbursement balances in account 2120 instead of 2400 as was prior practice.

Disbursing Officer Cash (Line 1.C): DON reported an increase of \$82,902 thousand, 40 percent, in 2<sup>nd</sup> Quarter, FY 2005. The majority of the increase, \$78,746 thousand relates to the additional foreign currency held by Marine Corps Expeditionary Forces, Camp Lejeune, to meet deployment and mission requirements.

Judgment Fund Liabilities (Line 1.D): To implement new Treasury guidance, Judgment Fund Liabilities were recorded in USSGL 2110 starting 1<sup>st</sup> Quarter, FY 2005, and USSGL 2110 account is mapped to Note 12 rather than Note 15. Therefore, there is a 100 percent decrease in Judgment Fund Liabilities.

Non-Federal Other Liabilities.

Accrued Fund Payroll and Benefits (Line 2.A): Accrued Fund Payroll and Benefits increased \$159,927 thousand, 173 percent, in 2<sup>nd</sup> Quarter FY 2005 due to a timing difference in pay periods.

Temporary Early Retirement Authority (Line 2.E): The TERA program was not extended to 2<sup>nd</sup> Quarter FY 2005. Therefore, there is a 100 percent decrease in Temporary Early Retirement Authority.

Excess/ Obsolete Structures (Line 2.F.2): Excess/ Obsolete Structures decreased \$43,587 thousand, 13 percent, in 2<sup>nd</sup> Quarter FY 2005 as a result of a budget reduction.

Capital Leases Liability (Line 2.H): Capital Leases Liability decreased \$130 thousand, 96 percent, in 2<sup>nd</sup> Quarter FY 2005 due to the Navy reporting less Capital Lease liability in the DCI and the expiration of leases during this period.

Other Liabilities (Line 2.I): Other Liabilities decreased \$116,257 thousand, 36 percent. The following attributed to the decrease:

- \$64,000 thousand in liability litigation was paid and is no longer recognized.
- \$23,238 thousand in Cancelled Appropriations was remapped to Payables (Note 12).
- \$17,514 thousand decrease in Contract Incentives.
- \$11,505 thousand decrease in Contract Holdbacks.

**Information Related to Other Liabilities**

**Intragovernmental Other Liabilities:**

Judgment Fund (Line 1.D).

To implement the guidance from the Treasury, Judgment Fund Liabilities was recorded in USSGL 2110 starting 1<sup>st</sup> Quarter, FY 2005, and USSGL 2110 account is mapped to Note 12.

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

	As of March 31, 2005
Liability to Treasury & Others	\$2,667,240,993.53
Unemployment	81,598,321.74
Employment Benefit	47,210,127.74
Total Intragovernmental Other Liabilities	<u>\$2,796,049,443.01</u>

With respect to the major fiduciary balances, the DON must reconcile with the Department of Labor and the Office of Personnel Management. In 2<sup>nd</sup> Quarter FY 2005, the DON reported the following Intragovernmental Fiduciary liabilities: \$446,009 thousand in FECA, \$81,598 in Unemployment, \$47,210 thousand in Employment Benefit.

**Non-Federal Other Liabilities:**

Non-Environmental Disposal Liability Disclosure.

The DON recognizes the Non-Environmental disposal liability for nuclear powered assets when the asset is initially placed in service. The Non-Environmental costs are included with the environmental disposal costs and reported in Note 14. However, the \$590,418 thousand reported is estimated Non-Environmental disposal liability for conventional military equipment.

Excess/Obsolete Structures (Line 2.F.2).

The reported amount of \$289,478 thousand is an estimate of disposing excess/obsolete structures at active installations.

Other Liabilities (Line 2.I.) includes \$115,441 thousand Contract Holdbacks and \$88,677 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.

## Capital Lease Liability

As of March 31

	2005				2004
	Asset Category				Total
	Land and Buildings	Equipment	Other	Total	
<b>1. Future Payments Due</b>					
A. 2005	\$ 0.00	\$ 5,347.20	\$ 0.00	\$ 5,347.20	\$ 135,406.00
B. 2006	0.00	0.00	0.00	0.00	0.00
C. 2007	0.00	0.00	0.00	0.00	0.00
D. 2008	0.00	0.00	0.00	0.00	0.00
E. 2009	0.00	0.00	0.00	0.00	0.00
F. After 5 Years	0.00	0.00	0.00	0.00	0.00
G. Total Future Lease Payments Due	\$ 0.00	\$ 5,347.20	\$ 0.00	\$ 5,347.20	\$ 135,406.00
H. Less: Imputed Interest Executory Costs	0.00	0.00	0.00	0.00	0.00
I. Net Capital Lease Liability	\$ 0.00	\$ 5,347.20	\$ 0.00	\$ 5,347.20	\$ 135,406.00
<b>2. Capital Lease Liabilities Covered by Budgetary Resources</b>				\$ 0.00	\$ 135,406.00
<b>3. Capital Lease Liabilities Not Covered by Budgetary Resources</b>				\$ 5,347.20	\$ 0.00

### 4. Other Information Related to Capital Lease Liability

#### Fluctuation and/or Abnormalities

The DON reported a decrease of \$130 thousand, 96 percent, in Equipment Leases, net in 2<sup>nd</sup> Quarter, FY 2005 when compared with 2<sup>nd</sup> Quarter, FY 2004. This reflects the ongoing effort to validate Equipment Leases in the DPAS database and the expiration of leases for the period.

#### 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 2005. The proper breakout of future payments to appropriate years will be done when a process for capturing lease liabilities is implemented.

Capital Leases Liabilities \$135,406 in FY 2004 should be under line 3, Capital Leases Liabilities Not Covered by Budgetary Resources rather than line 2, Capital Leases Liabilities Covered by Budgetary Resources.

#### 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.



**Note 16. Commitments and Contingencies****Legal 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 year 2004, the DON General Fund materiality threshold for reporting litigation, claims, or assessments was \$33.3 million. The amount 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 threshold. This amount represents the maximum amount 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 as of 30 September 2004 that met the materiality threshold. However, DON legal counsel was unable to express an opinion concerning the likely outcome of these cases. The Legal Representation Letter process will be updated in 4<sup>th</sup> quarter FY 2005. The DON General Fund materiality threshold for fiscal year 2005 will be \$53.2 million.

**Other Commitments and Contingencies**

In addition, DON has other contingent liabilities primary consisting of \$3,666 thousand resulting from contractual actions and \$100 thousand (the estimated cost) to dispose of seven aircraft that had been used for training.

In addition to contingent liabilities, contractual commitments for cancelled appropriations consists of an estimated of \$3.3 million.

**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.

<b>Note 17.</b>	<b>Military Retirement Benefits and Other Employment Related Actuarial Liabilities</b>
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As of March 31	2005				2004
	Actuarial Present Value of Projected Plan Benefits	Assume Interest Rate (%)	(Less: Assets Available to Pay Benefits)	Unfunded Actuarial Liability	Unfunded Actuarial Liability
<b>1. Pension and Health Benefits</b>					
A. Military Retirement Pensions	\$ 0.00		\$ 0.00	\$ 0.00	\$ 0.00
B. Military Retirement Health Benefits	0.00		0.00	0.00	0.00
C. Medicare-Eligible Retiree Benefits	0.00		0.00	0.00	0.00
D. Total Pension and Health Benefits	\$ 0.00		\$ 0.00	\$ 0.00	\$ 0.00
<b>2. Other</b>					
A. FECA	\$ 1,575,815,538.46		\$ 0.00	\$ 1,575,815,538.46	\$ 1,589,970,895.43
B. Voluntary Separation Incentive Programs	0.00		0.00	0.00	0.00
C. DoD Education Benefits Fund	0.00		0.00	0.00	0.00
D. <u>{Enter Program Name}</u>	0.00		0.00	0.00	0.00
E. Total Other	\$ 1,575,815,538.46		\$ 0.00	\$ 1,575,815,538.46	\$ 1,589,970,895.43
<b>3. Total Military Retirement Benefits and Other Employment Related Actuarial Liabilities:</b>	\$ 1,575,815,538.46		\$ 0.00	\$ 1,575,815,538.46	\$ 1,589,970,895.43

Actuarial Cost Method Used:

Assumptions:

Market Value of Investments in Market-based and Marketable Securities:

#### **4. Other Information Related 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 Budget's economic assumptions for 10-year Treasury notes and bonds. Interest rate assumptions utilized for discounting were as follows:

FY 2005

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:

<u>CBY</u>	<u>COLA</u>	<u>CPIM</u>
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 details the numbers used in support of the allocation:

	<u>Personnel</u>	<u>Allocation %</u>
DON General Fund	111,166	57%
DON 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.

<b>Note 18.</b>	<b>Disclosures Related to the Statement of Net Cost</b>
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**Fluctuation and/or Abnormalities**

The DON reported a decrease of \$9,760,053 thousand, 15 percent, in the Net Cost of Operations in 2<sup>nd</sup> Quarter FY 2005. A decrease of \$7,003,692 was reported in the Military Construction account, and a decrease of \$6,897,661 was reported in the Procurement account. These decreases were offset by other variances.

Intragovernmental Earned Revenue (Line 1.B) increased \$288,890 thousand, 38 percent, from the 2<sup>nd</sup> Quarter FY 2004. Significant increases are with the following trading partners:

<u>Trading Partner</u>	<u>Amounts (in thousands)</u>
Army General Fund	\$100,214
Army Working Capital Fund	139,106
Other Defense Organizations GF	36,675
Other Defense Organizations WCF	60,224

Earned Revenue From the Public (Line 1.E) increased \$1,358,934 thousand, 102 percent, from the 2<sup>nd</sup> Quarter FY 2004. The increase resulted in part from increased activity with DON's public customers and in part from adjustments to cover Intragovernmental revenues in the trading partner process. After identification of revenues from DON's Intragovernmental trading partners that is reported as Intragovernmental, the remaining revenue is classified as Public. In 2<sup>nd</sup> Quarter FY 2005, the elimination process identified the majority of revenues as Intragovernmental. The identification of the majority of revenues being from other governmental sources, and the minority being from the public, is supported by the unofficial Report on Reimbursements (DD725).

Current systems do not consistently differentiate Public costs from Intragovernmental costs. Therefore, costs have to be controlled at the grand total level and then adjusted for trading partner submissions and other known items. Compounding this methodology is the fact that costs were controlled at the Intragovernmental (and then allocated to Public) level in 2<sup>nd</sup> Quarter FY 2004, but are now being controlled at the Public level (and then allocated to Intragovernmental) in 2<sup>nd</sup> Quarter FY 2005. This change in accounting treatment makes comparisons problematic.

Gross Costs, Intragovernmental and Public decreased \$8,112,229 thousand, 25 percent, from the 2<sup>nd</sup> Quarter FY 2004. Depreciation adjustments in the Military Construction and Procurement accounts in the amount of \$7,002,229 thousand and losses on disposal of \$1,655,320 thousand for buildings and structures were recorded in FY 2004; making FY 2005 costs appear lower by comparison. There are other Gross Cost offsets such as increases in the Military Personnel accounts and decreases in the Procurement accounts.

**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.

## Gross Cost and Earned Revenue by Budget Functional Classification

As of March 31

	2005			2004
	Gross Cost	(Less: Earned Revenue)	Net Cost	Net Cost
<b>Budget Functional Classification</b>				
1. Department of Defense Military (051)	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
2. Water Resources by U.S. Army Corps of Engineers (301)	0.00	0.00	0.00	0.00
3. Pollution Control and Abatement by US. Army Corps of Engineers (304)	0.00	0.00	0.00	0.00
4. Federal Employees Retirement and Disability, Department of Defense Military Retirement Fund (602)	0.00	0.00	0.00	0.00
5. Veterans Education, Training, and Rehabilitation by Department of Defense Education Benefits Trust Fund (702)	0.00	0.00	0.00	0.00
6. Medicare Eligible Retiree Health Care Fund (551)	0.00	0.00	0.00	0.00
<b>7. Total</b>	<b>\$ 0.00</b>	<b>\$ 0.00</b>	<b>\$ 0.00</b>	<b>\$ 0.00</b>

### Gross Cost to Generate Intragovernmental Revenue and Earned Revenue (Transactions with Other Federal—Non-DoD—Entities) by Budget Functional Classification

As of March 31

	2005			2004
	Gross Cost to Generate Intragovernmental Revenue	(Less: Earned Revenue)	Net Cost	Net Cost
1. Department of Defense Military (051)	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
2. Water Resources by U.S. Army Corps of Engineers (301)	0.00	0.00	0.00	0.00
3. Pollution Control and Abatement by US. Army Corps of Engineers (304)	0.00	0.00	0.00	0.00
4. Federal Employees Retirement and Disability Department of Defense Military Retirement Trust Fund (602)	0.00	0.00	0.00	0.00
5. Veterans Education, Training, and Rehabilitation by Department of Defense Education Benefits Trust Fund (702)	0.00	0.00	0.00	0.00
6. Medicare Eligible Retiree Health Care Fund (551)	0.00	0.00	0.00	0.00
<b>7. Total</b>	<b>\$ 0.00</b>	<b>\$ 0.00</b>	<b>\$ 0.00</b>	<b>\$ 0.00</b>

## Benefit Program Expenses

As of March 31	2005	2004
1. Service Cost	\$ 0.00	\$ 0.00
2. Period Interest on the Benefit Liability	0.00	0.00
3. Prior (or past) Service Cost	0.00	0.00
4. Period Actuarial Gains or (Losses)	0.00	0.00
5. Gains/Losses Due to Changes in Medical Inflation Rate Assumption	0.00	0.00
<b>6. Total Benefit Program Expense</b>	<b>\$ 0.00</b>	<b>\$ 0.00</b>

Amounts for Foreign Military Sales (FMS) Program Procurements from Contractors

### Stewardship Assets

#### **Disclosures Related to 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.

### Suborganization Program Costs



<b>Note 19.</b>	<b>Disclosures Related to the Statement of Changes in Net Position</b>
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As of March 31	2005	2005	2004	2004
	Cumulative Results of Operations	Unexpended Appropriations	Cumulative Results of Operations	Unexpended Appropriations
<b>1. Prior Period Adjustments Increases (Decreases) to Net Position</b>				
A. Changes in Accounting Standards	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
B. Errors and Omissions in Prior Year Accounting Reports	0.00	0.00	(25,913,749,160.94)	25,913,749,160.94
C. Other Prior Period Adjustments	0.00	0.00	0.00	0.00
D. Total Prior Period Adjustments	\$ 0.00	\$ 0.00	\$ (25,913,749,160.94)	\$ 25,913,749,160.94
<b>2. Imputed Financing</b>				
A. Civilian CSRS/FERS Retirement	\$ 108,560,795.85	\$ 0.00	\$ 124,213,060.49	\$ 0.00
B. Civilian Health	159,799,870.00	0.00	145,832,203.00	0.00
C. Civilian Life Insurance	473,799.30	0.00	503,227.58	0.00
D. Judgment Fund	14,660,901.89	0.00	14,397,300.08	0.00
E. Total Imputed Financing	\$ 283,495,367.04	\$ 0.00	\$ 284,945,791.15	\$ 0.00

### 3. Other Information Related to the Statement of Changes in Net Position

#### Other Disclosures

##### 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

Navy GF

Treasury appropriation 20X1743, and that portion of 20X1741 that is related to the No FEAR Act are required to be repaid by DON.

<b>Note 20.</b>	<b>Disclosures Related to the Statement of Budgetary Resources</b>
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As of March 31	2005	2004
1. Net Amount of Budgetary Resources Obligated for Undelivered Orders at the End of the Period	\$ 86,909,727,528.97	\$ 82,893,969,326.88
2. Available Borrowing and Contract Authority at the End of the Period	0.00	739,274.00

### 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 \$16,787 thousand between the SBR Appropriations Received and the Statement of Change of Net Position (SOCNP) Appropriations Received is due to the Trust Funds and Special Receipt Accounts, USSGL 4114, not being included in the Appropriations Received line of the SOCNP.

#### Other Disclosures

Obligations Incurred includes \$87,114,222 thousand of Direct Program Obligations and \$5,300,985 thousand of Reimbursable Program Obligations.

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

In FY 2005, DoD treated Foreign Military Sales (FMS) Trust Fund transactions as Non-Federal, 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. Office of the Under Secretary of Defense (Comptroller) 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. Thus far in FY 2005, \$10,085 thousand was transferred from the NDSF to the Shipbuilding and Conversion, Navy appropriation and \$924 thousand was transferred to the Department of Energy.

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. Thus far in FY 2005, \$265,955 thousand was transferred from ER, N to the Operations and Maintenance, Navy appropriation and \$204 thousand was transferred to the Department of Energy.

<b>Note 21.</b>	<b>Disclosures Related to the Statement of Financing</b>
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**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. For 2<sup>nd</sup> Quarter FY 2005, an adjustment of \$1,453,517 thousand was recorded.

**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.

<b>Note 22.</b>	<b>Disclosures Related to the Statement of Custodial Activity</b>
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Not applicable.

<b>Note 23.</b>	<b>Other Disclosures</b>
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As of March 31	2005					2004
<b>1. ENTITY AS LESSEE- Operating Leases</b>						
Future Payments Due <u>Fiscal Year</u>	<u>Land and Buildings</u>	<u>Equipment</u>	<u>Other</u>	<u>Total</u>	<u>Total</u>	<u>Total</u>
2006	\$ 19,399,785.00	\$ 0.00	\$ 0.00	\$ 19,399,785.00	\$ 7,248,101.00	\$ 7,248,101.00
2007	20,498,002.00	0.00	0.00	20,498,002.00	7,551,908.00	7,551,908.00
2008	21,510,875.24	0.00	0.00	21,510,875.24	7,855,735.00	7,855,735.00
2009	22,578,765.00	0.00	0.00	22,578,765.00	8,160,249.00	8,160,249.00
2010	22,330,402.00	0.00	0.00	22,330,402.00	N/A	N/A
After 5 Years	0.00	0.00	0.00	0.00	0.00	0.00
Total Future Lease Payments Due	\$ 106,317,829.24	\$ 0.00	\$ 0.00	\$ 106,317,829.24	\$ 30,815,993.00	\$ 30,815,993.00

### Fluctuations and/or Abnormalities

The DON reported an increase of \$67,556 thousand, 174 percent, in Operating Leases Future Payment in 2<sup>nd</sup> Quarter FY 2005. The increase is due to better data collection efforts throughout the Navy shore establishment. Five shore regions reported Operating Leases in FY 2005 as compared with FY 2004 when only one region reported Operating Leases.

### Definitions

Lessee – A person or entity that 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 that does not substantially transfer all the benefits and risk of ownership. Payments are charged to expense over the lease term as they become payable.

### Other Disclosure

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