

United States Army Annual Financial Statement



*The Cost of Freedom: A Challenge, Not a Choice.*





## **Fiscal Year 2006 United States Army Annual Financial Statement**

Message from the Secretary of the Army	iii
Message from the Assistant Secretary of the Army (Financial Management and Comptroller)	v
Message from the Assistant Secretary of the Army (Civil Works)	vii
Management's Discussion & Analysis	1
General Fund – Principal Financial Statements, Notes, and Supplementary Information	35
Working Capital Fund – Principal Financial Statements, Notes, and Supplementary Information	113
Civil Works Fund – Management's Discussion & Analysis	161
Civil Works Fund – Principal Financial Statements, Notes, and Supplementary Information	179



*The Cost of Freedom: A Challenge, Not a Choice.*

2006

November 13, 2006

Five years after the tragic events of September 11, and through five years of demanding combat operations in Iraq and Afghanistan as well as operations in support of Homeland security and disaster relief, the Army remains the preeminent landpower in the world today.

The all-volunteer force has answered the call to duty and put boots on the ground in nearly 70 countries around the globe. In FY 2006, the active Army had its best recruiting year in almost a decade, while the National Guard had its best year in thirteen years. In total, we recruited more than 175,000 young Americans.

Nearly 260,000 Soldiers are deployed and forward stationed around the world, fighting and winning the Global War on Terrorism with great courage, commitment and compassion. This long war is unlike any other we have fought. Asymmetric and irregular, it requires our Army to continually adapt, change and find innovative ways to defeat a lethal enemy that remains dispersed, elusive and willing to kill large numbers of innocent civilians to achieve its aims.

As we look to the future, our overall challenge remains twofold: to fight and win a protracted war against global terror and to continue forging the Army of the future. Our strategy is to build a Future Force through transformation and modernization while sustaining our current global commitments.

We have made significant progress in transitioning the operational Army into a brigade-based modular force. To date, the Army has converted 73 percent of its brigades to the modular design—35 Active and 16 Army National Guard Brigades of the 70 planned. This transformation is occurring in combination with our key modernization programs, the Future Combat Systems and the revamping of Army aviation. The Army's key ground modernization program, the Future Combat Systems, will provide our forces significant tactical and operational advantages.

Through Army business transformation, we will free up resources for the operational Army, including restationing, resetting and growing the force, and delivering improved equipment to the Soldier in a timely manner. Our Lean Six Sigma efforts will be particularly helpful in reaching this goal.

The Army requires extensive and sustainable financial resources to execute its plan. As a nation, we must ensure that the Army receives the funding it needs. Providing for our volunteer Soldiers must be a national priority and not a matter of affordability. It is our responsibility to ensure that the men and women who wear the Army's uniform continue to be the best trained, best organized, best equipped, and best sustained military force in history. They deserve nothing less.



**Francis J. Harvey**

*Secretary of the Army*



*The Cost of Freedom: A Challenge, Not a Choice.*

2006

## Message From the Assistant Secretary of the Army (Financial Management and Comptroller)

---

v

November 13, 2006

Manning, equipping and training an Army at war demands effective and efficient resource management. To accomplish this, the Army must understand its past – how we have used previously appropriated funds; its present – how we can meet current missions with current and budgeted resources; and its future – how requirements will change.

To understand the past, the Army must have rigorous and disciplined accounting practices, strong financial controls and modern financial systems. To meet the demands of the present, we must assure that budget requests are sound and defensible, and that supplemental funding covers validated needs not recognized through the regular budgeting process. Comprehending future possibilities may be the most difficult of these tasks, demanding the ability to predict how the Army must change in a rapidly evolving 21st century security environment.

During fiscal year 2006, the Army made significant progress in each of these aspects of resource management. Development of the General Fund Enterprise Business System (GFEBS) reached an important milestone, with the system completing a successful technology demonstration involving real property inventory at Ft. Jackson, SC. GFEBS is on track, with the full financial system blueprint due to be completed in spring 2007 and deployment of a fully capable system at Ft. Jackson expected in spring 2008. In 2006 the Army also tested the Funds Control Module (FCM), new software that integrates logistics and financial systems, allowing accelerated fund availability verification and better controls for order processing. With these and other technology initiatives, the Army is improving its financial management so that we can be better stewards of our resources.

2006 also presented some significant financial operations challenges. The annual appropriation was not received until the end of the first quarter and the final supplemental appropriation arrived at the end of the third quarter, requiring continuous adjustment of resources between competing demands in a dynamic operational environment. Army financial managers did an extraordinary job providing the budget justifications and reprogramming documentation to Congress that supported the management decisions of an Army at war.

Perhaps one of the most noteworthy accomplishments in 2006 was our effort to better understand the true cost of the Army. Following a careful analysis (which was vetted within and beyond the Defense Department), FM&C ascertained that, to meet its current mission under current doctrine, the Army requires approximately \$138 billion (in FY 2008 dollars). We had known for some time that there was an imbalance between the Army's missions, as laid out in the National Defense Strategy, and the financial resources available to fulfill them. This solid quantification of the strategy-resources mismatch should enable Army, DoD and congressional leaders to make better-informed policy and fiscal decisions in the future.

These are challenging times for the Army. The pace of military operations and our simultaneous organizational transformation continue to demand significant personal sacrifice by the men and women of our all-volunteer force. As financial managers, we must make sure that they can accomplish their missions. That means leveraging Army resources so that the force can meet the challenges of the 21st century security environment, showing American taxpayers that they are getting the right return on their investment. I am confident that, during the coming year, we will continue to make progress in building an Army ready to defend the nation anywhere, anytime.



**Nelson M. Ford**

*Assistant Secretary of the Army (Financial Management and Comptroller)*



*The Cost of Freedom: A Challenge, Not a Choice.*

2006



## Message From the Assistant Secretary of the Army (Civil Works)

---

vii

During Fiscal Year 2006, the Army Corps of Engineers continued its long-standing tradition of serving the nation in peace and war. Through its military program, the Corps continued with reconstruction work in the countries of Iraq and Afghanistan in an effort to help bring security, stability and economic opportunity to the region. As the fiscal year began, the nation's attention was focused on the Gulf Coast and the city of New Orleans where, a month earlier Hurricane Katrina, and later Hurricane Rita, caused devastating destruction. The Corps mounted a massive year-long response, rebuilding stronger levees and floodwalls through its Civil Works program, and clearing debris, repairing roofs, providing temporary housing, and restoring power through its leadership role under the Department of Homeland Security's National Response Plan. The events of the past year are a reminder of how critical the Army Civil Works mission is to the safety, security and economy of our great nation.

As depicted in this annual report, much has been accomplished in the nine Civil Works business programs, and much remains to be done. Over the past ten years, Corps flood damage reduction projects have prevented damages averaging approximately \$20 billion per year. Corps projects provide hydroelectric power, an environmentally sustainable, reliable and efficient domestic energy source, and continuing effort is needed to bring reliability and production rates up to industry standards. With the rapid growth in world trade, coastal harbors and inland waterways are more vital to our nation's economy than ever before. With an aging infrastructure and changes in the dimensions of the vessels in the world fleet, the Corps is faced with significant challenges to reduce unscheduled closure times and improve the reliability of the nation's navigation systems. Through its aquatic ecosystem restoration program, the Corps is making tremendous investments in restoring the natural values of degraded environments, such as the Everglades.

The above examples provide a glimpse of the challenges that lie ahead for the Army's Civil Works program. The annual report addresses these and similar issues in the other Corps business programs. Investment in the Civil Works program is based on performance, with objectives and measures that focus on opportunities to realize economic and environmental benefits with each investment increment.

The Army's commitment to the Civil Works program is strong. The strategic goals are to sustain development of our nation through integrated water resource management, to protect the environment and natural resources, to ensure project performance, to reduce vulnerability to natural disasters, and to ensure that the Army Corps of Engineers is a world-class public engineering organization. These goals will be achieved as the Corps continues to serve the public in collaboration with non-Federal public and private partners, stakeholders and users of Civil Works projects and programs across our great country.



**John Paul Woodley, Jr.**

*Assistant Secretary of the Army (Civil Works)*



### ***Relevant and Ready Landpower in Service to the Nation***

*The Nation has entrusted the Army with preserving its peace and freedom, defending its democracy, and providing opportunities for its Soldiers to serve the country and personally develop their skills and citizenship. Consequently, we are and will continuously strive to remain among the most respected institutions in the United States. To fulfill our solemn obligation to the Nation, we must remain the preeminent land power on earth—the ultimate instrument of national resolve; strategically dominant on the ground where our Soldiers’ engagements are decisive.*

---

The Honorable Francis J. Harvey, Secretary of the Army

## Overview

The United States (U.S.) continues to face an unprecedented national security threat. Defending the nation in this tough environment has placed tremendous demands on the Army. Yet, the all-volunteer force has demonstrated its commitment to fighting an adaptive enemy, while also meeting America's obligations to traditional allies and our homeland.

At the same time, the Army is proceeding with a sweeping transformation effort – implementing innovative and efficient business practices, modernizing equipment, revamping its organizational and operational structures, and adapting tactics to meet a broad range of new asymmetric threats.

Sustaining the all-volunteer force is the most important strategic issue facing the Army today. The Army must fully man, equip and train its units. The Army also must provide its Soldiers and their families a quality of life that equals the quality of service they give the nation. Obtaining adequate, timely and consistent funding is therefore essential.

Today's appropriations, and fiscal guidance for the future, do not match the Army's current operational and readiness requirements, however. Without sufficient resources, the Army cannot continue at the current pace and proceed with transformation. Faltering in the current war is not an option, nor is delaying or abandoning activities that will enable the Army to maintain its position as the world's pre-eminent land power. It is important for all stakeholders – the



Sgt. David Burns, from the 1st Brigade Combat Team, 1st Armored Division, conducts a checkpoint assessment in Tal Afar, Iraq.

General Fund and Working Capital Fund

# 2006

Defense Department, the Office of Management and Budget (OMB), the U.S. Congress and the American public – to understand this strategy-resources mismatch and fix the disparity that threatens the Army’s ability to meet its mission.

Supplemental appropriations continue to be essential to the Army’s ability to execute its mission. This funding, however, is not predictable or sustained, which creates inefficiencies. This funding challenge has required the Army to constantly shift resources and incur increased overhead costs. In addition, accommodating the uneven flow of cash has drawn significant amounts of time and attention from the senior leadership – human resources that could be better spent otherwise. These challenges are discussed in detail in the *Possible Future Effects of Existing Events and Conditions* section.

Despite funding challenges, the Army has accelerated its transformation momentum. We are proceeding apace with training and education programs, based on recent combat experiences, to develop innovative and adaptive Soldiers and leaders. The Army also is adapting its doctrine for training, fighting and sustaining the force. The switch to more capable, more flexible and more deployable brigades is progressing rapidly, and the Army is increasing Soldier and unit effectiveness and protection. The Army intends to keep moving forward in fiscal year (FY) 2007 and is confident its success will continue, as long as proper support is made available.

## Mission

The Army mission is to support the National Security and Defense strategies by providing well-trained, well-led, and well-equipped forces to the combatant commanders. This mission encompasses the intent of the U.S. Congress, as defined in Title 10 of the U.S. Code, for the military to:

- Preserve the peace and security of, and provide the defense for, the U.S., the Territories, Commonwealths, and Possessions of the U.S., and any areas occupied by the U.S.;
- Support the national policies;
- Implement national objectives; and
- Overcome any nations responsible for aggressive acts that imperil the peace and security of the U.S.



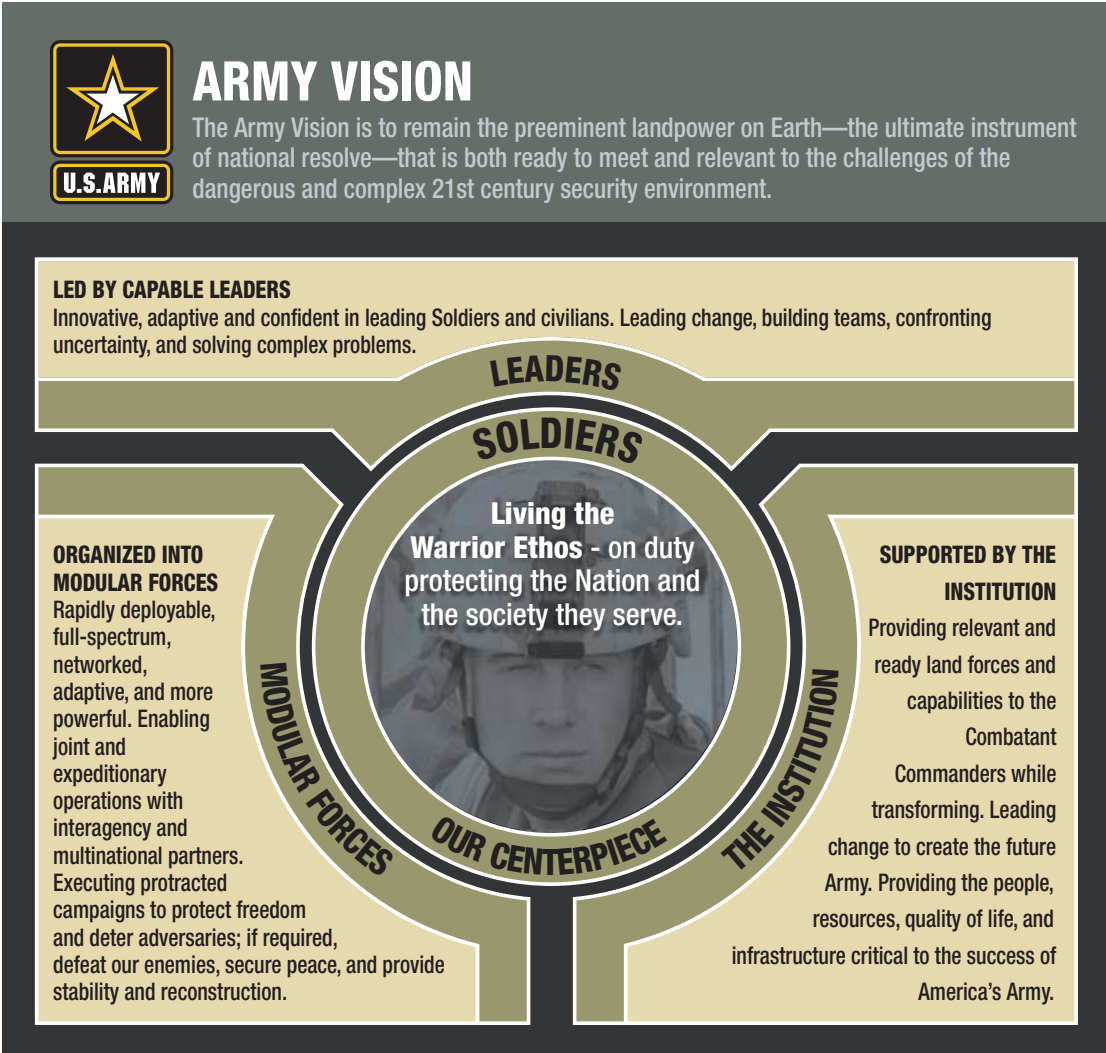
Soldiers from the 2nd Brigade Combat Team, 1st Infantry Division, take up defensive positions on a snow-covered berm at the Grafenwohr Training Area in Germany.

This mission has remained constant throughout the 230-year life of the Army; however, the environment and nature of conflict have changed dramatically over that same time, especially in the context of today’s Global War on Terrorism (GWOT). New adversaries and the growth in asymmetric warfare have compelled the Army to transform how it trains and equips its Soldiers, how those Soldiers are organized and how they fight. This near-revolution is progressing rapidly, and it must not slow or falter if the Army is to continue to meet the nation’s domestic and international security obligations today and into the future.

**Vision**

The Army is committed to remaining the world’s preeminent land power – relevant and ready at all times to serve the nation and to support our allies. The Army will continue to supply U.S. combatant commanders with the forces necessary to defeat any adversary, in any situation, at any time. The Army therefore must fully train and appropriately organize its forces; develop innovative and adaptive leaders; and design support structures appropriate for the new global security environment.

Figure 1. Army Vision

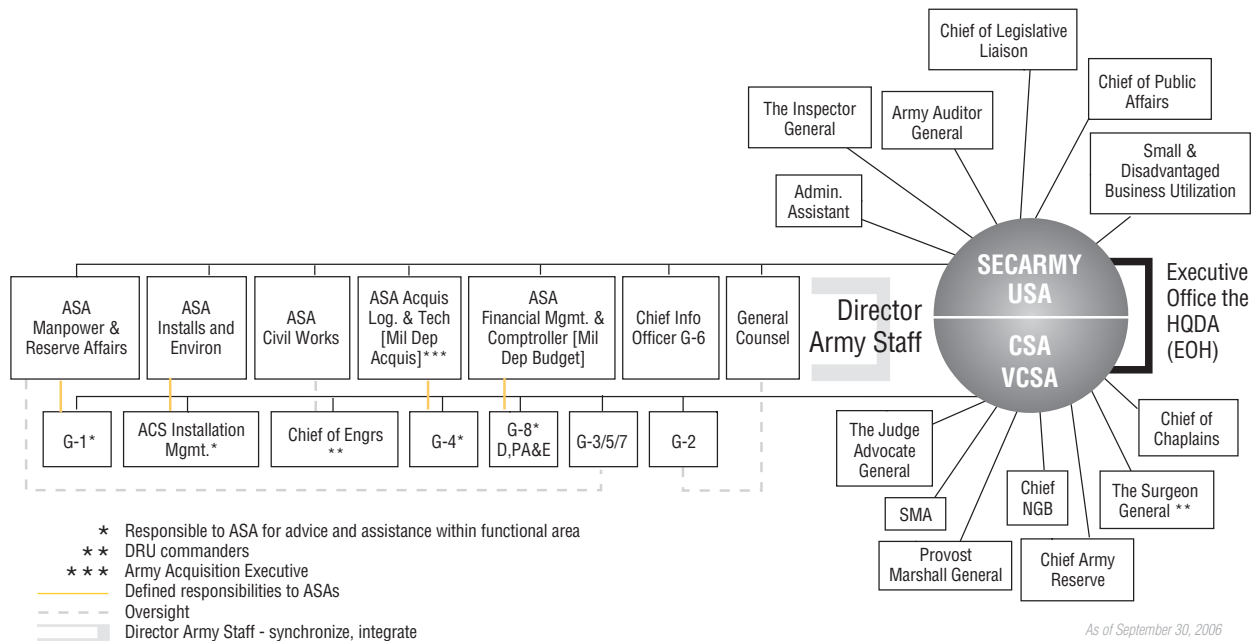


## Organization of the Army

The Army is a very large and complex organization, with more than 580,000 Soldiers on active duty; about 160,000 are deployed and another 108,000 are forward-stationed outside the U.S. These warfighters are supported by more than 239,000 civilians, who are critical members of the institution at every level.

The Army is organized with the primary objective of supporting and sustaining the mobilization, training and deployment of its Soldiers, anywhere in the world. The Headquarters, Department of the Army (HQDA) (Figure 2), under the direction of the Secretary of the Army and the Chief of Staff, leads and manages the entire Army.

Figure 2. Headquarters, Department of the Army (HQDA)



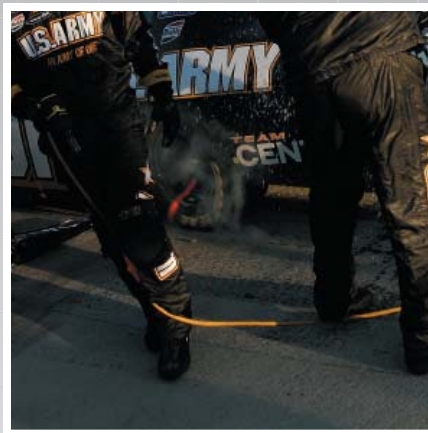
Effective October 1, 2006, the Army reorganized the command structure below the HQDA level. The purpose of the reorganization, which eliminated the Major Army Commands, is to better support a leaner, more agile, modular force.

The Army organizational structure consists of two interdependent pieces: (1) the warfighting, operational Army; and (2) the institutional Army, which supports those operational forces by providing the training, facilities and equipment necessary to prepare and sustain Soldiers for their mission.

The operational Army provides the land power capabilities for the combatant commander. Within the operational Army, the transition from a division-centric warfighting force to a brigade-centric force continues. At the heart of this change is the modularization and standardization of Army brigade combat teams (BCT), a process that is essential to the development of a more rapidly deployable, flexible and powerful force.

Viewed by its constituent elements, the Army can be separated into the active and reserve components.

The active component consists of full-time Soldiers assigned to the operational and institutional organizations that perform day-to-day Army missions. The U.S. Congress annually reviews and mandates the number of Soldiers that the Army may maintain.



*"The metaphor of the racecar to describe the difference between the operational army and the institutional army, I think, is a good one. The pit crew would be the institutional army. It's those things that stand behind the operational force and enable it to be properly trained, properly equipped, properly recruited, properly manned, and properly structured."*

LTG N. Ross Thompson, III, Army Director of Program Analysis and Evaluation

The reserve component consists of the Army National Guard (ARNG) and the U.S. Army Reserve (USAR). The ARNG has two missions: federal and state. Its federal mission is to provide trained and ready forces for wartime, national emergencies and other requirements as necessary. Its state mission is to train for, and respond to, domestic emergencies and other missions as required by state law. Unless federally mobilized, ARNG units are commanded by their state executive, usually the governor.

The USAR is the primary federal reserve force of the Army. The USAR provides specialized units and resources to support the deployment and sustainment of Army forces around the globe. In addition, the USAR is the main source of individual Soldiers to augment headquarters staff and to fill vacancies in the active component. Throughout FY 2006 and several prior fiscal years, the Army experienced unprecedented high levels of reserve component activation and deployment. This, combined with brigade modularization, marks the present as the era of most profound change in the Army since World War II.

## **Performance Goals, Objectives and Results**

Our nation remains at war and engaged in a long struggle of continuously evolving conflict against learning, adaptive enemies. The GWOT requires us to be heavily engaged in two distinct theatres – Iraq and Afghanistan – while maintaining a geographically broad presence in dozens of other nations. The Army anticipates sustaining this level of commitment for the foreseeable future. In addition, the Army's role in the homeland security mission, with more than 9,000 supporting operations in the continental U.S., is greater than at any other time, except the days immediately following the terrorist attacks of September 11, 2001.

Within this context, the Army continues to pursue comprehensive transformation in order to realize its vision of providing the nation dominant land power that is relevant and ready to meet the challenges of a dangerous and complex 21st century security environment. This transformation is framed in terms of the broader defense transformation effort and addresses the needs of the Joint Force as well as the needs of the Army.

In the spring of 2005, the Army published an annex to the Department of Defense Annual Report to the President and Congress. It serves as the statutory performance plan for FY 2006, required by the Government Performance and Results Act (GPRA) of 1993. This annex, and the GPRA, use the strategy set by the Secretary of the Army as the context in which to examine what the Army 'bought' with the resources entrusted to it by the American people.

The four overarching strategies laid out by Army leadership for FY 2006 are supported by 19 strategic initiatives (Figure 3). The nineteenth initiative, *Securing Financial Resources and Legislative Authorities to Meet Requirements*, acts as the foundation without which the Army cannot fully execute the other initiatives.

In FY 2006, the Army conducted a detailed analysis to validate the force structure cost associated with accomplishing the missions set forth in the Office of the Secretary of Defense (OSD) Quadrennial Defense Review (QDR). The analysis determined that, in order to support fully the QDR, the Army requires basic appropriations of \$138 billion in FY 2008 dollars, a figure that is 30 percent above historical funding levels. The potential impact of this shortfall is discussed in detail in the *Possible Future Effects of Existing Events and Conditions* section.

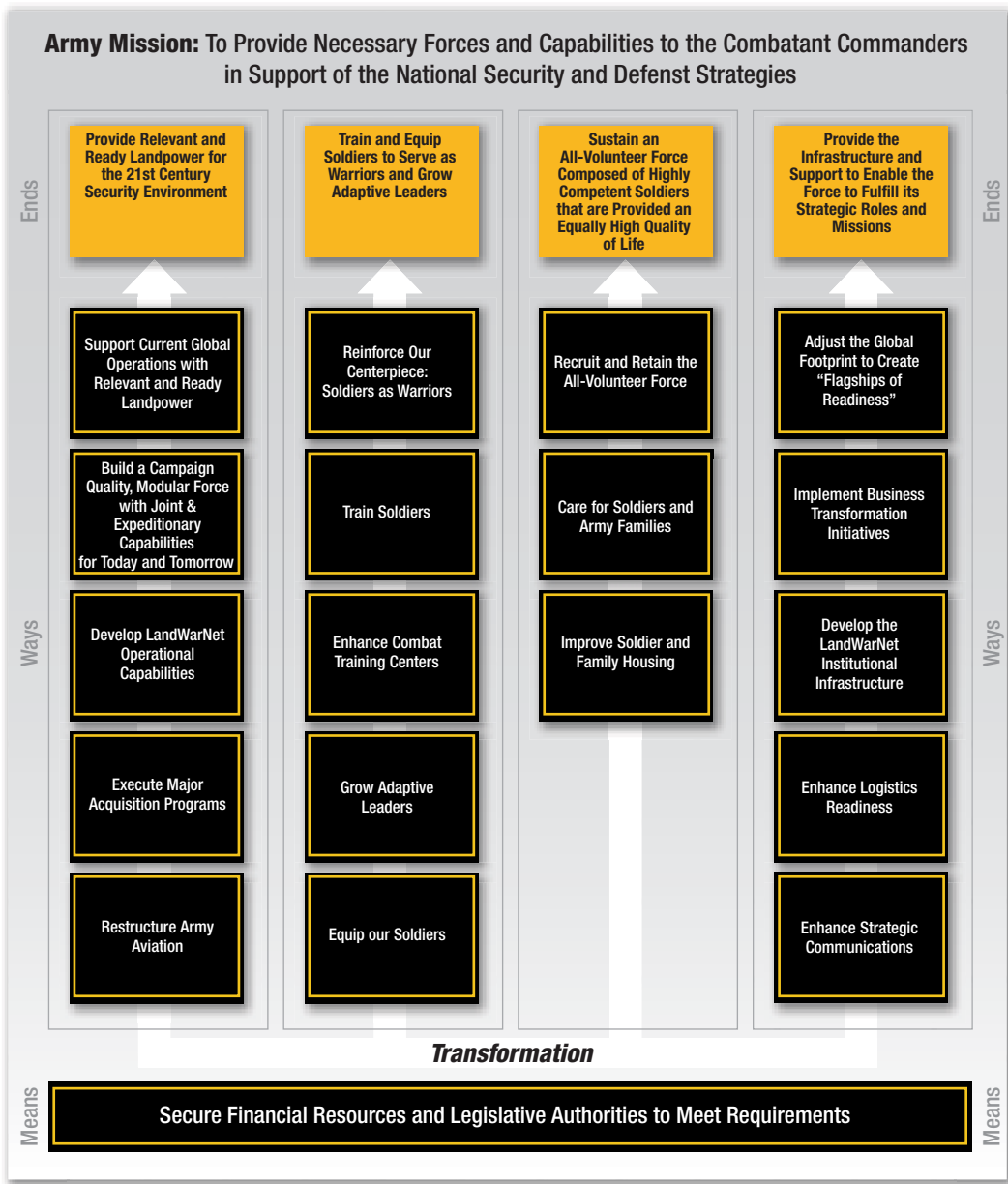
The Army Strategy Map has continued to evolve since our GPRA plan was written in February 2005; some initiatives were removed while new ones were added. Army programs are aligned to the current 19 initiatives. The following section discusses FY 2006 Army strategy, goals and program performance results.

Strategic initiatives are guiding the Army through the transformation of the operational force and the streamlining of business processes. Most of these initiatives have mature and actionable performance measures; current results are presented below. The Army is working to ensure that it has effective performance measures for all current strategic initiatives.



Figure 3. Army Strategy Map

### Army Vision: Relevant and Ready Landpower in Service to the Nation







Army Strategy

**Provide Relevant and Ready Land Power for the 21st Century Security Environment**

The initiatives which support this first overarching strategy are interrelated and include:

- Support current global operations with relevant and ready land power;
- Build a campaign-quality modular force with joint and expeditionary capabilities for today and tomorrow;
- Develop LandWarNet operational capabilities;
- Execute major acquisition programs; and
- Restructure Army aviation.

The Army is simultaneously fighting today’s battles and remolding the operational force into smaller, self-sufficient tactical units (the modular force). As part of the process, the Army is rebalancing critical skill sets to ensure that all units have the knowledge and capabilities required to succeed on the battlefield. Through LandWarNet, tactical units will attain improved situational awareness via voice, video and data transmissions that are pushed to the individual Soldier. In addition, these units will be equipped with Future Combat Systems technology to improve lethality and survivability. The Army also is modernizing its air capabilities to reduce maintenance, increase survivability and improve readiness.

***Support Current Global Operations with Relevant and Ready Land Power***

The pace of operations in the new security environment presents a number of significant force management challenges to the Army. Of the approximately 580,000 Soldiers presently serving on active duty – 505,000 in the active component and 75,000 mobilized ARNG and USAR Soldiers – about 160,000 are deployed to support operations in Iraq, Afghanistan and other theaters (85,000 active component, 45,000 ARNG and 30,000 USAR).

Repeated deployments affect recruiting and retention, and they have a very real impact on our ability to care for our Soldiers and their families. To meet today’s challenges and to better position troops for the future, the Army is pursuing numerous initiatives that will reduce force management risk. By developing the Army Modular Force, we will significantly increase the pool of rotating units. By employing the Army Force Generation Model (ARFORGEN), we will reduce the stress on the force. The results will be greater stability, unit cohesion and readiness, and less uncertainty for families.

### ***Build a Campaign-Quality Modular Force with Joint and Expeditionary Capabilities for Today and Tomorrow***

To maximize force effectiveness and strategic flexibility, the Army is reorganizing to a modular, brigade-based structure that will:

- (1) Increase the number of BCTs available to meet operational commitments while maintaining combat effectiveness that is equal to or better than that of the previous division-based force;
- (2) Create brigade-based combat and support formations with common organizational designs that can be easily tailored to meet the varied demands of the geographic combatant commanders, thereby reducing joint planning and execution complexities;
- (3) Redesign organizations to perform as integral parts of the Joint Force, making them more effective across the range of military operations and enhancing their ability to contribute to joint, interagency and multinational efforts.

The re-organized BCTs consist of 3,500 to 4,000 Soldiers and are organized and trained the way they will fight. The BCTs are more robust, require less augmentation, and are standardized in design, which increases interoperability and eases planning and logistical support requirements. These new modular formations also operate effectively in joint, interagency and multinational environments, and enhance joint concepts for battle command, fires, logistics, force projection, intelligence, and air and missile defense. BCTs will be able to take full advantage of expanding joint training opportunities.

To man the brigade-based modular force, the Army intends to increase its operational end-strength. Congress has authorized the Army to add 30,000 Soldiers to the active component (AC), for a total of 512,400.

As the Army creates modular capabilities, it also is realigning the active and reserve components. A different equilibrium between the two components is needed to create a depth of forces that can support sustained operations while providing predictability for Soldiers and families. Reality dictates that the reserve component (RC) cease to be a strategic reserve and instead be integrated as an operational reserve. Restructuring initiatives also will address low density/high demand capabilities and the redistribution of uniformed personnel from the institutional force to the operating force.

Additionally, the Army is rebalancing unit capabilities and critical skill sets to ensure consistency with organizational restructuring, to relieve stress on low density/high demand units, and to improve unit readiness and deployability. The current AC/RC rebalancing program includes 73,000 skill set changes and elimination of 43,000 RC spaces that represent excess structure. By the end of FY 2006, the Army had redistributed 39,000 slots and eliminated 18,000.

The ARFORGEN process leverages modular unit designs and operational cycles to create a sustained deployment posture of operationally ready units in predictable patterns while retaining the capacity to surge combat power for major operations. The process enables commanders to identify deployment windows and manage readiness and training of forces accordingly. As the Army grows from 48 to 70 BCTs, the ARFORGEN will lengthen Soldiers' time at home station between deployments.

By the end of FY 2006, the active component had transformed 31 of the 42 programmed BCTs to a modular design. A transformed BCT is defined as a unit that has reorganized and is manned, trained and equipped within resource constraints. An additional four brigades began the transformation process in FY 2006. It can take up to 12 months for active-component heavy and infantry brigades to complete the transition, and as long as 24 months for Stryker brigades.

The ARNG began transforming in FY 2005 with an accelerated plan that allows early reorganization, manning and training under the new BCT design. Transformation for an ARNG BCT can take as long as 48 months. By the

end of FY 2009, the ARNG will have completed seven BCTs, and another nine will be finished by FY 2010. The overall transformation plan is on track to achieve a combined total of 70 BCTs, 42 in the active component and 28 in the ARNG, by FY 2013. Table 1 provides a summary of BCT transformation.

Table 1. BCT Transformation Summary

	FY 2004	FY 2005	FY 2006
AC Transformed	2	18	31
ARNG Transformed	0	0	0
<b>Total Transformed*</b>	<b>2</b>	<b>18</b>	<b>31</b>
AC Transforming	11	8	4
ARNG Transforming	0	7	16
<b>Total Transforming**</b>	<b>11</b>	<b>15</b>	<b>20</b>
<b>Total Transformation</b>	<b>13</b>	<b>33</b>	<b>51</b>

\*Transformed means the unit has completed its initial reorganization and re-equipping to a modular design within resource constraints, is participating in the ARFORGEN process, and may be used against a requirement.

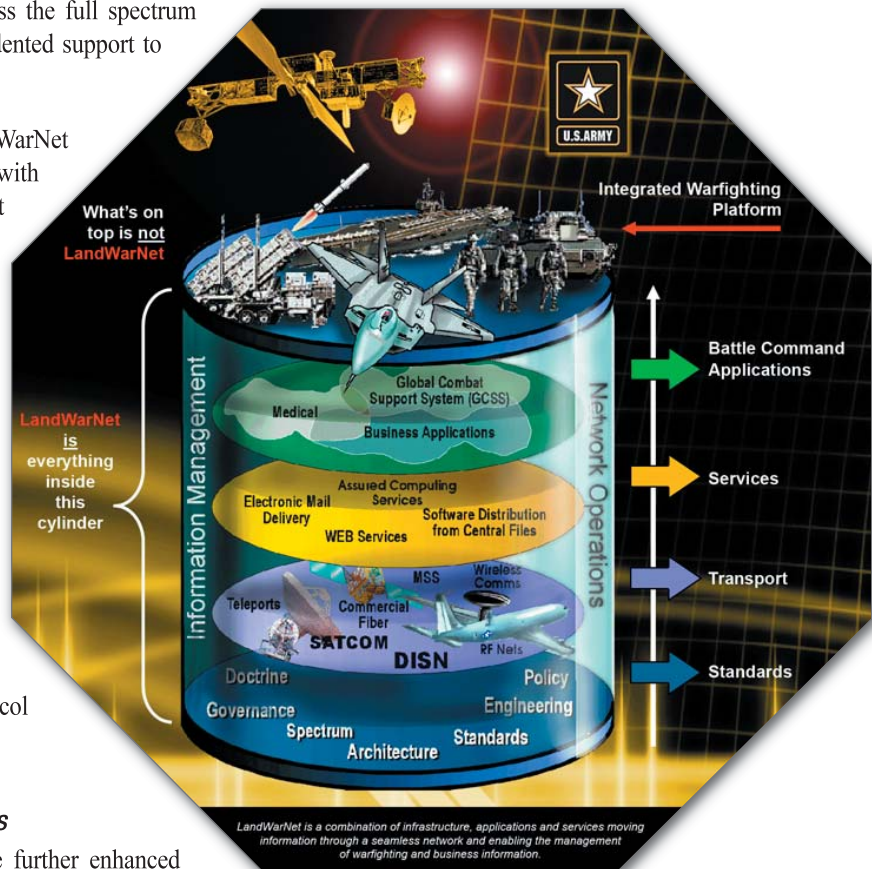
\*\* Transforming means the unit is still undergoing initial reorganization and re-equipping to a modular design within resource constraints.

**Develop LandWarNet Operational Capabilities**

LandWarNet (Figure 4) is a combination of infrastructure and services that extends voice, video and data transmissions to the edges of tactical formations. The goal is to push these capabilities deeper and deeper into the modular Army force – to brigades, battalions, companies and individual Soldiers. The result will be improved operational cycle times, unprecedented levels of flexibility and agility for logistical support, and wider availability of actionable intelligence and situational awareness. LandWarNet’s benefits will echo across the full spectrum of conflict, including lending unprecedented support to natural disaster response.

In FY 2006, within the operational LandWarNet initiative, the Army equipped divisions with a state-of-the-art satellite and Internet Protocol (IP) communications system, down to the maneuver battalion level. The Army also implemented Teleport Generation 1 capabilities; achieved Everything over Internet Protocol (EOIP) implementation in Joint Special Operations Command; equipped seven active divisions with EOIP as well as RC units deploying to Operation Enduring Freedom (OEF) and Operation Iraqi Freedom (OIF); and implemented Active Directory on 99 percent of the Army’s portion of the Non-Classified Internet Protocol Router Network.

Figure 4. LandWarNet



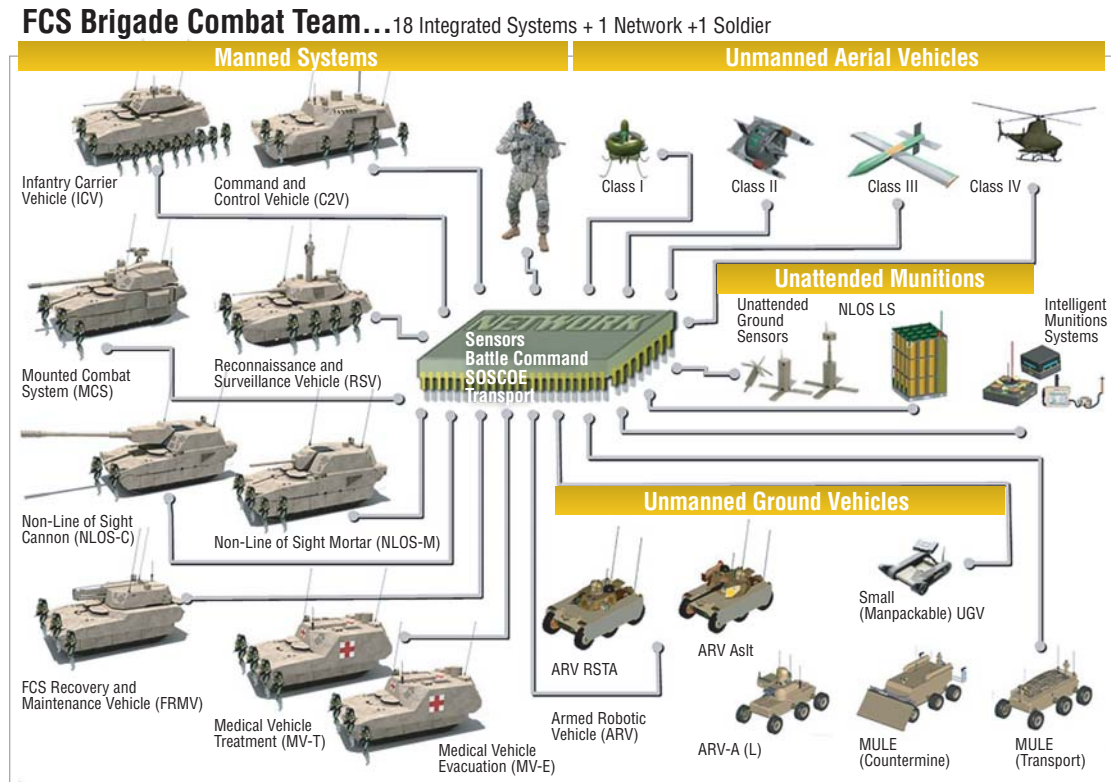
**Execute Major Acquisition Programs**

The Army’s overall capability will be further enhanced through a strong Future Combat Systems (FCS) program. FCS is the key modernization program for the Army. When fielded, the FCS-equipped BCT will represent the first full modernization of our ground forces in more than four decades. In the interim, the FCS program is developing and fielding spin-off technologies to current forces. Simply put, the FCS program is the fastest and surest way to modernize the Army.

The FCS BCT (Figure 5) consists of a family of integrated manned and unmanned systems that provide mobile, networked command and control capabilities, autonomous robotic systems, precision direct and indirect

fires, organic sensor capabilities, and adverse-weather reconnaissance, surveillance, targeting and acquisition. In FY 2006, the Army met developmental milestones for the FCS program on schedule and within budgeted costs.

Figure 5. Future Combat Systems



As of September 1, 2006

### Restructure Army Aviation

The Army continues to transform its aviation structure to develop modular, capabilities-based forces that are optimized to operate in a joint and expeditionary environment. Over the next six years the Army plans to procure more than 1,000 new rotary and fixed-wing aircraft, using funds made available through termination of the Comanche program. The Army also will modernize aircraft sensors, execute safety and reliability modifications, and add aircraft survivability equipment. This effort will reduce maintenance costs, increase survivability and improve readiness rates. Key components of the aviation modernization plan include accelerating modernization of reserve component aviation and unmanned aerial vehicle programs, as well as pushing forward the development of a common cockpit for cargo and utility aircraft.

Table 2. Restructuring Army Aviation

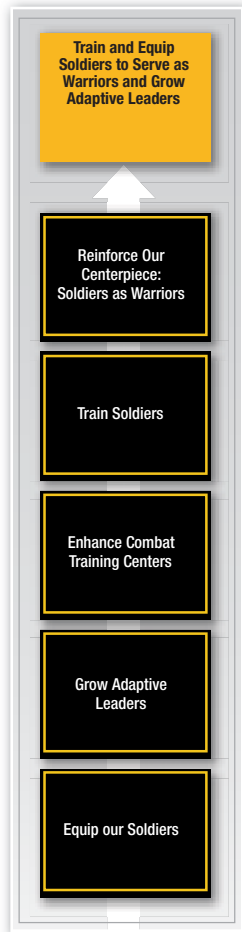
	FY 2005 Delivered	FY 2006 Goals	FY 2006 Delivered
# of Aircraft Reset (Mix of OEF/OIF Returning Aircraft)	626	506	547
MH-47G Produced	12	13	16
UH-60 Recapitalization	26	26	25
CH-47 Recapitalization	2	6	2
AH-64 Recapitalization	152	144	144
Combat Aviation Brigades (CAB) All Components	2	5	11



A soldier awaits UH-60 Black Hawk helicopters to extract his Soldiers after an early morning raid on Baji Island, Iraq.







Army Strategy

**Train and Equip Soldiers to Serve as Warriors and Grow Adaptive Leaders**

The five initiatives in this overarching strategy include:

- Reinforce our centerpiece – Soldiers as warriors;
- Train Soldiers;
- Enhance the combat training centers;
- Grow adaptive leaders; and
- Equip our Soldiers.

***Reinforce Our Centerpiece: Soldiers as Warriors***

Soldiers are the centerpiece of our Army. No matter how much the tools of warfare improve, it is the Soldier who must accomplish the mission. The Soldier remains the ultimate combination of sensor and shooter.

Mental and physical toughness underpin the beliefs embraced in the Soldier’s Creed and must be developed within all Soldiers — without regard to their specialty, their unit or their location on the battlefield. Last year, the Army implemented the additional rigor mandated by the Chief of Staff’s Warrior Ethos concept. The new program of instruction in basic combat increases the Soldier’s warfighting capability through enhanced training on individual tasks and battle drills. The Army continues to modify these tasks and drills to ensure that training is relevant to today’s combat environment. The Army also is proceeding with the officer education system started in FY 2005, known as the Basic Officer Leader Course II. This program focuses on critical warrior tasks for all newly commissioned officers. The Intermediate Level Education program replaced the Command and General Staff Officer Course, expanding the Army’s ability to educate 100 percent of its mid-grade officers, with a focus on their specific career paths.

***Train Soldiers***

In FY 2006, the Army provided trained and ready forces to support commanders around the globe as well as critical homeland defense missions. To make sure Soldiers were combat-ready in FY 2006, the Army provided an appropriate mix of live, virtual and constructive training. The active and reserve components fully executed their ground and air training plans (Table 3), which included actual miles driven and hours flown, as well as virtual miles associated with the use of simulators.

Table 3. Ground and Air OPTEMPO (Active)

	FY 2002	FY 2003	FY 2004	FY 2005	FY 2006 Goal	FY 2006 Actual
Ground OPTEMPO (Mileage)	944	1,071	1,512	991	899	1,058
Air OPTEMPO (Flight Hours)	13.1	15.1	17.4	18.4	13.1	21.6

NOTE: Actual FY 2006 amounts are estimates based on execution through August 2006. Actual execution includes total execution (Home Station and Contingency Operations) as reported by Army units using Standard Army Management Information Systems.

**Enhance Combat Training Centers**

The Combat Training Centers (CTC) provide realistic joint and combined-arms training that approximates actual combat, according to Army and Joint doctrine. The CTCs are at the core of the Army’s collective training strategy and have dedicated resources beyond those available at home-station training sites. The CTCs have drastically changed their training approach to better prepare Soldiers for the demands of operations in Iraq and Afghanistan, using improved facilities, civilians on the battlefield and realistic scenarios. Training is specifically tailored to prepare units for the conditions in the combat zones to which they will deploy. While the CTCs have retained the capability to return to the high-intensity unit training needed for other potential theaters of war and the new modular brigades, the current focus has shifted to counter-insurgency operations and lessons from combat in Iraq and Afghanistan. The training environment emphasizes rapid change and adaptation to current activities. The complex, event-driven scenarios challenge the BCT to execute multiple, simultaneous missions that include integrated enablers from the Army and the Joint community.

**Grow Adaptive Leaders**

The contemporary operational environment has proven that our military leaders must possess skills beyond those of pure tactical war fighting. They must become pentathletes: strong multi-skilled leaders who are able to transition between complex tasks with relative ease, to think strategically and creatively, and to build teams. They must be able to negotiate, be culturally astute, have basic foreign language abilities and be capable of conducting information and stability and reconstruction operations. The Army is committed to:

- Incorporating cultural awareness training and education into all levels of professional military education;
- Developing expertise in counterinsurgency operations among Soldiers and leaders from the tactical to strategic level; and
- Encouraging language and cultural training and education throughout the Army – in schools, on line, through self-development and at the CTCs.

Table 4. Number of NCO's and Officers trained in leadership courses in FY 2006

	Warrior Leader Course	Basic NCO Course	Advanced NCO Course	Sergeant's Major Academy	Intermediate Level Education	Senior Service College
2006 Trained	42,275	44,220	14,801	1,307	872	1,541

Our leaders, both military and civilian, also must be effective in managing, leading and changing large organizations. They need to be skilled in governance, statesmanship and diplomacy. They must be confident and

competent decision makers, who are prudent risk takers, innovative, adaptive and accountable. They must be empathetic and positive. And, as always, our leaders must set the standard for integrity and character.

The Army is keenly aware of the valuable contributions of our civilians in supporting the National Military Strategy. The Civilian Leader Development mission is to "...ensure the Army provides training, education and operational experiences to develop leader competencies and enhance capabilities of Army civilians in support of Soldiers, the Army, and the nation." To accomplish this, a new training and educating paradigm is required. As a result, the Civilian Leader Development Program is being revamped into a training and education system – the Civilian Education System (CES) – that is similar to the military leader development system. The CES will focus on areas derived from the Office of Personnel Management leadership competencies and competencies identified by the Center for Army Leadership. CES, which will be implemented in January 2007, will provide leader development training and education that support civilian leaders’ career path requirements. The Army also is committed to promoting lifelong learning and self-development.

***Equip Our Soldiers***

Our Soldiers rely on and deserve the very best force protection and mission-essential equipment we can provide. And they play a large role in setting Army requirements. In 2002, Soldiers alerted the institutional Army to the pressing need for different systems and materiel more suited to the GWOT areas of operation, such as desert and mountain terrain and climate, urban street fighting and sniper fire. Soldiers can also take credit for identifying requirements for new forms of protection, lighter-weight gear and methods to carry large supplies of ammunition.

The Rapid Fielding Initiative (RFI) was developed to enhance soldier warfighting capabilities by using commercial-off-the-shelf technology, rather than waiting for acquisition programs, to address Soldier requirements and shortfalls. To date, more than 750,000 Soldiers – including approximately 350,000 in 2006 – have benefited from the enhancements provided by RFI equipment. The Army will field RFI items to the remainder of the operating force by the end of September 2007, for a total of more than one million Soldiers.



Army recruits assume defensive positions en route to a live-fire exercise during basic combat training at Fort Jackson, S.C.





Army Strategy

**Sustain an All-Volunteer Force Composed of Highly Competent Soldiers That Are Provided an Equally High Quality of Life**

The initiatives in this overarching strategy include:

- Recruit and retain the all-volunteer force;
- Care for Soldiers and Army families; and
- Improve Soldier and family housing.

***Recruit and Retain the All-Volunteer Force***

While the recruiting environment is challenging, the Army will continue to recruit highly qualified Soldiers. Our goal was for high school diploma graduates (HSDGs) to comprise no less than 90 percent of recruits. Typically, high school graduates are at lower risk for attrition and, therefore, are the most desirable group from which to draw. Although we achieved only 81 percent HSDGs, first-term attrition is declining and training base attrition is at an historic low – both positive signs that we are recruiting, training and retaining a highly qualified force (Table 5).

Table 5. Recruiting Quality – Percent High School Diploma Graduates (HSDG)

	FY 2003	FY 2004	FY 2005	FY 2006
HSDG Goal	90	90	90	90
HSDG Actual	94	92	87	81

The Army has continued to aggressively reshape recruiting resources for all components in order to address our recruiting challenges. The FY 2006 budget provided more than \$1.5 billion for recruiting programs. We thus were able to increase the number of recruiters. We also raised the maximum enlistment bonus from \$20,000 to \$40,000 for active component Soldiers, and from \$10,000 to \$20,000 for reserve component recruits. The Army College Fund incentive was increased to \$72,900 for qualified active component applicants. Additionally, we created new initiatives, to include the Recruiter Incentive Pay and Referral Bonus. However, the recruiting environment has not improved, and FY 2007 will require the same (or higher) level of resources and support as FY 2006.

Table 6. Recruiting

	FY 2003 Actual	FY 2004 Actual	FY 2005 Actual	FY 2006 Goal	FY 2006 Actual
Active Army	74,132	77,587	73,373	80,000	80,635
Army Reserve	27,365	21,292	19,400	25,500	25,378
Army National Guard	54,202	49,210	50,219	70,000	69,042

Due to the GWOT, several special skills are in high demand. To fill them, it has been necessary to augment our recruiting and retention



Table 7. Active Component End-Strength Within 2%

	FY 2003	FY 2004	FY 2005	FY 2006
Goal	480,000	482,400	502,400	502,400
Congressional Baseline	N/A	N/A	512,400	512,400
Actual	499,301	499,543	492,728	505,402
% Delta	+4.0%	+3.6%	-2.0%	+0.6%

Performance Measure: The number of Soldiers on active duty at the end of the year.

Table 8. Selected Reserve (USAR and ARNG) End-Strength Within 2%

	FY 2003	FY 2004	FY 2005	FY 2006
Goal	555,000	555,000	555,000	555,000
Actual	562,981	547,049	522,182	536,263
% Delta	+1.4%	-1.4%	-5.9%	-3.4%

Performance Measure: The number of Soldiers in the USAR and ARNG at the end of the year.

Table 9. Active and Reserve Component Retention

	FY 2003 Actual	FY 2004 Actual	FY 2005 Actual	FY 2006 Goal	FY 2006 Actual
Active Army	54,151	60,010	69,512	64,000	67,307
Army Reserve	13,749	16,330	16,485	17,712	18,223
Army National Guard	52,832	47,012	33,804	34,875	41,083

Performance Measure: Measures the number of Soldiers reenlisted during a given FY against the published goals.

incentives. For example, to retain quality Special Forces Soldiers, the Army instituted a bonus program that pays up to \$150,000 for senior non-commissioned officers to remain in the service. Also, in order to retain retirement-eligible Special Forces Soldiers who have more than 25 years of service, the Army is developing an Assignment Incentive Pay program.

Beyond Special Forces, the Army has boosted reenlistment bonuses to a maximum of \$40,000 for those not in high-demand specialties. These programs alone are not enough, however. They must be matched with a commensurate commitment to Soldiers' families and provide an excellent quality of life.

Recruiting Soldiers who are confident, adaptive, competent and able to handle the full complexity of 21st century warfare in this combined, joint, expeditionary environment is highly competitive and will continue to be very challenging. We will continue to develop and implement programs to address those challenges.



A Soldier with his sniffer dog during Operation Mendota in Mosul, Iraq.

### ***Care for Soldiers and Army Families***

To retain our Soldiers and meet the needs of their families, we need to care for them with exceptional well-being programs. The Army is committed to attaining a quality-of-life for our people that matches the quality of their service. To better fulfill this promise during war, we have initiated programs to improve spouse employment, to ease the transition of high school students during moves and to extend in-state college tuition rates to military families. We continue to improve healthcare, childcare, youth programs, schools and facilities for our families. The Army also is concerned about our Soldiers' financial health and in FY 2006 completed a multiyear initiative to eliminate Soldiers' out-of-pocket housing expenses.

To improve unit cohesion and readiness, while reducing unit turbulence and uncertainty for families, the Army is changing how we man our units. Under Force Stabilization, the Army plans to keep Soldiers in each assignment longer and will synchronize their assignments to BCT rotational schedules. Stabilization will create more deployable, combat-capable units while improving predictability and quality of life for Soldiers and their families. Soldiers and their families will be able to build deeper roots in their communities and enjoy better opportunities for spouse employment, continuity of healthcare and schooling, and access to stronger support networks that enhance well-being

### ***Improve Soldier and Family Housing***

Housing programs are essential to demonstrating our concern for Soldiers and their families. In concert with the private sector, the Army continues to focus considerable effort on the Residential Communities Initiative and the Barracks Modernization Program. Congressional support for these initiatives has had a dramatic effect on improving the quality of life for our Soldiers and their families.

Our housing programs are on track to eliminate inadequate dependent housing in the United States by FY 2007 and worldwide by FY 2008, through privatization, construction and divestiture of units. In FY 2006, we privatized 12,000, bringing the total to 71,500. The Army also modernized 5,600 barracks spaces.







Army Strategy

**Provide the Infrastructure and Support to Enable the Force to Fulfill its Strategic Roles and Missions**

The initiatives in this overarching strategy include:

- Adjusting the global footprint to create “Flagships of Readiness”;
- Implementing business transformation initiatives;
- Developing LandWarNet institutional infrastructure;
- Enhancing logistics readiness; and
- Enhancing strategic communications.

***Adjust Global Footprint to Create “Flagships of Readiness”***

Collectively, our installations are an essential component in maintaining our Army. They are the platforms from which we rapidly mobilize and deploy military power. They play a vital role in training the force and in reconstituting it upon return from deployment. They also serve as a sophisticated reach-back capability for the deployed commander seeking information and other support. Equally important, installations sustain our military families.

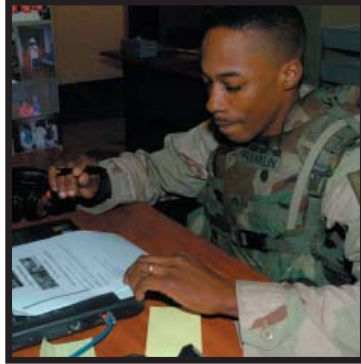
As part of the Army’s plan to create installation “Flagships of Readiness”, two rail infrastructure projects were scheduled for FY 2006. One was completed, and the other will be funded and finished in FY 2007. Five installation projects expanded shipping centers, built pallet processing facilities and upgraded equipment warehousing, which factors into force readiness. Since FY 2005, the Army also has completed six aerial port of embarkation (APOE) infrastructure improvement projects. A seventh, at Peterson Air Force Base, which serves Fort Carson, Colorado, will be finished in FY 2007. Upgrades to seaports and ammunition igloos were underfunded in FY 2006, however; as a result, the Army completed only 75 percent of those projects.

As we focus on the demands of current operations, Army installations continue to face many challenges. Our new modular brigades require new facilities. The Army will incur substantial infrastructure changes and requirements as global repositioning and Base Realignment and Closure proceed. As we proceed, the Army must ensure that it maintains strategic responsiveness and a healthy and pleasant environment for its Soldiers and their families.

***Implement Business Transformation Initiatives***

Transformation of our business processes promotes the long-term health of the Army, while freeing human and financial resources that can be used to meet warfighting requirements and reduce risk across the force. The Army is developing a culture of continuous





### Implementing the President's Management Agenda

The Army is achieving management improvement results through the implementation of the five government-wide initiatives of the President's Management Agenda (PMA). In all five areas, the Army is showing sustained progress and improved results.

- Strategic Management of Human Capital – We continued to deploy National Security Personnel System (NSPS), linked Senior Executive Service (SES) performance plans to strategic plans, and reduced hiring time for new SES to 30 days and non-SES to 45 days.
- Competitive Sourcing – Publicly announced competitions total 1,634 for FY 2006, with 4,945 positions projected for public announcement by the end of FY 2007 under the A-76 process.
- Improvement of Financial Management – DoD began reporting financial management progress against the Financial Improvement Audit Readiness (FIAR) Plan that measures all services against five initiatives.
- Budget Performance Integration Initiative – The Army developed performance measures for all 148 of its major programs, which equal 100 percent of the budget.
- eGovernment – We attained satisfactory information technology business plans (OMB Exhibit 300 forms) for all of major IT systems and met Federal Information Security Management Act (FISMA) requirements.

improvement that will provide dividends now and into the future. Toward that end, the Army has embarked on an ambitious Lean Six Sigma (LSS) campaign to improve its processes service-wide. LSS is a business improvement methodology that maximizes value by achieving the fastest rate of improvement in customer satisfaction, cost, quality, process, speed and invested capital. LSS, in combination with organizational analysis and design and the effective and efficient application of enterprise solutions and knowledge-based situational awareness, will spread business transformation throughout the Army.

The Army currently is pursuing process improvement initiatives in numerous institutional areas, including the requirements determination process, the resource allocation process and recruiting. Among them is the General Fund Enterprise Business System (GFEBS). GFEBS is an integrated financial management system that will provide web-based, online, real-time transaction and information capability accessible to all Army and Defense Department components. GFEBS will fulfill the requirements of the Federal Financial Management Improvement Act of 1996 and enable the Army to comply with the Chief Financial Officers Act of 1990 by improving performance, standardizing processes, reducing legacy stove-piped systems and providing all levels of leadership with reliable, relevant and timely financial information. Release 1.1 was completed in FY 2006 and the program executed a successful technology demonstration at Ft. Jackson, SC.

### *Develop the LandWarNet Institutional Infrastructure*

The institutional Army, the Army's business platform, must transform if it is to achieve joint, standardized data collection processes, effective communication linkages and efficient information sharing among stakeholders. The Army intends to

increase responsiveness to combatant commanders by applying information management concepts and information technologies (IT), and implementing sound IT investment governance. This includes the establishment of a net-centric architectural framework and technical standards, the use of IT portfolio management to maximize Army and

Joint capabilities, and delivery of core enterprise services to support the Army's functional needs. In FY 2006, the Army improved IT infrastructure at 34 installations; established the Net-Centric Data Strategy Center of Excellence; established mission areas and domains to govern IT investments and developed transformation plans to implement Army IT portfolio management; and delivered an integrated interoperable publish-and-subscribe methodology for tactical command and control functional applications.

### ***Enhance Logistics Readiness***

The critical task for Army logistics is to effectively sustain the combat readiness of deployed forces and to maintain the materiel readiness of the current force. This requires a fundamental shift from supply-based to distribution-based logistics and conversion to modular support structures.

In order to implement better business practices across the logistics spectrum, the Army will continue to provide support for the Enterprise Resource Planning (ERP) components of the Single Army Logistics Enterprise, including:

- Global Combat Service Support – Army (GCSS-A) for tactical level logistics;
- The Logistics Modernization Program (LMP) for wholesale logistics; and
- Seamless integration into Product Life Cycle Management Plus (PLM+)

Together, these initiatives will put our logistics management practices in-line with world-class businesses and give us the tools we need to better manage the resources Americans have given us.

### **Conclusion**

Our challenge in the years ahead is to establish a balance between current readiness and future investments, while keeping risk at moderate levels as we support our global commitments and prepare for future challenges. In the near term, we plan to minimize our future risks by rolling higher-payoff technologies into the current force when they become available.

We must continue to transform our institutional processes to generate resources required by the operational Army. This includes improving management and business processes, implementing financial improvement initiatives, modernizing our installations and ensuring a quality of life that makes service attractive.

Everything we do is tied to enabling Soldiers to continue to fight and win our nation's wars. We must provide the Soldier the equipment to fight and win. We must care for both our Soldiers and their families. We owe our Soldiers the best of everything, and the financial management community will remain dedicated to serving them as they serve the United States.



**Appendix to Performance Goals, Objectives, and Results**

The OSD Management Initiative Decision (MID) 901 (dated 20 December 2002) directs the components, including the Army, to ensure that their individual performance plans and balanced scorecards:

- Reflect the balanced scorecard quadrants associated with the risk management framework;
- Reflect the performance objectives established under the Department’s balanced scorecard for the QDR risk management framework; and
- Align with and support the outcomes and supporting performance metrics of its next higher organization.

**Figure 6. Alignment of Army Strategy and Initiatives to DoD Risk Management Framework**

Army Strategic Initiative	OSD Risk Management Quadrant	OSD Goal
<b>Army Strategy: Provide Relevant and Ready Landpower for the 21st Century Security Environment</b>		
Support Current Global Operations with Relevant and Ready Land Power	Operational Risk	Do We Have The Right Forces Available
Build a Campaign-Quality Modular Force with Joint and Expeditionary Capabilities for Today and Tomorrow	Future Challenges Risk	Develop More Effective Organizations
Develop LandWarNet Operational Capabilities	Future Challenges Risk	Drive Innovative Joint Operations
Execute Major Acquisition Programs	Institutional Risk	Streamline Decision Processes. Drive Financial Management and Acquisition Excellence
Restructure Army Aviation	Future Challenges Risk	Define and Develop Transformational Capabilities
<b>Army Strategy: Train and Equip Soldiers to Serve as Warriors and Grow Adaptive Leaders</b>		
Reinforce Our Centerpiece: Soldiers as Warriors	Force Management Risk	Maintain a Quality Workforce
Train Soldiers	Operational Risk	Are They Currently Ready
Enhance the Combat Training Centers	Operational Risk	Are They Currently Ready
Grow Adaptive Leaders	Force Management Risk	Shape the Force of the Future
Equip our Soldiers	Institutional Risk	Streamline Decision Processes. Drive Financial Management and Acquisition Excellence
<b>Army Strategy: Sustain an All-Volunteer Force Composed of Highly Competent Soldiers that are Provided an Equally High Quality of Life</b>		
Recruit and Retain the All-Volunteer Force	Force Management Risk	Maintain a Quality Workforce
Care for Soldiers and Army families	Institutional Risk	Realign Support to the Warfighter
Improve Soldier and Family Housing	Institutional Risk	Improve the Readiness and Quality of Key Facilities
<b>Army Strategy: Provide the Infrastructure and Support to Enable the Force to Fulfill its Strategic Roles and Missions</b>		
Adjust the Global Footprint to Create “Flagships of Readiness”	Institutional Risk	Improve the Readiness and Quality of Key Facilities
Implement Business Transformation Initiatives	Institutional Risk	Manage Overhead / Indirect Cost
Develop LandWarNet Institutional Infrastructure	Future Challenges Risk	Define and Develop Transformational Capabilities
Enhance Logistics Readiness	Future Challenges Risk	Define and Develop Transformational Capabilities
Enhance Strategic Communications	Future Challenges Risk	Drive Innovative Joint Operations
<b>All Army Strategies</b>		
Secure Financial Resources and Legislative Authorities To Meet Requirements	Institutional Risk	Streamline Decision Processes. Drive Financial Management and Acquisition Excellence

### Analysis of Financial Statements and Stewardship Information

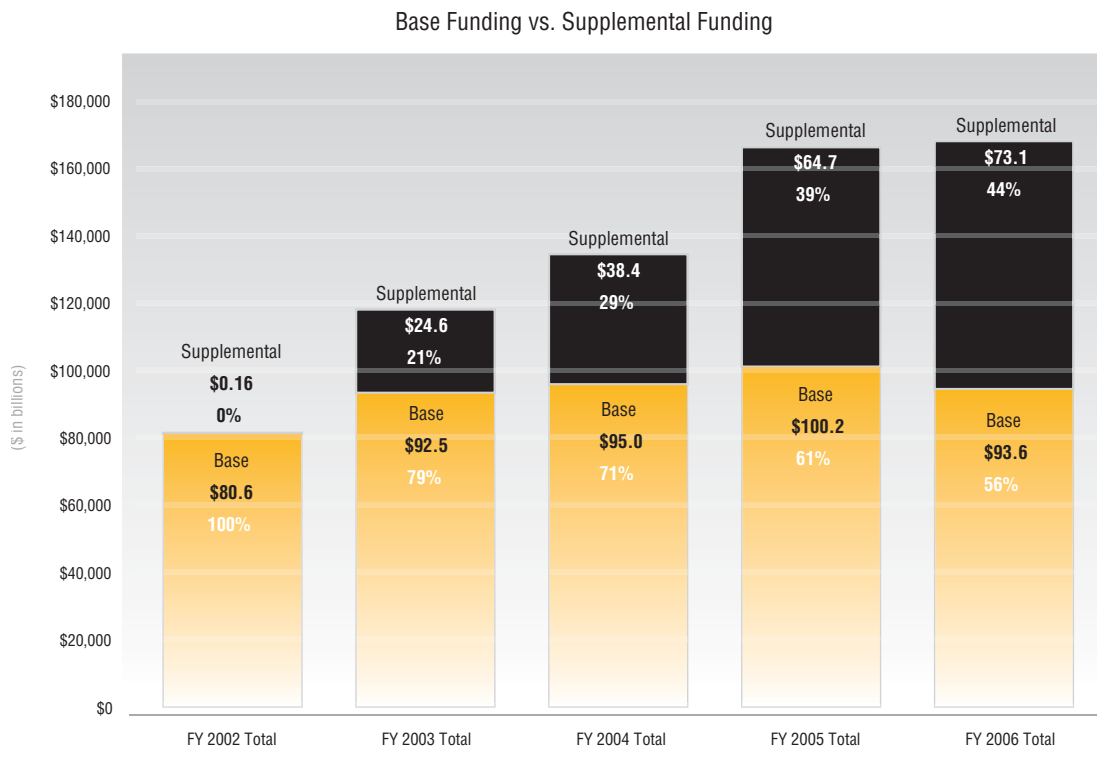
As discussed in the accompanying independent auditor’s report, longstanding financial management challenges prevent the Army from producing auditable financial statements for the Army General Fund and Army Working Capital Fund. The Army continues to work with the Department of Defense (DoD) to develop sustainable business practices and enhanced internal controls that will improve financial management processes and produce quality financial management information. These processes must be supported by compliant business systems and an effective set of management controls.

In October 2005, the Deputy Secretary of Defense established the Defense Business Transformation Agency (BTA) to ensure consistency, consolidation and coordination of DoD enterprise-level business systems; and to reduce redundancies in business systems and overhead costs. The BTA’s mission is to transform business operations in order to augment warfighter support while enabling financial accountability and improving investment governance across DoD. The Army has been a leader within DoD in embracing BTA guidance, both in terms of adopting business practices that conform to the Business Enterprise Architecture (BEA) and providing feedback as to their efficacy. The Army’s core financial management modernization program, GFEBS, adopted early BEA-initiated data standardization initiatives, such as the Standard Financial Information Structure and Real Property Inventory Requirements.

### General Fund Financial Results

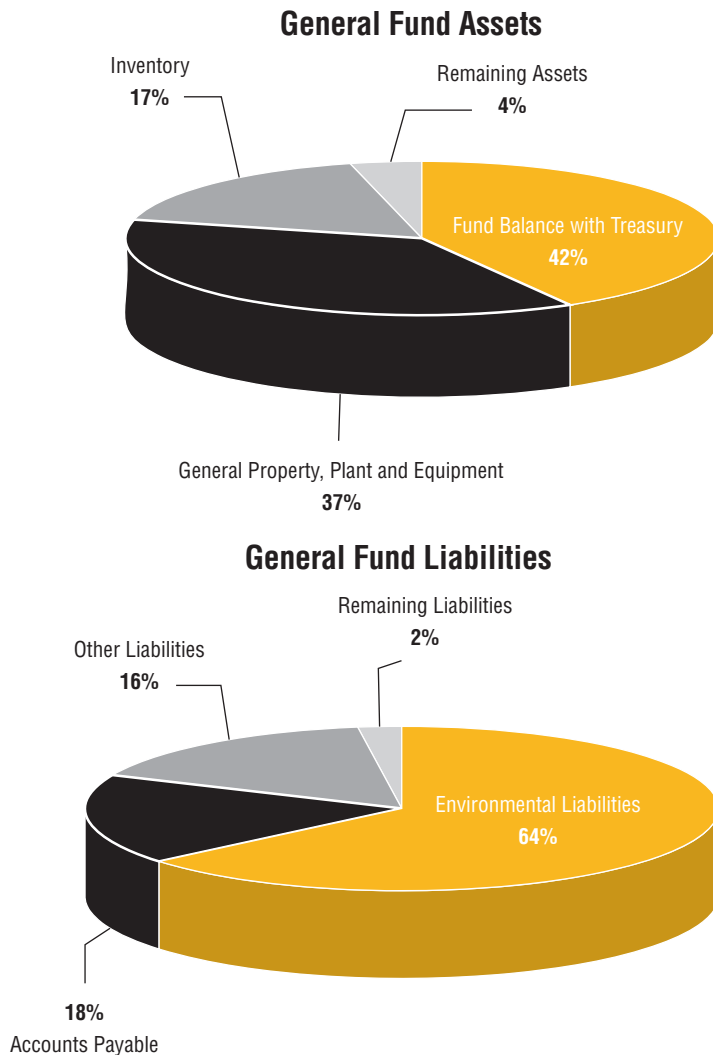
Supplemental appropriations continue to be essential to the Army’s ability to execute its mission. Supplemental funding accounted for 39 percent of the Army’s \$164.9 billion in total obligation authority in FY 2005. In FY 2006, supplemental funding accounted for 44 percent of the \$166.7 billion in total obligation authority.

Figure 7. Total Funding



*Amounts shown represent funding as received on Department of the Treasury warrants and do not include additions or subtractions resulting from reprogramming and Standard Form (SF) 1151 Non-expenditure Transfer Authorizations.*

Figure 8. Composition of General Fund Assets and Liabilities



**General Fund Balance Sheet**

The Army General Fund balance sheet includes total assets that exceed \$226 billion. Two asset categories – Fund Balance with Treasury and General Property, Plant and Equipment (GPP&E) – make up 79 percent of total assets, with values of \$94.6 billion and \$84.2 billion, respectively.

Liabilities primarily consist of \$45 billion in Environmental Liabilities and \$12.5 billion in Accounts Payable.

Fund Balance with Treasury grew by \$7.5 billion in FY 2006 due to an increase in the DoD appropriations received to ensure that resources, equipment and supplies remain available without interruption in support of OIF and OEF. GPP&E increased \$6.6 billion due to the change in valuation method for military equipment. Environmental Liabilities increased \$5.2 billion as new program cost estimating tools were introduced in FY 2006.

Figure 9. Select General Fund Assets and Liabilities

<b>General Fund</b>				
<i>\$ in billions</i>				
Asset Type	FY 2005	FY 2006	Change	Percentage of FY 2006 Assets
Fund Balance with Treasury	\$87.1	\$94.6	\$7.5	42%
General Property, Plant and Equipment	77.6	84.2	6.6	37%
Inventory	37.7	38.6	0.9	17%
Remaining Assets	7.0	9.1	2.1	4%
<b>Total Assets</b>	<b>\$209.4</b>	<b>\$226.5</b>	<b>\$17.1</b>	<b>100%</b>
Liability Type	FY 2005	FY 2006	Change	Percentage of FY 2006 Liabilities
Environmental Liabilities	\$39.8	\$45.0	\$5.2	64%
Accounts Payable	12.0	12.5	0.5	18%
Other Liabilities	8.8	11.3	2.5	16%
Remaining Liabilities	1.7	1.5	(0.2)	2%
<b>Total Liabilities</b>	<b>\$62.3</b>	<b>\$70.3</b>	<b>\$8.0</b>	<b>100%</b>

**Army Working Capital Fund Financial Results**

The primary mission of Army Working Capital Fund (AWCF) activities is to help the Army maintain constant readiness by providing supplies, equipment and ordnance necessary to support the projection and sustainment of forces in the most efficient and cost-effective manner possible. In carrying out this mission, the activities are obligated to control and to reduce costs. The AWCF measures financial performance through three primary means – cash management, carryover and net and accumulated operating results – and operational performance through two primary means – stock availability and production through-put.

**Cash Management**

The ability to generate cash is dependent on setting rates to recover full costs, including any previous year losses, accurately projecting workload and meeting established operational goals. Unlike the private sector, the Army does not have lines of credit. Therefore, it must maintain sufficient cash on hand in the AWCF account at the U.S. Treasury to pay liabilities when due. To minimize the cash balance required for operating and capital disbursements, the AWCF projects collections and disbursements on a monthly basis, working within a 10 percent margin of error.

Table 10. AWCF Cash

	FY 2004	FY 2005	FY 2006
Collections	12,248.7	14,383.6	14,512.8
Disbursements	11,619.4	14,708.7	14,260.8
Net Outlays	(629.3)	325.1	(252.0)
Cash Balance	948.5	623.3	875.3

The AWCF ended FY 2006 with a cash balance of \$875.3 million, \$278.1 million above the required seven-to-10-day level of \$597.2 million. In June 2006, the AWCF received \$347.1 million from the FY 2006 supplemental appropriation to replace war reserve and prepositioned stocks and to augment inventories. The AWCF cash balance should return to a level closer to its corpus requirement when operations in Iraq and Afghanistan begin to decline and payments associated with the delivery of replacement stocks and repair of equipment are made at levels higher than inventory sales.

**Carryover**

Carryover is work carried over from one fiscal year to the next, which provides continuity for the industrial workforce. Despite a \$94.7 million congressional mark against FY 2006 Operation and Maintenance, Army (OMA) funding for excess carryover (orders received but not completed at the end of a fiscal year) in the Industrial Operations’ activity group, carryover was kept substantially below the ceiling as depicted in the table below. Carryover is projected to remain below the ceiling across the budget forecast, which is a tribute to the intensive management of aggressive production schedules.

Table 11. AWCF Carryover

	FY 2004	FY 2005	FY 2006
New Orders	3,437.1	4,517.6	5,320.0
Carryover Ceiling	1,626.3	1,705.6	2,017.0
Carryover	1,485.3	1,394.1	1,991.0

**Net and Accumulated Operating Results**

Net Operating Results (NOR) represent the difference between costs and revenues in an accounting period. Accumulated Operating Results (AOR) represent the aggregate of all recoverable net earnings, including prior year adjustments, since inception of the activity. The goal of the AWCF is to break even over time. An activity group’s financial performance is

Table 12. Net Operating Results and Accumulate Operating Results by Business Area

	FY 2004	FY 2005	FY 2006
Industrial Operations NOR*	241.3	191.9	(209.3)
Industrial Operatons AOR	455.2	647.1	437.8
Supply Management NOR	134.0	(71.4)	5.5
Supply Management AOR	29.2	(42.2)	(36.7)

\*Includes prior year AOR adjustments.

measured by comparing actual results to the goal of breaking even over time. The rates in the Industrial Operations activity group will be set to return the positive AOR. The rate in the Supply Management activity group will be set to recoup the negative AOR.

### Stock Availability

Stock Availability measures the percentage of requisitions for stocked items completely filled within established timeframes. The Department of Defence and the Army have set a target of 85 percent stock availability. Although

Table 13. Stock Availability (percentage)

	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter
FY 2004	73%	69%	74%	76%
FY 2005	76%	78%	82%	79%
FY 2006	85%	86%	84%	85%

ongoing contingency operations and the high level of OPTEMPO in support of OIF and GWOT have placed a significant burden on the Army's spares inventory, steady improvement of stock availability was seen in FY 2006 due to receipt of needed materiel.

### Production

Although the Industrial Operations activity group is comprised of an array of installation activities, the preponderance of workload relates to depot maintenance. Major operations in Iraq and Afghanistan are placing tremendous

Table 14. Annual Production Through-put\*

	FY 2004	FY 2005	FY 2006
Depot Aircraft	4	44	46
Helicopter Engines	<200	>600	>700
Bradleys	144	318	600
HMMWVs	<100	>5,000	7,398
Machine Guns	14,000	43,000	50,000
Firefinders Radars	<1	45	57
Track Shoes	120,000	395,000	400,000

\* Through-put is simply a count of the weapon systems completed for any given year.

demands on equipment. Because of higher operational tempo, rough desert environments and limited depot maintenance available in theater, operational fleets are aging four years for every year in theater. To counter this, the Army established a reset program designed to reverse the effects of combat stress on equipment and to prepare equipment for future missions.

A key component of the reset program is the recapitalization of equipment. Through

recapitalization, depots replace and/or upgrade numerous component parts, which supports the Army's conversion to modular formations, a key element of transformation.

The Army's depots and their efforts to partner with industry are critical to the entire reset effort. The Army estimates it will take close to two years after the return of forces from Iraq and Afghanistan to completely reconstitute equipment. Because of actions taken to surge in support of wartime requirements, the Industrial Operations activity group has dramatically increased depot production over pre-war levels, as illustrated below:

In recent years, the Army has begun implementing Lean Six Sigma to reengineer many of its manufacturing and administrative processes. The objective is to streamline operations across the enterprise, reduce bureaucracy, and improve flexibility and agility. In FY 2006, the Army was proud to be recognized for our Lean Six Sigma improvements through the award of several Shingo Prizes for Excellence in Manufacturing.

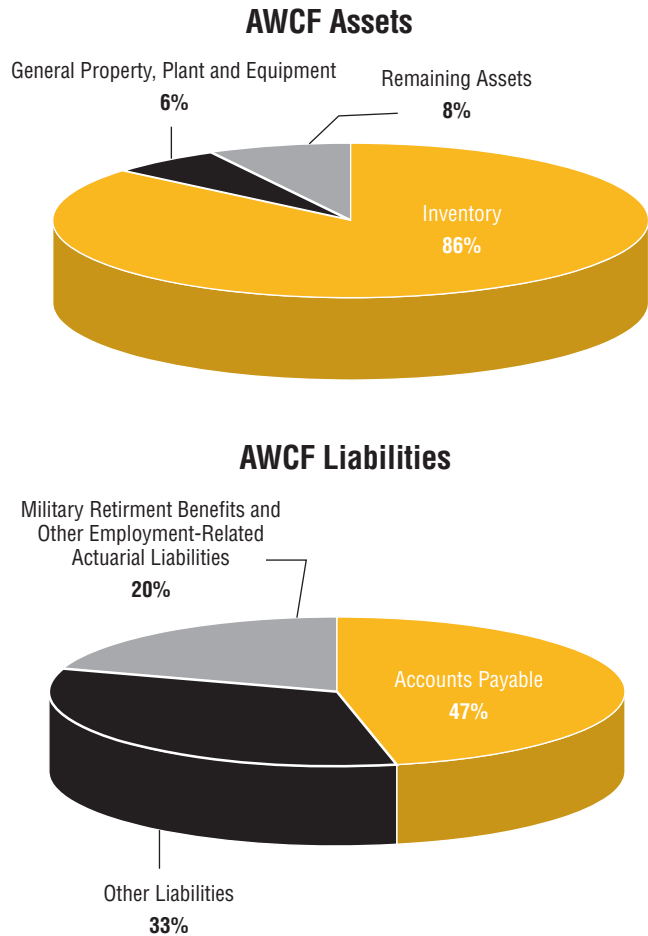
### AWCF Balance Sheet

The AWCF balance sheet shows total assets exceeding \$20 billion. The vast majority of AWCF assets are Inventory, followed by \$1.3 million in GPP&E. Liabilities consist of \$654.9 million in Accounts Payable and \$526.8 million in Other Liabilities, which includes payroll, benefits, accrued annual leave and workman's compensation





Figure 10. AWCF Assets and Liabilities



(the Federal Employees' Compensation Act, or FECA, administered by the Department of Labor on behalf of the Army and reimbursed by AWCF). The remaining liabilities, \$262.5 million, represent the actuarial amount of workman's compensation (FECA) estimated to be paid in the future for death, disability, medical and miscellaneous costs for approved compensation cases.

The majority of AWCF assets are the inventory items it holds to meet its mission of providing supplies, equipment and ordnance necessary to support the projection and sustainment of the force. In FY 2006, Inventory and Related Property increased by \$2.0 billion as the AWCF accelerated the replenishment of inventory.

Figure 11. Select AWCF Assets and Liabilities

**Working Capital Fund**

*\$ in billions*

Asset Type	FY 2005	FY 2006	Change	Percentage of FY 2006 Assets
Inventory	\$15.9	\$17.9	\$2.0	86%
General Property, Plant and Equipment	1.2	1.3	0.1	6%
Remaining Assets	1.3	1.6	0.3	8%
<b>Total Assets</b>	<b>\$18.4</b>	<b>\$20.8</b>	<b>\$2.4</b>	<b>100%</b>
Liability Type	FY 2005	FY 2006	Change	Percentage of FY 2006 Liabilities
Accounts Payable	\$0.4	\$0.7	\$0.3	47%
Other Liabilities	0.7	0.5	(0.2)	33%
Military Retirement Benefits and Other Employment-Related Actuarial Liabilities	0.3	0.3	0.0	20%
<b>Total Liabilities</b>	<b>\$1.4</b>	<b>\$1.5</b>	<b>\$0.1</b>	<b>100%</b>

## Possible Future Effects of Existing Events and Conditions

As stated in the conclusion to the Performance Goals, Objectives and Results section, there exists a mismatch between the cost of the National Defense Strategy and the resources allocated to the Army to execute that strategy. The Army requires a base budget 30 percent greater than today's to fully resource the doctrinal QDR force. Further, to meet operational reality, the Army has had to rely on substantial supplemental appropriations.

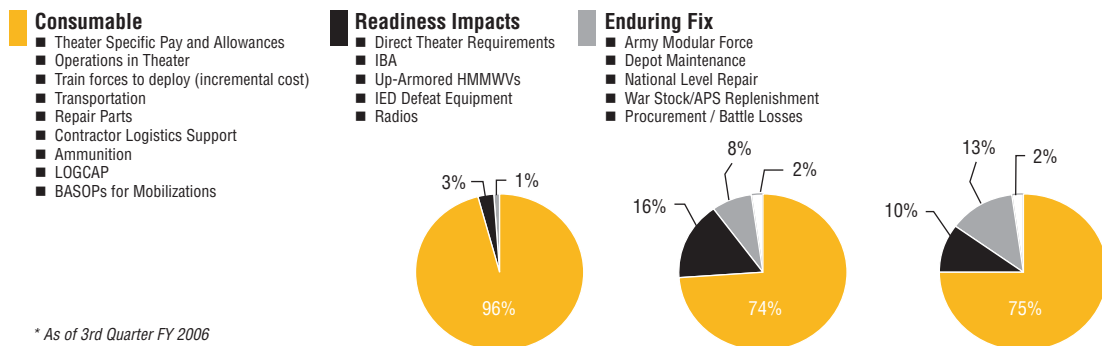
The future effects of the current funding situation cannot be overstated. Already, this strategy-resources mismatch is the key factor in decreasing readiness today, and hampers our ability to implement durable change for the future. In FY 2006, the Army was forced to shift (reprogram) billions of dollars from equipment and operation and maintenance accounts to cover personnel costs. Shifting funds from the accounts that buy the materiel and weapon systems our Soldiers use every day to fight and train, that run our installations, and that support daily activities, directly impacts readiness. Reprogramming allows us to avert a financial crisis today, but causes other problems for the long run.

The requirement to reset equipment and to restore units to full readiness upon their return from operational deployments is fundamental to sustaining the full range of current global commitments and to preparing for emerging threats. The Army is carrying forward multibillion dollar shortfalls in our reset program and our overall procurement account. Under current plans, the Army does not have enough funding in the base budget to cover the cost of resetting the force. Without supplemental funding, readiness would drop rapidly. Resetting the force while simultaneously fighting the GWOT and transforming to become a more powerful, more flexible, more deployable force is a complex task that necessitates a sustained national commitment and careful balancing of resources.

The Army base budget is designed to cover all of Army activities that can be reasonably forecasted, including such items as Soldier pay and benefits, operation and maintenance and the enduring changes discussed in the Performance Results section. The Army must also obtain funding sufficient to prosecute the Global War on Terrorism while simultaneously improving and maintaining the readiness of the Army – active component, National Guard and Army Reserve. Toward that end, Congress has provided substantial resources through supplemental appropriations to cover contingency operations. The unpredictable timing inherent in supplemental funding, however, fosters inefficiencies in the resource allocation process.

Even with supplemental funding, at the current funding levels the Army cannot implement the enduring changes required to meet the challenges of the 21st century. The vast majority of supplemental funding has been spent on consumable items needed for on-going operations; while only a small percentage has supported long-term fixes, such as modularizing the force, depot-level maintenance activities, national-level repair and replenishment of war stocks and Army pre-positioned equipment sets. Figure 12 illustrates how the Army has spent supplemental funding since FY 2004.

Figure 12. How the Army Spent Supplemental Funds\*

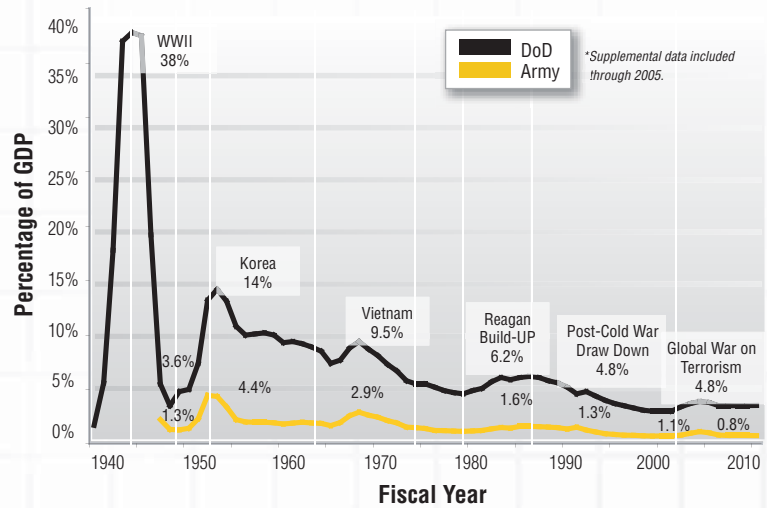


Due to the extraordinary level of commitment and operational activity demanded of the Army since September 11, 2001, the amounts of supplemental funding required to keep pace with the daily cost of prosecuting the GWOT have been high. This has created the perception – an incorrect perception – that the Army is flush with cash.

The timing of supplemental appropriations is also problematic. As the Army is not fully funded through the base budget, Army management must implement stop-gap measures. For example, in the second half of FY 2006, the Army imposed hiring freezes and limited travel.

To put the ongoing funding challenges in historical perspective, defense spending as a percentage of Gross Domestic Product (GDP) is at its lowest point in 60 years (Figure 13). However, the OPTEMPO of the Army is at its highest levels since World War II. As a country, the equivalent of 3.8 percent of GDP is allocated towards national defense. The Army is getting the equivalent of 1.1 percent – and that figure includes supplemental appropriations.

Figure 13. DoD and Army Outlays as a Percentage of GDP

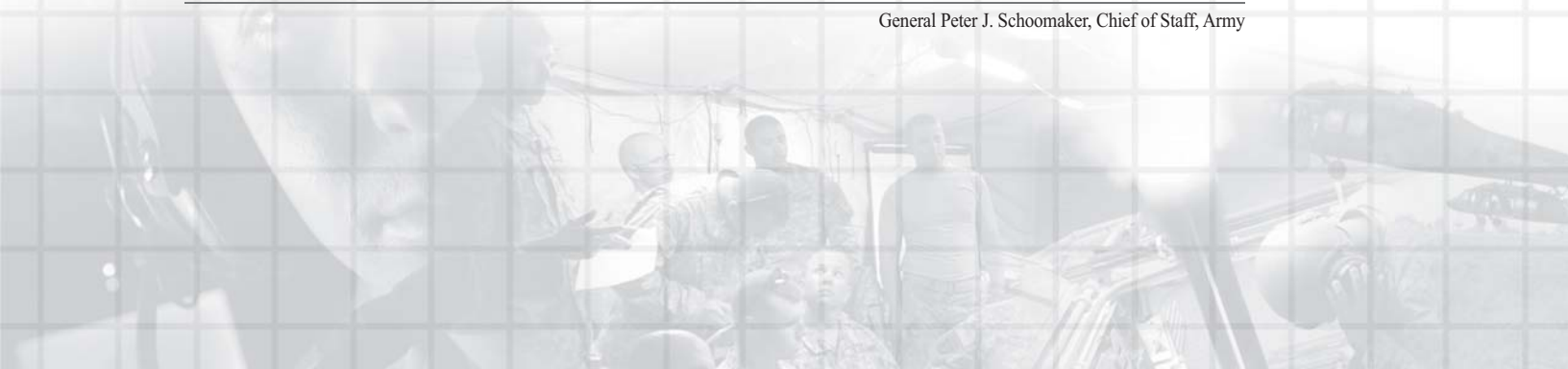


Source: National Defense Budget Estimates for FY 2006, Office of the Under Secretary of Defense (Comptroller)



*“Let there be no mistake, our Soldiers’ effectiveness in battle, both today and tomorrow, ultimately depends upon a national commitment to recruit, train, equip, and support them and their families properly. This is a matter of National priorities, not affordability.”*

General Peter J. Schoomaker, Chief of Staff, Army





## LIMITATIONS



**U.S. ARMY**

### LIMITATIONS OF THE FINANCIAL STATEMENTS

The financial statements have been prepared to report the financial position and results of operations for the entity, pursuant to the requirements of Title 31, United States Code, section 3515(b).

While the statements have been prepared from the books and records of the entity, in accordance with the formats prescribed by the Office of Management and Budget, the statements are in addition to the financial reports used to monitor and control budgetary resources which are prepared from the same books and records.

The statements should be read with the realization that they are for a component of the United States Government, a sovereign entity.

**CONSOLIDATED BALANCE SHEET***As of September 30, 2006 and 2005 (\$ in Thousands)*

	2006 Consolidated	2005 Consolidated
<b>ASSETS (Note 2)</b>		
Intragovernmental:		
Fund Balance with Treasury (Note 3)		
Entity	\$ 94,430,198	\$ 86,799,034
Non-Entity Seized Iraqi Cash	30,216	61,370
Non-Entity-Other	172,515	232,913
Investments (Note 4)	3,407	3,495
Accounts Receivable (Note 5)	357,183	276,635
Other Assets (Note 6)	601,861	824,303
Total Intragovernmental Assets	<u>\$ 95,595,380</u>	<u>\$ 88,197,750</u>
Cash and Other Monetary Assets (Note 7)	\$ 1,784,810	\$ 1,482,046
Accounts Receivable, Net (Note 5)	627,721	584,005
Loans Receivable (Note 8)	0	0
Inventory and Related Property, Net (Note 9)	38,639,039	37,703,353
General Property, Plant and Equipment, Net (Note 10)	84,243,850	77,572,649
Investments (Note 4)	0	0
Other Assets (Note 6)	5,694,685	3,844,524
<b>TOTAL ASSETS</b>	<u><u>\$ 226,585,485</u></u>	<u><u>\$ 209,384,327</u></u>
<b>LIABILITIES (Note 11)</b>		
Intragovernmental:		
Accounts Payable (Note 12)	\$ 1,593,783	\$ 1,918,309
Debt (Note 13)	11,404	0
Other Liabilities (Note 15 & 16)	3,181,296	2,372,261
Total Intragovernmental Liabilities	<u>\$ 4,786,483</u>	<u>\$ 4,290,570</u>
Accounts Payable (Note 12)	\$ 10,884,262	\$ 10,137,011
Military Retirement and Other Federal Employment Benefits (Note 17)	1,461,098	1,663,650
Environmental and Disposal Liabilities (Note 14)	44,975,237	39,760,514
Loan Guarantee Liability (Note 8)	12,853	12,394
Other Liabilities (Note 15 and Note 16)	8,148,757	6,401,916
<b>TOTAL LIABILITIES</b>	<u><u>\$ 70,268,690</u></u>	<u><u>\$ 62,266,055</u></u>
<b>NET POSITION</b>		
Unexpended Appropriations - Earmarked Funds (Note 23)	\$ 0	\$ 0
Unexpended Appropriations - Other Funds	85,045,798	74,704,745
Cumulative Results of Operations - Earmarked Funds	42,792	0
Cumulative Results of Operations - Other Funds	71,228,205	72,413,527
<b>TOTAL NET POSITION</b>	<u><u>\$ 156,316,795</u></u>	<u><u>\$ 147,118,272</u></u>
<b>TOTAL LIABILITIES AND NET POSITION</b>	<u><u>\$ 226,585,485</u></u>	<u><u>\$ 209,384,327</u></u>

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

Department of Defense - Department of the Army

**CONSOLIDATED STATEMENT OF NET COST***As of September 30, 2006 and 2005 (\$ in Thousands)*

	2006 Consolidated	2005 Consolidated
<b>Program Costs</b>		
Gross Costs	\$ 175,017,272	\$ 156,166,632
(Less: Earned Revenue)	(10,403,521)	(9,740,447)
Net Program Costs	<u>\$ 164,613,751</u>	<u>\$ 146,426,185</u>
<b>Cost Not Assigned to Programs</b>	0	0
<b>(Less: Earned Revenue Not Attributable to Programs)</b>	0	0
<b>Net Cost of Operations</b>	<u>\$ 164,613,751</u>	<u>\$ 146,426,185</u>

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

**CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION**

As of September 30, 2006 and 2005 (\$ in Thousands)

	Earmarked Funds		All Other Funds	
<b>CUMULATIVE RESULTS OF OPERATIONS</b>				
<b>Beginning Balances</b>	\$	35,140	\$	115,207,483
<b>Prior Period Adjustments:</b>				
Changes in accounting principles (+/-)		0		0
Corrections of errors (+/-)		0		(42,829,096)
<b>Beginning Balances, as adjusted</b>	\$	35,140	\$	72,378,387
<b>Budgetary Financing Sources:</b>				
Appropriations received		0		0
Appropriations transferred-in/out (+/-)		0		0
Other adjustments (rescissions, etc.) (+/-)		0		0
Appropriations used		0		163,679,472
Nonexchange revenue		9,198		0
Donations and forfeitures of cash and cash equivalents		4,754		0
Transfers-in/out without reimbursement (+/-)		0		453,164
Other budgetary financing sources (+/-)		0		0
<b>Other Financing Sources:</b>				
Donations and forfeitures of property		0		27,457
Transfers-in/out without reimbursement (+/-)		0		565,989
Imputed financing from costs absorbed by others		0		964,108
Other (+/-)		(10)		(2,232,911)
<b>Total Financing Sources</b>	\$	13,942	\$	163,457,279
<b>Net Cost of Operations (+/-)</b>		6,291		164,607,460
<b>Net Change</b>	\$	7,651	\$	(1,150,181)
<b>Ending Balances</b>	\$	42,791	\$	71,228,206
<b>UNEXPENDED APPROPRIATIONS</b>				
<b>Beginning Balances</b>	\$	0	\$	74,704,745
<b>Prior Period Adjustments:</b>				
Changes in accounting principles (+/-)		0		0
Corrections of errors (+/-)		0		0
<b>Beginning balances, as adjusted</b>	\$	0	\$	74,704,745
<b>Budgetary Financing Sources:</b>				
Appropriations received		0		173,014,453
Appropriations transferred-in/out (+/-)		0		3,169,768
Other adjustments (rescissions, etc.) (+/-)		0		(2,163,696)
Appropriations used		0		(163,679,472)
Nonexchange revenue		0		0
Donations and forfeitures of cash and cash equivalents		0		0
Transfers-in/out without reimbursement (+/-)		0		0
Other budgetary financing sources (+/-)		0		0
<b>Other Financing Sources:</b>				
Donations and forfeitures of property		0		0
Transfers-in/out without reimbursement (+/-)		0		0
Imputed financing from costs absorbed by others		0		0
Other (+/-)		0		0
<b>Total Financing Sources</b>	\$	0	\$	10,341,053
<b>Net Cost of Operations (+/-)</b>		0		0
<b>Net Change</b>		0		10,341,053
<b>Ending Balances</b>	\$	0	\$	85,045,798

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



Department of Defense - Department of the Army

**CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION**

As of September 30, 2006 and 2005 (\$ in Thousands)

	Eliminations	2006 Consolidated	2005 Consolidated
<b>CUMULATIVE RESULTS OF OPERATIONS</b>			
<b>Beginning Balances</b>	\$ 0	\$ 115,242,623	\$ 109,208,001
<b>Prior Period Adjustments:</b>			
Changes in accounting principles (+/-)	0	0	0
Corrections of errors (+/-)	0	(42,829,096)	(42,829,096)
<b>Beginning Balances, as adjusted</b>	\$ 0	\$ 72,413,527	\$ 66,378,905
<b>Budgetary Financing Sources:</b>			
Appropriations received	0	0	0
Appropriations transferred-in/out (+/-)	0	0	0
Other adjustments (rescissions, etc.) (+/-)	0	0	0
Appropriations used	0	163,679,472	150,048,733
Nonexchange revenue	0	9,198	9,331
Donations and forfeitures of cash and cash equivalents	0	4,754	5,609
Transfers-in/out without reimbursement (+/-)	0	453,164	3,721,535
Other budgetary financing sources (+/-)	0	0	2,141
<b>Other Financing Sources:</b>			
Donations and forfeitures of property	0	27,457	0
Transfers-in/out without reimbursement (+/-)	0	565,989	528,071
Imputed financing from costs absorbed by others	0	964,108	1,092,805
Other (+/-)	0	(2,232,921)	(2,947,418)
<b>Total Financing Sources</b>	\$ 0	\$ 163,471,221	\$ 152,460,807
<b>Net Cost of Operations (+/-)</b>	0	164,613,751	146,426,185
<b>Net Change</b>	\$ 0	\$ (1,142,530)	\$ 6,034,622
<b>Ending Balances</b>	\$ 0	\$ 71,270,997	\$ 72,413,527
<b>UNEXPENDED APPROPRIATIONS</b>			
<b>Beginning Balances</b>	\$ 0	\$ 74,704,745	\$ 73,238,304
<b>Prior Period Adjustments:</b>			
Changes in accounting principles (+/-)	0	0	0
Corrections of errors (+/-)	0		0
<b>Beginning balances, as adjusted</b>	\$ 0	\$ 74,704,745	\$ 73,238,304
<b>Budgetary Financing Sources:</b>			
Appropriations received	0	173,014,453	149,831,938
Appropriations transferred-in/out (+/-)	0	3,169,768	2,560,759
Other adjustments (rescissions, etc) (+/-)	0	(2,163,696)	(877,523)
Appropriations used	0	(163,679,472)	(150,048,733)
Nonexchange revenue	0	0	0
Donations and forfeitures of cash and cash equivalents	0	0	0
Transfers-in/out without reimbursement (+/-)	0	0	0
Other budgetary financing sources (+/-)	0	0	0
<b>Other Financing Sources:</b>			
Donations and forfeitures of property	0	0	0
Transfers-in/out without reimbursement (+/-)	0	0	0
Imputed financing from costs absorbed by others	0	0	0
Other (+/-)	0	0	0
<b>Total Financing Sources</b>	\$ 0	\$ 10,341,053	\$ 1,466,441
<b>Net Cost of Operations (+/-)</b>	0	0	0
<b>Net Change</b>	0	10,341,053	1,466,441
<b>Ending Balances</b>	\$ 0	\$ 85,045,798	\$ 74,704,745

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

**COMBINED STATEMENT OF BUDGETARY RESOURCES**

As of September 30, 2006 and 2005 (\$ in Thousands)

	Budgetary Financing Accounts		Non Budgetary Financing Accounts	
	2006 Combined	2005 Combined	2006 Combined	2005 Combined
<b>BUDGETARY RESOURCES</b>				
Unobligated balance, brought forward, October 1	\$ 15,477,292	\$ 22,880,756	\$ 1,525	\$ 1,424
Recoveries of prior year unpaid obligations	16,851,046	17,033,447	0	0
Budget authority				
Appropriation	173,027,517	149,846,916	0	0
Borrowing authority	0	0	11,404	0
Contract authority	0	0	0	0
Spending authority from offsetting collections				
Earned				
Collected	21,805,492	20,948,239	326	101
Change in receivables from Federal sources	(20,488)	(415,099)	0	0
Change in unfilled customer orders				
Advance received	420,284	77,733	0	0
Without advance from Federal sources	805,587	2,159,939	0	0
Anticipated for rest of year, without advances	0	0	0	0
Previously unavailable	0	0	0	0
Expenditure transfers from trust funds	0	0	0	0
Subtotal	196,038,392	172,617,728	11,730	101
Nonexpenditure transfers, net, anticipated and actual	3,169,768	3,415,759	0	0
Temporarily not available pursuant to Public Law	0	0	0	0
Permanently not available	(2,163,696)	(877,523)	0	0
<b>Total Budgetary Resources</b>	<b>\$ 229,372,802</b>	<b>\$ 215,070,167</b>	<b>\$ 13,255</b>	<b>\$ 1,525</b>
<b>Status of Budgetary Resources:</b>				
Obligations incurred:				
Direct	\$ 186,913,360	\$ 175,086,215	\$ 11,962	\$ 0
Reimbursable	25,435,449	24,506,660	0	0
Subtotal	\$ 212,348,809	\$ 199,592,875	\$ 11,962	\$ 0
Unobligated balance:				
Apportioned	14,880,099	13,665,452	535	1,525
Exempt from apportionment	4,035	11,980	0	0
Subtotal	14,884,134	13,677,432	535	1,525
Unobligated balance not available	2,139,859	1,799,860	758	0
<b>Total status of budgetary resources</b>	<b>\$ 229,372,802</b>	<b>\$ 215,070,167</b>	<b>\$ 13,255</b>	<b>\$ 1,525</b>
<b>Change in Obligated Balance:</b>				
Obligated balance, net				
Unpaid obligations, brought forward, October 1	\$ 80,720,880	\$ 71,629,016	\$ 0	\$ 0
Less: Uncollected customer payments from Federal Sources, brought forward, October 1	(16,351,456)	(14,606,617)	0	0
Total unpaid obligated balance	64,369,424	57,022,399	0	0
Obligations incurred net (+/-)	\$ 212,348,809	\$ 199,592,876	\$ 11,962	\$ 0
Less: Gross outlays	(186,063,536)	(173,467,566)	(11,962)	0
Obligated balance transferred, net				
Actual transfers, unpaid obligations (+/-)	0	0	0	0
Actual transfers, uncollected customer payments from Federal sources (+/-)	0	0	0	0
Total Unpaid obligated balance transferred, net	0	0	0	0
Less: Recoveries of prior year unpaid obligations, actual	(16,851,046)	(17,033,447)	0	0
Change in uncollected customer payments from Federal sources (+/-)	(785,100)	(1,744,839)	0	0
Obligated balance, net, end of period				
Unpaid obligations	90,155,105	80,720,880	0	0
Less: Uncollected customer payments (+/-) from Federal sources (-)	(17,136,557)	(16,351,456)	0	0
Total, unpaid obligated balance, net, end of period	73,018,548	64,369,424	0	0
<b>Net Outlays</b>				
<b>Net Outlays:</b>				
Gross outlays	186,063,536	173,467,566	11,962	0
Less: Offsetting collections	(22,225,774)	(21,025,971)	(325)	(101)
Less: Distributed Offsetting receipts	(783,002)	(195,234)	0	0
<b>Net Outlays</b>	<b>\$ 163,054,760</b>	<b>\$ 152,246,361</b>	<b>\$ 11,637</b>	<b>\$ (101)</b>

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

Department of Defense - Department of the Army

**CONSOLIDATED STATEMENT OF FINANCING**

As of September 30, 2006 and 2005 (\$ in Thousands)

	2006 Consolidated	2005 Consolidated
<b>Resources Used to Finance Activities:</b>		
Budgetary Resources Obligated		
Obligations incurred	\$ 212,360,771	\$ 199,592,875
Less: Spending authority from offsetting collections and recoveries (-)	(39,862,247)	(39,804,359)
Obligations net of offsetting collections and recoveries	\$ 172,498,524	\$ 159,788,516
Less: Offsetting receipts (-)	(783,002)	(195,234)
Net obligations	\$ 171,715,522	\$ 159,593,282
Other Resources		
Donations and forfeitures of property	27,457	0
Transfers in/out without reimbursement (+/-)	565,989	528,071
Imputed financing from costs absorbed by others	964,108	1,092,805
Other (+/-)	(2,232,921)	(2,947,418)
Net other resources used to finance activities	\$ (675,367)	\$ (1,326,542)
<b>Total resources used to finance activities</b>	<b>\$ 171,040,155</b>	<b>\$ 158,266,740</b>
<b>Resources Used to Finance Items not Part of the Net Cost of Operations</b>		
Change in budgetary resources obligated for goods, services and benefits ordered but not yet provided		
Undelivered Orders (-)	\$ (9,451,160)	\$ (10,942,905)
Unfilled Customer Orders	1,225,872	2,237,672
Resources that fund expenses recognized in prior periods	(294,876)	(1,282,337)
Budgetary offsetting collections and receipts that do not affect net cost of operations	783,327	195,334
Resources that finance the acquisition of assets	(30,921,684)	(26,752,491)
Other resources or adjustments to net obligated resources that do not affect net cost of operations		
Less: Trust or Special Fund Receipts Related to exchange in the Entity's Budget (-)	0	0
Other (+/-)	1,639,475	2,419,346
<b>Total resources used to finance items not part of the net cost of operations</b>	<b>\$ (37,019,046)</b>	<b>\$ (34,125,381)</b>
<b>Total resources used to finance the net cost of operations</b>	<b>\$ 134,021,109</b>	<b>\$ 124,141,359</b>
<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:		
Increase in annual leave liability	\$ 100,742	\$ 91,655
Increase in environmental and disposal liability	5,214,723	0
Upward/Downward reestimates of credit subsidy expense (+/-)	0	0
Increase in exchange revenue receivable from the the public (-)	0	0
Other (+/-)	223,353	54,908
Total components of Net Cost of Operations that will not require or generate resources in future periods	\$ 5,538,818	\$ 146,563
Components not Requiring or Generating Resources:		
Depreciation and amortization	23,824,451	16,965,074
Revaluation of assets or liabilities (+/-)	404	1,074
Other (+/-)		
Trust Fund Exchange Revenue	0	(82)
Cost of Goods Sold	3,061	0
Operating Material & Supplies Used	0	0
Other	1,225,908	5,172,197
Total components of Net Cost of Operations that will not require or generate resources	\$ 25,053,824	\$ 22,138,263
<b>Total components of net cost of operations that will not require or generate resources in the current period</b>	<b>\$ 30,592,642</b>	<b>\$ 22,284,826</b>
<b>Net Cost of Operations</b>	<b>\$ 164,613,751</b>	<b>\$ 146,426,185</b>

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

**COMBINED STATEMENT OF CUSTODIAL ACTIVITY***As of September 30, 2006 and 2005 (\$ in Thousands)*

	2006 Combined	2005 Combined
<b>SOURCE OF COLLECTIONS</b>		
Deposits by Foreign Governments	\$ 0	\$ 136,000
Seized Iraqi Cash	0	1
Other Collections	0	0
Total Cash Collections	<u>\$ 0</u>	<u>\$ 136,001</u>
Accrual Adjustments (+/-)	0	0
Total Custodial Collections	<u>\$ 0</u>	<u>\$ 136,001</u>
<b>DISPOSITION OF COLLECTIONS</b>		
Disbursed on Behalf of Foreign Governments and International Organizations	\$ 34,564	\$ 82,613
Seized Assets Disbursed on behalf of Iraqi People	31,154	52,061
Increase (Decrease) in Amounts to be Transferred	(34,564)	53,387
Collections Used for Refunds and Other Payments	0	0
Retained by The Reporting Entity	0	0
Seized Assets Retained for Support of the Iraqi People	(31,154)	(52,060)
Total Disposition of Collections	<u>\$ 0</u>	<u>\$ 136,001</u>
<b>NET CUSTODIAL COLLECTION ACTIVITY</b>	<u>\$ 0</u>	<u>\$ 0</u>

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

## Note 1. Significant Accounting Policies

### 1.A. Basis of Presentation

These financial statements have been prepared to report the financial position and results of operations of the Department of the Army, as required by the “Chief Financial Officers Act of 1990,” expanded by the “Government Management Reform Act of 1994,” and other appropriate legislation. The financial statements have been prepared from the books and records of the Army General Fund in accordance with the “DoD Financial Management Regulation,” Office of Management and Budget Circular (OMB) A-136, Financial Reporting Requirements, and to the extent possible generally accepted accounting principles (GAAP). The accompanying financial statements account for all resources for which the Army General Fund is responsible. Information relative to classified assets, programs and operations is aggregated and reported in such a manner that is not discernable.

The Army General Fund is unable to fully implement all elements of GAAP and the OMB Circular A-136, due to limitations of its financial management processes and systems and nonfinancial systems and processes that feed into the financial statements. The Army General Fund derives its reported values and information for major asset and liability categories largely from nonfinancial systems, such as inventory systems and logistics systems. These systems were designed to support reporting requirements for maintaining accountability over assets and reporting the status of Federal Appropriations, rather than preparing financial statements in accordance with GAAP. The Army General Fund continues to implement process and system improvements to address the limitations many of which are detailed below. The Army General Fund currently has agreed with 12 auditor identified financial statement material weaknesses: (1) Financial Management Systems, (2) Accounting Adjustments, (3) Intragovernmental Transactions and Eliminations, (4) Abnormal Account Balances, (5) Accounts Receivable, (6) Inventory and Related Property, (7) Property, Plant, and Equipment, (8) Accounts Payable, (9) Environmental Liabilities, (10) Statement of Net Cost, (11) Statement of Budgetary Resources, and (12) Statement of Financing.

### 1.B. Mission of the Reporting Entity

The Army mission is to support National Security and Defense Strategies by providing well-trained, well-led, and well-equipped forces to the combatant commanders. This mission encompasses the intent of Congress, as defined in Title 10 of the U.S. Code, to preserve the peace and security and provide for the defense of the U.S., the territories, commonwealths, and possessions of the U.S., and any areas occupied by the U.S.; support national policies; implement national objectives; and overcome any nations responsible for aggressive acts that imperil the peace and security of the U.S.

This mission has been unchanged for the 230-year life of the Army, but the environment and nature of conflict have undergone many changes over that same time, especially with the Global War on Terror. This has required the Army to undergo a simultaneous transformation process in the way that it fights and in the way that it trains and equips its Soldiers. This transformation is progressing rapidly, but it must be taken to its full conclusion if the Army is to continue to meet the Nation’s domestic and international security obligations today and into the future.

### 1.C. Appropriations and Funds

The Army General Fund receives its appropriations and funds as general, working capital (revolving), trust, special, and deposit funds. The Army General Fund uses appropriations and funds to execute their missions and report on resource usage.

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

Working capital funds receive their initial funding 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. The working capital fund entities provide goods and services on a reimbursable basis. Reimbursable receipts fund ongoing operations and generally are available in their entirety for use without further congressional action.

Trust funds contain receipts and expenditures 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 fund accounts are used to record government receipts reserved for a specific purpose.

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

Deposit funds are used to record amounts held temporarily until paid to the appropriate government or public entity. The Army General Fund acts as an agent or a custodian for funds awaiting distribution, for example payroll taxes.

## **1.D. Basis of Accounting**

For FY 2006, Army General Fund financial management systems were unable to meet all of the requirements for full accrual accounting. Many of the Army General Fund's financial and nonfinancial feeder systems and processes were designed and implemented prior to the issuance of GAAP for federal agencies in 1994. Therefore, these systems were not designed to collect and record financial information on the full accrual accounting basis as required by GAAP. Most of the Army General Fund's legacy systems were designed to record information on a budgetary basis.

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

In addition, DoD identifies program costs based upon the major appropriation groups provided by the Congress. Current processes and systems, however, do not capture and report accumulated costs for major programs based upon the performance measures as required by the Government and Performance and Results Act (GPR). The DoD 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**

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

The Army General Fund does not include nonmonetary support provided by U.S. allies for common defense and mutual security in amounts reported in the Statement of Net Cost and the Statement of Financing. The U.S. has cost sharing agreements with other countries. Examples include countries where there is a mutual or reciprocal defense agreement, where U.S. troops are stationed, or where the U.S. Fleet is in a port.

## **1.F. Recognition of Expenses**

For financial reporting purposes, DoD policy requires recognition of operating expenses in the period incurred. However, because the Army General Fund's financial and nonfinancial feeder systems were not designed to collect and record financial information on the full accrual accounting basis, accrual adjustments are made for major items such as payroll expenses, accounts payable, and environmental liabilities and unbilled revenue. The Army General Fund's expenditures for capital and other long-term assets are recognized as operating expenses based on depreciation. In the case of Operating Materials and Supplies (OM&S), operating expenses are generally recognized when the items are purchased. Efforts are underway to migrate towards the consumption method for recognizing OM&S expenses.

## **1.G. Accounting for Intragovernmental Activities**

Preparation of reliable financial statements requires the elimination of transactions occurring among entities within the DoD or between two or more federal agencies. The Army General Fund, however, cannot accurately identify most of its intragovernmental transactions by customer because the Army General Fund's systems do not track buyer and seller data needed to match related transactions. Seller entities within the DoD provide summary seller-side balances for revenue, accounts receivable, and unearned revenue to the buyer-side internal DoD accounting offices. In most cases, the buyer-side records are adjusted to agree with DoD seller-side balances. Intra-DoD intragovernmental balances are then eliminated. The Army General Fund properly eliminates the revenue results from intra-DoD sales of capitalized assets. The DoD is developing long-term system 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 effectively with existing or foreseeable resources.

The Department of the Treasury Financial Management Service (FMS), is responsible for eliminating transactions between the DoD and other federal agencies. The Treasury Financial Manual, Part 2 – Chapter 4700, "Agency Reporting Requirements for the Financial Report of the United States Government" and the Treasury's "Federal Intragovernmental Transactions Accounting Policy Guide," provide guidance for reporting and reconciling intragovernmental balances. While the Army General Fund is unable to fully reconcile intragovernmental

transactions with all federal partners, the Army General Fund is able to reconcile balances pertaining to investments in federal securities, borrowings from the U.S. Treasury and the Federal Financing Bank, Federal Employees' Compensation Act transactions with the Department of Labor (DOL), and benefit program transactions with the Office of Personnel Management (OPM). The DoD's proportionate share of public debt and related expenses to the federal government are not included. The federal government does not apportion debt and its related costs to federal agencies. The DoD's financial statements, therefore, do not report any portion of the public debt or interest thereon, nor do the statements report the source of public financing whether from issuance of debt or tax revenues.

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

## **1.H. Transactions with Foreign Governments and International Organizations**

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

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

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

In addition, the DFAS sites and the USACE Finance Center submit reports to the Department of the Treasury, by appropriation, on interagency transfers, collections received and disbursements issued. The Department of the Treasury records this information to the applicable Fund Balance with Treasury (FBWT) account. Differences between the Army General Fund's recorded balance in the FBWT accounts and Treasury's FBWT accounts sometimes result and are subsequently reconciled.

### **1.J. Foreign Currency**

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

The majority of cash and all foreign currency is classified as nonentity and, therefore, is restricted. Amounts reported consist primarily of cash and foreign currency held by Disbursing Officers to carry out their paying, collecting and foreign currency accommodation exchange missions. Cash seized during Operation Iraqi Freedom is restricted for use to assist the Iraqi people and support the restoration of Iraq.

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

### **1.K. Accounts Receivable**

As presented in the Balance Sheet, accounts receivable includes accounts, claims and refunds receivable from other federal entities or from the public. Allowances for uncollectible accounts due from the public are based upon analysis of collection experience by fund type. The DoD does not recognize an allowance for estimated uncollectible amounts from other federal agencies. Claims against other federal agencies are to be resolved between the agencies (per Code of Federal Regulations 4 CFR 101).

The Army General Fund bases the estimate of uncollectible accounts receivable from the public on percentage of aged receivables by category. The allowance is calculated by using 50 percent of aged receivables, except foreign debt and debt as reported in the Defense Debt Management System in the 180-day to 2-year category and 100 percent of aged receivables in the greater than 2-year category.

## 1.L. Loans Receivable

Not Applicable

## 1.M. Inventories and Related Property

Most of the Army General Fund's inventories are currently reported at an approximation of historical cost using the latest acquisition cost adjusted for holding gains and losses. The latest acquisition cost method is used because legacy inventory systems were designed for materiel management rather than accounting. Although these systems provide visibility and accountability over inventory items, they do not maintain historical cost data necessary to comply with the SFFAS No. 3, "Accounting for Inventory and Related Property." Additionally, these systems cannot produce financial transactions using the USSGL, as required by the Federal Financial Management Improvement Act of 1996 (P.L. 104-208). By utilizing new systems development processes, the Army General Fund has transitioned, and is continuing to transition, the inventory to the moving average cost method. The Army General Fund is uncertain of the percentage of inventory now being reported from systems that have transitioned to moving average cost functionality. However, since the on-hand balances which transitioned were not, for the most part, baselined to auditable historical cost, the reported values remain noncompliant with SFFAS 3 and GAAP.

The Army General Fund manages only military or government specific materiel under normal conditions. Items commonly used are available from the commercial sector are not managed in the Army General Fund materiel management activities. Operational cycles are irregular, and the military risks associated with stock-out positions have no commercial parallel. The Army General Fund holds materiel based on military need and support for contingencies. Therefore, the DoD does not attempt to account separately for "inventory held for sale" and "inventory held in reserve for future sale" based on SFFAS No. 3 definitions.

Related property includes operating materials and supplies (OM&S). The OM&S, including munitions not held for sale, are valued at standard purchase price. The DoD uses both the consumption method and the purchase method of accounting for OM&S. Items that are centrally managed and stored, such as ammunition and engines, are generally recorded using the consumption method and are reported on the Balance Sheet as OM&S. When current systems cannot fully support the consumption method, the Army General Fund uses the purchase method. Under this method, materials and supplies are expensed when purchased. During FY 2006, the Army General Fund expensed significant amounts using the purchase method because the systems could not support the consumption method or management deemed that the item was in the hands of the end user.

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

The Army General Fund recognizes condemned material as "Excess, Obsolete, and Unserviceable." The cost of disposal is greater than the potential scrap value; therefore, the net value of condemned material is zero. Potentially redistributed material, 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.

Past audits identified uncertainties about the completeness and existence of reported values of inventory. Inventory available and purchased for resale includes consumable spare and repair parts and repairable items owned and managed by the Army General Fund. This inventory is retained to support military or national contingencies. Inventory held for repair is damaged inventory that requires repair to make it suitable for sale. It is more economical to repair than to procure these inventory items. Because the Army General Fund often relies on weapon systems and machinery no longer in production, the Army General Fund supports a process that encourages the repair and rebuilding of certain items. This repair cycle is essential to maintaining a ready, mobile and armed military force. Work in process balances include costs related to the production or servicing of items, including direct material, direct labor, applied overhead and other direct costs. Work in process also includes the value of finished products or completed services pending the submission of bills to the customer. The work in process designation may also be used to accumulate the amount paid to a contractor under cost reimbursable contracts, including amounts withheld from payment to ensure performance, and amounts paid to other government plants for accrued costs of end items of material ordered but not delivered. Work in process includes munitions in production and depot maintenance work with its associated labor, applied overhead and supplies used in the delivery of maintenance services.

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

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

The Army General Fund invests in nonmarketable securities. The two types of nonmarketable securities are par value and market-based intragovernmental securities. The Bureau of Public Debt issues nonmarketable par value intragovernmental securities. Nonmarketable, market-based intragovernmental securities mimic marketable securities, but are not publicly traded.



## 1.0. General Property, Plant and Equipment

The Department is moving away from a standard capitalization threshold for all categories (e.g. real property, military equipment, etc.) of General Property Plant, and Equipment (PP&E) to one that is specific for each individual category.

The Department revised the capitalization threshold from \$100,000 to \$20,000 for real property. The Army will validate existing real property values and implement sustainable business processes prior to incorporating the revised capitalization threshold for financial statement reporting. The current \$100,000 capitalization threshold remains unchanged for the remaining General PP&E categories.

General PP&E assets are capitalized at historical acquisition cost plus capitalized improvements when an asset has a useful life of two or more years and the acquisition cost equals or exceeds the DoD capitalization threshold of \$100,000. The DoD also requires capitalization of improvement costs over the DoD capitalization threshold of \$100,000 for General PP&E. The DoD depreciates all General PP&E, other than land, on a straight-line basis.

Prior to FY 1996, General PP&E was capitalized if it had an acquisition cost of \$15,000, \$25,000, and \$50,000 for fiscal years 1993, 1994, and 1995, respectively, and an estimated useful life of two or more years. General PP&E previously capitalized at amounts below \$100,000 were written off General Fund financial statements in FY 1998. When it is in the best interest of the government, the Army General Fund provides government property to contractors to complete contract work. The Army General Fund either owns or leases such property, or it is purchased directly by the contractor for the government based on contract terms. When the value of contractor-procured General PP&E exceeds the DoD capitalization threshold, it must be reported on the Army General Fund's Balance Sheet.

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

The SFFAS No. 23, "Eliminating the Category National Defense Property, Plant, and Equipment," established generally accepted accounting principles for valuing and reporting military equipment (e.g. ships, aircraft, combat vehicles, weapons) in federal financial statements. The standard provided for the use of estimated historical cost for valuing military equipment if obtaining actual historical cost information is not practical. The Department estimated historical cost using the Bureau of Economic Analysis (BEA) estimates to calculate the value of the military equipment for reporting periods from October 1, 2002 through March 31, 2006.

Effective 3rd Quarter, FY 2006, the Department is replacing the BEA estimation methodology with military equipment values based on internal Departmental records. To create a baseline, the Department initially identified the universe of military equipment by accumulating information relating to program funding and associated military equipment, equipment useful life, program acquisitions and disposals. The military equipment baseline is updated using expenditure information, and information related to acquisition and logistics to identify acquisitions and disposals.

## 1.P. Advances and Prepayments

The Army General Fund records payments in advance of the receipt of goods and services as advances or prepayments and reports them as assets on the Balance Sheet. The Army General Fund recognizes advances and prepayments as expenses when it receives the related goods and services.

## 1.Q. Leases

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

Office space and leases entered into by the Army General Fund in support of contingency operations are the largest component of operating leases. These costs were gathered from existing leases, General Service Administration (GSA) bills and Inter-service Support Agreements.

Future year projections use the Consumer Price Index (CPI), rather than the DoD inflation factor. The CPI impacts increases to the leases, especially those at commercial lease sites. Equipment leases have a variety of lease terms which are not expected to be renewed upon expiration. Other operating leases are generally one-year leases. The Army General Fund expects to continue to reduce the level of owned assets while increasing the number of leased assets. The Army General Fund will strive to replace commercial leases with more economical GSA leases.

## **1.R. Other Assets**

The Army General Fund conducts business with commercial contractors under two primary types of contracts: fixed price and cost reimbursable. To alleviate the potential financial burden on the contractor that long-term contracts can cause, the Army General Fund provides financing payments. One type of financing payment that the Army General Fund makes for real property is based upon a percentage of completion. In accordance with the SFFAS No. 1, "Accounting for Selected Assets and Liabilities," such payments are treated as construction in process and are reported on the General PP&E line on the Balance Sheet and in the related note.

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

Contract financing payments are defined in the Federal Acquisition Regulations (FAR), Part 32, as authorized disbursements of monies to a contractor prior to acceptance of supplies or services by the Government. These payments are designed to alleviate the potential financial burden on contractors performing on certain long-term contracts and facilitate competition for defense contracts. Contract financing payments clauses are incorporated in the contract terms and conditions and may include advance payments, performance-based payments, commercial advance and interim payments, progress payments based on cost, and interim payments under certain cost-reimbursement contracts. Contract financing payments do not include invoice payments, payments for partial deliveries, lease and rental payments, or progress payments based on a percentage or stage of completion, which the Defense Federal Acquisitions Regulations Supplement (DFARS) authorizes only for construction of real property, shipbuilding, and ship conversion, alteration, or repair. Progress payments for real property and ships are reported as Construction in Progress in Note 10.

## **1.S. Contingencies and Other Liabilities**

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

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

Other liabilities arise as a result of anticipated disposal costs for the Army General Fund's assets. This type of liability has two components: nonenvironmental and environmental. Consistent with SFFAS No. 6, "Accounting for Property, Plant, and Equipment," recognition of an anticipated environmental disposal liability begins when the asset is placed into service. Nonenvironmental disposal liabilities are recognized when management decides to dispose of an asset based upon the DoD's policy, which is consistent with SFFAS No. 5, "Accounting for Liabilities of Federal Government." The DoD recognizes nonenvironmental disposal liabilities for military equipment nuclear-powered assets when placed into service. Such amounts are developed in conjunction with, and not easily identifiable separately from, environmental disposal costs.

### **1.T. Accrued Leave**

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

### **1.U. Net Position**

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

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

Cumulative Results of Operations represent the net difference, since inception of an activity, between expenses and losses and financing sources (including appropriations, revenue, and gains). Beginning with FY 1998, the cumulative results also include donations and transfer in and out of assets without reimbursement.

### **1.V. Treaties for Use of Foreign Bases**

The Army General Fund has the use of land, building, and other overseas facilities that are obtained through various international treaties and agreements negotiated by the Department of State. The Army General Fund purchases capital assets overseas with appropriated funds; however, the host country retains title to land and improvements. Generally, treaty terms allow the Army General Fund continued use of these properties until the treaties expire. In the event treaties or other agreements are terminated, whereby use of the foreign bases is prohibited, losses are recorded for the value of any nonretrievable capital assets. This takes place after negotiations between the U.S. and the host country have determined the amount to be paid the U.S. for such capital investments.

### **1.W. Comparative Data**

Balance Sheet and Statement of Net Cost fluctuations greater than two percent of total assets on the Balance Sheet or ten percent from the prior period presented are explained within the notes to the financial statements.

### **1.X. Unexpended Obligations**

The Army General Fund 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. In-transit payments are those payments that have been made to other agencies or entities that have not been recorded in their accounting records. These payments are applied to the entities' outstanding accounts payable balance. In-transit collections are those collections from other agencies or entities that have not been recorded in the accounting records. These collections are also applied to the entities' accounts receivable balance.

The DoD policy is to allocate supported undistributed disbursements and collections between federal and nonfederal categories based on the percentage of 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 Army General Fund follows this procedure. Unsupported undistributed collections and disbursements represent collections and disbursements that are not in agreement with accounting records. These are normally reconciled in the following month.

### **1.Z. Development Fund for Iraq**

On June 28, 2004, transfer of power from the Coalition Provisional Authority (CPA) to the Interim Iraqi Government (IIG) occurred. Prior to the transfer, the CPA was responsible for the management and accounting of the Development Fund for Iraq (DFI). Ongoing resolution of issues surrounding transfers of approximately \$1.7 billion of DFI assets, including \$86 million transferred from IIG to the Multi-National Force-Iraq in August 2004, will require additional disclosure in future financial statements. The Army General Fund has established a plan to reconcile and account for these amounts and record DFI funds received. As of the 4th Quarter, FY 2006, Army General Fund has reconciled the \$86 million transferred from IIG. The Army General Fund has recorded a total of \$136 million in DFI assets, which includes the \$86 million reconciled and a \$50 million transfer in 1st Quarter, FY 2005. See Note 22 for additional discussion on DFI.

## Note 2. Nonentity Assets

As of September 30	2006		2005	
<i>(Amounts in thousands)</i>				
1. Intragovernmental Assets				
A. Fund Balance with Treasury	\$	202,731	\$	294,283
B. Accounts Receivable		0		0
C. Total Intragovernmental Assets	\$	202,731	\$	294,283
2. Nonfederal Assets				
A. Cash and Other Monetary Assets	\$	1,784,810	\$	1,482,046
B. Accounts Receivable		50,670		53,773
C. Other Assets		0		0
D. Total Nonfederal Assets	\$	1,835,480	\$	1,535,819
3. Total Nonentity Assets	\$	2,038,211	\$	1,830,102
4. Total Entity Assets	\$	224,547,274	\$	207,554,225
5. Total Assets	\$	226,585,485	\$	209,384,327

### Fluctuations and/or Abnormalities

Total Nonentity Assets increased \$208.1 million, or 11 percent, from FY 2005 to FY 2006 primarily caused by an increase in cash and other monetary assets, which increased \$302.8 million due to advances from the Republic of Korea received during FY 2006 for engineering and construction work to be done by the U.S. Army Corps of Engineers. In addition, Fund Balance with Treasury decreased \$91.6 million, or 31 percent, from FY 2005 to FY 2006 due to decreases in Nonentity Seized Iraqi Cash and Nonentity Other.

Fund Balance with Treasury Nonentity Seized Iraqi Cash decreased \$31.2 million, or 51 percent from FY 2005 to FY 2006 due to disbursements in support of the Iraqi people throughout the fiscal year. Disbursements will continue until all cash is liquidated. A breakout of the disbursements is reflected in Note 22.

Fund Balance with Treasury Nonentity Other includes development funds for Iraq and deposit funds. Fund Balance with Treasury Nonentity Other decreased \$60.4 million, or 26 percent, from FY 2005 to FY 2006, primarily caused by a decrease in the Army Member Savings Deposit accounts of \$91.4 million as a result of transferring accrued funds to the account steward, the Department of the Navy, in 4th Quarter, FY 2006. The Department of the Navy is responsible for making the disbursements to the military service members. In addition, the Army General Fund implemented Office of the Secretary of Defense guidance to reclassify Thrift Savings Plan suspense accounts as nonentity in 3rd Quarter, FY 2006 resulting in a \$31.3 million increase.

### Definitions

Nonentity assets are assets for which the Army General Fund maintains stewardship accountability and responsibility to report, but are not available for the Army General Fund's operation.

Nonentity Fund Balance with Treasury consists of deposit funds, seized Iraqi cash and development fund for Iraq. Deposit funds are generally used to record amounts held temporarily until paid to the appropriate government or public entity. Seized Iraqi cash is former Iraqi regime monies confiscated by coalition forces. The development fund for Iraq consists of proceeds from Iraqi oil sales, repatriated assets from the United States and other nations, and deposits from unencumbered oil-for-food program funds.

Nonentity Cash and Other Monetary Assets consist of cash held by disbursing officers to carry out their paying, collecting, and foreign currency accommodation exchange missions. Foreign currency is valued using the Department of the Treasury prevailing rate of exchange.

Nonentity Nonfederal Accounts Receivable are primarily from cancelled year appropriations. These receivables will be returned to the Department of the Treasury as miscellaneous receipts once collected.

### Note 3. Fund Balance with Treasury

As of September 30	2006	2005
<i>(Amounts in thousands)</i>		
1. Fund Balances		
A. Appropriated Funds	\$ 94,368,206	\$ 86,709,695
B. Revolving Funds	19,851	47,069
C. Trust Funds	1,051	798
D. Special Funds	41,090	41,472
E. Other Fund Types	202,731	294,283
F. Total Fund Balances	\$ 94,632,929	\$ 87,093,317
2. Fund Balances Per Treasury Versus Agency		
A. Fund Balance per Treasury	\$ 95,471,092	\$ 87,794,995
B. Fund Balance per Army	94,632,929	87,093,317
3. Reconciling Amount	\$ 838,163	\$ 701,678

#### Fluctuations and/or Abnormalities

Entity Fund Balance with Treasury increased \$7.6 billion, or 9 percent, from FY 2005 to FY 2006 primarily due to an increase in the DoD appropriations received in FY 2006. Appropriations received increased to ensure that resources, equipment, and supplies remain available without interruption in support of Operation Iraqi Freedom and Operation Enduring Freedom. The increase also funds an increase in military basic pay and in basic allowance for housing. Finally, the increase provides funds for the procurement of equipment to address immediate shortfalls for the National Guard and Reserve, for armor and personal protection equipment, and training and equipment for Afghan and Iraqi Security Forces.

#### Reconciling Amount

The Department of the Treasury reports an additional \$838.2 million in Fund Balance with Treasury than reported by the Army General Fund. This includes \$702.9 million in canceling year authority, \$164.9 million in unavailable receipts, and \$30.6 million in a transfer fund where Army General Fund executes the funding on behalf of the Executive Office of the President and the Department of Transportation that is not included in Army General Fund's Fund Balance with Treasury. In addition, \$60.2 million in transfer funds are reported by the Department of the Treasury under the Department of Transportation and Department of Agriculture whereas the Army General Fund includes these funds in its Treasury balance.

#### Vested Iraqi Cash

The Army General Fund has collected \$1.7 billion of Vested Iraqi Cash which is included in the \$94.4 billion in appropriated funds. These funds are Iraqi funds in U.S. banks that were frozen by Executive Order, vested in the Department of the Treasury and authorized for use to benefit the people of Iraq. The Army General Fund disbursed \$1.7 billion in support of the Iraqi people as follows:

Vested Iraqi Cash	Amount
<i>(Amounts in thousands)</i>	
	\$1,724,131
<b>Collected</b>	
<b>Disbursed</b>	
Iraqi Salaries	\$1,184,791
Repair/Reconstruction/Humanitarian Assistance	148,923
Iraqi Ministry Operations (Ministry of Finance, Defense, etc.)	356,818
Total Disbursed	\$1,690,532
<b>Remaining Funds</b>	\$33,599

### Other Fund Types

Other Fund Types consists of deposit funds, seized Iraqi cash and development fund for Iraq. Deposit funds are generally used to record amounts held temporarily until paid to the appropriate government or public entity. Seized Iraqi cash is former Iraqi regime monies confiscated by coalition forces. The development fund for Iraq consists of proceeds from Iraqi oil sales, repatriated assets from the United States and other nations, and deposits from unencumbered oil-for-food program funds.

### Canceling Appropriated Funds

As of September 2006, the Army withdrew \$702.9 million in canceling appropriated funds in accordance with the Department of the Treasury's policy.

### Status of Fund Balance with Treasury

As of September 30	2006		2005	
<i>(Amounts in thousands)</i>				
1. Unobligated Balance				
A. Available	\$	14,884,671	\$	13,678,958
B. Unavailable		2,140,616		1,799,859
2. Obligated Balance not yet Disbursed	\$	90,155,105	\$	80,720,880
3. Nonbudgetary FBWT	\$	4,592,476	\$	7,250,455
4. NonFBWT Budgetary Accounts	\$	(17,139,939)	\$	(16,354,933)
5. Total	\$	94,632,929	\$	87,095,219

### Fluctuations and/or Abnormalities

Total Status of Fund Balance with Treasury increased \$7.5 billion, or 9 percent, from FY 2005 to FY 2006 primarily due to increased appropriations received in FY 2006. Appropriations received increased in Army General Fund's operation and maintenance to fully fund key readiness programs critical to the Global War on Terror, in military pay due to an overall pay increase and an increase in basic allowance for housing to eliminate out-of-pocket expenses for military personnel, and for the procurement of equipment to address immediate shortfalls for the National Guard and Reserve.

### Definitions

The Status of Fund Balance with Treasury consists of unobligated and obligated balances. These balances reflect the budgetary authority remaining for disbursements against current or future obligations. In addition, the Status includes various accounts that affect either budgetary reporting or Fund Balance with Treasury, but not both.

Unobligated Balance represents the cumulative amount of budgetary authority that has not been set aside to cover outstanding obligations. Unobligated Balance is classified as available or unavailable and is associated with appropriations expiring at fiscal year end that remain available only for obligation adjustments until the account is closed. The Army General Fund does not have any restrictions on unobligated balances.

Obligated Balance not yet Disbursed represents funds that have been obligated for goods that have not been received or services that have not been performed.

Nonbudgetary Fund Balance with Treasury includes entity and nonentity Fund Balance with Treasury accounts which do not have budgetary authority, such as unavailable receipt accounts or clearing accounts.

Non-Fund Balance with Treasury Budgetary Accounts include budgetary accounts that do not affect Fund Balance with Treasury, such as contract authority, borrowing authority, and investment accounts. This category reduces the Status of Fund Balance with Treasury.

## Disclosures Related to Suspense/Budget Clearing Accounts

As of September 30	2004	2005	2006	(Decrease)/ Increase from FY 2005 - 2006
<i>(Amounts in thousands)</i>				
Account				
F3845 – Personal Property Proceeds	\$ 0	\$ 931	\$ 360	\$ (571)
F3875 – Disbursing Officer Suspense	0	(27,176)	555,556	582,732
F3880 – Lost or Cancelled Treasury Checks	0	7,973	19,311	11,338
F3882 – Uniformed Services Thrift Savings Plan Suspense	(820)	25,084	31,181	6,097
F3885 – Interfund/IPAC Suspense	0	(36,501)	(24,652)	11,849
F3886 – Thrift Savings Plan Suspense	187	117	72	( 45)
Total	\$ (633)	\$ (29,572)	\$ 581,828	\$ 611,400

### Fluctuations and/or Abnormalities

Suspense/Budget Clearing accounts increased \$611.4 million, or 2,070 percent, from FY 2005 to FY 2006 primarily due to the \$582.7 million increase in F3875 caused by a timing difference in the disbursement of military and civilian payroll taxes. In 4th Quarter, FY 2006, this account included individual income and Federal Insurance Contributions Act (FICA) tax withholdings, whereas 4th Quarter, FY 2005 payroll tax withholdings were disbursed prior to the end of the accounting period. Disbursement for the payroll withholdings related to individual income and FICA tax for FY 2006 is expected in October 2006.

A substantial amount of increases/decreases in the suspense accounts from FY 2004 to FY 2005, reflects a change in year end recording. In the past, at the end of each fiscal year most suspense/budget clearing accounts were reduced to zero (as required by the Department of the Treasury) by transferring the balances to proper appropriation accounts. For FY 2005 the Office of Management and Budget requested the departments to not reduce the budget clearing accounts to zero at year end.

The Army General Fund transferred the following accounts to their Operation and Maintenance Account for FY 2004 (amounts in thousands):

Accounts	FY 2004
<i>(Amounts in thousands)</i>	
F3845 Personal Property Proceeds	\$3,805
F3875 Disbursing Officer Suspense	37,389
F3880 Lost or Cancelled Treasury Checks	33,815
F3885 Interfund/IPAC Suspense	(18,896)

### Definitions

The F3845 suspense account represents the balance of proceeds from the sale of personal property.

The F3875 suspense clearing account represents the Disbursing Officer's suspense, which includes military pay's Federal Income tax withholding monies.

The F3880 suspense account represents the balance of Treasury checks that have either been lost by the payee and need to be reissued, have never been cashed by the payee, or have been cancelled by the Department of the Treasury and need to be transferred to the original appropriation.

The F3882 suspense account was established for the Uniformed Services Thrift Savings Plan in FY 2002. The amounts in this account represent a timing difference between the posting of the Thrift Savings Plan deductions by the National Finance Center and the posting of these amounts in the military accounting systems in the following month.

The F3885 suspense account includes the Interfund and Intragovernmental Payment and Collections (IPAC) suspense.

The F3886 suspense account includes payroll deductions for civilian employees Thrift Savings Plan.

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

As of September 30	2004	2005	2006	(Decrease)/ Increase from FY 2005 to 2006
<i>(Amounts in thousands)</i>				
1. Total Problem Disbursements, Absolute Value				
A. Unmatched Disbursements (UMDs)	\$ 69,858	\$ 120,703	\$ 44,409	(76,294)
B. Negative Unliquidated Obligations (NULO)	24,424	20,927	15,445	(5,482)
2. Total In-transit Disbursements, Net	\$ 1,652,211	\$ 1,143,441	\$ 1,942,899	799,458

### Fluctuations and/or Abnormalities

Absolute UMDs decreased \$76.3 million, or 63 percent, from FY 2005 to FY 2006 primarily due to a change in process in FY 2006 where contingency disbursing stations in Iraq and Kuwait process payments via an electronic file rather than shipping vouchers via postal service. Consequently, the unmatched disbursements decreased due to the enhanced timing of posting disbursements into the accounting system and with the Department of the Treasury. In addition, changes were completed to an Automatic Reject Control System during FY 2006, which led to quicker isolation of problems, implementation of corrective actions, and an increase of the automatic posting rate of Mechanization of Contract Administration Services disbursements.

Absolute NULO decreased \$5.5 million, or 26 percent, from FY 2005 to FY 2006 primarily due to Military Pay operations change in procedure in 1st Quarter, FY 2006 to report obligations by the specific fiscal station, as opposed to open allotment level allowing more oversight of obligations at a detailed level.

Net In-transit disbursements increased \$799.5 million, or 70 percent, from FY 2005 to FY 2006 primarily due to Mechanization of Contract Administration Services files for payments received that did not get loaded into the accounting system before September 30, 2006.

### Definitions

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

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

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

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

### Aged UMDs, NULOs, and In-transits

The Army General Fund absolute value UMDs, NULOs, and \$8.8 million in aged in-transit disbursements represent problem disbursements. UMDs and NULOs are considered to be problem disbursements immediately, while in-transits are considered normal business activity up to the 30-day aging category. After 30 days, they are considered problem disbursements.

### Problem disbursements related to Foreign Military Sales

In FY 2006, Army General Fund problem disbursements included \$9.5 thousand, \$799.5 million, and \$2.3 billion in UMDs, NULOs, and total in-transit disbursements, respectively, that are associated with foreign military sales.



## Note 4. Investments and Related Interest

As of September 30	2006				
	Cost	Amortization Method	Amortized (Premium) / Discount	Investments, Net	Market Value Disclosure
<i>(Amounts in thousands)</i>					
1. Intragovernmental Securities					
A. Nonmarketable, Market-Based	\$ 3,337	Effective interest	\$ 46	\$ 3,383	\$ 3,380
B. Accrued Interest	24			24	24
C. Total Intragovernmental Securities	<u>\$ 3,361</u>		<u>\$ 46</u>	<u>\$ 3,407</u>	<u>\$ 3,404</u>
2. Other Investments					
A. Total Investments	<u>\$ 0</u>		<u>\$ 0</u>	<u>\$ 0</u>	<u>N/A</u>
3. Intragovernmental Securities					
A. Nonmarketable, Market-Based	\$ 3,463	Effective interest	\$ 14	\$ 3,477	\$ 3,471
B. Accrued Interest	18			18	18
C. Total Intragovernmental Securities	<u>\$ 3,481</u>		<u>\$ 14</u>	<u>\$ 3,495</u>	<u>\$ 3,489</u>

### Relevant Information for Comprehension

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

The Federal Government does not set aside assets to pay future benefits or other expenditures associated with earmarked funds. The cash receipts collected from the public for an earmarked fund are deposited in the Department of the Treasury, which uses the cash for general government purposes. The Department of the Treasury securities are issued to the Army General Fund as evidence of its receipts. Treasury securities are an asset to the Army General Fund and a liability to the Department of the Treasury. Because the Army General Fund and the Department of the Treasury are both parts of the Government, these assets and liabilities offset each other from the standpoint of the government as a whole. For this reason, they do not represent an asset or a liability in the U.S. Government-wide financial statements. The Department of the Treasury securities provides the Army General Fund with authority to draw upon the Department of the Treasury to make future benefit payments or other expenditures. When Army General Fund requires redemption of these securities to make expenditures, the government finances those expenditures out of accumulated cash balances, by raising taxes or other receipts, by borrowing from the public or repaying less debt, or by curtailing other expenditures. This is the same way that the government finances all other expenditures.

## Note 5. Accounts Receivable

As of September 30	2006			2005
	Gross Amount Due	Allowance For Estimated Uncollectibles	Accounts Receivable, Net	Accounts Receivable, Net
<i>(Amounts in thousands)</i>				
1. Intragovernmental Receivables	\$ 357,182	\$ N/A	\$ 357,182	\$ 276,634
2. Nonfederal Receivables (From the Public)	\$ 752,367	\$ (124,646)	\$ 627,721	\$ 584,005
3. Total Accounts Receivable	<u>\$ 1,109,549</u>	<u>\$ (124,646)</u>	<u>\$ 984,903</u>	<u>\$ 860,639</u>

### Fluctuations and/or Abnormalities

Intragovernmental Receivables increased \$80.5 million, or 29 percent, from FY 2005 to FY 2006 primarily due to a \$90 million increase with Defense Agencies. The receivables with Defense Agencies increased due to research and development performed for advanced component

prototypes in support of Soldier Biological and Chemical Command and due to increases in operation support for land force readiness, specifically base operations during FY 2006. Army General Fund can not identify the specific Defense Agency associated with the increases due to the implementation of a change in allocation methodology for intragovernmental receivables to Defense Agencies in 1st Quarter, FY 2006.

**Relevant Information for Comprehension**

Non-Federal Receivables (from the Public) consists of accounts receivable, refunds receivable, claims receivable, and interest receivable. The following schedule illustrates the major contributors to Gross Amount Due from Non-Federal Accounts Receivable (from the Public), by type of debt:

Type of Debt	
<i>(Amounts in thousands)</i>	
Military Pay (In Service Debt Only)	\$124,103
Civilian Pay (In Service Debt Only)	34,311
Individual Out-of-Service	198,197
Contractor Debt	128,734
Vendor Debt	1,194
Non Appropriated Funds	40,890
Foreign Military Sales (FMS)	29,930
Non FMS Foreign Government Indebtedness	71,695
Sales of Goods & Services (Excluding Referrals to CDS - Columbus)	30,295
Interest, Penalty and Administrative	38,230
Other	54,813
Subtotal	<u>\$752,392</u>
Undistributed Collections Public	(25)
Gross Non-Federal Accounts Receivable (Public)	<u><u>\$752,367</u></u>

## Aged Accounts Receivable

As of September 30	2006		2005	
	Intragovernmental	Nonfederal	Intragovernmental	Nonfederal
<i>(Amounts in thousands)</i>				
CATEGORY				
Nondelinquent				
Current	\$ 1,311,916	\$ 454,202	\$ 1,168,045	\$ 386,915
Noncurrent	0	0	0	0
Delinquent				
1 to 30 days	\$ 1,400	\$ 1,270	\$ 29,384	\$ 4,772
31 to 60 days	834	10,481	570	10,910
61 to 90 days	2,486	20,184	5,137	28,836
91 to 180 days	4,042	25,401	9,303	68,398
181 days to 1 year	6,506	20,895	2,756	103,908
Greater than 1 year and less than or equal to 2 years	2,714	40,034	207	54,541
Greater than 2 years and less than or equal to 6 years	0	51,565	0	39,808
Greater than 6 years and less than or equal to 10 years	0	117,830	0	67,020
Greater than 10 years	0	10,528	0	7,664
Subtotal	\$ 1,329,898	\$ 752,390	\$ 1,215,402	\$ 772,772
Less Supported Undistributed Collections	(35,470)	(23)	52,512	(63,039)
Less Eliminations	(937,246)	0	(991,280)	0
Less Other	0	0	0	0
Total	\$ 357,182	\$ 752,367	\$ 276,634	\$ 709,733

Nondelinquent accounts receivable are receivables not yet due under the contract or billing documents pertaining to the receivable. Current nondelinquent accounts receivable are those that are due in the next 12 months. Noncurrent nondelinquent accounts receivable are those amounts that are due beyond the next 12 months. Delinquent accounts receivable are aged from the date the account is considered delinquent as outlined in the DoD Financial Management Regulations.

The majority of intragovernmental accounts receivable are in current status. Of the \$18 million delinquent, \$10 million is related to debt with the other DoD entities, \$8 million is related to a charge back for lack of or improper documentation from the Federal Emergency Management Agency (FEMA), and \$1 million has been identified to the U.S. Coast Guard Medical Facilities. The DoD entities are receiving monthly 30 day delinquent notices until receivables are collected. Documentation is being collected for resubmission of the bills to FEMA. The Coast Guard payment process takes about eight weeks and is expected in early FY 2007.

The majority of nonfederal accounts receivable are in current status. Of the \$298.2 million delinquent, \$86.9 million is in litigation with the Deferment/Contract Appeals Board, \$159.6 million is in the Department of the Treasury's litigation board, \$5 million in bankruptcy court, \$1.4 million at the Department of Justice and \$45.3 million being actively pursued by Army with expected collection during the 1st Quarter, FY 2007.

The abnormal Supported Undistributed Collections of \$52.5 million reported in FY 2005 intragovernmental receivables represents an accounting error that was corrected in FY 2006.

## Note 6. Other Assets

As of September 30	2006	2005
<i>(Amounts in thousands)</i>		
1. Intragovernmental Other Assets		
A. Advances and Prepayments	\$ 601,861	\$ 824,303
B. Other Assets	0	0
C. Total Intragovernmental Other Assets	\$ 601,861	\$ 824,303
2. Nonfederal Other Assets		
A. Outstanding Contract Financing Payments	\$ 5,310,457	\$ 3,470,563
B. Other Assets (With the Public)	384,228	373,961
C. Total Nonfederal Other Assets	\$ 5,694,685	\$ 3,844,524
3. Total Other Assets	\$ 6,296,546	\$ 4,668,827

### Fluctuation and/or Abnormalities

Intragovernmental advances and prepayments decreased \$222.4 million, or 27 percent, from FY 2005 to FY 2006. The entire decrease is a result of advances with the Department of Interior. Based on a DoD review of Department of Interior's advances, advances were returned to the Army General Fund during the 3rd Quarter, FY 2006.

Nonfederal Other Assets increased \$1.9 billion, or 48 percent, from FY 2005 to FY 2006 primarily due to \$1.1 billion in outstanding contract financing payments for the procurement of Patriot Missiles and Bradley Combat Vehicles in support of the Global War on Terror during FY 2006 and \$780.5 million in Mechanization of Contract Administration Services contingent financing payments first recorded in the 4th Quarter, FY 2006.

Other Assets (with the public) largely consists of military pay and travel advances.

### Other Relevant Information

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

The Contract Financing Payment balance of \$5.3 billion is comprised of \$4.5 billion in contract financing payments and an additional \$780.5 million in estimated future payments that will be paid to the contractor upon future delivery and Government acceptance of a satisfactory product.

## Note 7. Cash and Other Monetary Assets

As of September 30	2006	2005
<i>(Amounts in thousands)</i>		
1. Cash	\$ 980,861	\$ 1,010,331
2. Foreign Currency	803,949	471,715
3. Total Cash, Foreign Currency, & Other Monetary Assets	\$ 1,784,810	\$ 1,482,046

**Fluctuations and/or Abnormalities**

Cash and Other Monetary Assets increased \$302.8 million, or 20 percent, from FY 2005 to FY 2006 due to an increase in advances from the Republic of Korea for engineering and construction work to be done by the U.S. Army Corps of Engineers. Construction projects include upgrading electrical systems, water and sewer systems, housing, schools, fences, and bridges on various bases in Korea. The first increase occurred in 3rd Quarter, FY 2006 with the receipt of an advance of \$249.6 million with the remaining advance of \$125.2 million occurring in 4th Quarter, FY 2006. Disbursements of \$41.6 million and \$9.0 million were incurred against these advances in the 3rd and 4th Quarters respectively resulting in the net increase of \$324.2 million.

**Definitions**

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

**Foreign Currency** – The total U.S. dollar equivalent of purchased and non-purchased foreign currencies held in foreign currency fund accounts.

**Other Monetary Assets - 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 and is not used by Army General Fund.

**Other Information Related to Cash and Other Monetary Assets**

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

**Breakdown of Cash**

Cash and foreign currency are broken down into the elements shown in the table below:

Breakdown of Cash	U.S. \$ / Negotiable Instruments	Foreign Currency
<i>(Amounts in thousands)</i>		
Cash on Deposit in Bank	\$240,019	\$802,170
Cash on Hand	256,305	985
Cash – Undeposited Collections	74	0
Custody of Contingency Cash	885	0
Cash in Transit	17,626	0
Cash – Other	3,298	0
Cash adjustments	2,195	0
Total Cash on Hand	\$520,402	\$803,155
Total Cash in Custody of Agents	460,459	794
Total Cash	\$980,861	\$803,949

The amount reported as Cash in the Custody of Agents, \$461.3 million, reflects cash provided to the disbursing agents. However, due to inherent timing differences based on location, this amount is not properly reduced by agent disbursements thus causing the Disbursing Officer's cash to be subject to overstatement.

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

As of September 30

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

The Federal Credit Reform Act of 1990 governs all amended loan guarantee commitments made after FY 1991 resulting in loan guarantees.

Loan guarantee liabilities are reported at the net present value. The cost of the loan guarantee is the net present value of the following estimated projected cash flows:

- Payments by the Department to cover defaults and delinquencies, interest subsidies, or other payments; offset by
- Payments to the Department including origination and other fees, penalties and recoveries.

### **Armament Retooling and Manufacturing Support Initiative**

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

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

### **Direct Loans Obligated After FY 1991**

Not applicable.

### **Total Amount of Direct Loans Disbursed**

Not applicable.

### **Subsidy Expense for Post FY 1991 Direct Loan**

Not applicable.

### **Subsidy Rate for Direct Loans**

Not applicable.

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

Not applicable.

### **Defaulted Guaranteed Loans from Post FY 1991 Guarantees**

Not applicable.

**Guaranteed Loans Outstanding**

As of September 30	Outstanding Principal of Guaranteed Loans, Face Value	Amount of Outstanding Principal Guaranteed
<i>(Amounts in thousands)</i>		
Guaranteed Loans Outstanding		
1. Military Housing Privatization Initiative	\$ 0	\$ 0
2. Armament Retooling & Manufacturing Support Initiative	\$ 20,508	\$ 18,232
3. Total	\$ 20,508	\$ 18,232
<b>2006</b>		
New Guaranteed Loans Disbursed		
1. Military Housing Privatization Initiative	\$ 0	\$ 0
2. Armament Retooling & Manufacturing Support Initiative	\$ 2,694	\$ 2,290
3. Total	\$ 2,694	\$ 2,290
<b>2005</b>		
New Guaranteed Loans Disbursed		
1. Military Housing Privatization Initiative	\$ 0	\$ 0
2. Armament Retooling & Manufacturing Support Initiative	\$ 740	\$ 629
3. Total	\$ 740	\$ 629

The FY 2005 disbursements of \$740 thousand and \$629 thousand are due to an FY 2005 loan closing and disbursement of an FY 2004 loan obligation. The FY 2006 disbursements of \$2.7 million and \$2.3 million are due to disbursements on loan obligations incurred in prior years.

**Liabilities for Post FY 1991 Loan Guarantees, Present Value**

As of September 30	2006	2005
<i>(Amounts in thousands)</i>		
Loan Guarantee Program(s)		
1. Military Housing Privatization Initiative	\$ 0	\$ 0
2. Armament Retooling & Manufacturing Support Initiative	12,853	12,394
3. Total	\$ 12,853	\$ 12,394

## Subsidy Expense for Post FY 1991 Loan Guarantees

As of September 30

(Amounts in thousands)

2006	Interest Differential	Defaults	Fees	Other	Total
<b>1. New Loan Guarantees</b>					
Disbursed:					
Military Housing Privatization Initiative	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
Armament Retooling & Manufacturing Support Initiative	0	0	0	0	0
<b>Total</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 0</b>
2005	Interest Differential	Defaults	Fees	Other	Total
<b>2. New Loan Guarantees</b>					
Disbursed:					
Military Housing Privatization Initiative	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
Armament Retooling & Manufacturing Support Initiative	0	0	0	0	0
<b>Total</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 0</b>
2006	Modifications	Interest Rate Reestimates	Technical Reestimates	Total Reestimates	Total
<b>3. Modifications and Reestimates:</b>					
Military Housing Privatization Initiative	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
Armament Retooling & Manufacturing Support Initiative	0	162	11,532	11,694	11,694
<b>Total</b>	<b>\$ 0</b>	<b>\$ 162</b>	<b>\$ 11,532</b>	<b>\$ 11,694</b>	<b>\$ 11,694</b>
2005	Modifications	Interest Rate Reestimates	Technical Reestimates	Total Reestimates	Total
<b>4. Modifications and Reestimates:</b>					
Military Housing Privatization Initiative	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
Armament Retooling & Manufacturing Support Initiative	0	0	0	0	0
<b>Total</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 0</b>
<b>5. Total Loan Guarantee:</b>					
Military Housing Privatization Initiative	\$ 0	\$ 0			
Armament Retooling & Manufacturing Support Initiative	11,694	0			
<b>Total</b>	<b>\$ 11,694</b>	<b>\$ 0</b>			



The increase of \$162 thousand for Interest Rate Reestimates and \$11.5 million for Technical Reestimates for FY 2006 are for an impending loss claim for a guaranteed loan that was defaulted in September 2006.

### Subsidy Rates for Loan Guarantees

As of September 30	Interest Supplements	Defaults	Fees and other Collections	Other	Total
<i>(Amounts in thousands)</i>					
Loan Guarantee Programs:					
1. Military Housing Privatization Initiative	0.00%	0.00%	0.00%	0.00%	0.00%
2. Armament Retooling & Manufacturing Support Initiative	0.00%	20.00%	0.00%	0.00%	20.00%

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

As of September 30	2006	2005
<i>(Amounts in thousands)</i>		
1. Beginning Balance of the Loan Guarantee Liability	\$ 12,394	\$ 12,293
2. Add: Subsidy Expense for Guaranteed Loans Disbursed during the Reporting Years by Component		
A. Interest Supplement Costs	\$ 0	\$ 0
B. Default Costs (Net of Recoveries)	0	0
C. Fees and Other Collections	0	0
D. Other Subsidy Costs	0	0
E. Total of the above Subsidy Expense Components	\$ 0	\$ 0
3. Adjustments		
A. Loan Guarantee Modifications	\$ 0	\$ 0
B. Fees Received	0	60
C. Interest Supplements Paid	0	0
D. Foreclosed Property and Loans Acquired	0	0
E. Claim Payments to Lenders	(11,436)	0
F. Interest Accumulation on the Liability Balance	201	41
G. Other	0	0
H. Total of the above Adjustments	\$ (11,235)	\$ 101
4. Ending Balance of the Loan Guarantee Liability before Reestimates	\$ 1,159	\$ 12,394
5. Add or Subtract Subsidy Reestimates by Component		
A. Interest Rate Reestimate	162	0
B. Technical/default Reestimate	11,532	0
C. Total of the above Reestimate Components	\$ 11,694	\$ 0
6. Ending Balance of the Loan Guarantee Liability	\$ 12,853	\$ 12,394

The Fees Received decreased \$60 thousand, or 100 percent, from FY 2005 to FY 2006 due to FY 2005 guaranteed fees on the \$12 million in loan obligations that were not received in FY 2006.

The Claim Payments to Lenders increased \$11.4 million from FY 2005 to FY 2006 due to a January 2006 payment on a loss claim to a bank for a defaulted loan to make bullet casings.

The Interest Accumulation on the Liability Balance increased \$160 thousand from FY 2005 to FY 2006 due to the implementation of Department of the Treasury guidance to include an estimate of accrued interest revenue from the Department of the Treasury. The interest is calculated using the Department of Agriculture's consolidate credit tool.

The Reestimate Components increased \$11.7 million, or 100 percent, from FY 2005 to FY 2006 primarily due new impending loss claims for a guaranteed loan that was defaulted in September 2006.

## Administrative Expenses

Administrative Expense is limited to separately identified expenses administered to direct and guaranteed loans. Administrative Expense for the ARMS is a fee paid to the U.S. Department of Agriculture RBS for administering the loan guarantees under the ARMS, which is a joint program. There were no administrative expenses in FY 2006.

## Note 9. Inventory and Related Property

As of September 30	2006		2005	
<i>(Amounts in thousands)</i>				
1. Inventory, Net	\$	94,400	\$	109,586
2. Operating Materials & Supplies, Net		38,544,639		37,593,767
3. Stockpile Materials, Net		0		0
4. Total	\$	38,639,039	\$	37,703,353

## Inventory, Net

As of September 30	2006			2005	Valuation Method
	Inventory, Gross Value	Revaluation Allowance	Inventory, Net	Inventory, Net	
<i>(Amounts in thousands)</i>					
1. Inventory Categories					
A. Available and Purchased for Resale	\$ 18,549	\$ (554)	\$ 17,995	\$ 20,057	LAC
B. Held for Repair	0	0	0	0	
C. Excess, Obsolete, and Unserviceable	19	(19)	0	0	NRV
D. Raw Materials	0	0	0	0	
E. Work in Process	76,405	0	76,405	89,529	SP
F. Total	\$ 94,973	\$ (573)	\$ 94,400	\$ 109,586	

### 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

0 = Other

## Restrictions of Inventory Use, Sale, or Disposition

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

- Distributions without reimbursements made when authorized by DoD directives;
- War Reserve Materiel to include fuels and subsistence items that are considered restricted; and
- Inventory, with the exception of safety stocks, may be sold to foreign, state and local governments, private parties, and contractors in accordance with current policies and guidance or at the direction of The President.

**Other Information**

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

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

Excess, obsolete, and unserviceable inventory is condemned material that must be retained for management purposes. Work in Process includes munitions in production and depot maintenance work with its associated labor, applied overhead, and supplies used in the delivery of maintenance services. The U.S. Standard General Ledger does not include a separate Work in Process account unrelated to sales.

Managers determine which items are more costly to repair than replace. Items retained for management purposes are coded condemned. The net value of these items is zero, and is shown as excess, obsolete, and unserviceable. The category includes all material held for sale. Economically repairable material is categorized as held for repair.

The Army General Fund expects a year-to-year decrease in CAWCF Inventory as the program progresses toward its final closeout. The CAWCF program managers are uncertain as to the final closeout date. Effective September 30, 1998, CAWCF officially stopped the acceptance of new orders for the procurement of conventional ammunitions.

**Operating Materials and Supplies, Net**

As of September 30	2006			2005	Valuation Method
	OM&S Gross Value	Revaluation Allowance	OM&S, Net	OM&S, Net	
<i>(Amounts in thousands)</i>					
1. OM&S Categories					
A. Held for Use	\$ 38,544,639	\$ 0	\$ 38,544,639	\$ 37,593,767	LAC
B. Held for Repair	0	0	0	0	
C. Excess, Obsolete, and Unserviceable	295,578	(295,578)	0	0	SP
D. Total	\$ 38,840,217	\$ (295,578)	\$ 38,544,639	\$ 37,593,767	

**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

**Relevant Information for Comprehension**

Operating Material and Supplies (OM&S) includes spare and repair parts, ammunition, and tactical missiles. The Army General Fund reported \$3.0 billion of OM&S Held for Future Use. This amount represents ammunition held under a host nation treaty agreement and is not intended for use by U.S. Forces. The ammunition is intended for use in defense of the host nation by the host nation. The category Held for Use includes all material able to be issued. Economically repairable material is categorized as held for repair.

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

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

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

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

## Stockpile Materials, Net

Not applicable.

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

As of September 30	2006					2005
	Depreciation/ Amortization Method	Service Life	Acquisition Value	(Accumulated Depreciation/ Amortization)	Net Book Value	Prior FY Net Book Value
<i>(Amounts in thousands)</i>						
1. Major Asset Classes						
A. Land	N/A	N/A	\$ 515,882	\$ N/A	\$ 515,882	\$ 473,405
B. Buildings, Structures, and Facilities	S/L	20 or 40	45,256,045	(28,925,653)	16,330,392	15,420,688
C. Leasehold Improvements	S/L	lease term 2-5 or	14,431	(10,706)	3,725	2,618
D. Software	S/L	10	536,052	(246,355)	289,697	348,416
E. General Equipment	S/L	5 or 10	3,516,473	(2,386,277)	1,130,196	1,076,527
F. Military Equipment	S/L	various	97,915,799	(39,045,993)	58,869,806	53,890,902
G. Assets Under Capital Lease	S/L	lease term	166,617	(147,111)	19,506	28,002
H. Construction-in- Progress	N/A	N/A	7,064,762	N/A	7,064,762	6,246,266
I. Other			19,884	0	19,884	85,825
J. Total General PP&E			\$ 155,005,945	\$ (70,762,095)	\$ 84,243,850	\$ 77,572,649

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

#### Legend for Valuation Methods:

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

#### Fluctuations and/or Abnormalities

General property, plant and equipment increased \$6.7 billion, or 9 percent, from FY 2005 to FY 2006 primarily due to the change in evaluation method for military equipment. If the evaluation method for military equipment had not changed, military equipment would have increased \$1.7 billion for FY 2006.

The Department changed its method of valuing military equipment in 3rd Quarter, FY 2006. Previously, military equipment was valued using Bureau of Economic Analysis (BEA) data. Beginning with the 3rd Quarter, FY 2006, military equipment is valued based on internal records. The value of military equipment for the 4th Quarter, FY 2005 was restated from \$96.7 billion to \$53.9 billion for comparative purposes using the new valuation method.

For 4th Quarter, FY 2006, military equipment is valued at \$58.9 billion based on internal records. Under the previously used BEA valuation methodology, this equipment would have been valued at \$98.4 billion.

Other includes the projected value of forest product sales (timber reserve).

Currently, there are no restrictions for General PP&E.

#### Other Information Related to Heritage Assets and Stewardship Land

The mission of the DoD, including the Army General Fund, is to provide the military forces needed to deter war and protect the security of the United States by organizing, training, supplying, equipping and mobilizing forces for assignment in support of that mission. Executing the mission requires efficient and effective use of resources in a manner that ensures operational and environmental sustainability, while

respecting the history and heritage that reflect and support the military mission. The Army General Fund has stewardship responsibilities for Heritage Assets that date not only from the military history of the land, but from prior historic and prehistoric occupations. The Army General Fund relies upon Heritage Assets, such as historic buildings, and stewardship land for daily use in administration, housing, or training soldiers. Those heritage assets not currently employed as “multi-use,” such as archeological collections or museum collections, are important items that embody the multi-faceted history of the land, the military, the local communities, and the nation - the heritage that the Army defends.

The Army’s policy for managing cultural resources and heritage assets are published in Army Regulations 200-4, *Cultural Resources Management*, and 870-20, *Army Museums, Historical Artifacts, and Art*. These policies provide in-depth procedures for managing the Army’s cultural resources and museum collections. The Army regulations take into account the Army’s responsibilities under various legal compliance requirements such as the National Historic Preservation Act, the Native American Graves Protection and Repatriation Act, the National Environmental Policy Act, and the Archeological Resources Protection Act, among others. The regulations provide guidance to all Active Army, Army Reserves and National Guard units and installations as to the appropriate policies, responsibilities, procedures, and requirements affecting heritage assets. These policies are designed to ensure that Army installations and commanders make informed decisions regarding the cultural resources under their stewardship in compliance with public laws, in support of the military mission and consistent with sound principles of cultural resource management.

The DoD Financial Management Regulation defines the categories of heritage assets reported by each of the military services.

Heritage Assets are items that are distinguished by historical or natural significance; cultural, educational, or artistic importance; or significant architectural characteristics. Heritage Assets are expected to be preserved. Heritage Assets shall be reported within the following categories.

Museums: Buildings that house collection-type items including artwork, archeological artifacts, archival materials, and other historical artifacts. The primary use of such buildings shall be the preservation, maintenance, and display of the collection-type Heritage Assets.

Monuments and Memorials: Sites and structures built to honor and preserve the memory of significant individuals and/or events in history.

Cemeteries: Land on which gravesites of prominent historical figures are located.

Archeological Sites: Land on which items of significance are located.

Buildings and Structures: Includes buildings and structures that are listed on, or eligible for listing on the National Register of Historic Places, including Multi-use Heritage Assets. These are buildings other than those used as museums.

Major Collections: Significant collections that are maintained outside of a museum.

## Assets Under Capital Lease

As of September 30	2006		2005	
<i>(Amounts in thousands)</i>				
1. Entity as Lessee, Assets Under Capital Lease				
A. Land and Buildings	\$	166,071	\$	166,071
B. Equipment		546		546
C. Accumulated Amortization		(147,111)		(138,615)
D. Total Capital Leases	\$	19,506	\$	28,002

### Fluctuations and/or Abnormalities

Assets Under Capital Lease decreased by \$8.5 million, or 30 percent, from FY 2005 to FY 2006 due to straight-line amortization of leased assets during FY 2006.

### Relevant Information Related to Assets under Capital Lease

The Army General Fund is the lessee in eight Section 801 Family Housing Leases, which consist of two on-post and six off-post housing facilities. These leases have between one and seven years remaining on their terms. In addition, the Eighth U.S. Army G-3 Aviation leases equipment for a training simulator first reported in 3rd Quarter, FY 2005. As shown in Note 15, the Net Capital Lease Liability is \$33.1 million. Of that net, current liability is valued at \$11.8 million and non-current liability is \$21.3 million. The future executory and imputed interest costs, as shown in a combined form in Note 15 Capital Lease Liability section, are \$7.6 million and \$5.7 million, respectively. Future executory costs are estimates based on historical data. The imputed interest that was necessary to reduce the net minimum lease payments to the present value was calculated at the incremental borrowing rate at the inception of the leases.

## Note 11. Liabilities Not Covered by Budgetary Resources

As of September 30	2006		2005	
<i>(Amounts in thousands)</i>				
1. Intragovernmental Liabilities				
A. Accounts Payable	\$	0	\$	0
B. Debt		0		0
C. Other		472,874		473,993
D. Total Intragovernmental Liabilities	\$	472,874	\$	473,993
2. Nonfederal Liabilities				
A. Accounts Payable	\$	96,276	\$	90,204
B. Military Retirement and Other Federal Employment Benefits		1,461,098		1,663,650
C. Environmental Liabilities		41,662,756		38,399,062
D. Other Liabilities		4,493,222		4,357,513
E. Total Nonfederal Liabilities	\$	47,713,352	\$	44,510,429
3. Total Liabilities Not Covered by Budgetary Resources	\$	48,186,226	\$	44,984,422
4. Total Liabilities Covered by Budgetary Resources	\$	22,082,464	\$	17,281,633
5. Total Liabilities	\$	70,268,690	\$	62,266,055

### Relevant Information for Comprehension

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

### Intragovernmental Liabilities

Intragovernmental Liabilities Other represents liabilities associated with Federal Employees Compensation Act, unemployment benefits, and canceled accounts receivable.

### Nonfederal Liabilities

Nonfederal Liabilities Other represents unfunded annual leave, contingent liabilities, capital lease liabilities, and custodial liabilities.

Nonfederal Other Employment-Related Actuarial Liabilities represents the actuarial liability for Federal Employees Compensation Act.

## Note 12. Accounts Payable

As of September 30	2006			2005	
	Accounts Payable	Interest, Penalties, and Administrative Fees	Total	Total	
<i>(Amounts in thousands)</i>					
1. Intragovernmental Payables	\$ 1,593,783	\$ N/A	\$ 1,593,783	\$ 1,918,309	
2. Non-Federal Payables (to the Public)	10,884,188	74	10,884,262	10,137,011	
3. Total	\$ 12,477,971	\$ 74	\$ 12,478,045	\$ 12,055,320	

### Fluctuations and/or Abnormalities

Intragovernmental Payables with entities other than the Army General Fund decreased \$324.5 million, or 17 percent, from FY 2005 to FY 2006, primarily due to a \$227.2 million decrease with General Services Administration. During FY 2006, the Army General Fund

adjusted accounts payable to agree with the accounts receivable reported by General Services Administration and, therefore, does not have supporting records to determine the reason for the decrease. Efforts are underway to coordinate with General Services Administration to obtain proper documentation or adequate reconciliations.

### Definitions

Intragovernmental Payables consists of amounts owed to other federal agencies for goods or services ordered and received but not paid. Interest, penalties, and administrative fees are not applicable to intragovernmental payables.

Non-Federal payables (to the Public) are payables for debts owed to individuals and entities outside the federal government.

## Note 13. Debt

As of September 30 <i>(Amounts in thousands)</i>	2006			2005
	Beginning Balance	Net Borrowings	Ending Balance	Ending Balance
1. Agency Debt				
A. Debt to the Treasury	\$ 0	\$ 11,404	\$ 11,404	\$ 0
B. Debt to the Federal Financing Bank	0	0	0	0
C. Total Agency Debt	\$ 0	\$ 11,404	\$ 11,404	\$ 0
2. Total Debt	\$ 0	\$ 11,404	\$ 11,404	\$ 0

Debt to the Treasury increased \$11.4 million, or 100 percent, from FY 2005 to FY 2006 for borrowing authority received from the Department of the Treasury in 2nd Quarter, FY 2006 for a loan default related to the Armament Retooling and Manufacturing Support Initiative (ARMS). This initiative is designed to encourage commercial use of Army General Fund's inactive ammunition plants through many incentives for businesses willing to locate to a government ammunition production facility. The Army General Fund, by means of ARMS Initiative legislation, established a loan guarantee program to facilitate commercial firms' use of specified ammunition manufacturing facilities.

## Note 14. Environmental Liabilities and Disposal Liabilities

As of September 30	2006			2005
	Current Liability	Noncurrent Liability	Total	Total
<i>(Amounts in thousands)</i>				
1. Environmental Liabilities--Nonfederal				
A. Accrued Environmental Restoration Liabilities				
1. Active Installations—Installation Restoration Program (IRP) and Building Demolition and Debris Removal (BD/DR)	\$ 379,462	\$ 2,539,781	\$ 2,919,243	\$ 3,211,982
2. Active Installations—Military Munitions Response Program (MMRP)	19,216	3,298,574	3,317,790	5,182,734
3. Formerly Used Defense Sites—IRP and BD/DR	158,136	4,011,443	4,169,579	4,227,450
4. Formerly Used Defense Sites--MMRP	86,654	14,710,623	14,797,277	14,584,052
B. Other Accrued Environmental Liabilities—Active Installations				
1. Environmental Corrective Action	9,707	362,305	372,012	379,604
2. Environmental Closure Requirements	2,759	94,088	96,847	96,847
3. Environmental Response at Operational Ranges	6,490	297,596	304,086	304,087
4. Other	0	35,676	35,676	0
C. Base Realignment and Closure (BRAC)				
1. Installation Restoration Program	25,778	497,908	523,686	523,443
2. Military Munitions Response Program	10,670	789,642	800,312	634,093
3. Environmental Corrective Action / Closure Requirements	3,451	28,825	32,276	54,146
4. Other	149,165	0	149,165	112,026
D. Environmental Disposal for Weapons Systems Programs				
1. Nuclear Powered Aircraft Carriers	0	0	0	0
2. Nuclear Powered Submarines	0	0	0	0
3. Other Nuclear Powered Ships	0	0	0	0
4. Other National Defense Weapons Systems	0	0	0	0
5. Chemical Weapons Disposal Program	2,460,994	14,996,294	17,457,288	10,450,050
6. Other	0	0	0	0
2. Total Environmental Liabilities	\$ 3,312,482	\$ 41,662,755	\$ 44,975,237	\$ 39,760,514

### Other Disclosures

Others Category Disclosure Comparative Table	FY 2006	FY 2005
<i>(Amounts in thousands)</i>		
<b>Other Accrued Environmental Costs - Other</b>		
Low Level Radioactive Waste	\$35,676	\$0
<b>Base Realignment and Closure - Other</b>		
BRAC Unliquidated Liabilities that can not be categorized within BRAC program lines on Note 14	149,165	112,026
<b>Total</b>	<b>\$184,841</b>	<b>\$112,026</b>



Amounts are presented in the Note 14 Environmental Liabilities and Disposal Liabilities schedule. See Environmental Disclosures section of this note for additional information.

### Fluctuations and Abnormalities

#### Accrued Environmental Restoration Liabilities

Active Installations - Military Munitions Response Program (MMRP) decreased \$1.9 billion, or 36 percent, from FY 2005 to FY 2006. The decrease is due to the use of more refined estimates from site evaluations and installation action plan workshops to determine a more realistic path forward. Additionally, the decrease is due to Defense Environmental Restoration Program (DERP) site reclassification to the Base Realignment and Closure (BRAC) program during FY 2006.

#### Other Accrued Environmental Liabilities – Active Installations

Other Accrued Environmental Liabilities – Other increased \$35.7 million, or 100 percent, from FY 2005 to FY 2006 due to reclassification of various environmental liabilities by the Low Level Radioactive Waste program managers during FY 2006. This information was formerly disclosed on Note 16, Commitments and Contingencies as a possible contingent liability.

#### Base Realignment and Closure (BRAC)

BRAC - MMRP increased \$166.2 million, or 26 percent, from FY 2005 to FY 2006 due to the reclassification of 38 DERP active sites to the BRAC MMRP in FY 2006 as a result of the BRAC 2005 law to close active installations.

BRAC - Environmental Corrective Action / Closure Requirements decreased \$21.9 million, or 40 percent, from FY 2005 to FY 2006. This entire decrease is attributable to disbursement of funds to process corrective actions at BRAC installations during FY 2006.

BRAC - Other increased \$37.1 million or 33 percent from FY 2005 to FY 2006. This entire increase was due to new contracts for continued cleanup at BRAC installations initiated in FY 2006.

#### Chemical Demilitarization Program

The Chemical Weapons Disposal Program liability increased \$7 billion, or 67 percent, from FY 2005 to FY 2006. The entire increase is attributable to the initial use of the Army Cost Position in 3rd Quarter, FY 2006 rather than an inflationary adjusted FY 2003 Acquisition Program Baseline. It is expected that the total liability will fluctuate as a result of program execution and revised program cost estimates.

## Environmental Disclosures

As of September 30	2006	2005
<i>(Amounts in thousands)</i>		
A. Amount of operating and capital expenditures used to remediate legacy waste. Legacy wastes are the remediation efforts covered by IRP, MMRP, and BD/DR regardless of funding source.	0	0
B. The unrecognized portion of the estimated total cleanup costs associated with general property, plant and equipment.	0	0
C. The estimated cleanup costs associated with general property, plant and equipment placed into service during each fiscal year.	0	0
D. Changes in total cleanup costs due to changes in laws, regulations, and/or technology.	0	0
E. Portion of the changes in estimated costs due to changes in laws and technology that is related to prior periods.	0	0

The Army General Fund reports zeros in the Environmental Disclosure table for this quarter. The Army General Fund is unable to systematically report and gather information for items presented above. These reporting deficiencies result from system and internal control weaknesses. The Army General Fund will continue coordination with the Office of the Under Secretary of Defense (Comptroller) to address these deficiencies and additionally outline specific tasks and milestones in the Army Chief Financial Officer's Strategic Plan in the future.

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

## **Applicable Laws and Regulations**

### **Defense Environmental Restoration Program**

The Army General Fund is required to cleanup contamination resulting from past waste disposal practices, leaks, spills and other past activity prior to 1986 from hazardous substances and wastes that created a public health or environmental risk and prior to FY 2003 from unexploded ordnance (UXO), discarded military munitions, and munitions constituents at other than operational ranges under the DERP, established by Section 211 of the Superfund Amendments and Reauthorization Act of 1986 codified in Title 10 of the United States Code 2701. The Army General Fund is also required to cleanup contamination resulting from waste disposal practices, leaks, spills and other activity after 1986 from hazardous substances and wastes and after FY 2003 from UXO, discarded military munitions, and munitions constituents migrating from an operational range under the Army Compliance Cleanup Program. Applicable laws are as follows for the DERP, Non-DERP, Low Level Radioactive Waste, and the BRAC programs:

- Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA)
- Superfund Amendments and Reauthorization Act
- Clean Water Act
- Safe Drinking Water Act
- Clean Air Act
- Resource Conservation and Recovery Act (RCRA)
- Toxic Substances Control Act (TSCA)
- Low Level Radioactive Waste Policy Amendments
- National Defense Authorization Acts

### **Chemical Demilitarization Program**

There are two primary public laws that require the chemical stockpile and non-stockpile chemical materiel destruction efforts to be carried out as part of the Chemical Demilitarization Program. The first is the 1986 Defense Authorization Act (Public Law (PL) 99-145, as amended by subsequent acts) that directed the DoD to destroy the unitary chemical stockpile while providing for maximum protection of the environment, public, and personnel involved in the destruction effort by April 29, 2004. The deadline for completion of destruction was amended by subsequent acts to April 29, 2007. The second is the 1993 Defense Authorization Act (PL 102-484) which required the establishment of the Non-Stockpile Chemical Material Project to safely dispose of all non-stockpile chemical materiel. The destruction operations being carried out using the facilities and equipment developed and fielded as part of the program are also subject to numerous federal and state environmental regulations. The major regulations applicable to the program are as follows:

- CERCLA
- Clean Water Act
- Clean Air Act
- RCRA
- TSCA

### **Methods for Assigning Estimated Total Cleanup Costs to Current Operating Periods**

#### **DERP, Non-DERP, and BRAC**

The Army General Fund uses engineering estimates and independently validated models to estimate environmental liabilities. The Remedial Action Cost Engineering Requirements (RACER) is the Army's preferred model. The Army General Fund relies upon the Air Force, which is the RACER executive agent, to validate the model in accordance with DoD Instruction 5000.61 and primarily uses the model to estimate the liabilities based on data received during a preliminary assessment and initial site investigation. The Army primarily uses engineering estimates after obtaining extensive data during the remedial investigation/feasibility phase of the environmental project. Once the environmental cost estimates are complete, the Army complies with accounting standards to assign costs to current operating periods.

In compliance with accounting standards, the Army General Fund expenses the costs for cleanup associated with general property, plant, and equipment (PP&E) placed into service prior to October 1, 1997 unless the costs are intended to be recovered through user charges. If the costs are recovered through user charges, then the Army General Fund expenses the portion of the asset that has passed since the general PP&E was placed into service and systematically recognizes the remaining cost over the life of the asset.

For general PP&E placed into service after September 30, 1997, the Army General Fund is required to expense the associated environmental costs systematically over the life of the asset. The Army expenses the full cost to cleanup contamination for stewardship PP&E at the time the asset is placed into service. The Army General Fund will use two methods for systematic recognition: physical capacity for operating landfills and life expectancy in years for all other assets.

**Chemical Demilitarization Program**

The basis for calculating environmental liabilities for the Army components of the Chemical Demilitarization Program is a bottoms up estimate developed using parametric, analogous, and engineering methodologies, as appropriate. The schedule component of the estimate is based on analysis of historical processing rates with down time adjustments. The cost methodology is based on the historical costs of the project and utilizes the Army cost analysis community directed Automated Cost Estimating Integrated Tool software as the platform for cost modeling. To the greatest extent possible, actual costs are broken down to produce a site-specific model based on actual or analogous costs. Inclusion of site-specific schedules in the model results in the current working estimate. The estimate and its methodology have been independently reviewed, supported, and approved by the Deputy Assistant Secretary of the Army (Cost and Economics) staff as well as the Army Cost Review Board, the Assistant Secretary of the Army (Financial Management and Comptroller), and the Army Acquisition Executive.

**Types of Environmental Liabilities and Disposal Liabilities Identified****DERP, Non-DERP, and BRAC**

The Army General Fund has environmental clean up requirements for the DERP sites at active installations, BRAC installations, Formerly Used Defense Sites, non-DERP sites at active installations, weapon systems programs, and chemical weapons disposal programs. The DERP and non-DERP sites are required to clean up contamination in coordination with regulatory agencies, other responsible parties, and current property owners. For the Army General Fund, environmental disposal for weapons systems programs consists of chemical weapons disposal.

**Chemical Demilitarization Program**

The Army, as Executive Agent within the DoD, provides policy, direction, and oversight for the Chemical Demilitarization Program, except at the Pueblo, Colorado and Blue Grass, Kentucky locations. The disposal program for these locations is managed separately by the Program Manager for Assembled Chemical Weapons Alternatives that reports directly to the Office of the Under Secretary of Defense (Acquisition, Technology and Logistics).

The Chemical Demilitarization Program mission is to safely and effectively destroy the entire U.S. stockpile of chemical agents and munitions located at Johnston Island in the Pacific and in Utah, Alabama, Oregon, Arkansas, Indiana, and Maryland in accordance with public law. The Johnston Island facility has completed its mission and facility closure. The Maryland facility has completed the disposal mission and is currently undergoing closure. The other five facilities are currently in operation and working to complete their disposal missions. The Chemical Demilitarization Program mission also includes the safe disposal of non-stockpile chemical materiel. This includes binary chemical weapons, old chemical weapons recovered as part of remediation and recovery operations, and miscellaneous materiel associated with chemical weapon production, storage, testing, maintenance, and disposal. The Chemical Demilitarization Program does not include the mission to recover and dispose of buried chemical weapons.

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

The Army General Fund had changes in estimates resulting from overlooked or previously unknown contaminants, better site characterization with sampling, re-estimation based on different assumptions, and lessons-learned. Environmental liabilities can also change in the future due to changes in laws and regulations, changes in agreements with regulatory agencies, and advances in technology.

**Uncertainty Regarding the Accounting Estimates used to Calculate the Reported Environmental Liabilities****DERP, Non-DERP, and BRAC**

The environmental liabilities for the Army General Fund are based on accounting estimates which require certain judgments and assumptions that are believed to be reasonable based upon information available to us at the time of calculating the estimates. The actual results may materially vary from the accounting estimates if agreements with regulatory agencies require remediation to a different degree than anticipated when calculating the estimates. The liabilities also can be impacted if further investigation of the environmental sites discloses contamination different than known at the time of the estimates.

In addition to the liabilities reported above, the Army General Fund is uncertain regarding the extent of the liabilities at installations that are realigning or closing as a result of the FY 2005 BRAC round. The Army General Fund is in the process of determining the extent of environmental liabilities at bases due to realign or close; in particular those liabilities associated with unexploded ordnance on training ranges that are due to realign or close.

**Chemical Demilitarization Program**

The schedules and cost estimates in the approved baseline for this liability estimate are the best available and have been through the formal Acquisition Program Baseline approval process at the time of report submission. It should be noted that they are subject to fact of life changes and impacts from program risks and uncertainties inherent to the task of chemical demilitarization and the political sensitivity of the program. These risks may include processing changes required to meet the operational schedules due to the deteriorating condition of the stockpile and additional schedule time and/or cost to address changes in environmental laws or Congressional requirements.

## Note 15. Other Liabilities

As of September 30	2006			2005
	Current Liability	Noncurrent Liability	Total	Total
<i>(Amounts in thousands)</i>				
1. Intragovernmental				
A. Advances from Others	\$ 155,613	\$ 0	\$ 155,613	\$ 138,074
B. Deposit Funds and Suspense Account Liabilities	704,266	0	704,266	213,950
C. Disbursing Officer Cash	1,784,811	0	1,784,811	1,482,046
D. Judgment Fund Liabilities	0	0	0	0
E. FECA Reimbursement to the Department of Labor	99,409	175,876	275,285	274,311
F. Other Liabilities	261,321	0	261,321	263,880
G. Total Intragovernmental Other Liabilities	\$ 3,005,420	\$ 175,876	\$ 3,181,296	\$ 2,372,261
2. Nonfederal				
A. Accrued Funded Payroll and Benefits	\$ 918,321	\$ 0	\$ 918,321	\$ 578,786
B. Advances from Others	1,222,335	0	1,222,335	866,239
C. Deferred Credits	0	0	0	0
D. Deposit Funds and Suspense Accounts	0	0	0	0
E. Temporary Early Retirement Authority	0	0	0	0
F. Nonenvironmental Disposal Liabilities				
(1) Military Equipment (Nonnuclear)	0	0	0	0
(2) Excess/Obsolete Structures	0	0	0	0
(3) Conventional Munitions Disposal	0	1,217,768	1,217,768	1,318,443
G. Accrued Unfunded Annual Leave	3,078,596	0	3,078,596	2,728,211
H. Capital Lease Liability	11,777	21,277	33,054	47,031
I. Other Liabilities	760,723	917,960	1,678,683	863,206
J. Total Nonfederal Other Liabilities	\$ 5,991,752	\$ 2,157,005	\$ 8,148,757	\$ 6,401,916
3. Total Other Liabilities	\$ 8,997,172	\$ 2,332,881	\$ 11,330,053	\$ 8,774,177

### Fluctuations and/or Abnormalities

#### Intragovernmental

Intragovernmental Other Liabilities increased \$809.0 million, or 34 percent, from FY 2005 to FY 2006 primarily due to fluctuations in Deposit Funds and Suspense Accounts Liabilities and Disbursing Officer Cash.

Deposit Funds and Suspense Account Liabilities increased by \$490.3 million, or 229 percent, from FY 2005 to FY 2006 primarily due to a timing difference in the disbursement of payroll tax withholdings and Federal Insurance Contributions Act (FICA). In FY 2005, the disbursement for withheld tax withholdings and FICA was disbursed in September 2005 whereas in FY 2006 the disbursements will not occur until October 2006. This timing difference is a normal part of business.

Disbursing Officer Cash increased \$302.8 million, or 20 percent, from FY 2005 to FY 2006 primarily due to an increase in advances from the Republic of Korea during FY 2006 for engineering and construction work to be done by the U.S. Army Corps of Engineers to upgrade electrical systems, water and sewer systems, housing, schools, fences, and bridges on various bases in Korea.

Intragovernmental Other Liabilities, Other consists of unemployment compensation; cancelled accounts receivable; employee benefits for retirement, health and life insurance; and education benefits trust fund.

#### Nonfederal

Nonfederal Other Liabilities increased \$1.7 billion, or 27 percent, from FY 2005 to FY 2006 primarily due to reporting of contingent liabilities, accrued unfunded annual leave, and accrued funded payroll and benefits. Beginning in 4th Quarter, FY 2006, Army General Fund began reporting the Mechanization of Contract Administration Services contingent liability for \$780.5 million that was not required to be recognized in prior years. The Accrued Unfunded Annual Leave increased \$350.4 million due to the continued deployment of soldiers in

support of Operation Iraqi Freedom restricting the use of annual leave during FY 2006. The Accrued Funded Payroll and Benefits increased \$339.5 million as a result of capturing previously omitted Military Pay accruals beginning in 2nd Quarter, FY 2006. The Military Pay anti-deficiency act review identified that Army General Fund was not properly capturing the required Military Pay accruals.

Contingent Liabilities balance includes \$780.5 million in estimated future contract financing payments that will be paid to the contractor upon delivery and Government acceptance of a satisfactory product. In accordance with contract terms, specific rights to the contractor's work vests with the Government when a specific type of contract financing payments are made, thereby protecting taxpayer funds in the event of contract nonperformance. These rights should not be misconstrued as the rights of ownership. The Department is under no obligation to pay the contractor for amounts greater than the amounts authorized in the contract until delivery and Government acceptance of a satisfactory product. Because it is probable that the contractor will complete its efforts and deliver a satisfactory product to the Department and the amount of potential future payments are estimable, the Department has recognized a contingent liability for estimated future payments, which are conditional pending delivery and Government acceptance of a satisfactory product.

Nonfederal Other Liabilities, Other consists of employer contributions and payroll taxes, contingent liabilities, contract holdbacks, and custodial liabilities for Iraqi seized cash and development fund for Iraq.

## Capital Lease Liability

As of September 30	2006				2005
	Asset Category				Total
	Land and Buildings	Equipment	Other	Total	
<i>(Amounts in thousands)</i>					
1. Future Payments Due					
A. 2006	\$ 0	\$ 0	\$ 0	\$ 0	\$ 20,929
B. 2007	18,008	150	0	18,158	18,157
C. 2008	8,529	156	0	8,685	8,685
D. 2009	5,376	93	0	5,469	5,469
E. 2010	5,376	0	0	5,376	5,376
F. 2011	0	0	0	0	0
G. After 5 Years	8,682	0	0	8,682	8,682
H. Total Future Lease Payments Due	\$ 45,971	\$ 399	\$ 0	\$ 46,370	\$ 67,298
I. Less: Imputed Interest Executory Costs	13,218	98	0	13,316	20,267
J. Net Capital Lease Liability	\$ 32,753	\$ 301	\$ 0	\$ 33,054	\$ 47,031
2. Capital Lease Liabilities Covered by Budgetary Resources				\$ 22,667	\$ 26,466
3. Capital Lease Liabilities Not Covered by Budgetary Resources				\$ 10,387	\$ 20,565

The Army General Fund is the lessee in eight capital leases for military family housing and one equipment lease. The Office of Management and Budget Circular A-136 directs that any capital leases entered into during FY 1992 or later are required to be fully funded in the first year of the lease.

### Capital Lease Liabilities Covered by Budgetary Resources

The present value of the lease payments, \$22.7 million, for leases originating after FY 1991 plus the current portion of the Pre-1992 leases are shown as Covered by Budgetary Resources.

### Capital Lease Liabilities Not Covered by Budgetary Resources

The remaining six leases that originated before FY 1992 are funded on a fiscal year basis causing the non-current amounts of \$10.4 million to be shown as Not Covered by Budgetary Resources.

## Note 16. Commitments and Contingencies

### Relevant Information for Comprehension

The Army General Fund is a party in various administrative proceedings and legal actions, with claims including environmental damage claims, equal opportunity matters, and contractual bid protests. The Army General Fund has accrued contingent liabilities for legal actions where the Army's Office of the General Counsel considers an adverse decision probable and the amount of loss is measurable. In the event of an adverse judgment against the Government, some of the liabilities may be payable from the Judgment Fund. The Army General fund records Judgment fund liabilities in Note 15, "Other Liabilities," and Note 12 "Accounts Payable." See Notes 15 and 12 for details.

### Nature of Contingency

The FY 2006 Army Legal Representation Letter outlines claims against the Army General Fund totaling \$28 billion for which the Army Office of General Counsel is unable to express an opinion. The historical payout percentage for these cases is less than one percent. To determine the historical payout, the Army Office of General Counsel divides the total amount reported as a payout in the fiscal year by the total amount of claimed in the Army Legal Representation Letter.

The Army General Fund has other contingent liabilities in which the possibility of loss is considered reasonable. These liabilities are not accrued in the Army General Fund's financial statements nor reported in the FY 2006 Army Legal Representation Letter. As of September 30, 2006, the Army General Fund had approximately \$307.8 million in claims considered reasonably possible. These contingent liabilities and estimates are presented in the following table. Estimates for litigations, claims and assessments are required to be fully supported. Additionally, Army General Fund has coordinated with Army Office of General Counsel to ensure that estimates agree with the legal representation letters and management summary schedule.

Title of Contingent Liabilities	Estimate
<i>(Amounts in thousands)</i>	
Litigation Division	\$136,021
Administrative Tort Claims	50,000
European Environmental Claims	50,000
Army Environmental Law Division	46,226
Army Contract Appeals Division	24,913
Network Enterprise Technology Command	400
Army Personnel Claims	228
<b>Total</b>	<b>\$307,788</b>

### Other Information Pertaining to Commitments

The Army General Fund has entered into contractual commitments that require future use of financial resources. It has significant amounts of long-term lease obligations, undelivered orders, and cancelled accounts payable. The amount of contractual commitments for 4th Quarter, FY 2006 is presented in the following schedule.

Title of Contractual Commitments	
<i>(Amounts in thousands)</i>	
Long-term lease obligations	\$33,053
Undelivered orders	\$80,793,552
Cancelled accounts payable	\$96,276

## Note 17. Military Retirement and Other Federal Employment Benefits

As of September 30	2006				2005
	Present Value of Benefits	Assumed Interest Rate (%)	(Less: Assets Available to Pay Benefits)	Unfunded Liability	Present Value of Benefits
<i>(Amounts in thousands)</i>					
1. Pension and Health Actuarial Benefits					
A. Military Retirement Pensions	\$ 0		\$ 0	\$ 0	\$ 0
B. Military Retirement Health Benefits	0		0	0	0
C. Military Medicare-Eligible Retiree Benefits	0		0	0	0
D. Total Pension and Health Actuarial Benefits	\$ 0		\$ 0	\$ 0	\$ 0
2. Other Actuarial Benefits					
A. FECA	\$ 1,461,098	5.31%	\$ 0	\$ 1,461,098	\$ 1,663,650
B. Voluntary Separation Incentive Programs	0		0	0	0
C. DoD Education Benefits Fund	0		0	0	0
D. Total Other Actuarial Benefits	\$ 1,461,098		\$ 0	\$ 1,461,098	\$ 1,663,650
3. Other Federal Employment Benefits	\$ 0		\$ 0	\$ 0	\$ 0
4. Total Military Retirement and Other Federal Employment Benefits:	\$ 1,461,098		\$ 0	\$ 1,461,098	\$ 1,663,650

### Fluctuations and/or Abnormalities

The FECA actuarial liability decreased \$202.6 million, or 12 percent, from FY 2005 to FY 2006 primarily due to the Army General Fund reporting the US Corps of Engineers' liability in FY 2005. In 4th Quarter, FY 2006 the US Corps of Engineers reported its own portion of the FECA actuarial liability.

### Federal Employees Compensation Act (FECA)

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

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

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

As of September 30	2006	2005
(Amounts in thousands)		
1. Intragovernmental Costs	\$ 43,852,068	\$ 39,987,321
2. Public Costs	131,165,204	116,179,311
3. Total Costs	<u>\$ 175,017,272</u>	<u>\$ 156,166,632</u>
4. Intragovernmental Earned Revenue	\$ (9,063,319)	\$ (8,491,159)
5. Public Earned Revenue	(1,340,202)	(1,249,288)
6. Total Earned Revenue	<u>\$ (10,403,521)</u>	<u>\$ (9,740,447)</u>
7. Net Cost of Operations	<u>\$ 164,613,751</u>	<u>\$ 146,426,185</u>

### Fluctuation and/or Abnormalities

Gross Costs increased \$18.9 billion, or 12 percent, from FY 2005 to FY 2006 primarily due to a \$5.1 billion increase in future funded expenses, \$6.6 billion increase in procurement, and \$2.7 billion increase in military construction. The increase in future funded expense is for environmental liabilities reported in FY 2006 for the Chemical Weapons Disposal Program. The program implemented the use of a new cost estimation process beginning in 3rd Quarter, FY 2006.

The increase in procurement cost is a direct impact of a cumulative change in estimate for military equipment per Office of the Secretary of Defense guidance from October 1, 2005 to June 30, 2006 beginning in 3rd Quarter, FY 2006.

The increase in military construction is due to the construction, modifications, and procurement of facilities and attendant items for the Army during FY 2006, specifically due to modifications required for the Fort Bragg, Fort Lewis, Fort Wainwright, and other Army installations.

### Definitions

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

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

### Other Information Regarding Costs

The Consolidated Statement of Net Cost in the federal government is unique because its principles are driven by understanding the net cost of programs and/or organizations that the federal government supports through appropriations or other means. This statement provides gross and net cost information that can be related to the amount of output or outcome for a given program and/or organization administered by a responsible reporting entity.

The amounts presented in the Consolidated Statement of Net Cost are based on funding, obligation, accrual, and disbursing transactions, which are not always recorded using accrual accounting. The Army General Fund's systems do not always record the transactions on an accrual basis as is required by the Generally Accepted Accounting Principles. The information presented also includes data from non-financial feeder systems to capture all cost and financing sources for Army General Fund.

The Army General Fund recorded a prior period adjustment due to a change in the methodology for reporting of military equipment. The FY 2005 restatement impacts the value of general property, plant, and equipment and associated accumulated depreciation reported on the balance sheet. The Department has determined that developing the prior year value for the depreciation expense is cost-prohibitive, and thus has elected not to restate the Statement of Net Cost.



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

As of September 30	2006		2005	
	Cumulative Results of Operations	Unexpended Appropriations	Cumulative Results of Operations	Unexpended Appropriations
<i>(Amounts in thousands)</i>				
1. Prior Period Adjustments Increases (Decreases) to Net Position Beginning Balance				
A. Changes in Accounting Standards	\$ 0	\$ 0	\$ 0	\$ 0
B. Errors and Omissions in Prior Year Accounting Reports	(42,829,096)	0	(42,829,096)	0
C. Total Prior Period Adjustments	\$ (42,829,096)	\$ 0	\$ (42,829,096)	\$ 0
2. Imputed Financing				
A. Civilian CSRS/FERS Retirement	\$ 306,148	\$ 0	\$ 316,873	\$ 0
B. Civilian Health	561,369	0	525,159	0
C. Civilian Life Insurance	1,784	0	1,655	0
D. Judgment Fund	94,807	0	249,118	0
E. IntraEntity	0	0	0	0
F. Total Imputed Financing	\$ 964,108	\$ 0	\$ 1,092,805	\$ 0

### Prior Period Adjustments: Errors and Omissions in Prior Year Accounting Reports

The Army General Fund recorded a \$42.8 billion prior period adjustment due to a change in the methodology for reporting of military equipment, resulting in a \$42.8 billion restatement for FY 2005. The FY 2005 restatement impacts the value of general property, plant, and equipment and associated accumulated depreciation reported on the balance sheet. The Department has determined that developing the prior year value for the depreciation expense is cost-prohibitive, and thus has elected not to restate the Statement of Net Cost.

In accordance with the Statement of Federal Financial Accounting Standards (SFFAS) No. 23, Eliminating the Category National Defense Property, Plant, and Equipment, the Department reported military equipment values in the financial statements beginning in FY 2003. As an interim measure, while the Department worked to develop its military equipment baseline from internal records, the military equipment values reported were based on information from the Bureau of Economic Analysis (BEA).

Effective 3rd Quarter, FY 2006, the Department replaced the BEA estimation methodology with a valuation based on internal Departmental records. During the process of establishing a baseline, we discovered that the BEA estimates had failed to consider disposals, thresholds, and construction in process. While an estimation methodology is acceptable per SFFAS 23, due to the nature of the BEA omissions, we consider that the method we previously used was not compliant with Generally Accepted Accounting Principles, and thus have treated the adjustment as correction of a material error.

### Cumulative Results of Operations

Other Budgetary Financing Sources (All other funds) and Other Financing Sources (Other) represent adjustments to bring the proprietary accounts into agreement with the budgetary accounts. Due to system deficiencies, there are unreconciled differences between the budgetary and proprietary trial balances. The net effect of these adjustments is reflected on Other budgetary financing sources and Other Financing Sources on the Statement of Net Position.

### Unexpended Appropriations

Appropriations Received (All other funds) on the Statement of Changes in Net Position does not agree with the Appropriations Received on the Statement of Budgetary Resources due to differences between proprietary and budgetary accounting concepts and reporting requirements. The Statement of Budgetary Resources includes \$13.1 million in receipts for Appropriated Trust or Special Fund Receipts that are not included in the Statement of Changes in Net Position.

Other Adjustments represent recessions and cancelled authority enacted during FY 2006.

## Note 20. Disclosures Related to the Statement of Budgetary Resources

As of September 30	2006	2005
<i>(Amounts in thousands)</i>		
1. Net Amount of Budgetary Resources Obligated for Undelivered Orders at the End of the Period	\$ 80,977,698	\$ 71,524,849
2. Available Borrowing and Contract Authority at the End of the Period	11,404	0

### Undelivered Orders

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

### Supplemental Appropriations Received

Appropriations received increased primarily due to the enactment of Public Law 109-234, FY 2006 Emergency Supplemental Appropriations Act for Defense, the Global War on Terror, and Hurricane Recovery. This appropriation will fund ongoing military, diplomatic, and intelligence operations in the Global War on Terror; stabilization and counter-insurgency activities in Iraq and Afghanistan; and other humanitarian assistance.

### Breakdown of Emergency Supplemental Appropriations

<i>(Amounts in billions)</i>	
Appropriation	Total
Military Personnel	\$6.8
Operations & Maintenance	18.0
Afghanistan Security Forces	1.9
Iraqi Security Forces	3.0
Joint Improvised Explosive Device Defeat Fund	2.0
Procurement	8.9
Research, Development, Test and Evaluation	0.1
<b>Total Army Supplemental</b>	<b>\$40.7</b>

### Reporting of Appropriations Received

Appropriations received on the Statement of Budgetary Resources do not agree with appropriations received on the Statement of Changes in Net Position because of differences between proprietary and budgetary accounting concepts and reporting requirements. The differences are made up of the recording of receipts for trust and special funds and the appropriations anticipated-indefinite accounts.

### Presentation of Statement of Budgetary Resources

The Statement of Budgetary Resources does not include eliminating entries because the statements are presented as combined and combining. Therefore, a Disaggregated Statement of Budgetary Resources is included in the Required Supplementary Information section of the financial statements.

### Breakdown of Apportionment Categories

Office of Management and Budget Circular A-136 specifically requires disclosure of the amount of direct and reimbursable obligations incurred against amounts apportioned under Category A (apportioned by fiscal quarter), Category B (apportioned by project or activity), and Exempt from Apportionment. Obligations incurred consists of \$178.6 billion in Category A, Direct; \$8.3 billion in Category B, Direct; \$19.5 billion in Category A, Reimbursable; and \$5.9 billion in Category B, Reimbursable. This disclosure agrees with the aggregate of the related information as reported on the Budgetary Execution Report and Obligations Incurred on the Statement of Budgetary Resources.

### Terms of Borrowing Authority

Borrowing authority increased due to a loan default relating to the Armament Retooling and Manufacturing Support Initiative (ARMS). This initiative is designed to encourage commercial use of inactive Army General Fund ammunition plants through many incentives for businesses willing to locate to a government ammunition production facility. The Army General Fund, by means of ARMS Initiative legislation, established a loan guarantee program to facilitate commercial firms' use of specified ammunition manufacturing facilities. The Army General Fund and Department of Agriculture Rural Business-Cooperative Service (RBS) established a Memorandum of Understanding for the RBS to administer the ARMS Initiative Loan Guarantee Program. The borrowing authority was received from Treasury to pay for a loan 90 percent guaranteed by ARMS to make bullet casings. The loan was defaulted in August 1999 and Army General Fund was in litigation to determine the actual amount of debt owed. In January 2006, Army General Fund used the borrowing authority to pay for the guaranteed loan.

**Differences with the Budget of the United States Government**

A Nonbudgetary Credit Program Finance Account section allows for a clear distinction between budgetary and nonbudgetary credit program financing. Nonbudgetary credit financing accounts are reported separately from the budgetary totals in the Budget of the United States Government. Separate reporting on the Statement of Budgetary Resources enhances reconciliation of the two sets of information.

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

**Note 21. Disclosures Related to the Statement of Financing**

The Statement of Financing is intended to explain and define the relationship between net obligations from budgetary accounting and net cost of operations from proprietary accounting. The following Statement of Financing lines are presented as combined instead of consolidated due to intra-agency budgetary transactions not being eliminated:

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

Other Resources – Other, and Other resources or adjustments to net obligated resources that do not affect net cost operations – Other includes Other Gains and Losses which represents adjustments to bring the proprietary accounts into agreement with the budgetary accounts. Due to system deficiencies, there are unreconciled differences between the budgetary and proprietary trial balances. In addition, Other resources or adjustment to net obligated resources that do not affect net cost operations – Other includes transfers in and out without reimbursement.

Other Components Requiring or Generating Resources in Future Period represents increases in future funded expense for various liabilities such as Federal Employment Compensation Act, Judgment Fund, Unemployment Compensation, and Closed Accounts Payable.

Other Components not Requiring or Generating Resources is comprised of Other Expenses not Requiring Budgetary Resources for the Iraqi Relief and Reconstruction Fund. The Iraqi Relief and Reconstruction Fund is a transfer fund where Army General Fund executes the funding on behalf of the Executive Office of the President. The Department of the Treasury requires that the execution for this type of transfer is presented on Army General Fund's financial statements except for the Statements of Budgetary Resources. A reconciling item is included in Other because Obligations incurred on the Statement of Financing does not include expenses related to the Iraqi Relief and Reconstruction Fund.

Components Requiring or Generating Resources in Future Period reports \$5.5 billion increases in unfunded expenses that were incurred during FY 2006. The cumulative total of unfunded expenses from all fiscal years is reported as "Liabilities Not Covered by Budgetary Resources" in Note 11.

**Note 22. Disclosures Related to the Statement of Custodial Activity**

The Statement of Custodial Activity displays current year collections and disbursements for two custodial accounts: Development Fund for Iraq and Iraqi Seized Assets. Funds held in a Custodial Activity are only used for their stated purposes and are not available for the Department's use.

**Development Fund for Iraq (DFI)**

The DFI is for urgent humanitarian assistance, reconstruction, and other projects carried out for the benefit of the Iraqi people. In the current year, there were \$34.6 million in disbursements by the Multi-National Force Iraq with no additional deposits. Some of the disbursements for FY 2005 were incorrectly classified. Disbursements during FY 2006 were processed to correct the misclassification which caused negative disbursements for Education, Refugees, Human Rights, and Governance. As of September 30, 2006, \$18.8 million remains to be disbursed.

	During FY 2006	Cumulative from Inception
<i>(Amounts in Thousands)</i>		
<b>Source of Collections</b>		
Deposits By Foreign Governments	\$0	\$136,000
<b>Disposition of Collections</b>		
Security and Law Enforcement	\$216	\$979
Electric Sector	20,778	45,145
Oil Infrastructure	36	466
Water Resources and Sanitation	9,922	16,584
Transportation and Telecommunications	64	5,272
Roads, Bridges and Construction	794	5,024
Health Care	154	2,874
Private Sector Development	3,364	7,181
Education, Refugees, Human Rights, and Governance	(764 )	33,652
Total Disbursed on Behalf of Foreign Governments	34,564	117,177
Retained for Future Support of Foreign Governments *	(34,564 )	18,823
<b>Total Disposition of Collections</b>	<b>\$0</b>	<b>\$136,000</b>
<b>Net Custodial Collection Activity</b>	<b>\$0</b>	<b>\$0</b>

\*Retained for Future Support of Foreign Governments is reflected as an Increase/(Decrease) in Amounts to be Transferred on the Statement of Custodial Activity

#### Seized Assets

During Operation Iraqi Freedom, the U.S. Government seized assets from the Iraqi Government that are used in support of the Iraqi people. In FY 2006, \$31.2 million was disbursed with no additional seized assets. As of September 30, 2006, \$30.2 million of seized monetary assets remain to be disbursed in support of the Iraqi people as shown in the table below.

	During FY 2006	Cumulative from Inception
<i>(Amounts in Thousands)</i>		
<b>Source of Collections</b>		
Seized Iraqi Cash	\$0	\$927,216
<b>Disposition of Collections</b>		
Iraqi Salaries	\$0	\$30,838
Repair/Reconstruction/Humanitarian Assistance	31,154	526,113
Iraqi Ministry Operations (Ministry of Finance, Defense, etc.)	0	264,737
Fuel/Supplies	0	75,312
<b>Total Disbursed on Behalf of Iraqi People</b>	<b>31,154</b>	<b>897,000</b>
Retained for Future Support of the Iraqi People	(31,154 )	30,216
<b>Total Disposition of Collections</b>	<b>\$0</b>	<b>\$927,216</b>
<b>Net Custodial Collection Activity</b>	<b>\$0</b>	<b>\$0</b>

**Note 23. Earmarked Funds**

BALANCE SHEET As of September 30 <i>(Amounts in thousands)</i>	MRF	MERHCF	Other Earmarked Funds	Eliminations	Total
<b>ASSETS</b>					
Fund balance with Treasury	\$ 0	\$ 0	\$ 43,434	\$ 0	\$ 43,434
Investments	0	0	3,407	0	3,407
Accounts and Interest Receivable	0	0	22,965	(22,965)	0
Other Assets	0	0	0	0	0
<b>Total Assets</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 69,806</b>	<b>\$ (22,965)</b>	<b>\$ 46,841</b>
<b>LIABILITIES and NET POSITION</b> As of September 30					
Military Retirement Benefits and Other Federal Employment Benefits	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
Other Liabilities	0	0	27,014	0	27,014
Unexpended Appropriations	0	0	0	0	0
Cumulative Results of Operations	0	0	42,792	0	42,792
<b>Total Liabilities and Net Position</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 69,806</b>	<b>\$ 0</b>	<b>\$ 69,806</b>
<b>STATEMENT OF NET COST</b> As of September 30					
Program Costs	\$ 0	\$ 0	\$ 6,291	\$ 0	\$ 6,291
Less Earned Revenue	0	0	0	0	0
<b>Net Program Costs</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 6,291</b>	<b>\$ 0</b>	<b>\$ 6,291</b>
Less Earned Revenues Not Attributable to Programs	0	0	0	0	0
<b>Net Cost of Operations</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 6,291</b>	<b>\$ 0</b>	<b>\$ 6,291</b>
<b>STATEMENT OF CHANGES IN NET POSITION</b> As of September 30					
Net Position Beginning of the Period	\$ 0	\$ 0	\$ 35,140	\$ 0	\$ 35,140
Net Cost of Operations	0	0	6,291	0	6,291
Budgetary Financing Sources	0	0	13,953	0	13,953
Other Financing Sources	0	0	(10)	0	(10)
<b>Change in Net Position</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 7,652</b>	<b>\$ 0</b>	<b>\$ 7,652</b>
<b>Net Position End of Period</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 42,792</b>	<b>\$ 0</b>	<b>\$ 42,792</b>

**Earmarked Funds**

Earmarked Funds represent funds received from outside sources for specific purposes. Army receives earmarked for the following:

- Sale of Hunting and Fishing Permits. Fees are received from individuals for the issuance of special hunting and fishing permits. The funds for this account are used for wildlife, fish, and game conservation and rehabilitation on military reservations.
- Restoration of Rocky Mountain Arsenal. Funds are received from private industry for the cleanup of contamination areas of Rocky Mountain Arsenal. Public Law 99-661, Section 1367 provides the authority for this explicit use.
- Royalties for Use of DoD-Military Insignia and Trademarks. Funds are received from the sale of commemorative memorabilia, trademarks, and licensing activities. The funds are used to replenish inventory stock for such items and other related Commemorative Program expenses. The authority to create expenditures originates from Public Law 102-484, Section 378.

- Forest and Wildlife Conservation, Military Reservations. These funds are produced from the sale of forest products that are in excess of operation and maintenance expenses at fiscal year-end for the payment of entitlements to States.
- National Science Center. Funds received from the collection of fees for the use of the National Science Center and use for the operation and maintenance of the National Science Center as authorized under Public Law 99-145, Defense Authorization Act 1986, Section 1459.
- Bequest of Major General Fred C. Ainsworth to Walter Reed Army Medical Center. Funds received from interest on investments for the use of purchasing supplies and equipment for the library at Walter Reed Army Medical Center.
- Department of the Army General Gift Fund. Funds are received from private parties and estates and used for various purposes.

The Total Earmarked Funds column is shown as consolidated. All intra-DoD activity between earmarked funds and non-earmarked funds has been eliminated from this column, which causes assets to not equal liabilities and net position.

## Note 24. Other Disclosures

As of September 30	2006			
	Asset Category			
	Land and Buildings	Equipment	Other	Total

(Amounts in thousands)

### 1. ENTITY AS LESSEE-Operating Leases

#### Future Payments Due

#### Fiscal Year

2007	\$	6,298	\$	0	\$	0	\$	6,298
2008		4,950		0		0		4,950
2009		3,794		0		0		3,794
2010		2,118		0		0		2,118
2011		67		0		0		67
After 5 Years		15,484		0		0		15,484

Total Future Lease Payments Due	\$	32,711	\$	0	\$	0	\$	32,711
---------------------------------	----	--------	----	---	----	---	----	--------

### Definitions

Lessee – A person or entity who receives the use and possession of leased property (e.g. real estate or equipment) from a lessor in exchange for payment of funds.

Operating Lease - A lease which does not substantially transfer all the benefits and risks of ownership. Payments are charged to an expense account over the lease term as it becomes payable.

### Relevant Information for Comprehension

Land and Building lease periods vary and are not expected to be renewed at the end of the lease term. There are no material escalation clauses or contingent rental restrictions. Costs are gathered from existing leases, General Service Administration bills, and Interservice Support Agreements of which the largest component is office space. Future year projections use the Consumer Price Index (CPI), rather than the DoD inflation factor. The CPI impacts increases to the leases, especially those at commercially leased sites.



## FY 2006 Required Supplementary Stewardship Information (RSSI)

### National Defense Property, Plant, and Equipment

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

The following summarizes Heritage Assets. In most cases, the additions and deletions are the result of sites/installations: (a) identifying cemeteries and historical facilities; (b) disposing of Base Realignment and Closure (BRAC) property or excess installations; and (c) privatization based on the Residential Communities Initiative program. BRAC Mission Closure installations and sites also are included in this report.

Heritage Assets					
For Fiscal Year Ended September 30, 2006					
(a)	(b)	(c)	(d)	(e)	(f)
	Measurement /Quantity	As of 10/1/05	Additions	Deletions	As of 9/30/06
Museums (Note 2)	Each	60	1	0	61
Monuments and Memorials (Note 3)	Each	1,240	60	75	1,225
Cemeteries (Note 4)	Sites	466	67	62	471
Archeological Sites (Note 6)	Sites	68,280	4,008	3,821	68,467
Buildings & Structures (Note 1)	Each	10,066	310	1142	9,234
Major Collections (Note 5)	Each	90	17	1	106

#### Notes:

1. Historical Buildings and Structures: buildings and structures designated as historical exclude museums, monuments, and memorials. The number of Buildings and Structures increased as a result of the following initiatives:
  - Installations conducting real property surveys and making adjustments according to their findings;
  - Active installations now reporting previously omitted National Guard Bureau buildings and structures designated as heritage assets; and
  - Both National Guard and Reserve are now reporting new buildings and structures designated as heritage assets.
2. Museums: The Army Museum System consists of 61 museums and museum activities in the active Army and Army Reserve. There are a relatively small number of federally-owned artifacts in National Guard Museum activities, which are primarily state entities. In addition, there is historical property displayed in numerous regimental rooms, trophy rooms, officer's clubs, visitor's centers, chapels, and headquarters building elements that are not individually recognized by the Department of the Army as museums or museum activities.
3. Memorial/Monuments: includes category code 76020 (monuments).
4. Cemeteries: includes category code 76030 (cemetery), 76031 (National Cemeteries), 76032 (Veterans Cemeteries), and excludes 76033 (Pet Cemeteries).
5. Major Collections: The US Army Tank automotive & Armaments Life Cycle Management Command (TACOM LCMC) reports two (2) major collections under the Army Donations Program consisting of Ceremonial Rifles and Monuments/Static Displays. The Ceremonial Rifle collection consists of 371,163 weapons in the hands of 29,402 veterans' organizations, law enforcement agencies and National cemeteries.

Major collections also include 84 archeological collections identified at individual Army installations. These collections, kept in perpetuity, are managed in accordance with Federal Regulations. While some collections are available to the public, a number of items within an Archeological Collection are protected by Federal regulations such as the Native American Graves Protection and Repatriation Act (1990). Each installation maintaining an archeological collection is considered to have only one collection, regardless of whether the collection is divided among different facilities or locations. The collections are the responsibility of the Army, but may be in the care of a contractor, a public institution or other entity.



6. Archeological collections: The Army reports Archeological Sites in two categories:
- All recorded archeological sites on Army-owned Federal land whose eligibility is undetermined; and
  - All archeological sites eligible for the National Register as determined by a formal evaluation process.

The first number reflects the total number of archeological sites for which the Army is responsible for managing and evaluating their significance. This number was calculated as of September 30, 2006. The Army does not generally acquire or remove new archeological sites during the calendar year, but instead identifies new sites on existing Army land or evaluates existing sites during the course of the financial year. New land acquisitions that include new archeological sites will be specifically noted in future calendar year “additions”. Typical additions reflect the Army’s policy to inventory land in accordance with Sections 106 and 110 of the National Historic Preservation Act. As more land is surveyed, more archeological sites are identified. Deletions reflect changes to the status of a recorded archeological site that may have been determined ineligible for listing, or they may be evidence of an accounting correction by an installation. In some cases, an archeological site may appear as a deletion if it was mitigated or destroyed, or if multiple sites previously counted as individual sites were found to have only one official trinomial number.

The conditions of archeological sites across the Army remain varied from poor to excellent, based on a number of factors, including the environmental setting, the type of the site, and the effects of Army activities. If an Army activity has the potential to adversely affect an archeological site eligible for the National Register of Historic Places, the installation’s Installation Cultural Resource Management Plan (ICRMP) defines the installation’s actions to address that potential damage. Army installations use ICRMPs to manage their cultural resources, including archeological sites that are in compliance with federal requirements. These plans provide for site protection, site conditions monitoring, and mitigation procedures. Overall, the conditions of sites on Army installations are “fair,” based on the Army’s cultural resource management procedures.

The following summarizes Stewardship Land. Additions/deletions are the result of: (a) acquiring additional land through donation or withdrawal from public domain; (b) identification of missing land records; and (c) disposal of BRAC Closure sites or transfer of land to another DOD agency. BRAC Mission Closure installations and sites are included in this report.

<b>Stewardship Land</b>				
For Fiscal Year Ended September 30, 2006				
<i>(Acres in Thousands)</i>				
(a)	(b)	(c)	(d)	(e)
	As of 10/1/05	Additions	Deletions	As of 9/30/06
Land Use				
Mission (Note 1)	6,914.50	.37	5.62	6,909.25
Parks & Historic Sites (Note 2)	.94	.08	.07	.95
Total				

**Notes:**

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

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

<b>Non-federal Physical Property</b>					
<b>Yearly Investment in State and Local Governments</b>					
For Fiscal Years FY 2002 through FY 2006					
<i>(In Millions of Dollars)</i>					
(a) Categories	(b) FY 2002	(c) FY 2003	(d) FY 2004	(e) FY 2005	(f) FY 2006
<b>Transferred Assets:</b>					
1. National Defense Mission Related	\$7.4	\$85.0	\$54.7	\$70.7	\$66.5
<b>Funded Assets:</b>					
2. National Defense Mission Related	0	0	0	0	0
Total	\$7.4	\$85.0	\$54.7	\$70.7	\$66.5

**Notes:**

- Investment values included in this report are based on Non-federal Physical Property outlays (expenditures). Outlays are used because current DoD systems are unable to capture and summarize costs in accordance with the Federal Accounting Standards requirements.
- Data provided here are significant because these are properties that are owned by the various U.S. Property and Fiscal Offices and are essential in accomplishing the mission of the Army National Guard.
- Costs of maintenance of these non-federal assets are included in the budgetary resources of Army National Guard.
- These properties represent non-cash items that were transferred to State and local governments.

The following summarizes Basic Research, Applied Research, and Development Investments and provides examples of each.

<b>Investments in Research and Development</b>					
<b>Yearly Investment in Research and Development</b>					
For Fiscal Years FY 2002 through FY 2006					
<i>(In Millions of Dollars)</i>					
(a) Categories	(b) FY 2002	(c) FY 2003	(d) FY 2004	(e) FY 2005	(f) FY 2006
Basic Research	\$206.4	\$226.9	\$291.6	\$360.0	\$355.4
Applied Research	864.1	847.2	886.8	995.1	1,006.8
Development					
Advanced Technology Development	863.1	988.6	1,010.4	1,185.8	1,369.3
Advanced Component Development and Prototypes	897.7	880.1	767.7	830.3	659.7
Systems Development and Demonstration	1,954.9	2,265.1	3,288.3	4,309.4	4,963.5
Research, Development, Test and Evaluation Management Support	880.9	979.4	1,069.8	1,157.3	1,287.5
Operational Systems Development	970.4	964.9	929.8	1,156.7	1,218.7
Total	\$6,637.5	\$7,152.2	\$8,244.4	\$9,994.6	\$10,860.9

**Narrative Statement:**

**Basic Research** is the systematic study directed toward greater knowledge or understanding of the fundamental aspects of phenomena and of observable facts without specific applications towards processes or products in mind. It includes all scientific study and experimentation directed toward increasing fundamental knowledge and understanding in those fields of the physical, engineering, environmental, and life sciences related to long-term national security needs. It is farsighted high payoff research that provides the basis for technological progress.

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

**Defense Research Sciences (PE 0601102A):** This program fosters fundamental scientific knowledge and contributes to the sustainment of U.S. Army scientific and technological superiority in land war fighting capability, provides new concepts and technologies for the Army's Future Force, and provides the means to exploit scientific breakthroughs and avoid technological surprises. It fosters innovation in Army niche areas and where the commercial incentive to invest is lacking due to limited markets. It also focuses university single investigators on research areas of Army interest. The in-house portion of the program capitalizes on the Army's scientific talent and specialized facilities to expeditiously transition knowledge and technology into the appropriate developmental activities. The extramural program leverages the research efforts of other government agencies, academia, and industry. This translates to a coherent, well-integrated program which is executed by four primary contributors: 1) the Army Research, Development and Engineering Command (RDECOM); 2) the U.S. Army Engineer Research and Development Center (ERDC); 3) the Army Medical Research and Materiel Command (MRMC) laboratories; and 4) the Army Research Institute for Behavioral and Social Sciences (ARI). The basic research program is coordinated with the other Services via Defense Science and Technology Reliance (Defense Basic Research Advisory Group), the Defense Basic Research Technology Area Review and Assessment (TARA) process and other inter-service working groups. This program responds to the scientific and technological requirements of the Department of Defense Basic Research Plan by enabling technologies that can significantly improve joint war fighting capabilities.

**University and Industry Research Centers (PE 0601104A):** A significant portion of the work performed within this program directly supports Future Force requirements by providing research that supports enabling technologies for Future Force capabilities. Broadly, the work in this program falls into three categories: Collaborative Technology Alliances (CTAs), University Centers of Excellence (COE), and paradigm-shifting centers - University-Affiliated Research Centers (UARCs). The Army has formed CTAs to leverage large investments by the commercial sector in basic research areas that are of great interest to the Army. Collaborative Technology Alliances involve partnerships between industry, academia, and the Army Research Laboratory to incorporate the practicality of industry, the expansion of the boundaries of knowledge from universities, and Army scientists to shape mature and transition technology. This program also includes the Army's COE, which focus on expanding the frontiers of knowledge in research areas where the Army has enduring needs. COEs couple state-of-the-art research programs at academic institutions with broad-based graduate education programs to increase the supply of scientists and engineers in information sciences, materials science, electronics, automotive and rotary wing technology. Historically Black Colleges and Universities and Minority Institution (HBCU/MI) Centers of Excellence address critical research areas for Army Transformation. This program also includes the four Army UARCs, which have been created to exploit opportunities to advance new capabilities through a sustained long-term multidisciplinary effort. Also included in this program is eCYBERMISSION, the Army's national web-based competition to stimulate interest in science, math and technology among middle and high school students.

**Applied Research** is the systematic study to understand the means to meet a recognized and specific need. It is a systematic expansion and application of knowledge to develop useful materials, devices, systems or methods. It may be oriented, ultimately, toward the design, development, and improvement of prototypes and new processes to meet general mission area requirements. Applied research may translate promising basic research into solutions for broadly defined military needs, short of system development.

*The following are two representative program examples for this category:*

**Materials Technology (PE 0602105A):** This program researches and evaluates materials technologies for armor and armaments that will significantly enhance the survivability and lethality of Future Combat Systems (FCS) and Future Force systems and, where feasible, can be exploited to enhance Current Force capabilities. It provides the technology base required for solving materials-related problems in individual Soldier support equipment, armor, armaments, aircraft, ground and combat vehicles and combat support.

**Combat Vehicle and Automotive Technology (PE 0602601A):** This program researches, investigates and applies combat vehicle and automotive component technologies that will improve survivability, mobility, sustainability, and maintainability of Army ground combat and tactical vehicles. As combat vehicle systems become smaller and lighter, one of the greatest technological and operational challenges is providing adequate crew protection without reliance on heavy passive armor. This challenge will be met using a layered approach, including long-range situational awareness, multi-spectral signature reduction, Active Protection (AP) systems and advanced lightweight armor in place of heavy conventional armor. This program also funds the National Automotive Center (NAC). The goal of the NAC is to leverage large commercial investments in automotive technology research and development, pursuing automotive-oriented technology programs that have potential benefit to military ground vehicles. Additionally this program investigates, evaluates and characterizes unique AP countermeasure concepts for intercepting chemical energy and kinetic energy threats before they reach the target vehicle. This program also investigates hybrid electric propulsion and electronic vehicle component technologies.

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

1. **Advanced Technology Development:** This area of technology includes all efforts to mature technology (hardware or software) sufficient for demonstration in an operational environment—this may be live or virtual. In this program experimental systems or subsystems are

demonstrated to prove the technical feasibility and military utility of the approach selected. Advanced technology development provides the path for the rapid development and demonstration of new components and systems. The most complex efforts in this program are designated as Advanced Technology Demonstrations (ATDs). The Army's ATDs are developed to facilitate the smooth transition of advanced technology into systems as part of a formal acquisition program.

2. **Advanced Component Development and Prototypes (ACD&P)** evaluates integrated technologies in as realistic an operating environment as possible to assess the performance or cost reduction potential of advanced technology. Programs in this phase are generally system specific. Major outputs of ACD&P development are hardware and software components, or complete weapon systems, ready for operational and developmental testing and field use.
3. **System Development and Demonstration** concludes the program or project and prepares it for production. It consists primarily of preproduction efforts, such as logistics and repair studies. Major outputs are weapons systems finalized for complete operational and developmental testing.
4. **RDT&E Management Support** includes research, development, test and evaluation efforts and funds to sustain and/or modernize the installations or operations required for general research, development, test and evaluation.
5. **Operational Systems Development** includes developmental efforts to upgrade systems that have been fielded or have received approval for full rate production and anticipate production funding in the current or subsequent fiscal years.

*The following are five representative program examples of development:*

**Electronic Warfare Advanced Technology (PE 0603008A):** The goal of this program is to provide enabling technologies for a secure, mobile, wireless network that will operate reliably in diverse and complex terrain, in all environments for the Army's Future Force and, where feasible, exploit opportunities to enhance Current Force capabilities. Technologies will be matured and demonstrated to address this challenge with distributed, mobile, secure, self-organizing communications networks. A key objective is to demonstrate seamlessly integrated communications technologies across all network tiers, ranging from unattended networks and sensors through maneuver elements and airborne/space assets. To accomplish the goal this program will investigate and leverage external communication technologies and combine technology options in a series of Command, Control, Communications, and Computers Intelligence, Surveillance and Reconnaissance (C4ISR) On-The-Move (OTM) experiments to measure the battlefield effectiveness for Future Combat System (FCS) Brigade Combat Team (BCT) and the Future Force. This program also provides: protection technologies for tactical wireless networks against modern network attacks; smart communication technologies to network and control unmanned systems anywhere on the battlefield enabling timely sensor-decider-engagement linkage to defeat critical targets; advanced antenna technologies for greater communications mobility, range and throughput; and automated network management aids.

**Advanced Tank Armament System (PE 0603653A):** This program supports the development of the Stryker family of vehicles. A critical need exists to improve the deploy ability and operational effectiveness of rapid response/early entry forces. The Stryker family includes: Infantry Carrier Vehicle (ICV), Reconnaissance Vehicle (RV), Mobile Gun System (MGS), Mortar Carrier (MC), Commander's Vehicle (CV), Fire Support Vehicle (FSV), Engineer Squad Vehicle (ESV), Medical Evacuation Vehicle (MEV), Anti-Tank Guided Missile Vehicle (ATGM), and Nuclear/Biological/Chemical Reconnaissance (NBC RV). The use of a common platform/common chassis design reduces requirements for repair parts and logistics support in the area of operations.

**Air Defense Command, Control and Intelligence -- Engineering Development (PE 0604741A):** This program supports the Air and Missile Defense Planning and Control System (AMDPCS), which is an Army Future Force System with Homeland Defense capabilities that allows for the integration of Air and Missile Defense (AMD) operations. It also supports the Forward Area Air Defense Command, Control, and Intelligence (FAAD C2I) System, which provides continuously tailored situational awareness and situational understanding of the battle space. The mission is to collect, digitally process and disseminate real time target cueing and tracking information, common tactical air picture, and command, control, and intelligence information.

**Army Test Ranges and Facilities (0605601A):** This program provides the institutional funding required to operate the developmental test activities required by Department of Defense (DoD), Department of the Army (DA) weapon system developers and Research, Development, and Engineering Centers. This funding does not pay for program specific test costs. All functions and resources associated with this program are managed by the U.S. Army Developmental Test Command (DTC), a subordinate command of the Army Test and Evaluation Command (ATEC). This program provides resources to operate four Army Major Range and Test Facility Bases (MRTFB): White Sands Missile Range (WSMR), New Mexico; Electronic Proving Ground (EPG), Fort Huachuca, Arizona; Aberdeen Test Center (ATC), Aberdeen Proving Ground (APG), Maryland; Yuma Proving Ground (YPG), Arizona.

This program also provides the resources to operate the Army's developmental test capability at: the Aviation Technical Test Center, Fort Rucker, Alabama; and the Redstone Technical Test Center, Redstone Arsenal, Alabama. It also provides the resources for test planning and safety verification/confirmation at Headquarters, DTC located at APG. Developmental test capabilities at the test ranges have been uniquely established, are in place to support test and evaluation (T&E) requirements of funded weapons programs, and are required to assure technical performance, adherence to safety requirements, reliability, logistics supportability, and quality of materiel in development and in production.

**Multiple Launch Rocket System (MLRS) Product Improvement Program (PIP) (0603778A):** This program provides support for the following improvements to MLRS: High Mobility Artillery Rocket System (HIMARS), M270A1, Guided Multiple Launch Rocket System (GMLRS) and GMLRS Unitary munition which provide precision strike capability.

- HIMARS, is a C-130 transportable launcher mounted on a Family of Medium Tactical Vehicles (FMTV) chassis. HIMARS is capable of firing either six MLRS Family of Munitions (MFOM) rockets or one Army Tactical Missile (ATACMS) Family of Munitions (AFOM) missile, including precision munitions, to a range of 300KM.
- The M270A1 upgraded MLRS launcher is mounted on a Bradley Fighting Vehicle chassis, and is capable of firing the MFOM and the AFOM, including precision munitions, to a range of 300KM.
- GMLRS is a precision munition which provides an increased range and Global Positioning System (GPS) accuracy. Fired from M270A1 and HIMARS launchers, GMLRS comes in two variants: Dual Purpose Improved Conventional Munitions (DPICM) which contains 414 sub munitions, for attacking area targets with improved accuracy and significantly reduced hazardous duds; and GMLRS Unitary which has a 200lb High Explosive (HE) warhead for attacking point targets with reduced collateral damage.

## Real Property Deferred Maintenance Amounts

*As of September 30, 2006*

### Narrative Statement:

FY2006 sustainment requirements for the Army are from version 6.1 of the DoD Facilities Sustainment Model (FSM). The required and executed amounts represent facilities funded from Operations & Maintenance (O&M), Army Family Housing (AFH), and Working Capital Fund (WCF) appropriations, and from Non-Appropriated Funds (NAF). Sustainment funding contributions from host nation funding (Japan) and military pay are included. The appropriated amount includes no contribution from WCF, NAF and host nation funding as these funds are not appropriated by Congress. Army sustainment data includes facilities that are multi-use heritage assets. The sustainment data excludes facilities funded from Research, Development, Test and Evaluation (RDTE), and Procurement appropriations, and Chemical Depots, because we lack separately identifiable sustainment funding for these locations.

Annual Sustainment FY 2006				
Property Type	1. Required	2. Appropriated	3. Executed	4. Difference
Buildings, Structures, and Utilities	\$3,114.5M	\$2,500.1M	\$2,767.8M	\$346.7M

Annual Deferred Sustainment Trend				
Property Type	FY 2003	FY 2004	FY 2005	FY 2006
Buildings, Structures, and Utilities	\$792.3M	\$959.9M	\$1,008.0M	\$346.7M

Army Restoration & Modernization (R&M) requirements are modeled in the annual Installation Status Report (ISR). During ISR data collection, facility occupants evaluate the condition of each facility against published standards. The inspection generates a quality improvement cost estimate for each facility based on the condition rating of each component of the facility, and the component improvement cost factor. Improvement cost factors are developed for each component within each facility type.

The requirement reported for General PP&E R&M is the ISR cost to improve the quality of facilities to full up Q-1 status, which represents full improvement cost for each facility. For FY2006, these requirements address facility types funded from Army appropriated operations and maintenance (O&M), working capital fund (WCF), and Army family housing (AFH) funds. The Army's R&M requirement does not include requirements for facilities funded by Department of Defense agencies (DECA, DLA, TMA, DODDS), non-appropriated funds-NAF (recreation, sports), Army Air Force Exchange Service, and private funding. The R&M requirement also excludes costs for utilities planned for privatization, closures from base realignment and closure (BRAC) decisions, ammunition plants and chemical depots.

The Army's estimate to return these facilities to a full-up Q-1 status for FY2006 is \$22.2B, based on the 2006 ISR. Reduced requirements for FY 2006 are a result of two actions:

- Investments in restoration and modernization show improvements to the condition of facilities.
- Privatization efforts continue to move utilities and Army family housing away from Army responsibility to recapitalize.

Restoration & Modernization Requirements			
Property Type	End FY 2005	End FY 2006	Change
Buildings, Structures, and Utilities	\$24.4B	\$22.2B	-\$2.2B

Military Equipment  
Deferred Maintenance Amounts

As of September 30, 2006

*(Amount in Thousands)*

(a)	(b)
Major Type	
1. Aircraft	\$190,000
2. Ships	0
3. Missiles	\$155,500
4. Combat Vehicles	\$299,400
5. Other Weapons Systems	\$293,200
Total	\$938,100

The Op-30 report from the FY 2007 President Budget was used to compile the deferred depot level maintenance. Depot Maintenance Operations and Planning System (DMOPS) is the automated system for capturing depot-level deferred maintenance data.

**Stewardship Property, Plant and Equipment Condition:**

The Federal Accounting Standards Advisory Board (FASAB), Statement of Federal Financial Accounting Standards 29 - Heritage Assets and Stewardship Land, requires the Army to report the condition of heritage assets and stewardship land as required supplementary information. The FASAB standard states that the condition of an asset is based on an evaluation of the physical status/state of an asset, its ability to perform as planned, and its continued usefulness. Given the aforementioned criteria, most Army heritage assets and stewardship land are in an acceptable physical state and have established data compilation standards. Specific examples of Stewardship Property, Plant and Equipment condition are outlined below:

- Major Collections: The U.S. Army Tank Automotive and Armaments Life Cycle Management Command (TACOM LCMC) reports two major collections under the Army Donations Program consisting of Ceremonial Rifles and Monuments/Static Displays. The Ceremonial Rifles collection is in good condition with 101,985 rifles considered lost or stolen and 95 percent serial number accountability of the remaining 269,178 weapons. The Monuments/Static display collection consists of 5,375 major end items located in 3,169 organizations, which are in good condition with 100 percent accountability.
- Archeological Collections: The condition of the Army's Archeological Collections is good. Thirty three percent of the Army's existing archeological collections need upgrading of either curatorial facilities, accessioning, packaging and/or conservation to meet Federal requirements under title 36, chapter I of the code of federal regulation part 79 - Curation of Federally-Owned and Administered Archeological Collections.



**STATEMENT OF DISAGGREGATED BUDGETARY RESOURCES**

As of September 30, 2006 and 2005 (\$ in Thousands)

	Other	Research, Development, Test & Evaluation	Operation and Maintenance
<b>BUDGETARY FINANCING ACCOUNTS</b>			
<b>BUDGETARY RESOURCES</b>			
Unobligated balance, brought forward, October 1	\$ 5,576,863	\$ 2,308,224	\$ 1,525,639
Recoveries of prior year unpaid obligations	182,894	1,576,841	9,533,254
Budget authority			
Appropriation	8,724,028	11,240,197	71,144,696
Borrowing authority	0	0	0
Contract authority	0	0	0
Spending authority from offsetting collections			
Earned			
Collected	88	4,144,826	12,258,122
Change in receivables from Federal sources	87	65,638	(12,879)
Change in unfilled customer orders			
Advance received	0	41,971	87,620
Without advance from Federal sources	(726)	421,326	(224,206)
Anticipated for rest of year, without advances	0	0	0
Previously unavailable	0	0	0
Expenditure transfers from trust funds	0	0	0
Subtotal	\$ 8,723,477	\$ 15,913,958	\$ 83,253,353
Nonexpenditure transfers, net, anticipated and actual	(2,351,937)	615,848	889,982
Temporarily not available pursuant to Public Law	0	0	0
Permanently not available	(26,047)	(219,324)	(850,595)
<b>Total Budgetary Resources</b>	<b>\$ 12,105,250</b>	<b>\$ 20,195,547</b>	<b>\$ 94,351,633</b>
<b>Status of Budgetary Resources:</b>			
Obligations incurred:			
Direct	\$ 8,549,773	\$ 12,142,842	\$ 78,921,190
Reimbursable	13,696	5,359,087	13,452,403
Subtotal	8,563,469	17,501,929	92,373,593
Unobligated balance:			
Apportioned	3,519,583	2,579,115	424,619
Exempt from apportionment	4,035	0	0
Subtotal	3,523,618	2,579,115	424,619
Unobligated balance not available	18,164	114,504	1,553,420
<b>Total status of budgetary resources</b>	<b>\$ 12,105,251</b>	<b>\$ 20,195,548</b>	<b>\$ 94,351,632</b>
<b>Change in Obligated Balance:</b>			
Obligated balance, net			
Unpaid obligations, brought forward, October 1	\$ 1,918,960	\$ 8,869,649	\$ 34,298,575
Less: Uncollected customer payments from Federal sources, brought forward October 1	(4,271)	(3,477,142)	(6,360,776)
Total unpaid obligated balance	1,914,689	5,392,507	27,937,799
Obligations incurred net (+/-)	\$ 8,563,469	\$ 17,501,929	\$ 92,373,593
Less: Gross outlays	(6,772,855)	(15,032,449)	(80,852,392)
Obligated balance transferred, net			
Actual transfers, unpaid obligations (+/-)	0	0	0
Actual transfers, uncollected customer payments from Federal sources (+/-)	0	0	0
Total Unpaid obligated balance transferred, net	0	0	0
Less: Recoveries of prior year unpaid obligations, actual	(182,894)	(1,576,841)	(9,533,254)
Change in uncollected customer payments from Federal sources (+/-)	640	(486,964)	237,085
Obligated balance, net, end of period			
Unpaid obligations	3,526,680	9,762,287	36,286,522
Less: Uncollected customer payments (+/-) from Federal sources (-)	(3,632)	(3,964,106)	(6,123,691)
Total, unpaid obligated balance, net, end of period	3,523,048	5,798,181	30,162,831
<b>Net Outlays</b>			
<b>Net Outlays:</b>			
Gross outlays	6,772,855	15,032,449	80,852,392
Less: Offsetting collections	(88)	(4,186,797)	(12,345,741)
Less: Distributed Offsetting receipts	(783,002)	0	0
<b>Net Outlays</b>	<b>\$ 5,989,765</b>	<b>\$ 10,845,652</b>	<b>\$ 68,506,651</b>



	Procurement	Military Personnel	Military Construction/Family Housing	2006 Combined	2005 Combined
\$	3,139,105	\$ 330,804	\$ 2,596,656	\$ 15,477,292	\$ 22,880,756
	1,424,875	3,430,037	703,146	16,851,046	17,033,447
	24,890,956	53,135,553	3,892,087	173,027,517	149,846,916
	0	0	0	0	0
	0	0	0	0	0
	1,372,751	221,124	3,808,580	21,805,492	20,948,239
	(41,171)	(47,231)	15,068	(20,488)	(415,099)
	2,970	0	287,723	420,284	77,733
	35,563	(11,397)	585,028	805,587	2,159,939
	0	0	0	0	0
	0	0	0	0	0
	0	0	0	0	0
\$	26,261,069	\$ 53,298,049	\$ 8,588,486	\$ 196,038,392	\$ 172,617,728
	2,183,002	2,139,513	(306,640)	3,169,768	3,415,759
	0	0	0	0	0
	(342,045)	(534,766)	(190,920)	(2,163,696)	(877,523)
\$	32,666,006	\$ 58,663,637	\$ 11,390,728	\$ 229,372,802	\$ 215,070,167
\$	25,325,841	\$ 58,185,538	\$ 3,788,175	\$ 186,913,360	\$ 175,086,215
	1,671,362	198,528	4,740,373	25,435,449	24,506,660
	26,997,203	58,384,066	8,528,548	212,348,809	199,592,875
	5,482,787	18,252	2,855,744	14,880,099	13,665,452
	0	0	0	4,035	11,980
	5,482,787	18,252	2,855,744	14,884,134	13,677,432
	186,017	261,317	6,437	2,139,859	1,799,860
\$	32,666,007	\$ 58,663,635	\$ 11,390,729	\$ 229,372,802	\$ 215,070,167
\$	26,638,521	\$ 1,191,314	\$ 7,803,860	\$ 80,720,880	\$ 71,629,016
	(2,244,936)	(31,510)	(4,232,821)	(16,351,456)	(14,606,617)
	24,393,585	1,159,804	3,571,039	64,369,424	57,022,399
\$	26,997,203	\$ 58,384,067	\$ 8,528,548	\$ 212,348,809	\$ 199,592,876
	(22,343,392)	(54,256,654)	(6,805,794)	(186,063,536)	(173,467,566)
	0	0	0	0	0
	0	0	0	0	0
	0	0	0	0	0
	(1,424,875)	(3,430,037)	(703,146)	(16,851,046)	(17,033,447)
	5,608	58,628	(600,096)	(785,100)	(1,744,839)
	29,867,458	1,888,691	8,823,467	90,155,105	80,720,880
	(2,239,328)	27,118	(4,832,918)	(17,136,557)	(16,351,456)
	27,628,130	1,915,809	3,990,549	73,018,548	64,369,424
	22,343,392	54,256,654	6,805,794	186,063,536	173,467,566
	(1,375,722)	(221,124)	(4,096,302)	(22,225,774)	(21,025,971)
	0	0	0	(783,002)	(195,234)
\$	20,967,670	\$ 54,035,530	\$ 2,709,492	\$ 163,054,760	\$ 152,246,361

**STATEMENT OF DISAGGREGATED BUDGETARY RESOURCES**

As of September 30, 2006 and 2005 (\$ in Thousands)

	Other	Research, Development, Test & Evaluation	Operation and Maintenance
<b>NONBUDGETARY FINANCING ACCOUNTS</b>			
<b>BUDGETARY RESOURCES</b>			
Unobligated balance, brought forward, October 1	\$ 1,525	\$ 0	\$ 0
Recoveries of prior year unpaid obligations	0	0	0
Budget authority			
Appropriation	0	0	0
Borrowing authority	11,404	0	0
Contract authority	0	0	0
Spending authority from offsetting collections			
Earned			
Collected	325	0	0
Change in receivables from Federal sources	0	0	0
Change in unfilled customer orders			
Advance received	0	0	0
Without advance from Federal sources	0	0	0
Anticipated for rest of year, without advances	0	0	0
Previously unavailable	0	0	0
Expenditure transfers from trust funds	0	0	0
Subtotal	11,729	0	0
Nonexpenditure transfers, net, anticipated and actual	0	0	0
Temporarily not available pursuant to Public Law	0	0	0
Permanently not available	0	0	0
<b>Total Budgetary Resources</b>	<b>\$ 13,254</b>	<b>\$ 0</b>	<b>\$ 0</b>
<b>Status of Budgetary Resources:</b>			
Obligations incurred:			
Direct	\$ 11,962	\$ 0	\$ 0
Reimbursable	0	0	0
Subtotal	11,962	0	0
Unobligated balance:			
Apportioned	535	0	0
Exempt from apportionment	0	0	0
Subtotal	535	0	0
Unobligated balance not available	757	0	0
<b>Total status of budgetary resources</b>	<b>\$ 13,254</b>	<b>\$ 0</b>	<b>\$ 0</b>
<b>Change in Obligated Balance:</b>			
Obligated balance, net			
Unpaid obligations, brought forward, October 1	\$ 0	\$ 0	\$ 0
Less: Uncollected customer payments from Federal sources, brought forward, October 1	0	0	0
Total unpaid obligated balance	0	0	0
Obligations incurred net (+/-)	\$ 11,962	\$ 0	\$ 0
Less: Gross outlays	(11,962)	0	0
Obligated balance transferred, net			
Actual transfers, unpaid obligations (+/-)	0	0	0
Actual transfers, uncollected customer payments from Federal sources (+/-)	0	0	0
Total Unpaid obligated balance transferred, net	0	0	0
Less: Recoveries of prior year unpaid obligations, actual	0	0	0
Change in uncollected customer payments from Federal sources (+/-)	0	0	0
Obligated balance, net, end of period			
Unpaid obligations	0	0	0
Less: Uncollected customer payments (+/-) from Federal sources (-)	0	0	0
Total, unpaid obligated balance, net, end of period	0	0	0
<b>Net Outlays</b>			
<b>Net Outlays:</b>			
Gross outlays	11,962	0	0
Less: Offsetting collections	(325)	0	0
Less: Distributed Offsetting receipts	0	0	0
<b>Net Outlays</b>	<b>\$ 11,637</b>	<b>\$ 0</b>	<b>\$ 0</b>

Procurement	Military Personnel	Military Construction/Family Housing	2006 Combined	2005 Combined
\$ 0	\$ 0	\$ 0	\$ 1,525	\$ 1,424
0	0	0	0	0
0	0	0	0	0
0	0	0	11,404	0
0	0	0	0	0
0	0	0	326	101
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	11,730	101
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
\$ 0	\$ 0	\$ 0	\$ 13,255	\$ 1,525
\$ 0	\$ 0	\$ 0	\$ 11,962	\$ 0
0	0	0	0	0
0	0	0	11,962	0
0	0	0	535	1,525
0	0	0	0	0
0	0	0	535	1,525
0	0	0	758	0
\$ 0	\$ 0	\$ 0	\$ 13,255	\$ 1,525
\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
0	0	0	0	0
0	0	0	0	0
\$ 0	\$ 0	\$ 0	\$ 11,962	\$ 0
0	0	0	(11,962)	0
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	0	0
0	0	0	11,962	0
0	0	0	(325)	(101)
0	0	0	0	0
\$ 0	\$ 0	\$ 0	\$ 11,637	\$ (101)

**Required Supplemental Information - Part A**

**AT21 - Army General Fund**

(\$ Amounts in Thousands)

<b>Schedule, Part A DoD Intra-governmental Asset Balances</b>	<b>Treasury Index</b>	<b>Fund Balance with Treasury</b>	<b>Accounts Receivable</b>	<b>Loans Receivable</b>	<b>Investments</b>	<b>Other</b>
Executive Office of the President	11		\$1,245			
Department of Agriculture	12		\$1,647			\$498
Department of Commerce	13		\$316			\$7,264
Department of the Interior	14		\$197			\$264,733
Department of Justice	15		\$20,182			\$979
Department of Labor	16		\$0			
Navy General Fund	17		\$52,816			
United States Postal Service	18		\$28			
Department of State	19		\$1,924			
Department of the Treasury	20	\$94,632,928	\$1,071		\$3,406	
Office of Personnel Management	24		\$50			\$92,871
Library of Congress	3		\$10			
Nuclear Regulatory Commission	31		\$91			
Department of Veterans Affairs	36		\$602			
General Service Administration	47		\$50			\$23,344
Independent Agencies	48		\$241			
National Science Foundation	49		\$10			
Central Intelligence Agency	56		\$139			
Air Force General Fund	57		\$34,964			\$56,502
Tennessee Valley Authority	64					\$154
Environmental Protection Agency	68		\$217			\$2,992
Department of Transportation	69		\$157			\$3,008
Homeland Security	70		\$9,055			\$71,784
Small Business Administration	73					\$155
American Battle Monuments	74		\$4			
Department of Health and Human Services	75		\$0			\$16
National Aeronautics and Space Administration	80		\$1,225			\$3,105
Armed Forces Retirement Home	84		\$7			
Department of Energy	89		\$485			\$7,484
Selective Service System	90		\$238			
Department of Education	91		\$219			
Independent Agencies	95		\$900			
US Army Corps of Engineers	96		\$9,879			\$0
Other Defense Organizations General Funds	97		\$167,935			\$186
Other Defense Organizations Working Capital Funds	97-4930		\$21,536			\$66,584
Army Working Capital Fund	97-4930.001		\$22,606			
Navy Working Capital Fund	97-4930.002		\$6,572			
Air Force Working Capital Fund	97-4930.003		\$564			\$202
<b>Totals</b>		<b>\$94,632,928</b>	<b>\$357,182</b>		<b>\$3,406</b>	<b>\$601,861</b>

## Required Supplemental Information - Part B

### AT21 - Army General Fund

(\$ Amounts in Thousands)

Schedule, Part B DoD Intra-governmental entity liabilities	Treasury Index	Accounts Payable	Debts/Borrowings From Other Agencies	Other
Executive Office of the President	11			\$36,345
Department of Agriculture	12	\$11,860	\$0	
Department of Commerce	13	\$530		
Department of the Interior	14	\$5,900		\$92
Department of Justice	15	\$3,425		
Department of Labor	16	\$13		\$422,208
Navy General Fund	17	\$16,144		\$73
United States Postal Service	18	\$10,503		
Department of State	19	\$73,289		\$2,407
Department of the Treasury	20	\$212,515	\$11,404	\$167
Office of Personnel Management	24	\$4,738		\$62,488
Federal Communications Commission	27	\$396		
Library of Congress	3			\$15
Nuclear Regulatory Commission	31	\$97		
Department of Veterans Affairs	36	\$5,853		\$1,488
General Service Administration	47	\$295,511		
National Science Foundation	49	\$2,021		
Central Intelligence Agency	56			\$217
Air Force General Fund	57	\$20,239		\$660
Tennessee Valley Authority	64	\$12,271		
Environmental Protection Agency	68	\$11,585		
Department of Transportation	69	\$26,050		\$185
Homeland Security	70	\$12,139		\$49,577
Department of Health and Human Services	75	\$328		\$53,939
National Aeronautics and Space Administration	80	\$3,380		\$9,786
Department of Energy	89	\$23,794		\$48
Independent Agencies	95			\$614
US Army Corps of Engineers	96	\$5,675		
Other Defense Organizations General Funds	97	\$14,332		\$1,245
Other Defense Organizations Working Capital Funds	97-4930	\$584,635		
Army Working Capital Fund	97-4930.001	\$211,321		
Navy Working Capital Fund	97-4930.002	\$23,849		
Air Force Working Capital Fund	97-4930.003	\$1,387		
The General Fund of the Treasury	99			\$2,539,742
<b>Totals</b>		<b>\$1,593,780</b>	<b>\$11,404</b>	<b>\$3,181,296</b>

## Required Supplemental Information - Part C

### AT21 - Army General Fund

(\$ Amounts in Thousands)

Schedule, Part C DoD Intra-governmental revenue and related costs	Treasury Index	Earned Revenue
The Judiciary	10	\$40
Executive Office of the President	11	\$29,326
Department of Agriculture	12	\$5,730
Department of Commerce	13	\$7,514
Department of the Interior	14	\$1,113
Department of Justice	15	\$20,209
Department of Labor	16	\$1
Navy General Fund	17	\$1,009,494
United States Postal Service	18	\$668
Department of State	19	\$342,346
Department of the Treasury	20	\$9,318
Office of Personnel Management	24	\$159
Federal Communications Commission	27	\$177
Social Security Administration	28	\$1
Library of Congress	3	\$3,736
Nuclear Regulatory Commission	31	\$140
Department of Veterans Affairs	36	\$2,552
General Service Administration	47	\$3,818
Independent Agencies	48	\$1,055
National Science Foundation	49	\$1,628
Central Intelligence Agency	56	\$13,647
Air Force General Fund	57	\$1,274,029
National Labor Relations Board	63	\$201
Environmental Protection Agency	68	\$1,896
Department of Transportation	69	\$15,052
Homeland Security	70	\$243,835
American Battle Monuments	74	\$11
Department of Health and Human Services	75	\$53,859
National Aeronautics and Space Administration	80	\$21,281
Armed Forces Retirement Home	84	\$19
National Archives and Records Administration	88	\$112
Department of Energy	89	\$6,621
Other Legislative Branch Agencies	9	\$67
Selective Service System	90	\$2,727
Department of Education	91	\$2,595
Arms Control and Disarmament Agency	94	\$20
Independent Agencies	95	\$7,688
US Army Corps of Engineers	96	\$213,706
Other Defense Organizations General Funds	97	\$4,927,306
Other Defense Organizations Working Capital Funds	97-4930	\$121,931
Army Working Capital Fund	97-4930.001	\$0
Navy Working Capital Fund	97-4930.002	\$74,065
Air Force Working Capital Fund	97-4930.003	\$13,461
DoD Medicare-Eligible Retiree Health Care Fund		\$104,482
<b>Totals</b>		<b>\$8,537,636</b>

## Required Supplemental Information - Part E

### AT21 - Army General Fund

*(\$ Amounts in Thousands)*

Schedule, Part E	Treasury Index	Transfers In	Transfers Out
<b>DoD Intra-governmental non-exchange revenues</b>			
Executive Office of the President	11	\$453,164	
Air Force General Fund	57	\$26,738	
US Army Corps of Engineers	96	\$35	
Other Defense Organizations General Funds	97	\$544,888	\$6,422
Other Defense Organizations Working Capital Funds	97-4930	\$2,300	\$1,618
Army Working Capital Fund	97-4930.001	\$68	
The General Fund of the Treasury	99	\$0	
<b>Totals</b>		<b>\$1,027,193</b>	<b>\$8,040</b>







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

November 8, 2006

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

SUBJECT: Independent Auditor's Report on the Fiscal Year 2006 Army General Fund Financial  
Statements (Report No. D-2007-018)

The Chief Financial Officers Act of 1990, as amended, requires the Department of Defense Inspector General to audit the accompanying Army General Fund Consolidated Balance Sheet as of September 30, 2006 and 2005, the related Consolidated Statement of Net Cost, the Consolidated Statement of Changes in Net Position, the Combined Statement of Budgetary Resources, the Combined Statement of Financing, and the Statement of Custodial Activity for the fiscal years then ended. The financial statements are the responsibility of Army management. The Army is also responsible for implementing effective internal control and for complying with laws and regulations. We are unable to give an opinion on the Army General Fund Fiscal Year 2006 financial statements because of limitations on the scope of our work. Thus, the financial statements may be unreliable. In addition to our disclaimer of opinion on the financial statements, we are including the required Report on Internal Control and Compliance with Laws and Regulations. The Report on Internal Control and Compliance with Laws and Regulations is an integral part of our disclaimer of opinion on the financial statements and should be considered in assessing the results of the audit.

### Disclaimer of Opinion on the Financial Statements

The Assistant Secretary of the Army (Financial Management and Comptroller) acknowledged to us that financial management systems used to prepare the Army General Fund financial statements do not substantially comply with Federal financial management system requirements, generally accepted accounting principles, or the U.S. Government Standard General Ledger at the transaction level. Therefore, Army cannot provide adequate evidence supporting various material amounts on the financial statements. As a result, we did not perform auditing procedures to determine whether material amounts on the financial statements were fairly presented. We did not perform these and other auditing procedures because Section 1008(d) of the FY 2002 National Defense Authorization Act limits the Department of Defense Inspector General to perform only audit procedures required by generally accepted government auditing standards that are consistent with the representations made by management. The Army has also acknowledged, and prior audits have identified, the material weaknesses listed in the Summary of Internal Control. These material weaknesses also affect the reliability of certain information contained in the annual financial statements—much of which is taken from the same data sources as the basic financial statements.<sup>1</sup> Therefore, we are unable to express, and we do not express, an opinion on the basic financial statements. Additionally, the purpose of the audit was not to express an opinion on the information accompanying the basic financial statements. Accordingly, we express no opinion on the accompanying information.

---

<sup>1</sup> The annual financial statements include the basic financial statements, management discussion and analysis, consolidating and combining financial statements, Required Supplementary Stewardship Information, Required Supplementary Information, and Other Accompanying Information.

## Summary of Internal Control

In planning our audit, we considered Army internal control over financial reporting and compliance. We did this to determine our procedures for auditing the financial statements and to comply with Office of Management and Budget guidance, but our purpose was not to express an opinion on internal control. Accordingly, we do not express an opinion on internal control over financial reporting and compliance. However, previously identified reportable conditions, all of which are material, continued to exist in the following areas:

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

Material weaknesses are reportable conditions in which internal controls do not reduce (to a relatively low level) the risk of misstatements that are material to the financial statements and that might not be timely detected by employees while performing their normal assigned functions.

Reportable conditions are matters coming to the auditor's attention that, in his or her judgment, should be communicated to management because they represent significant deficiencies in the design or operation of internal control, which could adversely affect the organization's ability to initiate, record, process, and report financial data consistent with the assertions of management in financial statements. We performed financial-related audit work in DoD that was not part of the Chief Financial Officers Act audit and we identified weaknesses in contingent legal liabilities and cash in the custody of agents, which we consider to be reportable conditions.

Our internal control work (conducted during prior audits) would not necessarily disclose all reportable conditions. The Attachment offers additional details on reportable conditions, most of which we consider to be material internal control weaknesses.

## Summary of Compliance with Laws and Regulations

Our work to determine compliance with selected provisions of applicable laws and regulations related to financial reporting was limited because management acknowledged, and prior audits confirm, that instances of noncompliance continue to exist. The Assistant Secretary of the Army (Financial Report and Comptroller) acknowledged to us that many of its financial management and feeder systems do not comply with the requirements of the Federal Financial Management Information Act of 1996. The Army was also unable to comply with the Government Performance and Results Act requirements because it

did not have cost accounting systems in place to collect, process, and report operating costs. Therefore, we did not determine whether the Army was in compliance with all applicable laws and regulations related to financial reporting. Providing an opinion on compliance with certain provisions of laws and regulations was not an objective of our audit and, accordingly, we do not express such an opinion. See the Attachment for additional details on compliance with laws and regulations.

### Management Responsibility

Management is responsible for:

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

We provided a draft of this report to the Army.



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

Attachment:  
As stated



## Report on Internal Control and Compliance with Laws and Regulations

### Internal Control

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

**Material Weaknesses.** Management acknowledged that previously identified reportable conditions, all of which are material, continue to exist.

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

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

**Accounting Adjustments.** Because of inadequate financial management systems and processes, journal voucher adjustments and data calls were used to prepare the Army General Fund financial statements. Defense Finance and Accounting Service Indianapolis Operations did not adequately support \$270.1 billion in journal voucher adjustments used to prepare the Army General Fund financial statements. Specifically, Defense Finance and Accounting Service Indianapolis Operations made:

- \$130.1 billion in unsupported adjustments to force amounts to agree with other sources of information and records or financial statement lines,
- \$32.1 billion in unsupported adjustments to intragovernmental accounts to force the accounts to agree with the records of the Army's trading partners,
- \$44.4 billion in unsupported adjustments to correct errors and reclassify amounts to other accounts, and
- \$63.5 billion in unsupported adjustments to force general ledger accounts to agree with status of appropriations data (or ending balance adjustments) without reconciling the differences or determining which data source was correct.

**Intragovernmental Eliminations.** DoD is unable to collect, exchange, and reconcile buyer and seller intragovernmental transactions, resulting in adjustments that cannot be verified. This is primarily because of systems limitations, as the majority of the systems currently used within DoD do not allow for the capture of buyer-side information for use in reconciliations and eliminations. DoD and Army accounting systems were unable to capture trading partner data at the transaction level in a manner that facilitated required trading partner eliminations, and

DoD guidance did not require adequate support for eliminations. In addition, DoD procedures required that buyer-side transaction data be forced to agree with seller-side transaction data without performing proper reconciliations. Therefore, Defense Finance and Accounting Service Indianapolis Operations made \$32.1 billion in unsupported adjustments to intragovernmental accounts to force the accounts to agree with the records of Army's trading partners.

**Abnormal Account Balances.** Defense Finance and Accounting Service Indianapolis Operations did not detect, report, or take action to eliminate abnormal balances included in the Army General Fund accounting records. The FY 2006 trial balance data for the Army General Fund included 180 general ledger accounts with \$149.6 billion of unresolved abnormal balances for proprietary and budgetary accounts used by Defense Finance and Accounting Service Operations as part of the compilation of the Army General Fund financial statements. The FY 2006 trial balance data for the Army General Fund included an additional 79 budgetary general ledger accounts with abnormal balances of \$962 billion. Defense Finance and Accounting Service Indianapolis Operations considers this budgetary data to be so unreliable that the trial balance for budgetary accounts must be constructed from other budgetary reports.

In response to DoD IG Report No. D-2004-118, "Army General Fund Controls Over Abnormal Balances For Field Accounting Activities," September 28, 2004, Defense Finance and Accounting Service Indianapolis Operations stated that the Defense Departmental Reporting System-Budgetary Module (Budgetary Module) would significantly reduce abnormal balances in accounting records. Defense Finance and Accounting Service Indianapolis Operations estimated the completion date for corrective action to be September 30, 2005. However, the implementation of the Budgetary Module has been delayed until January 2007. The DoD Financial Management Regulation has not been revised to require the disclosure of the amounts of unresolved abnormal balances for all financial statement lines affected in the notes to the financial statements. Since FY 2004, the Army has chosen not to disclose abnormal balances in the financial statement footnotes. However, the Army reported abnormal balances as an area of concern in its FY 2006 Annual Statement of Assurance. Abnormal balances not only distort the Army General Fund financial statements, but also indicate internal control and operational deficiencies and may conceal instances of fraud.

**Fund Balance With Treasury.** DoD and its Components, including the Army, have had long-standing problems in reconciling transaction activity in their Fund Balance with Treasury accounts. Appropriation balances recorded in the accounting records do not agree with balances held at Treasury. Therefore, the Defense Finance and Accounting Service Indianapolis Operations made unsupported adjustments that had a net effect of \$38.3 billion on the three Fund Balance With Treasury line items.

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

- noncompliance with policies and procedures regarding referrals to the Debt Management Office and the Department of Treasury and for write-offs of 2 year old debt,
- a lack of controls to ensure all entitlement system receivables (vendor pay, civilian pay, and interest) are recorded in the accounting systems, and
- a lack of controls to ensure that accounts receivable balances are supportable at the transaction level.

As a result, Defense Finance and Accounting Service Indianapolis Operations made \$688.9 million in unsupported adjustments for FY 2006 that decreased accounts receivable balances by \$436 million.

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

**General Property, Plant, and Equipment.** Statement of Federal Financial Accounting Standards No. 6, “Accounting for Property, Plant, and Equipment,” requires that all General Property, Plant, and Equipment be recorded at cost, and that depreciation expense be recognized on all General Property, Plant, and Equipment. The Army has acknowledged that real property was not recorded at acquisition or historical cost and did not include all costs needed to bring the real property to a form and location suitable for its intended use. Also, the Army could not support the reported cost of Military Equipment in accordance with Statement of Federal Financial Accounting Standards No. 6. Military Equipment was not recorded at acquisition or historical cost and did not include all costs needed to bring the equipment to a form and location suitable for its intended use. The Army also lacks financial accountability systems for all its Military Table of Equipment unit property books that comply with the Federal Financial Management Improvement Act of 1996.

**Accounts Payable.** The Army is unable to properly account for and report Accounts Payable. Defense Finance and Accounting Service Indianapolis Operations made \$6 billion in unsupported adjustments for FY 2006 that increased Accounts Payable by \$268.3 million. In addition, the Army accounting systems do not capture trading partner data at the transaction level in a manner that facilitates trading partner aggregations for intra-agency sales. Therefore, the Army has acknowledged that it was unable to reconcile intragovernmental accounts payable to the related intragovernmental accounts receivable that generated the payables.

**Environmental Liabilities.** The Army has not properly estimated and reported its environmental liabilities. For example, the processes used to report environmental liabilities for the Defense Environmental Restoration Program, Base Realignment and Closure, and the non Defense Environmental Restoration Program on the financial statements were not adequate to establish or maintain sufficient documentation and audit trails. Although estimators were properly qualified to perform estimates, the Army did not document supervisory reviews of estimates and did not have adequate quality control programs in place to ensure the reliability of data.

**Statement of Net Cost.** The financial information contained in the Statement of Net Cost is not presented by programs that align with major goals and outputs described in the DoD strategic and performance plans required by the Government Performance and Results Act. Because financial processes and systems do not correlate costs with performance measures, revenues and expenses are reported by appropriation categories. The amounts presented in the Statement of Net Cost are based on funding, obligation, and disbursing transactions, which are not always recorded using accrual accounting. Army systems do not always record the transactions on an accrual basis as is required by the generally accepted accounting principles. To capture all cost and financing sources for the Army, the information presented also includes data from nonfinancial feeder systems. In addition, Army General Fund budgetary and proprietary information does not correlate. As a result, Defense Finance and Accounting Service Indianapolis Operations made \$14.9 billion in unsupported adjustments to force costs to agree with obligation information. Specifically, these adjustments forced costs reported on the Statement of Net Cost to match the value of Expended Appropriations minus the amount of Capitalized Assets reported on the Statement of Financing.

**Statement of Budgetary Resources.** The Army accounting systems do not provide or capture data needed for obligations incurred or prior year obligations recovered in accordance with Office of Management and Budget Circular No. A-11, “Preparation, Submission, and Execution of the Budget Requirements.” Although the Army developed an alternative methodology to calculate these items, the amount of distortion cannot be reliably determined. The Statement of Budgetary Resources does not include eliminating entries and, therefore, a Disaggregated Statement of Budgetary Resources is included in the Required Supplementary Information section of the financial statements. The Army uses budget execution data, which is composed of transaction report codes, to prepare the monthly Standard Form 133 and the quarterly Federal Agencies Centralized Trial Balance System II budgetary general ledger accounts. Defense Finance and Accounting Service Indianapolis Operations personnel then use the Federal Agencies Centralized Trial Balance System II data to prepare the Statement of Budgetary Resources. Because both the Standard Form 133 and the Statement of Budgetary Resources are prepared using budget execution data, there is no true reconciliation between the two reports. Office of Management and Budget Circular No. A-136, “Financial Reporting Requirements,” states that the Statement of Budgetary Resources should be predominantly derived from an entity’s budgetary general ledger, instead of being based on budget execution data. In FY 2006,

Defense Finance and Accounting Service Indianapolis Operations prepared \$1.4 billion in unsupported adjustments that affected general ledger accounts used in the Statement of Budgetary Resources.

Defense Finance and Accounting Service Indianapolis Operations reported budget execution data to the Department of the Treasury that did not agree with the data reported on the Army financial statements. The differences between the amounts reported on the Standard Forms 133 provided to the Office of Management and Budget and the Army General Fund Statement of Budgetary Resources totaled \$115.9 billion for fourth quarter FY 2005 and \$1.1 billion for first quarter FY 2006. This occurred because Defense Finance and Accounting Service Indianapolis Operations did not perform an effective reconciliation among Federal Agencies Centralized Trial Balance System II data, the Army General Fund Statement of Budgetary Resources, and the Standard Form 133 prepared for the Army. As a result, Defense Finance and Accounting Service Indianapolis Operations used one set of budget execution data to manage Army funds, but provided the Department of the Treasury a different set of budget execution data for the Office of Management and Budget's use. Also, Defense Finance and Accounting Service Indianapolis Operations reported inaccurate and misleading budget execution data on the Standard Form 133 provided to the Army, Army Statements of Budgetary Resources and related footnote, and to the Department of the Treasury for the Standard Forms 133 provided to the Office of Management and Budget. In addition, Defense Finance and Accounting Service Indianapolis Operations will perpetuate the material differences in the newly-fielded accounting system if the differences are not corrected.

**Statement of Financing.** The Office of Management and Budget requires a consolidated Statement of Financing, except for the budgetary information used to calculate net obligations, which must be presented on a combined basis. However, the Statement of Financing for the Army General Fund is prepared on a combined basis. Also, because the differences between the Statement of Net Cost and the Statement of Financing were not reconciled, the Statement of Financing does not accurately present the relationship between budgetary obligations incurred by the Army General Fund and its Net Cost of Operations. For example, Defense Finance and Accounting Service Indianapolis Operations prepared \$14.8 billion in unsupported adjustments to force costs to agree with obligation information.

**Other Reportable Conditions.** During FY 2006, as part of our financial-related audits, we noted deficiencies related to contingent legal liabilities and cash in the custody of agents.

The Army legal representation process did not provide meaningful assessments of potential liabilities and was not linked to the Army process for reporting and disclosing contingent legal liabilities on the financial statements. The legal representation letter from the Army Office of General Counsel and its attached management schedule did not corroborate either the \$205.7 million reported on the Balance Sheet as part of Non-Federal Other Liabilities or the \$307.8 million disclosed as contingent legal liabilities on footnote 16 in the FY 2006 Army General Fund Financial Statements.

Internal and physical controls over Army Cash and Other Monetary Assets were inadequate. The auditors also concluded that cash in the custody of agents reported on the Monthly Accountability Form (Standard Form 1219) was unreliable and unauditible. The Defense Finance and Accounting Service Indianapolis Operations used the monthly Consolidated Statement of Accountability to make a \$1.78 billion adjustment to the accounting records. This occurred because the Army and the Defense Finance and Accounting Service were not in compliance with reporting and control requirements mandated by the Office of Management and Budget and DoD. As a result, there was no assurance that cash transactions were recorded, accumulated, and reported properly and that cash was adequately safeguarded. In addition, the Army may have materially overstated the \$1.78 billion of Cash and Other Monetary Assets reported on the Army General Fund Balance Sheet.

These financial management deficiencies are indications of material weaknesses and reportable conditions in internal control that may adversely affect any decision by Army management that is based, in whole or in part, on information that is inaccurate because of these deficiencies. Financial information reported by DoD may also contain misstatements resulting from these deficiencies.



## Compliance with Laws and Regulations

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

**Statutory Financial Management Systems Reporting Requirements.** The Army is required to comply with financial management systems reporting requirements. For example, the Federal Financial Management Information Act of 1996 requires the Army to establish and maintain financial management systems that comply substantially with Federal financial management systems requirements, applicable Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level. In addition, the Federal Managers' Financial Integrity Act of 1982 requires DoD to evaluate the systems and to annually report whether those systems are in compliance with applicable requirements. The Act requires that each agency develop and maintain an integrated agency accounting and financial management system, including financial reporting and internal control. The system should comply with internal control standards and applicable accounting principles, standards, and requirements; and it should provide for complete, reliable, consistent, and timely information.

The Army acknowledged that many of its critical financial management and feeder systems do not comply substantially with Federal financial management systems requirements, Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level. The Army was also unable to comply with the Chief Financial Officers Act because its financial management systems were not integrated, and it has acknowledged that many of its financial management and feeder systems do not comply with applicable Federal accounting standards.

In an attempt to comply with statutory reporting requirements and applicable financial systems requirements in the future, the Secretary of Defense has initiated a comprehensive financial management reform program. DoD is currently undergoing a major reevaluation of the ways in which it performs its financial management operations. The centerpiece of this financial management reform effort is the development of a DoD-Wide Business Enterprise Architecture. The Business Enterprise Architecture essentially will be a blueprint describing the Department's future financial management systems and processes.

**Government Performance and Results Act.** The Government Performance and Results Act requires each Federal agency to prepare a strategic plan and annual performance plans and reports. The Army did not comply with the Government Performance and Results Act because it did not have cost accounting systems in place to collect, process, and report operating costs. This resulted in the Army General Fund Statement of Net Cost being unable to provide cost-of-operations data that were consistent with the Government Performance and Results Act performance goals and measures.

## Audit Disclosures

The Assistant Secretary of the Army (Financial Management and Comptroller) acknowledged to us on January 27, 2006, that the Army financial management systems cannot provide adequate evidence supporting various material amounts on the financial statements. Therefore, we did not conduct detailed testing related to the previously identified deficiencies. In addition, we did not perform audit work related to the following selected provisions of laws and regulations.

- Antideficiency Act
- Provisions Governing Claims of the United States Government
- Federal Credit Reform Act of 1990
- Pay and Allowance System for Civilian Employees
- Prompt Payment Act

This report does not include recommendations to correct the material internal control weaknesses and instances of noncompliance because previous audit reports contained recommendations for corrective actions.



## LIMITATIONS



### LIMITATIONS OF THE FINANCIAL STATEMENTS

The financial statements have been prepared to report the financial position and results of operations for the entity, pursuant to the requirements of Title 31, United States Code, section 3515(b).

While the statements have been prepared from the books and records of the entity, in accordance with the formats prescribed by the Office of Management and Budget, the statements are in addition to the financial reports used to monitor and control budgetary resources which are prepared from the same books and records.

The statements should be read with the realization that they are for a component of the United States Government, a sovereign entity.

**CONSOLIDATED BALANCE SHEET**

As of September 30, 2006 and 2005 (\$ in Thousands)

	2006 Consolidated		2005 Consolidated	
<b>ASSETS (Note 2)</b>				
Intragovernmental:				
Fund Balance with Treasury (Note 3)				
Entity	\$	875,344	\$	623,330
Non-Entity Seized Iraqi Cash		0		0
Non-Entity-Other		0		0
Investments (Note 4)		0		0
Accounts Receivable (Note 5)		243,005		366,622
Other Assets (Note 6)		8,670		0
Total Intragovernmental Assets	\$	1,127,019	\$	989,952
Cash and Other Monetary Assets (Note 7)	\$	0	\$	0
Accounts Receivable, Net (Note 5)		9,355		12,035
Loans Receivable (Note 8)		0		0
Inventory and Related Property, Net (Note 9)		17,939,567		15,933,141
General Property, Plant and Equipment, Net (Note 10)		1,267,070		1,228,213
Investments (Note 4)		0		0
Other Assets (Note 6)		417,914		333,741
<b>TOTAL ASSETS</b>	<b>\$</b>	<b>20,760,925</b>	<b>\$</b>	<b>18,497,082</b>
<b>LIABILITIES (Note 11)</b>				
Intragovernmental:				
Accounts Payable (Note 12)	\$	78,917	\$	105,603
Debt (Note 13)		0		0
Other Liabilities (Note 15 & 16)		58,150		75,579
Total Intragovernmental Liabilities	\$	137,067	\$	181,182
Accounts Payable (Note 12)	\$	576,037	\$	295,820
Military Retirement and Other Federal Employment Benefits (Note 17)		262,499		286,523
Environmental and Disposal Liabilities (Note 14)		0		0
Loan Guarantee Liability (Note 8)		0		0
Other Liabilities (Note 15 and Note 16)		468,617		642,522
<b>TOTAL LIABILITIES</b>	<b>\$</b>	<b>1,444,220</b>	<b>\$</b>	<b>1,406,047</b>
<b>NET POSITION</b>				
Unexpended Appropriations - Earmarked Funds (Note 23)	\$	0	\$	0
Unexpended Appropriations - Other Funds		0		0
Cumulative Results of Operations - Earmarked Funds		0		0
Cumulative Results of Operations - Other Funds		19,316,705		17,091,035
<b>TOTAL NET POSITION</b>	<b>\$</b>	<b>19,316,705</b>	<b>\$</b>	<b>17,091,035</b>
<b>TOTAL LIABILITIES AND NET POSITION</b>	<b>\$</b>	<b>20,760,925</b>	<b>\$</b>	<b>18,497,082</b>

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

Department of Defense - Army Working Capital Fund

**CONSOLIDATED STATEMENT OF NET COST***As of September 30, 2006 and 2005 (\$ in Thousands)*

	<b>2006 Consolidated</b>	<b>2005 Consolidated</b>
<b>Program Costs</b>		
Gross Costs	\$ 15,905,976	\$ 12,616,600
(Less: Earned Revenue)	(17,697,044)	(14,474,627)
Net Program Costs	\$ (1,791,068)	\$ (1,858,027)
<b>Cost Not Assigned to Programs</b>	0	0
<b>(Less: Earned Revenue Not Attributable to Programs)</b>	0	0
<b>Net Cost of Operations</b>	<b>\$ (1,791,068)</b>	<b>\$ (1,858,027)</b>

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

**CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION**

As of September 30, 2006 and 2005 (\$ in Thousands)

	Earmarked Funds		All Other Funds	
<b>CUMULATIVE RESULTS OF OPERATIONS</b>				
<b>Beginning Balances</b>	\$	0	\$	17,091,034
<b>Prior Period Adjustments:</b>				
Changes in Accounting Principles (+/-)		0		0
Corrections of errors (+/-)		0		0
<b>Beginning Balances, as adjusted</b>	\$	0	\$	17,091,034
<b>Budgetary Financing Sources:</b>		0		0
Appropriations received		0		0
Appropriations transferred-in/out (+/-)		0		0
Other Adjustments (recissions, etc.) (+/-)		0		0
Appropriations used		0		459,521
Nonexchange revenue		0		0
Donations and forfeitures of cash and cash equivalents		0		0
Transfers-in/out without reimbursement (+/-)		0		0
Other budgetary financing sources (+/-)		0		0
<b>Other Financing Sources:</b>		0		0
Donations and forfeitures of property		0		0
Transfers-in/out without reimbursement (+/-)		0		7
Imputed financing from costs absorbed by others		0		157,074
Other (+/-)		0		(181,999)
<b>Total Financing Sources</b>	\$	0	\$	434,603
<b>Net Cost of Operations (+/-)</b>		0		(1,791,068)
<b>Net Change</b>	\$	0	\$	2,225,671
<b>Ending Balances</b>	\$	0	\$	19,316,705
<b>UNEXPENDED APPROPRIATIONS</b>				
<b>Beginning Balances</b>	\$	0	\$	0
<b>Prior Period Adjustments:</b>				
Changes in accounting principles (+/-)		0		0
Corrections of errors (+/-)		0		0
<b>Beginning Balances, as adjusted</b>	\$	0	\$	0
<b>Budgetary Financing Sources:</b>		0		459,521
Appropriations received		0		459,521
Appropriations transferred-in/out (+/-)		0		0
Other adjustments (rescissions, etc) (+/-)		0		0
Appropriations used		0		(459,521)
Nonexchange revenue		0		0
Donations and forfeitures of cash and cash equivalents		0		0
Transfers-in/out without reimbursement (+/-)		0		0
Other budgetary financing sources (+/-)		0		0
<b>Other Financing Sources:</b>		0		0
Donations and forfeitures of property		0		0
Transfers-in/out without reimbursement (+/-)		0		0
Imputed financing from costs absorbed by others		0		0
Other (+/-)		0		0
<b>Total Financing Sources</b>	\$	0	\$	0
<b>Net Cost of Operations (+/-)</b>		0		0
<b>Net Change</b>		0		0
<b>Ending Balances</b>	\$	0	\$	0

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

Department of Defense - Army Working Capital Fund

**CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION**

As of September 30, 2006 and 2005 (\$ in Thousands)

	Eliminations	2006 Consolidated	2005 Consolidated
<b>CUMULATIVE RESULTS OF OPERATIONS</b>			
<b>Beginning Balances</b>	\$ 0	\$ 17,091,034	\$ 15,370,834
<b>Prior Period Adjustments:</b>			
Changes in Accounting Principles (+/-)	0	0	0
Corrections of errors (+/-)	0	0	0
<b>Beginning Balances, as adjusted</b>	\$ 0	\$ 17,091,034	\$ 15,370,834
<b>Budgetary Financing Sources:</b>	0	0	0
Appropriations received	0	0	0
Appropriations transferred-in/out (+/-)	0	0	0
Other Adjustments (recissions, etc.) (+/-)	0	0	0
Appropriations used	0	459,521	53
Nonexchange revenue	0	0	0
Donations and forfeitures of cash and cash equivalents	0	0	0
Transfers-in/out without reimbursement (+/-)	0	0	(515,944)
Other budgetary financing sources (+/-)	0	0	0
<b>Other Financing Sources:</b>			
Donations and forfeitures of property	0	0	0
Transfers-in/out without reimbursement (+/-)	0	7	0
Imputed financing from costs absorbed by others	0	157,074	147,135
Other (+/-)	0	(181,999)	230,930
<b>Total Financing Sources</b>	\$ 0	\$ 434,603	\$ (137,826)
<b>Net Cost of Operations (+/-)</b>	0	(1,791,068)	(1,858,027)
<b>Net Change</b>	\$ 0	\$ 2,225,671	\$ 1,720,201
<b>Ending Balances</b>	\$ 0	\$ 19,316,705	\$ 17,091,035
<b>UNEXPENDED APPROPRIATIONS</b>			
<b>Beginning Balances</b>	\$ 0	\$ 0	\$ 53
<b>Prior Period Adjustments:</b>			
Changes in accounting principles (+/-)	0	0	0
Corrections of errors (+/-)	0	0	0
<b>Beginning Balances, as adjusted</b>	\$ 0	\$ 0	\$ 53
<b>Budgetary Financing Sources:</b>			
Appropriations received	0	459,521	0
Appropriations transferred-in/out (+/-)	0	0	0
Other adjustments (rescissions, etc) (+/-)	0	0	0
Appropriations used	0	(459,521)	(53)
Nonexchange revenue	0	0	0
Donations and forfeitures of cash and cash equivalents	0	0	0
Transfers-in/out without reimbursement (+/-)	0	0	0
Other budgetary financing sources (+/-)	0	0	0
<b>Other Financing Sources:</b>			
Donations and forfeitures of property	0	0	0
Transfers-in/out without reimbursement (+/-)	0	0	0
Imputed financing from costs absorbed by others	0	0	0
Other (+/-)	0	0	0
<b>Total Financing Sources</b>	\$ 0	\$ 0	\$ (53)
<b>Net Cost of Operations (+/-)</b>	0	0	0
<b>Net Change</b>	0	0	(53)
<b>Ending Balances</b>	\$ 0	\$ 0	\$ 0

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

**COMBINED STATEMENT OF BUDGETARY RESOURCES**

As of September 30, 2006 and 2005 (\$ in Thousands)

	Budgetary Financing Accounts		Non-Budgetary Financing Accounts	
	2006 Combined	2005 Combined	2006 Combined	2005 Combined
<b>BUDGETARY RESOURCES</b>				
Unobligated balance, brought forward, October 1	\$ 1,176,499	\$ 1,530,241	\$ 0	\$ 0
Recoveries of prior year unpaid obligations	1,372,092	1,435,592	0	0
Budget authority				
Appropriation	459,521	0	0	0
Borrowing authority	0	0	0	0
Contract authority	9,970,837	10,951,904	0	0
Spending authority from offsetting collections				
Earned				
Collected	14,013,375	14,180,281	0	0
Change in receivables from Federal sources	(142,805)	(29,369)	0	0
Change in unfilled customer orders				
Advance received	39,953	19,271	0	0
Without advance from Federal sources	59,027	(774,190)	0	0
Anticipated for rest of year, without advances	0	0	0	0
Previously unavailable	0	0	0	0
Expenditure transfers from trust funds	0	0	0	0
Subtotal	24,399,908	24,347,897	0	0
Nonexpenditure transfers, net, anticipated and actual	0	(515,944)	0	0
Temporarily not available pursuant to Public Law	0	0	0	0
Permanently not available	(10,299,718)	(8,798,841)	0	0
<b>Total Budgetary Resources</b>	<b>\$ 16,648,781</b>	<b>\$ 17,998,945</b>	<b>\$ 0</b>	<b>\$ 0</b>
<b>Status of Budgetary Resources:</b>				
Obligations incurred:				
Direct	\$ 0	\$ 0	\$ 0	\$ 0
Reimbursable	14,857,316	16,822,445	0	0
Subtotal	\$ 14,857,316	\$ 16,822,445	\$ 0	\$ 0
Unobligated balance:				
Apportioned	1,791,465	1,176,499	0	0
Exempt from apportionment	0	0	0	0
Subtotal	1,791,465	1,176,499	0	0
Unobligated balance not available	0	1	0	0
<b>Total status of budgetary resources</b>	<b>\$ 16,648,781</b>	<b>\$ 17,998,945</b>	<b>\$ 0</b>	<b>\$ 0</b>
<b>Change in Obligated Balance:</b>				
Obligated balance, net				
Unpaid obligations, brought forward, October 1	\$ 10,331,509	\$ 8,953,395	\$ 0	\$ 0
Less: Uncollected customer payments from Federal sources, brought forward, October 1	(4,181,756)	(4,985,314)	0	0
Total unpaid obligated balance	6,149,753	3,968,081	0	0
Obligations incurred net (+/-)	\$ 14,857,316	\$ 16,822,445	\$ 0	\$ 0
Less: Gross outlays	(14,260,837)	(14,008,740)	0	0
Obligated balance transferred, net				
Actual transfers, unpaid obligations (+/-)	0	0	0	0
Actual transfers, uncollected customer payments from Federal sources (+/-)	0	0	0	0
Total Unpaid obligated balance transferred, net	0	0	0	0
Less: Recoveries of prior year unpaid obligations, actual	(1,372,092)	(1,435,592)	0	0
Change in uncollected customer payments from Federal sources (+/-)	83,777	803,558	0	0
Obligated balance, net, end of period				
Unpaid obligations	9,555,896	10,331,509	0	0
Less: Uncollected customer payments (+/-) from Federal Sources(-)	(4,097,980)	(4,181,756)	0	0
Total, unpaid obligated balance, net, end of period	5,457,916	6,149,753	0	0
<b>Net Outlays</b>				
<b>Net Outlays:</b>				
Gross outlays	14,260,837	14,008,740	0	0
Less: Offsetting collections	(14,053,327)	(14,199,551)	0	0
Less: Distributed Offsetting receipts	0	0	0	0
<b>Net Outlays</b>	<b>\$ 207,510</b>	<b>\$ (190,811)</b>	<b>\$ 0</b>	<b>\$ 0</b>

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



Department of Defense - Army Working Capital Fund

**CONSOLIDATED STATEMENT OF FINANCING**

As of September 30, 2006 and 2005 (\$ in Thousands)

	2006 Consolidated	2005 Consolidated
<b>Resources Used to Finance Activities:</b>		
Budgetary Resources Obligated		
Obligations incurred	\$ 14,857,316	\$ 16,822,445
Less: Spending authority from offsetting collections and recoveries (-)	(15,341,642)	(14,831,585)
Obligations net of offsetting collections and recoveries	\$ (484,326)	\$ 1,990,860
Less: Offsetting receipts (-)	0	0
Net obligations	\$ (484,326)	\$ 1,990,860
Other Resources		
Donations and forfeitures of property	0	0
Transfers in/out without reimbursement (+/-)	7	1
Imputed financing from costs absorbed by others	157,074	147,135
Other (+/-)	(181,998)	230,930
Net other resources used to finance activities	\$ (24,917)	\$ 378,066
<b>Total resources used to finance activities</b>	<b>\$ (509,243)</b>	<b>\$ 2,368,926</b>
<b>Resources Used to Finance Items not Part of the Net Cost of Operations</b>		
Change in budgetary resources obligated for goods, services and benefits ordered but not yet provided		
Undelivered Orders (-)	\$ 1,113,635	\$ (1,514,883)
Unfilled Customer Orders	98,980	(754,919)
Resources that fund expenses recognized in prior periods	(24,024)	(21,283)
Budgetary offsetting collections and receipts that do not affect net cost of operations	0	0
Resources that finance the acquisition of assets	(8,630,584)	(7,998,973)
Other resources or adjustments to net obligated resources		
Less: Trust or Special Fund Receipts Related to Exchange in the entitys Budget (-)	0	0
Other (+/-)	181,991	(230,931)
<b>Total resources used to finance items not part of the net cost of operations</b>	<b>\$ (7,260,002)</b>	<b>\$ (10,520,989)</b>
<b>Total resources used to finance the net cost of operations</b>	<b>\$ (7,769,245)</b>	<b>\$ (8,152,063)</b>
<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:		
Increase in annual leave liability	\$ 5,056	\$ 28,898
Increase in environmental and disposal liability	0	0
Upward/Downward reestimates of credit subsidy expense (+/-)	0	0
Increase in exchange revenue receivable from the the public (+/-)	0	0
Other (+/-)	1,515	0
Total components of Net Cost of Operations that will require or generate resources in future periods	\$ 6,571	\$ 28,898
Components not Requiring or Generating Resources:		
Depreciation and amortization	31,293	95,884
Revaluation of assets or liabilities (+/-)	781,326	699,913
Other (+/-)		
Trust Fund Exchange Revenue	0	0
Cost of Goods Sold	5,718,283	6,025,370
Operating Material & Supplies Used	0	0
Other	(559,296)	(556,029)
Total components of Net Cost of Operations that will not require or generate resources	\$ 5,971,606	\$ 6,265,138
<b>Total components of net cost of operations that will not require or generate resources in the current period</b>	<b>\$ 5,978,177</b>	<b>\$ 6,294,036</b>
<b>Net Cost of Operations</b>	<b>\$ (1,791,068)</b>	<b>\$ (1,858,027)</b>

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



## Note 1. Significant Accounting Policies

### 1.A. Basis of Presentation

These financial statements have been prepared to report the financial position and results of operations of the Army Working Capital Fund (AWCF), as required by the Chief Financial Officers Act of 1990, amended by the Government Management Reform Act of 1994, and other appropriate legislation. The financial statements have been prepared from the books and records of AWCF in accordance with the Department of Defense (DoD) Financial Management Regulation, Office of Management and Budget (OMB) Circular A-136, Financial Reporting Requirements, and to the extent possible, Federal generally accepted accounting principles (Federal GAAP).

The accompanying financial statements account for all resources for which AWCF is responsible. Under the above guidance, classified assets, programs, and operations have been excluded from the statement, or otherwise aggregated and reported, in such a manner that they are no longer classified. The AWCF financial statements are in addition to the financial reports also prepared by AWCF pursuant to OMB directives that are used to monitor and control AWCF use of budgetary resources.

The AWCF is unable to fully implement all elements of Federal GAAP and OMB Circular A-136 due to limitations of its financial and nonfinancial management processes and systems. The Army derives its reported values and information for major asset and liability categories largely from nonfinancial feeder systems, such as inventory and logistics systems. These systems were designed to support reporting requirements focusing on maintaining accountability over assets and reporting the status of Federal appropriations rather than preparing financial statements in accordance with Federal GAAP. As a result, AWCF cannot currently implement every aspect of Federal GAAP and OMB Circular A-136. The AWCF continues to implement processes and system improvements addressing the limitations of its financial and nonfinancial feeder systems. As of year-end fiscal year (FY) 2005, AWCF has agreed with eight auditor-identified financial statement material weaknesses: (1) financial management systems and processes; (2) inventory; (3) general property, plant, and equipment; (4) intragovernmental transactions and eliminations; (5) accounting adjustments; (6) accounts payable; (7) Statement of Net Cost; and (8) Statement of Financing.

The accounting structure of Federal agencies is designed to reflect both accrual and budgetary accounting transactions. Under the accrual method of accounting, revenues are recognized when earned, and expenses are recognized when incurred, without regard to receipt or payment of cash. The budgetary accounting principles, on the other hand, are designed to recognize the obligation of funds according to legal requirements, which in many cases is prior to the occurrence of an accrual-based transaction. The recognition of budgetary accounting transactions is essential for compliance with legal constraints and controls over the use of Federal funds.

### 1.B. Mission of the Reporting Entity

The AWCF is part of the Defense Working Capital Fund, and is divided into two separate business areas: Supply Management and Industrial Operations. These business areas ensure delivery of critical items, such as petroleum products, repair parts, consumable supplies, depot maintenance services, munitions, and weapons to support the deployment and projection of lethal force as and when required by the nation.

### 1.C. Appropriations and Funds

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

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

### 1.D. Basis of Accounting

The AWCF generally records transactions on an accrual accounting basis as is required by Federal GAAP. For FY 2006, AWCF financial management systems are unable to meet all of the requirements for full accrual accounting. Many AWCF financial and nonfinancial feeder systems and processes were designed and implemented prior to the issuance of Federal GAAP for Federal agencies and, therefore, were not designed to collect and record financial information on the full accrual accounting basis as required by Federal GAAP.

The AWCF has undertaken efforts to determine the actions required to bring all of its financial and nonfinancial feeder systems and processes into compliance with all elements of Federal GAAP. One such action is the current revision of its accounting systems to record transactions

based on the US Standard General Ledger (USSGL). At this time, not all AWCF accounting systems are USSGL compliant. In addition, with the full implementation of the Logistics Modernization Program (LMP), AWCF will be in compliance with Statement of Federal Financial Accounting Standard (SFFAS) No. 4, "Managerial Cost Accounting Concepts and Standards for the Federal Government." As of December 31, 2003, LMP has been implemented at Tobyhanna Army Depot, Communications–Electronics Command, and other Army Materiel Command activities. Until LMP is fully implemented and all of the processes are updated to collect and report financial information as required by Federal GAAP, some of AWCF financial data will be based on budgetary transactions (obligations, disbursements, collections), and nonfinancial feeder systems. For example, most financial information presented on the Statement of Net Costs is based on accrued costs; however, some of the financial information is based on obligations and disbursements.

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

### **1.E. Revenues and Other Financing Sources**

The AWCF Industrial Operations activities recognize revenue according to the percentage-of-completion method. Supply Management activities recognize revenue when an inventory item is sold. Prices set for products and services offered through AWCF are intended to recover the full costs (cost plus administrative fees) incurred by these activities. Unearned revenue is recorded as deferred revenue until earned.

Other financing sources reported by AWCF do not include nonmonetary support provided by our allies for common defense and mutual security. The United States has agreements with foreign countries that include both direct and indirect sharing of costs that each country incurs in support of the same general purpose. Examples include countries where there is a mutual or reciprocal defense agreement, where U.S. troops are stationed, or where the U.S. Fleet is serviced in a port. The DoD is reviewing these types of financing and cost reductions in order to establish accounting policies and procedures to identify what, if any, of these costs are appropriate for disclosure in AWCF financial statements in accordance with Federal GAAP. Recognition of support provided by host nations would affect both financing sources and expense recognition.

### **1.F. Recognition of Expenses**

For financial reporting purposes, DoD policy requires the recognition of operating expenses in the period incurred. However, because AWCF financial and nonfinancial feeder systems were not designed to collect and record financial information on the full accrual accounting basis, accrual adjustments are made for major items such as payroll expenses and accounts payable. Expenditures for capital and other long-term assets are not recognized as expenses in AWCF operations until depreciated, as in the case of property, plant, and equipment (PP&E). Net increases or decreases in unexpended appropriations are recognized as a change in the net position.

The AWCF adjusted operating expenses as a result of the elimination of balances between DoD Components. See Note 18, Disclosures Related to the Statement of Net Cost, for disclosure of elimination amounts.

### **1.G. Accounting for Intragovernmental Activities**

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

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

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

The AWCF civilian employees participate in the Civil Service Retirement System (CSRS) or the Federal Employees Retirement Systems (FERS). Employees and personnel covered by FERS also have varying coverage under Social Security. The AWCF funds a portion of civilian and military pensions. Reporting civilian pensions under CSRS and FERS is the responsibility of the Office of Personnel Management (OPM). The AWCF recognizes an imputed expense for the portion of civilian employee pensions and other retirement benefits funded by

OPM in the Statement of Net Cost and recognizes corresponding imputed revenue from the civilian employee pensions and other retirement benefits in the Statement of Changes in Net Position.

To prepare reliable financial statements, transactions occurring between components or activities within AWCF must be eliminated for consolidated financial reporting purposes. However, AWCF cannot accurately identify all intragovernmental transactions by its related components or activities because AWCF systems do not track buyer and seller data needed to match related transactions. The Defense Finance and Accounting Service (DFAS) is responsible for eliminating transactions between components or activities of AWCF. Beginning in FY 1999, seller entities within AWCF provided summary seller-side balances for revenue, accounts receivable, transfers-in/out, and unearned revenue to the buyer-side internal AWCF accounting offices. In most cases, the buyer-side records have been adjusted to recognize unrecorded costs and accounts payable. The AWCF intragovernmental balances are then eliminated. The DoD and AWCF are developing long-term system 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 effectively with existing or foreseeable resources.

The Department of the Treasury Financial Management Service (FMS), is responsible for eliminating transactions between the DoD and other federal agencies. The Treasury Financial Manual, Part 2 – Chapter 4700, “Agency Reporting Requirements for the Financial Report of the United States Government” and the Treasury’s “Federal Intragovernmental Transactions Accounting Policy Guide,” provide guidance for reporting and reconciling intragovernmental balances. While the AWCF is unable to fully reconcile intragovernmental transactions with all federal partners, the AWCF is able to reconcile balances pertaining to borrowings from the U.S. Treasury and the Federal Financing Bank, Federal Employees’ Compensation Act transactions with the Department of Labor (DOL), and benefit program transactions with the Office of Personnel Management (OPM). The DoD’s proportionate share of public debt and related expenses to the federal government are not included. The federal government does not apportion debt and its related costs to federal agencies. The DoD’s financial statements, therefore, do not report any portion of the public debt or interest thereon, nor do the statements report the source of public financing whether from issuance of debt or tax revenues.

## **1.H. Transactions with Foreign Governments and International Organizations**

Each year, AWCF sells defense items and services to foreign governments and international organizations, primarily under the provisions of the Arms Export Control Act of 1976. Under the provisions of the Act, DoD has the authority to sell defense articles and services to foreign countries and international organizations generally at no profit or loss to the U.S. government. Customers may be required to make payments in advance.

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

The Department of the Treasury accounts maintain AWCF monetary financial resources. The DFAS, Military Services, U.S. Army Corps of Engineers (USACE) disbursing stations as well as the Department of State financial service centers process the majority of cash collections, disbursements, and adjustments for the Federal government worldwide. Each disbursing station prepares monthly reports that provide information to the Department of the Treasury on check issues, electronic fund transfers, interagency transfers, and deposits.

In addition, DFAS sites and 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 Department of the Treasury’s system. Differences between AWCF and Department of the Treasury’s records sometime result and are subsequently reconciled. Material disclosures are provided in Note 3. Differences between accounting offices’ detail level records and Department of the Treasury FBWT accounts are disclosed in Note 3, Fund Balance with Treasury, specifically differences caused by in-transit disbursements and unmatched disbursements, which are not recorded in the accounting offices’ detail level records.

## **1.J. Foreign Currency**

Not applicable.

## **1.K. Accounts Receivable**

As presented in the Balance Sheet, accounts receivable includes accounts, claims, and refunds receivables from other Federal agencies and the public. Federal accounts receivable arise generally from the provision of goods and services to other Federal agencies and, with the exception of occasional billing disputes, are considered to be fully collectible. Receivables from the public generally arise from the provision of goods and services to state, local, and foreign governments. Refunds receivable, however, are overpayments by the Federal government in the process of being collected. An allowance for doubtful accounts is established for reporting purposes based on past experience in the collection of accounts receivable and analysis of outstanding balances by fund type. The AWCF methodology recognizes an allowance of

50 percent for all nonfederal debt between 180 days and two years old, and a 100 percent allowance for all nonfederal debt over two years old. The allowance is updated annually, based on the aged accounts receivable at the end of the 2nd Quarter. The AWCF does not recognize an allowance for estimated uncollectible amounts from other Federal agencies. Claims against other Federal agencies are to be resolved between the agencies (per Code of Federal Regulations 4 CFR 101). Material disclosures are provided in Note 5, Accounts Receivable.

### **1.L. Loans Receivable**

Not applicable.

### **1.M. Inventories and Related Property**

The inventory reported in AWCF financial statements is not all valued using the same valuation method. The AWCF inventories are reported using the Latest Acquisition Cost (LAC), which approximates historical cost, adjusted for holding gains and losses, and Moving Average Cost (MAC), which computes a new average cost each time a purchase is made. The AWCF uses LAC method because its inventory systems were designed for material management rather than accounting, except for activities that have transitioned to LMP. The systems provide accountability and visibility over inventory items. They do not maintain, however, the exact historical cost data necessary to comply with SFFAS No. 3, "Accounting for Inventory and Related Property," nor can they directly produce financial transactions using USSGL, as required by the Federal Financial Management Improvement Act of 1996. The AWCF transition to LMP will also allow the use of a MAC methodology for valuing inventory that, when fully implemented, will allow AWCF to comply with SFFAS No. 3 (see Note 9, Inventory and Related Property).

Approximately 22 percent of the AWCF's inventory value is now being reported from systems that have transitioned to moving average cost functionality. However, since the on-hand balances which transitioned were not, for the most part, baselined to auditable historical cost, the reported values remain noncompliant with SFFAS 3 and GAAP.

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, 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 DoD material management activities. Operational cycles are irregular, and the military risks associated with stock-out positions have no commercial parallel. The AWCF holds material based on military need and support for contingencies. Therefore, AWCF does not attempt to account separately for items held for current or future sale.

In accordance with new DoD policy, the Army accounts for condemned material as excess, obsolete, and unserviceable. The net value of this type of condemned material is zero, because the costs of disposal are greater than the potential scrap value. Potentially redistributable material, presented in previous years as excess, obsolete and unserviceable, is included in held for use or held for repair categories according to its condition.

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

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

Not applicable.

### **1.O. General Property, Plant and Equipment**

General Property, Plant & Equipment (PP&E) assets are capitalized at historical acquisition cost plus capitalized improvements when an asset has a useful life of two or more years, and when the acquisition cost equals or exceeds DoD capitalization threshold. The capitalizations threshold was revised from \$100 thousand to \$20 thousand for real property. The current \$100 thousand capitalization threshold remained unchanged for the remaining General PP&E categories. The Army will validate existing real property values and implement sustainable business processes prior to incorporating the revised capitalization threshold for financial statement reporting. All General PP&E, other than land, is depreciated on a straight-line basis. Land is not depreciated.

Prior to FY 1996, General PP&E with an acquisition cost of \$15 thousand, \$25 thousand, and \$50 thousand for FY 1993, FY 1994, and FY 1995 respectively, and an estimated useful life of two or more years was capitalized. These assets remain capitalized and reported on AWCF financial statements.

For AWCF activities, all PP&E used in the performance of their mission is categorized as General PP&E, whether or not it meets the definition of any other PP&E categories. Heritage Assets and Stewardship Land owned or maintained on AWCF installations are reported in the Required Supplemental Stewardship Information Report of the Army General Fund. Material disclosures are provided in Note 10, General PP&E, Net.

Internal use software is capitalized at cost if the acquisition cost is \$100 thousand or more. For commercial off-the-shelf software, the capitalized costs include the amount paid to the vendor for the software; for contractor-developed software, it includes the amount paid to a contractor to design, program, install, and implement the software. Capitalized costs for internally developed software include the full cost (direct and indirect) incurred during the software development stage. The estimated useful life for calculating amortization of software is two to five years using the straight-line method.

### **1.P. Advances and Prepayments**

The AWCF records payments made prior to the receipt of goods and services as advances or prepayments and reports them as assets on the Balance Sheet. The AWCF recognizes advances and prepayments as expenses when it receives the related goods and services.

### **1.Q. Leases**

Not applicable.

### **1.R. Other Assets**

The AWCF conducts business with commercial contractors under two primary types of contracts: fixed price and cost reimbursable. To alleviate the potential financial burden on the contractor that long-term contracts can cause, AWCF provides financing payments. Real property financing payments are based upon a percentage of completion. In accordance with SFFAS No. 1, "Accounting for Selected Assets and Liabilities," such payments are treated as construction in progress and are reported on the General PP&E line on the Balance Sheet and in Note 10, General PP&E, Net.

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

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

Contract financing payments are defined in the Federal Acquisition Regulations (FAR), Part 32, as authorized disbursements of monies to a contractor prior to acceptance of supplies or services by the Government. These payments are designed to alleviate the potential financial burden on contractors performing on certain long-term contracts and facilitate competition for defense contracts. Contract financing payments clauses are incorporated in the contract terms and conditions and may include advance payments, performance-based payments, commercial advance and interim payments, progress payments based on cost, and interim payments under certain cost-reimbursement contracts. Contract financing payments do not include invoice payments, payments for partial deliveries, lease and rental payments, or progress payments based on a percentage or stage of completion, which the Defense Federal Acquisitions Regulations Supplement (DFARS) authorizes only for construction of real property, shipbuilding, and ship conversion, alteration, or repair. Progress payments for real property and ships are reported as Construction in Progress in Note 10.

### **1.S. Contingencies and Other Liabilities**

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

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

### **1.T. Accrued Leave**

The AWCF reports as liabilities civilian annual leave that has been accrued and not used as of the balance sheet date. The liability reported at the end of the accounting period reflects the current pay rates.

## **1.U. Net Position**

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

Cumulative results of operations for AWCF represents the excess of revenues over expenses less refunds to customers and returns to the Department of the Treasury since fund inception. Beginning with FY 1998, the cumulative results also include donations and transfers-in/out of assets without reimbursement.

## **1.V. Treaties for Use of Foreign Bases**

Not applicable.

## **1.W. Comparative Data**

The financial statements and accompanying notes to the financial statements report the financial position and results of operations as of the end of the 4th Quarter, FY 2006. The DoD requires disclosure of variances exceeding 10 percent (when comparing prior year and current year statements) or two percent of total assets. The required disclosure threshold applies only to the Balance Sheet and Statement of Net Cost. In addition, DoD requires variance disclosure on some items not directly linked to the Balance Sheet or Statement of Net Cost.

## **1.X. Unexpended Obligations**

The AWCF obligates funds to provide goods and services for outstanding orders not yet delivered. The financial statements do not reflect this liability for payment for goods or services not yet delivered.

## **1.Y. 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 Department of the Treasury. These amounts should agree with the undistributed amounts reported on the departmental accounting reports. In-transit payments are those payments that have been made to other agencies or entities that have not been recorded in their accounting records. These payments are applied to the entities' outstanding accounts payable balance. In-transit collections are those collections from other agencies or entities that have not been recorded in the accounting records. These collections are also applied to the entities' accounts receivable balance.

The DoD policy is to allocate supported undistributed disbursements and collections between Federal and nonfederal categories based on the percentage of Federal and nonfederal accounts payable and accounts receivable. The AWCF records unsupported undistributed disbursements in accounts payable and unsupported undistributed collections in other liabilities.



**Note 2. Nonentity Assets**

As of September 30	2006	2005
<i>(Amounts in thousands)</i>		
1. Intragovernmental Assets		
A. Fund Balance with Treasury	\$ 0	\$ 0
B. Accounts Receivable	0	0
C. Total Intragovernmental Assets	\$ 0	\$ 0
2. Nonfederal Assets		
A. Cash and Other Monetary Assets	\$ 0	\$ 0
B. Accounts Receivable	0	0
C. Other Assets	0	0
D. Total Nonfederal Assets	\$ 0	\$ 0
3. Total Nonentity Assets	\$ 0	\$ 0
4. Total Entity Assets	\$ 20,760,925	\$ 18,497,082
5. Total Assets	\$ 20,760,925	\$ 18,497,082

**Definitions**

Nonentity assets are assets held by an entity but are not available for use in the operations of the entity. The Army Working Capital Fund (AWCF) does not have nonentity assets.

Entity assets are resources that AWCF has the authority to use or where management is legally obligated to use funds to meet entity obligations.

**Note 3. Fund Balance with Treasury**

As of September 30	2006	2005
<i>(Amounts in thousands)</i>		
1. Fund Balances		
A. Appropriated Funds	\$ 0	\$ 0
B. Revolving Funds	875,344	623,330
C. Trust Funds	0	0
D. Special Funds	0	0
E. Other Fund Types	0	0
F. Total Fund Balances	\$ 875,344	\$ 623,330
2. Fund Balances Per Treasury Versus Agency		
A. Fund Balance per Treasury	\$ 875,344	\$ 623,330
B. Fund Balance per AWCF	875,344	623,330
3. Reconciling Amount	\$ 0	\$ 0

**Fluctuations and/or Abnormalities**

Fund Balance with Treasury increased \$252.0 million, or 40 percent due to the following:

In 1st Quarter, FY 2006, the Army Working Capital Fund (AWCF) received a warrant for \$106.5 million in accordance with DoD Appropriation Act, 2006, P.L. 109-148, 119 STAT 2680. In 1st Quarter, FY 2006, AWCF distributed \$42.5 million for war reserves and Army combat uniforms to the Supply Management (SMA) business area and \$64.0 million to the Industrial Operations (IO) business area for industrial mobilization capacity.

In 3rd Quarter, FY 2006, AWCF received a warrant for \$348.3 million in accordance with Emergency Supplemental Appropriations Act for Defense, the Global War on Terror, and Hurricane Recovery, 2006, P.L. 109-234, 120 STAT 418. In 3rd Quarter, FY 2006, the SMA business area received \$92.1 million for war reserves and \$255.0 million for inventory augmentation. The IO business area received \$1.2 million for fuel cost increases.

In 4th Quarter, FY 2006, funds were appropriated to the Defense-Wide Defense Working Capital Fund in title IX, Division A of the Department of Defense Appropriations Act, 2006, P.L. 109-148, 119 STAT 2680. The IO business area received \$4.7 million for fuel cost increases.

The \$459.5 million in appropriations received, as discussed above, were offset by disbursements that exceeded collections during FY 2006 in the amount of \$207.5 million.

## Status of Fund Balance with Treasury

As of September 30 <i>(Amounts in thousands)</i>	2006	2005
1. Unobligated Balance		
A. Available	\$ 1,791,465	\$ 1,176,499
B. Unavailable	0	0
2. Obligated Balance not yet Disbursed	\$ 9,555,896	\$ 10,331,508
3. Nonbudgetary FBWT	\$ 0	\$ 0
4. NonFBWT Budgetary Accounts	\$ (10,472,017)	\$ (10,884,677)
5. Total	<u>\$ 875,344</u>	<u>\$ 623,330</u>

### Definitions

The Status of Fund Balance with Treasury consists of unobligated and obligated balances. These balances reflect the budgetary authority remaining for disbursements against current or future obligations. In addition, the Status includes various accounts that affect either budgetary reporting or Fund Balance with Treasury (FBWT), but not both.

Unobligated Balance represents the cumulative amount of budgetary authority that has not been set aside to cover outstanding obligations. Unobligated Balance is classified as available or unavailable and is associated with contract authority, customer orders, and appropriations.

Obligated Balance not yet Disbursed represents funds that have been obligated for goods that have not been received or goods and or services that have been received but have not been disbursed.

Nonbudgetary FBWT includes entity and nonentity FBWT accounts which do not have budgetary authority, such as unavailable receipt accounts or clearing accounts.

NonFBWT Budgetary Accounts include budgetary accounts that do not affect FBWT, such as contract authority, borrowing authority, and investment accounts. This category reduces the Status of Fund Balance with Treasury.

There are no restrictions on Unobligated Balances Available.

### Fluctuations and/or Abnormalities

Unobligated Balance Available increased \$615.0 million, or 52 percent from FY 2005 to FY 2006. This change is attributable to increased unfilled orders in the IO business area for repair of military equipment. During the 4th Quarter, FY 2006, the IO business area received \$436 million of reimbursable customer orders after AWCF customers received supplemental funding. These orders came from Army General Fund, Air Force, Marine Corps, and other DoD entities.

Obligated Balance not yet Disbursed decreased \$775.6 million, or 8 percent, from FY 2005 to FY 2006. Between FY 2005 and FY 2006, SMA business area disbursements remained relatively constant while net obligations decreased by \$722.3 million.

NonFBWT Budgetary Accounts decreased \$412.7 million, or 4 percent from FY 2005 to FY 2006. During FY 2005, AWCF received contract authority to incur obligations exceeding earnings in the SMA business area to support anticipated operational requirements in support of

contingency missions Operation Enduring Freedom, Iraqi Freedom, and Noble Eagle. In FY 2006, the SMA business area had a lower level of activity than in FY 2005. As a result, earnings and obligations were less in FY 2006 than in FY 2005 primarily due to customer funding shortfalls and reduced overall customer spending throughout the 3rd and 4th Quarters of FY 2006.

### Disclosures Related to Suspense/Budget Clearing Accounts

The Suspense/Budget Clearing Accounts shown above are maintained and reported by the Army General Fund. Some transactions relating to AWCF may be in suspense accounts, but are not identifiable. When they are identified to AWCF, they will be transferred from the suspense/clearing account to the correct Department of the Treasury appropriation.

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

As of September 30	2004	2005	2006	(Decrease)/ Increase from FY 2005 to 2006
<i>(Amounts in thousands)</i>				
1. Total Problem Disbursements, Absolute Value				
A. Unmatched Disbursements (UMDs)	\$ 25,484	\$ 10,064	\$ 4,843	\$ (5,221)
B. Negative Unliquidated Obligations (NULO)	3,810	3,773	2,703	(1,070)
2. Total In-transit Disbursements, Net	\$ 135,730	\$ 94,626	\$ 180,610	\$ 85,984

#### Definitions

An Unmatched Disbursement (UMD) occurs when a payment does not match to a corresponding obligation in the accounting system. Absolute value is the sum of the positive values of debit and credit transactions without regard to the sign (plus or minus).

A Negative Unliquidated Obligation (NULO) occurs when a payment is made against a valid obligation, but the payment is greater than the amount of the obligation recorded in the official accounting system. These payments have been made using available funds and are based on valid receiving reports for goods and services delivered under valid contracts.

In-transit Disbursements represent the net value of disbursements and collections made by a DoD disbursing activity on behalf of an accountable activity but have not been posted in an accounting system.

#### Fluctuations and/or Abnormalities

Unmatched Disbursements (UMD) decreased \$5.2 million or 52 percent from FY 2005 to FY 2006. This decrease is attributed to system and process improvements implemented in 1st Quarter, FY 2006 at Defense Finance and Accounting Service (DFAS)-St. Louis. These improvements allow for quicker isolation of problems and expedite the corrective process. DFAS-St. Louis worked with the Logistics Modernization Program (LMP) to receive better information enabling them to match Mechanization of Contract Administration Services (MOCAS) disbursements to LMP obligations in more timely manner.

Negative Unliquidated Obligations (NULO) decreased \$1.1 million or 28 percent from FY 2005 to FY 2006. This decrease is attributed to changes made in 1st Quarter, FY 2006 by DFAS-St. Louis that streamlined the error correction process. DFAS-St. Louis worked with the LMP to receive better information enabling them to match MOCAS disbursements to LMP obligations in more timely manner.

In-transit Disbursements increased \$86.0 million, or 91 percent, from FY 2005 to FY 2006. This increase is attributed to disbursement files reported by DFAS-Columbus on behalf of DFAS-St. Louis and DFAS-Rock Island received after the year-end processing deadline. Although these payments were disbursed in FY 2006, they were not recorded in the accounting systems until early FY 2007. These disbursements are considered in-transit until recorded in the accounting systems.

#### Other Disclosures

There are no problem disbursements related to Foreign Military Sales in AWCF.

There are no discrepancies between the amounts reported in the problem disbursement metric furnished to DFAS-Arlington and the Note 3 schedule.

## Note 4. Investments and Related Interest

Not applicable.

## Note 5. Accounts Receivable

As of September 30	2006			2005	
	Gross Amount Due	Allowance For Estimated Uncollectibles	Accounts Receivable, Net	Accounts Receivable, Net	
<i>(Amounts in thousands)</i>					
1. Intragovernmental Receivables	\$ 243,005	\$ N/A	\$ 243,005	\$ 366,622	
2. Nonfederal Receivables (From the Public)	\$ 16,896	\$ (7,541)	\$ 9,355	\$ 12,035	
3. Total Accounts Receivable	\$ 259,901	\$ (7,541)	\$ 252,360	\$ 378,657	

### Fluctuations and/or Abnormalities

Intragovernmental Receivables decreased \$123.6 million, or 34 percent, from FY 2005 to FY 2006. The majority of the decrease, \$116.5 million, is attributable to a change in billing criteria in the Supply Management (SMA) business area. During the 3rd Quarter, FY 2006, the Army Working Capital Fund (AWCF) accelerated the billing cycle. Previously, AWCF did not bill the customer until seven days after preparation of the material release order. The customer is now billed after two days.

Nonfederal Receivables, Net decreased \$2.7 million or 22 percent, from FY 2005 to FY 2006. The decrease is attributable to a decrease in outstanding Foreign Military Sales (FMS) receivables in the SMA business area. Previously, AWCF did not bill the FMS customer until seven or more days after confirmation of shipment. The FMS customer is now billed two days after shipment.

### Aged Accounts Receivable

As of September 30	2006		2005	
	Intragovernmental	Nonfederal	Intragovernmental	Nonfederal
<i>(Amounts in thousands)</i>				
CATEGORY				
<b>Nondelinquent</b>				
Current	\$ 254,993	\$ 11,930	\$ 407,782	\$ 13,298
Noncurrent	0	0	0	0
<b>Delinquent</b>				
1 to 30 days	\$ 1,822	\$ 196	\$ 8,014	\$ 230
31 to 60 days	374	1	203	178
61 to 90 days	119	19	48	0
91 to 180 days	65	27	99	59
181 days to 1 year	117	303	723	3,559
Greater than 1 year and less than or equal to 2 years	79	3,822	4,556	5
Greater than 2 years and less than or equal to 6 years	83	3	55	1
Greater than 6 years and less than or equal to 10 years	0	7	0	9
Greater than 10 years	0	588	0	1,395
<b>Subtotal</b>	\$ 257,652	\$ 16,896	\$ 421,480	\$ 18,734
Less Supported Undistributed Collections	21,939	0	0	0
Less Eliminations	(36,586)	0	(53,967)	0
Less Other	0	0	(891)	0
<b>Total</b>	\$ 243,005	\$ 16,896	\$ 366,622	\$ 18,734

The table above identifies aged accounts receivable groups for AWCF as reported in AWCF Monthly Report on Receivables (MRR).

The balance of \$21.9 million reported as supported undistributed collections is abnormal due to differences between the Department of the Treasury and AWCF field reported collections. The majority of these collections were previously reported by the former Army Information Services business area, which closed at the end of FY 2003. The AWCF did not properly close out and transfer existing collection balances to the SMA business area. The AWCF is still working to resolve the abnormal balance.

During FY 2005, AWCF did not separately identify \$20.1 million of supported undistributed collections on the MRR and incorrectly included these amounts in the current Intragovernmental Accounts Receivable totals. Also, during FY 2005, AWCF incorrectly included \$891.3 thousand of unsupported undistributed collections in the current Intragovernmental Accounts Receivable total. These unsupported undistributed collection amounts were not included in AWCF Intragovernmental Accounts Receivable financial statement balances. The improper MRR reporting issues were corrected beginning with the 3rd Quarter, FY 2006.

#### Relevant Information

The AWCF does not have any Nondelinquent Accounts Receivable over 30 days old.

The majority of accounts receivable from Federal sources are in a current status. The AWCF follows the DoD concept of operations for collections. This requires follow-up actions at 30-day intervals with ordering activities.

The majority of accounts receivable due from the public are in a current status. Delinquent accounts receivable from the public includes \$3.7 million in disputed billings pending resolution. Further, \$336.7 thousand has been referred to the Department of the Treasury for collection and \$674.7 thousand has been referred to the Department of Justice for legal action. The remaining debt of \$236.5 thousand is being actively pursued by AWCF in accordance with the Debt Collection Improvement Act of 1996.

## Note 6. Other Assets

As of September 30	2006	2005
<i>(Amounts in thousands)</i>		
1. Intragovernmental Other Assets		
A. Advances and Prepayments	\$ 8,670	\$ 0
B. Other Assets	0	0
C. Total Intragovernmental Other Assets	\$ 8,670	\$ 0
2. Nonfederal Other Assets		
A. Outstanding Contract Financing Payments	\$ 417,830	\$ 331,500
B. Other Assets (With the Public)	84	2,241
C. Total Nonfederal Other Assets	\$ 417,914	\$ 333,741
3. Total Other Assets	\$ 426,584	\$ 333,741

#### Fluctuations and/or Abnormalities

Intragovernmental Other Assets increased \$8.7 million, or 12,384,263 percent from FY 2005 to FY 2006. The entire balance in Intragovernmental Other Assets Advances and Prepayments is based upon unearned revenue reported by the Defense Reutilization and Marketing Office (DRMO). The DRMO bills Army Working Capital Fund (AWCF) at the beginning of each quarter for hazardous waste removal work that DRMO expects to perform in that quarter for the Supply Management (SMA) business area. The \$8.7 million advance represents the amount DRMO billed over the amount of actual revenue earned. This account balance is dictated by trading partner seller-side rules.

Nonfederal Other Assets increased \$84.2 million or 25 percent, from FY 2005 to FY 2006. During the 4th Quarter, FY 2006, AWCF recognized a contingent liability for the estimated future funded payments that will be paid upon delivery and acceptance of a satisfactory product. The majority of this increase is attributable to contingent liabilities for estimated future funded payments. A contingent liability in the amount of \$855.3 thousand is attributable to the Industrial Operations business area, while a contingent liability in the amount of \$87.7 million is attributable to the SMA business area.

Other Assets (With the Public) consists of travel advances and prepaid expenses.

**Other Disclosures**

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

The Nonfederal Other Assets Outstanding Contract Financing Payments balance of \$417.8 million is comprised of \$329.3 million in Contract Financing Payments and an additional \$88.5 million in estimated future funded payments that will be paid to the contractor upon future delivery and Government acceptance of a satisfactory product (see additional discussion in Note 15, Other Liabilities).

**Note 7. Cash and Other Monetary Assets**

Not applicable.

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

Not applicable.

**Note 9. Inventory and Related Property**

As of September 30	2006		2005	
<i>(Amounts in thousands)</i>				
1. Inventory, Net	\$	17,939,567	\$	15,933,141
2. Operating Materials & Supplies, Net		0		0
3. Stockpile Materials, Net		0		0
4. Total	\$	17,939,567	\$	15,933,141

**Inventory, Net**

As of September 30	2006			2005	Valuation Method
	Inventory, Gross Value	Revaluation Allowance	Inventory, Net	Inventory, Net	
<i>(Amounts in thousands)</i>					
1. Inventory Categories					
A. Available and Purchased for Resale	\$ 19,948,643	\$ (5,190,993)	14,757,650	\$ 13,389,441	LAC,MAC
B. Held for Repair	4,877,241	(1,738,468)	3,138,773	2,517,932	LAC,MAC
C. Excess, Obsolete, and Unserviceable	557,240	(557,240)	0	0	NRV
D. Raw Materials	43,144	0	43,144	25,768	MAC,SP,L
E. Work in Process	0	0	0	0	AC
F. Total	\$ 25,426,268	\$ (7,486,701)	17,939,567	\$ 15,933,141	

**Legend for Valuation Methods:**

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

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

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

- 1) Distributions without reimbursement are made when authorized by DoD directives;
- 2) War reserve material includes petroleum products and subsistence items that are considered restricted; and
- 3) Inventory, with the exception of safety stocks, may be sold to foreign, state, and local governments; private parties; and contractors in accordance with current policies and guidance or at the direction of the President.

There are no restrictions on disposition of inventory as related to environmental or other liabilities.

**3. Other Information:****Definitions**

The Inventory, Net is composed of the categories listed below. Inventory items are assigned to a category based upon the type and condition of the asset.

Inventory Available and Purchased for Resale – spare and repair parts, clothing and textiles, petroleum products, and ammunition.

Inventory Held for Repair – damaged material held as inventory that is more economical to repair than to dispose of.

Excess, Obsolete, and Unserviceable Inventory – condemned materiel that must be retained for management purposes.

Raw Materials – items consumed in the production of goods for sale or in the provision of services for a fee.

**Fluctuations and/or Abnormalities**

Total Inventory increased \$2.0 billion, or 13 percent, from FY 2005 to FY 2006. This increase is detailed in the paragraph below.

The Inventory Available and Purchased for Resale increased \$1.4 billion, or 10 percent, from FY 2005 to FY 2006. Approximately \$977.3 million of the increase is attributable to several performance based logistics contracts established by the Aviation and Missile Command in FY 2004 and FY 2005 to accelerate the replenishment of inventory. The contracts with General Electric Company and Honeywell to supply various engines and Sikorsky Aircraft Corporation and Boeing supply airframes and component parts. These contracts will last for another three to five years. Also, the Tank-automotive and Armaments Command has increased inventory levels by \$591.4 million in support of Operation Iraqi Freedom and Operation Enduring Freedom.

**Operating Materials and Supplies, Net**

Not applicable

**Stockpile Materials, Net**

Not applicable

## Note 10. General PP&E, Net

As of September 30	2006					2005
	Depreciation/ Amortization Method	Service Life	Acquisition Value	(Accumulated Depreciation/ Amortization)	Net Book Value	Prior FY Net Book Value
<i>(Amounts in thousands)</i>						
1. Major Asset Classes						
A. Land	N/A	N/A	\$ 0	\$ N/A	\$ 0	\$ 0
B. Buildings, Structures, and Facilities	S/L	20 Or	2,231,876	(1,438,786)	793,090	797,228
C. Leasehold Improvements	S/L	40 lease term	95,213	(79,006)	16,207	18,877
D. Software	S/L	2-5 Or	433,573	(262,275)	171,298	87,092
E. General Equipment	S/L	10	1,497,770	(1,247,840)	249,930	275,791
F. Military Equipment	S/L	5 or 10	0	0	0	0
G. Assets Under Capital Lease	S/L	Various lease term	0	0	0	0
H. Construction-in- Progress	S/L	N/A	36,545	N/A	36,545	49,225
I. Other	N/A	N/A	0	0	0	0
J. Total General PP&E			<u>\$ 4,294,977</u>	<u>\$ (3,027,907)</u>	<u>\$ 1,267,070</u>	<u>\$ 1,228,213</u>

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

Legend for Valuation Methods:

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

### Other Disclosures

There are no known restrictions on the use or convertibility of the Army Working Capital Fund (AWCF) general property, plant, and equipment.

The entire amount shown on the Leasehold Improvements line is for improvements made to facilities at Corpus Christi Army Depot (CCAD). The CCAD, a tenant on a Navy installation, does not maintain a lease with the Navy. The AWCF records improvements made on these facilities as leasehold improvements.

Heritage Assets and Stewardship Land owned or maintained on AWCF installations are reported in the Required Supplemental Stewardship Information Report of the Army General Fund.

### Assets Under Capital Lease

The AWCF does not have any Assets Under Capital Lease.



**Note 11. Liabilities Not Covered by Budgetary Resources**

As of September 30	2006	2005
<i>(Amounts in thousands)</i>		
1. Intragovernmental Liabilities		
A. Accounts Payable	\$ 0	\$ 0
B. Debt	0	0
C. Other	48,768	47,253
D. Total Intragovernmental Liabilities	\$ 48,768	\$ 47,253
2. Nonfederal Liabilities		
A. Accounts Payable	\$ 0	\$ 0
B. Military Retirement Benefits and Other Employment-Related Actuarial Liabilities	262,499	286,523
C. Environmental Liabilities	0	0
D. Other Liabilities	0	0
E. Total Nonfederal Liabilities	\$ 262,499	\$ 286,523
3. Total Liabilities Not Covered by Budgetary Resources	\$ 311,267	\$ 333,776
4. Total Liabilities Covered by Budgetary Resources	\$ 1,132,953	\$ 1,072,271
5. Total Liabilities	\$ 1,444,220	\$ 1,406,047

**Definitions**

Intragovernmental Other Liabilities represents future funded Federal Employees Compensation Act (FECA) liabilities billed to the Army Working Capital Fund (AWCF) by the Department of Labor (DOL). This amount represents amounts paid by the DOL to beneficiaries for which DOL has billed AWCF.

Military Retirement Benefits and Other Employment-Related Actuarial Liabilities represents the FECA actuarial liability as estimated for AWCF by DOL. This amount represents amounts that DOL estimates will be paid to beneficiaries in the future on behalf of AWCF.

**Note 12. Accounts Payable**

As of September 30	2006			2005
	Accounts Payable	Interest, Penalties, and Administrative Fees	Total	Total
<i>(Amounts in thousands)</i>				
1. Intragovernmental Payables	\$ 78,917	\$ N/A	\$ 78,917	\$ 105,603
2. Nonfederal Payables (to the Public)	576,037	0	576,037	295,820
3. Total	\$ 654,954	\$ 0	\$ 654,954	\$ 401,423

**Fluctuations and/or Abnormalities**

Intragovernmental Payables decreased \$26.7 million, or 25 percent, from FY 2005 to FY 2006. The decrease is primarily attributable to decreased payables with the Defense Logistics Agency (DLA). The Army Working Capital Fund (AWCF) is required to follow Department of Defense (DoD) seller side rules based on trading partner reported balances. During FY 2006, the DLA reported less accounts receivable business with AWCF. Therefore, AWCF was required to match DLA reported accounts receivable with AWCF accounts payable.

Nonfederal Payables increased \$280.2 million, or 95 percent, from FY 2005 to FY 2006. The increase is primarily attributable to corrections of abnormal accounts payable balances that were reported by the Logistics Modernization Program (LMP) for the Supply Management business area in FY 2005. During FY 2006, the LMP Program Management Office worked with Army Working Capital Fund (AWCF) to initiate systemic corrections, which reduced the previously reported abnormal balances. The FY 2006 corrections reduced the abnormal balance by \$211.0 million to the current abnormal balance of \$88.7 million. This is an unresolved issue that AWCF is continuing to research.

## Note 13. Debt

Not applicable.

## Note 14. Environmental Liabilities and Disposal Liabilities

Not applicable.

## Note 15. Other Liabilities

As of September 30	2006			2005
	Current Liability	Noncurrent Liability	Total	Total
<i>(Amounts in thousands)</i>				
1. Intragovernmental				
A. Advances from Others	\$ 0	\$ 0	\$ 0	\$ 19,661
B. Deposit Funds and Suspense Account Liabilities	0	0	0	0
C. Disbursing Officer Cash	0	0	0	0
D. Judgment Fund Liabilities	0	0	0	0
E. FECA Reimbursement to the Department of Labor	21,675	27,093	48,768	47,253
F. Other Liabilities	9,382	0	9,382	8,665
G. Total Intragovernmental Other Liabilities	\$ 31,057	\$ 27,093	\$ 58,150	\$ 75,579
2. Nonfederal				
A. Accrued Funded Payroll and Benefits	\$ 70,441	\$ 0	\$ 70,441	\$ 91,586
B. Advances from Others	83,267	0	83,267	42,429
C. Deferred Credits	0	0	0	0
D. Deposit Funds and Suspense Accounts	(898)	0	(898)	(891)
E. Temporary Early Retirement Authority	0	0	0	0
F. Nonenvironmental Disposal Liabilities				
(1) National Defense PP&E (Nonnuclear)	0	0	0	0
(2) Excess/Obsolete Structures	0	0	0	0
(3) Conventional Munitions Disposal	0	0	0	0
(4) Other	0	0	0	0
G. Accrued Unfunded Annual Leave	100,812	0	100,812	95,756
H. Capital Lease Liability	0	0	0	0
I. Other Liabilities	126,461	88,534	214,995	413,642
J. Total Nonfederal Other Liabilities	\$ 380,083	\$ 88,534	\$ 468,617	\$ 642,522
3. Total Other Liabilities	\$ 411,140	\$ 115,627	\$ 526,767	\$ 718,101

### Fluctuations and/or Abnormalities

Total Other Liabilities decreased 191.3 million, or 27 percent, due to the following:

Total Intragovernmental Other Liabilities decreased \$17.4 million, or 23 percent, primarily due to a \$19.7 million, or 100 percent, decrease in Intragovernmental Advances from Others from FY 2005 to FY 2006. The reduction resulted from a change in reporting procedure. In FY 2005, the \$19.7 million reported as advances was based upon over-billings resulting in unearned revenue reported by the Army Working Capital Fund (AWCF). The unearned revenue was erroneously attributed to advances from Army General Fund. Further research revealed that the unearned revenue was actually collections received in excess of earnings. Beginning in 1st Quarter, FY 2006, and throughout FY 2006, the unearned revenue and associated advance were eliminated from AWCF financial statements.

Total Nonfederal Other Liabilities decreased \$173.9 million, or 27 percent, primarily due to a decrease in Nonfederal Other Liabilities of \$198.6 million, or 48 percent, from FY 2005 to FY 2006. During FY 2005, AWCF reported other liabilities when accepting ownership of materiel at the point of origin. This amount also erroneously included a liability for materiel that should not have been recorded until the materiel was received at the destination. In September 2006, in accordance with audit recommendations, AWCF fixed this procedure and

now correctly records the liability in accordance with the terms of the contract. The correction resulted in a Nonfederal Other Liability decrease of \$274.3 million between FY 2005 and FY 2006. However, the reduction was offset by an \$88.5 million contingent liability that was established during the 4th Quarter, FY 2006, for estimated future contract financing payments that will be paid to the contractor upon delivery, and Government acceptance of, a satisfactory product.

The \$898.0 thousand abnormal balance in Nonfederal Deposit Funds and Suspense Accounts is due to differences between the Department of the Treasury and AWCF field reported collections. The majority of this amount results from a balance brought forward that existed in FY 2005. The AWCF is working to resolve these differences.

#### Other Disclosures

The Intragovernmental Other Liabilities line includes employer contributions for employee benefits and payroll taxes payable.

The Nonfederal Other Liabilities line consists of inventory in-transit posted by the Logistics Modernization Program (LMP), contingent liabilities, contract holdbacks, and employer's contribution for employee benefits.

Contingent liabilities balance includes \$88.5 million in estimated future contract financing payments that will be paid to the contractor upon delivery, and Government acceptance of, a satisfactory product. In accordance with contract terms, specific rights to the contractor's work vests with the Government when a specific type of contract financing payments is made, thereby protecting taxpayer funds in the event of contract nonperformance. These rights should not be misconstrued as the rights of ownership. The Department is under no obligation to pay the contractor for amounts greater than the amounts authorized in the contract until delivery and Government acceptance of a satisfactory product. Because it is probable that the contractor will complete its efforts and deliver a satisfactory product to the Department and the amount of potential future payments are estimable; the Department has recognized a contingent liability for estimated future payments, which are conditional pending delivery and Government acceptance of a satisfactory product.

#### Capital Lease Liability

Not applicable.

## Note 16. Commitments and Contingencies

#### Relevant Information

The Army Working Capital Fund (AWCF) is a party in various administrative proceedings and legal actions, with claims including environmental damage claims, equal opportunity matters, and contractual bid protests. The AWCF has accrued contingent liabilities for legal actions where the Army's Office of the General Counsel considers an adverse decision probable and the amount of loss is measurable. In the event of an adverse judgment against the Government, some of the liabilities may be payable from the Judgment Fund. The AWCF records Judgment Fund liabilities in Note 15 Other Liabilities, and Note 12 Accounts Payable. See Notes 15 and 12 for details.

#### Nature of Contingency

The FY 2006 Army Legal Representation Letter outlines one claim against AWCF totaling \$486.7 million for which the Army Office of General Counsel is unable to express an opinion.

The AWCF has other contingent liabilities in which the possibility of loss is considered reasonable. These liabilities are not accrued in the Army's financial statements nor are reported in the FY 2006 Army Legal Representation Letter. As of September 30, 2006, AWCF has approximately \$140 thousand in claims considered reasonably possible. These contingent liabilities and estimates are presented in the following table. Estimates for litigations, claims and assessments are required to be fully supported. Additionally, AWCF has coordinated with Army Office of General Counsel to ensure that estimates agree with the legal representation letters and management summary schedule.

#### Estimate of the Possible Liability

*(Amounts in thousands)*

<b>Title of Contingent Liabilities</b>	<b>Estimate</b>
Army Materiel Command	\$140

#### Other Disclosures

The AWCF does not have open contracts citing cancelled appropriations.

## Note 17. Military Retirement and Other Federal Employment Benefits

As of September 30	2006				2005
	Present Value of Benefits	Assumed Interest Rate (%)	(Less: Assets Available to Pay Benefits)	Unfunded Liability	Present Value of Benefits
<i>(Amounts in thousands)</i>					
1. Pension and Health Actuarial Benefits					
A. Military Retirement Pensions	\$ 0		\$ 0	\$ 0	\$ 0
B. Military Retirement Health Benefits	0		0	0	0
C. Military Medicare-Eligible Retiree Benefits	0		0	0	0
D. Total Pension and Health Actuarial Benefits	\$ 0		\$ 0	\$ 0	\$ 0
2. Other Actuarial Benefits					
A. FECA	\$ 262,499	5.31	\$ 0	\$ 262,499	\$ 286,523
B. Voluntary Separation Incentive Programs	0		0	0	0
C. DoD Education Benefits Fund	0		0	0	0
D. Total Other Actuarial Benefits	\$ 262,499		\$ 0	\$ 262,499	\$ 286,523
3. Other Federal Employment Benefits	\$ 0		\$ 0	\$ 0	\$ 0
4. Total Military Retirement and Other Federal Employment Benefits:	\$ 262,499		\$ 0	\$ 262,499	\$ 286,523

Actuarial Cost Method Used: See below

Assumptions: See below

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

### Actuarial Cost Method Used

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

### Assumptions

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

### Other Disclosures

The AWCF does not invest in Market-based and Marketable Securities.

The Army Working Capital Fund (AWCF) actuarial liabilities decreased \$24.0 million since the previous calculation at the end of FY 2005.

Actuarial liabilities are computed for employee compensation benefits as mandated by the Federal Employment Compensation Act (FECA). The Office of Personnel Management provides updated Army actuarial liabilities during the 4th Quarter of each fiscal year. The AWCF computes its portion of the total Army actuarial liability based on the percentage of AWCF FECA expense to the total Army FECA expense.

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

As of September 30	2006	2005
<i>(Amounts in thousands)</i>		
1. Intragovernmental Costs	\$ 450,715	\$ 2,016,164
2. Public Costs	15,455,261	10,600,436
3. Total Costs	<u>\$ 15,905,976</u>	<u>\$ 12,616,600</u>
4. Intragovernmental Earned Revenue	\$ (11,459,046)	\$ (7,556,355)
5. Public Earned Revenue	(6,237,998)	(6,918,272)
6. Total Earned Revenue	<u>\$ (17,697,044)</u>	<u>\$ (14,474,627)</u>
7. Net Cost of Operations	<u>\$ (1,791,068)</u>	<u>\$ (1,858,027)</u>

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

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

The Statement of Net Cost is unique because its principles are driven by understanding the net cost of programs and/or organizations that the Federal Government supports through appropriations or other means. This statement provides gross and net cost information that can be related to the amount of output or outcome for a given program and/or organization administered by a responsible reporting entity.

While the Army Working Capital Fund (AWCF) activities generally record transactions on an accrual basis, as is required by federal generally accepted accounting principles, the systems do not always capture actual costs. Information presented on the Consolidated Statement of Net Cost is primarily based on budgetary obligation, disbursement, or collection transactions, as well as information from non-financial feeder systems. The AWCF is in the process of upgrading its financial and logistical feeder systems to the Logistics Modernization Program (LMP) to address this issue.

The AWCF does not own heritage assets or stewardship land.

The Statement of Net Cost includes expenses and other gains and losses. It does not include expenses related to capitalized purchases. Per seller side rules, intragovernmental costs, including intra-AWCF costs, are matched to the revenue reported by federal trading partners. Public costs are derived by subtracting the federal trading partner amounts from the total expenses and other gains and losses contained in AWCF accounting systems.

In 4th Quarter, FY 2005, AWCF begin identifying purchases reported as revenue by federal trading partners and separating those purchases from other expenses. These capitalized purchases are reflected within the Statement of Financing.

**Fluctuations and/or Abnormalities**

Gross Costs increased \$3.3 billion or 26 percent between FY 2005 and FY 2006. The 4th quarter, FY 2005, Gross Costs should have been \$16.1 billion, instead of the \$12.6 billion reported at year-end due to an over elimination of intra-AWCF costs. In 4th quarter, FY 2005, AWCF eliminated an additional \$3.5 billion as intra-AWCF costs on the financial statements because intragovernmental trading partners could not be identified. During FY 2005, sufficient detail needed to identify AWCF trading partners was not available. When AWCF could not identify trading partners, the costs were reported as intra-AWCF and eliminated from the statement. Beginning in the 1st Quarter, FY 2006, AWCF improved trading partner identification processes to provide for more accurate reporting of Intragovernmental Costs.

Earned Revenue increased \$3.2 billion or 22 percent between FY 2005 and FY 2006. The 4th Quarter, FY 2005, Earned Revenue should have been \$18.0 billion, instead of the \$14.5 billion reported at year-end due to an over elimination of intra-AWCF Earned Revenue. In 4th Quarter, FY 2005, AWCF eliminated an additional \$3.5 billion in intra-AWCF Earned Revenue on the financial statements because intragovernmental trading partners could not be identified. During FY 2005, sufficient detail needed to identify AWCF trading partners was not available. When AWCF could not identify trading partners, the Earned Revenue was reported as intra-AWCF and eliminated from the statement. Beginning in the 1st Quarter, FY 2006, AWCF improved trading partner identification processes to provide for more accurate reporting of Intragovernmental Earned Revenue.

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

As of September 30	2006		2005	
	Cumulative Results of Operations	Unexpended Appropriations	Cumulative Results of Operations	Unexpended Appropriations
<i>(Amounts in thousands)</i>				
1. Prior Period Adjustments Increases (Decreases) to Net Position Beginning Balance				
A. Changes in Accounting Standards	\$ 0	\$ 0	\$ 0	\$ 0
B. Errors and Omissions in Prior Year Accounting Reports	0	0	0	0
C. Total Prior Period Adjustments	\$ 0	\$ 0	\$ 0	\$ 0
2. Imputed Financing				
A. Civilian CSRS/FERS Retirement	\$ 53,486	\$ 0	\$ 55,172	\$ 0
B. Civilian Health	103,362	0	91,750	0
C. Civilian Life Insurance	226	0	213	0
D. Judgment Fund	0	0	0	0
E. IntraEntity	0	0	0	0
F. Total Imputed Financing	\$ 157,074	\$ 0	\$ 147,135	\$ 0

### Legend:

CSRS – Civil Service Retirement System

FERS – Federal Employees Retirement System

Other Financing Sources – Other consists of the net of transfers-in and transfers-out for which trading partners cannot be identified.

## Note 20. Disclosures Related to the Statement of Budgetary Resources

As of September 30	2006	2005
<i>(Amounts in thousands)</i>		
1. Net Amount of Budgetary Resources Obligated for Undelivered Orders at the End of the Period	\$ 9,001,781	\$ 10,115,417
2. Available Borrowing and Contract Authority at the End of the Period	6,374,039	6,702,921

The Army Working Capital Fund (AWCF) had \$14.9 billion reimbursable obligations for apportionment category B. Category B apportionments provide funding for the entire fiscal year without quarterly limitations.

The AWCF does not make eliminating entries in the Statement of Budgetary Resources because the statements are presented as combined and combining and, therefore, are presented as a Disaggregated Statement of Budgetary Resources in the Required Supplementary Information section of the financial statements.

### Contract Authority

Operating contract authority for the Supply Management (SMA) business area increased \$1.0 billion to accommodate increased obligations to support higher sales.

The contract authority for the capital investment program increased overall by \$2.3 million. SMA decreased \$5.2 million due to reduced software purchases while the Industrial Operations (IO) business area increased \$7.5 million primarily to provide for additional equipment purchases.

**Reimbursable Authority**

Reimbursable authority in the IO business area increased \$2.2 billion due to higher than anticipated orders.

**Appropriations**

In 1st Quarter, FY 2006, AWCF received a warrant for \$106.5 million in accordance with DoD Appropriation Act, 2006, P.L. 109-148, 119 STAT 2680. In 1st Quarter, FY 2006, AWCF distributed \$42.5 million for war reserves and Army combat uniforms to the SMA business area and \$64.0 million to the IO business area for industrial mobilization capacity.

In 3rd Quarter, FY 2006, AWCF received a warrant for \$348.3 million in accordance with Emergency Supplemental Appropriations Act for Defense, the Global War on Terror, and Hurricane Recovery, 2006, P.L. 109-234, 120 STAT 418. In 3rd Quarter, FY 2006, the SMA business area received \$92.1 million for war reserves and \$255.0 million for inventory augmentation. The IO business area received \$1.2 million for fuel cost increases.

In 4th Quarter, FY 2006, AWCF received a warrant for \$4.7 million in accordance with title IX, Division A of the Department of Defense Appropriations Act, 2006, P.L. 109-148, 119 STAT 2680. The IO business area received this \$4.7 million for fuel cost increases.

**Other Disclosures**

There are no legal arrangements affecting the use of unobligated balances of budgetary authority.

The AWCF did not receive any capital infusions beyond the appropriations discussed above.

**Note 21. Disclosures Related to the Statement of Financing**

The objective of the Statement of Financing is to allow users to understand the difference between the Statement of Budgetary Resources and the Statement of Net Cost. The statement provides this understanding through a comprehensive reconciliation process.

The Army Working Capital Fund (AWCF) budgetary data does not agree with its proprietary expenses and assets capitalized. This results in a difference in net cost between the Statement of Net Cost and the Statement of Financing. Resources That Finance the Acquisition of Assets were adjusted by \$1.6 billion to bring the statements into agreement. The differences between budgetary and proprietary data for AWCF were reported as material weaknesses in the FY 2005 AWCF annual financial statement report.

The following Statement of Financing lines are presented as combined instead of consolidated due to interagency budgetary transactions not being eliminated:

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

Other Resources Other consists of other gains and other losses primarily attributable to differences between intragovernmental transfers-in/out for which trading partners could not be identified.

Other Resources or Adjustments to Net Obligated Resources that do not affect Net Cost of Operations Other consists mostly of other gains and other losses primarily attributable to differences between intragovernmental transfers-in/out for which trading partners could not be identified.

Components Requiring or Generating Resources in Future Period Other consists of the increase in the FECA liability.

Components not Requiring or Generating Resources Other Other consists of cost capitalization offsets.

The AWCF does not have any allocation transfers.

Components Requiring or Generating Resources in Future Period reports a \$1.5 million increase in unfunded expenses that were incurred during FY 2006. The \$1.5 million is the increase between FY 2005 and FY 2006 on Note 11, Liabilities not Covered by Budgetary Resources, for Unfunded Federal Employees Compensation Act (FECA) liability as reported on the line Intragovernmental Liabilities Other.

## **Note 22. Disclosures Related to the Statement of Custodial Activity**

Not Applicable.

## **Note 23. Earmarked Funds**

Not applicable.

## **Note 24. Other Disclosures**

Not applicable.





**STATEMENT OF DISAGGREGATED BUDGETARY RESOURCES**

As of September 30, 2006 and 2005 (\$ in Thousands)

	Working Capital Funds	2006 Combined	2005 Combined
<b>BUDGETARY FINANCING ACCOUNTS</b>			
<b>BUDGETARY RESOURCES</b>			
Unobligated balance, brought forward, October 1	\$ 1,176,499	\$ 1,176,499	\$ 1,530,241
Recoveries of prior year unpaid obligations	1,372,092	1,372,092	1,435,592
Budget authority			
Appropriation	459,521	459,521	0
Borrowing authority	0	0	0
Contract authority	9,970,836	9,970,837	10,951,904
Spending authority from offsetting collections			
Earned			
Collected	14,013,376	14,013,375	14,180,281
Change in receivables from Federal sources	(142,805)	(142,805)	(29,369)
Change in unfilled customer orders			
Advance received	39,952	39,953	19,271
Without advance from Federal sources	59,028	59,027	(774,190)
Anticipated for rest of year, without advances	0	0	0
Previously unavailable	0	0	0
Expenditure transfers from trust funds	0	0	0
Subtotal	24,399,908	24,399,908	24,347,897
Nonexpenditure transfers, net, anticipated and actual	0	0	(515,944)
Temporarily not available pursuant to Public Law	0	0	0
Permanently not available	(10,299,718)	(10,299,718)	(8,798,841)
<b>Total Budgetary Resources</b>	<b>\$ 16,648,781</b>	<b>\$ 16,648,781</b>	<b>\$ 17,998,945</b>
<b>Status of Budgetary Resources:</b>			
Obligations incurred:			
Direct	\$ 0	\$ 0	\$ 0
Reimbursable	14,857,316	14,857,316	16,822,445
Subtotal	14,857,316	14,857,316	16,822,445
Unobligated balance:			
Apportioned	1,791,465	1,791,465	1,176,499
Exempt from apportionment	0	0	0
Subtotal	1,791,465	1,791,465	1,176,499
Unobligated balance not available	0	0	1
<b>Total status of budgetary resources</b>	<b>\$ 16,648,781</b>	<b>\$ 16,648,781</b>	<b>\$ 17,998,945</b>
<b>Change in Obligated Balance:</b>			
Obligated balance, net			
Unpaid obligations, brought forward, October 1	\$ 10,331,508	\$ 10,331,509	\$ 8,953,395
Less: Uncollected customer payments from Federal sources, brought forward, October 1	(4,181,757)	(4,181,756)	(4,985,314)
Total unpaid obligated balance	6,149,751	6,149,753	3,968,081
Obligations incurred net (+/-)	\$ 14,857,316	\$ 14,857,316	\$ 16,822,445
Less: Gross outlays	(14,260,836)	(14,260,837)	(14,008,740)
Obligated balance transferred, net			
Actual transfers, unpaid obligations (+/-)	0	0	0
Actual transfers, uncollected customer payments from Federal sources (+/-)	0	0	0
Total Unpaid obligated balance transferred, net	0	0	0
Less: Recoveries of prior year unpaid obligations, actual	(1,372,092)	(1,372,092)	(1,435,592)
Change in uncollected customer payments from Federal sources (+/-)	83,777	83,777	803,558
Obligated balance, net, end of period			
Unpaid obligations	9,555,896	9,555,896	10,331,509
Less: Uncollected customer payments (+/-) from Federal sources (-)	(4,097,979)	(4,097,980)	(4,181,756)
Total, unpaid obligated balance, net, end of period	5,457,917	5,457,916	6,149,753
<b>Net Outlays</b>			
<b>Net Outlays:</b>			
Gross outlays	14,260,836	14,260,837	14,008,740
Less: Offsetting collections	(14,053,328)	(14,053,327)	(14,199,551)
Less: Distributed Offsetting receipts	0	0	0
<b>Net Outlays</b>	<b>\$ 207,508</b>	<b>\$ 207,510</b>	<b>\$ (190,811)</b>

Department of Defense - Army Working Capital Fund

**STATEMENT OF DISAGGREGATED BUDGETARY RESOURCES**

As of September 30, 2006 and 2005 (\$ in Thousands)

	Working Capital Funds	2006 Combined	2005 Combined
<b>NONBUDGETARY FINANCING ACCOUNTS</b>			
<b>BUDGETARY RESOURCES</b>			
Unobligated balance, brought forward, October 1	\$ 0	\$ 0	\$ 0
Recoveries of prior year unpaid obligations	0	0	0
Budget authority			
Appropriation	0	0	0
Borrowing authority	0	0	0
Contract authority	0	0	0
Spending authority from offsetting collections			
Earned			
Collected	0	0	0
Change in receivables from Federal sources	0	0	0
Change in unfilled customer orders			
Advance received	0	0	0
Without advance from Federal sources	0	0	0
Anticipated for rest of year, without advances	0	0	0
Previously unavailable	0	0	0
Expenditure transfers from trust funds	0	0	0
Subtotal	0	0	0
Nonexpenditure transfers, net, anticipated and actual	0	0	0
Temporarily not available pursuant to Public Law	0	0	0
Permanently not available	0	0	0
<b>Total Budgetary Resources</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 0</b>
<b>Status of Budgetary Resources:</b>			
Obligations incurred:			
Direct	\$ 0	\$ 0	\$ 0
Reimbursable	0	0	0
Subtotal	0	0	0
Unobligated balance:			
Apportioned	0	0	0
Exempt from apportionment	0	0	0
Subtotal	0	0	0
Unobligated balance not available	0	0	0
<b>Total status of budgetary resources</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 0</b>
<b>Change in Obligated Balance:</b>			
Obligated balance, net			
Unpaid obligations, brought forward, October 1	\$ 0	\$ 0	\$ 0
Less: Uncollected customer payments from Federal sources, brought forward, October 1	0	0	0
Total unpaid obligated balance	0	0	0
Obligations incurred net (+/-)	\$ 0	\$ 0	\$ 0
Less: Gross outlays	0	0	0
Obligated balance transferred, net			
Actual transfers, unpaid obligations (+/-)	0	0	0
Actual transfers, uncollected customer payments from Federal sources (+/-)	0	0	0
Total Unpaid obligated balance transferred, net	0	0	0
Less: Recoveries of prior year unpaid obligations, actual	0	0	0
Change in uncollected customer payments from Federal sources (+/-)	0	0	0
Obligated balance, net, end of period			
Unpaid obligations	0	0	0
Less: Uncollected customer payments (+/-) from Federal sources (-)	0	0	0
Total, unpaid obligated balance, net, end of period	0	0	0
<b>Net Outlays</b>			
<b>Net Outlays:</b>			
Gross outlays	0	0	0
Less: Offsetting collections	0	0	0
Less: Distributed Offsetting receipts	0	0	0
<b>Net Outlays</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 0</b>

**Required Supplemental Information - Part A**

**AT97 - Army Working Capital Fund**

(\$ in Thousands)

<b>Schedule, Part A DoD Intra-governmental Asset Balances</b>	<b>Treasury Index</b>	<b>Fund Balance with Treasury</b>	<b>Accounts Receivable</b>	<b>Loans Receivable</b>	<b>Investments</b>	<b>Other</b>
Executive Office of the President	11		\$210			
Department of Agriculture	12		\$7			
Department of the Interior	14		\$0			
Department of Justice	15		\$95			
Navy General Fund	17		\$11,884			
Department of State	19		\$49			
Department of the Treasury	20	\$875,343	\$99			
Army General Fund	21		\$211,321			
Library of Congress	3		\$14			
Department of Veterans Affairs	36		\$13			
General Service Administration	47		\$191			
Central Intelligence Agency	56		\$202			
Air Force General Fund	57		\$5,039			
Department of Transportation	69		\$403			
Homeland Security	70		\$1,030			
Department of Health and Human Services	75		\$60			
National Aeronautics and Space Administration	80		\$0			
Department of Energy	89		\$11			
US Army Corps of Engineers	96		\$40			
Other Defense Organizations General Funds	97		\$4,297			
Other Defense Organizations Working Capital Funds	97-4930		\$5,149			\$8,669
Navy Working Capital Fund	97-4930.002		\$2,474			
Air Force Working Capital Fund	97-4930.003		\$419			
<b>Totals</b>		<b>\$875,343</b>	<b>\$243,007</b>	<b>\$0</b>	<b>\$0</b>	<b>\$8,669</b>

### Required Supplemental Information - Part B

#### AT97 - Army Working Capital Fund

(\$ in Thousands)

Schedule, Part B DoD Intra-governmental entity liabilities	Treasury Index	Accounts Payable	Debts/Borrowings From Other Agencies	Other
Department of Labor	16			\$48,768
Navy General Fund	17	\$1,745		
Army General Fund	21	\$22,606		
Office of Personnel Management	24			\$9,382
Air Force General Fund	57	\$6		
US Army Corps of Engineers	96	\$0		
Other Defense Organizations General Funds	97	\$96		
Other Defense Organizations Working Capital Funds	97-4930	\$46,777		\$0
Navy Working Capital Fund	97-4930.002	\$4,607		
Air Force Working Capital Fund	97-4930.003	\$3,081		
<b>Totals</b>		<b>\$78,918</b>		<b>\$58,150</b>

**Required Supplemental Information - Part C**

**AT97 - Army Working Capital Fund**

*(\$ in Thousands)*

<b>Schedule, Part C</b>	<b>Treasury Index</b>	<b>Earned Revenue</b>
<b>DoD Intra-governmental revenue and related costs</b>		
Executive Office of the President	11	\$3,597
Department of Agriculture	12	\$99
Department of Commerce	13	(\$29)
Department of the Interior	14	\$22
Department of Justice	15	\$3,338
Navy General Fund	17	\$410,292
Department of State	19	\$436
Department of the Treasury	20	\$136
Army General Fund	21	\$10,387,173
Office of Personnel Management	24	\$5
Library of Congress	3	\$111
Department of Veterans Affairs	36	\$13
General Service Administration	47	\$801
Central Intelligence Agency	56	\$1,569
Air Force General Fund	57	\$100,157
Department of Transportation	69	\$3,635
Homeland Security	70	\$7,047
Department of Health and Human Services	75	\$613
National Aeronautics and Space Administration	80	\$64
Department of Energy	89	\$10
US Army Corps of Engineers	96	\$402
Other Defense Organizations General Funds	97	\$103,178
Other Defense Organizations Working Capital Funds	97-4930	\$73,474
Navy Working Capital Fund	97-4930.002	\$168,304
Air Force Working Capital Fund	97-4930.003	\$194,266
<b>Totals</b>		<b>\$11,458,713</b>

**Required Supplemental Information - Part E**

**AT97 - Army Working Capital Fund**

*(\$ in Thousands)*

<b>Schedule, Part E</b>	<b>Treasury Index</b>	<b>Transfers In</b>	<b>Transfers Out</b>
<b>DoD Intra-governmental non-exchange revenue</b>			
Army General Fund	21		\$68
Other Defense Organizations Working Capital Funds	97-4930	\$75	
<b>Totals</b>		<b>\$75</b>	<b>\$68</b>







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

November 8, 2006

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

SUBJECT: Independent Auditor's Report on the Fiscal Year 2006 Army Working Capital Fund  
Financial Statements (Report No. D-2007-013)

The Chief Financial Officers Act of 1990, as amended, requires the Department of Defense Inspector General to audit the accompanying Army Working Capital Fund Consolidated Balance Sheet as of September 30, 2006 and 2005, the related Consolidated Statement of Net Cost, the Consolidated Statement of Changes in Net Position, the Combined Statement of Budgetary Resources, and the Combined Statement of Financing for the fiscal years then ended. The financial statements are the responsibility of Department of Army management. The Army is also responsible for implementing effective internal control and for complying with laws and regulations. We are unable to give an opinion on the Fiscal Year 2006 Army Working Capital Fund Financial Statements because of limitations on the scope of our work. Thus, the financial statements may be unreliable. In addition to our disclaimer of opinion on the financial statements, we are including the required Report on Internal Control and Compliance with Laws and Regulations. The Report on Internal Control and Compliance with Laws and Regulations is an integral part of our disclaimer of opinion on the financial statements and should be considered in assessing the results of the audit.

### Disclaimer of Opinion on the Financial Statements

The Assistant Secretary of the Army (Financial Management and Comptroller) acknowledged to us that the financial management and feeder systems that provide evidence supporting the Army Working Capital Fund financial statements do not comply with Federal financial management system requirements, generally accepted accounting principles, and the U.S. Government Standard General Ledger at the transaction level. Therefore, we did not perform auditing procedures to determine whether material amounts on the financial statements were fairly presented. We did not perform these and other auditing procedures because Section 1008(d) of the FY 2002 National Defense Authorization Act limits the Department of Defense Inspector General to perform only audit procedures required by generally accepted government auditing standards that are consistent with the representations made by management. The Army has also acknowledged, and prior audits have identified, the material weaknesses listed in the Summary of Internal Control. These material weaknesses also affect the reliability of certain information contained in the annual financial statements—much of which is taken from the same data sources as the basic financial statements.<sup>1</sup> Therefore, we are unable to express, and we do not express, an opinion on the basic financial statements. Additionally, the purpose of the audit was not to express an opinion on the information accompanying the basic financial statements. Accordingly, we express no opinion on the accompanying information.

<sup>1</sup> The annual financial statements include the basic financial statements, management discussion and analysis, consolidating and combining financial statements, Required Supplementary Stewardship Information, Required Supplementary Information, and Other Accompanying Information.

## Summary of Internal Control

In planning our audit, we considered Army internal control over financial reporting and compliance. We did this to determine our procedures for auditing the financial statements and to comply with Office of Management and Budget guidance, but our purpose was not to express an opinion on internal control. Accordingly, we do not express an opinion on internal control over financial reporting and compliance. However, previously identified reportable conditions, all of which are material, continued to exist in the following areas:

- Financial Management Systems
- Inventory
- General Property, Plant, and Equipment
- Intragovernmental Transactions and Eliminations
- Accounting Adjustments
- Accounts Payable
- Statement of Net Cost
- Statement of Financing

Material weaknesses are reportable conditions in which internal controls do not reduce (to a relatively low level) the risk of misstatements that are material to the financial statements and that might not be timely detected by employees while performing their normal assigned functions.

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

Our internal control work (conducted during prior audits) would not necessarily disclose all reportable conditions. The Attachment offers additional details on reportable conditions, all of which we consider to be material internal control weaknesses.

## Summary of Compliance with Laws and Regulations

Our work to determine compliance with selected provisions of applicable laws and regulations related to financial reporting was limited because management acknowledged, and prior audits confirm, that instances of noncompliance continue to exist. The Army acknowledged to us that many of its critical financial management and feeder systems do not comply with the requirements of the Federal Financial Management Information Act of 1996. Therefore, we did not determine whether the Army complied with all applicable laws and regulations related to financial reporting. Providing an opinion on compliance with certain provisions of laws and regulations was not an objective of our audit and, accordingly, we do not express such an opinion. See the Attachment for additional details on compliance with laws and regulations.

## Management Responsibility

Management is responsible for:

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

- complying with applicable laws and regulations.

We provided a draft of this report to the Army. Army officials concurred with the facts and conclusions in the report. Army officials also provided technical comments, which have been incorporated as appropriate. Army officials expressed their continuing commitment to address the problems this report outlines.



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

Attachment:  
As stated



## Report on Internal Control and Compliance with Laws and Regulations

### Internal Control

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

**Material Weaknesses.** Management acknowledged that previously identified reportable conditions, all of which are material, continue to exist.

**Financial Management Systems.** Army Working Capital Fund systems are unable to meet all of the requirements for full accrual accounting. The systems do not collect and record financial information, as required by generally accepted accounting principles. Financial and nonfinancial feeder systems are not integrated and do not contain an audit trail at the transaction level for the amounts reported in the proprietary and budgetary account balances. The Army Working Capital Fund derives most of its financial information for major accounts from noncompliant financial systems, such as the Commodity Command Standard System and the Standard Industrial Funds System.

In FY 2003, the Army began the deployment of the Logistics Modernization Program as its future core accounting system for the Army Working Capital Fund. The Army originally anticipated full implementation of the Logistics Modernization Program system by September 2005. However, implementation problems and the system's inability to stabilize data and achieve compliance with the Federal Financial Management Information Act of 1996 at the initial field locations have prevented further implementation of the system.

During FY 2006, as part of our financial-related audits, we noted deficiencies in the ability of the Logistics Modernization Program system to properly record transactions in the U.S. Government Standard General Ledger. The Logistics Modernization Program system did not have the internal system functionality to perform prevalidation with DoD payment systems as required by Public Law 108-287. In other words, the system could not match obligations to anticipated disbursements before payment. The Army also disclosed in the notes to its FY 2006 Army Working Capital Fund Financial Statements instances where the Logistics Modernization Program system did not properly populate general ledger accounts and either reported abnormal balances or required forced journal entries to remedy the situation. These problems could further delay the implementation of the system. Other system changes are also necessary. For example, the Logistics Modernization Program system is unable to record memorandum entries in the U.S. Government Standard General Ledger for current year asset activity and receive General Property, Plant, and Equipment data from feeder systems as required for Federal financial management system requirements.

Full deployment of the Logistics Modernization Program system is scheduled for FY 2010. This implementation date is contingent on the ability to restructure the system acquisition process, improve project governance, and meet performance goals. Because the Army is relying on the success of the Logistics Modernization Program system to obtain an unqualified opinion on the Army Working Capital Fund financial statements, these problems could jeopardize Army's success.

**Inventory.** The existing inventory valuation method does not produce an auditable approximation of historical cost. The Army uses the latest acquisition cost method of valuing most of the inventory because Army legacy inventory systems were designed for materiel management rather than accounting. The systems provide accountability and visibility over inventory items, but do not maintain the historical cost data necessary to comply with Statement of Federal Financial Accounting Standards No. 3, "Accounting for Inventory and Related Property." The systems are unable to produce financial transactions using the U.S. Government Standard General Ledger accounts and neither the Defense Finance and Accounting Service nor the Army reconciled all differences between the accounting records and the logistical records. Instead, the Defense Finance and Accounting Service accepted the data from the logistical records and adjusted the accounting records by at least \$3.6 billion.

**General Property, Plant, and Equipment.** The reported value of Army Working Capital Fund General Property, Plant, and Equipment is unreliable because the Army lacked the documentation needed to support the historic acquisition cost of its assets. Information on the acquisition date and cost is not always available and is sometimes incorrectly recorded. These conditions will continue to exist until the Army can establish a methodology to baseline and support the reported acquisition costs of its General Property, Plant, and Equipment. In addition, the Army did not implement the new DoD capitalization threshold of \$20,000 for real property assets. During FY 2006, the Army reported that the Integrated Facilities System used to report real property assets was substantially compliant with the Federal Financial Management Information Act of 1996. In August 2006, the DoD Office of Inspector General announced an audit to evaluate the controls over Army Working Capital Fund real property assets. The audit will determine whether controls over real property additions, deletions, and modifications entering the Integrated Facilities System are sufficient to maintain accurate balances once the Army establishes a supportable baseline.

**Intragovernmental Transactions and Eliminations.** DoD is unable to collect, exchange, and reconcile buyer and seller intragovernmental transactions, resulting in adjustments that cannot be verified. DoD and Army Working Capital Fund systems do not capture the trading partner financial data at the transaction level, as necessary, to facilitate the reconciliation and elimination of intragovernmental transactions. DoD procedures require that buyer-side transaction data be forced to agree with seller-side transaction data from other intragovernmental entities without the entities performing proper reconciliations. As a result, Defense Finance and Accounting Service Indianapolis made \$15.4 billion in adjustments to Army Working Capital Fund accounts to force these accounts into agreement with the corresponding records of intragovernmental trading partners.

**Accounting Adjustments.** Defense Finance and Accounting Service Indianapolis did not adequately support \$8 billion in journal vouchers used to prepare the Army Working Capital Fund financial statements. Defense Finance and Accounting Service Indianapolis made the unsupported adjustments to force amounts to agree with other sources of information and records used to prepare the FY 2006 Army Working Capital Fund Financial Statements. Defense Finance and Accounting Service Indianapolis did not always follow the established minimum requirements for documenting journal vouchers to support adjusting accounting entries made to the general ledger accounts. The resulting unsupported accounting adjustments presented a material uncertainty regarding the line item balances on the FY 2006 Army Working Capital Fund Financial Statements. These adjustments affected the financial information on all of the statements.

**Accounts Payable.** Army Working Capital Fund systems are unable to properly account for and report Accounts Payable. The Supply Management activity group does not establish Accounts Payable in accordance with Statement of Federal Financial Accounting Standards No. 1, "Accounting for Selected Assets and Liabilities," which requires the Army to establish an Accounts Payable when it accepts title to goods or services. The Army recognized Accounts Payable based on the physical receipt of the goods or services rather than when the Government accepted title to the goods or services. The Army further misstated the Accounts Payable balances by approximately \$174.9 million because organizations using the Logistics Modernization Program system had not resolved \$88.7 million in abnormal Accounts Payable balances and reported \$86.2 million in Accounts Payable related to inventories in transit that the Army had accepted at the shipping point as "other liabilities." Defense Finance and Accounting Service Indianapolis was unable to reconcile intragovernmental Accounts Payable with the intragovernmental Accounts Receivable that generated the payable. As a result, the Defense Finance and Accounting Service Indianapolis made \$39.5 million in unsupported adjustments to increase intragovernmental Accounts Payable to force the amounts to agree with Army Working Capital Fund trading partners. Defense Finance and Accounting Service Indianapolis also adjusted Accounts Payable with the public downward by \$2.7 million for undistributed disbursements.

**Statement of Net Cost.** The Statement of Net Cost was not presented by responsibility segments consistent with DoD performance goals and measures. Accounting systems were unable to accurately capture costs for Army Working Capital Fund programs and properly account for intragovernmental transactions and related eliminations. In addition, the Army Working Capital Fund used budgetary obligation, collection, and disbursement data to present some of the information reported on the Statement of Net Cost.

**Statement of Financing.** The Office of Management and Budget requires a consolidated Statement of Financing except for the budgetary information used to calculate net obligations, which is prepared on a combined basis. The Army Working Capital Fund prepares the Statement of Financing on a combined basis. Also, because no reconciliation of differences between the Statement of Net Cost and the Statement of Financing occurred, the Statement of Financing does not accurately present the relationship between budgetary obligations incurred by the Army Working Capital Fund and its Net Cost of Operations. For example, Defense Finance and Accounting Service Indianapolis prepared \$1.6 billion in unsupported adjustments to the equipment general ledger account to force costs to match with obligation information.

These financial management deficiencies are indications of material weaknesses in internal control that may adversely affect any decision by Army management that is based, in whole or in part, on information that is inaccurate because of these deficiencies. Financial information reported by DoD may also contain misstatements resulting from these deficiencies.

## Compliance with Laws and Regulations

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

**Statutory Financial Management Systems Reporting Requirements.** The Army Working Capital Fund is required to comply with financial management systems reporting requirements. For example, the Federal Financial Management Information Act of 1996 requires DoD to establish and maintain financial management systems that comply substantially with Federal financial management systems requirements, applicable Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level. In addition, the Federal Managers' Financial Integrity Act of 1982 requires the Army to evaluate its systems and to report annually whether those systems comply with applicable requirements. The Chief Financial Officers Act of 1990 requires that each agency develop and maintain an integrated agency accounting and financial management system, including financial reporting and internal control. The system should comply with internal control standards and applicable accounting principles, standards, and requirements; and it should provide complete, reliable, consistent, and timely information.

The Army acknowledged that many of its critical financial management and feeder systems did not substantially comply with Federal financial management system requirements, generally accepted accounting principles, and the U.S. Government Standard General Ledger at the transaction level. The Army was also unable to comply with the Chief Financial Officers Act of 1990, which requires agencies to develop and maintain integrated agency accounting and financial systems.

## Audit Disclosures

The Army acknowledged to us on February 10, 2006, that the Army Working Capital Fund financial management systems cannot provide adequate evidence supporting various material amounts on the financial statements. Therefore, we did not conduct audit work related to the previously identified deficiencies.

In addition, we did not perform audit work related to the following selected provisions of laws and regulations:

- Antideficiency Act
- Provisions Governing Claims of the United States Government
- Federal Credit Reform Act of 1990
- Pay and Allowance System for Civilian Employees
- Prompt Payment Act

This report does not include recommendations to correct the material internal control weaknesses and instances of noncompliance because previous audit reports contained recommendations for corrective actions.









### ***Relevant and Ready Landpower in Service to the Nation***

*The Civil Works' mission is constantly evolving to keep pace with the changing needs of the Nation. Today, those missions fall in four broad areas: water infrastructure, environmental management and restoration, emergency response and assistance, and engineering support and technical services.*

## Overview

### Mission

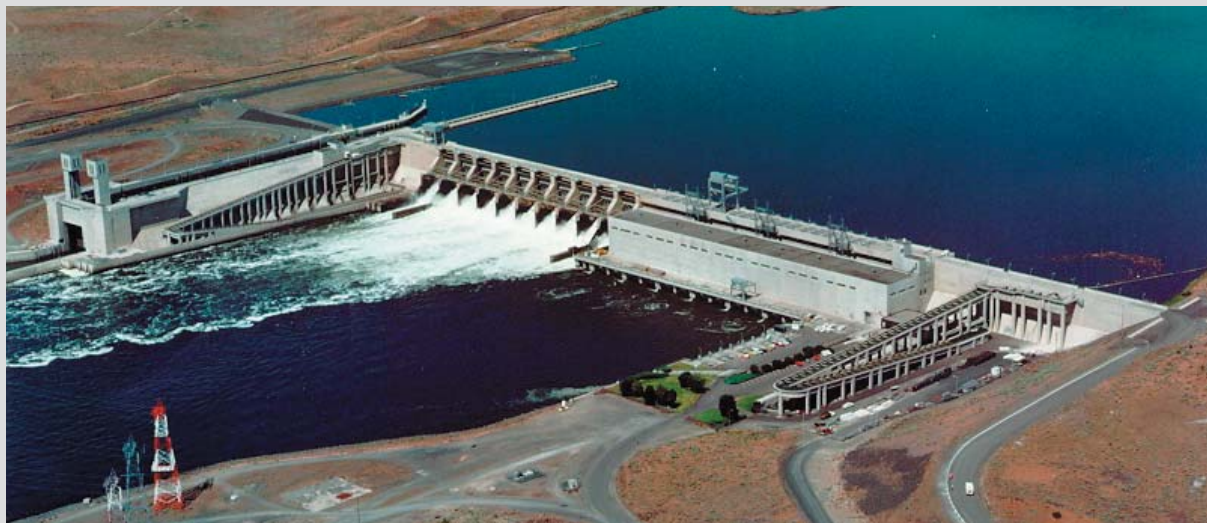
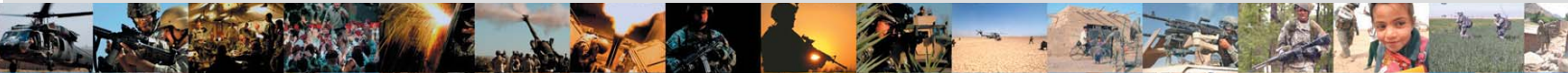
The civil works mission is to contribute to the national welfare and serve the public by providing the nation and the Army with quality, responsive development and management of the nation's water resources; protection, restoration, and management of the environment; disaster response and recovery; and engineering and technical services. The mission will be accomplished in an environmentally sustainable, economic, and technically sound manner through partnerships with other governmental agencies and nongovernmental organizations.

### *Developing and Managing Water Resources*

The original role of the Corps of Engineers in civil works, as it related to developing and managing water resources, was to support navigation by maintaining and improving water channels. Over the years and through subsequent legislation, the Corps' role was expanded to include flood damage reduction, hydroelectric power generation, recreation, and water storage.

### *Protecting, Restoring, and Managing the Environment*

The Rivers and Harbors Act of 1899 required the Corps to prevent the obstruction of navigable waterways. As concern over the environment grew in the late 20th century, the Clean Water Act of 1972 greatly broadened the



Ice Harbor Lock and Dam-Lake Sacajawea is Unit 1 of 4 included in the "Lower Snake River Project, Washington, and Idaho"

Civil Works Fund

# 2006

Corps' responsibility by providing authority over the dredging and filling in of United States' waters, including the country's wetlands. The civil works program's environmental responsibilities have continued to grow through additional legislation.



U.S. Army Corps of Engineers deployable tactical operations system trailers assist in hurricane recovery effort.

### ***Responding and Assisting in Disaster Relief***

Throughout the Corps' history, America has relied on the civil works program for help in times of national disaster. This help is now provided under two basic authorities: the Flood Control and Coastal Emergency Act (P.L. 84-99, as amended), and the Robert T. Stafford Disaster and Emergency Assistance Act. The primary role of the civil works program in emergency relief and recovery operations is to provide public works and engineering support.

### ***Providing Engineering Support and Technical Services***

In Titles 10 and 33 of the U.S. Code, Congress expresses its intent that the Corps provide services on a reimbursable basis to other federal entities; state, local, and tribal governments; private firms; and international organizations. Additional authorities to provide services that are applicable to all federal agencies are provided in Titles 15, 22, and 31. These authorities include providing services to foreign governments.

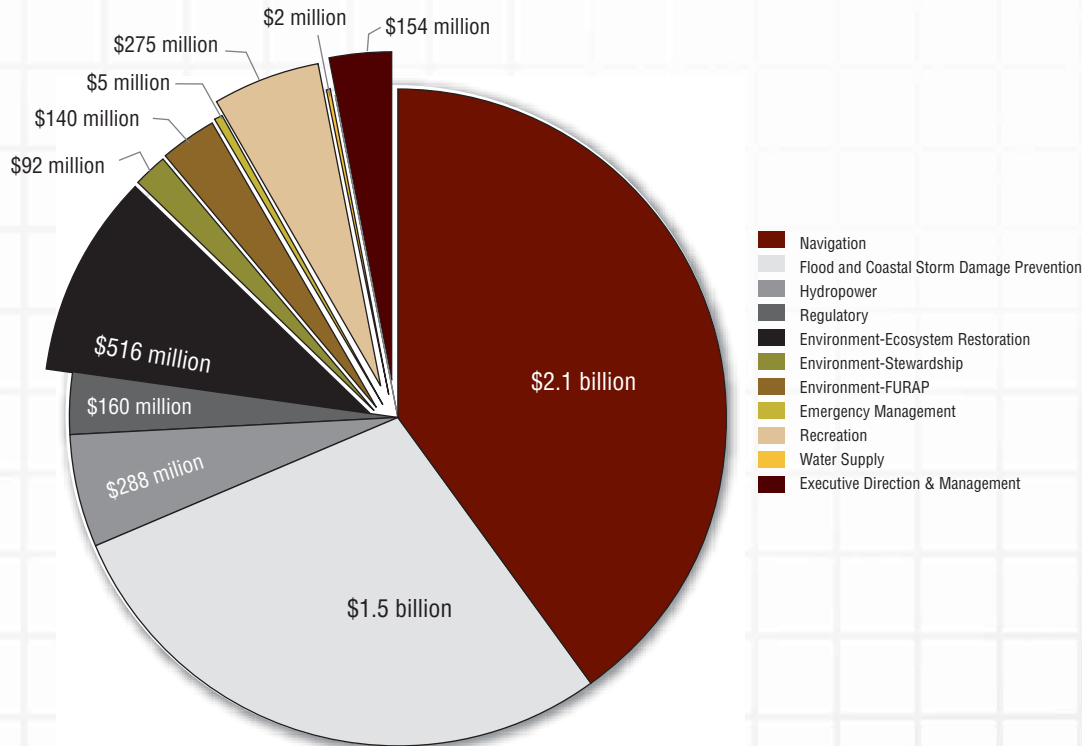


A United States Coast Guard cutter and an ore carrier pass each other in a Michigan navigation channel maintained by the USACE.

### Civil Works Programs

The Corps has multiple programs to accomplish its mission. Figure 14 lists the programs that receive direct appropriations; furthermore it shows the funds used for executive direction and management for those programs. Another program, support for others, is conducted on a reimbursable basis. Each program specifically addresses a single mission component, but each may also contribute to one or more of the other’s missions.

Figure 14. FY 2006 Civil Works Initial Appropriation by Program



### Navigation

The navigation program is responsible for providing safe, reliable, efficient, and environmentally sustainable waterborne transportation systems for the movement of commercial goods and for national security needs. The program seeks to meet this responsibility through a combination of capital improvements and the operation and maintenance of existing infrastructure projects. The navigation program is vital to the nation’s economic prosperity: 95 percent of America’s overseas international trade moves through its ports. Our nation’s marine transportation system (MTS) encompasses a network of navigable channels, waterways, and infrastructure maintained by the Corps, as well as publicly and privately owned vessels, marine terminals, inter-modal connections, shipyards, and repair facilities. The MTS consists of approximately 12,000 miles of inland and intracoastal waterways; over 900 coastal, Great Lakes, and inland harbors; and channel projects that are maintained by the Corps.

In FY 2006, this \$2.06 billion program accounted for over 38 percent of civil works appropriations.

## Flood and Coastal Storm Damage Reduction Program

This program is aimed at saving lives and reducing property damage in the event of floods and coastal storms. The civil works program has constructed 8,500 miles of levees and dikes, 383 reservoirs, and more than 90 storm damage reduction projects along 240 miles of the nation's 2,700 miles of shoreline. With the exception of the reservoirs, most of the infrastructure constructed under this program is owned and operated by the sponsoring cities, towns, and agricultural levee districts.

The flood and coastal storm damage reduction program has compiled an impressive record of performance. In the period 1995–2004, floods in unprotected areas caused the United States an average of \$5.4 billion yearly in property damage. In the same period, Corps projects in protected areas prevented \$22.9 billion in average annual damages. Through FY 2000, the nation had invested \$43.6 billion (\$122 billion, adjusted for inflation) in flood damage reduction projects, preventing an estimated \$419 billion (\$709 billion, adjusted for inflation) of flood damage. Adjusted for inflation, these figures show a return on investment of more than \$6.36 in damage prevented for each dollar spent. The program also has helped reduce the number of lives lost annually due to floods from an average of 179 in the decade 1972–1981 to 89 in the period 1991–2000.

In FY 2006, this \$1.51 billion program accounted for more than 28 percent of civil works appropriations.

## Environmental Protection, Restoration, and Management

Three distinct programs, aquatic ecosystem restoration, stewardship of Corps lands, and the Formerly Utilized Sites Remedial Action Program, make up the environmental program. Responding to the growing national awareness of the importance of the natural environment, these programs address many issues such as monitoring water quality at dam sites, managing the natural resources on 11.5 million acres of land and water at 456 multi-purpose Corps project sites, restoring degraded aquatic habitats to more natural conditions, and clean up of hazardous material.

The Army's mission in the area of aquatic ecosystem restoration is to help restore aquatic habitat to a less degraded and more natural condition in ecosystems whose structures, functions, and dynamic processes have become degraded. The emphasis is on restoration of nationally or regionally significant habitat where the solution primarily involves manipulating the hydrology and geomorphology. During fiscal year (FY) 2005, a total of 32,500 acres of aquatic, wetland, and floodplain habitat were restored.

In FY 2006, the combined environmental programs received a total initial appropriation of \$748 million, which accounted for almost 14 percent of the total civil works initial appropriation.



Ducks, geese, and other waterfowl are protected on more than 85,200 acres of Army Corps of Engineers land devoted to wildlife management.

## Regulation of Wetlands and Waterways

In accordance with the Rivers and Harbors Act of 1899 (Sec. 10) and the Clean Water Act of 1972 (Sec. 404), as amended, the Army Civil Works Regulatory Program regulates the discharge of dredged and fill material into waters of the United States, including wetlands. The Corps implements many of its oversight responsibilities by means of a permit process.

Throughout the permit evaluation process, the Corps must comply with the National Environmental Policy Act and other applicable environmental and historic preservation laws. The objective of the program is to protect America's aquatic resources while allowing reasonable use of private property for important economic or infrastructure development on both private and public lands. The Corps must also consider the views of other federal, tribal, state, and local governments and agencies; interest groups; and the general public when rendering its final permit decisions.

In FY 2006, this \$160 million program accounted for almost 3 percent of civil works appropriations.

## Emergency Management

Throughout Corps history, America has relied on the civil works program for help in times of national disaster. Emergency management continues to be an important part of the civil works program. The civil works program supports the Department of Homeland Security in carrying out the National Response Plan. The Corps' primary role in support of this plan is to provide emergency support in areas of public works and engineering. The Corps responds to more than 30 presidential disaster declarations in a typical year, and its highly trained workforce is prepared to deal with both man-made and natural disasters. After being struck by three major storms in 2005, the 2006 hurricane season has been relatively mild.

In FY 2006 the Corps continues to support major recovery operations in the Gulf Coast region in response to Hurricanes Rita and Katrina. Over 8,000 Corps employees were deployed from their home stations to assist in this response; and at the end of FY 2005, several thousand Corps employees remained deployed in Florida, Louisiana, Texas and Mississippi. Corps personnel provide temporary housing, power, debris removal, ice, water, and infrastructure support to the impacted region.

Hurricanes Katrina, Rita, Wilma, and Ophelia caused significant damage to the flood protection and hurricane protection projects along the Gulf Coast and South Atlantic states. Hurricane Katrina alone caused extensive damage to the hurricane shore protection and flood control projects in the states of Louisiana, Mississippi and Alabama,



Two large loads of pumping equipment and their support crew from the Corps of Engineers Little Rock District pass through the Inner Harbor Navigation Canal Lock. The equipment was unloaded in New Orleans to help pump the water out of the lower Ninth Ward.

totaling over \$2.1 billion. Major damages to the storm protection system in the New Orleans area included major breaches of significant sections of levees and floodwalls on the Lake Pontchartrain and Vicinity and the New Orleans to Venice projects that required major repairs prior to the beginning of hurricane season on June 1, 2006. Emergency repairs to these projects totaled more than \$800 million and were completed before the start of the 2006 hurricane season. Repair work on other projects in the New Orleans area is continuing.

In addition, major improvements and accelerated completion of portions of authorized projects in the New Orleans area were authorized by Congress through additional emergency supplemental appropriations. Planning and construction of these improvements began in early FY 2006 and will continue through FY 2010. To date, \$5.6 billion has been appropriated for the repairs and improvements authorized for the storm and flood damage reduction systems in New Orleans, Southeast Louisiana, and other Gulf Coast states.

The Corps not only makes contributions to domestic emergency management efforts, it also plays a major role on the international stage through its participation in the civil military emergency preparedness program. In support of DoD, the Corps shares emergency management knowledge and expertise with U.S. Allies and partners in the former Soviet Republics and Eastern Europe. This valuable program brings together key leaders and builds relationships between nations in direct support of the National Defense Strategy.

In FY 2006, this program received new budget authority of \$5 million, accounting for less than 1 percent of civil works' new appropriation authority.



A USACE employee makes two children "official safety officers" and tells them to be responsible for their own safety and the safety of their parents and friends.

## Hydropower

The Corps' multi-purpose authorities afford hydroelectric power as an additional benefit of projects built for navigation and flood control. The Corps is the largest owner/operator of hydroelectric power plants in the United States and one of the largest in the world. The Corps operates 345 generating units at 75 multipurpose reservoirs, mostly in the Pacific Northwest, accounting for about 24 percent of America's hydroelectric power and about three percent of the country's total electric-generating capacity. Its hydroelectric plants produce nearly 100 billion kilowatt-hours each year, sufficient to serve about 10 million households—equal to ten cities the size of Seattle, Washington. Hydropower is a renewable source of energy and one of the least environmentally disruptive sources of electric power, producing none of the airborne emissions that contribute to acid rain or the greenhouse effect.

In FY 2006, this \$288 million program accounted for just over five percent of civil works appropriations.





167  
Niagara Falls altitude varies from 100 to 600 feet and the power of the falling water is used to generate electricity. This picture, looking down river, shows both falls.

## Water Supply

Careful management of the nation's water supply is critical to limiting water shortages and lessening the impact of droughts. The Corps has an important role in ensuring that homes, businesses, and farms nationwide have enough water to meet their needs. The Corps has the authority for water supply as part of projects that serve navigation, flood protection, and hydroelectric purposes.

In FY 2006, this \$2 million program accounted for less than 1 percent of civil works appropriations.

## Recreation

The Corps is an important provider of outdoor recreation as an ancillary benefit of flood prevention and navigation projects. The mission of the recreation program is to provide quality outdoor public recreation experiences to serve the needs of present and future generations and to contribute to the quality of American life, while managing and conserving natural resources consistent with ecosystem management principles.

This \$275 million program accounted for just over five percent of the civil works budget in FY 2006.

## Organizational Structure

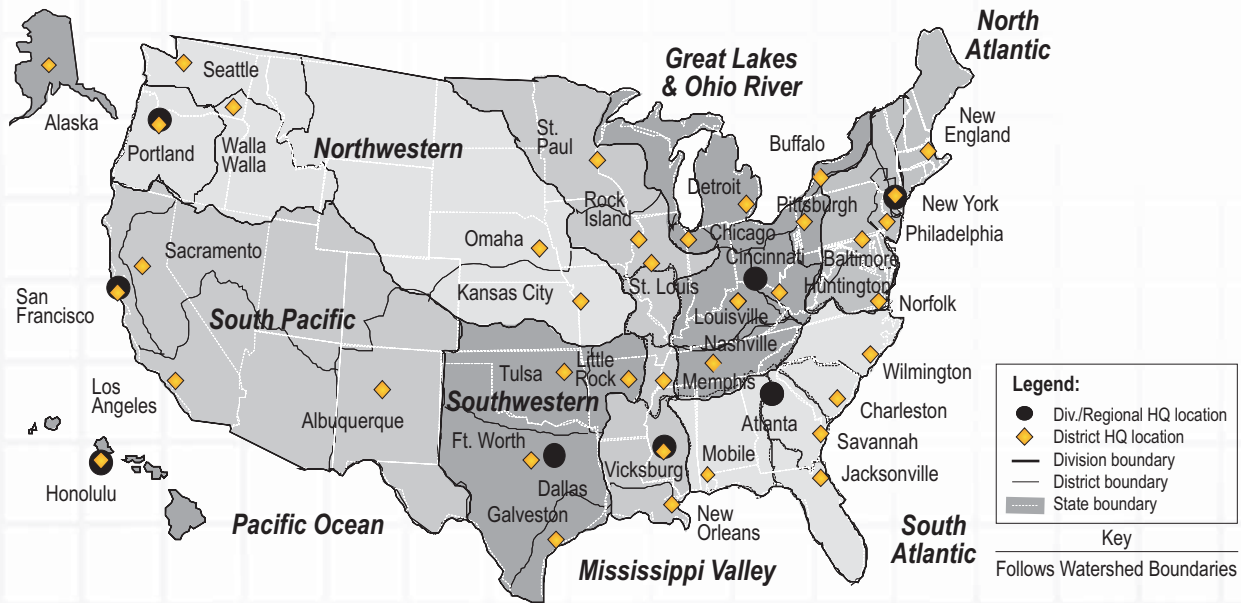
### The Workforce

The Corps employs almost 35,000 people, including 650 military officers and 24,800 civilians, who perform civil works duties. It is funded through the energy and water development appropriation and executes programs through eight regional divisions and 38 of the 41 districts of the Corps of Engineers — the remaining three districts have only military-related missions. There is a ninth provisional division in the Gulf Region supporting operations in Iraq and Afghanistan and it has four provisional districts embedded within the division.

Figure 15 shows the division boundaries. These are defined by watersheds and drainage basins, reflecting the water resources nature of the civil works mission.

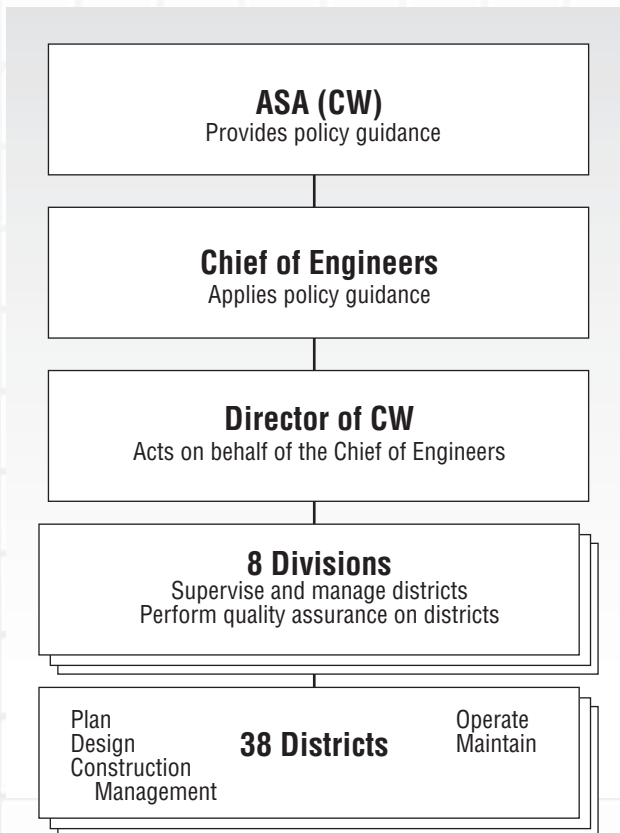
The distribution of civil works employees similarly highlights the customer focus of the program: 95 percent of employees work at the district level, labs or field operating agencies reflecting the fact that project management is performed at the district level. The civil works program contracts out to civilian companies all of its construction

Figure 15. Civil Works Boundaries



and most of its design work. As many as 150,000 people are indirectly employed in support of civil works projects. These contractual arrangements have served the nation well in times of emergency.

Figure 16. Civil Works Levels of Authority



### The Leadership

Oversight of civil works is provided through four levels of authority. As shown in Figure 16, the Assistant Secretary of the Army for Civil Works (ASA (CW)) is appointed by the President and is responsible for civil works policy. The Chief of Engineers is a military officer who reports to the ASA (CW) and is responsible for mission accomplishment. He delegates most of his responsibilities for managing the various programs to the Director of Civil Works. The Chief of Engineers, through the Director of Civil Works, is responsible for the leadership and management of the civil works program and for ensuring that policies established by the ASA (CW) are applied to all phases of the civil works mission. The divisions, commanded by division engineers, are regional offices responsible for the supervision and management of their subordinate districts, including the monitoring and quality assurance of district work. The districts are the foundation of the civil works mission, managing water resource development over a project's life cycle.



## Civil Works Fund Performance Results

Civil works directly impacts America's prosperity, competitiveness, quality of life, and environmental stability. In March 2004 the civil works leaders published a strategic plan that provides a framework for enhancing the sustainability of America's resources. The strategic goals listed in the plan support the strategic direction of Corps over the five-year period from FY 2004 – FY 2009. Key performance measures developed in conjunction with the Office of Management and Budget through the Performance Assessment Rating Tool process for FY 2002 – FY 2006 are presented below.

### Goal 1: Provide Sustainable Development and Integrated Management of the Nation's Water Resources.

#### *Navigation*

**Objective:** To invest in navigation infrastructure that is fully capable of supporting maritime requirements in environmentally sustainable ways where economically justified.

**Performance Indicator:** Track navigation lock availability by identifying trends in scheduled and unscheduled lock closures for the navigation system, measured in hours.

**Performance Result:** The Corps uses the same indicator as in Goal 3; please see Table 18 for the results.

#### *Flood and Coastal Storm Damage Reduction*

**Objective:** To invest in flood and coastal storm damage reduction solutions when the benefits exceed the costs.

**Performance Indicator:** This is measured by the performance of civil works facilities in reducing damage where flooding otherwise would have been experienced.

**Performance Result:** The Corps uses the same indicator as in Goal 3; please see Table 19 for the results.

#### *Hydropower*

**Objective:** To invest in hydropower solutions when benefits exceed the costs.

**Performance Result:** The Corps uses the same indicator as in Goal 3; please see Table 20 for the results.

### Goal 2: Repair Past Environmental Degradation and Prevent Future Environmental Losses

#### *Regulatory*

**Objective:** To administer the regulatory program in a manner that protects the aquatic environment (assures zero net-loss of wetlands).

**Performance Indicators:** The eight measures listed in Table 15 serve as indicators to assist Corps personnel to determine their progress in meeting this objective. The indicators are explained below along with the Fiscal Year 2006 goals.

- **Individual permit compliance.** The Corps shall complete compliance inspections on 15 percent of all individual permits issued and constructed within the preceding fiscal year.
- **General permit compliance.** The Corps shall complete compliance inspections of 5 percent of all general permits with reporting requirements issued and constructed within the preceding fiscal year.

- **Mitigation site compliance.** The Corps shall complete field compliance inspections of 15 percent of active mitigation sites each fiscal year. Active mitigation sites are those sites authorized through the permit process. They are monitored as part of the permit process but have not met final approval under the permit special conditions.
- **Mitigation inspections or audits.** The Corps shall complete compliance inspections or audits on 50 percent of active mitigation banks and in lieu of fee programs annually.
- **Resolution of non-compliance issues.** The Corps will reach resolution on non-compliance with permit conditions or mitigation requirements on 25 percent of activities determined to be non-compliant at the end of the previous fiscal year and determined to be non-compliant during the current fiscal year.
- **Resolution of enforcement actions.** The Corps shall reach resolution on 25 percent of all pending enforcement actions (i.e., unauthorized activities) that are unresolved at the end of the previous fiscal year and have been received during the current fiscal year.
- **General permit decisions.** The Corps shall reach permit decisions on 90 percent of all general permit applications within 60 days.
- **Individual permits.** The Corps shall reach permit decisions on 65 percent of all standard permits and letters of permission within 120 days. This standard shall not include individual permits with Formal Endangered Species Act consultations.

Table 15. Regulatory Indicators

	FY 2002	FY 2003	FY 2004	FY 2005
Percent of compliance inspections on individual permits	21	18	16	14
Percent of compliance inspections on general	7	6	5	5
Percent of active mitigation sites inspected	13	15	11	9
Percent of compliance inspections on active mitigation banks	25	25	20	19
Percent resolution on non-compliance with permit conditions or mitigation requirements	33	30	26	24
Percent resolution on pending enforcement actions	25	25	37	23
Percent of general permit applications decisions made within 60 days.	90	88	85	85
Percent of standard permits and letter of permission permit decisions made within 120 days	65	58	61	61

Note: FY 2006 data were not available at time of printing.

### *Environmental Remediation*

**Objective:** To achieve the clean-up objectives of the Formerly Utilized Sites Remedial Action Program. The Corps uses three outcome measures to indicate progress meeting this objective: Minimize risk to human health and the environment, maximize the cubic yardage of contaminated material disposed in a safe and legal disposal facility, and return the maximum number of affected individual properties to beneficial use.

**Performance Indicators:** The measures listed in Table 16 serve as indicators to assist Corps personnel to determine their progress in meeting this objective. The indicators are explained below.

- **Number of records of decision (ROD) signed.** As studies are completed and best alternatives for cleanup activities are decided, the number of RODs will increase. A final ROD establishes the final cleanup standard, which controls the actual estimate of the remaining environmental liability for each site.
- **Number of remedial investigations (RI) completed.** The RI establishes the baseline risk assessment whereby the level of risk to human health and the environment is identified.

- **Number of action memorandums signed.** Where warranted by risk or other limited factors, action memorandums allow the Corps to move toward reducing risk more rapidly than through production of a ROD. No action memorandums are presently identified.
- **Cubic yardage of contaminated material disposed.** Target soil amounts are dependent on previous-year funding and scheduled activities.
- **Number of remedies in place or response complete.** As select portions of sites or complete sites meet their remedial action goals, the risk to human health and the environment is reduced to within acceptable levels and properties are able to be used within a community without fear of increasing cancer risk or further degrading the environment.

Table 16. Remedial Action Indicators

	FY 2004 (actual)		FY 2005 (actual)		FY 2006 (estimated)	
	Target	Actual	Target	Actual	Target	Actual
Number of RODs signed	9	9	2	3	3	2
Remedial investigations completed	21	21	4	5	5	4
Action memos signed	3	3	-	-	1	1
Cubic yards of contaminated material removed (in thousands)	2,927	2,927	168	243	213	225
Individual properties returned to beneficial use	65	65	5	5	15	15
Remedies in place or response complete	4	4	1	2	2	0

Complete FY 2006 data were not available at time of printing.

### *Environmental Stewardship*

**Objective:** To improve the efficiency and effectiveness of existing Corps water resources projects.

**Performance Indicator:** The outcome for this objective is to manage projects in an efficient manner. This measure is an assessment of federal costs avoided in relation to the program cost. Revenue recovered each year, equivalent to the federal costs avoided, will vary due to the nature and extent of the sustainability practices implemented. The program emphasis, however, is on resource sustainability as opposed to revenue generation. Indicator results data are in Table 25.

**Objective:** To ensure healthy and sustainable lands and waters and associated natural resources on Corps lands in public trust to support multiple purposes.

**Performance Indicator:** This measure is defined as the number of Corps fee-owned acres classified as in a sustainable condition divided by the total number of Corps fee-owned acres. The result provides an indicator of the condition status of all Corps fee-owned acres. Sustainable is defined as meeting the desired state. The acreage is not significantly impacted by any factors that can be managed and does not require intensive management to maintain the health. The acreage also meets operational goals and objectives set forth in applicable management documents. Results for this indicator may also be found in Table 24.

**Performance Indicator:** This measure demonstrates the status of Corps efforts in completing basic, level one natural resource inventories required by ER 1130-2-540. Such inventories are necessary for sound resource management decisions and strategies development. The measure is defined as the sum total number of acres of completed inventory for each of the four components of the minimum level one natural resources inventory, divided by four times the total number of Corps fee-owned acres. The proportion (percentage) yielded is used to evaluate the relative completeness of the inventory. Results for this indicator may be found in Table 17.

**Performance Indicator:** A master plan is completed, per regulation, to foster an efficient and cost-effective project for natural resources, cultural resources, and recreational management programs. This measure demonstrates Corps commitment to fully integrate environmental stewardship in the management of operating projects. The measure is expressed as a percentage and is derived by dividing the number of required master plans completed in compliance with regulation, divided by the total number of required master plans. Results for this indicator may be found in Table 17.

**Objective:** To ensure that the operation of all Civil Works facilities and management of associated lands, including out-granted lands, complies with the environmental requirements of relevant federal, state, and local laws and regulations.

**Performance Indicator:** This measure is the percentage of significant environmental findings corrected compared to the number identified. The goal is 100 percent corrected. Results for this indicator may be found in Table 17.

**Objective:** To meet the mitigation requirements of authorizing legislation or applicable Corps authorization decision document.

**Performance Indicator:** This measure demonstrates the Corps performance in meeting mitigation requirements that are specified in project authorizations.

Table 17. Environmental Stewardship Indicators

	FY 2005 Actual	FY 2006 Actual	FY 2006 Estimate
Efficiency Percentage	9	1	1
Percent of sustainable acreage	37	40	36
Percent of natural resources inventory completed	33	36	33
Percent of master plans completed	32	35	33
Percent of significant environmental findings corrected	75	100	70
Percent of mitigated land meeting requirements	76	95	76

Complete FY 2006 data were not available at time of printing.

The measure is a percentage of the number of designated Corps-administered mitigation lands (acres) meeting mitigation requirements divided by the total number of designated Corps-administered mitigation lands, or the number of pounds (or number of individual) fish produced in a mitigation hatchery, divided by the number of fish to be produced at a mitigation hatchery to meet the mitigation requirement. Results for this indicator may be found in Table 17.

### *Environmental Stewardship*

**Objective:** Restore degraded, significant ecosystems structure, function and process to a more natural condition by investing in restoration projects or features that make a positive contribution to the nation's environmental resources in a cost-effective manner.

**Performance Indicators:** Four indicators were recently established that will assist Corps personnel to determine progress in meeting this objective. The Corps began collecting performance data relating these indicators during the current year and sufficient data are not yet available to establish baselines.

- **Number of acres of habitat restored, created, improved, or protected.** The number of acres of habitat restored is an appropriate measure for documenting progress towards restoration of degraded ecosystems.
- **Number of nationally significant acres of habitat restored, created, improved, or protected.** This measure will document the subset of acres of habitat restored each year that have high-quality outputs as compared to national needs.
- **Dollars per acre to restore, create, improve, or protect nationally significant habitat.** The cost of the projects that produce nationally significant acres in any given year will be used to calculate this figure. In the long run through efficiencies in project execution or other considerations, the goal would be to restore more acres per dollar expended.
- **Percentage of all acres of habitat restored, created, improved, or protected that are nationally significant.** Restoration of acreage that meets the criteria for national significance is expected to have the greatest impact on the restoration of the nation's ecosystems. The goal is to increase the percentage of nationally significant acres over time.

### Goal 3: Ensure that Projects Perform to Meet Authorized Purposes and Evolving Conditions

#### Navigation

**Objective:** To address the operation and maintenance backlog.

**Performance Indicator:** Track navigation lock availability to identify trends in scheduled and unscheduled hours closed for the navigation system. Table 18 shows unscheduled closure trends.

Table 18. Unscheduled Lock Closures

	FY 2003	FY 2004	FY 2005	FY 2006
Lock unscheduled closures (in thousands of hours)	47	39	44	68

#### Flood and Coastal Storm Damage Reduction

**Objective:** To improve the efficiency and effectiveness of existing Corps water resource projects.

**Performance Indicator:** This is measured by the performance of civil works facilities in reducing damage where flooding otherwise would have been experienced.

**Performance Result:** Table 19 shows that during FY 2005, the Corps prevented \$24 billion in flood damages. This can be compared to \$21.4 billion, the 10-year moving average that is used to smooth out the significant fluctuations in year-to-year flood damages prevented that are associated with variations in meteorological events.

Table 19. Flood Damages Prevented

	FY 2003	FY 2004	FY 2005
Flood damage prevented (in billions of dollars)	\$15.7	\$22.5	\$24.0
10-year rolling average	\$19.6	\$21.7	\$21.4

Note: FY 2006 data were not available at time of printing.

#### Hydropower

**Objective:** To improve the efficiency and effectiveness of existing Corps water resource projects.

**Performance Indicator:** The objective of the hydropower program is to maintain a high availability of hydroelectric power-generating capability at multipurpose reservoir projects. There are two primary indicators with which to measure successful performance toward this objective. One is to keep the forced outage (unplanned) rate at or below 2.0 percent. The lower the forced outage rate, the more reliable and the less expensive is the electrical power provided to the customer. The second goal is to maintain the power generating unit's availability during peak demand periods at or above 95 percent.

Table 20. Power Generating Capability

	2003	2004	2005
Percent of forced outages	3.45	4.00	4.66
Percent available during periods of peak demand	88.44	87.48	87.24

Note: FY 2006 data were not available at time of printing.

#### Recreation

**Objective:** To provide justified outdoor recreation opportunities in an effective and efficient manner at all Corps-operated water resources projects.

**Performance Indicators:** The three measures listed in Table 21 serve as indicators to assist Corps personnel to determine their progress in meeting the Corps' recreation efficiency objective. The indicators are explained on the following page.

**Total NED Benefits.** NED benefits are estimated using the Unit Day Value Method, which was originally developed by the Water Resources Council.<sup>1</sup>

- **Benefit to cost ratio.** This is the ratio of recreation benefits to recreation costs.
- **Cost recovery.** This indicator measures the percent of total recreation receipts to the recreation budget.

Table 21. Recreation Efficiency

	FY 2004	FY 2005	FY 2006
Total NED Benefits (in millions of dollars)	\$1,223	\$1,243	\$1,216
Benefit to Cost Ratio	4.28	4.30	4.27
Cost Recovery	16%	16%	16%

**Objective:** To provide continued outdoor recreation opportunities to meet the needs of present and future generations.

**Performance Indicator:** The recreation unit day availability is a measure of the capacity of facilities to provide recreation opportunities. It

is expressed in millions of days that Corps recreation units were available for public use. Results for this indicator may be found in Table 22.

Table 22. Recreation Day Availability

	FY 2004	FY 2005	FY 2006
Available for Use Days (in millions of days)	74	74	74

**Objective:** To provide a safe and healthful outdoor recreation environment for Corps customers.

**Performance Indicators:** The four measures listed in Table 23 serve as indicators to assist Corps personnel to determine their progress in meeting the Corps' recreation objectives. The indicators are explained below.

- **Customer service.** This is measured as a percentage of visitors to Corps-managed recreation areas who reported acceptable service.
- **Customer Satisfaction.** This is measured as a percentage of visitors reporting satisfaction with their visit to a Corps recreation area.

Table 23. Recreation Service Measures

	FY 2004	FY 2005	FY 2006
Customer Service – Visitor Centers	Note 1	79%	78%
Customer Service – Recreation Areas	Note 1	51%	50%
Customer Satisfaction	Note 2	88%	87%
Facility Service	Note 3	48%	48%
Facility Condition	3.7	3.7	3.7

Note 1: Services standards were revised in FY 2005 and FY 2004 data are not comparable with the current format.

Note 2: There is no completed survey data available for FY 2004.

Note 3: This measure was established at the end of FY 2004 and FY 2005 is the first year data was collected.

- **Facility service.** This is measured as the percentage of visitors served at a Corps-managed recreation area with a facility condition score of 4 or better, which indicates their experience was fair to good.

- **Facility condition.** This is the average condition of facilities at Corps-managed recreation areas. The score is based on a seven-point scale where 1 = poor and 7 = excellent.

### **Water Supply**

**Objective:** To provide water supply storage in a cost-efficient and environmentally responsible manner, in partnership with nonfederal water management plans, that is consistent with law and policy.

<sup>1</sup> NED benefits arising from recreation experiences are measured in terms of willingness to pay for each increment of supply or type of recreation opportunity. The unit day value method relies on expert or informed opinion and judgment to approximate the average willingness to pay of users of federal or federally assisted recreation resources. The unit day value is estimated at the park (recreation area) level by evaluating each park against a set of published criteria. By applying a carefully thought-out and adjusted unit day value to estimated use, an approximation is obtained that may be used as an estimate of project recreation benefit (i.e., NED benefits = Unit Day Value X Recreation Use in Visitor Days).



**Performance Indicator:** To assist in measuring progress toward this objective, the Corps measures the percentage of the acre-feet of water supply storage space under contract compared to the acre-feet of space available for water storage.

Table 24. Acre-Feet of Water Supply

	FY 2004	FY 2005
Acre-Feet Available (in millions of acre-feet)	9.856	9.761
Acre-Feet Under Contract (in millions of acre-feet)	9.108	9.356
Percent Under Contract	92.4	95.9

Note: FY 2006 data were not available at time of printing.

**Performance Indicator:** Another measure the Corps uses for water supply is cost recovery. This is measured as a percentage of costs available for recovery compared to costs recovered.

Table 25. Cost Recovery

	FY 2004	FY 2005
Costs Available for Recovery (in millions of dollars)	\$1,477.2	\$1,459.8
Costs Recovered (in millions of dollars)	\$1,064.0	\$1,096.1
Percent Recovered	72.0	75.0

Note: FY 2006 data were not available at time of printing.

### Goal 4: Reduce Vulnerabilities and Losses to the Nation and the Army from Natural and Man-Made Disasters, Including Terrorism

The purpose of this goal is to manage the risks associated with all types of hazards and to increase the responsiveness to disasters of the civil works emergency management program within the Corps' Office of Homeland Security in support of federal, state, and local emergency management efforts. Disaster preparedness and response capabilities are not limited to water-related disasters, but draw on the engineering skills and management capabilities of the Corps, encompassing a broad range of natural disasters and national emergencies. Emergency readiness contributes to national security.

**Objective:** To attain and maintain a high, consistent state of preparedness.

**Performance Indicators:** The two measures listed in Table 26 serve as indicators to assist Corps personnel to determine their progress in meeting the Corps' emergency management objective. The indicators are explained below.

- **Planning response team readiness.** The Corps has established designated Planning and Response Teams (PRT) that are organized to provide rapid emergency response for a specific mission area. This measure is calculated as a percentage of time during the fiscal year that PRTs are fully staffed, trained, and ready to deploy.
- **Project inspection performance.** The Corps performs inspections of flood control works operated and maintained by public sponsors to insure and assess their operations and maintenance condition. This measure is determined by the percentage of scheduled inspections completed during the fiscal year.

Table 26. Emergency Preparedness Measures

	FY 2004	FY 2005
Planning Response Team Readiness	93%	82%
Project Inspection Performance	90%	96%

Note: FY 2006 data were not available at time of printing.

**Performance Indicator:** The Corps performs repairs of flood control projects damaged by flood or storm under authority of P.L. 84-99. This measure is determined by the percentage of projects damaged during a fiscal year that are repaired prior to the next flood season.

Table 27. All-Hazards Response Measure

	FY 2004	FY 2005
Restoration Of Damaged Projects	92%	75%

Note: FY 2006 data were not available at time of printing.

**Objective:** To ensure effective and efficient long-term recovery operations.

Table 28. Long-Term Recovery Measure

	FY 2004	FY 2005
Inspected Projects With Satisfactory Condition Ratings	93%	94%

Note: FY 2006 data were not available at time of printing.

**Performance Indicator:** Under the Corps Rehabilitation and Inspection Program, inspected projects are given condition ratings that characterize the project maintenance condition. This measure is determined by the percentage of

the total projects inspected during the fiscal year that received a rating of at least minimally acceptable.

## Possible Future Effects of Existing Conditions

### The Marine Transportation System (MTS)

#### *Background*

The national vision for the MTS is for it to be a safe, secure and globally integrated network that, in harmony with the environment, ensures a free-flowing, seamless, and reliable movement of people and commerce along its waterways, sea lanes, and intermodal connections. In order to do that, the nation needs to invest in the maintenance and construction of adequate infrastructure. Today, approximately 20 percent of the gross domestic product of the United States is generated by foreign trade, and approximately 95 percent of that trade is moved by water. The value of the foreign tonnage is over \$900 billion and generates 16 million jobs. Current forecasts predict that maritime trade will double, or possibly triple in the next 20 years. The MTS moved approximately 2.5 billion tons of the 15 billion tons of the freight moved in, out, and within the United States in 2004. This system is comprised of 1,000 harbor channels; 25,000 miles of inland, intracoastal, and coastal waterways; and 240 lock chambers. Eleven of these locks are over 100 years old and 122 are over 50 years old.

#### *Effects of Aging Infrastructure*

As trade expands, our aging infrastructure is being increasingly strained. If our maritime transportation network is going to keep pace with the increasing demands placed on it, it will be necessary to enhance efficiencies and improve throughput in the near term while making significant future investments. Otherwise, any substantial disruption to the system will have devastating economic impact and irreversible repercussions in the global marketplace. For example, in 2002 there was a work slow-down along the West Coast; while this was a labor issue, it is estimated that this minor disruption in the flow of goods cost the U.S. economy as much as \$1 billion per day and the permanent loss of some cargoes to Canadian ports. The MTS' aging infrastructure resulted in the emergency closure of the McAlpine locks and dam on the inland waterways in 2004. The closure caused the stranding of more than 1,800 barges and the equivalent capacity of 80,000 trucks for more than 14 days.



## Analysis of Financial Statements and Stewardship Information

### Civil Works Fund Financial Results

#### Civil Works Balance Sheet

The Army Civil Works Fund balance sheet includes total assets that exceed \$43 billion. Two asset categories – Fund Balance with Treasury and General Property, Plant and Equipment – make up almost 81 percent of total assets, with values of \$8.1 billion and \$26.8 billion, respectively.

Liabilities primarily consist of \$0.7 billion in Environmental Liabilities and \$0.5 billion in Accounts Payable.

Fund Balance with Treasury increased by \$5.0 billion (159 percent) in FY 2006 due to additional funds in the flood control and coastal emergencies appropriations. The increased funding was due to the unprecedented hurricane season in the Gulf of Mexico during 2005. Primary hurricane relief efforts included debris clean-up and removal, and purchases of ice, water, and tarps for coverage of damaged roofs.

Environmental Liabilities increased \$0.2 billion (23 percent). The increase was due to recording the liability for feasibility study cost estimates in 4th Quarter, FY 2006, for Formerly Utilized Sites Remedial Action Program project sites. The feasibility costs were not included in the FY 2005 statements and were adjusted based on an audit recommendation in FY 2006.

Figure 17. Composition of General Fund Assets and Liabilities

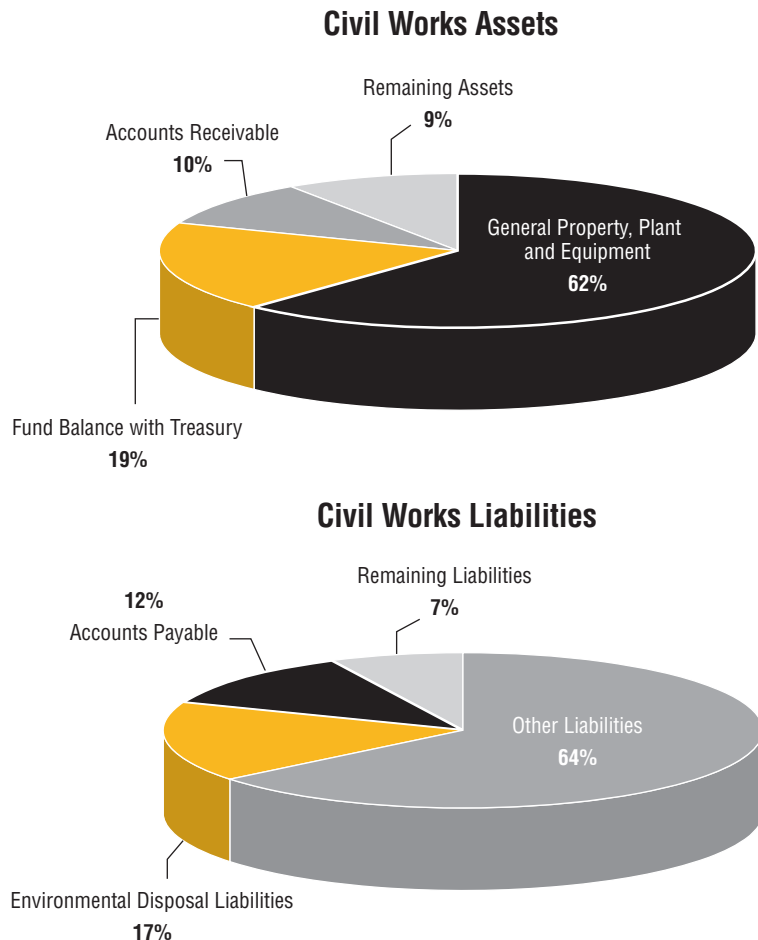


Figure 18. Select Civil Works Fund Assets and Liabilities

Civil Works Fund				
\$ in billions				
Asset Type	FY 2005	FY 2006	Change	Percentage of FY 2006 Assets
General Property, Plant and Equipment	\$26.8	\$26.8	\$0.0	62%
Fund Balance with Treasury	\$3.1	\$8.1	\$5.0	19%
Accounts Receivable	\$2.4	\$4.2	\$1.8	10%
Remaining Assets	\$3.2	\$4.1	\$0.9	9%
<b>Total Assets</b>	<b>\$35.5</b>	<b>\$43.2</b>	<b>\$7.7</b>	<b>100%</b>
Liability Type	FY 2005	FY 2006	Change	Percentage of FY 2006 Liabilities
Other Liabilities	\$2.6	\$2.7	\$0.1	65%
Environmental and Disposal Liabilities	\$0.5	\$0.7	\$0.2	16%
Accounts Payable	\$0.6	\$0.5	(\$0.1)	13%
Remaining Liabilities	0.0	0.3	\$0.3	6%
<b>Total Liabilities</b>	<b>\$3.7</b>	<b>\$4.2</b>	<b>\$0.5</b>	<b>100%</b>



## LIMITATIONS



**U.S. ARMY**

### LIMITATIONS OF THE FINANCIAL STATEMENTS

The financial statements have been prepared to report the financial position and results of operations for the entity, pursuant to the requirements of Title 31, United States Code, section 3515(b).

While the statements have been prepared from the books and records of the entity, in accordance with the formats prescribed by the Office of Management and Budget, the statements are in addition to the financial reports used to monitor and control budgetary resources which are prepared from the same books and records.

The statements should be read with the realization that they are for a component of the United States Government, a sovereign entity.

**CONSOLIDATED BALANCE SHEET**

As of September 30, 2006 and 2005 (\$ in Thousands)

	2006 Consolidated	2005 Consolidated
<b>ASSETS (Note 2)</b>		
Intragovernmental:		
Fund Balance with Treasury (Note 3)		
Entity	\$ 8,141,325	\$ 3,138,201
Non-Entity Seized Iraqi Cash	0	0
Non-Entity-Other	6,028	7,849
Investments (Note 4)	3,571,456	3,127,832
Accounts Receivable (Note 5)	2,407,555	613,904
Other Assets (Note 6)	0	0
Total Intragovernmental Assets	<u>\$ 14,126,364</u>	<u>\$ 6,887,786</u>
Cash and Other Monetary Assets (Note 7)	\$ 1,310	\$ 1,147
Accounts Receivable, Net (Note 5)	1,773,773	1,750,925
Loans Receivable (Note 8)	0	0
Inventory and Related Property, Net (Note 9)	121,340	117,384
General Property, Plant and Equipment, Net (Note 10)	26,821,962	26,780,102
Investments (Note 4)	0	0
Other Assets (Note 6)	440,839	0
<b>TOTAL ASSETS</b>	<u><u>\$ 43,285,588</u></u>	<u><u>\$ 35,537,344</u></u>
<b>LIABILITIES (Note 11)</b>		
Intragovernmental:		
Accounts Payable (Note 12)	\$ 93,841	\$ 87,230
Debt (Note 13)	13,924	14,600
Other Liabilities (Note 15 & 16)	1,987,573	1,956,895
Total Intragovernmental Liabilities	<u>\$ 2,095,338</u>	<u>\$ 2,058,725</u>
Accounts Payable (Note 12)	\$ 442,199	\$ 535,882
Military Retirement and Other Federal Employment Benefits (Note 17)	250,575	0
Environmental and Disposal Liabilities (Note 14)	653,315	529,617
Loan Guarantee Liability (Note 8)	0	0
Other Liabilities (Note 15 and Note 16)	753,399	600,880
<b>TOTAL LIABILITIES</b>	<u><u>\$ 4,194,826</u></u>	<u><u>\$ 3,725,104</u></u>
<b>NET POSITION</b>		
Unexpended Appropriations - Earmarked Funds (Note 23)	\$ 0	\$ 0
Unexpended Appropriations - Other Funds	7,443,696	1,005,843
Cumulative Results of Operations - Earmarked Funds	5,588,141	0
Cumulative Results of Operations - Other Funds	26,058,925	30,806,397
<b>TOTAL NET POSITION</b>	<u><u>\$ 39,090,762</u></u>	<u><u>\$ 31,812,240</u></u>
<b>TOTAL LIABILITIES AND NET POSITION</b>	<u><u>\$ 43,285,588</u></u>	<u><u>\$ 35,537,344</u></u>

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

Department of Defense - US Army Corps of Engineers

**CONSOLIDATED STATEMENT OF NET COST***As of September 30, 2006 and 2005 (\$ in Thousands)*

	2006 Consolidated	2005 Consolidated
<b>Program Costs</b>		
Gross Costs	\$ 11,196,356	\$ 10,261,283
(Less: Earned Revenue)	(5,104,928)	(2,581,577)
Net Program Costs	<u>\$ 6,091,428</u>	<u>\$ 7,679,706</u>
<b>Cost Not Assigned to Programs</b>	0	0
<b>(Less: Earned Revenue Not Attributable to Programs)</b>	0	0
<b>Net Cost of Operations</b>	<u>\$ 6,091,428</u>	<u>\$ 7,679,706</u>

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

**CONSOLIDATED STATEMENT OF NET POSITION**

As of September 30, 2006 and 2005 (\$ in Thousands)

	Earmarked Funds		All Other Funds	
<b>CUMULATIVE RESULTS OF OPERATIONS</b>				
<b>Beginning Balances</b>	\$	4,781,544	\$	26,024,852
<b>Prior Period Adjustments:</b>				
Changes in accounting principles (+/-)		0		0
Corrections of errors (+/-)		0		0
<b>Beginning balances, as adjusted</b>	\$	4,781,544	\$	26,024,852
<b>Budgetary Financing Sources:</b>		0		0
Appropriations received		0		0
Appropriations transferred-in/out (+/-)		0		0
Other adjustments (rescissions, etc.) (+/-)		0		0
Appropriations used		0		4,516,312
Nonexchange revenue		1,841,682		0
Donations and forfeitures of cash and cash equivalents		0		0
Transfers-in/out without reimbursement (+/-)		8,362		284,043
Other budgetary financing sources (+/-)		0		0
<b>Other Financing Sources:</b>				
Donations and forfeitures of property		0		19,888
Transfers-in/out without reimbursement (+/-)		(135,271)		135,457
Imputed financing from costs absorbed by others		0		261,624
Other (+/-)		0		0
<b>Total Financing Sources</b>	\$	1,714,773	\$	5,217,324
<b>Net Cost of Operations (+/-)</b>		1,115,652		4,975,776
<b>Net Change</b>	\$	599,121	\$	241,548
<b>Ending Balances</b>	\$	5,380,665	\$	26,266,400
<b>UNEXPENDED APPROPRIATIONS</b>				
<b>Beginning Balances</b>	\$	0	\$	1,005,843
<b>Prior Period Adjustments:</b>				
Changes in accounting principles (+/-)		0		0
Corrections of errors (+/-)		0		0
<b>Beginning balances, as adjusted</b>	\$	0	\$	1,005,843
<b>Budgetary Financing Sources:</b>				
Appropriations received		0		10,980,882
Appropriations transferred-in/out (+/-)		0		27,114
Other adjustments (rescissions, etc) (+/-)		0		(53,831)
Appropriations used		0		(4,516,312)
Nonexchange revenue		0		0
Donations and forfeitures of cash and cash equivalents		0		0
Transfers-in/out without reimbursement (+/-)		0		0
Other budgetary financing sources (+/-)		0		0
<b>Other Financing Sources:</b>				
Donations and forfeitures of property		0		0
Transfers-in/out without reimbursement (+/-)		0		0
Imputed financing from costs absorbed by others		0		0
Other (+/-)		0		0
<b>Total Financing Sources</b>	\$	0	\$	6,437,853
<b>Net Cost of Operations (+/-)</b>		0		0
<b>Net Change</b>	\$	0	\$	6,437,853
<b>Ending Balances</b>	\$	0	\$	7,443,696

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



Department of Defense - US Army Corps of Engineers

**CONSOLIDATED STATEMENT OF NET POSITION**

As of September 30, 2006 and 2005 (\$ in Thousands)

	Eliminations	2006 Consolidated	2005 Consolidated
<b>CUMULATIVE RESULTS OF OPERATIONS</b>			
<b>Beginning Balances</b>	\$ 0	\$ 30,806,396	\$ 32,276,299
<b>Prior Period Adjustments:</b>			
Changes in accounting principles (+/-)	0	0	0
Corrections of errors (+/-)	0	0	0
<b>Beginning balances, as adjusted</b>	\$ 0	\$ 30,806,396	\$ 32,276,299
<b>Budgetary Financing Sources:</b>	0	0	0
Appropriations received	0	0	0
Appropriations transferred-in/out (+/-)	0	0	0
Other adjustments (rescissions, etc.) (+/-)	0	0	0
Appropriations used	0	4,516,312	4,009,707
Nonexchange revenue	0	1,841,682	1,632,662
Donations and forfeitures of cash and cash equivalents	0	0	0
Transfers-in/out without reimbursement (+/-)	0	292,405	326,390
Other budgetary financing sources (+/-)	0	0	274
<b>Other Financing Sources:</b>			
Donations and forfeitures of property	0	19,888	1,490
Transfers-in/out without reimbursement (+/-)	0	186	(3,048)
Imputed financing from costs absorbed by others	0	261,624	241,581
Other (+/-)	0	0	748
<b>Total Financing Sources</b>	\$ 0	\$ 6,932,097	\$ 6,209,804
<b>Net Cost of Operations (+/-)</b>	0	6,091,428	7,679,706
<b>Net Change</b>	\$ 0	\$ 840,669	\$ (1,469,902)
<b>Ending Balances</b>	\$ 0	\$ 31,647,065	\$ 30,806,397
<b>UNEXPENDED APPROPRIATIONS</b>			
<b>Beginning Balances</b>	\$ 0	\$ 1,005,843	\$ 396,362
<b>Prior Period Adjustments:</b>			
Changes in accounting principles (+/-)	0	0	0
Corrections of errors (+/-)	0	0	0
<b>Beginning balances, as adjusted</b>	\$ 0	\$ 1,005,843	\$ 396,362
<b>Budgetary Financing Sources:</b>			
Appropriations received	0	10,980,882	4,629,502
Appropriations transferred-in/out (+/-)	0	27,114	27,602
Other adjustments (rescissions, etc.) (+/-)	0	(53,831)	(37,916)
Appropriations used	0	(4,516,312)	(4,009,707)
Nonexchange revenue	0	0	0
Donations and forfeitures of cash and cash equivalents	0	0	0
Transfers-in/out without reimbursement (+/-)	0	0	0
Other budgetary financing sources (+/-)	0	0	0
<b>Other Financing Sources:</b>			
Donations and forfeitures of property	0	0	0
Transfers-in/out without reimbursement (+/-)	0	0	0
Imputed financing from costs absorbed by others	0	0	0
Other (+/-)	0	0	0
<b>Total Financing Sources</b>	\$ 0	\$ 6,437,853	\$ 609,481
<b>Net Cost of Operations (+/-)</b>	0	0	0
<b>Net Change</b>	\$ 0	\$ 6,437,853	\$ 609,481
<b>Ending Balances</b>	\$ 0	\$ 7,443,696	\$ 1,005,843

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

**COMBINED STATEMENT OF BUDGETARY RESOURCES**

As of September 30, 2006 and 2005 (\$ in Thousands)

	Budgetary Financing Accounts		Non Budgetary Financing Accounts	
	2006 Combined	2005 Combined	2006 Combined	2005 Combined
<b>BUDGETARY RESOURCES</b>				
Unobligated balance, brought forward, October 1	\$ 5,003,186	\$ 1,693,278	\$ 0	\$ 0
Recoveries of prior year unpaid obligations	0	0	0	0
Budget authority				
Appropriation	12,439,718	5,987,913	0	0
Borrowing authority	0	0	0	0
Contract authority	0	0	0	0
Spending authority from offsetting collections				
Earned				
Collected	9,407,099	6,471,705	0	0
Change in receivables from Federal sources	1,690,685	11,130	0	0
Change in unfilled customer orders				
Advance received	22,685	(34,324)	0	0
Without advance from Federal sources	(719,532)	3,306,341	0	0
Anticipated for rest of year, without advances	0	0	0	0
Previously unavailable	0	0	0	0
Expenditure transfers from trust funds	0	0	0	0
Subtotal	22,840,655	15,742,765	0	0
Nonexpenditure transfers, net, anticipated and actual	\$ (8,068)	\$ 257,392	\$ 0	\$ 0
Temporarily not available pursuant to Public Law	(10,000)	(10,000)	0	0
Permanently not available	(54,490)	(38,390)	0	0
<b>Total Budgetary Resources</b>	<b>\$ 27,771,283</b>	<b>\$ 17,645,045</b>	<b>\$ 0</b>	<b>\$ 0</b>
<b>Status of Budgetary Resources:</b>				
Obligations incurred:				
Direct	\$ 6,902,331	\$ 5,739,464	\$ 0	\$ 0
Reimbursable	11,500,680	6,902,397	0	0
Subtotal	\$ 18,403,011	\$ 12,641,861	\$ 0	\$ 0
Unobligated balance:				
Apportioned	8,621,365	4,421,128	0	0
Exempt from apportionment	746,850	581,999	0	0
Subtotal	9,368,215	5,003,127	0	0
Unobligated balance not available	57	57	0	0
<b>Total status of budgetary resources</b>	<b>\$ 27,771,283</b>	<b>\$ 17,645,045</b>	<b>\$ 0</b>	<b>\$ 0</b>
<b>Change in Obligated Balance:</b>				
Obligated balance, net				
Unpaid obligations, brought forward, October 1	3,945,373	3,171,189	0	0
Less: Uncollected customer payments from Federal sources, brought forward, October 1	\$ (5,449,985)	\$ (2,132,513)	\$ 0	\$ 0
Total unpaid obligated balance	(1,504,612)	1,038,676	0	0
Obligations incurred net (+/-)	\$ 18,403,011	\$ 12,641,861	\$ 0	\$ 0
Less: Gross outlays	(16,870,276)	(11,867,676)	0	0
Obligated balance transferred, net				
Actual transfers, unpaid obligations (+/-)	0	0	0	0
Actual transfers, uncollected customer payments from Federal sources (+/-)	0	0	0	0
Total Unpaid obligated balance transferred, net	0	0	0	0
Less: Recoveries of prior year unpaid obligations, actual	0	0	0	0
Change in uncollected customer payments from Federal sources (+/-)	(971,153)	(3,317,472)	0	0
Obligated balance, net, end of period				
Unpaid obligations	5,478,111	3,945,373	0	0
Less: Uncollected customer payments (+/-) from Federal sources (-)	(6,421,138)	(5,449,985)	0	0
Total, unpaid obligated balance, net, end of period	(943,027)	(1,504,612)	0	0
<b>Net Outlays</b>				
<b>Net Outlays:</b>				
Gross outlays	16,870,276	11,867,676	0	0
Less: Offsetting collections	(9,429,787)	(6,437,381)	0	0
Less: Distributed Offsetting receipts	(1,906,618)	(1,744,668)	0	0
<b>Net Outlays</b>	<b>\$ 5,533,871</b>	<b>\$ 3,685,627</b>	<b>\$ 0</b>	<b>\$ 0</b>

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

Department of Defense - US Army Corps of Engineers

**CONSOLIDATED STATEMENT OF FINANCING**

As of September 30, 2006 and 2005 (\$ in Thousands)

	2006 Consolidated	2005 Consolidated
<b>Resources Used to Finance Activities:</b>		
Budgetary Resources Obligated		
Obligations incurred	\$ 18,403,011	\$ 12,641,861
Less: Spending authority from offsetting collections and recoveries (-)	(10,400,937)	(9,754,852)
Obligations net of offsetting collections and recoveries	\$ 8,002,074	\$ 2,887,009
Less: Offsetting receipts (-)	(1,906,618)	(1,744,668)
Net obligations	\$ 6,095,456	\$ 1,142,341
Other Resources		
Donations and forfeitures of property	19,888	1,490
Transfers in/out without reimbursement (+/-)	186	(3,048)
Imputed financing from costs absorbed by others	261,624	241,581
Other (+/-)	0	748
Net other resources used to finance activities	\$ 281,698	\$ 240,771
<b>Total resources used to finance activities</b>	<b>\$ 6,377,154</b>	<b>\$ 1,383,112</b>
<b>Resources Used to Finance Items not Part of the Net Cost of Operations</b>		
Change in budgetary resources obligated for goods, services and benefits ordered but not yet provided		
Undelivered Orders (-)	\$ (1,566,815)	\$ (839,097)
Unfilled Customer Orders	(696,847)	3,272,017
Resources that fund expenses recognized in prior periods	(23,032)	(25,840)
Budgetary offsetting collections and receipts that do not affect net cost of operations	1,906,618	1,744,668
Resources that finance the acquisition of assets	(7,078)	(13,136)
Other resources or adjustments to net obligated resources that do not affect net cost of operations		
Less: Trust or Special Fund Receipts Related to exchange in the Entity's Budget (-)	(10,000)	(10,000)
Other (+/-)	(20,075)	1,560
<b>Total resources used to finance items not part of the net cost of operations</b>	<b>\$ (417,229)</b>	<b>\$ 4,130,172</b>
<b>Total resources used to finance the net cost of operations</b>	<b>\$ 5,959,925</b>	<b>\$ 5,513,284</b>
<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		
Increase in annual leave liability	\$ 0	\$ 0
Increase in environmental and disposal liability	123,698	0
Upward/Downward reestimates of credit subsidy expense (+/-)	0	0
Increase in exchange revenue receivable from the the public (-)	(16,838)	(34)
Other (+/-)	326,995	540,581
Total components of Net Cost of Operations that will require or generate resources in future periods	\$ 433,855	\$ 540,547
Components not Requiring or Generating Resources:		
Depreciation and amortization	525,076	1,195,609
Revaluation of assets or liabilities (+/-)	(269,050)	1,046,654
Other (+/-)		
Trust Fund Exchange Revenue	0	0
Cost of Goods Sold	743	2,764
Operating Material & Supplies Used	0	0
Other	(559,121)	(619,152)
Total components of Net Cost of Operations that will not require or generate resources	(302,352)	1,625,875
<b>Total components of net cost of operations that will not require or generate resources in the current period</b>	<b>\$ 131,503</b>	<b>\$ 2,166,422</b>
<b>Net Cost of Operations</b>	<b>\$ 6,091,428</b>	<b>\$ 7,679,706</b>

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



## Note 1. Significant Accounting Policies

### 1.A. Basis of Presentation

These financial statements have been prepared to report the financial position and results of operations of the US Army Corps of Engineers (USACE) Civil Works, as required by the “Chief Financial Officers Act of 1990,” expanded by the “Government Management Reform Act of 1994,” and other appropriate legislation. The financial statements have been prepared from the books and records of USACE in accordance with the “Department of Defense Financial Management Regulation (DoDFMR),” the Office of Management and Budget (OMB) Circular A-136, Financial Reporting Requirements, and to the extent possible Generally Accepted Accounting Principles (GAAP). The accompanying financial statements account for all Civil Works resources for which USACE is responsible. The USACE Civil Works does not have classified assets, programs, or operations.

Based on the February 2006 Office of the Secretary of Defense, Comptroller approval of USACE readiness for a fiscal year (FY) 2006 audit, USACE believes all past material weaknesses have been corrected.

The USACE’s financial statements are prepared from the consolidation of general ledger financial data reported from the Corps of Engineers Financial System (CEFMS) to the Corps of Engineers Enterprise Management Information System (CEEMIS).

### 1.B. Mission of the Reporting Entity

The primary missions of USACE include maintaining navigation channels, reducing flooding, assisting during natural disasters and other emergencies, and making waterways passable. The financial statements are presented on the accrual basis of accounting as required by the Statement of Federal Financial Accounting Standards (SFFAS).

### 1.C. Appropriations and Funds

The USACE Civil Works Program receives Federal funding through annual Energy and Water Development Appropriations Acts. Program funding also comes from nonfederal project sponsors who share in project costs according to formulas established by project authorization acts. A third source of funding comes through the Supports for Others Program, which is conducted under reimbursable agreements with Federal agencies.

The USACE Civil Works Program receives its appropriations and funds as general, revolving funds, trust, special, and deposit funds. The USACE uses these appropriations and funds to execute their missions and report on resource usage.

General funds are used for financial transactions funded by congressional appropriations, including personnel, operations and maintenance, research and development, procurement, and construction accounts.

Revolving funds receive their initial funding through an appropriation or a transfer of resources from existing appropriations or funds and use those capital resources to finance the initial startup. The revolving fund provides goods and services on a reimbursable basis. Reimbursable receipts fund ongoing operations and generally are available in their entirety for use without further congressional action.

Trust funds contain receipts and expenditures 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 fund accounts are used to record government receipts reserved for a specific purpose.

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

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

In 1997, USACE received borrowing authority from the Department of the Treasury for the three years 1997 through 1999 to finance capital improvements to the Washington Aqueduct. Appropriation 96X3128 was established to record financial transactions for these capital improvements.

The asset accounts used to prepare the principal financial statements are categorized as entity/nonentity. 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. Nonentity 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**

96X3112 Flood Control, Mississippi River and Tributaries  
96X3121 Investigations  
96 3121 Investigations (fiscal year)  
96X3122 Construction, General  
96X3123 Operation and Maintenance, General  
96X3124 General Expenses  
96X3125 Flood Control and Coastal Emergencies  
96X3126 Regulatory Program  
96X3128 Washington Aqueduct Capital Improvements  
96 3129 Payment to the South Dakota Terrestrial Wildlife Habitat Restoration Trust Fund (fiscal year)  
96X3130 Formerly Utilized Sites Remedial Action Program  
96 3132 Office of Assistant Secretary of the Army, Civil Works (fiscal year)  
96X6094 Advances from the District of Columbia

**Revolving Funds**

96X4902 Revolving Fund

**Special Funds**

96X5007 Special Recreation Use Fees  
96X5066 Hydraulic Mining in California, Debris  
96X5090 Payments to States, Flood Control Act of 1954  
96X5125 Maintenance and Operation of Dams and Other Improvements of Navigable Waters  
96X5493 Fund for Non-Federal Use of Disposal Facilities  
96 5493 Fund for Non-Federal Use of Disposal Facilities (fiscal year)

**Trust Funds**

96X8217 South Dakota Terrestrial Wildlife Habitat Restoration Trust Fund  
96X8333 Coastal Wetlands Restoration Trust Fund  
96 20X8861 Inland Waterways Trust Fund  
96X8862 Rivers and Harbors Contributed and Advance Funds  
96 20X8863 Harbor Maintenance Trust Fund

**Transfer Funds**

96 12X1105 State and Private Forestry, Forest Service  
96 14X1039 Construction, National Park Service  
96 14X5035 Land Acquisition and State Assistance, National Park Service  
96 14X5573 Permit Processing Fund, Bureau of Land Management  
96 46X0200 Appalachian Regional Development Programs, Appalachian Regional Commission  
96 69X8083 Federal - Aid Highways (Liquidation of Contract Authorization), Federal Highways Administration  
96 89X4045 Bonneville Power Administration Fund, Power Marketing Administration, Department of Energy

**Nonentity:****Deposit Funds**

96X6500 Advances Without Orders from Non-Federal Sources  
96X6501 Small Escrow Amounts

**Clearing Accounts**

96F3875 Budget Clearing Account (suspense)  
96F3880 Unavailable Check Cancellations and Overpayments (suspense)  
96F3885 Undistributed Intragovernmental Payments

**Receipt Accounts**

96 0891 Miscellaneous Fees for Regulatory and Judicial Services, Not Otherwise Classified  
96 1060 Forfeitures of Unclaimed Money and Property  
96 1099 Fines, Penalties, and Forfeitures, Not Otherwise Classified  
96 1299 Gifts to the United States, Not Otherwise Classified  
96 1435 General Fund Proprietary Interest, Not Otherwise Classified  
96 3220 General Fund Proprietary Receipts, Not Otherwise Classified, All Other

96 5005	Land and Water Conservation Fund
96 5007	Special Recreation Use Fees
96 5066	Hydraulic Mining in California
96 5090	Receipts from Leases of Lands Acquired for Flood Control, Navigation, and Allied Purposes
96 5125	Licenses under Federal Power Act, Improvements of Navigable Waters, Maintenance and Operation of Dams, etc., (50%)
96 5493	User Fees, Fund for Non-Federal Use of Disposal Facilities

**Obsolete Accounts:**

96 13X1450	96 89X0224	96X6145	96F3886	96 1499
96 14X2301	96 20X8145	96X6275	96 0199	96 2413
96 19 00 1082	96X3930	96X6302	96 0869	96 2814
96 47X4542	96X6050	96X6999	96 1030	96 3102
96 67X0204	96X6075	96X8868	96 1040	96 3124
96 72 00/01 1021	96X6134	96F3879	96 1210	

**1.D. Basis of Accounting**

The USACE's financial transactions are recorded on an accrual accounting basis as required by Generally Accepted Accounting Principles (GAAP). Under the accrual method, revenues are recognized when earned and expenses are recognized when a liability is incurred without regard to receipt or payment of cash. Budgetary accounting is accomplished through unique general ledger accounts to facilitate compliance with legal and internal control requirements associated with the use of Federal funds in accordance with the Department of the Treasury Financial Manual.

CEFMS is used at all divisions, districts, centers, laboratories, and field offices. CEFMS is a fully integrated, automated, and comprehensive financial management system that simplifies the management of all aspects of USACE's business. The general ledger chart of accounts in CEFMS is compliant with the US Government Standard General Ledger (USSGL).

In addition, USACE identifies program costs based upon the major appropriation groups provided by Congress. Current processes and systems capture and report accumulated costs for major programs based upon the performance measures as required by the Government and Performance and Results Act. CEFMS includes a cost reporting

methodology that balances the need for cost information required by the 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**

The USACE receives congressional appropriations as financing sources for general funds on either an annual or multi-year basis. When authorized by legislation, these appropriations are supplemented by revenues generated by sales of goods or services. The USACE recognizes revenue as a result of costs incurred or services provided to other Federal agencies and the public. Full cost pricing is USACE's standard policy for services provided as required by OMB Circular A-25. The USACE recognizes revenue when earned.

The USACE does not include nonmonetary support provided by US allies for common defense and mutual security in amounts reported in the Statement of Net Cost and the Statement of Financing. The US has cost sharing agreements with other countries. Examples include countries where there is a mutual or reciprocal defense agreement, where US troops are stationed, or where the US fleet is in a port.

**1.F. Recognition of Expenses**

For financial reporting purposes, DoD policy requires the recognition of operating expenses in the period incurred. The USACE's financial system collects and records financial information on the full accrual accounting basis. Expenses, such as civilian earned leave, are financed in the period when earned. An exception is sick leave, which is expensed as taken. Accrual adjustments are made for environmental liabilities. The USACE's expenditures for capital and other long-term assets are recognized as operating expenses based on depreciation. In the case of Operating Materials and Supplies (OM&S), operating expenses are recognized when consumed.

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

## **1.G. Accounting for Intragovernmental Activities**

Preparation of reliable financial statements requires the elimination of transactions occurring among entities within the DoD or between two or more federal agencies. The USACE is responsible for eliminating transactions between components and activities.

The Department of the Treasury, Financial Management Service (FMS), is responsible for eliminating transactions between DoD and other federal agencies. The Treasury Financial Manual, Part 2 – Chapter 4700, “Agency Reporting Requirements for the Financial Report of the United States Government” and the Treasury’s “Federal Intragovernmental Transactions Accounting Policy Guide,” provide guidance for reporting and reconciling intragovernmental balances. While USACE is unable to fully reconcile intragovernmental transactions with all federal partners, USACE is able to reconcile balances pertaining 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. The USACE implemented policies and procedures related to reconciling intragovernmental assets, liabilities, revenues, and expenses for nonfiduciary transactions. The USACE is unable to reconcile with entities whose financial systems are not designed to capture pertinent information to fully reconcile intragovernmental transactions. The USACE’s proportionate share of public debt and related expenses of the federal government are not included. The federal government does not apportion debt and its related costs to federal agencies. The USACE’s financial statements, therefore, do not report any portion of the public debt or interest thereon, nor do the statements report the source of public financing whether from issuance of debt or tax revenues.

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

## **1.H. Transactions with Foreign Governments and International Organizations**

The USACE does have transactions with foreign governments and/or international organizations.

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

The USACE’s monetary financial resources are maintained in US Treasury accounts. The disbursing offices of the Defense Finance and Accounting Service (DFAS), the Military Services, the USACE Finance Center (UFC) and the Department of State’s financial service centers process the majority of USACE’s cash collections, disbursements, and adjustments worldwide. Each disbursing station prepares monthly reports that provide information to the Department of the Treasury on check issues, electronic fund transfers, interagency transfers, and deposits.

In addition, DFAS sites and UFC submit reports to the Department of the Treasury, by appropriation, on interagency transfers, collections received, and disbursements issued. The Department of the Treasury records this information to the applicable Funds Balance with Treasury (FBWT) account. Differences between USACE’s recorded balance in the FBWT accounts and Department of the Treasury’s FBWT accounts sometimes result and are subsequently reconciled.

### **1.J. Foreign Currency**

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

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

The USACE conducts operations overseas. Foreign currency fluctuations require adjustment to the original obligation amount at the time of payment. The USACE does not separately identify currency fluctuations.



### **1.K. Accounts Receivable**

As presented in the Balance Sheet, accounts receivable includes accounts, claims, and refunds receivable from other federal entities or from the public. Allowances for uncollectible accounts due from the public are based upon analysis of collection experience by fund type. The USACE 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 (per Code of Federal Regulations 4 CFR 101).

The USACE bases the estimate of uncollectible accounts receivable from the public on the cumulative balance of delinquent public receivables aged in accordance with current USACE policy. The calculation and financial transaction update are performed automatically in CEFMS.

### **1.L. Direct Loans and Loan Guarantees**

The USACE does not operate a direct loan and/or loan guarantee program.

### **1.M. Inventories and Related Property**

The USACE's inventories are reported at approximate historical cost based on a moving weighted average that is based on actual cost divided by quantity. A perpetual record of inventory is maintained in CEFMS to allow for recomputation of the average unit cost as new receipts are recorded. CEFMS maintains historical cost data necessary to comply with SFFAS No. 3, "Accounting for Inventory and Related Property." Additionally, CEFMS produces financial transactions using the USSGL, as required by the Federal Financial Management Improvement Act of 1996 (P.L. 104-208).

Related property includes operating materials and supplies (OM&S). The OM&S are valued at net realizable value. For the most part, USACE is using the consumption method of accounting for OM&S, as defined in the SFFAS No. 3, as material that has not been issued to the end user. Once OM&S is issued, the material and/or supplies are expensed.

Work in process (WIP) balances include costs related to the production or servicing of items, including direct material, direct labor, applied overhead and other direct costs. WIP also includes the value of finished products or completed services pending the submission of bills to the customer. The WIP designation may also be used to accumulate the amount paid to a contractor under cost reimbursable contracts, including amounts withheld from payment to ensure performance, and amounts paid to other government plants for accrued costs of end items of material ordered but not delivered.

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

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

Amounts reported reflect the value of investments in the South Dakota Terrestrial Wildlife Habitat Restoration, Inland Waterways, and Harbor Maintenance trust fund accounts, which are managed by the Department of the Treasury.

### **1.O. General Property, Plant and Equipment**

The USACE Civil Works General Property, Plant, and Equipment (PP&E) is capitalized at historical acquisition cost plus capitalized improvements when an asset has a useful life of two or more years and the acquisition cost exceeds \$25.0 thousand. One exception is all buildings and structures related to hydropower projects are capitalized regardless of cost. During FY 2003, USACE increased its buildings and structures capitalization threshold from \$0 to \$25.0 thousand for all Civil Works appropriations with the exception of revolving fund and hydropower related assets. All Civil Works buildings and structures capitalized under \$25.0 thousand (excluding revolving fund and hydropower assets) were expensed in FY 2003 and removed from CEFMS. Beginning in FY 2004, all Civil Works buildings and structures under \$25.0 thousand are expensed except for hydropower assets.

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

The 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, USACE reports only government property in the possession of contractors that is maintained in USACE property systems. The DoD has issued property accountability and reporting requirements that require USACE Components to maintain, in their property systems, information on all property furnished to contractors. This action and other DoD proposed actions are structured to capture and report the information necessary for compliance with Federal accounting standards.

## **1.P. Advances and Prepayments**

The USACE records payments in advance of the receipt of goods and services as advances or prepayments and reports them as assets on the Balance Sheet. The USACE recognizes advances and prepayments as expenses when it receives the related goods and services.

## **1.Q. Leases**

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

## **1.R. Other Assets**

The USACE conducts business with commercial contractors under two primary types of contracts: fixed price and cost reimbursable. To alleviate the potential financial burden on the contractor that long-term contracts can cause, USACE provides financing payments. One type of financing payment that USACE makes for real property is based upon a percentage of completion. In accordance with the SFFAS No. 1, "Accounting for Selected Assets and Liabilities," such payments are treated as construction in process and are reported on the General PP&E line on the Balance Sheet and in the related note.

## **1.S. Contingencies and Other Liabilities**

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

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

Other liabilities arise as a result of anticipated disposal costs for USACE's assets. This type of liability has two components: nonenvironmental and environmental. Consistent with SFFAS No.6, "Accounting for Property, Plant, and Equipment," recognition of an anticipated environmental disposal liability begins when the asset is placed in service.

## **1.T. Accrued Leave**

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

## **1.U. Net Position**

Net Position consists of unexpended appropriations and cumulative results of operations. Unexpended appropriations represent the amounts of authority that are unobligated and have not been rescinded or withdrawn. Unexpended appropriations also represent amounts obligated for which legal liabilities for payments have not been incurred.

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

## **1.V. Treaties for Use of Foreign Bases**

The USACE Civil Works does not have treaties for use of foreign bases.

## 1.W. Comparative Data

Financial statement fluctuations greater than two percent of total assets on the Balance Sheet or ten percent from the prior period presented are explained within the notes to the financial statements.

## 1.X. Unexpended Obligations

The USACE 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 Department of the Treasury. These amounts should agree with the undistributed amounts reported on the departmental accounting reports. In-transit payments are those payments that have been made to other agencies or entities that have not been recorded in their accounting records. These payments are applied to the entities' outstanding accounts payable balance. In-transit collections are those collections from other agencies or entities that have not been recorded in the accounting records. These collections are applied to the entities' accounts receivable balance.

The DoD policy is to allocate supported undistributed disbursements and collections between federal and nonfederal categories based on the percentage of 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 USACE does not follow this procedure. All undistributed disbursements and collections for USACE are unrecorded Intragovernmental Payment and Collection (IPAC) transactions. These transactions are all federal. The USACE Civil Works does not have in-transit payments or collections.

## Note 2. Nonentity Assets

As of September 30	2006	2005
<i>(Amounts in thousands)</i>		
1. Intragovernmental Assets		
A. Fund Balance with Treasury	\$ 6,028	\$ 7,849
B. Accounts Receivable	0	0
C. Total Intragovernmental Assets	\$ 6,028	\$ 7,849
2. Nonfederal Assets		
A. Cash and Other Monetary Assets	\$ 1,310	\$ 1,147
B. Accounts Receivable	1,751,549	1,722,336
C. Other Assets	0	0
D. Total Nonfederal Assets	\$ 1,752,859	\$ 1,723,483
3. Total Nonentity Assets	\$ 1,758,887	\$ 1,731,332
4. Total Entity Assets	\$ 41,526,701	\$ 33,806,012
5. Total Assets	\$ 43,285,588	\$ 35,537,344

### Other Information

Asset accounts are categorized either as entity or nonentity. Entity accounts consist of resources that the agency has authority to use, or when management is legally obligated to use funds to meet entity obligations. Nonentity Assets are assets that are held by an entity, but are not available for use in the operations of the entity.

Intragovernmental nonentity fund balance with treasury consists of amounts collected into deposit and suspense accounts.

Cash and Other Monetary Assets is comprised of \$4.4 thousand in change funds for recreation cashiers, \$492.8 thousand in disbursing officer's cash, and \$812.8 thousand in foreign currency.

Nonentity nonfederal accounts receivable represents all current and noncurrent receivables due from nonfederal sources. This includes \$858.9 million in long-term receivables due from state and local municipalities for water storage contracts; \$31.1 million in current receivables due from state and local municipalities for water storage; \$863.8 million in accrued interest receivable; \$452.1 thousand in penalties, fines, and administrative fees receivable; \$1.2 million in long-term receivables for hydraulic mining; and \$1.5 million for other miscellaneous receivables. An additional \$671.5 thousand represents the amount due from the leasing of land acquired for flood control purposes. Nonentity accounts receivables are recorded in unavailable receipt accounts and funds will be returned to the Department of the Treasury when collected. The allowance for doubtful accounts totals \$6.1 million for nonentity nonfederal accounts receivables.

### Note 3. Fund Balance with Treasury

As of September 30 <i>(Amounts in thousands)</i>	2006	2005
1. Fund Balances		
A. Appropriated Funds	\$ 6,423,985	\$ 1,600,628
B. Revolving Funds	1,090,769	965,552
C. Trust Funds	93,727	86,885
D. Special Funds	5,287	1,920
E. Other Fund Types	533,585	491,065
F. Total Fund Balances	<u>\$ 8,147,353</u>	<u>\$ 3,146,050</u>
2. Fund Balances Per Treasury Versus Agency		
A. Fund Balance per Treasury	\$ 8,181,330	\$ 3,180,160
B. Fund Balance per USACE	<u>8,147,353</u>	<u>3,146,050</u>
3. Reconciling Amount	<u>\$ 33,977</u>	<u>\$ 34,110</u>

#### Fluctuations

Total Fund Balances increased by \$5.0 billion (159%). The US Army Corps of Engineers (USACE) Civil Works Program receives federal funding through the annual Energy and Water Development Appropriations Act. The USACE received additional funding of \$2.0 billion during 2nd Quarter, FY 2006 and \$3.0 billion during 3rd Quarter, FY 2006, for Flood Control and Coastal Emergencies due to the unprecedented hurricane season in the Gulf of Mexico during 2005. Additional funds were for hurricane relief efforts to include debris clean-up and removal, and purchases of ice, water and tarps for coverage of damaged roofs.

#### Reconciling Amount

The Reconciling Amount for Fund Balance per USACE does not include receipt accounts. The USACE closed receipt accounts according to the Treasury Financial Management Transmittal Letter, but they were included on the Financial Management Service Receipt Account Trial Balance at September 30, 2006. Fund Balance per the USACE includes cash reported by the Department of the Treasury for Inland Waterways and Harbor Maintenance trust funds, for which USACE is identified as the lead agency for reporting. Fund Balance per USACE does not include cancelled appropriations.

#### Other Information

Appropriated Funds includes net disbursements for undistributed Intragovernmental Payment and Collection (IPAC) transactions. These were distributed to the appropriate funds during October 2006.

Other Fund Types (nonentity) consist of deposit accounts which are not available to finance USACE activities. Other Fund Types (entity) consists of borrowing authority, contributed funds and the suspense account established to finance Washington Aqueduct operations.

**Status of Fund Balance with Treasury**

As of September 30	2006		2005	
<i>(Amounts in thousands)</i>				
1. Unobligated Balance				
A. Available	\$	8,970,843	\$	5,003,319
B. Unavailable		3,557,277		58
2. Obligated Balance not yet Disbursed	\$	5,478,110	\$	6,622,332
3. Nonbudgetary FBWT	\$	54,953	\$	(3,734)
4. NonFBWT Budgetary Accounts	\$	(9,913,830)	\$	(8,475,925)
5. Total	\$	8,147,353	\$	3,146,050

**Fluctuations**

Total Status of Fund Balance with Treasury increased \$5.0 billion (159%).

Unobligated Balance Available increased from receipt of additional funding of \$2.0 billion during 2nd Quarter, FY 2006 and \$3.0 billion during 3rd Quarter, FY 2006, for the Flood Control and Coastal Emergencies appropriation due to the unprecedented hurricane season in the Gulf of Mexico during 2005. The additional funds were for hurricane relief efforts to include debris clean-up and removal, and purchases of ice, water and tarps for coverage of damaged roofs. In addition, the Unobligated Balance Available decreased \$1.3 billion beginning in 1st Quarter, FY 2006 and continuing through 4th Quarter, FY 2006. This was due to processing of obligations against reimbursable orders from Federal Emergency Management Agency.

In FY 2005, Receipts Unavailable for Obligation Upon Collection and Receipts and Appropriations Temporarily Precluded from Obligation were included in Obligated Balance not yet Disbursed. A footnote mapping correction was made in 2nd Quarter, FY 2006 to report these accounts as Unobligated Balance Unavailable. This resulted in the increase of \$3.6 billion from FY 2005 to FY 2006. This mapping occurred in 2nd Quarter, FY 2006.

**Definitions**

The Status of Fund Balance with Treasury consists of unobligated and obligated balances. These balances reflect the budgetary authority remaining for disbursements against current or future obligations. In addition, the Status of Fund Balance with Treasury includes various accounts that affect either budgetary reporting or the Fund Balance with Treasury (FBWT), but not both.

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

Obligated Balance not yet Disbursed represents funds that have been obligated for goods that have not been received or services that have not been performed.

Nonbudgetary FBWT includes entity and nonentity FBWT accounts which do not have budgetary authority, such as unavailable receipt accounts or clearing accounts.

NonFBWT Budgetary Accounts include budgetary accounts that do not affect FBWT such as contract authority, borrowing authority, and investment accounts. This category reduces the Status of Fund Balance with Treasury.

**Restricted Unobligated Unavailable Balances**

Unobligated Balance is segregated to show Available and Unavailable amounts in the note schedule. Certain unobligated balances may be restricted to future use and are not apportioned for current use. The USACE is the lead agency for reporting the financial data for the Inland Waterways, Harbor Maintenance, and South Dakota Terrestrial Wildlife Habitat Restoration trust funds. The Department of the Treasury, Bureau of Public Debt (BPD) maintains the investments and the investment accounting records and invests the trust fund receipts. The BPD transfers funds to the individual trust funds as funds are needed.

## Disclosures Related to Suspense/Budget Clearing Accounts

As of September 30	2004	2005	2006	(Decrease)/ Increase from FY 2005 - 2006
<i>(Amounts in thousands)</i>				
<b>Account</b>				
F3845 – Personal Property Proceeds	\$ 0	\$ 0	\$ 0	0
F3875 – Disbursing Officer Suspense	113	632	855	223
F3880 – Lost or Cancelled Treasury Checks	0	0	(168)	(168)
F3882 – Uniformed Services Thrift Savings Plan Suspense	0	0	0	0
F3885 – Interfund/IPAC Suspense	0	(12,215)	(591)	11,624
F3886 – Thrift Savings Plan Suspense	0	0	0	0
<b>Total</b>	<b>\$ 113</b>	<b>\$ (11,583)</b>	<b>\$ 96</b>	<b>\$ 11,679</b>

### Fluctuations

The Total Disclosures Related to Suspense/Budget Clearing Accounts changed by \$11.7 million (101%). The balance at yearend FY 2005 was for unposted Intragovernmental Payment and Collection (IPAC) disbursements and resulted in a \$12.2 million negative balance. Processing of this total balance in FY 2006, coupled with current month unposted IPAC transactions totaling \$591.3 thousand, results in an overall \$11.6 million change in the suspense account balance from yearend FY 2005 to yearend FY 2006. USACE implemented automation 1st Quarter, FY 2006 to identify the obligation number in the Corps of Engineers Financial Management System (CEFMS) related to IPAC transactions. This automation replaced previous manual processes for posting IPAC transactions. The increase of \$223.0 thousand in Disbursing Officer Suspense is due to collections during September 2006 pending corrections of a long term agreement at Omaha District and collections primarily during August 2006 for leases at Nashville District. The decrease of \$168.0 thousand in Lost or Cancelled Treasury Checks is due to invalid chargeback received from the Department of the Treasury during May 2006. The USACE requested reversal of this chargeback in June 2006.

### Abnormalities

The Interfund/IPAC Suspense has an abnormal balance due to recording IPAC net disbursements of (\$591.3) thousand.

### Other Information

The Disbursing Officer Suspense account represents the primary source of the overall positive balance. The Disbursing Officer Suspense account reported a positive balance of \$855.9 thousand. The Interfund/IPAC Suspense account reported a negative balance of (\$591.3) thousand. These two suspense accounts temporarily hold collections or disbursements until they can be assigned or identified to a valid appropriation.

The Lost or Cancelled Treasury Checks account reported a negative balance of (\$168.0) thousand. This amount represents the balance of Treasury checks that (1) have either been lost by the payee and need to be reissued, (2) have never been cashed by the payee, or (3) have been cancelled by the Department of the Treasury and need to be transferred to the original appropriation.

The USACE Civil Works does not have the following accounts: Personal Property Processed, Uniformed Services Thrift Savings Plan Suspense, or Thrift Savings Plan Suspense.

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

The USACE Civil Works does not have Problem Disbursements and In-transit Disbursements.

**Note 4. Investments and Related Interest**

As of September 30	2006				
	Cost	Amortization Method	Amortized (Premium) / Discount	Investments, Net	Market Value Disclosure
<i>(Amounts in thousands)</i>					
<b>1. Intragovernmental Securities</b>					
A. Nonmarketable, Market-Based	\$ 3,632,883	Level Yield Calculation	\$ (81,320)	\$ 3,551,563	\$ 3,519,489
B. Accrued Interest	19,893			19,893	19,893
C. Total Intragovernmental Securities	<u>\$ 3,652,776</u>		<u>\$ (81,320)</u>	<u>\$ 3,571,456</u>	<u>\$ 3,539,382</u>
<b>2. Other Investments</b>					
A. Total Investments	<u>\$ 0</u>		<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ N/A</u>
<b>3. Intragovernmental Securities</b>					
A. Nonmarketable, Market-Based	\$ 3,189,406	Level Yield Calculation	\$ (77,682)	\$ 3,111,724	\$ 3,105,672
B. Accrued Interest	16,108			16,108	16,108
C. Total Intragovernmental Securities	<u>\$ 3,205,514</u>		<u>\$ (77,682)</u>	<u>\$ 3,127,832</u>	<u>\$ 3,121,780</u>
<b>4. Other Investments</b>					
A. Total Investments	<u>\$ 0</u>		<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ N/A</u>

**Fluctuations**

Total Intragovernmental Securities increase of \$443.6 million (14%) in intragovernmental securities, investments, and interest is due to several factors. Harbor Maintenance Trust Fund reported an increase in investments of \$514.1 million. The increase was first reported 1st Quarter, FY 2006 and continued through 4th Quarter, FY 2006 and is due to an increase in volume for taxes collected daily on imports and foreign trade from increased traffic in the harbors. South Dakota Terrestrial Wildlife Habitat Restoration Trust Fund reported a \$13.2 million increase in investments in 4th Quarter, FY 2006. The increase is due to the Department of the Treasury investing the \$10.0 million annual appropriation, received from the general fund, in Market-Based Treasury Notes which mature in two, five, and ten years. All interest received from the notes shall be invested in Market-Based Treasury Notes maturing September 15, 2008, yielding 3%. Inland Waterways Trust Fund reported a decrease in investments of \$83.7 million in 4th Quarter, FY 2006. The decrease is caused by expenditure authority transferred by the Department of the Treasury to the Inland Waterways Trust Fund expenditure account. The funds are transferred from invested balances to cover expenditures. As funds are withdrawn, investment accounts decrease.

Tax revenues are from imports, domestics, excise, foreign trade and passengers. The tax revenues are collected daily by the US Customs Service and are deposited into the Department of the Treasury. These revenues are recorded on a cash basis and are strictly a point-of-service collection. The tax revenues are invested by the Department of the Treasury and are reported on the Bureau of Public Debt (BPD) financial statements for Harbor Maintenance and Inland Waterways Trust Funds.

**Other Information**

The Federal Government does not set aside assets to pay future benefits or other expenditures associated with Harbor Maintenance, Inland Waterways, and South Dakota Terrestrial Wildlife Habitat Restoration trust funds. The cash receipts collected from the public for an earmarked fund are deposited in the Department of the Treasury, which uses the cash for general government purposes. The Department of the Treasury securities are issued to the US Army Corp of Engineers (USACE) as evidence of its receipts. The Department of the Treasury securities are an asset to USACE and a liability to the Department of the Treasury. Because USACE and the Department of the Treasury are both parts of the government, these assets and liabilities offset each other from the standpoint of the government as a whole. For this reason, they do not represent an asset or a liability in the US Government-wide financial statements. The Department of the Treasury securities provide USACE with authority to draw upon the Department of the Treasury to make future benefit payments or other expenditures. When USACE requires redemption of these securities to make expenditures, the government finances those expenditures out of accumulated cash balances, by raising taxes or other receipts, by borrowing from the public or repaying less debt, or by curtailing other expenditures. This is the same way that the government finances all other expenditures.

Total investments include \$195.0 million in one-day certificates and \$3.4 billion in bonds and notes. The breakdown of total investments among the trust funds is as follows: \$3.2 billion in the Harbor Maintenance Trust Fund, \$262.3 million in the Inland Waterways Trust Fund, and \$88.7 million in the South Dakota Terrestrial Wildlife Habitat Restoration Trust Fund.

The Department of the Treasury also provides the investment market value based on the bid price provided by the Federal Reserve Bank of New York on September 30, 2006.

## Note 5. Accounts Receivable

As of September 30	2006			2005
	Gross Amount Due	Allowance For Estimated Uncollectibles	Accounts Receivable, Net	Accounts Receivable, Net
<i>(Amounts in thousands)</i>				
1. Intragovernmental Receivables	\$ 2,407,555	\$ N/A	\$ 2,407,555	\$ 613,904
2. Nonfederal Receivables (From the Public)	\$ 1,779,857	\$ (6,084)	\$ 1,773,773	\$ 1,750,925
3. Total Accounts Receivable	\$ 4,187,412	\$ (6,084)	\$ 4,181,328	\$ 2,364,829

### Fluctuations

Intragovernmental Receivables increased \$1.8 billion (292%). The increase is primarily attributed to an increase in reimbursable work with the Department of Homeland Security. The new receivables are predominantly due from the Federal Emergency Management Agency (FEMA), and are associated with disaster relief efforts for hurricanes Katrina, Rita, and Wilma at the US Army Corps of Engineers (USACE) New Orleans, Vicksburg, and Galveston Districts. The increase in intragovernmental receivables for hurricane relief efforts was initially reported in 1st Quarter, FY 2006 and continued through 4th Quarter, FY 2006.

### Other Information

The method of calculating the allowance for estimated uncollectibles is based on the cumulative balance of delinquent public receivables aged in accordance with current USACE policy. USACE uses the aging of accounts receivable method to calculate the allowance for estimated uncollectibles. The calculation is performed automatically in the Corps of Engineers Financial Management System (CEFMS).

The Code of Federal Regulations (4CFR 101) prohibits the write-off of receivables from another federal agency. As such, no allowance for estimated uncollectible amounts is recognized for these receivables.

The USACE was able to reconcile its accounts receivable balances with the accounts payable balances of other Department of Defense trading partners that have systems which capture pertinent information. No material differences were identified. The USACE is unable to reconcile with other intragovernmental trading partners whose financial systems are not designed to capture pertinent information to fully reconcile intragovernmental transactions.

The amount of public receivables on the Treasury Report on Receivables Due from the Public (TROR) differs from the balance of public receivables reported on the balance sheet. The TROR does not include the allowance for estimated uncollectibles.



**Aged Accounts Receivable**

As of September 30	2006		2005	
	Intragovernmental	Nonfederal	Intragovernmental	Nonfederal
<i>(Amounts in thousands)</i>				
CATEGORY				
<b>Nondelinquent</b>				
Current	\$ 739,757	\$ 71,567	\$ 579,802	\$ 72,286
Noncurrent	0	1,621,941	0	1,601,437
<b>Delinquent</b>				
1 to 30 days	\$ 181,164	\$ 2,931	\$ 9,650	\$ 2,949
31 to 60 days	169,359	282	5	149
61 to 90 days	11	147	7,723	229
91 to 180 days	604,648	334	9,709	1,007
181 days to 1 year	718,231	15,529	29,023	15,682
Greater than 1 year and less than or equal to 2 years	1,970	15,857	5,849	19,322
Greater than 2 years and less than or equal to 6 years	4,496	43,380	2,672	31,907
Greater than 6 years and less than or equal to 10 years	11	7,889	11	11,729
Greater than 10 years	0	0	0	0
<b>Subtotal</b>	<b>\$ 2,419,647</b>	<b>\$ 1,779,857</b>	<b>\$ 644,444</b>	<b>\$ 1,756,697</b>
Less Supported Undistributed Collections	0	0	0	0
Less Eliminations	(12,092)	0	(30,540)	0
Less Other	0	0	0	0
<b>Total</b>	<b>\$ 2,407,555</b>	<b>\$ 1,779,857</b>	<b>\$ 613,904</b>	<b>\$ 1,756,697</b>

**Delinquent Intragovernmental Receivables**

The total delinquent intragovernmental accounts receivable is \$1.7 billion. Of the \$1.7 billion delinquent, \$1.6 billion is due from FEMA, mostly resulting from the receivables associated with hurricanes Katrina, Rita, and Wilma at USACE New Orleans, Vicksburg, and Galveston Districts. The USACE has reduced its delinquent FEMA receivables by \$552.0 million since July 2006. This is due to new Intergovernmental Payment and Collection (IPAC) arrangements coupled with concerted efforts among Headquarters USACE, the USACE Finance Center, and FEMA personnel. The Coast Guard and the Environmental Protection Agency have delinquent receivables totaling \$10.3 million, of which \$8.0 million is related to the Oil Pollution Act. The USACE continues to evaluate and improve the effectiveness of the intragovernmental payment and collections process and implement improvements to these processes. The USACE is aggressively pursuing collection action for delinquent intragovernmental accounts receivable.

**Delinquent Nonfederal Receivables (From the Public)**

The amount of delinquent nonfederal receivables is \$86.3 million. Of the total delinquent receivables, \$52.8 million is owed by the Commonwealth of Puerto Rico on a 50 year contract for the Cerrillos Dam water storage at USACE Jacksonville District. Additionally, \$14.3 million is owed by the Oklahoma Water Resources Board for water storage space at USACE Tulsa District. The USACE is aggressively pursuing collection action for delinquent nonfederal accounts receivable.

**Nondelinquent Noncurrent Nonfederal Receivables (From the Public)**

The \$1.6 billion in nondelinquent noncurrent nonfederal receivables consists of amounts due from state and local municipalities for long-term water storage contracts.

## Note 6. Other Assets

As of September 30	2006	2005
<i>(Amounts in thousands)</i>		
1. Intragovernmental Other Assets		
A. Advances and Prepayments	\$ 0	\$ 0
B. Other Assets	0	0
C. Total Intragovernmental Other Assets	\$ 0	\$ 0
2. Nonfederal Other Assets		
A. Outstanding Contract Financing Payments	\$ 0	\$ 0
B. Other Assets (With the Public)	440,839	0
C. Total Nonfederal Other Assets	\$ 440,839	\$ 0
3. Total Other Assets	\$ 440,839	\$ 0

### Fluctuations

Other Assets (With the Public) increased \$440.8 million (100%). The increase is attributable to reporting the costs associated with fish and wildlife mitigation studies as intangible assets when related to hydropower projects. The studies are conducted in the Portland and Walla Walla Districts. Based on comments from the Department of Defense, Office of the Inspector General, the US Army Corps of Engineers (USACE) should be consistent with the methodology used by the Bonneville Power Administration (BPA) to account for costs involving fish mitigation studies, since the Federal Columbia River Power System combines the accounts of BPA and USACE. In accordance with Statement of Financial Accounting Standard No. 71, "Accounting for the Effects of Certain Types of Regulation," BPA is granted the authority to capitalize and amortize all or part of the incurred cost that would otherwise be charged to expense. The USACE has implemented this policy and records the costs in US Standard General Ledger 1990 – other assets. This accounting method became effective 2nd Quarter, FY 2006.

### Other Information

Other Assets (With the Public) consists of amounts attributable to the cost of fish and wildlife mitigation studies related to the hydropower projects. At the completion of each study, USACE will determine if a tangible asset will be constructed as a direct result of the study. If so, USACE will hold the cost in construction-in-progress until the construction is complete. If not, USACE will place in service the cost of the study as an intangible asset.

## Note 7. Cash and Other Monetary Assets

As of September 30	2006	2005
<i>(Amounts in thousands)</i>		
1. Cash	\$ 497	\$ 556
2. Foreign Currency	813	591
3. Total Cash, Foreign Currency, & Other Monetary Assets	\$ 1,310	\$ 1,147

### Fluctuations

Total Cash, Foreign Currency, & Other Monetary Assets increased \$163.5 thousand (14%) and is attributed to a purchase of \$200.0 thousand US dollar equivalent of Korean won in September 2006. The currency was purchased to process payment due in October 2006 for a contract established in won. The decrease in Disbursing Officer's Accountability (Cash) of \$58.8 thousand is due to recouping travel advances issued to USACE Memphis and Vicksburg district employees assigned to debris cleanup for Hurricane Katrina in the Gulf of Mexico, and settlements of permanent change of station advances for USACE Savannah and Ft. Worth district employees during 4th Quarter, FY 2006.

### Other Information

Cash consists of \$492.8 thousand in Disbursing Officer's Accountability for travel advances issued, and \$4.4 thousand in change funds for recreation cashiers. Cash and foreign currency is nonentity, and is, therefore, restricted. There are no significant effects from changes in the foreign currency exchange rate.

The USACE translates foreign currency to US 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 US Government's acquisition of foreign currency for its official disbursements and accommodation of exchange transactions. The USACE maintains a balance of Japanese yen, Euro dollars, and Korean won for disbursements made at Japan, Europe and Far-East districts.

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

Not applicable.

## Note 9. Inventory and Related Property

As of September 30	2006		2005	
<i>(Amounts in thousands)</i>				
1. Inventory, Net	\$	24,259	\$	117,237
2. Operating Materials & Supplies, Net		97,081		147
3. Stockpile Materials, Net		0		0
4. Total	\$	121,340	\$	117,384

### Inventory, Net

As of September 30	2006			2005		Valuation Method
	Inventory, Gross Value	Revaluation Allowance	Inventory, Net	Inventory, Net		
<i>(Amounts in thousands)</i>						
1. Inventory Categories						
A. Available and Purchased for Resale	\$ 0	\$ 0	0	\$ 94,996		MAC
B. Held for Repair	0	0	0	0		MAC
C. Excess, Obsolete, and Unserviceable	0	0	0	0		MAC
D. Raw Materials	0	0	0	0		MAC
E. Work in Process	24,259	0	24,259	22,241		MAC
F. Total	\$ 24,259	\$ 0	24,259	\$ 117,237		

#### Legend for Valuation Methods:

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

SP = Standard Price

AC = Actual Cost

NRV = Net Realizable Value

O = Other

MAC = Moving Average Cost

### Fluctuations

Total inventory decreased \$93.0 million (79%). During 4th Quarter, FY 2005, the US Army Corps of Engineers (USACE) reported Inventory Available and Purchased for Resale. Based on Statement of Federal Financial Accounting Standards (SFFAS) No. 3, "Accounting for Inventory and Related Property," USACE determined that the inventory did not fit the criteria for inventory held for sale because there was no sale outside USACE activities. As a result, during 4th Quarter, FY 2006, USACE reported the inventory as Operating Materials and Supplies (OM&S). Multiple USACE activities have inventory, but the majority is within the Mississippi Valley Region activities.

### Restrictions of Inventory Use, Sale, or Disposition

There are no restrictions on the use of inventory.

### Other Information

General composition of USACE Work in Process (WIP) inventory is tangible personal property that is in the process of production. WIP includes associated labor, applied overhead and supplies used in the delivery of services. The inventory valuation method is based on a

moving weighted average based on actual cost divided by quantity. A perpetual record of inventory is maintained to allow for recomputation of the average unit cost as new receipts are recorded. There is no change from the prior year's accounting method. There are no changes to the prior year's criteria for WIP.

The inventory data reported on the financial statements is derived from the Corps of Engineers Financial Management System (CEFMS). CEFMS is a comprehensive system that is designed to capture and maintain historical cost data necessary to fully comply with the SFFAS No. 3.

## Operating Materials and Supplies, Net

As of September 30	2006			2005	Valuation Method
	OM&S Gross Value	Revaluation Allowance	OM&S, Net	OM&S, Net	
<i>(Amounts in thousands)</i>					
1. OM&S Categories					
A. Held for Use	\$ 97,096	\$ (15)	\$ 97,081	\$ 147	NRV
B. Held for Repair	0	0	0	0	NRV
C. Excess, Obsolete, and Unserviceable	0	0	0	0	NRV
D. Total	\$ 97,096	\$ (15)	\$ 97,081	\$ 147	

### Legend for Valuation Methods:

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

### Fluctuations

Total OM&S increased \$97.0 million. During 4th Quarter, FY 2006, the USACE reported Inventory Available and Purchased for Resale. Based on Statement of Federal Financial Accounting Standards (SFFAS) No. 3, "Accounting for Inventory and Related Property," USACE determined that the inventory did not fit the criteria for inventory held for sale because there was no sale outside USACE activities. As a result, during 4th Quarter, FY 2006, USACE reported the inventory as Operating Materials and Supplies (OM&S). Multiple USACE activities have inventory, but the majority is within the Mississippi Valley Region activities.

### Other Information

General composition of USACE OM&S is personal property to be consumed in normal operations. OM&S includes materials for constructing river revetment bedding, spare and repair parts, miscellaneous office supplies, and metered mail. The valuation method is based on net realizable value. There is no change from the prior year's accounting method. There are no restrictions on OM&S. The relevant cost associated with maintaining the available operating materials and supplies, as well as the time required to replenish the operating materials and supplies, are the criteria used in determining the assigned category. There are no changes to the prior year's criteria.

## Stockpile Materials, Net

The USACE does not have Stockpile Materials.

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

As of September 30	2006					2005
	Depreciation/ Amortization Method	Service Life	Acquisition Value	(Accumulated Depreciation/ Amortization)	Net Book Value	Prior FY Net Book Value
<i>(Amounts in thousands)</i>						
1. Major Asset Classes						
A. Land	N/A	N/A	\$ 8,914,787	\$ N/A	\$ 8,914,787	\$ 8,900,815
B. Buildings, Structures, and Facilities	S/L	20 Or 40	27,366,591	(13,039,517)	14,327,074	14,516,153
C. Leasehold Improvements	S/L	lease term	37,755	(24,355)	13,400	12,561
D. Software	S/L	2-5 Or 10	82,702	(57,206)	25,496	36,863
E. General Equipment	S/L	5 or 10	1,313,004	(654,981)	658,023	643,576
F. Military Equipment	S/L	Various	0	0	0	0
G. Assets Under Capital Lease	S/L	lease term	0	0	0	0
H. Construction-in- Progress	N/A	N/A	2,849,493	N/A	2,849,493	2,642,702
I. Other			33,690	(1)	33,689	27,432
J. Total General PP&E			\$ 40,598,022	\$ (13,776,060)	\$ 26,821,962	\$ 26,780,102

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

**Legend for Valuation Methods:**

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

**General PP&E – Significant Amount of Assets**

A cumulative total of \$2.6 billion of intangible assets has been reclassified as land. These assets are comprised of relocation and administrative costs associated with the acquisition of land in conjunction with hydropower projects. Costs were originally classified as intangible assets in order to comply with Federal Energy Regulatory Commission (FERC) guidelines on cost recovery. However, the decision was made during 4th Quarter, FY 1999, that these costs were improperly classified in accordance with the Statement of Federal Financial Accounting Standards, No. 6, "Accounting for Property, Plant and Equipment (PP&E)," as they were part of the initial acquisition cost of the land and should have been classified as such. We have also made a reversing entry for current year amortization in our statements to properly reflect the effect of the transfer into land where accumulated depreciation is inappropriate. Supporting documentation for approximately \$17.3 billion of the \$26.8 billion recorded in the PP&E line is being supported by alternate methods as agreed upon by the Inspector General, Department of Defense (DoD) and the US Army Corps of Engineers (USACE) in a June 9, 2004, Memorandum of Agreement.

The service life for USACE's multiple purpose project assets is derived from guidance provided by FERC based on industry standards. The hydropower project related assets make up \$7.6 billion of the book value of USACE's PP&E.

The USACE currently operates and maintains 75 hydroelectric power plants, generating about 24% of America's hydroelectric power. All power generated by these 75 hydroelectric power plants is transmitted to Power Marketing Administration (PMA) for distribution to customers across their respective regions. Each fiscal year, USACE prepares a "Statement of Expenses" broken down by plant, district, and region and provides this information to the PMAs to assist in their Power Repayment Study. The PMAs then collect power receipts (revenues) from customers and return the receipts to the Department of the Treasury.

The USACE's policy requires all capital improvements to real property, occupied but not owned by USACE, with a useful life of two or more years and cost of \$25.0 thousand or more, to be capitalized as leasehold improvements.

In USACE's FY 2006 construction-in-progress (CIP) account, \$151.0 million of the \$2.8 billion (5%) is attributable to a dormant project formally known as the "Elk Creek Lake Project" located at USACE Portland District. The project, which was authorized by the 1962 Flood Control Act, was originally authorized to perform the purpose of flood control. In 1971, construction began on the project but after completing only 33% of its design height, the project was shut down due to a court-ordered injunction. Additional analysis under the National Environmental Policy Act is required to remove the injunction. To date, the environmental concerns have not been resolved and the project is sitting in a hold status until such time these issues are resolved. Therefore, USACE will continue to carry the construction costs of the "Elk Creek Lake Project" in the CIP account until a final decision is made concerning the outcome of the project.

Due to the severity of hurricanes Katrina, Rita, and Wilma, USACE conducted a 100% review of all real and personal property assets within the affected areas. As a result of this review, USACE found that three real property assets with a net book value of \$153.1 thousand were destroyed and retired. Five personal property assets and 66 real property assets were damaged with an estimated repair cost of over \$16.4 million. All repairs are either currently on-going or scheduled during FY 2007. In addition, two real property assets with a net book value of over \$9.5 million are still under investigation to determine the extent of the damages and the estimated cost of repairs.

The USACE has no restrictions on the use or convertibility of General PP&E.

There were no changes to accounting standards that required adjustment.

Asset donations include \$15.3 million in land tracts donated in prior years in the USACE Kansas City, Savannah, and Ft. Worth districts. The USACE adjusted the value of the land tracts to the fair market value of the land at the time of the donation. These assets were previously recorded at zero or nominal value.

Other consists of assets awaiting disposal.

### **Heritage Assets and Stewardship Land**

The USACE administers the Lake Superior Marine Museum as part of the Operations and Maintenance Mission of the Detroit District. This museum has gone inadvertently unreported in previous submittals on USACE's heritage assets.

The USACE has one major collection managed by Headquarters, USACE Office of History. The collection consists of historical memorabilia and historic artifacts and records.

Other than multipurpose heritage assets, heritage assets are not material to the mission of USACE.

Heritage assets classified as land are special land plots containing archaeological sites that are listed on the National Register of Historic Places, or which are eligible to be listed.

Heritage assets on display are assumed to be in adequate condition for display purposes, consistent with their origins, unless otherwise noted. Reported heritage assets are free of material conditions that are counter to safeguarding, adequately protecting, and properly managing those assets; they have not materially degraded while under the care of USACE. The existence of most of the uncategorized heritage assets is informally known to be adequate for display purposes, however, the condition of many uncategorized assets is unknown.

Cemeteries and archeological sites are archeological properties listed on, or eligible for, the National Register of Historic Places. These archeological assets cover almost the entire range of human occupation of the Continental United States, beginning with the Kennewick Man Discovery Site in the state of Washington, dating to approximately 10,000 years before present, to archeological remains of early European-American settlements such as Fort Independence in Georgia.

Buildings and structures include a range of historic resources from a covered bridge in Sacramento District to early farming structures in Savannah District. It also includes some nontraditional structures such as a snag boat that operated on the Mississippi River.

The USACE currently does not have any land classified as stewardship land.

### **Assets Under Capital Lease**

The USACE has no assets under capital lease.

## Note 11. Liabilities Not Covered by Budgetary Resources

As of September 30	2006	2005
<i>(Amounts in thousands)</i>		
1. Intragovernmental Liabilities		
A. Accounts Payable	\$ 0	\$ 0
B. Debt	13,592	14,251
C. Other	1,961,767	1,930,884
D. Total Intragovernmental Liabilities	\$ 1,975,359	\$ 1,945,135
2. Nonfederal Liabilities		
A. Accounts Payable	\$ 0	\$ 0
B. Military Retirement and Other Federal Employment Benefits	250,272	0
C. Environmental Liabilities	653,315	529,617
D. Other Liabilities	77,275	26,055
E. Total Nonfederal Liabilities	\$ 980,862	\$ 555,672
3. Total Liabilities Not Covered by Budgetary Resources	\$ 2,956,221	\$ 2,500,807
4. Total Liabilities Covered by Budgetary Resources	\$ 1,238,605	\$ 1,224,297
5. Total Liabilities	\$ 4,194,826	\$ 3,725,104

### Fluctuations

Total Liabilities Not Covered by Budgetary Resources increased \$455.4 million (18%) mainly due to reporting actuarial liability for the Federal Employees Compensation Act (FECA). Actuarial liability for FECA increased \$250.3 million. The initial recording of the liability was in 4th Quarter, FY 2006. The Department of Labor (DOL) provides the liability amounts at the Department level (Department of the Army, Department of the Navy). The DOL is unable to provide a FECA actuarial liability specific to the US Army Corps of Engineers (USACE) Civil Works Program. USACE determined the actuarial liability by using a three year average of total USACE FECA bills as a percentage of the total Department of the Army bills. That percentage was applied to the amount of total actuarial liability for the Department of the Army to arrive at the USACE portion.

The remaining increase is primarily due to recording additional environmental liabilities of \$88.4 million in 2nd Quarter, FY 2006, \$433.5 thousand in 3rd Quarter, FY 2006, and \$34.9 million in 4th Quarter, FY 2006 for the Formerly Utilized Sites Remedial Action Program (FUSRAP). Studies and final Records of Decision documenting the cleanup requirements have been completed at numerous sites. The amounts for environmental liabilities for the FUSRAP were initially determined and reported in 4th Quarter, FY 2005.

### Other Information

Intragovernmental Liabilities – Other includes offsetting custodial liability to accounts receivable, Judgment Fund liabilities-Contract Dispute Act (CDA), and workmen's compensation liabilities under FECA. The custodial liability is for amounts that will be deposited in the general fund of the Department of the Treasury when collected and are primarily related to water storage contracts. The USACE is seeking supplemental funding for CDA liability. The FECA liability will not be funded until FY 2007.

Nonfederal Liabilities – Military Retirement Benefits and Other Employment-Related Actuarial Liabilities include actuarial liability for FECA.

Nonfederal Liabilities – Other Liabilities include contingent liability for probable losses related to lawsuits filed by the state of Nebraska and the county of Knox, Nebraska, contingent liability based on percentage of tort, litigation and contract dispute claims, and contracts with continuation clauses.

## Note 12. Accounts Payable

As of September 30	2006			2005
	Accounts Payable	Interest, Penalties, and Administrative Fees	Total	Total
<i>(Amounts in thousands)</i>				
1. Intragovernmental Payables	\$ 93,841	\$ N/A	\$ 93,841	\$ 87,230
2. Nonfederal Payables (to the Public)	442,199	0	442,199	535,882
3. Total	\$ 536,040	\$ 0	\$ 536,040	\$ 623,112

### Fluctuations

Nonfederal Payables (to the Public) decreased \$93.7 million (17%). The decrease is mainly attributed to liquidating accounts payable for projects involving dredging and excavation of channels, repair to and maintenance of dams and levees, and operation of reservoirs in the US Army Corps of Engineers (USACE) North Atlantic Division and USACE South Atlantic Division. The decrease occurred in 4th Quarter, FY 2006.

### Other Information

Intragovernmental Payables consist of amounts owed to other Federal Agencies for goods or services ordered and received, but not yet paid. Interest, penalties, and administrative fees are not applicable to intragovernmental payables.

The USACE has no known delinquent accounts payable; therefore, no amount is reported for interest, penalties, and administrative fees. However, USACE paid \$1.2 million in interest from Civil Works appropriations on payments subject to the Prompt Payment Act during FY 2006.

The USACE was able to reconcile its accounts payable balance with the accounts receivable balances of other Department of Defense trading partners that have systems which capture pertinent information. No material reconciling differences were identified. The USACE is unable to reconcile with other intragovernmental trading partners whose financial systems are not designed to capture pertinent information to fully reconcile Intragovernmental transactions.

## Note 13. Debt

As of September 30	2006			2005	
	Beginning Balance	Net Borrowing	Ending Balance	Net Borrowing	Ending Balance
<i>(Amounts in thousands)</i>					
1. Agency Debt (Intragovernmental)					
A. Debt to the Treasury	\$ 14,600	\$ (676)	\$ 13,924	\$ (767)	\$ 14,600
B. Debt to the Federal Financing Bank	0	0	0	0	0
C. Total Agency Debt	\$ 14,600	\$ (676)	\$ 13,924	\$ (767)	\$ 14,600
2. Total Debt	\$ 14,600	\$ (676)	\$ 13,924	\$ (767)	\$ 14,600

### Other Information

During fiscal years 1997, 1998, and 1999, the US Army Corp of Engineers (USACE) executed three promissory notes totaling \$75.0 million with the Department of the Treasury. Funds provided were used for capital improvements to the Washington Aqueduct. Arlington County, the city of Falls Church, Virginia, and the District of Columbia provide funding to repay the debt. The District of Columbia repaid the remaining portion of their debt in 2nd Quarter, FY 2004. Actual cumulative drawdown of the funds has been made from the Department of the Treasury in the amount of \$74.9 million. There were no drawdowns of funds from the Department of the Treasury for 4th Quarter, FY 2006. During FY 2006, principal repayments total \$659.1 thousand and accrued interest payable is \$16.4 thousand.

Treasury Drawdown	Cumulative Principal Repayments	FY 2006 Interest Accrual	Total Debt
\$74.9 million	- \$61.3 million	+ \$332 thousand	= \$13.9 million



**Note 14. Environmental Liabilities and Disposal Liabilities**

As of September 30	2006			2005
	Current Liability	Noncurrent Liability	Total	Total
<i>(Amounts in thousands)</i>				
1. Environmental Liabilities--Nonfederal				
A. Accrued Environmental Restoration Liabilities				
1. Active Installations—Installation Restoration Program (IRP) and Building Demolition and Debris Removal (BD/DR)	\$ 0	\$ 0	\$ 0	\$ 0
2. Active Installations—Military Munitions Response Program (MMRP)	0	0	0	0
3. Formerly Used Defense Sites—IRP and BD/DR	0	0	0	0
4. Formerly Used Defense Sites--MMRP	0	0	0	0
B. Other Accrued Environmental Liabilities—Active Installations				
1. Environmental Corrective Action	0	0	0	0
2. Environmental Closure Requirements	0	0	0	0
3. Environmental Response at Operational Ranges	0	0	0	0
4. Other	0	653,315	653,315	529,617
C. Base Realignment and Closure (BRAC)				
1. Installation Restoration Program	0	0	0	0
2. Military Munitions Response Program	0	0	0	0
3. Environmental Corrective Action / Closure Requirements	0	0	0	0
4. Other	0	0	0	0
D. Environmental Disposal for Weapons Systems Programs				
1. Nuclear Powered Aircraft Carriers	0	0	0	0
2. Nuclear Powered Submarines	0	0	0	0
3. Other Nuclear Powered Ships	0	0	0	0
4. Other National Defense Weapons Systems	0	0	0	0
5. Chemical Weapons Disposal Program	0	0	0	0
6. Other	0	0	0	0
2. Total Environmental Liabilities	\$ 0	\$ 653,315	\$ 653,315	\$ 529,617

Others Category Disclosure Comparative Table		
<i>(Amounts in thousands)</i>	(Current FY)	(Prior FY)
<b>Other Accrued Environmental Costs - Other</b>		
The accrued environmental cost for the liability is reported for the Formerly Utilized Sites Remedial Action Program, which was established to respond to radiological contamination from early US atomic energy and weapons program. See Other Disclosures.	\$653,315	\$529,617
<b>Total</b>	<b>653,315</b>	<b>529,617</b>

**Fluctuations**

Other Accrued Environmental Liabilities (Other) increased by \$123.7 million (23%). The increase is due to recording the liability for feasibility study cost estimates of \$44.0 million and \$32.0 million for new remediation costs in 4th Quarter, FY 2006 for Formerly Utilized Sites Remedial Action Program (FUSRAP) project sites. The liability also increased by \$36.0 million in 2nd Quarter, FY 2006 for updates to remediation cost estimates for the FUSRAP project sites. All increases are for the project sites listed in Other Information. The remaining increase of \$11.7 million is for a one-time correction in 2nd Quarter, FY 2006 to the starting costs for the St. Louis Airport, St. Louis Airport Vicinity Property, and the Latty Avenue Properties FUSRAP project sites.

**Other Information**

The US Army Corps of Engineers (USACE) is responsible for the FUSRAP, which was established to respond to radiological contamination from early US Atomic Energy and Weapons Program. This program is funded through a Civil Works appropriation. The amount of the liability is determined after studies have been completed and final Records of Decision documenting the cleanup requirements are prepared. The amount of the liability is recorded as Other Accrued Environmental Liabilities. The remaining categories of environmental liabilities do not apply to the USACE Civil Works Program.

The USACE recognizes noncurrent environmental liabilities for the FUSRAP at the following project sites: St. Louis Downtown Site Accessible Soils, St. Louis Airport Site, Latty Avenue Properties Site, St. Louis Airport Vicinity Properties Site, Maywood Site Soils, Middlesex Sampling Plant Soils, Shpack Landfill Site, W. R. Grace Building 23 Site, Colonie Interim Storage Site Soils, Luckey Site Soils, Linde Air Products Site Soils, Painesville Site, Ashland Site, St. Louis Downtown Site Inaccessible Soils, Iowa Army Ammunition Plant FUSRAP Site, Colonie Interim Storage Site Groundwater, Maywood Site Groundwater, Middlesex Sampling Plant Site Groundwater, Combustion Engineering Site, DuPont Chambers Works Site, W. R. Grace Radioactive Waste Disposal Area Site, Sylvania-Corning Plant Site, Linde Air Products Site Groundwater, Luckey Site Groundwater, Seaway Industrial Park Site, Shallow Land Disposal Area Site, Former Harshaw Chemical Company Site, Guterl Specialty Steel Site, and Niagara Falls Interim Storage Site.

The USACE recognizes contingent liabilities related to this program but the liability amounts are currently unknown. The project sites are: St. Louis Downtown Site Inaccessible Soils, Iowa Army Ammunition Plant FUSRAP Site, Middlesex Sampling Plant Site Groundwater, Combustion Engineering Site, DuPont Chambers Works Site, W. R. Grace Radioactive Waste Disposal Area Site, Seaway Industrial Park Site, Niagara Falls Storage Site, Shallow Land Disposal Area Site, Former Harshaw Chemical Company Site, and Guterl Specialty Steel Site.

The USACE has completed the assessment of all real and personal property either partially or completely impaired by hurricanes Katrina, Rita and Wilma, with all known impairments properly reflected in the financial statements. In conjunction with the assessment of assets, USACE has also completed its review of any potential liabilities, including environmental liabilities, which may have occurred due the hurricanes with all known liabilities being properly recorded.

Environmental liabilities not related to FUSRAP are currently unknown for the following project sites: Sonoma Firing Range and Sonoma Underground Storage Tanks Monitoring Wells in Sonoma, California; Black Rock Lock and Mount Morris Dam in New York; Bradford Island Landfill and North Pacific Division Materials Laboratory in Oregon; Saint Georges Bridge in Pennsylvania; and John H. Kerr Dam and Reservoir in Virginia.

**Environmental Disclosures**

As of September 30	2006	2005
<i>(Amounts in thousands)</i>		
A. Amount of operating and capital expenditures used to remediate legacy waste. Legacy wastes are the remediation efforts covered by IRP, MMRP, and BD/DR regardless of funding source.	0	0
B. The unrecognized portion of the estimated total cleanup costs associated with general property, plant and equipment.	0	0
C. The estimated cleanup costs associated with general property, plant and equipment placed into service during each fiscal year.	0	0
D. Changes in total cleanup costs due to changes in laws, regulations, and/or technology.	0	0
E. Portion of the changes in estimated costs due to changes in laws and technology that is related to prior periods.	0	0

**Applicable laws and regulations for cleanup requirements**

Energy and Water Development Appropriations Act, Public Law 106-60, § 611; Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA, 42 USC § 9601 et seq.), as amended; and National Oil and Hazardous Substances Pollution Contingency Plan (NCP, 40 C.F.R. 300).

**Method for assigning estimated total cleanup cost to current operating periods**

The USACE uses site-specific engineering estimates for assigning estimated environmental costs. Both the cost to complete remedial investigation/feasibility studies through a Record of Decision and the estimated cost of chosen remedies are reported. Engineering estimates, using appropriate tools, such as the Micro-Computer Assisted Cost Estimating System (M-CACES), and using the extensive data collected during the remedial investigation/feasibility study phase of the environmental project are used. The estimated costs of studies are reported during the early part of the remedial investigation and the estimated cost of the chosen remedy is reported after release of the Proposed Plan.

**Types of environmental liabilities and disposal liabilities identified**

The USACE, through an annual Energy and Water Development Appropriation, is responsible for executing the FUSRAP at sites deemed eligible by the Department of Energy. Under FUSRAP, USACE cleans up contamination in the US resulting from work performed as part of the nation's early atomic energy program. Consistent with the requirements of CERCLA, USACE coordinates with regulatory agencies, other responsible parties, and current property owners.

**Nature of estimates and the disclosure of information regarding possible changes due to inflation, deflation, technology, or applicable laws and regulations**

Engineering estimates for cleanup of individual sites are made using data obtained during the remedial investigation/feasibility study phase of the CERCLA process. These estimates are updated upon contract award, and periodically, to account for inflation/deflation and fluctuations in labor rates, transportation rates, disposal charges, and to reflect changes in site conditions. The finalization of the Record of Decision for each site sets the cleanup standard that establishes the criteria for determining when site remediation is complete.

**Uncertainty regarding the accounting estimates used to calculate the reported environmental liabilities**

The volume of contaminated material and the cost to dispose of such material, including transportation, are the elements of project estimates with the greatest uncertainty and potential for significant effect upon project costs.

**Note 15. Other Liabilities**

As of September 30	2006			2005
	Current Liability	Noncurrent Liability	Total	Total
<i>(Amounts in thousands)</i>				
1. Intragovernmental				
A. Advances from Others	\$ 9,835	\$ 0	\$ 9,835	\$ 11,247
B. Deposit Funds and Suspense Account Liabilities	1,648	0	1,648	594
C. Disbursing Officer Cash	493	0	493	552
D. Judgment Fund Liabilities	164,221	0	164,221	162,645
E. FECA Reimbursement to the Department of Labor	20,522	27,224	47,746	46,851
F. Other Liabilities	91,853	1,671,777	1,763,630	1,735,006
G. Total Intragovernmental Other Liabilities	\$ 288,572	\$ 1,699,001	\$ 1,987,573	\$ 1,956,895
2. Nonfederal				
A. Accrued Funded Payroll and Benefits	\$ 380,917	\$ 0	\$ 380,917	\$ 376,600
B. Advances from Others	132,360	0	132,360	104,775
C. Deferred Credits	0	0	0	0
D. Deposit Funds and Suspense Accounts	6,978	0	6,978	(2,742)
E. Temporary Early Retirement Authority	0	0	0	0
F. Nonenvironmental Disposal Liabilities				
(1) Military Equipment (Nonnuclear)	0	0	0	0
(2) Excess/Obsolete Structures	0	0	0	0
(3) Conventional Munitions Disposal	0	0	0	0
G. Accrued Unfunded Annual Leave	0	0	0	0
H. Capital Lease Liability	0	0	0	0
I. Other Liabilities	233,144	0	233,144	122,247
J. Total Nonfederal Other Liabilities	\$ 753,399	\$ 0	\$ 753,399	\$ 600,880
3. Total Other Liabilities	\$ 1,041,971	\$ 1,699,001	\$ 2,740,972	\$ 2,557,775

**Fluctuations**

Total Nonfederal Other Liabilities increased by \$152.5 million (25%). There was an increase of \$103.5 million in contract holdbacks primarily in the Flood Control and Coastal Emergencies appropriation for recovery work related to hurricanes Katrina, Rita, and Wilma in the US Army Corps of Engineers (USACE) New Orleans, Vicksburg, and Galveston districts. The increase occurred primarily in the 1st Quarter, FY 2006, but has continued throughout FY 2006. Contingent liabilities also increased by \$33.4 million. The USACE recognized a contingent liability for \$40 million for two probable losses in the Omaha District in the 4th Quarter, FY 2006, for cases above the materiality threshold

of \$7.2 million. The USACE also recognized a contingent liability for \$33 million for reasonably possible losses for pending contract claims, civil litigation and tort cases below the threshold of \$7.2 million in the 4th Quarter, 2006. The likelihood of an unfavorable or potential liability was determined by using a three-year historical-loss average of 10% applied to the outstanding balance of \$330 million for these cases. No contingent liabilities for claims or litigation were recorded in prior fiscal years because no cases above the materiality threshold of \$7.2 million were considered probable losses or the amount of the loss could not be determined. The recognition of the contingent liability for cases below the \$7.2 million materiality threshold represents a change in accounting practice implemented in the 4th Quarter, FY 2006. The USACE also reported an insurance reserve account for \$39.6 million as a contingent liability at the 4th Quarter, FY 2005. The USACE determined that the insurance reserve account should be reclassified from a liability to a gain in the 1st Quarter, FY 2006.

#### **Composition of Other Liabilities**

Intragovernmental Other Liabilities (current) includes the custodial liability to offset interest and accounts receivable which, when collected, will be returned to the Department of the Treasury and the liability for employer contributions and payroll taxes payable. Intragovernmental Other Liabilities (noncurrent) represent future revenue from long-term water storage contracts and hydraulic mining contracts. The USACE records a custodial liability for receivables from water storage and hydraulic mining contracts. The receipts are deposited to the general fund of the Department of the Treasury when collected.

Nonfederal Other Liabilities includes contract holdbacks on construction-in-progress payments and unfunded contingent liabilities for probable and reasonably possible losses for contract claims, civil litigation and tort claims.

#### **Other Information**

The USACE is not delinquent on any payments to the Department of Labor for the Federal Employees Compensation Act (FECA).

The USACE has completed the assessment of all real and personal property either partially or completely impaired by hurricanes Katrina, Rita, and Wilma, with all know impairments properly reflected in the financial statements. In conjunction with the assessment of assets, USACE has also completed its review of any potential liabilities, including environmental liabilities, which may have occurred due to the hurricanes with all known liabilities being properly recorded.

Judgment Fund Liabilities. The USACE Civil Works Directorate has recognized 37 unfunded liabilities arising from Judgment Fund Contract Disputes Act (CDA) settlements in accordance with the Interpretation of Federal Financial Accounting Standards No. 2, "Accounting for Treasury Judgment Fund Transactions." The USACE cannot fund the CDA claims since it is funded by projects and funding does not include an allowance for this type of claim. The USACE sought supplemental appropriations for payment of CDA claims in FY 2000 and FY 2006 which were not approved. The FY 2007 budget does not provide funding for payment of the CDA claims. The USACE will include a request for payment of the CDA claims in its FY 2008 budget.

#### **Capital Lease Liability**

The USACE has no capital lease liabilities.

### **Note 16. Commitments and Contingencies**

#### **Disclosures Related to Commitments and Contingencies:**

The US Army Corps of Engineers (USACE) is a party in various administrative proceedings and legal actions, with claims including environmental damage claims, equal opportunity matters, and contractual bid protests. The USACE has accrued contingent liabilities for legal actions where the USACE's Office of the General Counsel (OGC) considers an adverse decision probable and the amount of loss is measurable. In the event of an adverse judgment against the Government, some of the liabilities may be payable from the Judgment Fund. The USACE records Judgment Fund liabilities in Note 15, "Other Liabilities" and Note 12 "Accounts Payable."

Proprietary contingencies are commonly referred to as contingent liabilities. The USACE had 31 cases above the materiality threshold of \$7.2 million and OGC has determined that 4 cases were probable, 8 cases were unable to determine, and 19 were remote. Two of the probable cases were recorded as liabilities for \$40.0 million dollars and the amount was not determinable in the other two cases. The USACE management treated the eight cases that OGC was not able to determine as reasonably possible. The total amount of these eight claims is \$224.5 million and the potential loss is not determinable.

The USACE also has a total of \$330.0 million in pending contract claims, civil litigation and tort cases which were individually under the threshold of \$7.2 million. As such, the likelihood of an unfavorable outcome or potential liability is provided as an overall assessment of all cases currently pending and not on an individual basis (as with the over-threshold cases). The likelihood of an unfavorable or potential liability was determined by using a three-year historical average. The total dollar amount of the cases closed was divided by the total dollar amount claimed in those closed cases for each of the last three years which were then used to calculate the three year average of 10%. This average represents the percentage that has historically been paid on claims and is based entirely on historical data. The merits of each

individual case have not been taken into consideration. Based on the 10% average, a contingent liability of \$33.0 million was recorded.

The amounts disclosed for litigations, claims, and assessments are fully supportable and agree with USACE's legal representation letters and management summary schedule.

The USACE does not have undelivered orders for open contracts citing cancelled appropriations which may remain unfilled or unreconciled and for which the reporting entity may incur a contractual commitment for payment.

The USACE does not have contractual arrangements such as fixed price contracts with escalation, price redetermination, or incentive clauses; contracts authorizing variations in quantities; and contracts where allowable interest may become payable based on contractor claims under the "Dispute" clause contained in contracts.

The USACE is responsible for the Formerly Utilized Sites Remedial Action Program (FUSRAP), which was established to respond to radiological contamination from the early US Atomic Energy and Weapons Program. The FUSRAP program is funded through a Civil Works appropriation. The USACE recognizes liabilities related to this program but the liability amounts are currently unknown. The project sites are: St. Louis Downtown Site Inaccessible Soils, Iowa Army Ammunition Plant FUSRAP Site, Middlesex Sampling Plant Site Groundwater, Combustion Engineering Site, DuPont Chambers Works Site, W. R. Grace Radioactive Waste Disposal Area Site, Seaway Industrial Park Site, Niagara Falls Storage Site, Shallow Land Disposal Area Site, Former Harshaw Chemical Company Site, and Guterl Specialty Steel Site. Environmental liabilities not related to FUSRAP are currently unknown for the following project sites: Sonoma Firing Range and Sonoma Underground Storage Tanks Monitoring Wells in Sonoma, California; Black Rock Lock and Mount Morris Dam in New York; Bradford Island Landfill and North Pacific Division Materials Laboratory in Oregon; Saint Georges Bridge in Pennsylvania; and John H. Kerr Dam and Reservoir in Virginia.

Since these cases fail to satisfy the criteria to record a contingent liability in accordance with the Statement of Federal Financial Accounting Standard No. 5, "Accounting for Liabilities of the Federal Government," no amount is included in the financial statements.

## Note 17. Military Retirement and Other Federal Employment Benefits

As of September 30	2006				2005
	Present Value of Benefits	Assumed Interest Rate (%)	(Less: Assets Available to Pay Benefits)	Unfunded Liability	Present Value of Benefits
<i>(Amounts in thousands)</i>					
1. Pension and Health Actuarial Benefits					
A. Military Retirement Pensions	\$ 0		\$ 0	\$ 0	\$ 0
B. Military Retirement Health Benefits	0		0	0	0
C. Military Medicare-Eligible Retiree Benefits	0		0	0	0
D. Total Pension and Health Actuarial Benefits	\$ 0		\$ 0	\$ 0	\$ 0
2. Other Actuarial Benefits					
A. FECA	\$ 250,272	4.53%	\$ 0	\$ 250,272	\$ 0
B. Voluntary Separation Incentive Programs	0		0	0	0
C. DoD Education Benefits Fund	0		0	0	0
D. Total Other Actuarial Benefits	\$ 250,272		\$ 0	\$ 250,272	\$ 0
3. Other Federal Employment Benefits	\$ 303		\$ (303)	\$ 0	\$ 0
4. Total Military Retirement and Other Federal Employment Benefits:	\$ 250,575		\$ (303)	\$ 250,272	\$ 0

Actuarial Cost Method Used: The Department of the Army (DA) actuarial liability for workers' compensation benefits is developed by the Department of Labor (DOL) and provided to the DA at the end of each fiscal year. Actuarial Federal Employees' Compensation Act (FECA) liability includes the expected liability for death, disability, medical and miscellaneous costs for approved compensation cases. The actuarial liability is determined using a method that utilized historical benefit payment patterns to estimate the ultimate payments. The DOL is unable to provide a FECA actuarial liability specific to the US Army Corps of Engineers (USACE) Civil Works Program. The USACE Civil Works liability was included in the total DA amount provided by DOL. The USACE determined the actuarial liability by using a three year average of total USACE FECA bills as a percentage of the total Department of Army bills. That percentage was applied to the amount of actuarial liability of the total DA to arrive at USACE portion.

Assumptions: The projected annual benefit payments are discounted to the present value using the Office of Management and Budget economic assumptions for 10-year US Treasury notes and bonds. To provide more specifically for the effects of inflation on the liability for future workers' compensation benefits, wage inflation factors (cost of living allowance) and medical inflation factors are applied to the calculation of projected future benefits.

Market Value of Investments in Market-based and Marketable Securities: Does not apply to USACE.

**Fluctuations**

The increase of \$250.5 million (100%) in Other Actuarial Benefits – FECA is due to initial recording of the Federal Employees' Compensation Act (FECA) actuarial liability in 4th Quarter, FY 2006.

**Other Disclosures**

The constructed amount of \$ 240.0 million for the FY 2005 actuarial liability was determined using the three-year average method. This amount was not reported on the FY 2005 financial statements. The change in actuarial liability since the previous calculation is an increase of \$10.3 million.

The actuarial liability is computed for the USACE Civil Works Program.

Other Federal Employment Benefits consist of accrued civilian severance pay.

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

As of September 30	2006	2005
<i>(Amounts in thousands)</i>		
1. Intragovernmental Costs	\$ 1,336,192	\$ 1,378,785
2. Public Costs	9,860,164	8,882,498
3. Total Costs	<u>\$ 11,196,356</u>	<u>\$ 10,261,283</u>
4. Intragovernmental Earned Revenue	\$ (4,593,977)	\$ (2,152,799)
5. Public Earned Revenue	(510,951)	(428,778)
6. Total Earned Revenue	<u>\$ (5,104,928)</u>	<u>\$ (2,581,577)</u>
7. Net Cost of Operations	<u>\$ 6,091,428</u>	<u>\$ 7,679,706</u>

**Fluctuations**

Total Cost increased \$935.1 million. The increase was due to additional costs for flood control and coastal emergency efforts in support of the unprecedented hurricane season in the US Army Corps of Engineers (USACE) New Orleans, Vicksburg and Galveston districts. The costs include debris clean-up and removal, and purchases of ice, water and tarps for coverage of damaged roofs. The costs were initially recorded in 1st Quarter, FY 2006 and continued through 4th Quarter, FY 2006.

Total Earned Revenue increased \$2.5 billion (98%) mainly due to reimbursable work performed for the Federal Emergency Management Agency (FEMA) on the hurricane relief efforts in USACE New Orleans, Vicksburg, and Galveston districts. The increase in revenue for hurricane relief efforts in these districts was first reported 1st Quarter, FY 2006 due to hurricanes Katrina, Rita, and Wilma and continued through 4th Quarter, FY 2006.

**Other Information**

Intragovernmental costs and revenue are related to transactions made between two reporting entities within the federal government. Public costs and revenues are exchange transactions made between the reporting entity and a nonfederal entity.

The USACE was able to reconcile its intragovernmental costs and revenue balances with other Department of Defense trading partners that have systems which capture pertinent information. No material reconciling differences were identified. The USACE is unable to reconcile with other intragovernmental trading partners whose financial systems are not designed to capture pertinent information to fully reconcile intragovernmental transactions.

The Consolidated Statement of Net Cost (SoNC) 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 SoNC are based on obligations, disbursements, and accruals. The USACE records transactions on an accrual basis as required by generally accepted accounting principles.

There were no costs associated with acquiring, constructing, improving, reconstructing or renovating heritage assets or acquiring stewardship land.

The USACE Civil Works does not have military equipment.

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

As of September 30	2006		2005	
	Cumulative Results of Operations	Unexpended Appropriations	Cumulative Results of Operations	Unexpended Appropriations
<i>(Amounts in thousands)</i>				
1. Prior Period Adjustments Increases (Decreases) to Net Position Beginning Balance				
A. Changes in Accounting Standards	\$ 0	\$ 0	\$ 0	\$ 0
B. Errors and Omissions in Prior Year Accounting Reports	0	0	0	0
C. Total Prior Period Adjustments	\$ 0	\$ 0	\$ 0	\$ 0
2. Imputed Financing				
A. Civilian CSRS/FERS Retirement	\$ 92,355	\$ 0	\$ 97,212	\$ 0
B. Civilian Health	139,010	0	134,320	0
C. Civilian Life Insurance	402	0	397	0
D. Judgment Fund	29,857	0	9,652	0
E. IntraEntity	0	0	0	0
F. Total Imputed Financing	\$ 261,624	\$ 0	\$ 241,581	\$ 0

### Other Information

Appropriations on the Statement of Budgetary Resources (SBR) do not agree with appropriations received on the Statement of Changes in Net Position (SCNP) due to differences between proprietary and budgetary accounting concepts and reporting requirements. Appropriated trust, contributed, and special fund receipts in the amount of \$1.5 billion are included in appropriations on the SBR. These funds do not update the proprietary appropriations received amount reported on the SCNP.

The eliminations column on the Statement of Net Position reflects zero balances. All intra-entity eliminations that would appear on this statement are in the categories of transfers. The reciprocal accounts for transfers (transfers-in and out) all net on their respective transfers lines, and thus the zero balances.

## Note 20. Disclosures Related to the Statement of Budgetary Resources

As of September 30 <i>(Amounts in thousands)</i>	2006	2005
1. Net Amount of Budgetary Resources Obligated for Undelivered Orders at the End of the Period	\$ 3,985,839	\$ 2,419,101
2. Available Borrowing and Contract Authority at the End of the Period	0	0

### Other Information

**Apportionment Categories.** The amount of direct and reimbursable obligations incurred against amounts apportioned under Category A in the Statement of Budgetary Resources (SBR) includes: \$6.9 billion for direct; \$35.5 million for obligations exempt from apportionment; \$11.5 billion for reimbursable obligations; and \$88.0 thousand for reimbursable obligations exempt from apportionment. The US Army Corps of Engineers (USACE) has no apportionments under Category B. Undelivered orders presented in the SBR include undelivered orders-unpaid for both direct and reimbursable funds.

Category A apportionments distribute budgetary resources by fiscal quarter. Category B apportionments distribute budgetary resources by activity, project, object or a combination of these categories. Exempt budgetary resources are not subject to apportionment because they are not appropriated funds. Funding sources for exempt category comes from sources outside the federal government.

Intraentity transactions have not been eliminated because the statements are presented as combined and combining.

Borrowing authority is for capital improvements to the Washington Aqueduct. Funding to repay the debt is provided by Arlington County, Virginia, and the city of Falls Church, Virginia. Loan repayments are made on a quarterly basis, as required. A debt of \$13.9 million remains from the original \$75.0 million debt. During FY 2006, principal payments totaled \$659.1 thousand and interest payments totaled \$723.9 thousand.

No material adjustments were made to budgetary resources available at the beginning of the year.

**Permanent Indefinite Appropriations.** The USACE receives budget authority from trust funds established by the Department of the Treasury for Coastal Wetlands, Inland Waterways, Harbor Maintenance, and South Dakota Terrestrial Wildlife Habitat Restoration in order to maintain USACE's mission areas of water resources and environment. Special funds receive receipts from hydraulic mining in California; leases of land acquired for flood control, navigation, and allied purposes; and licenses under the Federal Power Act for improvements of navigable water including maintenance and operation of dams.

There are no legal arrangements that affect the use of unobligated balances of budget authority.

**Capital Infusion.** The USACE received a supplemental appropriation of \$2.9 billion during 2nd Quarter, FY 2006 for hurricane relief effort in the Gulf of Mexico and to address the Pandemic Influenza Act, 2006. A supplemental appropriation of \$3.7 billion was received during 3rd Quarter, FY 2006 for hurricane recovery and for global war on terror.

**Change in Reporting Procedure.** Per Office of Management and Budget Circular A-136, the parent agency should report the budgetary activity for allocation transfers. The child, USACE, shall report the activity relating to the allocation in all of its financial statements, except the SBR. Prior to 2nd Quarter, FY 2006, USACE reported an SBR in its financial statements for transfer funds. Beginning 2nd Quarter, FY 2006, adjustments are made to zero out the balances in the budgetary accounts imported from USACE's trial balances, except for the amount needed in allocation transfers to close out the beginning balance of total actual resources collected at FY 2006 yearend. Residual activity appears on the SBR derived from beginning balances in undelivered orders, delivered orders-unpaid, and allocations to be transferred. The Inland Waterways and Harbor Maintenance trust funds are not included in this change in reporting procedure because USACE is the lead agency for reporting and includes the parent budgetary activity in its financial statements, including the SBR.

## Note 21. Disclosures Related to the Statement of Financing

### Abnormal Balances

Revaluation of assets or liabilities has a negative balance because of an abnormal balance reported in the other losses account. This account has an abnormal balance of \$269.7 million. This is due to the reversal of \$255.6 million in construction in progress costs that were written off in FY 2004 for fish mitigation studies in the US Army Corps of Engineers' (USACE) Portland and Walla Walla districts. A decision was



made in FY 2006 to reverse the prior year loss and record the costs of the fish mitigation studies as an “other asset.” The USACE reversed \$49.4 million of the prior year loss in the 2nd Quarter, FY 2006. The remaining costs of \$206.2 million were reversed in the 3rd Quarter, FY 2006. The abnormal balance amount also includes \$17.1 million to place an asset in service that was previously written off in FY 2004 in the Louisville District. The asset was transferred to the leaseholder in error. The correcting entry was made in the 1st Quarter, FY 2006.

### Other Information

Budgetary data is in agreement with proprietary expenses and capitalized assets.

The USACE made no adjustment to the Statement of Financing to bring it into balance with the Statement of Net Cost.

The following Statement of Financing lines are presented as combined instead of consolidated due to interagency budgetary transactions not being eliminated:

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

### Composition of Other Resources or Adjustments to Net Obligated Resources that do not Affect Net Cost of Operations: Other

This includes asset donations. Adjustments for \$15.3 million for the value of land tracts donated in prior years were made in the USACE Kansas City, Savannah, and Ft. Worth districts. The USACE adjusted the value of the land tracts to the fair market value of the land at the time of the donation. These assets were previously recorded at zero or nominal value.

### Composition of Components Requiring or Generating Resources in Future Period: Other

This includes changes in actuarial liability for the Federal Employees Compensation Act (FECA). The amount also includes future funded expenses for contingent liabilities related to probable losses and reasonably possible losses for contract claims, civil litigation and tort claims against USACE; for new Judgment Fund Contract Dispute Act (CDA) claims; and for the increase in the amount of FECA expense recognized in FY 2006.

### Composition of Components not Requiring or Generating Resources: Other

This includes cost capitalization offset expense and other expenses not requiring budgetary resources. The cost capitalization offset account provides a mechanism to offset all direct costs in the expense accounts when those costs are subsequently capitalized into an in-process account. Other expenses not requiring budgetary resources includes current year expenses in the allocation transfer appropriations. Per Office of Management and Budget Circular A-136, the parent agency should report the budgetary activity for allocation transfers. The child, USACE, reports the activity related to the allocation in all of its financial statements except the Statement of Budgetary Resources (SBR). Therefore, current year expenses in the allocation transfer appropriations are reported as not requiring budgetary resources. Other expenses not requiring budgetary resources also includes reversing entries made in prior fiscal years that relate primarily to the write off of costs associated with non federal cost share projects. Current year costs associated with non-federal cost share projects in the Contributed Fund and costs related to Revolving Fund inventory sales are also recorded as other expenses not requiring budgetary resources.

### Allocation Transfers

The USACE recorded other expenses not requiring budgetary resources of \$195.7 million to reconcile budgetary activity with current period expenses for allocation transfers. The USACE received funds in FY 2006 from the following agencies for the listed transfer appropriations:

Department of Agriculture transferred funds to State and Private Forestry, Forest Service (96 12X1105) to assist in the treatment of disease in trees due to insect infestation at Rays Town Lake, Pennsylvania and Colsbrook Dam, Colorado.

Department of Transportation transferred funds to Federal Aid Highways (96 69X8083) for public bridge inventory and inspection in support of the Federal Lands Highway Program for FY 2005.

Department of Energy transferred funds to the Bonneville Power Administration (96 89X4045) for the maintenance of hydroelectric plants that USACE operates.

Department of Interior transferred funds to the Bureau of Land Management (BLM) Permit Processing Improvement Fund (96 14X5573) to expedite the review of jurisdictional and permit actions in the BLM pilot project offices located in Colorado, New Mexico, Utah, Wyoming, and Montana.

Appalachian Regional Commission transferred funds to USACE (96 46X0200) for design and construction assistance for public water and wastewater projects, water resource protection and development projects, and environmental restoration projects.

**Liabilities Not Covered by Budgetary Resources**

“Components Requiring or Generating Resources in Future Periods” reports unfunded expenses incurred in FY 2006 of \$327.0 million. The cumulative total of unfunded expenses from all fiscal years is reported as “Liabilities Not Covered by Budgetary Resources” in Note 11 totals \$2.9 billion. The difference of \$2.5 billion is due to the following:

Debt of \$13.6 million payable to Department of the Treasury for Borrowing Authority is unfunded. Arlington County, the city of Falls Church, Virginia, and the District of Columbia provide funding to repay the debt.

The offsetting custodial liability to accounts receivable for \$1.7 billion is unfunded. This amount will be deposited in the general fund of the Department of the Treasury and is primarily related to water storage contracts.

Future funded expense of \$46.8 million for Workmen’s Compensation liabilities under the Federal Employees Compensation Act (FECA) was recorded in prior fiscal years.

Future funded expense of \$162.6 million for CDA judgment fund claims was recognized in prior fiscal years.

The USACE recorded future funded expense for \$529.6 million in FY 2005 for unfunded environmental liabilities.

There is a difference of \$17.5 million between the current year unfunded liability for contracts with continuation clauses of \$4.3 million and the decrease in the amount of current year unfunded expense of \$21.8 million for the change in contracts with continuation clauses.

**Note 22. Disclosures Related to the Statement of Custodial Activity**

Not applicable.

**Note 23. Earmarked Funds**

BALANCE SHEET						
As of September 30						
<i>(Amounts in thousands)</i>						
	MRF	MERHCF	Other Earmarked Funds	Eliminations	Total	
<b>ASSETS</b>						
Fund balance with Treasury	\$ 0	\$ 0	\$ 603,213	\$ 0	\$ 603,213	
Investments	0	0	3,571,456	0	3,571,456	
Accounts and Interest Receivable	0	0	422,656	0	422,656	
Other Assets	0	0	841,708	0	841,708	
<b>Total Assets</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 5,439,033</b>	<b>\$ 0</b>	<b>\$ 5,439,033</b>	
<b>LIABILITIES and NET POSITION</b>						
As of September 30						
Military Retirement Benefits and Other Employment Related Actuarial Liabilities	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	
Other Liabilities	0	0	58,368	(138)	58,230	
Unexpended Appropriations	0	0	0	0	0	
Cumulative Results of Operations	0	0	5,380,665	207,476	5,588,141	
<b>Total Liabilities and Net Position</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 5,439,033</b>	<b>\$ 207,338</b>	<b>\$ 5,646,371</b>	
<b>STATEMENT OF NET COST</b>						
As of September 30						
Program Costs	\$ 0	\$ 0	\$ 1,115,922	\$ (28,974)	\$ 1,086,948	
Less Earned Revenue	0	0	(270)	253	( 17)	
<b>Net Program Costs</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 1,115,652</b>	<b>\$ (28,721)</b>	<b>\$ 1,086,931</b>	
Less Earned Revenues Not Attributable to Programs	0	0	0	0	0	
<b>Net Cost of Operations</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 1,115,652</b>	<b>\$ (28,721)</b>	<b>\$ 1,086,931</b>	
<b>STATEMENT OF CHANGES IN NET POSITION</b>						
As of September 30						
Net Position Beginning of the Period	\$ 0	\$ 0	\$ 4,781,544	\$ 0	\$ 4,781,544	
Net Cost of Operations	0	0	1,115,652	(28,721)	1,086,931	
Other Nonexchange Revenue	0	0	1,850,044	178,755	2,028,799	
Other Financing Sources	0	0	(135,271)	0	(135,271)	
<b>Change in Net Position</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 599,121</b>	<b>\$ 207,476</b>	<b>\$ 806,597</b>	
<b>Net Position End of Period</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 5,380,665</b>	<b>\$ 207,476</b>	<b>\$ 5,588,141</b>	

**Other Disclosures**

The Total Earmarked Funds column is shown as consolidated. All intra-Department of Defense (DoD) activity between earmarked funds and non-earmarked funds has been eliminated from this column, which causes assets to not equal liabilities and net position.

There has been no change in legislation during or subsequent to the reporting period and before the issuance of the financial statements that significantly changes the purpose of these funds or that redirects a material portion of the accumulated balances.

### **US Army Corps of Engineers (USACE) Earmarked Funds**

Special Recreation Use Fees, Title 16 United States Code (USC) 4061-6a, granted USACE the authority to charge and collect fair and equitable Special Recreation Use Fees at recreation facilities and campgrounds located at lakes or reservoirs under the jurisdiction of USACE. Types of allowable fees include daily use fees, admission fees, recreational fees, annual pass fees, and other permit type fees. The revenue is received from the public and is an inflow of resources to the government. It is intended to maintain and operate the recreation and camping facilities. This fund is classified as a special fund and utilizes both receipt and expenditure accounts in accounting for and reporting the fund.

Hydraulic Mining in California, Debris, Title 33 United States Code (USC) 683, states that those operating hydraulic mines through which debris flows in part or in whole to a body restrained by a dam or other work erected by the California Debris Commission shall pay a tax as determined by the Federal Energy Regulatory Commission (the Commission). The tax is paid annually on a date fixed by the Commission. Taxes imposed under this code are collected and then expended under the supervision of USACE and the direction of the Department of the Army. The revenue is received from the public and is an inflow of resources to the government. The purpose of the fund is for repayment of funds advanced by the federal government or other agency for construction, restraining works, settling reservoirs, and for maintenance. This fund is classified as a special fund and utilizes both receipt and expenditure accounts in accounting for and reporting the fund.

Payments to States, Flood Control Act of 1954, Title 33 USC 701c-3, establishes that 75% of all funds received and deposited from the leasing of lands acquired by the US for flood control, navigation and allied purposes, including the development of hydroelectric power, shall be returned to the state in which the property is located. The USACE collects lease receipts into a receipt account. The revenue is received from the public and is an inflow of resources to the government. Funds are appropriated in the amount of 75% of the receipts in the following fiscal year and disbursed to the states. This fund is classified as a special fund and utilizes both receipt and expenditure accounts in accounting for and reporting the fund.

Maintenance and Operation of Dams and Other Improvements of Navigable Waters, Title 16 USC 803(f), 810, states that whenever a reservoir or other improvement is constructed by the US, the Federal Power Commission, now known as the Federal Energy Regulatory Commission, shall assess charges against any licensee directly benefited, and any amount so assessed shall be paid into the Department of the Treasury. The USC further states that all charges arising from other licenses, except those charges established by the Commission for purpose of administrative reimbursement, shall be paid to the Department of the Treasury from which specific allocations will be made. From the specific allocations, 50% of charges from all other licenses is reserved and appropriated as a special fund in the Department of the Treasury. This special fund is to be expended under the direction of the Secretary of the Army for the maintenance and operation of dams and other navigation structures that are owned by the US or for construction, maintenance, or operation of headwater or other improvements of navigable waters of the US. This fund is classified as a special fund and utilizes both receipt and expenditure accounts in accounting for and reporting the fund. The revenue is received from the public and is an inflow of resources to the government.

Fund for Nonfederal Use of Disposal Facilities (for dredged material) was established by Title 33 USC 2326. This title provides that the Secretary of the Army (Secretary) may permit the use of any dredged material disposal facility under the jurisdiction of, or managed by, the Secretary by a nonfederal interest if the Secretary determines that such use will not reduce the availability of the facility for project purposes. The Secretary may impose fees to recover capital, operation and maintenance costs associated with such use. Any monies received through collection of fees under this law shall be available to the Secretary, and shall be used by the Secretary, for the operation and maintenance of the disposal facility from which the fees were collected. This fund is classified as a special fund and utilizes both receipt and expenditure accounts in accounting for and reporting the fund. The revenue is received from the public and is an inflow of resources to the government.

South Dakota Terrestrial Wildlife Habitat Restoration Trust Fund was established by Public Law 106-53, Sec. 603. Yearly transfers are made from the general fund of the Department of the Treasury to the trust fund for investment purposes. Investment activity is managed by the Department of the Treasury, Bureau of Public Debt (BPD). The BPD purchases and redeems nonmarketable market-based securities issued by the Department of the Treasury, BPD. Investments include one-day certificates, bonds, and notes. When the fund reaches the aggregate amount of \$108.0 million, withdrawals may be made by USACE for payment to the state of South Dakota. The state shall use the payments to fund the annually scheduled work for wildlife habitat restoration. This fund is classified as a trust fund and utilizes both receipt and expenditure accounts in accounting for and reporting the fund.

Coastal Wetlands Restoration Trust Fund is authorized by Title 16 USC 3951-3956. This act grants parallel authority to USACE, along with the Environmental Protection Agency and the Fish and Wildlife Service to work with the state of Louisiana to develop, review, evaluate, and approve a plan that is proposed to achieve a goal of "no net loss of wetlands" in coastal Louisiana. The USACE is also responsible for allocating funds among the named task force members. Federal contributions are established at 75% of project costs or 85% if the state has an approved Coastal Wetlands Conservation Plan. This fund is classified as a trust fund expenditure account and receives funding transfers from the Sport Fish Restoration and Boating Trust Fund.

Rivers and Harbors Contributed and Advance Funds, authorized by Title 33 USC 701h, 702f, and 703, establishes funding to construct, improve, and maintain levees, water outlets, flood control, debris removal, rectification and enlargement of river channels, etc., in the course of flood control and river/harbor maintenance. Whenever any state or political subdivision thereof shall offer to advance funds for a flood control project duly adopted and authorized by law, the Secretary of the Army may in his discretion, receive such funds and expend the same

in the immediate prosecution of such work. Advances are from the public and are inflows of resources to the government. This fund is classified as a trust fund and utilizes both receipt and expenditure accounts in accounting for and reporting the fund.

Inland Waterways Trust Fund is authorized by Title 26 USC 9506. The law made the Inland Waterways Trust Fund available for USACE expenditures for navigation, construction, and rehabilitation projects on inland waterways. Collections for excise taxes from the public are made into the trust fund. The collections are invested and investment activity is managed by the Department of the Treasury, BPD. The BPD purchases and redeems nonmarketable market-based securities issued by the Department of the Treasury, BPD. Investments include one-day certificates, bonds and notes. The fund is classified as a trust fund and utilizes receipt and expenditure accounts in accounting for and reporting the fund.

Harbor Maintenance Trust Fund was authorized by Title 26 USC 9505. The USACE Civil Works mission is funded by the Energy and Water Developments Appropriations Act (the Act). The Act of 1986 was implemented to cover a portion of USACE operations and maintenance costs for deep draft navigation. As provided in the act, amounts in the Harbor Maintenance Trust Funds shall be available for making expenditures to carry out the functions specified in the act and for the payment of all expenses of administration incurred by the Department of the Treasury, USACE, and the Department of Commerce. Collections are made into the trust fund from taxes collected from imports, domestics, passengers and foreign trade. The collections are invested and investment activity is managed by the Department of the Treasury, BPD. The revenue is received from the public and is an inflow of resources to the government. The fund is classified as a trust fund and utilizes receipt and expenditure accounts in accounting for and reporting the fund.

## **Note 24. Other Disclosures**

During FY 2006, the US Army Corps of Engineers (USACE) received \$68.8 million in direct appropriations from the Department of Energy, Power Marketing Administration, for operation and maintenance activities at hydroelectric power plants operated by USACE at the Portland, Seattle and Walla Walla districts.



## FY 2006 Required Supplementary Stewardship Information (RSSI)

### Federal Mission Property, Plant and Equipment Yearly Investment in Federal Mission Property, Plant and Equipment

For Fiscal Year Ended September 30, 2006

(In Millions of Dollars)

(a) Categories	(b) FY2002	(c) FY2003	(d) FY2004	(e) FY2005	(f) FY2006
1. Bank Stabilization Projects	nr	nr	\$74	\$59	\$67
TOTAL:			\$74	\$59	\$67

#### Narrative Statement:

Investments in Federal Mission Property, Plant and Equipment refer to those expenses incurred by USACE for the protection of the riverbanks of the Mississippi River and other navigable waterways inside the continental United States. Stabilization and protection of the riverbanks are important to the flood control and navigation plans, serving to protect flood control features and to insure the desired alignment of the river's navigation channel. Stabilizing the riverbanks and channels provide an efficient navigation alignment, increase the flood-carrying capacity of the river, and or protection of the levees system to include the tributary basin improvements for major drainage. The process by which this is accomplished is by; cutoffs (shortening the river and reducing flood heights), revetment (controlling the river's meandering), dikes (directing the flow), and improvement dredging (realigning the river/channel).

#### Notes:

- For FY 2002 – 2003 USACE does not have historical data as FY04 was our first reporting of Federal Mission Property, Plant and Equipment in the Required Supplementary Stewardship Information section of the financial statements. (nr = Nonreporting)
- After major floods in 1882, 1912, 1913 and 1927 the Flood Control Act of 1928 was signed which committed the federal government to a definite program of flood control. This legislation authorized the Mississippi River and Tributaries Project, the nation's first comprehensive flood control and navigation act.
- Investments values included in this report are based on Nonfederal Physical Property outlays (expenditures). Outlays are used because current DOD systems are unable to capture and summarize costs in accordance with the Federal Accounting Standards requirements.

### Heritage Assets

For Fiscal Year Ended September 2006

(a)	(b) Measurement Quantity	(c) As of 10/01/05	(d) Additons	(e) Deletions	(f) As of 9/30/06
Museums	Each	1	0	0	1
Monuments & Memorials	Each	1	0	0	1
Cemeteries	Sites	0	0	0	0
Archeological Sites	Sites	142	0	0	142
Buildings & Structure	Each	349	1	0	350
Major Collections	Each	1	0	1	0

#### Narrative Statement

USACE administers the Lake Superior Marine Museum as part of the Operations and Maintenance Mission of the Detroit District. This museum has gone inadvertently unreported in previous submittals on USACE Heritage Assets.

The USACE has one Major Collection of historical memorabilia, historic artifacts, and records that is managed by the USACE Office of History. A previously reported major collection was removed this year as a result of a recent Government Accountability Office (GAO) audit. The audit determined that the collection, administered by the USACE Office of History, is a U.S. Army Major Collection housed by USACE and is reported by Army's Center for Military History as part of their property inventory.

Other than multipurpose heritage assets, heritage assets are not material to the mission of the USACE. Disclosures pertinent to multipurpose heritage assets are contained in the financial statements.

Heritage assets classified as Land are special land plots containing archaeological sites as listed on the National Register of Historic Places or eligible to be listed.

Heritage assets on display are assumed to be in adequate condition for display purposes, consistent with their origins, unless otherwise noted. Reported heritage assets are free of material conditions that are counter to safeguarding, adequately protecting, and properly managing those assets; they have not materially degraded while under the care of USACE. The existence of most of the un-categorized heritage assets is informally known to be adequate for display purposes, however, the condition of many un-categorized assets are unknown.

Cemeteries and Archeological Sites are archeological properties listed on or eligible for, the National Register of Historic Places. These archeological assets cover almost the entire range of human occupation of the Continental United States beginning with the Kennewick Man Discovery Site in Washington State, dating to approximately 10,000 years before present, to archeological remains of early European-American settlements such as Fort Independence in Georgia.

Buildings and Structures include a range of historic resources from a covered bridge in Sacramento District to early farming structures in Savannah District. It also includes some non-traditional structures such as a snag boat that operated on the Mississippi River. A new building and associated historic district, Conchas Dam and Conchas Dam Historic District, New Mexico was added to USACE inventory. One new historic building has been submitted to the National Register of Historic Places for listing this period.

<b>Non-federal Physical Property</b>					
<b>Yearly Investment in State and Local Governments</b>					
For Fiscal Year Ended September 30, 2006					
<i>(In Millions of Dollars)</i>					
(a) Categories	(b) FY2002	(c) FY2003	(d) FY2004	(e) FY2005	(f) FY2006
<b>Transferred Assets:</b>					
1. Federal Mission Related	nr	nr	\$4,429	\$1,324	\$1,229
<b>Funded Assets:</b>					
2. Federal Mission Related	nr	nr	0	0	0
<b>Total</b>			\$4,429	\$1,324	\$1,229

**Narrative Statement:**

Investments in Non-federal Property refers to those expenses incurred by USACE for the purchase, construction or major renovation of physical property owned by State and Local Governments, including major additions and replacements; the purchase of major equipment; and the purchase of improvement of other physical assets. The authority to enter into cost share agreements with nonfederal sponsors is governed under numerous Water Resources Development Acts starting with the Act of 1992.

**Notes:**

- For FY 2002 – 2003 USACE does not have historical data as FY04 was our first reporting of Non-federal Physical Property in the Required Supplementary Stewardship Information. The variance in the FY04 and FY05 amounts is due to FY04 figure being a first report cumulative number and the FY05 number is for FY05 cost share. (nr = Nonreporting)
- Under numerous authorities USACE provides design, build and construction services/management for the missions of commercial navigation, flood/storm damage reduction, hydropower, regulatory, environmental, recreation and water supply.
- Investments values included in this report are based on Non-federal Physical Property outlays (expenditures). Outlays are used because current DOD systems are unable to capture and summarize costs in accordance with the Federal Accounting Standards requirements.



<b>General Property, Plant and Equipment</b>	
<b>Real Property Deferred Maintenance Amounts</b>	
<i>As of September 30, 2006</i>	
(a)	(b)
Property Type/Major Class	
1. Real Property	
A. Buildings	0
B. Structures	\$1,846,659
2. Total	\$1,846,659

**Narrative Statement:**

Deferred maintenance at Civil Works water resources projects operated and maintained by the U.S. Army Corps of Engineers was determined through the budget development process whereby operations managers identify the operation and maintenance (O&M) needs at each project in the Civil Works inventory. O&M needs are based on inspections of project features, engineering analyses and historical experience.

**STATEMENT OF DISAGGREGATED BUDGETARY RESOURCES**

As of September 30, 2006 and 2005 (\$ in Thousands)

	Civil Works	2006 Combined	2005 Combined
<b>BUDGETARY FINANCING ACCOUNTS</b>			
<b>BUDGETARY RESOURCES</b>			
Unobligated balance, brought forward, October 1	\$ 5,003,186	\$ 5,003,186	\$ 1,693,278
Recoveries of prior year unpaid obligations	0	0	0
Budget authority			
Appropriation	12,439,718	12,439,718	5,987,913
Borrowing authority	0	0	0
Contract authority	0	0	0
Spending authority from offsetting collections			
Earned			
Collected	9,407,099	9,407,099	6,471,705
Change in receivables from Federal sources	1,690,685	1,690,685	11,130
Change in unfilled customer orders			
Advance received	22,685	22,685	(34,324)
Without advance from Federal sources	(719,532)	(719,532)	3,306,341
Anticipated for rest of year, without advances	0	0	0
Previously unavailable	0	0	0
Expenditure transfers from trust funds	0	0	0
Subtotal	\$ 22,840,655	\$ 22,840,655	\$ 15,742,765
Nonexpenditure transfers, net, anticipated and actual	(8,068)	(8,068)	257,392
Temporarily not available pursuant to Public Law	(10,000)	(10,000)	(10,000)
Permanently not available	(54,490)	(54,490)	(38,390)
<b>Total Budgetary Resources</b>	<b>\$ 27,771,283</b>	<b>\$ 27,771,283</b>	<b>\$ 17,645,045</b>
<b>Status of Budgetary Resources:</b>			
Obligations incurred:			
Direct	\$ 6,902,331	\$ 6,902,331	\$ 5,739,464
Reimbursable	11,500,680	11,500,680	6,902,397
Subtotal	18,403,011	18,403,011	12,641,861
Unobligated balance:			
Apportioned	8,621,365	8,621,365	4,421,128
Exempt from apportionment	746,850	746,850	581,999
Subtotal	9,368,215	9,368,215	5,003,127
Unobligated balance not available	57	57	57
<b>Total status of budgetary resources</b>	<b>\$ 27,771,283</b>	<b>\$ 27,771,283</b>	<b>\$ 17,645,045</b>
<b>Change in Obligated Balance:</b>			
Obligated balance, net			
Unpaid obligations, brought forward, October 1	3,945,373	3,945,373	3,171,189
Less: Uncollected customer payments from Federal sources, brought forward, October 1	\$ (5,449,985)	\$ (5,449,985)	\$ (2,132,513)
Total unpaid obligated balance	(1,504,612)	(1,504,612)	1,038,676
Obligations incurred net (+/-)	\$ 18,403,011	\$ 18,403,011	\$ 12,641,861
Less: Gross outlays	(16,870,276)	(16,870,276)	(11,867,676)
Obligated balance transferred, net			
Actual transfers, unpaid obligations (+/-)	0	0	0
Actual transfers, uncollected customer payments from Federal sources (+/-)	0	0	0
Total Unpaid obligated balance transferred, net	0	0	0
Less: Recoveries of prior year unpaid obligations, actual	0	0	0
Change in uncollected customer payments from Federal sources	(971,152)	(971,153)	(3,317,471)
Obligated balance, net, end of period			
Unpaid obligations	5,478,110	5,478,111	3,945,373
Less: Uncollected customer payments (+/-) from Federal sources (-)	(6,421,138)	(6,421,138)	(5,449,985)
Total, unpaid obligated balance, net, end of period	(943,028)	(943,027)	(1,504,612)
<b>Net Outlays</b>			
<b>Net Outlays:</b>			
Gross outlays	16,870,275	16,870,276	11,867,676
Less: Offsetting collections	(9,429,788)	(9,429,787)	(6,437,381)
Less: Distributed Offsetting receipts	(1,906,618)	(1,906,618)	(1,744,668)
<b>Net Outlays</b>	<b>\$ 5,533,871</b>	<b>\$ 5,533,871</b>	<b>\$ 3,685,627</b>

Department of Defense - US Army Corps of Engineers

**STATEMENT OF DISAGGREGATED BUDGETARY RESOURCES**

As of September 30, 2006 and 2005 (\$ in Thousands)

	Civil Works	2006 Combined	2005 Combined
<b>NONBUDGETARY FINANCING ACCOUNTS</b>			
<b>BUDGETARY RESOURCES</b>			
Unobligated balance, brought forward, October 1	\$ 0	\$ 0	\$ 0
Recoveries of prior year unpaid obligations	0	0	0
Budget authority			
Appropriation	0	0	0
Borrowing authority	0	0	0
Contract authority	0	0	0
Spending authority from offsetting collections			
Earned			
Collected	0	0	0
Change in receivables from Federal sources	0	0	0
Change in unfilled customer orders			
Advance received	0	0	0
Without advance from Federal sources	0	0	0
Anticipated for rest of year, without advances	0	0	0
Previously unavailable	0	0	0
Expenditure transfers from trust funds	0	0	0
Subtotal	0	0	0
Nonexpenditure transfers, net, anticipated and actual	0	0	0
Temporarily not available pursuant to Public Law	0	0	0
Permanently not available	0	0	0
<b>Total Budgetary Resources</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 0</b>
<b>Status of Budgetary Resources:</b>			
Obligations incurred:			
Direct	\$ 0	\$ 0	\$ 0
Reimbursable	0	0	0
Subtotal	0	0	0
Unobligated balance:			
Apportioned	0	0	0
Exempt from apportionment	0	0	0
Subtotal	0	0	0
Unobligated balance not available	0	0	0
<b>Total Status of Budgetary Resources</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 0</b>
<b>Change in Obligated Balance:</b>			
Obligated balance, net			
Unpaid obligations, brought forward, October 1	0	0	0
Less: Uncollected customer payments from federal sources, brought forward, October 1	\$ 0	\$ 0	\$ 0
Total unpaid obligated balance	0	0	0
Obligations incurred net (+/-)	\$ 0	\$ 0	\$ 0
Less: Gross outlays	0	0	0
Obligated balance transferred, net			
Actual transfers, unpaid obligations (+/-)	0	0	0
Actual transfers, uncollected customer payments from Federal sources (+/-)	0	0	0
Total Unpaid obligated balance transferred, net	0	0	0
Less: Recoveries of prior year unpaid obligations, actual	0	0	0
Change in uncollected customer payments from Federal sources (+/-)	0	0	0
Obligated balance, net, end of period			
Unpaid obligations	0	0	0
Less: Uncollected customer payments (+/-) from Federal sources (-)	0	0	0
Total, unpaid obligated balance, net, end of period	0	0	0
<b>Net Outlays</b>			
<b>Net Outlays:</b>			
Gross outlays	0	0	0
Less: Offsetting collections	0	0	0
Less: Distributed Offsetting receipts	0	0	0
<b>Net Outlays</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 0</b>

**Required Supplemental Information - Part A**

**AT96 - US Army Corps of Engineers**

*(\$ Amounts in Thousands)*

<b>Schedule, Part A</b>	<b>Treasury Index</b>	<b>Fund Balance with Treasury</b>	<b>Accounts Receivable</b>	<b>Loans Receivable</b>	<b>Investments</b>	<b>Other</b>
<b>DoD Intra-governmental Asset Balances</b>						
Unidentifiable Federal Agency Entity (Other than DoD entities)	0		\$1,033			
The Judiciary	10		\$11			
Department of Agriculture	12		\$169			
Department of Commerce	13		\$140			
Department of the Interior	14		\$394,149			
Department of Justice	15		\$115			
Department of Labor	16		\$46			
Navy General Fund	17		\$770			
United States Postal Service	18		\$34			
Department of State	19		\$1,019			
Department of the Treasury	20	\$8,147,352	\$12		\$3,571,456	
Army General Fund	21		\$5,675			
Social Security Administration	28		\$1			
Nuclear Regulatory Commission	31		\$6			
John F. Kennedy Center	33		\$37			
Department of Veterans Affairs	36		\$627			
General Service Administration	47		\$1			
National Science Foundation	49		\$7			
Air Force General Fund	57		\$941			
Railroad Retirement Board	60		\$0			
Tennessee Valley Authority	64		\$217			
Environmental Protection Agency	68		\$14,731			
Department of Transportation	69		\$997			
Homeland Security	70		\$1,885,497			
Agency for International Development	72		\$145			
American Battle Monuments	74		\$6			
Department of Health and Human Services	75		\$0			
National Aeronautics and Space Administration	80		\$17			
Department of Housing and Urban Development	86		\$5			
Department of Energy	89		\$73,842			
Independent Agencies	95		\$5			
Other Defense Organizations General Funds	97		\$450			
Army Working Capital Fund	97-4930.001		\$0			
The General Fund of the Treasury	99		\$26,614			
Architect of the Capitol			\$239			
<b>Totals might not match reports</b>	<b>Totals:</b>	<b>\$8,147,352</b>	<b>\$2,407,558</b>		<b>\$3,571,456</b>	

## Required Supplemental Information - Part B

### AT96 - US Army Corps of Engineers

(\$ Amounts in Thousands)

Schedule, Part B DoD Intra-governmental entity liabilities	Treasury Index	Accounts Payable	Debts/Borrowings From Other Agencies	Other
Unidentifiable Federal Agency Entity (Other than DoD entities)	0			\$43
Department of Agriculture	12	\$396		\$6
Department of Commerce	13	\$4,929		\$1,659
Department of the Interior	14	\$9,978		\$2,362
Department of Justice	15	\$48		\$2
Department of Labor	16			\$47,746
Navy General Fund	17	\$518		
United States Postal Service	18	\$0		
Department of State	19	\$746		\$379
Department of the Treasury	20	\$1,563	\$13,924	\$164,221
Army General Fund	21	\$9,879		\$0
Office of Personnel Management	24	\$4		\$13,830
Library of Congress	3	\$12		
Government Printing Office	4	\$182		
General Service Administration	47	\$15,545		\$163
Air Force General Fund	57	\$32		
Tennessee Valley Authority	64	\$1,580		
Environmental Protection Agency	68	\$247		\$34
Department of Transportation	69	\$90		
Homeland Security	70	\$9,263		\$19
Small Business Administration	73			\$1
Department of Health and Human Services	75	\$352		\$3,454
Department of Energy	89	\$2,302		\$1,712
Other Defense Organizations General Funds	97	\$255		
Other Defense Organizations Working Capital Funds	97-4930	\$8,930		
Army Working Capital Fund	97-4930.001	\$40		
Navy Working Capital Fund	97-4930.002	\$338		
The General Fund of the Treasury	99	\$26,614		\$1,751,940
<b>Totals might not match reports</b>	<b>Totals:</b>	<b>\$93,843</b>	<b>\$13,924</b>	<b>\$1,987,571</b>

## Required Supplemental Information - Part C

### AT96 - US Army Corps of Engineers

(\$ Amounts in Thousands)

Schedule, Part C	Treasury Index	Earned Revenue
<b>DoD Intra-governmental revenue and related costs</b>		
Unidentifiable Federal Agency Entity (Other than DoD entities)	0	\$1,813
The Judiciary	10	\$22
Department of Agriculture	12	\$12,035
Department of Commerce	13	\$8,987
Department of the Interior	14	\$18,363
Department of Justice	15	\$11,294
Department of Labor	16	\$39
Navy General Fund	17	\$4,953
United States Postal Service	18	\$164
Department of State	19	\$6,788
Department of the Treasury	20	\$1,020
Army General Fund	21	\$868,523
Office of Personnel Management	24	\$1,261
Social Security Administration	28	\$2
Nuclear Regulatory Commission	31	\$451
John F. Kennedy Center	33	\$1,622
Department of Veterans Affairs	36	\$4,434
General Service Administration	47	\$1,038
National Science Foundation	49	\$1,070
General Accounting Office	5	\$654
Air Force General Fund	57	\$45,409
Railroad Retirement Board	60	\$1
Tennessee Valley Authority	64	\$145
Environmental Protection Agency	68	\$71,944
Department of Transportation	69	\$9,933
Homeland Security	70	\$3,416,315
Agency for International Development	72	\$11,506
Department of Health and Human Services	75	\$5,028
National Aeronautics and Space Administration	80	\$8,780
Department of Housing and Urban Development	86	\$1,187
Department of Energy	89	\$33,202
Department of Education	91	\$9
Independent Agencies	95	\$1,374
Other Defense Organizations General Funds	97	\$39,038
Other Defense Organizations Working Capital Funds	97-4930	\$339
Army Working Capital Fund	97-4930.001	\$0
Navy Working Capital Fund	97-4930.002	\$947
Air Force Working Capital Fund	97-4930.003	\$127
Architect of the Capitol		\$3,715
<b>Totals might not match reports</b>	<b>Totals:</b>	<b>\$4,593,532</b>

## Required Supplemental Information - Part E

### AT96 - US Army Corps of Engineers

*(\$ Amounts in Thousands)*

Schedule, Part E DoD Intra-governmental non-exchange revenue	Treasury Index	Transfers In	Transfers Out
Department of Agriculture	12	\$24	\$34
Department of the Interior	14	\$63,775	
Army General Fund	21		\$35
Air Force General Fund	57	\$0	
Department of Transportation	69	\$904	
Department of Health and Human Services	75		\$29
Department of Energy	89	\$249,200	
The General Fund of the Treasury	99	(\$11,213)	\$10,000
<b>Totals might not match reports</b>	<b>Totals:</b>	<b>\$302,690</b>	<b>\$10,098</b>







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

November 8, 2006

MEMORANDUM FOR THE CHIEF OF ENGINEERS, U.S. ARMY CORPS OF ENGINEERS

SUBJECT: Independent Auditor's Report on the FY 2006 U.S. Army Corps of Engineers, Civil Works, Financial Statements (Report No. D 2007 016)

The Chief Financial Officers Act of 1990, as amended, requires the Department of Defense Inspector General to audit the accompanying U.S. Army Corps of Engineers, Civil Works, (USACE) Consolidated Balance Sheet as of September 30, 2006 and 2005, the related Consolidated Statement of Net Cost, the Consolidated Statement of Changes in Net Position, the Combined Statement of Budgetary Resources, and the Combined Statement of Financing for the fiscal years then ended. The financial statements are the responsibility of USACE management. USACE is also responsible for implementing effective internal control and for complying with laws and regulations. We are unable to give an opinion on the USACE FY 2006 financial statements because of limitations on the scope of our work. Thus, the financial statements may be unreliable. In addition to our disclaimer of opinion on the financial statements, we are including the required Report on Internal Control and Compliance with Laws and Regulations. The Report on Internal Control and Compliance with Laws and Regulations is an integral part of our disclaimer of opinion on the financial statements and should be considered in assessing the results of the audit.

### Disclaimer of Opinion on the Financial Statements

USACE asserted to us that the USACE FY 2006 Financial Statements are fairly presented in accordance with generally accepted accounting principles. Because USACE management asserted that the financial statements are free of material error and that all corrective actions from previously identified material deficiencies were completed, we performed auditing procedures to determine whether material amounts on the financial statements were fairly presented. However, time constraints precluded us from performing sufficient audit work to complete the audit. Therefore, we are unable to determine whether material amounts on the financial statements were fairly presented. Prior audits have identified material weaknesses listed in the Summary of Internal Control. These material weaknesses also affect the reliability of certain information contained in the annual financial statements—much of which is taken from the same data sources as the basic financial statements.<sup>1</sup> Therefore, we are unable to express, and we do not express, an opinion on the basic financial statements. Additionally, the purpose of the audit was not to express an opinion on the information accompanying the basic financial statements. Accordingly, we express no opinion on the accompanying information.

### Summary of Internal Control

In planning our audit, we considered USACE internal control over financial reporting and compliance. We did this to determine our procedures for auditing the financial statements and to comply with Office of Management and Budget guidance, but our purpose was not to express an opinion on internal control. Accordingly, we do not express an opinion on

<sup>1</sup> The annual financial statements include the basic financial statements, management discussion and analysis, consolidating and combining financial statements, Required Supplementary Stewardship Information, Required Supplementary Information, and Other Accompanying Information.

internal control over financial reporting and compliance. Time constraints precluded us from performing sufficient audit work to assess internal control over financial reporting and compliance or to follow up on previously identified reportable conditions listed below, all of which were deemed to be material.

- Fund Balance With Treasury and Unexpended Appropriations
- Accounts Receivable
- General Property, Plant, and Equipment
- Accounts Payable
- Financial Statement Compilation
- Financial Management Systems

However, USACE management has asserted that all corrective actions from previously identified material deficiencies were completed.

Material weaknesses are reportable conditions in which internal controls do not reduce (to a relatively low level) the risk of misstatements that are material to the financial statements and that might not be timely detected by employees while performing their normal assigned functions.

Reportable conditions are matters coming to the auditor’s attention that, in his or her judgment, should be communicated to management because they represent significant deficiencies in the design or operation of internal control, which could adversely affect the organization’s ability to initiate, record, process, and report financial data consistent with the assertions of management in financial statements. Our internal control work (conducted during prior audits) would not necessarily disclose all reportable conditions. The Attachment offers details on the reportable conditions listed above.

## **Summary of Compliance with Laws and Regulations**

Our work to determine compliance with selected provisions of applicable laws and regulations related to financial reporting was limited because time constraints precluded us from performing sufficient audit work to complete the review. Prior audits identified instances of noncompliance; however, USACE management has asserted that all corrective actions from previously identified material deficiencies were completed. See the Attachment for details on compliance with laws and regulations. USACE asserted to us that its financial management system comply substantially with Federal financial management systems requirements, applicable Federal accounting standards, and the U.S. Standard General Ledger at the transaction level, as required by the Federal Financial Management Improvement Act of 1996.

The Department of Defense Inspector General and the Government Accountability Office previously disclosed instances of noncompliance with the following.

- Federal Managers’ Financial Integrity Act of 1982
- Office of Management and Budget Circulars:
  - A-123, “Management Accountability and Control”
  - A-127, “Federal Management Systems”
  - A-130, “Management of Federal Information Resources”

## Management Responsibility

Management is responsible for:

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



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

Attachment:  
As stated

---

<sup>2</sup> The information was reported in GAO Report No. GAO-02-589, "Corps of Engineers Making Improvements, But Weaknesses Continue," June 2002; GAO Report No. GAO-01-89, "Significant Weaknesses in Corps of Engineers' Computer Controls," October 2000; and DoD IG Report No. D-2004-115, "Information System Security: The Followup on the Government Accountability Office and U.S. Army Audit Agency Recommendations for the U.S. Army Corps of Engineers (FOUO)," September 21, 2004.



## Report on Internal Control and Compliance with Laws and Regulations

### Internal Control

Management is responsible for implementing and maintaining effective internal control and for providing reasonable assurance that accounting data are accumulated, recorded, and reported properly; the requirements of applicable laws and regulations are met; and assets are safeguarded against misappropriation and abuse. USACE management has asserted that all corrective actions from previously identified material deficiencies were completed. Time constraints precluded us from performing sufficient audit work to assess internal control over financial reporting and compliance or to follow up on previously identified reportable conditions. Therefore, we do not express an opinion on internal control over financial reporting. However, we have previously identified the following material weaknesses and reportable conditions that could adversely affect a favorable opinion on internal control.

**Fund Balance With Treasury and Unexpended Appropriations.** USACE did not comply with generally accepted accounting principles in that it recorded improper funding transactions in the Corps of Engineers Financial Management System for the Fund Balance With Treasury and Unexpended Appropriations accounts. Furthermore, USACE did not establish Fund Balance With Treasury accounts in the Corps of Engineers Financial Management System for expenditure and receipt accounts as required by the United States Code and assigned by Department of Treasury and also omitted transactions applicable to the accounts. Finally, USACE commingled appropriation warrants and nonexpenditure transfers in the Corps of Engineers Financial Management System subsidiary accounts for Fund Balance With Treasury. As a result, USACE did not maintain reliable funding information in the Corps of Engineers Financial Management System for the Fund Balance With Treasury and Unexpended Appropriations accounts.

USACE erroneously reported unprocessed interagency transfer collections (that is, USACE reported collections that had not yet occurred) to the Department of Treasury and the Office of Management and Budget. In addition, the USACE revolving fund created unreconciled collection and disbursement differences. As a result, USACE did not report reliable Fund Balance With Treasury amounts to the Department of Treasury and the Office of Management and Budget.

**Accounts Receivable.** USACE Districts did not provide adequate source data and needs to improve the reconciliation of the general ledger to the subsidiary records for specific samples reviewed.

### General Property, Plant, and Equipment

**Buildings, Structures, and Facilities.** Deficiencies were noted involving useful lives, support for asset values, placed-in-service dates, asset classification (including bank stabilization), physical existence, and capital lease recording.

We identified a systemic weakness involving adjustments to useful lives in the Corps of Engineers Financial Management System. Specifically, the Corps of Engineers Financial Management System did not always distribute depreciation accurately across the life of buildings and structures, which affected the book value, accumulated depreciation, and the balance of the Buildings, Structures, and Facilities line item.

**Construction-in-Progress.** Deficiencies were noted involving the timely transfer of completed assets, the capitalization of expense-type events, non-Federal cost share projects, prior Construction-in-Progress errors, negative Construction-in-Progress, and other variances.

**Equipment.** Deficiencies were noted involving the lack of adequate documentation to support equipment values.

**Land.** Deficiencies were noted involving land costs originating in the Corps of Engineers Management Information System and land costs originating in the Corps of Engineers Financial Management System and with classification of reservoir costs.

**Accounts Payable.** USACE improperly recorded payables, did not properly review aged payables, did not record payables in the proper accounting period, and were unable to provide supporting documentation in a timely manner.

**Financial Statement Compilation.** The review of the FY 2004 year-end financial statement compilation process disclosed significant deficiencies in unsupported journal vouchers and undocumented differences in trial balance data. In addition, deficiencies existed with the Corps of Engineers Financial Management System general ledger correlations.

**Financial Management Systems.** In FY 2005, USACE acknowledged that its financial management systems do not fully comply with Federal financial management system requirements, applicable Federal accounting standards, and the U.S. Standard General Ledger at the transaction level. However, until we verify the USACE FY 2006 assertion that its financial management systems comply substantially with Federal financial management system requirements, applicable Federal accounting standards, and the U.S. Standard General Ledger at the transaction level, the possibility exists that USACE general and application computer control vulnerabilities make it difficult for USACE to ensure the reliability, confidentiality, and availability of financial and other sensitive data.

## Compliance with Laws and Regulations

Management is responsible for compliance with existing laws and regulations related to financial reporting. Our work to determine compliance with selected provisions of the applicable laws and regulations was limited because time constraints precluded us from performing sufficient audit work to complete the review. Prior audits identified instances of noncompliance; however, USACE management has asserted that all corrective actions from previously identified material deficiencies were completed. Therefore, we did not determine whether USACE was in compliance with selected provisions of all applicable laws and regulations related to financial reporting. Thus, we do not express an opinion on compliance with applicable laws and regulations.

USACE asserted to us that its financial management systems comply substantially with Federal financial management system requirements, applicable Federal accounting standards, and the U.S. Standard General Ledger at the transaction level, as required by the Federal Financial Management Improvement Act of 1996. Time constraints precluded us from performing sufficient audit work to determine whether USACE complied with all applicable laws and regulations related to financial reporting. However, the Department of Defense Inspector General and the Government Accountability Office audits previously established that USACE did not fully comply with the following financial management system reporting requirements.

- The Federal Managers’ Financial Integrity Act of 1982 requires agencies to evaluate the systems and to annually report whether those systems are in compliance with applicable requirements. When systems are not compliant, the statement must include a report of material weaknesses in accounting and administrative internal control with plans and a schedule for correcting the material weaknesses.
- Office of Management and Budget Circular A-123, revised June 21, 1995, requires agencies and individual Federal managers to take systematic and proactive measures to assess the adequacy of management controls in Federal programs and operations, identify needed improvements, take corresponding corrective actions, and report annually on management controls.
- Office of Management and Budget Circular A-127, revised July 23, 1993, requires agencies to develop, operate, evaluate, and report on financial management systems. It also requires that financial management systems provide complete, reliable, consistent, timely, and useful information.
- Office of Management and Budget Circular A-130, Appendix III:
  - establishes a minimum set of controls to be included in Federal automated information security programs,
  - assigns Federal agencies responsibilities for the security of automated information, and
  - links agency information security programs and agency management control systems established in accordance with Office of Management and Budget Circular A-123.

According to prior Government Accountability Office audit reports, USACE did not fully comply with the Federal Managers' Financial Integrity Act of 1982 and the Office of Management and Budget Circulars A-123 and A-130 requirements to protect the integrity of its financial management systems, identify needed improvements, and take corresponding corrective actions. During FY 2004, the Department of Defense Inspector General reviewed previously identified Government Accountability Office deficiencies related to general and application controls. The Department of Defense Inspector General audit report concluded that USACE had not fully implemented all of the Government Accountability Office recommendations. During FY 2006, USACE asserted that it substantially completed the prior Government Accountability Office recommendations. However, time constraints precluded us from performing sufficient audit work to determine whether USACE complied with all applicable laws and regulations related to financial reporting.

### **Audit Disclosures**

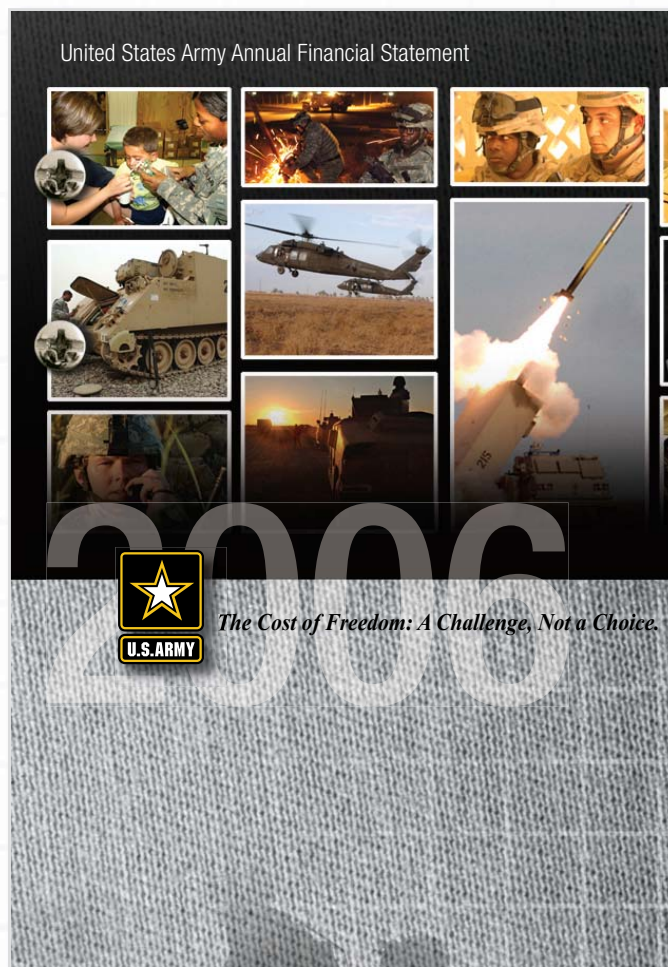
We did not perform audit work related to the following selected provisions of laws and regulations.

- Antideficiency Act
- Federal Credit Reform Act of 1990
- Pay and Allowance System for Civilian Employees
- Prompt Payment Act
- Provisions Governing Claims of the U.S. Government (including provisions of the Debt Collection Improvement Act of 1996)

This report does not include recommendations to correct the material internal control weaknesses and noncompliance with laws and regulations because previous audit reports contained recommendations for corrective actions.







We are interested in your feedback regarding the content of this report.  
Please feel free to e-mail your comments to [AAFS@hqda.army.mil](mailto:AAFS@hqda.army.mil) or write to:

**Department of the Army**  
Office of the Deputy Assistant Secretary of the Army  
(Financial Management and Comptroller)  
Office of the Financial Reporting Directorate  
Room 3A312, 109 Army Pentagon  
Washington, DC 20310-0109

Additional copies of this report can be obtained by sending a written request to  
the e-mail or mailing address listed above.

You may also view this document at: <http://www.asqfm.army.mil/fo/fod/cfo/cfo.asp>

*\*Unless otherwise noted, all photos on the cover and inside pages are courtesy of the U.S. Army*

## The Soldier's Creed

I am an American Soldier.

*Warrior*

*Team*

*Army Values*

I will always place the mission first.

I will never accept defeat.

I will never quit.

I will never leave a fallen comrade.

*Disciplined*

*Tough*

*Trained*

*Expert*

*Professional*

*Ready*

I am a guardian of freedom.

I live by this creed.



United States Army • 1500 Army Pentagon • Washington, DC, 20310-1500 • [www.army.mil](http://www.army.mil)