

**Audit**



**Report**

OFFICE OF THE INSPECTOR GENERAL

INSPECTOR GENERAL, DOD, OVERSIGHT OF THE  
AIR FORCE AUDIT AGENCY AUDIT OF THE FY 1995  
AIR FORCE CONSOLIDATED FINANCIAL STATEMENTS

Report No. 96-098

April 18, 1996

**Department of Defense**

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**INSPECTOR GENERAL  
DEPARTMENT OF DEFENSE  
400 ARMY NAVY DRIVE  
ARLINGTON, VIRGINIA 22202-2884**



April 18, 1996

**MEMORANDUM FOR UNDER SECRETARY OF DEFENSE (COMPTROLLER)  
AND CHIEF FINANCIAL OFFICER  
DIRECTOR, DEFENSE FINANCE AND ACCOUNTING  
SERVICE**

**SUBJECT: Audit Report on Inspector General, DoD, Oversight of the Air Force  
Audit Agency Audit of the FY 1995 Air Force Consolidated Financial  
Statements (Report No. 96-098)**

We are providing this report for your information and use and for transmittal to the Director, Office of Management and Budget. It includes our endorsement of the Air Force Audit Agency (AFAA) opinion on the FY 1995 Air Force Consolidated Financial Statements, along with the AFAA "Report of Audit: Opinion on Fiscal Year 1995 Air Force Consolidated Financial Statements." This audit was required by the Chief Financial Officers Act of 1990, as amended by the Federal Financial Management Act of 1994. Since the report contains no recommendations, management comments are not required.

We appreciate the courtesies extended to the audit staff. Questions on the audit should be directed to Mr. David C. Funk, Audit Program Director, at (303) 676-7445 (DSN 926-7445), or Mr. W. Andy Cooley, Audit Project Manager, at (303) 676-7393 (DSN 926-7393). See Appendix E for the report distribution. The audit team members are listed inside the back cover.

Robert J. Lieberman  
Assistant Inspector General  
for Auditing

Office of the Assistant Inspector General, Department of Defense

Report No. 96-098  
(Project No. 5FD-2024.01)

April 18, 1996

**Inspector General, DoD, Oversight of the  
Air Force Audit Agency Audit of the  
FY 1995 Air Force Consolidated  
Financial Statements**

**Executive Summary**

**Introduction.** The Chief Financial Officers Act of 1990, as amended by the Federal Financial Management Act of 1994, requires an audit of the Air Force consolidated financial statements. We delegated the audit of the FY 1995 Air Force consolidated financial statements to the Air Force Audit Agency. On March 1, 1996, the Air Force Audit Agency issued its "Report of Audit: Opinion on Fiscal Year 1995 Air Force Consolidated Financial Statements" (Project 94053001). In that report, the Air Force Audit Agency disclaimed an opinion on the financial statements. This report provides our endorsement of that disclaimer of opinion.

**Audit Objective.** The audit objective was to determine the accuracy and completeness of the audit of the FY 1995 Air Force consolidated financial statements conducted by the Air Force Audit Agency.

**Audit Results.** The Air Force Audit Agency's report stated that the auditors were unable to obtain sufficient evidence, or apply other auditing procedures, required to satisfy themselves as to the fairness of the information presented in the financial statements. Consequently, the Air Force Audit Agency was unable to express an opinion on the FY 1995 Air Force consolidated financial statements. See Appendix A for our endorsement of the Air Force Audit Agency's disclaimer of opinion. The Air Force Audit Agency's specific reasons for its disclaimer are found in its report (Appendix B).

**Internal Control Structure and Compliance With Laws and Regulations.** The Air Force Audit Agency issued reports on the Air Force's internal control structure and its compliance with laws and regulations. These reports are included in the Air Force Audit Agency's report (Appendix B).

**Summary of Recommendations and Management Comments.** This report contains no recommendations that are subject to resolution in accordance with DoD Directive 7650.3. Therefore, management comments are not required.

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## **Additional Information**

# Appendix A. IG, DoD, Endorsement Memorandum



INSPECTOR GENERAL  
DEPARTMENT OF DEFENSE  
400 ARMY NAVY DRIVE  
ARLINGTON, VIRGINIA 22202-2884



March 1, 1996

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE (COMPTROLLER)  
AND CHIEF FINANCIAL OFFICER  
DIRECTOR, DEFENSE FINANCE AND ACCOUNTING  
SERVICE

SUBJECT: Endorsement of the Disclaimer of Opinion on the FY 1995 Air Force  
Consolidated Financial Statements (Project No. 5FD-2024)

The Chief Financial Officers Act of 1990, as amended, requires financial statement audits by the statutory Inspectors General. On May 16, 1995, we delegated to the Air Force Audit Agency (AFAA) the audit of the FY 1995 Air Force consolidated financial statements. Summarized below are the AFAA opinion letter on the Air Force consolidated financial statements and the results of our review of the audit conducted by AFAA. We endorse the disclaimer of opinion expressed by AFAA (Enclosure) in its audit of the FY 1995 Air Force consolidated financial statements.

## Disclaimer of Opinion

The AFAA disclaimer of opinion on the FY 1995 Air Force consolidated financial statements, dated March 1, 1996 stated that AFAA was unable to obtain sufficient evidence or apply other auditing procedures required to satisfy itself as to the fairness of the information presented in the financial statements. Consequently, the AFAA was unable to express an opinion on the Air Force consolidated financial statements. We concur with the AFAA disclaimer of opinion.

The primary reason that prevented the AFAA from performing the audit was that financial information used to compile the FY 1995 Air Force consolidated financial statements was not reliable; and financial systems and processes, as well as the associated internal control structure, were not adequate to produce reliable financial information. Specific reasons cited by the AFAA for not expressing an opinion on the FY 1995 Air Force consolidated financial statements are summarized below.

- o Accounts were overstated by approximately \$2.4 billion and understated by \$2.1 billion.

- o As in previous years, the acquisition cost of assets, valued at \$258.4 billion, could not be verified due to system problems and document retention practices, and was further compounded by the lack of a transaction-driven general ledger.

- o Inventory systems contained approximately \$109 million in errors due to incorrect on-hand balances and unit pricing problems.

- o Assets continue to be double counted or excluded from account balances, and unserviceable assets are recorded at their full operational value.

Several of the conditions that resulted in disclaimers of opinion for the FYs 1992, 1993 and 1994 Air Force consolidated financial statements still existed in relation to the FY 1995 financial statements.

### Internal Controls and Compliance With Laws and Regulations

In accordance with generally accepted Government auditing standards, the AFAA issued reports on the Air Force internal controls and its compliance with laws and regulations. These reports stated that:

- o the internal control structure for financial reporting did not provide reasonable assurance of achieving the internal control objectives described in the Office of Management and Budget Bulletin 93-06, "Audit Requirements for Federal Financial Statements," January 8, 1993, and

- o existing systems and controls did not enable the Air Force and the Defense Finance and Accounting Service to fully comply with laws and regulations that materially affect the financial statements.

### Review of Air Force Audit Agency Work

To fulfill our responsibilities under the Chief Financial Officers Act of 1990 for determining the accuracy and completeness of the independent audit conducted by the AFAA, we:

- o reviewed the AFAA approach and planning of the audit,
- o evaluated qualifications and independence of AFAA auditors, and
- o monitored progress of the audit at key points.

In addition to the above oversight procedures, we also performed other procedures deemed necessary to satisfy ourselves as to the fairness and accuracy of the audit approach and conclusions.

We conducted our review of the AFAA audit of the FY 1995 Air Force consolidated financial statements in accordance with generally accepted Government auditing standards during the period May 16, 1995, through March 1, 1996. We found no indication that we could not place reliance on the AFAA opinion on the FY 1995 Air Force consolidated financial statements, its report on internal controls, and its report on compliance with laws and regulations.



Robert J. Lieberman  
Assistant Inspector General  
for Auditing

Enclosure



DEPARTMENT OF THE AIR FORCE  
WASHINGTON DC 20330-1000

1 March 1996

OFFICE OF THE SECRETARY

To the Secretary of the Air Force  
Chief of Staff, USAF

1. We audited the consolidated financial statements of the Air Force for the fiscal years (FYs) ended 30 September 1995 and 30 September 1994. In accordance with the Chief Financial Officers (CFO) Act of 1990; the Government Management Reform Act of 1994; and Office of Management and Budget (OMB) Bulletin 93-18, Audited Financial Statements, 25 June 1993, the Defense Finance and Accounting Service (DFAS) and Air Force management prepared the accompanying financial statements. Our audits of the Air Force's FY 1995 Principal Financial Statements resulted in nine reports containing 20 recommendations for improving Air Force financial management, internal controls, and compliance with laws and regulations. This report presents our opinion on the principal financial statements, our evaluation of the underlying system of internal controls, and our assessment of compliance with laws and regulations. Our audit of the FY 1995 statements showed that several of the conditions causing us to disclaim an opinion for FYs 1994, 1993, and 1992 still existed.

#### OPINION ON FINANCIAL STATEMENTS

2. We were not able to obtain sufficient evidential matter, or apply other auditing procedures, to satisfy ourselves as to the fairness of the Air Force consolidated financial statements. As a result, we are unable to express an opinion on the reliability of the FY 1995 Air Force financial statements because financial information was not reliable and financial systems and processes, as well as the associated internal control structure, were not adequate to produce reliable financial information.

3. Our audit found account overstatements of approximately \$2.4 billion and account understatements of \$2.1 billion. As in prior years, we could not verify the acquisition cost of assets, valued at \$258.4 billion, due to system problems and document retention practices and further compounded by the lack of a transaction-driven general ledger. We identified \$109 million in inventory systems errors caused by incorrect on-hand balances and unit pricing problems. Furthermore, we found that financial managers continued to double count assets, exclude assets from account balances, and record unserviceable assets at full operational value.

Conversely, our audit work on civilian pay, military pay, and cash operations provided more positive results. We concluded that Air Force civilian payroll and related accruals and military personnel costs at the installations reviewed were generally accurate and reliable, and internal controls were generally effective when properly applied. At the locations reviewed for cash operations, we did not identify any discrepancies that would materially affect the accuracy of the \$114.4 million cash balance included in the FY 1995 Air Force Consolidated Financial Statements. The details of these and other conditions are more fully discussed in Tab A of this report.

#### REPORT ON INTERNAL CONTROLS

4. Internal controls were generally adequate to provide proper physical safeguards over assets, but the internal control structure for financial reporting did not provide reasonable assurance of achieving the internal control objectives described in OMB Bulletin 93-06, Audit Requirements for Federal Financial Statements, 8 January 1993. We also determined that internal controls were not sufficient to provide a reasonable basis for determining material compliance with certain laws and regulations and to prevent material misstatements in the financial statements. For example, there was limited assurance that only valid transactions were processed because transactions were not always properly recorded, supported, and reported. In addition, 8,502 unreconciled differences existed between departmental and installation-level disbursement and collection data, resulting in a \$1.1 billion difference in those records. We could not trace many of the unreconciled differences to supporting documentation. Finally, DFAS personnel either did not perform, or did not adequately perform analyses of account balances and accounting reports. Further discussion of these issues is presented in Tab B of this report.

#### COMPLIANCE WITH LAWS AND REGULATIONS

5. Existing systems and controls did not enable the Air Force and DFAS to fully comply with laws and regulations that materially affect the financial statements. We reviewed significant provisions of the laws and regulations presented at Appendix III. Financial managers did not report materially nonconforming accounting systems as required under the Federal Managers' Financial Integrity Act (FMFIA), and procedures in effect created a risk of violating the Antideficiency Act. Further, the Air Force incurred interest penalties and lost vendor discounts because accounting offices did not promptly pay Air Force debts as intended by the Prompt Payment Act. These and other issues are discussed in Tab C of this report.

### INITIATIVES TO IMPROVE FINANCIAL DATA

6. The Air Force, DoD, and DFAS initiated several actions to improve Air Force financial data. The Secretary of the Air Force established a Financial Improvement Policy Council to coordinate Air Force and DFAS systems development work. DoD established the Acquisition and Financial Management Working Group to resolve the DoD-wide problem of differences in disbursements. Also, the Defense Finance Accounting Service-Denver Center (DFAS-DE) is developing concepts for an interim migratory accounting system called the General Ledger/Funds Control (GL/FC) system to improve Air Force financial data. In addition, DFAS-DE is in the process of implementing the Direct Contract Payment Notice System and has implemented the Automated Reconciliation System to improve controls over the obligation process. These systems should also reduce the time required to reconcile problem disbursements and discrepancies between Air Force data and DFAS-Columbus Center (DFAS-CO) data. DFAS-DE also made significant improvements in reconciling pay and personnel records, which contributed to increased accuracy of payroll data. We address additional management actions in Tab A of our audit report. Further, DFAS-DE made all appropriate audit-recommended adjustments to reported account balances and recommended footnote disclosures to improve presentation of Air Force financial statement data.

### OBJECTIVES, SCOPE, AND METHODOLOGY

7. Management is responsible for:
- a. Preparing annual financial statements in accordance with generally accepted accounting principles and OMB Bulletin 94-01, Form and Content of Agency Financial Statements, 16 November 1993.
  - b. Establishing and maintaining internal controls to provide reasonable assurance that the internal control objectives in OMB Bulletin 93-06 are met.
  - c. Complying with applicable laws and regulations.
8. We are responsible for obtaining reasonable assurance about whether (a) the financial statements are reliable (free of material misstatement and presented fairly in conformity with generally accepted accounting principles) and (b) relevant internal controls are in place and operating effectively. We are also responsible for testing compliance with selected provisions of laws and regulations.

9. To fulfill these responsibilities, we:

a. Examined, on a test basis, evidence supporting the amounts and disclosures in the financial statements.

b. Assessed the accounting principles used and significant estimates made by management.

c. Evaluated the overall presentation of the financial statements.

d. Evaluated and tested relevant internal controls.

e. Tested compliance with significant provisions of applicable laws and regulations.

10. We limited our work to accounting and other controls necessary to achieve the objectives outlined in our report on internal controls. Because of inherent limitations in any system of internal control, losses, noncompliance, or misstatements may nevertheless occur and not be detected.

11. We performed our work in accordance with generally accepted government auditing standards and the provisions of OMB Bulletin 93-06.

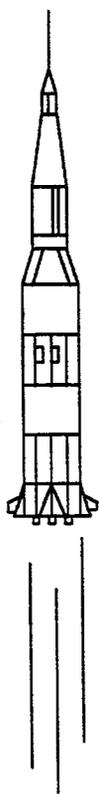
  
JACKIE R. CRAWFORD  
The Auditor General

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**Appendix B. AFAA Report, "Opinion on Fiscal Year 1995 Air Force Consolidated Financial Statements"**

**Project 95053001**

**1 March 1996**



# **REPORT OF AUDIT**

**OPINION ON FISCAL YEAR 1995  
AIR FORCE CONSOLIDATED  
FINANCIAL STATEMENTS**



**AIR FORCE AUDIT AGENCY**

Appendix B. AFAA Report, "Opinion on Fiscal Year 1995 Air Force Consolidated Financial Statements"



DEPARTMENT OF THE AIR FORCE  
WASHINGTON DC 20330-1000

OFFICE OF THE SECRETARY

MEMORANDUM FOR SECRETARY OF THE AIR FORCE  
CHIEF OF STAFF, USAF

FROM: SAF/AG

SUBJECT: Report of Audit, Opinion on Fiscal Year 1995 Air Force Consolidated Financial Statements (Project 95053001)

Our audit opinion on the Fiscal Year (FY) 1995 Air Force Consolidated Financial Statements follows. For details, please refer to the Opinion Letter and audit report. Management comments from the Assistant Secretary of the Air Force for Financial Management and Comptroller (SAF/FM) and Defense Finance and Accounting Service (DFAS) are at Appendix VIII.

The SAF/FM and DFAS comments indicate agreement with our basis for disclaiming an opinion and DFAS has planned actions to address recurring issues related to noncompliance with existing policy or regulations. Furthermore, SAF/FM and DFAS comments reiterate their goal of achieving an unqualified opinion but recognize that even though they are making progress, it will take several years to resolve existing accounting system weaknesses. DFAS did express concern with the accuracy of some summary data presented in the opinion and disagreed with our recommended treatment of unmatched recoupments of progress payments and our assertion that a \$6.9 billion decrease in munitions was not properly analyzed. These concerns and resolution of any disagreements will be addressed during processing of the supporting reports identified in Appendix IV.

We consider SAF/FM comments responsive to the issues addressed in this report. While the DFAS comments were generally responsive, some further resolution actions may be required in conjunction with our supporting reports.

*Jackie R Crawford*  
JACKIE R. CRAWFORD  
The Auditor General

**Project 95053001**

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**OPINION ON FISCAL YEAR 1995  
AIR FORCE CONSOLIDATED  
FINANCIAL STATEMENTS**

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Appendix B. AFAA Report, "Opinion on Fiscal Year 1995 Air Force Consolidated Financial Statements"



DEPARTMENT OF THE AIR FORCE  
WASHINGTON DC 20330-1000

1 March 1996

OFFICE OF THE SECRETARY

To the Secretary of the Air Force  
Chief of Staff, USAF

1. We audited the consolidated financial statements of the Air Force for the fiscal years (FYs) ended 30 September 1995 and 30 September 1994. In accordance with the Chief Financial Officers (CFO) Act of 1990; the Government Management Reform Act of 1994; and Office of Management and Budget (OMB) Bulletin 93-18, Audited Financial Statements, 25 June 1993, the Defense Finance and Accounting Service (DFAS) and Air Force management prepared the accompanying financial statements. Our audits of the Air Force's FY 1995 Principal Financial Statements resulted in nine reports containing 20 recommendations for improving Air Force financial management, internal controls, and compliance with laws and regulations. This report presents our opinion on the principal financial statements, our evaluation of the underlying system of internal controls, and our assessment of compliance with laws and regulations. Our audit of the FY 1995 statements showed that several of the conditions causing us to disclaim an opinion for FYs 1994, 1993, and 1992 still existed.

#### OPINION ON FINANCIAL STATEMENTS

2. We were not able to obtain sufficient evidential matter, or apply other auditing procedures, to satisfy ourselves as to the fairness of the Air Force consolidated financial statements. As a result, we are unable to express an opinion on the reliability of the FY 1995 Air Force financial statements because financial information was not reliable and financial systems and processes, as well as the associated internal control structure, were not adequate to produce reliable financial information.

3. Our audit found account overstatements of approximately \$2.4 billion and account understatements of \$2.1 billion. As in prior years, we could not verify the acquisition cost of assets, valued at \$258.4 billion, due to system problems and document retention practices and further compounded by the lack of a transaction-driven general ledger. We identified \$109 million in inventory systems errors caused by incorrect on-hand balances and unit pricing problems. Furthermore, we found that financial managers continued to double count assets, exclude assets from account balances, and record unserviceable assets at full operational value.

Conversely, our audit work on civilian pay, military pay, and cash operations provided more positive results. We concluded that Air Force civilian payroll and related accruals and military personnel costs at the installations reviewed were generally accurate and reliable, and internal controls were generally effective when properly applied. At the locations reviewed for cash operations, we did not identify any discrepancies that would materially affect the accuracy of the \$114.4 million cash balance included in the FY 1995 Air Force Consolidated Financial Statements. The details of these and other conditions are more fully discussed in Tab A of this report.

#### **REPORT ON INTERNAL CONTROLS**

4. Internal controls were generally adequate to provide proper physical safeguards over assets, but the internal control structure for financial reporting did not provide reasonable assurance of achieving the internal control objectives described in OMB Bulletin 93-06, Audit Requirements for Federal Financial Statements, 8 January 1993. We also determined that internal controls were not sufficient to provide a reasonable basis for determining material compliance with certain laws and regulations and to prevent material misstatements in the financial statements. For example, there was limited assurance that only valid transactions were processed because transactions were not always properly recorded, supported, and reported. In addition, 8,502 unreconciled differences existed between departmental and installation-level disbursement and collection data, resulting in a \$1.1 billion difference in those records. We could not trace many of the unreconciled differences to supporting documentation. Finally, DFAS personnel either did not perform, or did not adequately perform analyses of account balances and accounting reports. Further discussion of these issues is presented in Tab B of this report.

#### **COMPLIANCE WITH LAWS AND REGULATIONS**

5. Existing systems and controls did not enable the Air Force and DFAS to fully comply with laws and regulations that materially affect the financial statements. We reviewed significant provisions of the laws and regulations presented at Appendix III. Financial managers did not report materially nonconforming accounting systems as required under the Federal Managers' Financial Integrity Act (FMFIA), and procedures in effect created a risk of violating the Antideficiency Act. Further, the Air Force incurred interest penalties and lost vendor discounts because accounting offices did not promptly pay Air Force debts as intended by the Prompt Payment Act. These and other issues are discussed in Tab C of this report.

### INITIATIVES TO IMPROVE FINANCIAL DATA

6. The Air Force, DoD, and DFAS initiated several actions to improve Air Force financial data. The Secretary of the Air Force established a Financial Improvement Policy Council to coordinate Air Force and DFAS systems development work. DoD established the Acquisition and Financial Management Working Group to resolve the DoD-wide problem of differences in disbursements. Also, the Defense Finance Accounting Service-Denver Center (DFAS-DE) is developing concepts for an interim migratory accounting system called the General Ledger/Funds Control (GL/FC) system to improve Air Force financial data. In addition, DFAS-DE is in the process of implementing the Direct Contract Payment Notice System and has implemented the Automated Reconciliation System to improve controls over the obligation process. These systems should also reduce the time required to reconcile problem disbursements and discrepancies between Air Force data and DFAS-Columbus Center (DFAS-CO) data. DFAS-DE also made significant improvements in reconciling pay and personnel records, which contributed to increased accuracy of payroll data. We address additional management actions in Tab A of our audit report. Further, DFAS-DE made all appropriate audit-recommended adjustments to reported account balances and recommended footnote disclosures to improve presentation of Air Force financial statement data.

### OBJECTIVES, SCOPE, AND METHODOLOGY

7. Management is responsible for:

a. Preparing annual financial statements in accordance with generally accepted accounting principles and OMB Bulletin 94-01, Form and Content of Agency Financial Statements, 16 November 1993.

b. Establishing and maintaining internal controls to provide reasonable assurance that the internal control objectives in OMB Bulletin 93-06 are met.

c. Complying with applicable laws and regulations.

8. We are responsible for obtaining reasonable assurance about whether (a) the financial statements are reliable (free of material misstatement and presented fairly in conformity with generally accepted accounting principles) and (b) relevant internal controls are in place and operating effectively. We are also responsible for testing compliance with selected provisions of laws and regulations.

**Appendix B. AFAA Report, "Opinion on Fiscal Year 1995 Air Force Consolidated Financial Statements"**

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9. To fulfill these responsibilities, we:

a. Examined, on a test basis, evidence supporting the amounts and disclosures in the financial statements.

b. Assessed the accounting principles used and significant estimates made by management.

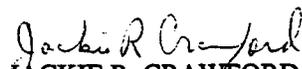
c. Evaluated the overall presentation of the financial statements.

d. Evaluated and tested relevant internal controls.

e. Tested compliance with significant provisions of applicable laws and regulations.

10. We limited our work to accounting and other controls necessary to achieve the objectives outlined in our report on internal controls. Because of inherent limitations in any system of internal control, losses, noncompliance, or misstatements may nevertheless occur and not be detected.

11. We performed our work in accordance with generally accepted government auditing standards and the provisions of OMB Bulletin 93-06.

  
JACKIE R. CRAWFORD  
The Auditor General

Project 95053001

TAB A

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## ACCURACY OF ACCOUNT BALANCES

### BACKGROUND

1. As of 30 September 1995, the Air Force Consolidated Statement of Financial Position reported total assets of \$323.8 billion, liabilities of \$8.3 billion, and net position totaling \$315.5 billion. The Statement of Operations reported total revenues and financing sources of \$58.9 billion and expenses of \$59.1 billion, while the budget for FY 1995 was about \$74.4 billion.
2. We performed an audit of the accompanying statement of financial position of the Air Force as of 30 September 1995 and the related statement of operations and changes in net position for the year then ended to determine if the financial statements fairly presented the Air Force financial condition as of 30 September 1995. DFAS published Air Force consolidated financial statements<sup>1</sup> on 1 March 1996 (Appendix VIII).

### CONCLUSION

3. Material uncertainties exist regarding the reasonableness of amounts reported in the FY 1995 Air Force Consolidated Financial Statements. Amounts reported on the statements, such as \$234.5 billion in property, plant, and equipment; \$54.7 billion in fund balances with Treasury; and \$23.9 billion in operating materials and supplies, were assembled from a variety of separate information systems of uncertain reliability. Further, for most items, we were unable to verify the account balances. Because of the unverifiable account balances and accounting system inadequacies, we do not express an opinion on the consolidated financial statements, and we caution users that these statements may not be totally reliable.

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<sup>1</sup> DFAS-DE issued the initial FY 1995 Air Force financial statements on 18 December 1995. Based on our audit and other information, DFAS-DE updated the statements and reissued them 2 February 1996.

**Project 95053001**

**TAB A**

**Accuracy of Account Balances**

### **MANAGEMENT ACTIONS**

4. In response to this and prior audits,<sup>2</sup> as well as continuing congressional and public concerns, the Air Force, DoD, and DFAS have initiated actions to address the problems discussed in this report. Once management corrects the reported problems, the Air Force should be capable of achieving more effective financial control over its assets as well as providing more reliable financial information to Air Force senior managers, Congress, and other interested parties. Specifically,

a. The Secretary of the Air Force established a Financial Improvement Policy Council to coordinate developments between the Air Force and DFAS, particularly in areas where Air Force information systems will interface with DFAS accounting systems.

b. The DoD Comptroller established the DoD Acquisition and Financial Management Working Group to resolve the DoD-wide problem of matching disbursements to valid obligations. The working group report, *Eliminating Unmatched Disbursements, A Combined Approach*, June 1995, contains 48 recommendations for DFAS and other agencies to correct conditions that cause unmatched disbursements and to eliminate existing mismatches, including possible write-offs.

c. DFAS-DE, in conjunction with the LOGICON Corporation and the accounting firm of KPMG Peat, Marwick, is developing concepts for a GL/FC system. The major goals of GL/FC include providing double entry, transaction based general ledgers; converting to the government standard chart of accounts (augmented by DoD); using the standard Budget and Accounting Classification Code; and providing a general ledger for each general ledger appropriation. When completed, this project should enable the Air Force to reduce the total number of financial systems and meet General Accounting Office (GAO), Treasury, FMFIA, CFO Act, and DoD accounting standards and requirements.

d. DFAS-DE has a Transfer of Management Responsibility (TMR) contract with the LOGICON Corporation to review management information systems that have both a functional (e.g., inventory tracking) and accounting application. LOGICON is charged with determining whether the functional user, e.g., Air

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<sup>2</sup> See Appendix II for a summary of prior audits.

Project 95053001

Accuracy of Account Balances

TAB A

Force Materiel Command (AFMC), or DFAS should have primary responsibility for maintaining the system and whether the system should be reported under FMFIA Section 4.

e. DFAS-DE is developing the Departmental Cash Management System to satisfy departmental accounting requirements and increase productivity while reducing costs of the cash management work force and systems. The system is being designed to correct material weaknesses, respond to audit findings, and reduce the outstanding balance of undistributed disbursements and negative unliquidated obligations. This system will replace the Merged Accountability and Fund Reporting (MAFR) system. DFAS-DE provided life cycle documentation for the conceptual exploration phase to DFAS Headquarters in April 1995 and DFAS Headquarters granted permission to proceed with software development in September 1995.

f. DFAS is converting the Air Force Standard Civilian Automated Pay System to the Defense Civilian Pay System with completion expected in 1997. DFAS converted the Air Force Joint Uniform Military Pay System to the Defense Joint Military Pay System (DJMS) in FY 1994 and made several enhancements to DJMS during FY 1995.

g. DFAS-DE is implementing the Direct Contract Payment Notice System at Central Procurement Accounting System locations and has fully implemented the Automated Reconciliation System within AFMC. DFAS-DE expects these systems will improve controls over the obligation process and reduce the time required to reconcile problem disbursements and discrepancies between Air Force and DFAS-CO data. DFAS-DE has also entered into an arrangement with AFMC to resolve AFMC unmatched disbursements.

h. DoD, DFAS, and the Air Force have initiated several programs that significantly reduced cash needed for daily Air Force operations. These initiatives decreased disbursing officer cash holding authority at active duty and Air Force Reserve (AFRES) locations. For example, disbursing officers now make disbursements using electronic funds transfer whenever possible, and government travelers use the American Express card to obtain cash advances. DFAS and Air Force financial managers have made effective management of cash more attainable with these initiatives. Reduced cash levels provide less opportunity of misappropriation of this highly vulnerable asset.

**Project 95053001**

**TAB A**

**Accuracy of Account Balances**

i. DFAS-DE and Air Force officials are implementing our previous recommendation to develop a systematic process for compiling and reporting contingent liabilities. DFAS issued guidance for recording and reporting contingent liabilities in the consolidated financial statements, and AFMC issued a memorandum providing field activities direction on managing contingent liabilities. In June 1995, the Deputy Assistant Secretary of the Air Force, Financial Operations, requested the accounting firm of Coopers & Lybrand to conduct a baseline assessment of Air Force Headquarters processes for capturing and reporting contingent liabilities. Also, the Office of the Assistant Secretary, Financial Management and Comptroller (SAF/FM) and DFAS-DE changed financial statement reporting of contingent liabilities; SAF/FM established procedures to obtain timely contingency data from the Air Force General Counsel; and DFAS-DE discontinued treating budgetary contingencies as contingent liabilities, a practice which caused significant misstatements in the past.

5. While awaiting the completion of system development efforts, DFAS-DE and Air Force management must address several significant issues to improve financial management operations. These issues include accounting for and valuing Air Force inventories and contractor-held Air Force property; improving internal controls by properly classifying, recording, supporting, and reporting financial transactions; deobligating current year funds before they expire and expiring funds before they cancel; and properly accounting for progress payments. The following paragraphs provide a synopsis of the significant issues which preclude an opinion on the Air Force financial statements for the fiscal year ended 30 September 1995.

## **AUDIT RESULTS**

### **Summary**

6. Conditions reported in past audits still exist. Also, we found significant conditions that adversely impacted four of the five management assertions embodied in the financial statement components. During this audit, we identified over \$4.5 billion of required adjustments to amounts reported in the statements, and \$1.8 billion in additional required footnote disclosures. DFAS-DE made all appropriate adjustments. However, we arrived at the adjustments using existing accounting systems and data, and many of those systems and associated data are known to be unreliable. Conversely, our audit work on civilian pay, military pay, and cash operations provided more positive results. We concluded that Air Force civilian payroll and related accruals and military personnel costs at the

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**Accuracy of Account Balances**

**TAB A**

installations reviewed were generally accurate and reliable, and internal controls were generally effective when properly applied. At the locations reviewed for cash operations, we did not identify any discrepancies that would materially affect the accuracy of the \$114.4 million cash balance included in the FY 1995 Air Force Consolidated Financial Statements.

**Previously Reported Conditions**

7. Our reports on the Air Force FY 1992, 1993, and 1994 financial statements identified a number of conditions which prevented us from expressing an opinion on the reliability of those statements. In our audit for FY 1995, we compared our prior findings with current conditions and found that the following conditions still exist:

- a. The Air Force does not have a transaction-driven general ledger.
- b. Existing accounting systems cannot produce auditable financial statements.
- c. Equipment and inventories were not reported accurately.
- d. Disbursement and collection account balances were questionable.
- e. Acquisition costs were not used for most assets.

**Significant Conditions**

8. We found significant conditions that adversely impacted four of the five management assertions defined by generally accepted government auditing standards<sup>3</sup> and embodied in the financial statement components. Specifically, we found significant conditions concerning the management assertions related to valuation or allocation, existence or occurrence, account completeness, and presentation and disclosure. Nothing came to our attention indicating significant conditions related to the management assertion of rights and obligations. We covered the significant conditions in more detail in separate reports provided to

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<sup>3</sup> Generally accepted government auditing standards incorporate the financial statement assertions defined by the American Institute of Certified Public Accountants (AICPA) in the Codification of Statements on Auditing Standards, AU Section 326.

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**TAB A**

**Accuracy of Account Balances**

Air Force and DFAS management for comment (Appendix IV). The following paragraphs address management assertions, the significant conditions we identified for each assertion, and the report that summarizes the conditions.

a. Valuation or Allocation. We identified the following conditions related to the appropriateness of amounts included in the financial statements for asset, liability, revenue, and expense accounts.

(1) Asset Cost. We could not determine the accuracy of account balances for property, plant, and equipment or operating materials and supplies, because the Air Force does not have a financial accounting system designed to accumulate, account for, and report the acquisition costs of these assets. Further, the Air Force uses standard costs to value these assets instead of acquisition costs as required by government accounting standards. DFAS-DE reported a \$258.4 billion general ledger balance for these assets as of 30 September 1995. (Reports of Audit 95053002 and 95053005)

(2) Government Furnished Property (GFP). The GFP balance reported by DFAS-DE in the FY 1995 Air Force Consolidated Financial Statements was \$33.9 billion less than the values contractors reported to the Defense Logistics Agency for inclusion in the Contractor Property Management System. This condition occurred because Air Force systems are not adequate to record, track, and report GFP owned by the Air Force and in the custody of contractors. (Report of Audit 96053011)

(3) MAFR. Data we retrieved from the MAFR system disclosed 8,502 disbursement and collection mismatches, with a cumulative value of \$1.1 billion, between DFAS-DE departmental records and defense accounting office (DAO) subsidiary data. We believe the number and value of disbursement and collection discrepancies, in conjunction with other reported fund control deficiencies, indicate that fund control data are not a reliable source of information for financial statement account balances. (Report of Audit 95053003)

(4) Satellite Launch Costs. HQ Air Force Space Command did not capitalize and include \$673.4 million in launch costs in general ledger account (GLA) 149 (Satellites, Complete), resulting in a corresponding understatement on the initial financial statements. Not only were we unable to determine the exact cause for this occurrence, Space Command personnel were also unable to

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reconstruct their launch cost calculation data or refute audit calculated launch costs. (Report of Audit 95053002)

(5) Inventory. We continue to identify errors in balances on hand and unit prices recorded in Air Force inventory systems.<sup>4</sup> Our physical inventories disclosed errors in recorded balances totaling \$28.3 million in the Financial Inventory Accounting and Billing System (FIABS) and the Standard Base Supply System (SBSS). We also identified unit price errors totaling \$109 million in the Combat Ammunition System, FIABS, and SBSS. (Report of Audit 95053005)

b. Existence or Occurrence. We identified the following significant conditions related to whether all assets and liabilities included in the 30 September 1995 financial statements existed at that date and whether all recorded transactions had occurred within the fiscal year ending on that date.

(1) Dual Reporting. Two different Air Force sources reported the same assets valued at over \$1 billion to DFAS. As a result, DFAS-DE included the reported amounts twice in the initial financial statements. Specifically,

(a) Satellites. HQ AFMC overstated the balance for GLA 149 provided to DFAS-DE, because Los Angeles AFB DAO personnel double counted a Defense Support Program satellite valued at \$396.9 million. (Report of Audit 95053002)

(b) Depot Munitions. The Air Force reported munitions inventories stored at DoD depots in both the FIABS and the Combat Ammunition System account balances provided to DFAS-DE, resulting in an overstatement of \$589 million. (Report of Audit 95053005)

(c) Signal System Assets. HQ AFMC and Offutt AFB both reported Tactical Airborne Signal Systems valued at \$39 million to DFAS-DE. (Report of Audit 95053005)

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<sup>4</sup> AFAA Report of Audit 94053031, Review of Inventories Not Held For Sale, Fiscal Year 1993 Air Force Consolidated Financial Statements, 1 July 1994; and AFAA Report of Audit 94053034, Review of Operating Materials and Supplies, Fiscal Year 1994 Air Force Consolidated Financial Statements, 27 June 1995.

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(2) Progress Payments. Accounting personnel at five locations recorded progress payments of \$208.5 million and progress payment recoupments of \$520.8 million in FY 1996 that should have been recorded in FY 1995. As a result, DFAS-DE overstated progress payments in the FY 1995 financial statements by a net of \$312.3 million. (Report of Audit 96053010)

(3) Account Support. Over \$227 million of accounts receivable, accounts payable, expenses, and obligations were either invalid, inadequately supported, or inaccurate. (Report of Audit 95053003)

(a) Accounts Receivable. At 16 Air Force installations reviewed, \$178 million of \$295 million in accounts receivable were either invalid, inadequately supported, or inaccurate.

(b) Accounts Payable & Expenses. Accounting personnel did not adequately support accounts payable valued at \$7.6 million at 18 locations and expenses of \$2.3 million at 7 locations.

(c) Obligations. Our review of 2,321 Undelivered Orders Outstanding, valued at over \$1 billion, identified that 635 (27 percent) balances, valued at 39.6 million were invalid or no longer needed.

c. Account Completeness. We identified the following significant conditions concerning the completeness of data included in the FY 1995 Air Force financial statements.

(1) Ammunition. The Air Force could not determine the correct amount of Air Force owned munitions to report to DFAS-DE for inclusion in the initial financial statements. On 27 October 1995, the Combat Ammunition System audit control point monitor at the Ogden Air Logistics Center reduced the end-of-year munitions inventory value to \$5.8 billion from the \$9.0 billion originally reported on 21 October 1995 because the monitor believed the previously submitted data was erroneous. The monitor reported an exact amount could not be determined because systems hardware problems prevented the accumulation of accurate inventory data. (Report of Audit 95053005)

(2) Property, Plant, and Equipment. HQ AFMC supplied DFAS-DE erroneous data for inclusion in the FY 1995 Air Force Statement of Financial Position. HQ AFMC did not include the value of recently declassified U-2 aircraft

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in the aircraft balances forwarded to DFAS-DE. HQ AFMC financial management personnel decided not to assign a new unit cost to each new aircraft type as they entered the aircraft into the Equipment Inventory, Multiple Status, and Utilization Reporting System database. As a result, the balance for GLA 141 (Aircraft, Complete) was understated by \$572 million. (Report of Audit 95053002)

(3) Excess and Unserviceable Assets. AFMC did not include \$527 million in assets in the GLA 147 (Excess and Surplus Property) balance reported to DFAS-DE. Specifically, AFMC did not report 102 aircraft obtained from commercial airlines and 112 photo shelters. As a result, Aerospace Maintenance and Regeneration Center accounting personnel did not report the \$527 million value of the property to DFAS-DE. (Report of Audit 95053005)

d. Presentation and Disclosure. We identified the following significant conditions related to the way the financial statement components were classified, described, and disclosed.

(1) Contingent Liabilities. While DFAS-DE and Air Force personnel significantly improved contingent liability reporting for FY 1995, we identified reporting errors affecting the accuracy of environmental cleanup, claims and litigation, future funding requirements, and procurement contract liabilities in the initial financial statements. (Report of Audit 96053013)

(a) Environmental Cleanup and Claims and Litigation. DFAS-DE presented outdated and unclear information in the footnotes to the financial statements. DFAS-DE requested updated information on environmental cleanup liabilities; however, the Air Force Civil Engineering Environmental Restoration Division provided 1993 cost estimates.

(b) Claims and Litigation. In presenting information on civil law and litigation cases, DFAS-DE did not disclose that the \$949 million reported included \$300 million for cases over \$100 million.

(c) Future Funding Requirements. DFAS-DE personnel included items that did not meet the definition of contingent liabilities and, thus, overstated contingent liabilities by over \$1.5 billion in footnote 31 of the initial financial statements. These items included unfunded accrued military and civilian leave (\$1.58 billion) and allowance for uncollectible accounts (\$5.2 million).

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(d) Procurement Contract Liabilities. DAO personnel did not report, and DFAS-DE did not include in the financial statements, \$44.7 million of procurement contract incentive fees and other contract contingent liabilities at five DAOs. Instead, DFAS-DE included these amounts along with all open commitments in Footnote 1P, Budgetary Contingencies. SAF/FM and DFAS-DE personnel acknowledged not using the DoD Uniform Chart of Accounts, which included an account for contingent liabilities, to capture FY 1995 financial information.

(2) Engines. During our FY 1995 audit, we found additional overstatements in FY 1994 balances. Specifically, we determined that DFAS-DE included the value for T56 and F100 engine modules in both the general fund and Defense Business Operations Fund financial statements for FY 1994. Prior to the end of FY 1994, engine module item managers at the San Antonio Air Logistics Center transferred these assets, valued at \$914 million, into the reparable spares system, a part of supplies data included in the Defense Business Operations Fund financial statements. However, because the Propulsion Product Group Manager at the San Antonio Air Logistics Center was not advised of the transfer, he reported the value of the assets to DFAS-DE and they also included the total in the FY 1994 Air Force general fund financial statements. Corrections were accomplished during the FY 1995 audit. (Report of Audit 95053002)

(3) Progress Payment Unmatched Recoupments. DAO personnel at four of five AFMC accountable stations included at least \$137.9 million of unmatched and possibly invalid recoupments in weapon systems progress payment account balances. As a result, the financial statements did not fully disclose unmatched recoupments and may have significantly understated progress payments. (Report of Audit 96053010)

(4) Excess and Unserviceable Assets. The Air Force maintained excess and unserviceable aircraft and engines in the Equipment Inventory, Multiple Status, Utilization Reporting System, and the Comprehensive Engine Management System, which feed general ledger accounts for operational assets (GLAs 141 and 143, Uninstalled Propulsion Units) rather than the excess and surplus property account (GLA 147). As a result, DFAS-DE overstated the value of military equipment in the initial financial statements by \$288.3 million, with a corresponding understatement of operating materials and supplies. (Reports of Audit 95053002 and 95053005)

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(5) Real Property. In Note 15 to the initial Statement of Financial Position, DFAS-DE included \$283.8 million of real property under Military Equipment instead of under Structures, Facilities, and Leasehold Improvements. (Report of Audit 95053002)

#### **Required Adjustments**

9. During our FY 1995 audit, we identified over \$4.5 billion of required adjustments to amounts reported in the statements and over \$1.8 billion in additional adjustments to the footnotes. DFAS-DE made all appropriate adjustments to the FY 1995 financial statements. Our recommended adjustments were needed to improve the accuracy and presentation of accounts impacting the balances for property, plant, and equipment; operating materials and supplies; and weapon system progress payments. DFAS-DE and the Air Force made current year adjustments of \$1.65 billion to property, plant, and equipment (satellites, aircraft, and engines) and \$672 million in adjustments to operating materials and supplies (ammunition and material-in-transit) financial statement account balances. DFAS-DE reduced a footnote balance for over \$1.5 billion of liabilities included in contingent liabilities and reclassified \$283.8 million of footnoted real property from property, plant, and equipment to structures, facilities, and leasehold improvements. In our FY 1995 review, we also identified over \$1 billion of adjustments required to prior period records. DFAS-DE made a \$914 million adjustment but could not obtain adequate support for the remaining amount. During FY 1995, DFAS-DE also made prior period adjustments totaling nearly \$3.4 billion for issues we identified in our previous review of the FY 1994 Air Force financial statements.

#### **Basis for Adjustments**

10. The adjustments summarized above are required based on audit findings. However, we arrived at the adjustments using existing accounting systems and data, and many of those systems and associated data are known to be unreliable. Consequently, even with all proposed adjustments, sufficient uncertainties regarding other amounts reported precluded us from expressing an opinion on the consolidated financial statements.

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**TAB B**

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## **REPORT ON INTERNAL CONTROLS**

### **BACKGROUND**

1. Management is responsible for establishing and maintaining an internal control structure to provide reasonable but not absolute assurance that obligations and costs are in compliance with applicable laws; funds, property, and other assets are safeguarded against waste, loss, unauthorized use, or misappropriation; and financial resources and expenditures applicable to the entity's operations are properly recorded and accounted for. A sound internal control structure helps management prepare reliable financial reports in accordance with applicable accounting standards and to maintain accountability over assets. In fulfilling this responsibility, management estimates and judgments are required to assess the expected benefits and related costs of internal control structure policies and procedures.

### **AUDIT RESULTS**

#### **Summary**

2. We determined that the Air Force internal control structure did not provide reasonable assurance of achieving the internal control objectives described in OMB Bulletin 93-06.<sup>5</sup> We identified reportable conditions in the areas of accounting system capabilities, financial data analysis, documentation, independent checks, and safeguarding assets. We believe the conditions we are reporting are material weaknesses.

#### **Reportable Conditions**

3. We noted certain matters involving the internal control structure and its operation that we consider to be reportable conditions under standards established by generally accepted government auditing standards and OMB Bulletin 93-06. Reportable conditions involve matters coming to our attention related to significant deficiencies in the design or operation of the internal control structure. These

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<sup>5</sup> A detailed explanation of these objectives is provided at Appendix I, paragraph 5.

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**Report on Internal Controls**

deficiencies could adversely affect the entity's ability to ensure that the objectives of the internal control structure are being achieved.

a. Accounting Systems. Due to significant accounting system internal control weaknesses, neither DFAS nor the Air Force can ensure they properly record, process, and summarize only valid transactions and provide accurate financial information. DFAS and the Air Force do not have a transaction-driven general ledger to provide a single source for compiling and reporting financial information for use in preparing the Air Force financial statements. Although DFAS-DE is developing a transaction-based financial management system, the system will not be fully operational for several years. Consequently, Air Force and DFAS-DE accounting personnel must extract data from multiple automated systems, as well as some manual systems, to prepare the annual Air Force consolidated financial statements. Some of the information used in the financial statements is received from Air Force sources that are not part of the financial community. Accounting personnel do not have the means to verify the validity of much of this data. This cumbersome compilation process contributes to control problems in presenting accurate financial statements, including the FY 1995 reporting issues identified in Tab A.

b. Analyses. DFAS personnel did not perform, or did not perform adequate, analyses of account balances and accounting reports. Analyzing financial statements and supporting accounts and reports is an essential control in assessing the reasonableness of reported balances and identifying potential misstatements. DFAS personnel could not support accounting adjustments or provide the rationale for account balance changes totaling over \$10 billion. For example:

(1) Account Adjustment Controls. DAO accounts control technicians at five of seven locations made over \$3.3 billion in adjustments to General Ledger Subsidiary Account (GLSA) 14641, Materiel On Hand-Supply Officer, without researching the basis for the adjustment. Rather than perform reconciliations, accounting technicians adjusted the general ledger balance to agree with the Computation of On Hand Investment Inventory Reconciliation List. DFAS-DE did not establish effective analytical procedures, train technicians on how to analyze differences, or investigate possible system problems causing differences between general ledger and supply records. As a result, the Operating Materials and Supplies line item on the Air Force financial statements was inaccurate. (Report of Audit 95053005)

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(2) Account Variance Controls. DFAS-DE General Ledger and Reports Branch personnel did not properly analyze significant variances in GLSA 14643, Ammunition, Air Force Stored; or GLSA 14644, Ammunition Stored With Other Government Agencies. Specifically, DFAS-DE personnel did not properly analyze a \$6.9 billion decrease (54 percent) from the FY 1994 balance, and thereby, did not identify an unsupported reduction in the account balance of \$3.2 billion as reported in Tab A. (Report of Audit 95053005)

(3) System Validation Checks. Our FIABS retrieval disclosed negative balances on hand for 173 stock numbers involving 138,000 units valued at \$34 million. The negative balances occurred because FIABS does not have a validation rule or check to prevent this condition. When supply personnel record more issues than assets available, record receipts as issues, or issue assets before recording their receipt, negative balances can result and financial statement balances can be understated. (Report of Audit 95053005)

(4) Supervisory Reviews. DAO personnel at two locations made accounting errors of nearly \$100 million that significantly affected reporting accuracy for weapon system progress payments. This condition occurred because accounting supervisors did not perform adequate reviews to detect accounting errors. (Report of Audit 96053010)

c. Documentation. Accounting personnel at 9 of 14 active duty locations and all 15 AFRES locations reviewed did not maintain adequate documentation to support accountability of cash assets. DAO management either was not aware of documentation requirements or did not exercise sufficient oversight to ensure compliance with established controls and procedures. Consequently, the accuracy of Air Force daily cash accountability was compromised. (Report of Audit 96053014)

d. Independent Checks. Accounting and operating personnel did not perform, or did not perform accurately, various verifications integral to the control over Air Force assets, including cash and negotiable instruments, inventories, and amounts owed by and due to the Air Force.

(1) Quarterly Cash Validations. Quarterly cash verifications performed at 11 of 14 Air Force locations and all 15 AFRES locations, were inadequate or needed procedural improvements to support the validity of the results. Properly

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performing and documenting quarterly cash verifications enhances control over this sensitive asset. (Report of Audit 96053014)

(2) Inventories. Although Air Force personnel took physical inventories of Operating Materials and Supply assets at eight locations, these inventories did not improve the accuracy of inventory records. For example, Air Force personnel conducting inventories attested to the presence of assets that were not on the installation or had been missing for several years. We questioned whether supply personnel conducted some inventories because inventory records did not indicate the inventory date. Completing physical inventories is vital to maintaining control over Air Force assets. Further, inventory accuracy directly affects financial statement accuracy. (Report of Audit 95053005)

(3) Reconciliations. Accounting technicians at 7 of 16 locations reviewed were not reconciling daily accounts receivable transactions to source documentation as required.<sup>6</sup> DAOs had assigned primary but not alternate responsibility for performing these duties. As a result, when primary personnel were reassigned or transferred off the installation, the duties were not performed. DAO reconciliation of daily transactions against source documents is a key internal control designed to ensure transactions are properly entered into the financial accounting system. (Report of Audit 95053003)

e. Adequate Safeguards. We identified weaknesses related to cash and related document security, separation of duties, and record accessibility. Limiting access to assets and records serves to deter unauthorized and unlawful acts while properly safeguarding cash and negotiable instruments limits opportunity for misappropriation.

(1) Security. We found security weakness at all 30 locations examined. For example, accounting personnel did not provide adequate controls over access to cash and related documents in safes and vaults, maintain required records pertaining to safes and vaults, or institute adequate robbery protection safeguards. (Report of Audit 96053014)

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<sup>6</sup> Air Force Manual (AFM) 177-370, USAF Standard Base-Level General Accounting and Finance System: H069/BQ, 5 February 1994.

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(2) Separation of Duties. Disbursing agents and alternate disbursing agents at 9 of 15 AFRES agent locations also performed cashier duties. Disbursing agents were not aware that performing two accountable positions (cashiering and disbursing) concurrently is prohibited.<sup>7</sup> (Report of Audit 96053014)

(3) Pay Record Accessibility Audit. Military pay personnel at five of eight Air National Guard and AFRES installations did not perform or performed improperly DJMS Pay Record Accessibility audits. These audits help ensure all personnel with access to DJMS, or personnel with dependents or relatives with access to DJMS, are paid only for authorized duty. (Report of Audit 95053004)

f. GFP. DFAS does not have a structured approach for compiling and reporting property owned by the Air Force and in the custody of contractors. Consequently, differences existed between amounts DFAS-DE included in the financial statements and amounts the Defense Logistics Agency obtained from contractor property records and entered into the Contractor Property Management System. DFAS-DE excluded up to \$33.9 billion from the Air Force financial statements as reported in Tab A, paragraph 8a(2). (Report of Audit 96053011)

#### Material Weaknesses

4. We believe the conditions reported in the previous paragraphs are material weaknesses. A material weakness is a reportable condition in which the design or operation of internal controls does not reduce to a relatively low level the risk that losses, noncompliance, or misstatements will go undetected. Under an adequate internal control system, some instances of loss, noncompliance, or misstatement material to the financial statements may occur but should be detected within a timely period by employees in the normal course of their assigned duties.

5. Our consideration of the internal control structure would not necessarily disclose all matters that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered material weaknesses as defined above. We also noted other matters involving the internal control structure and its operation that we have reported to Air Force and DFAS management in the associated FY 1995 audit reports listed at Appendix IV.

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<sup>7</sup> DoD Financial Management Regulation 7000.14-R, Volume 5, Disbursing Policies and Procedures, December 1993.

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TAB C

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## REPORT ON COMPLIANCE WITH LAWS AND REGULATIONS

### BACKGROUND

1. An entity's management is responsible for establishing an internal control structure to assure compliance with applicable laws and regulations. Issues which should concern management include:

a. Resources. Compliance with laws and regulations that could significantly affect the acquisition, protection, and use of the entity's resources, and the quantity, quality, timeliness, and cost of the products and services it produces and delivers.

b. Programs. Compliance with laws and regulations pertaining to the objectives of the entity's programs, activities, and functions; the manner in which programs and services are to be delivered; the population a program or service is to serve; and whether the programs, activities, and functions are being carried out in conformity with these laws and regulations.

2. Material instances of noncompliance are failures to follow requirements, or violations of prohibitions contained in laws or regulations that cause us to conclude that the aggregation of the misstatements resulting from those failures or violations is material to the financial statements, or the sensitivity of the matter would cause others to perceive the misstatements as significant. (Appendix III lists the laws and regulations we reviewed during this audit.)

### AUDIT RESULTS

#### Compliance With Laws and Regulations

3. Existing systems and controls did not enable the Air Force and DFAS to fully comply with laws and regulations that could have a direct and material effect on the FY 1995 Air Force financial statements. The Air Force and DFAS had not established an effective system of administrative controls over the disbursement

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Report on Compliance With Laws and Regulations

and close out of obligations as required by the Antideficiency Act. In addition, the Air Force incurred penalties and lost vendor discounts because accounting offices did not promptly pay Air Force debts as intended by the Prompt Payment Act. Further, we identified some instances of noncompliance with the FMFIA and DoD and Air Force directives. We considered the noncompliance reported below in forming our opinion on whether the FY 1995 Air Force Consolidated Financial Statements are fairly presented in all material respects in accordance with applicable accounting standards in effect for federal entities during the preparation of the entity's financial statements. The issues discussed in this tab do not affect our report on those statements presented in our opinion letter.

a. Antideficiency Act. DFAS has made a concerted effort to reduce mismatches in disbursement and collection data as cited in Tab A, paragraph 4b. However, the deficiencies in these areas (Tab A, paragraph 8a[3]), along with those affecting the validity of obligations (Tab A, paragraph 8b[3][c]), are still material. While we did not identify violations of the Antideficiency Act during our audit, the reported conditions significantly increase the probability that violations could occur. For example, unreconciled disbursement and collection mismatches increase the risk that cumulative disbursements will exceed appropriation or other legal limits. Conversely, accounting personnel lessen the risk of an Antideficiency Act violation when they follow up on dormant accounts, deobligate unneeded funds, or review obligated funds about to cancel.

b. Prompt Payment Act. We found that none of the 16 accounting offices reviewed promptly paid all Air Force debts as intended by the Prompt Payment Act. We identified 180 untimely payments out of 1,203 transactions examined. Accounting personnel did not properly date stamp some invoices when received and sometimes misunderstood the appropriate date for applying prompt payment requirements. As a result, the Air Force incurred interest penalties of \$3.46 million on 91,554 late payment invoices in FY 1995. In addition, during FY 1995, the Air Force did not receive \$2.9 million of economically justified vendor discounts on 109,425 invoices because payments were made beyond the discount date.<sup>8</sup> (Report of Audit 95053003)

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<sup>8</sup> DFAS-DE Prompt Payments Report, Fiscal Year Ending 30 September 1995, 29 November 1995; and Prompt Payment Report Worksheet Fiscal Year 1995.

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c. FMFIA. We identified noncompliance with two sections of the FMFIA.

(1) FMFIA, Section 2. DFAS and the Air Force did not report all internal control weaknesses in their FY 1995 Statements of Assurance. In our audit report on the FY 1992 Air Force financial statements, we recommended DFAS-DE identify internal control weaknesses relating to (a) reconciliation of control and subsidiary records, and (b) supporting documentation for fund control transactions in the FY 1993 Statement of Assurance to DFAS Headquarters. DFAS-DE implemented our FMFIA recommendation; however, the internal control weaknesses which prompted our FY 1992 recommendation continue, and the issue is no longer included in the DFAS-DE Statement of Assurance. DFAS-DE reported a material weakness in MAFR reconciliation; DFAS-DE and DFAS Headquarters reported a weakness in accounting for real and personal property in their Statement of Assurance; and the Air Force reported material weaknesses in contingent liabilities, the value of munitions inventory, and inventory accuracy rates in the FY 1995 Air Force Statement of Assurance. The lack of a systematic, structured approach for compiling and reporting GFP, as discussed in Tab B, paragraph 3f, was reported as a material weakness in the DFAS Headquarters statement of assurance.

(2) FMFIA, Section 4. The Air Force did not report four systems as materially nonconforming accounting systems in their FY 1995 statement of assurance because the TMR responsibility review cited in Tab A, paragraph 4d, was still in progress. The four systems, which produce information used in the Air Force financial statements, were the Combat Ammunition System; the Equipment Inventory, Multiple Status, and Utilization Reporting System; the Comprehensive Engine Management System; and the manual process for compiling satellite values. We previously reported these conditions in our FYs 1992, 1993, and 1994 audits of Air Force financial statements.<sup>9</sup> (Reports of Audit 95053002 and 95053005)

d. DoD Regulations. In Tabs A and B, we reported deficiencies in accounts receivable, accounts payable, expenses, quarterly cash verifications, security over

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<sup>9</sup> Appendix II lists the Air Force Audit Agency (AFAA) reports.

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Report on Compliance With Laws and Regulations

cash and related documents, and separation of duties. All the deficiencies occurred because accounting personnel were not aware of, or not adhering to, the provisions of the DoD Financial Management Regulation and Air Force directives. We noted the following additional regulatory noncompliances:

(1) Disbursing Officer Accountability. We identified cash management discrepancies which impacted disbursing officer accountability at 5 of 30 locations reviewed. For example, accounting personnel commingled a \$500,000 contingency fund with operating cash, did not report a loss of funds at year end, and did not record paid cash vouchers. Accounting personnel were not fully aware of cash management requirements.<sup>10</sup> (Report of Audit 96053014)

(2) Appointment of Authorized Officials. Disbursing and alternate disbursing agents at 26 of 30 locations did not acknowledge in writing their appointment and pecuniary liability as required.<sup>11</sup> Further, commanders did not provide written authorization to establish change funds in specified amounts. Accounting managers were not specifically aware of the regulatory requirements for these actions. (Report of Audit 96053014)

(3) Chart of Accounts. The Air Force did not use the DoD Uniform Chart of Accounts to capture accounting data in FY 1995 as required.<sup>12</sup> DFAS-DE did use the DoD Uniform Chart of Accounts to categorize financial information for the preparation of the Air Force consolidated financial statements. As we reported in Tab A, paragraph 8d(1)(c), not using the DoD Chart of Accounts prevented DFAS-DE from distinguishing contingent liabilities from other Air Force commitments. (Report of Audit 96053013)

e. Air Force Regulations. The issues discussed in Tab A, paragraph 8b(3)(b), and Tab B, paragraph 3d(3), resulted because accounting personnel did not

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<sup>10</sup> Same as footnote 7.

<sup>11</sup> Same as footnote 7.

<sup>12</sup> DoD 7000.14-R, Volume I, General Financial Management Information Systems and Requirements, May 1993.

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Report on Compliance With Laws and Regulations

TAB C

maintain and retain documentation as required.<sup>13</sup> We also identified a directive conflict in our draft Report of Audit, Review of Military Pay, Fiscal Year 1995 Air Force Consolidated Financial Statements (Project 95053004). We have not addressed any other issues of noncompliance with Air Force regulations in this report.

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<sup>13</sup> DoD 7000.14-R, Volume I; Air Force Regulation (AFR) 170-8, Accounting for Obligations, 15 January 1990; and DFAS-DE Regulation (DFAS-DER) 177-101, General Accounting and Finance Systems at Base Level, 15 February 1991.

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## BACKGROUND INFORMATION

### GENERAL

1. **Statutory Requirements.** The CFO Act of 1990 requires preparation of financial statements for each entity designated to report under CFO Act provisions. Prior to FY 1995, the Air Force prepared four principal statements: Statement of Financial Position, Statement of Operations and Changes in Net Position, Statement of Cash Flows, and Statement of Budgetary Resources and Actual Expenses, as directed by OMB Bulletin 94-01. The Government Management Reform Act of 1994 deleted the requirement for the latter two statements commencing with the FY 1996 financial statements. The DoD will not include these statements with the FY 1995 financial statements based upon a waiver received from OMB. The CFO Act initially required each agency to submit financial statements not later than 31 March following the end of the fiscal year under audit. While OMB granted waivers to the 31 March due date for FYs 1992 and 1993, OMB Bulletin 93-18 established a due date of 1 March after the close of the prior fiscal year commencing with FY 1994. The GMRA extends the 1 March due date indefinitely. DoD has published timeframes to be used within the department for financial statement preparation and audit.

2. **Accounting for Air Force Activity.** The Air Force general fund accounts for more than 99 percent of the assets, liabilities, revenues, and expenses shown on Air Force consolidated financial statements. The Air Force uses two methods to account for financial data as described below.

a. **General Ledger.** Air Force general ledger summary accounts track Air Force equity, budgetary items, and revenues. Those individual general ledger accounts were reported in the Air Force Trial Balance for General Funds, RCS: HAF-ACF (SA) 7105. DFAS-DE summarized this information into general ledger account balances but only used selected asset and liability account balances to prepare the annual Air Force financial statements.

b. **Status of Funds.** The Air Force uses the Status of Funds Data Base Transmission (DBT), RCS: HAF-ACF (AR) 7801, to report certain Air Force financial statement account balances such as accounts receivable, accounts payable, revenues, and expenses. The DBT accumulates and reports the status of Air Force funds. Base-level accounting offices initially prepare the DBT and the next higher Air Force command level consolidates the data by command. During FY 1994, most of the command-level review and consolidation process was moved

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to the Command Accounting and Reporting Division at DFAS-DE. This move was completed in FY 1995. The Command Accounting and Reporting Division reviews, updates, and edits the base-level data and enters the data into the Command On-Line Accounting and Reporting System. Command accounting prepares a consolidated DBT report and forwards this report to the Accounting and Reporting Division in DFAS-DE which enters the data into the Departmental On-Line Accounting and Reporting System (DOLARS), the Air Force departmental status of funds system. DFAS-DE ultimately summarizes this data and data from the 7105 reports in the Air Force financial statements. The Air Force uses the DBT reporting process because DFAS-DE has determined that this process is more reliable than general ledger reporting for certain accounts.

c. **Financial Statement Preparation.** The Air Force must use the DoD Uniform Chart of Accounts, based upon the US Government Standard General Ledger Chart of Accounts, to accumulate and report financial information. DFAS-DE first used the DoD Chart of Accounts in FY 1994 to categorize and prepare the Air Force financial statements, using a personal computer-based spreadsheet. In FY 1995, DFAS-DE began implementing the CFO Reporting System. When fully implemented, this system will extract data and categorize financial information in trial balance format through an automatic link to DOLARS, automatically prepare journal vouchers, and prepare the financial statements. The system will summarize to the US Government Standard General Ledger Chart of Accounts to produce the Air Force trial balance provided to the Department of the Treasury through the Federal Agencies' Centralized Trial Balance System. To produce the FY 1995 Air Force financial statements, DFAS-DE personnel entered the FY 1994 spreadsheet account balances into the CFO Reporting System and then manually entered journal vouchers into the system to adjust to FY 1995 account balances.

3. **FY 1995 Financial Statement Balances.** As of 30 September 1995, the Air Force Consolidated Statement of Financial Position reported total assets valued at about \$322.5 billion, liabilities of \$8.3 billion, and net position totaling \$314.2 billion. The Statement of Operations reported total revenues and financing sources of \$58.9 billion and expenses of \$59.1 billion. The Air Force budget authority for FY 1995 was about \$74.4 billion.

**INTERNAL CONTROLS**

4. **Purpose of Internal Controls.** The DoD Financial Management Regulation, DoD 7000.14-R, Volume I, states that the objectives of internal controls are to reasonably assure that:

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- Obligations and costs comply with applicable laws.
- All assets are safeguarded against waste, loss, unauthorized use, and misappropriation.
- Revenues and expenditures are recorded and accounted for properly so that accounts and reliable financial reports may be prepared and accountability of assets may be maintained.

5. **OMB Bulletin 93-06.** "Internal control structure," as it relates to the financial statements required by the CFO Act and as discussed in OMB Bulletin 93-06, means the plan of organization and policies and procedures adopted by management to provide reasonable assurance that the following objectives are met:

a. Transactions are properly recorded and accounted for to permit the preparation of reliable financial statements and to maintain accountability over assets.

b. Funds, property, and other assets are safeguarded against loss from unauthorized use or disposition.

c. Transactions, including those related to obligations and costs, are executed in compliance with (1) laws and regulations that could have a direct and material effect on the Principal Statements and where applicable, Combining Statements; and (2) any other laws and regulations that the OMB, entity management, or the Inspectors General have identified as being significant for which compliance can be objectively measured and evaluated.

6. **Other Authoritative Guidance.**

a. FMFIA of 1982.

(1) FMFIA, Section 2, requires each executive agency to report the status of management controls to the President and Congress annually by 31 December. The OMB developed guidelines in Circular A-123 (Revised), Management Accountability and Control, 21 June 1995, implemented by DoD and Air Force regulations, to meet Section 2 requirements. The status of management controls is reported via a Statement of Assurance and a Report on Material Weaknesses. The Statement of Assurance represents the agency head's informed judgment as to the overall adequacy and effectiveness of management controls within the agency.

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The Report on Material Weaknesses is the agency's vehicle for reporting plans to correct material weaknesses and progress against those plans. The Air Force annually evaluates its internal controls through the Internal Management Control program and reports the results to the Secretary of Defense.

(2) FMFIA, Section 4, requires each executive agency head to report annually to the President and the Congress whether its accounting systems are in conformance with Comptroller General principles and standards. The OMB developed guidelines in Circular A-127, Financial Management Systems, 23 July 1993, implemented by Air Force and DoD regulations, to meet Section 4 requirements. OMB guidance, further modified by DoD for its components, provides policies and procedures to develop, operate, evaluate, and report on financial management systems. Air Force guidance includes procedures for performing general and detailed accounting system reviews, determining material system weaknesses, and maintaining an accounting system inventory.

b. Defense Guidance. DoD Financial Management Regulation, DoD 7000.14-R, Volume 1, Chapter 7, May 1993, states the objectives of internal controls are to reasonably assure that (1) obligations and costs comply with applicable law; (2) assets are safeguarded against waste, loss, unauthorized use, and misappropriation; and (3) revenues and expenditures are recorded and accounted for properly so that accounts and reliable financial reports may be prepared and accountability of assets may be maintained. Control standards on documentation, recording of transactions and events, execution of transactions and events, separation of duties, supervision, and access to and accountability for resources are established to achieve those objectives.

## LAWS AND REGULATIONS

7. **Applicable Laws and Regulations.** Title 31, United States Code, (31 U.S.C. 3512, 3515); GAO Policy and Procedures Manual for Guidance of Federal Agencies, Title 2-Accounting; OMB Bulletin 94-01; and various other DoD, DFAS-DE, and Air Force regulations provide policy guidance and direction related to this audit. Among those, the significant provisions of the following pertain to this audit: DoD Directive 7000.14-R; DoD Directive 7200.1, Administrative Control of Appropriations, 7 May 1984; AFR 4-20, Volume 2, Disposition of Air Force Records, 1 May 1992; AFR 170-8; AFR 170-13, Accounting for Commitments, 30 July 1990; AFR 177-16, Administrative Control of Appropriations, November 1988; DFAS-DER 177-101; AFR 177-102, Commercial Transactions at Base Level, 15 November 1987; AFR 177-120, Central Procurement Transactions, 17 February 1988; AFM 177-370; DFAS-DER 177-373,

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DJMS-AC Financial Services Offices (FSO) Procedures, 1 November 1994; and AFM 177-372A, Volume I, Air Force Standard Civilian Automated Pay System (PA) Users Manual, 1 June 1994

a. 31 U.S.C. 3512. Sections of the CFO Act of 1990, the FMFIA of 1982, and the Budget and Accounting Procedures Act of 1950 are included in 31 U.S.C. 3512. Under 31 U.S.C 3512, the head of each agency is responsible for establishing and maintaining adequate systems of accounting and internal control. The law requires that these systems conform to Comptroller General accounting principles, standards, and related requirements and internal control standards. Agencies must report in an annual statement of assurance whether their accounting and internal control systems conform to Comptroller General standards.

b. Title 2. The GAO Policy and Procedures Manual for Guidance of Federal Agencies, Title 2-Accounting, contains Comptroller General accounting principles and standards with which 31 U.S.C. 3512 requires federal agencies to comply.

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## **AUDIT SCOPE AND PRIOR AUDIT COVERAGE**

### **AUDIT SCOPE**

1. Management is responsible for:
  - a. preparing the annual financial statements in conformity with applicable accounting principles;
  - b. establishing and maintaining internal controls and systems to provide reasonable assurance that the broad control objectives of FMFIA are met; and
  - c. complying with applicable laws and regulations.
2. The AFAA must plan and perform an audit to obtain reasonable assurance about whether (a) the financial statements are reliable (free of material misstatement and presented fairly in conformity with OMB Bulletin 94-01 and applicable accounting principles) and (b) relevant internal controls are in place and operating effectively. The AFAA must also test compliance with selected provisions of laws and regulations and perform limited audit procedures with respect to testing the consistency of other information presented in the annual financial statement with the consolidated financial statements.
3. To fulfill these responsibilities, we
  - a. examined, on a test basis, evidence supporting the amounts and disclosures in the financial statements;
  - b. assessed the accounting principles used and significant estimates made by management;
  - c. evaluated the overall presentation of the financial statements;
  - d. considered compliance with the process required by FMFIA for evaluating and reporting on internal control and accounting systems;
  - e. tested compliance with selected provisions of laws and regulations listed at Appendix III;

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- f. evaluated and tested relevant internal controls; and
  - g. obtained audit support from the DoD Office of Inspector General (DoDIG) at DFAS-DE, and the Defense Contract Audit Agency (DCAA) at selected contractor facilities.
4. We did not evaluate all internal controls relevant to operating objectives as broadly defined by FMFIA, such as those controls relevant to preparing statistical reports and ensuring efficient operations. We limited our work to accounting and other controls necessary to achieve the objectives outlined in our opinion on internal controls. Because of inherent limitations in any system of internal control, losses, noncompliance, or misstatements may nevertheless occur and not be detected. During the audit, we relied on computer-based data, although the scope of our audits did not always include a comprehensive test of system general and application controls to confirm the reliability of data. We also caution that projecting our evaluation to future periods is subject to the risk that controls may become inadequate because of changes in conditions or that the degree of compliance with controls may increase or deteriorate.
5. We accomplished the audit from May 1995 to January 1996 at SAF/FM; Deputy Chief of Staff for Logistics (AF/LG); 3 major command headquarters; 62 Air Force active duty, reserve, and guard locations; and 32 DFAS locations (DFAS-HQ, DFAS centers, DFAS operating locations, and DAOs). Specific locations are listed in the individual audit reports identified at Appendix IV. A draft of this report was provided to management in February 1996.
6. We conducted our audit in accordance with generally accepted government auditing standards and the provisions of OMB Bulletin 93-06. To the extent that audit results relate to activities at DFAS-DE, those results were based in part on DoDIG audit work and DCAA audit work at selected contractor facilities in support of our audit of GFP, draft Report of Audit 96053011. We believe our audit and the audit work of DoDIG and DCAA provide a reasonable basis for our opinion on Air Force consolidated financial statements.

**PRIOR AUDIT COVERAGE**

7. During the past 5 years, the GAO and the DoDIG each issued four reports addressing subjects related to issues in this report. In addition, AFAA issued audit opinions on the FYs 1992, 1993, and 1994 Air Force consolidated financial statements.

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a. **GAO Reports.** The four GAO reports included two reports on Air Force financial management and two reports on DoD-wide financial management.

(1) GAO Report AFMD 92-12, Financial Audit: Aggressive Actions Needed for Air Force to Meet Objectives of the CFO Act, 19 February 1992. The GAO concluded that Air Force accounting systems generated unreliable and inaccurate financial information which were of little value for either internal management purposes or external reporting. Additionally, the GAO found that the Air Force system of internal controls did not adequately safeguard all assets nor ensure that account payments and financial reports were reliable. The DoD stated that actions have been taken or are planned to address internal control weaknesses and inaccurate financial reporting problems discussed in this report.

(2) GAO Report NSIAD 94-106, DoD Procurement: Millions in Overpayments Returned by DoD Contractors, 14 March 1994. The GAO concluded that virtually all overpayments examined were detected by the contractors rather than the government. The GAO further concluded that contractor over-payments resulted because DFAS-CO either paid contractor invoices without recovering progress payments or made duplicate payments. The DoD stated that actions were being taken to clarify and strengthen payment practices, reinforce prompt debt collection procedures, and issue clearly stated and complete contract documents to deal with contractor overpayments.

(3) GAO Report AIMD 95-7, Financial Management: Status of Defense Efforts to Correct Disbursement Problems, 5 October 1994. The GAO found DoD records contained at least \$24.8 billion of problem disbursements as of 30 June 1994, including about \$5 billion related to canceled "M" account balances that DoD had been unable to reconcile. GAO concluded that despite numerous audit reports over the last 14 years that repeatedly identified DoD internal control weaknesses, DoD continued to experience serious problems in accounting for disbursements. GAO stated the DoD will not adequately resolve disbursement problems until the department corrects weaknesses in control procedures, which allow problem disbursements to occur, and improves the DoD contract pay and accounting systems. This report did not include management's response to the issues and findings addressed in the report.

(4) GAO Report NSIAD 96-8, Millions in Contract Payment Errors Not Detected and Resolved Promptly, 6 October 1995. The GAO concluded that contractors do not always return overpayments unless told to do so. Further, DFAS-CO cannot readily detect payment discrepancies because of significant errors in its automated payment records. GAO also found that even after a public

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accounting firm completed contract reconciliations to identify the amounts owed the government, DFAS-CO did not recover payments promptly. This report did not include management's response to the issues and findings addressed in the report.

b. DoDIG Reports. The four DoDIG reports summarized their audit work related to the Air Force FYs 1992, 1993, and 1994 financial statements.

(1) DoDIG Report 94-073, Defense Finance and Accounting Service Work on the Air Force FY 1992 Financial Statements, 31 March 1994. DoDIG concluded that DFAS-DE did not prepare complete, accurate, and reliable FY 1992 Air Force financial statements. They reported that DFAS-DE did not comply with the DoD Accounting Manual or maintain effective procedures and internal controls over its systems. In addition, DoDIG determined that internal controls over the budgetary process were ineffective. Further, the audit disclosed that the Statement of Operations did not include all activity affecting Air Force operations. As a result, revenues were overstated by \$424.5 million; support for operating expenses was unavailable for leases of \$8.3 billion, asset damage of \$568.7 million, and bad debts of \$24.7 million; extraordinary losses of \$1.2 billion were excluded; and prior period adjustments of \$13.0 billion were incorrect or omitted. Finally, DoDIG concluded DFAS-DE did not validate the accuracy of construction-in-progress data and did not adhere to Air Force guidance on government-furnished material and contractor-acquired material when preparing the financial statements.

(2) DoDIG Report 95-067, Defense Finance and Accounting Service Work on the Air Force FY 1993 Financial Statements, 30 December 1994. DoDIG reported that DFAS-DE did not adequately monitor US Treasury clearing accounts. Specifically, DFAS-DE did not reconcile differences, maintain accounts related to contract payments, monitor old accounts, or prepare written procedures for account oversight. These conditions could allow improper payments to go undetected and cause DAOs to lose their authority to disburse available appropriated funds. DoDIG also reported that accounts receivable and payable reported on the FY 1993 financial statements contained material errors because internal controls over manual computations used to calculate these balances did not ensure that only Air Force data were presented in the statements. DFAS-DE included a claim (receivable) against a contractor on a foreign military sales direct cite contract and a corresponding payable amount to the Foreign Military Sales Trust Fund. As a result, Accounts Receivable-Public and Accounts Payable-Federal were overstated by \$605 million each. DFAS-DE either concurred or concurred in principle with all recommendations and agreed to establish policies

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and procedures to monitor US Treasury clearing accounts and to improve the processes used to compile and compute the amounts shown on the financial statements.

(3) DoDIG Report 95-264, Defense Finance and Accounting Service Work on the Air Force FY 1994 Finance Statements, 29 June 1995. DoDIG reported that DFAS-DE did not adequately monitor the MAFR system because they did not designate a security manager for the system. Further, DFAS-DE did not perform periodic reviews to determine whether individuals had a continued need for access, and had not prepared written procedures for system security oversight. In addition, DoDIG reported that the MAFR system does not maintain audit trails or transaction histories for transactions originating at DFAS-DE. DFAS-DE agreed to complete a center operating instruction on MAFR system security by 30 September 1995. To correct the lack of an audit trail, DFAS-DE will implement the Defense Cash Management System during January 1998.

(4) DoDIG Report 95-301, Major Deficiencies Preventing Auditors From Rendering Audit Opinions on DoD General Fund Financial Statements, 29 August 1995. DoDIG identified four major deficiencies preventing auditors from rendering audit opinions: adequate accounting systems were not in place; assets were not reported adequately or valued properly; disbursements and collections were not adequately disclosed; and contingent liabilities were not recognized or adequately disclosed. The DoDIG used examples of Air Force deficiencies cited in the AFAA reports referenced in paragraph 7c below. In addition, DoDIG reported the following. The Air Force selected five accounting systems as the interim migratory accounting system to allow the Air Force to meet accounting system standards. While DFAS-DE established a September 1998 date for implementation, the interim migratory accounting system has not been approved by the Air Force or DFAS Headquarters. Further, military department auditors note that the planned general ledger systems will not fully integrate financial management systems with nonfinancial systems such as acquisition, logistics, supply, civil engineering, and other systems that compile data needed by the financial systems. DoDIG stated the DoD, DFAS, and military departments have initiated actions to resolve the disbursement, collection, and contingent liability issues, but that actions to date have not removed these impediments to issuing an audit opinion. The report contained no recommendations requiring management action.

c. AFAA Reports. AFAA issued audit opinions on the FYs 1992, 1993, and 1994 Air Force consolidated financial statements.

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(1) Report of Audit 92053011, Opinion on Fiscal Year 1992 Air Force Financial Statements, 29 June 1993. The report disclaimed an opinion on the FY 1992 Air Force consolidated financial statements because of material uncertainties related to the reasonableness of amounts reported in the financial statements and the adequacy of Air Force accounting systems. DFAS-DE assembled amounts reported on the statements from a variety of separate information systems of uncertain reliability and for most items auditors were unable to verify account balances. In addition, Air Force management did not provide management or legal representation letters. Also, the Air Force internal control structure did not provide reasonable assurance of achieving the internal control objectives described in OMB Bulletin 93-06. Finally, the Air Force did not fully comply with laws and regulations that materially affect the financial statements.

(2) Report of Audit 94053022, Opinion on Fiscal Year 1993 Air Force Consolidated Financial Statements, 30 June 1994. We reported the conditions found in FY 1992 continued in FY 1993, resulting in a disclaimer of opinion on the FY 1993 Air Force consolidated financial statements. Air Force and accounting personnel accounting errors found in the property, plant, and equipment and real property accounts ranged from \$83 million to \$18 billion, and DFAS-DE disbursement and collection records contained over 12,000 unreconciled differences valued at \$3.3 billion. While Air Force physical controls over assets were generally effective, Air Force and DFAS controls used to compile and report accurate, complete, and reliable financial information required improvement. Existing Air Force and DFAS systems and controls impacted their ability to fully comply with laws and regulations materially affecting the financial statements, and noncompliance with other laws and regulations that materially affect the financial statements was also noted.

(3) Report of Audit 94053001, Opinion on Fiscal Year 1994 Air Force Financial Statements, 1 March 1995. This report also disclaimed an opinion in FY 1994 Air Force and DFAS accounting errors caused double counting and over and understatements of financial statement lines ranging from \$9.4 million to \$1.8 billion. The financial statement line items affected included accounts receivable; accounts payable; operating expenses; property, plant, and equipment; progress payments; and the contingent liabilities footnote which understated this liability by \$72.3 billion. DFAS-DE's presentation of negative unliquidated obligations resulted in less than full disclosure of conditions and an understatement of over \$1.5 billion. Air Force was not using the DoD Uniform Chart of Accounts, controls over computers continued to be lacking, independent verifications of sensitive assets were not always performed, and weaknesses were

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noted in computer system access and cash controls. Existing Air Force and DFAS policies, procedures, systems, and controls caused the Air Force to be in danger of violating the Antideficiency Act, FMFIA, and the Prompt Payment Act. DAO noncompliance with DoD and Air Force regulations was noted, primarily in not performing required reconciliations.

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## **LAWS AND REGULATIONS**

We reviewed significant provisions of the laws and regulations listed below.

### **Public Laws**

Antideficiency Act, ch. 510 3, 34 Stat. 49 (codified as amended in 31 U.S.C. ss1341, 1342, 1349-1351, 1511-1519 [1988])

Budget and Accounting Procedures Act of 1950, ch. 946, 64 Stat. 832 (codified as amended in various sections of 31 U.S.C.)

Chief Financial Officers Act of 1990, Pub. L. No. 101-576, 104 Stat. 2838 (codified in various sections of 5 U.S.C., 31 U.S.C., 38 U.S.C., 42 U.S.C.)

Civil Service Retirement Act of 1930, ch. 34 1-18, 46 Stat. 468, as renumbered 31 July 1956, ch. 804, title IV, s401 70 Stat. 743 (codified as amended in 5 U.S.C. ss1308, 3323, 8331-8348 [1988])

Civil Service Reform Act of 1978, Pub. L. No. 95-454, 92 Stat. 1111 (codified in various sections of 5 U.S.C., 10 U.S.C., 15 U.S.C., 28 U.S.C., 38 U.S.C., 39 U.S.C., 42 U.S.C.)

Dual Compensation Act of 1964, Pub. L. No. 88-488, 19 August 1964

Fair Labor Standards Act of 1938, ch. 676, 52 Stat. 1060 (codified as amended in 29 U.S.C. ss201-219 [1988])

Federal Debt Collection Procedures Act of 1990, Pub. L. No. 101-647, Title XXXVI, Subtitle A, ss3611, 104 Stat. 4933 (codified in various sections of 28 U.S.C.)

Federal Employees' Compensation Act, ch. 458, 39 Stat. 742 (codified as amended in various sections of 5 U.S.C.)

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Federal Employees' Group Life Insurance Act of 1980, Pub. L. No. 96-427, 94 Stat. 1831 (codified in various sections of 5 U.S.C.)

Federal Employees Health Benefits Act of 1959, Pub. L. No. 86-382, 73 Stat. 708 (codified as amended in various sections of 5 U.S.C.)

Federal Managers' Financial Integrity Act of 1982, Pub L. No. 97-255, 96 Stat. 814, 31 U.S.C. ss1105, 1113, 3512 (1988)

Government Management Reform Act of 1994, Pub. L. No. 103-356, 13 October 1994, 108 Stat. 3412-3416

Prompt Payment Act, Pub. L. No. 97-177, 96 Stat. 85, 31 U.S.C. ss3901-3906 (1988)

**GAO Guidance**

Title 2, GAO's Policy and Procedures Manual for Guidance of Federal Agencies, 31 August 1987, and Title 7, Fiscal Guidance, July 1992

**OMB Bulletins and Circulars**

OMB Bulletin 94-01, Form and Content of Agency Financial Statements, 16 November 1993

OMB Circular A-34 (Revised), Instructions on Budget Execution, 8 August 1985

OMB Circular A-123, Management Accountability and Control, 21 June 1995

OMB Circular A-125 (Revised), Prompt Payment, 12 December 1989

OMB Circular A-127, Financial Management Systems, 23 July 1993

OMB Internal Control Guidelines, December 1982

**Treasury Guidance**

Treasury Financial Manual, Volume 1, For Guidance of Departments and Agencies, Transmittal Letter 521 Posted 2 April 1992

**Federal Accounting Standards Advisory Board**

Statement of Federal Accounting Standards Number 3, Accounting for Inventory and Related Property, 27 October 1993

**DoD Guidance**

DoD 5010.38, Internal Management Control Program, 14 April 1987

DoD 7000.14-R, Financial Management Regulation, Volume 1, General Financial Management Information, Systems, and Requirements, May 1993

DoD 7000.14-R, Financial Management Regulation, Volume 4, Accounting Policies and Procedures, January 1995

DoD 7000.14-R, Financial Management Regulation, Volume 5, Disbursing Policy and Procedures, December 1993

DoD 7000.14-R, Financial Management Regulation, Volume 7A, Military Pay and Allowances Entitlements Manual, December 1994

DoD 7000.14-R, Financial Management Regulation, Volume 8, Civilian Pay Policy and Procedures, January 1995

DoD 7220.9-M, Department of Defense Accounting Manual, 11 October 1985

DoD Directive 7200.1, Administrative Control of Appropriations, 7 May 1984

DoD Guidance on Form and Content of Financial Statements for FY 1994 and FY 1995 Financial Activity, 20 October 1994

**Defense Finance and Accounting Service Directives**

DFAS-DER 170-9, Fiscal Year-End Certification of Appropriation and Fund Balances, 30 June 1994

DFAS-DER, 177-101, General Accounting and Finance Systems at Base Level, 15 February 1991

DFAS-DER 177-104, Civilian Pay Transactions at Base Level, 30 August 1993

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DFAS-DE Manual 177-373, DJMS-AC Financial Services Offices (FSO) Procedures, 1 November 1994

**Air Force Directives**

AFR 4-20, Volume 2, Disposition of Air Force Records, 1 May 1992

Air Force Instruction (AFI) 21-103, Equipment Inventory, Status, and Utilization Reporting, 1 July 1995

AFI 21-202, Combat Ammunition System Procedures, 25 July 1994

Air Force Policy Directive 23-5, Reusing and Disposing of Materiel, April 1993

AFI 24-301, Vehicle Operations, April 1995

AFM 30-130, Base-Level Military Personnel System Users Manual, Volume I, 1 September 1992

AFI 32-6005, Unaccompanied Housing Management & Operations, 28 April 1994

AFI 32-9005, Real Property Accountability and Reporting, 30 September 1994

AFI 33-112, Automatic Data Processing Equipment (ADPE) Management, 6 May 1994

AFI 65-601, Volume I, Budget and Guidance Procedures, 21 October 1994

AFM 67-1, USAF Supply Manual, Volume I, Part One, and Volume II, Part Two, 1 July 1992

AFM 67-1, USAF Supply Manual, Volume I, Part Three, 26 June 1995

AFM 67-1, USAF Supply Manual, Volume II, Part Two, 1 October 1994

AFM 67-1, USAF Supply Manual, Volume II, Part Thirteen, 1 April 1994

AFM 136-824, Combat Ammunition System-Base, Volume I, March 1995, and Volume II, November 1991

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AFR 170-8, Accounting for Obligations, 15 January 1990

AFR 170-13, Accounting for Commitments, 30 July 1990

AFR 177-16, Administrative Control of Appropriations, 30 November 1988

AFP 177-31, General Funds General Ledger Accounting Procedures, 31 December 1991

AFR 177-102, Commercial Transactions at Base Level, 15 November 1987

AFR 177-120, Central Procurement Transactions, 17 February 1988

AFM 177-206, Automated Materiel Accounting System Integrated Within Standard Base Supply System: D00A/GV Users Manual, 1 October 1994

AFM 177-370, USAF Standard Base-Level General Accounting and Finance System: H069/BQ, 5 February 1994

AFM 177-372A, Volume I, Air Force Standard Civilian Automated Pay System (PA) Users Manual, 1 June 1994, and Volume II, Time and Attendance Reporting Civilian Pay System, December 1989.

AFM 177-373, Volume III, Defense Joint Military Pay System-Reserve Component Pay Manual, 1 January 1994

AFM 177-375, Medical Materiel Accounting System: H101/BV, 1 March 1991

AFR 177-390, Volume 4, Disbursing Officers Database Management System (DMS) Security H121H/TZ, 1 November 1993

Technical Order (TO) 00-25-2540-1, Comprehensive Engine Management System Engine Configuration, Status, and TCTO Reporting Procedures, 1 October 1992

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Appendix B. AFAA Report, "Opinion on Fiscal Year 1995 Air Force Consolidated Financial Statements"

**Project 95053001**

**ASSOCIATED AIR FORCE REPORTS OF AUDIT**

<u>Report Title</u>	<u>Report Number</u> <u>Date Issued</u>
Review of Property, Plant, and Equipment, Fiscal Year 1995 Air Force Consolidated Financial Statements	95053002 *30 Jan 96
Review of the Fund Control Process, Fiscal Year 1995 Air Force Consolidated Financial Statements	95053003 X Xxx XX
Review of Military Pay, Fiscal Year 1995 Air Force Consolidated Air Force Financial Statements	95053004 *29 Jan 96
Review of Operating Materials and Supplies, Fiscal Year 1995 Air Force Consolidated Financial Statements	95053005 *23 Feb 96
Review of Weapon System Progress Payments, Fiscal Year 1995 Air Force Consolidated Financial Statements	96053010 *20 Feb 96
Review of Government Furnished Property, Fiscal Year 1995 Air Force Consolidated Financial Statements	96053011 X Xxx XX
Review of Civilian Pay, Fiscal Year 1995 Air Force Consolidated Financial Statements	96053012 *29 Jan 96
Review of Contingent Liabilities, Fiscal Year 1995 Air Force Consolidated Financial Statements	96053013 *29 Jan 96
Review of Cash Operations, Fiscal Year 1995 Air Force Consolidated Financial Statements	96053014 *6 Feb 96

\* Date draft report of audit was released to management

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**Project 95053001**

**ACTIVITIES CONTACTED  
DURING THE AUDIT**

**Organization**

**Headquarters United States Air Force**

Office of the Assistant Secretary of the  
Air Force for Financial Management and  
Comptroller (SAF/FM)

Office of the Air Force  
General Counsel (SAF/GC)

Deputy Chief of Staff  
Logistics (AF/LG)

**Air Force Field Operating Agencies/Direct Reporting Units**

Air Force Legal Services Agency (AFLSA)

Air Force Management Engineering Agency (AFMEA)

Air Force Personnel Center (AFPC)

Air Force Recruiting Service (AFRS)

Air Force Services Agency (AFSVA)

11th Wing (11 WG)

**Defense Contract Audit Agency**

Boeing Resident Office  
Boeing Defense & Space Group, Kent WA

Boston Branch Office-MIT Suboffice  
Massachusetts Institute of Technology-  
Lincoln Laboratory, Cambridge MA

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**Activities Contacted During the Audit**

**Defense Contract Audit Agency (Cont'd)**

Central Region Resident Office  
Lockheed Martin Astronautics, Denver CO

Dallas Branch Office/Irving TX  
Chrysler Technology Airborne Systems, Waco TX

Huntsville Branch Office, Huntsville AL  
Pemco Aeroplex, Inc, Birmingham AL

Lockheed Fort Worth Resident Office  
Lockheed Fort Worth Company, Fort Worth TX

Lockheed Martin Aeronautical Systems Resident Office  
Lockheed Martin Aeronautical Systems, Marietta GA

Lockheed Martin Valley Forge Resident Office  
Lockheed Martin Astro Space, King of Prussia PA

McDonnell Douglas Aerospace Resident Office  
McDonnell Douglas Aerospace, Transport Aircraft  
Huntington Beach CA

Rockwell International Corporation Resident Office  
Rockwell International Corporation-  
North American Aircraft Division, Seal Beach CA  
Space Systems Division, Downey CA

St. Louis Branch Office  
Boeing Defense & Space Group, Wichita KS

**Defense Finance and Accounting Service (DFAS)**

Defense Finance and Accounting Service-Headquarters

Defense Finance and Accounting Service-Columbus Center (DFAS-CO)

Defense Finance and Accounting Service-Denver Center (DFAS-DE)

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**Activities Contacted During the Audit**

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**Office of Inspector General-Department of Defense (OIG-DOD)**

Office of the Assistant Inspector General  
for Auditing (OAIG-AUD)

Office of the Assistant Inspector General  
for Auditing, Finance and Accounting  
Directorate (OAIG-AUD-FA)

Office of the Assistant Inspector General  
for Auditing, Finance and Accounting  
Directorate, Denver and Columbus Field Offices  
(OAIG-AUD-FD and OAIG-AUD-FC)

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**MAJOR CONTRIBUTORS TO THIS REPORT**

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Rosalind A. Rees, Audit Manager

Mary L. Mattson, Auditor

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Project 95053001

**FINANCIAL STATEMENTS AND NOTES**

*Department of the Air Force*

Chief Financial  
Officer  
Annual Financial  
Statement  
FY 1995

March 1, 1996

**Project 95053001**

**Financial Statements and Notes**

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***DEPARTMENT OF THE AIR FORCE  
GENERAL FUNDS***

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Footnotes to the Principal Statements.....  
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***DEPARTMENT OF THE  
AIR FORCE***

***GENERAL FUNDS***

***OVERVIEW***

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GENERAL STATEMENT

The Air Force vision -- *Global Reach - Global Power* -- remains our fundamental strategy for building the future Air Force. It is a living strategy that was first put to the test during Operation Desert Storm and proved sound. Since Operation Desert Storm, that strategy has been more rigorously tested by global involvement in operations involving tens of thousands of flying hours and an operating tempo far beyond our Cold War norm. *Global Reach - Global Power* met this challenge; and we are confident the basic principles of *Global Reach - Global Power* will continue to serve the Air Force and our nation well into the next century. Indispensable to actualizing this far-reaching vision is the effective use of people, places, and things.

# Appendix B. AFAA Report, "Opinion on Fiscal Year 1995 Air Force Consolidated Financial Statements"

**Project 95053001**

**Financial Statements and Notes**

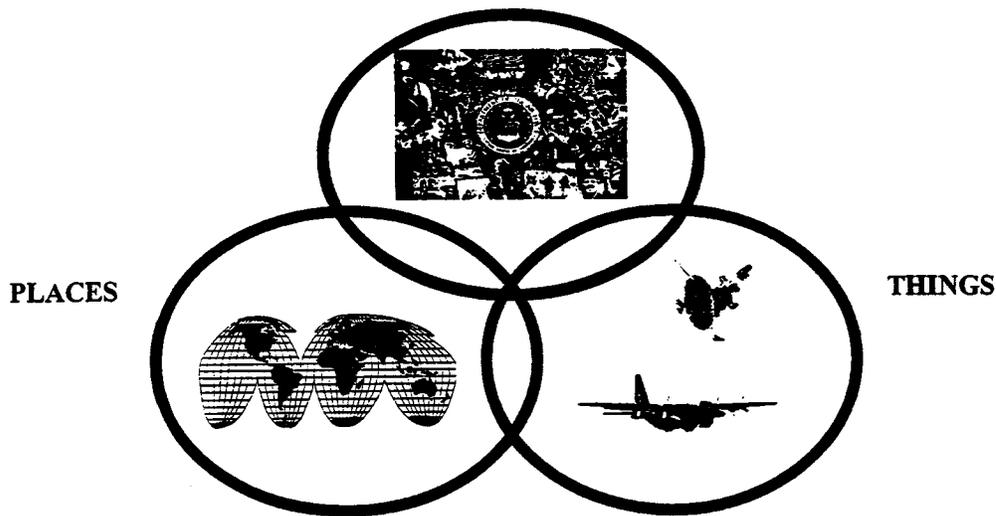
## Overview

### ***FUNDAMENTALS FOR A QUALITY AIR FORCE***

As stewards of the nation's air and space forces, it is critical we responsibly allocate our resources to build a force capable of meeting future demands. The forward-looking initiatives of recent years have produced an air and space force that is proficient, versatile, and tailored to support our National Security Strategy. We will continue to execute our responsibilities with the disciplined approach we have followed in the past. This approach is based on four key commitments:

- Recruit quality people and ensure they are trained and motivated to operate in a disciplined manner, and exhibit and respect Service core values - *People*
- Ensure our people and their families have the quality of life they deserve as they serve our nation - *People*
- Define our operational requirements and provide *Global Reach - Global Power* capabilities with a clear vision of what the Air Force contributes to the U.S. military's joint team - *Places*
- Fill equipment requirements with a lean and agile acquisition system - *Things*

### **PEOPLE**



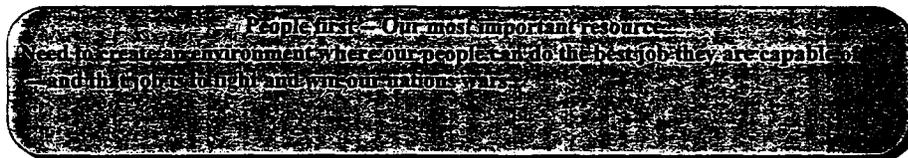
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**PEOPLE**



**INITIATIVES**

Fair and Equitable Compensation	<ul style="list-style-type: none"> <li>• Support maximum military pay raises</li> <li>• Prevent accelerated growth of military/civilian pay gap</li> <li>• Decrease "out of pocket" permanent change of station (PCS) costs</li> </ul>
Safe and Affordable Housing	<ul style="list-style-type: none"> <li>• Upgrade living standards for airman dormitories</li> <li>• Obtained one time adjustment to Basic Allowance for Quarters (BAQ) rates in FY 96 - 5.2% increase</li> <li>• Establish Variable Housing Allowance (VHA) locality floors</li> </ul>
Base and Community Programs	<ul style="list-style-type: none"> <li>• Provide child care for 43,000 children daily - still 8,000 spaces short (most under 3 years old)</li> <li>• Building new centers and refurbishing others to expand our capabilities</li> <li>• Preserve commissaries -- valued savings</li> </ul>
Accessible Quality Health Care	<ul style="list-style-type: none"> <li>• Support DoD health care initiatives: TRICARE; Overseas Family Member Dental Program</li> </ul>
Educational Opportunities	<ul style="list-style-type: none"> <li>• Expand Tuition Assistance</li> <li>• Preserve Montgomery GI Bill - 95% of those entering Air Force enroll in the program</li> </ul>
Reduce Operations Tempo	<ul style="list-style-type: none"> <li>• Achieve less than 120 deployed days per person per year                             <ul style="list-style-type: none"> <li>• Global sourcing to balance the work load</li> <li>• Reduced tasking where appropriate</li> <li>• Seek new ways to use Guard and Reserve Forces</li> </ul> </li> </ul>

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**PLACES**

The Air Force can do anything, at anytime, to perform any mission to defend the United States, its allies, and vital interests. Aerospace power also means providing help, domestically and internationally, for diplomatic and humanitarian purposes, and to support other U.S. objectives worldwide.

*Anywhere*

*Anytime*



*Any Mission*

# Appendix B. AFAA Report, "Opinion on Fiscal Year 1995 Air Force Consolidated Financial Statements"

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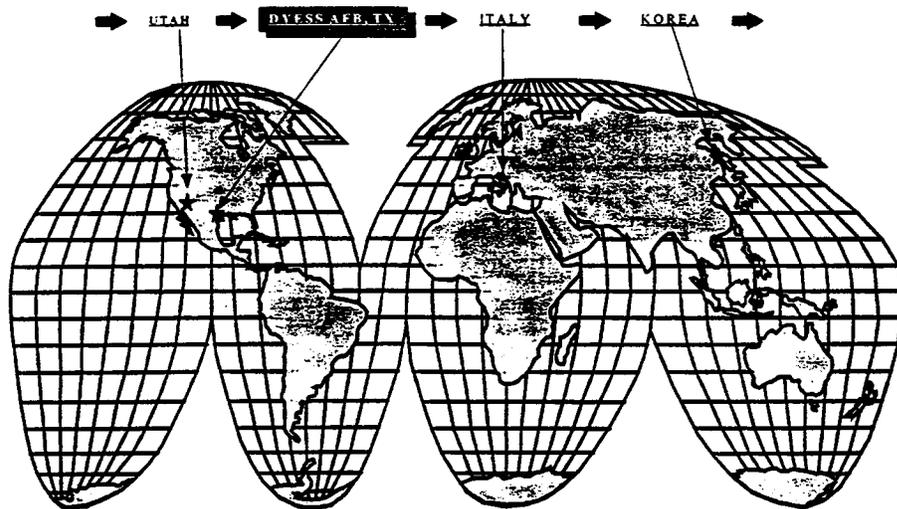
## Overview

### *Versatile Combat Forces*

The United States Air Force provides superior air and space forces, combining the responsiveness and firepower of long range bombers and the flexibility of sophisticated fighters with the global presence of an air and space command, control, communications, computers, and intelligence (C<sup>4</sup>I) architecture.



Air Force bombers can reach any point on the globe with lethal strikes in 20 hours.



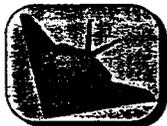
This was most visibly demonstrated in July, when the men and women of Dyess AFB, Texas, launched and recovered two B-1Bs that flew nonstop around-the-world after delivering ordnance on military training ranges in Italy, Korea, and Utah.

# Appendix B. AFAA Report, "Opinion on Fiscal Year 1995 Air Force Consolidated Financial Statements"

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## Overview



Our rapid deployable fighter forces provide us the staying power to overwhelm an opponent's forces, infrastructure, and command elements.



In September, NATO air operations in Bosnia once again proved air power can have a decisive role when serving explicit policy objectives. Air power's efforts in helping lift the siege of Sarajevo saved lives and helped pave the way for new negotiations, and eventually resulted in a peace treaty among the parties involved in this troubled part of the globe. The Air Force's success again demonstrates the value of unquestioned air dominance.

However, air superiority is not an American birthright. It is a mission area in which the Air Force has no desire or intention of fighting an equal fight. Future success rests on the next generation fighter, the F-22. The F-22's lethal combination of stealth, super cruise, and advanced integrated avionics will provide an unmatched capability for decades to come.

**F-16**



**F-22**



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APPENDIX VII

Overview



America's air mobility fleet gives our nation the speed and agility to respond to the full range of contingencies. No other nation in the world has this capability. Airlifters and tankers can deploy fighting forces or humanitarian assistance worldwide.

Assistance for victims of Hurricanes Marilyn & Opal



Operation Provide Promise



Operation Provide Comfort



The C-17 program has overcome past challenges and is now proving a highly capable military airlifter to lead our global military force into the next century. Additionally, the Air Force is modernizing its tried and proven C-130 fleet by replacing older models with the updated C-130J.

**Overview** \_\_\_\_\_



Space offers an unsurpassed vantage point and the possibility to access any point on the earth's surface in a matter of minutes. Militarily, this means the U.S. gains an extraordinary advantage.

**THE  
ULTIMATE HIGH GROUND**



By continuing to modernize, we strengthen our advantage. During the past year, contracts were awarded for:

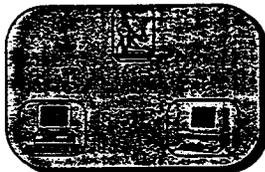
- A Space Missile Tracking System
- Space Based Infrared Systems (SBIRS), which will provide enhanced missile detection and critical tracking data for national and theater missile defense
- The Evolved Expendable Launch Vehicle (EELV) program. This program will provide a family of low cost launch vehicles for both military and commercial access to space

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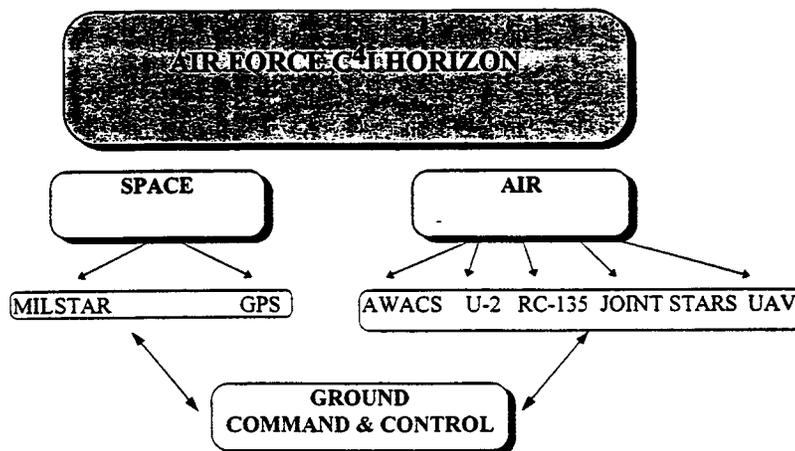
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Dominating the information spectrum has become as critical to conflict as occupying the land or controlling the air. The Air Force believes that if we can analyze, assess, and act faster than our adversary - we will win. At the heart of this process is:



To face these challenges we:

- Activated our first Unmanned Aerial Vehicle (UAV) squadron
- Implemented an expansive base information infrastructure of fiber optic networks
- Will activate an Information Warfare Squadron in August 1996

**Overview**

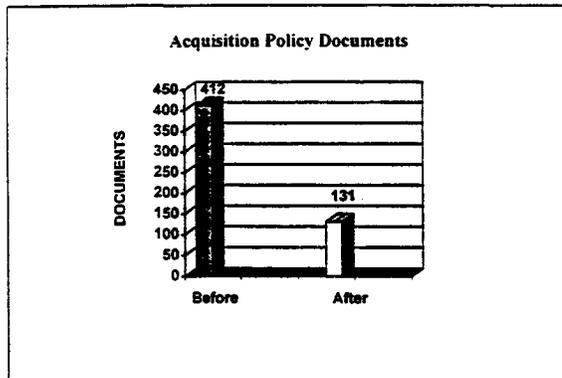
***THINGS***

The Air Force must continue to modernize its force with systems that possess clear and viable operational advantages. By reforming acquisition processes, optimizing our resources, and increasing our use of the commercial sector, we will develop a lean, agile acquisition system able to meet our challenges.

***Acquisition Reform***

At the heart of reform efforts are Lighting Bolt Initiatives -- designed to jump start cultural, business, and process changes:

- Revamping how we:
  - define requirements
  - select major systems contractors
  - manage programs
  - establish business arrangements
- Lighting Bolt Successes:



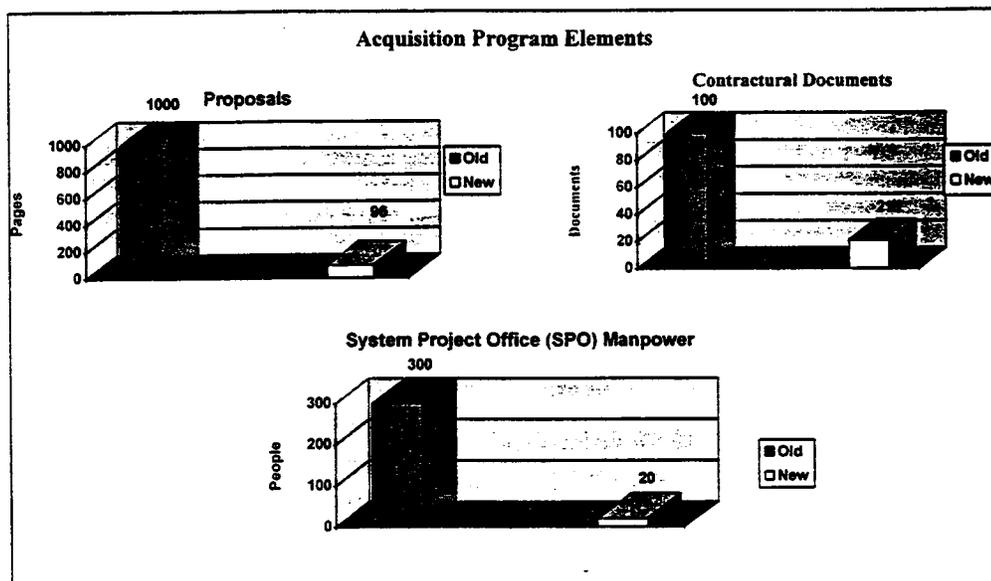
The Air Force took concentrated action to eliminate obsolete or redundant acquisition policies. Result was a 68% reduction in acquisition policy documents.

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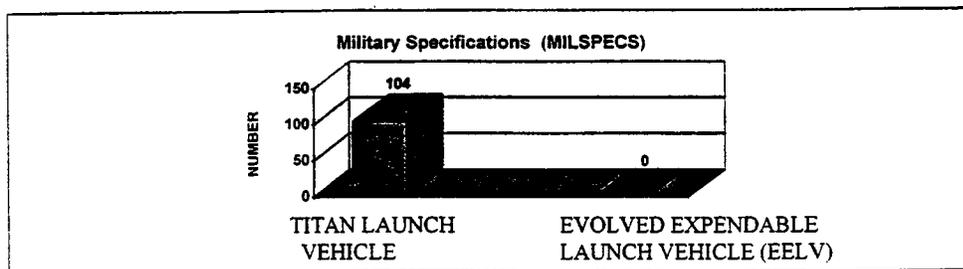
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In the past acquisition programs generated an inordinate amount of paperwork and SPO manning generally tended to be on the "heavy" side. Our success in streamlining these areas is shown by the contrast between the new Wind Corrected Munition Dispenser Program and what was the old norm.



We are also making a concerted effort to reduce or even eliminate the number of MILSPECS in procurement programs. As shown above, we were extremely successful in the EELV program.

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*Optimizing Resources*

To realize more economical and efficient acquisition programs, we have moved increasingly into cooperative programs with industry, other Services, other government agencies, and our allies:

**Other Services**

<b>Program</b>	<b>Results</b>
Joint Primary Aircraft Training System (JPATS)	<ul style="list-style-type: none"> <li>• Combined acquisition efforts when needs coincided</li> <li>• Increased savings in dollars and manpower</li> </ul>
Joint Strike Fighter (JSF)	<ul style="list-style-type: none"> <li>• Agreed to divide expenses and expertise with the Navy</li> <li>• Expect this approach to facilitate development of an affordable multi-role aircraft</li> </ul>

**Other Government Agencies**

<b>Project</b>	<b>Results</b>
National Polar Orbiting Operational Environmental Satellite System (NPOESS)	<ul style="list-style-type: none"> <li>• Combined meteorological satellite program with Department of Commerce</li> <li>• Anticipate savings of \$300 million</li> </ul>

**Joint - Service and International Science & Technology Programs (S&T)**

<b>Partner</b>	<b>Project</b>
France/Germany	<ul style="list-style-type: none"> <li>• S&amp;T Program to extend range of air-to-air missiles</li> </ul>
Navy/Multinational	<ul style="list-style-type: none"> <li>• New expanded crew ejection seat systems</li> </ul>
Joint Service/Multinational	<ul style="list-style-type: none"> <li>• Speakeasy radio program system</li> <li>• Provide near-seamless communication abilities for our joint-service and allied operations</li> </ul>

Overview

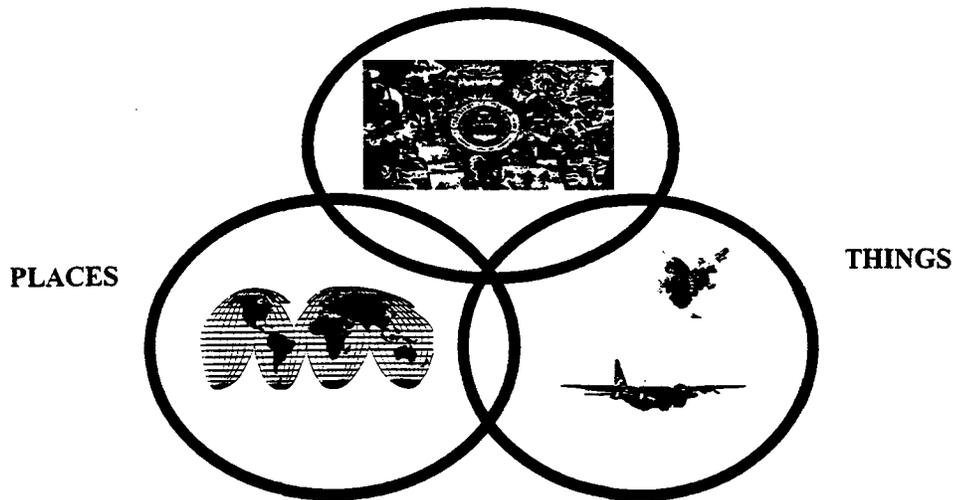
*Commercialization*

Breaking down the barriers between the defense and commercial sectors of the economy leads to better use of resources.

Commercial Sector Initiative

Project	Results
Evolve expendable Launch Vehicle (EELV)	<ul style="list-style-type: none"> <li>• Included commercial sector members on the team</li> <li>• Removed layers of management</li> <li>• Eliminated military specifications</li> <li>• Satisfied needs of the military and helped U.S. industry bolster its position in world space-launch market</li> </ul>

PEOPLE



***ENHANCING AIR FORCE HEADQUARTERS***

Pulling all this together requires an enhancement to the Air Force management structure. Balancing the competing demands of quality of life, modernization, and readiness, while preparing for the future requires enlightened decision making. Because *Global Reach - Global Power* exists in a dynamic environment -- influenced by sudden surges in technology and major shifts in the security environment-- we streamlined planning and programming to maximize our effectiveness and our efficiency. The result is that now, the Air Force is appropriately postured to take full advantage of opportunities on the horizon.

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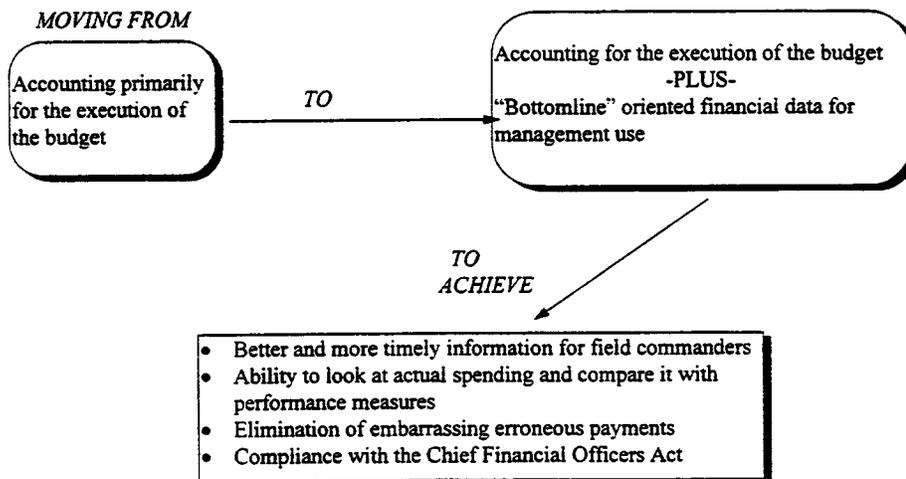
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**FINANCIAL ISSUES**

**THE FUTURE OF FINANCIAL MANAGEMENT IN THE AIR FORCE  
IN LIGHT OF HISTORIC CHANGES**



To expedite and control these changes, we are taking a number of steps to improve financial management in the Air Force. We now have a better organization to manage reform efforts. An office has been established on the Assistant Secretary of the Air Force, Financial Management and Comptroller (SAF/FM) staff that focuses on financial reform. Since many reform efforts involve other functional areas, we also created a senior coordinating group called the Financial Improvement Policy Council to keep the appropriate senior level managers informed of our efforts and to seek their cooperation.

Improving financial management starts with efforts to improve our systems BECAUSE:



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Current financial systems:

- are antiquated and designed to manage budgets
- do not accommodate double-entry bookkeeping or a standard transaction-driven general ledger -- impossible to obtain clean audit opinions
- few can automatically transfer data to other systems -- reentering data leads to errors

Defense Finance and Accounting Service (DFAS) has the lead in fixing most of our financial systems, but we are working closely with them to ensure customer needs are represented.

*Key Improvements Underway*

Project	Goals
<p>General Ledger/Funds Control (GL/FC) -- initial phase reengineers the existing general funds accounting system</p>	<ul style="list-style-type: none"> <li>• Provide double-entry, transaction-based general ledgers</li> <li>• Convert to government-standard chart of accounts</li> <li>• Use a standard Budget and Accounting Classification Code</li> <li>• Provide separate general funds general ledgers by appropriation</li> </ul>
<p>Feeder Systems Project seeks to improve financial components of logistics and other systems that provide financial information. As a first step, a Transfer of Management Responsibility (TMR) study is identifying these feeder systems.</p>	<ul style="list-style-type: none"> <li>• Identify feeder systems requiring Federal Managers' Financial Integrity Act (FMFIA) reviews</li> <li>• Delineate management responsibility for certifying system financial and accounting functionality/data</li> <li>• Plan for improvements to the systems</li> </ul>
<p>Civilian Pay/Military Pay</p>	<ul style="list-style-type: none"> <li>• Transition from unique systems to standard DoD migratory systems</li> <li>• Enhance the Defense Joint Military Pay System</li> <li>• Convert to the Defense Civilian Pay System (DCPS)</li> </ul>

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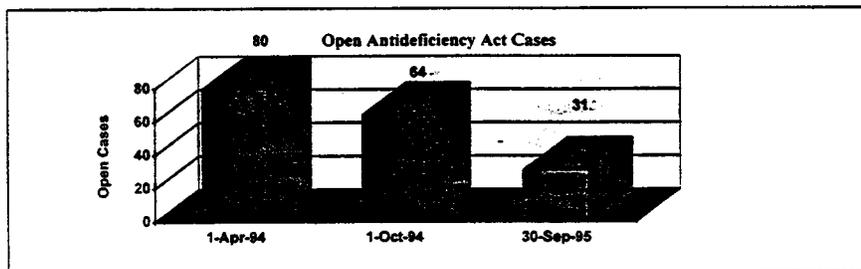
In addition to improving our systems, we need to



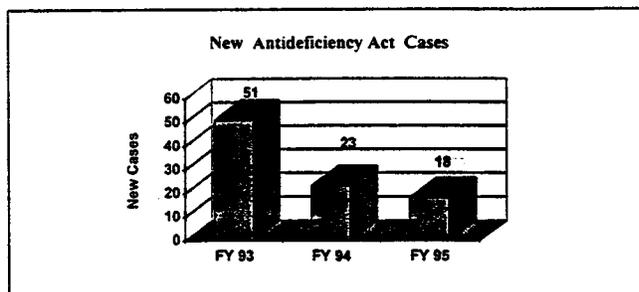
Our efforts focus on antideficiency cases, negative unliquidated obligations, and the CFO Report itself.

### *Antideficiency Act Cases*

Antideficiency Act cases involve the potential of over obligation of appropriated funds. The number of open cases in the Air Force has declined significantly:



Not only is our inventory decreasing, but more importantly the number of new cases has declined:



## Appendix B. AFAA Report, "Opinion on Fiscal Year 1995 Air Force Consolidated Financial Statements"

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### Overview

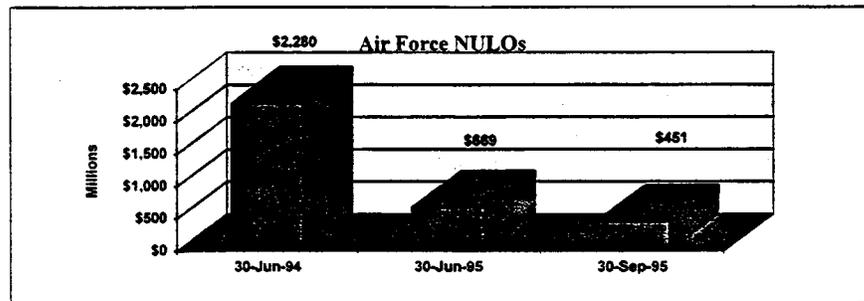
Current improvement efforts to minimize new cases:

- Training courses at several of our financial centers -- especially those heavily involved in procurement actions
- Working with Under Secretary of Defense (Comptroller) (USD(C)) to develop a training course for those assigned to investigate Antideficiency Act violations

#### *Negative Unliquidated Obligations (NULOs)*

A NULO is a financial disbursement that appears to exceed the obligation to which it has been matched -- essentially writing checks on accounts that appear to be in the red.

Following the lead of the Under Secretary of Defense (Comptroller) (USD(C)), the Air Force has made sizable progress reducing NULOs.



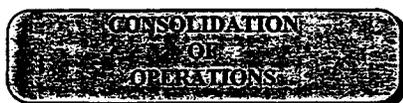
This excellent progress reflects much hard work on the part of DFAS-Denver, as well as extensive cooperation and work on the part of Air Force Materiel Command and Air Force Headquarters personnel.

#### *CFO Report*

Working to make more useful:

- Relevance to MAJCOM Commanders -- study conducted with MAJCOM personnel to determine refinements needed to make the CFO Report a useful, management tool
- Performance Measures -- reviewed current performance measures to ensure we're measuring the right things, the right way. This process will continue into FY96
- Better Presentation -- the CFO Report Overview and Supplemental sections were made more readable through the use of graphs, pictures, and format

**Overview**



Consolidation of base-level accounting operations has been one of the biggest challenges facing DFAS and Air Force financial management this year. DFAS activated six centralized operating locations (OPLOCs) which will support the Air Force. To date, fourteen Air Force base-level accounting operations have been consolidated, with another twenty planned for FY96.

To date, consolidations have gone as smoothly as could be expected given the magnitude of this change. Most of the problems can be attributed to the exodus of base-level employees, connectivity problems at the OPLOCs during start up, and difficulty in the transmission of financial documents. Most affected has been the payment of vendors, with the results reflected in a degradation of our Prompt Payment Act performance. The Air Force and DFAS are working closely to improve this situation.

The turbulence created by consolidation will continue to be problematic for the next few years. The Air Force will continue to work closely with DFAS to ensure consolidation does not seriously degrade the quality of our financial statements. We fully expect consolidation will yield significant cost savings and eventually improve the quality of our financial reporting.

***Summary of Current Management Initiatives***

Within the context of historic cultural change, the Air Force, with strong leadership from USD(C) and important help from DFAS, has made significant progress in financial management reform over the last year and a half. We now have a viable plan for system improvements, taken active efforts to improve the CFO Report, and sought outside advice. We have also affiliated ourselves with the Financial Executives Institute, a group of chief financial officers from private companies. They are providing us advice and helping us overcome criticism that the Air Force is not taking financial management reform seriously.

***Limitations of the Financial Statements***

The financial statements included in this report have been prepared to report on the financial position of the Air Force pursuant to the requirements of the CFO Act of 1990.

The accompanying financial statements account for all general funds for which the Department of the Air Force is responsible. Information relative to classified assets, programs, and operations has been aggregated and reported in such a manner that it is no longer classified.

While the statements have been prepared from the books and records of the Air Force, in accordance with the formats prescribed by OMB, the statements are different from the financial statements, used to monitor and control budgetary resources that are prepared from the same books and records. In addition, prior year balances have been adjusted based on information

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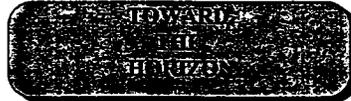
**Financial Statements and Notes**

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**Overview**

received subsequent to their issuance. Footnote 1.A to the principal statements contains additional information on these adjustments.

The statements should be read with the realization that they are for a component of a sovereign entity, that unfunded liabilities reported in the financial statements cannot be liquidated without the enactment of an appropriation, and that the payment of all liabilities other than for contracts can be abrogated by the sovereign entity.



With the military drawdown behind us, we are prepared to face whatever challenges may come our way. Those challenges are achievable because we have a vision that continues to provide America the world's greatest air and space force. That vision is *Global Reach - Global Power*. It served us well over the past five years and promises to serve us even better in the years ahead.

We are poised to accept the challenges of the future. With the benefit of experience, insight, and imagination, the United States Air Force will continue to provide the premier air and space force for the 21<sup>st</sup> century. We are mindful that our basic mission remains bedrock -- to be prepared to fight and win our nation's wars, and to do so with the most efficient use of the nation's treasures -- its young people and scarce resources. To get there, we will continue to ask much of our people and they can continue to expect much from their leadership. We are a team within a team. We understand our responsibilities and live by our commitments. As a team, the Air Force will continue to provide *Global Reach - Global Power* into the 21<sup>st</sup> century.

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**Principal Statements**

**Department of Defense  
Department of the Air Force  
Statement of Financial Position  
as of September 30, 1995  
(Thousands)**

	1995	1994 ADJUSTED
<b>ASSETS</b>		
<b>1. Entity Assets:</b>		
a. Transactions with Federal Entities:		
(1). Fund Balance with Treasury (Note 2)	<u>\$54,780,775</u>	<u>\$58,604,817</u>
(a). Funds Collected	5,292,558	6,995,310
(b). Funds Disbursed	(82,389,737)	(87,606,740)
(c). Funds With Treasury	131,877,954	139,216,247
(2). Investments, Net (Note 4)		
(3). Accounts Receivable, Net (Note 5)	1,362,859	1,313,299
(4). Interest Receivable, Net		
(5). Advances and Prepayments	3,152	3,598
(6). Other Intragovernmental (Note 6)		
b. Transactions With NonFederal Entities:		
(1). Investments (Note 4)		
(2). Accounts Receivable, Net (Note 5)	186,606	86,077
(3). Credit Program Receivables/Related Foreclosed Property, Net (Note 7)		
(4). Interest Receivable, Net		
(5). Advances and Prepayments (Note 9)	8,121,479	10,046,660
(6). Other Intragovernmental (Note 6)		
c. Cash and Other Monetary Assets (Note 3)		
d. Inventory, Net (Note 8)		
e. Work in Process (Note 9)		
f. Operating Materials/Supplies, Net (Note 10)	23,936,463	31,098,295
g. Stockpile Materials, Net (Note 11)		
h. Seized Property (Note 12)		
i. Forfeited Property, Net (Note 13)		
j. Goods held Under Price Support and Stabilization Programs, Net (Note 14)		
k. Property and Equipment, Net (Note 15)	234,478,315	223,762,327
l. Other Entity Assets		
<b>m. Total Entity Assets</b>	<u>\$322,869,649</u>	<u>\$324,915,073</u>
<b>2. NonEntity Assets:</b>		
a. Transactions With Federal Entities:		
(1). Fund Balance With Treasury (Note 2)	54,492	54,241
(2). Accounts Receivable, Net (Note 5)		
(3). Interest Receivable, Net		
(4). Other (Note 6)		

The accompanying notes are an integral part of these statements.

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 Statement of Financial Position  
 as of September 30, 1995

Assets Continued

**2. Non-Entity Assets Continued:**

**b. Transactions With NonFederal Entities:**

(1). Accounts Receivable, Net (Note 5)	773,902	742,882
(2). Interest Receivable, Net		
(3). Other (Note 6)	621	4,327
c. Cash and Other Monetary Assets (Note 3)	113,791	139,862
d. Other NonEntity Assets		
e. Total NonEntity Assets	<u>\$942,806</u>	<u>\$941,312</u>

**3. Total Assets**

<u>\$323,812,455</u>	<u>\$325,856,385</u>
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**LIABILITIES**

**4. Liabilities Covered by Budgetary Resources:**

**a. Transactions With Federal Entities:**

(1). Accounts Payable	1,147,223	1,502,625
(2). Interest Payable		
(3). Debt (Note 16)		
(4). Other Intragovernmental Liabilities (Note 17)	839,553	1,123,504

**b. Transactions With NonFederal Entities:**

(1). Accounts Payable	3,989,962	2,775,192
(2). Accrued Payroll and Benefits		
(a). Salaries and Wages	474,889	487,542
(b). Annual Accrued Leave		
(c). Severance Pay and Separation Allowance	16,643	18,850
(3). Interest Payable		
(4). Liabilities for Loan Guarantees (Note 7)		
(5). Lease Liabilities (Note 18)		
(6). Pensions and Other Actuarial Liabilities (Note 19)		
(7). Other Governmental Liabilities (Note 17)	2,357	4,086
c. Total Liabilities Covered by Budgetary Resources	<u>\$6,470,627</u>	<u>\$5,911,799</u>

The accompanying notes are an integral part of these statements. 78<sup>2</sup>

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Department of the Air Force  
Statement of Financial Position  
as of September 30, 1995  
Liabilities Continued**

**5. Liabilities Not Covered By Budgetary Resources:**

- a. Transactions With Federal Entities
  - (1). Accounts Payable
  - (2). Debt (Note 16)
  - (3). Other Intragovernmental Liabilities (Note 17)
- b. Transactions With NonFederal Entities
  - (1). Accounts Payable
  - (2). Debt (Note 16)
  - (3). Lease Liabilities (Note 18)
  - (4). Pensions and Other Actuarial Liabilities (Note 19)
  - (5). Other Governmental Liabilities (Note 17)
- c. **Total Liabilities Not Covered by Budgetary Resources**

1,812,972	1,606,067
-----------	-----------

<u>\$1,812,972</u>	<u>\$1,606,067</u>
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**6. Total Liabilities**

<u>\$8,283,599</u>	<u>\$7,517,866</u>
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**NET POSITION (Note 20)**

**7. Balances:**

- a. Unexpended Appropriations
- b. Invested Capital
- c. Cumulative Results of Operations
- d. Other
- e. Future Funding Requirements
- f. **Total Net Position**

50,867,644	55,176,574
------------	------------

266,433,656	264,769,035
-------------	-------------

1,714	1,279
-------	-------

(1,774,158)	(1,608,369)
-------------	-------------

<u>\$315,528,856</u>	<u>\$318,338,519</u>
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**8. Total Liabilities and Net Position**

<u>\$323,812,455</u>	<u>\$325,856,385</u>
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The accompanying notes are an integral part of these statements. 79<sup>3</sup>

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Department of Defense  
 Department of the Air Force  
 Statement of Operations (and Changes in Net Position)  
 For the Period Ended September 30, 1995  
 (Thousands)

	1995	1994 ADJUSTED
<b>REVENUES AND FINANCING SOURCES</b>		
1. Appropriated Capital Used	\$55,309,619	\$56,023,301
2. Revenues from Sales of Goods and Services		
a. To the Public	191,258	225,533
b. Intragovernmental	3,371,274	5,013,414
3. Interest and Penalties, Non-Federal		
4. Interest, Federal		
5. Taxes (Note 21)		
6. Other Revenues and Financing Sources (Note 22)	37,226	1,972
7. Less: Taxes and Receipts Transferred to the Treasury or Other Agencies		
8. Total Revenues and Financing Sources	<u>\$58,909,377</u>	<u>\$61,264,220</u>
<b>EXPENSES</b>		
9. Program or Operation Expenses (Note 23)	54,629,305	55,125,772
10. Cost of Goods Sold (Note 24)		
a. To the Public	191,258	225,533
b. Intragovernmental	3,371,274	5,013,414
11. Depreciation and Amortization		
12. Bad Debts and Write-offs	5,937	131,743
13. Interest		
a. Federal Financing Bank/Treasury Borrowing		
b. Federal Securities		
c. Other	3,460	2,019
14. Other Expenses (Note 25)	873,497	656,766
15. Total Expenses	<u>\$59,074,731</u>	<u>\$61,155,247</u>
16. Excess (Shortage) of Revenues and Financing Sources Over Total Expenses Before Extraordinary Items (Note 26)	(165,354)	108,973
17. Plus (Minus) Extraordinary Items (Note 26)		
18. Excess (Shortage) of Revenues and Financing Sources Over Total Expenses	<u>(\$165,354)</u>	<u>\$108,973</u>

The accompanying notes are an integral part of these statements.

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 For the Period Ended September 30, 1995  
 (Thousands)

	1995	1994 ADJUSTED
<b>EXPENSES Continued</b>		
19. Net Position, Beginning Balance, as Previously Stated	\$318,338,519	\$320,465,966
20. Adjustments (Note 27)		
21. Net Position, Beginning Balance, as Restated	<u>318,338,519</u>	<u>320,465,966</u>
22. Excess (Shortage) of Revenues and Financing Sources Over Total Expenses	(165,354)	108,973
23. Plus (Minus) Non Operating Changes (Note 28)	(2,644,309)	(2,236,420)
24. Net Position, Ending Balance	<u>\$315,528,856</u>	<u>\$318,338,519</u>

The accompanying notes are an integral part of these statements. 81<sup>5</sup>

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Footnotes

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**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE AIR FORCE  
GENERAL FUNDS  
FY 95**

**Note 1. Summary of Significant Accounting Policies**

**A. Basis of Presentation:**

These financial statements were prepared to report the financial position and results of operations of the Department of the Air Force, as required by the Chief Financial Officers (CFO) Act. They were prepared from the books and records of the Air Force in accordance with DoD Guidance on Form and Content of Financial Statements for FY 1994/1995 Financial Activity and DoD's accounting policies which are summarized in this note. These statements, therefore, are different from the financial reports, also prepared by the Air Force pursuant to Office of Management and Budget (OMB) directives, that are used to monitor and control DoD's use of budgetary resources.

Fiscal year (FY) 1992 was the first year audited financial statements were prepared for the Department of the Air Force as required by the CFO Act. The following year (FY 93), comparative financial statements were prepared for the Air Force. The CFO Act requires the Air Force prepare and submit for audit, financial statements for each revolving fund and trust fund of the Department, and each fund and account that performed substantial commercial functions during the preceding fiscal year. The Comptroller of the Air Force is required to issue two consolidated financial statements for FY 95 which include the Statement of Financial Position and Statement of Operations and Changes in Net Position. In previous years, the Statement of Cash Flows and Statement of Budgetary Resources and Actual Expenses were also required financial statements. However, the DoD requested and received OMB approval to eliminate these two statements for FY 95 CFO reporting.

The Statement of Financial Position and Statement of Operations and Changes in Financial Position were restated to permit the preparation of comparative statements in the format required by the Department of Defense and the Office of Management and Budget. Prior period discrepancies discovered during the audit cycle also dictated a restatement (see Note 27). The following depict the restatements:

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Statement of Financial Position  
(Thousands)

<u>Line #</u>	<u>Prior Year Balance</u>	<u>Adjustments to Prior Year Balance</u>	<u>Adjusted Balance for FY 94</u>
1b(5)	138,247	9,908,413	10,046,660
1e	9,908,413	<9,908,413>	0
1f	32,332,526	<1,234,231>	31,098,295
1k	227,596,423	<3,834,096>	223,762,327
1m	329,983,400	<5,068,327>	324,915,073
2b(3)	0	4,327	4,327
2d	4,327	<4,327>	0
3	330,924,712	<5,068,327>	325,856,385
4a(1)	1,503,436	<811>	1,502,625
4a(4)	979,315	144,189	1,123,504
4a(5)	144,189	<144,189>	0
4b(1)	2,774,381	811	2,775,192
5b(5)	1,461,783	144,284	1,606,067
5b(6)	144,284	<144,284>	0
7a	55,173,986	2,588	55,176,574
7b	269,837,362	<5,068,327>	264,769,035
7d	0	1,279	1,279
7e	<1,604,502>	<3,867>	<1,608,369>
7f	323,406,846	<5,068,327>	318,338,519
8	330,924,712	<5,068,327>	325,856,385

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Statement of Operations and Changes  
In Net Position  
(Thousands)

<u>Line #</u>	<u>Prior Year Balance</u>	<u>Adjustment to Prior Year Balance</u>	<u>Adjusted Balance for FY 94</u>
1			
Appro. Avail.	74,505,463	<74,505,463>	0
Appropriated			
Capital Used	0	56,023,301	56,023,301
2a	219,755	5,778	225,533
2b	5,019,191	<5,777>	5,013,414
8	0	61,264,220	61,264,220
8a	79,746,381	<79,746,381>	0
8b	25,322,130	<25,322,130>	0
8c	54,424,251	<54,424,251>	0
10	4,852,869	<4,852,869>	0
10a	0	225,533	225,533
10b	0	5,013,414	5,013,414
14	0	656,766	656,766
14a	2,877	<2,877>	0
14b	21,879	<21,879>	0
15	60,137,169	1,018,078	61,155,247
16	<5,712,918>	5,821,891	108,973
18	<5,712,918>	5,821,891	108,973
19	320,466,406	<440>	320,465,966
21	320,466,406	<440>	320,465,966
22	0	108,973	108,973
22A	<5,712,918>	5,712,918	0
22B	<632,000>	632,000	0
22B3	10,231,358	<10,231,358>	0
22B4	9,599,358	<9,599,358>	0
23	<946,000>	1,290,420	<2,236,420>
24	323,406,846	<5,068,327>	318,338,519

**B. Reporting Entity:**

The United States Air Force was created on September 18, 1947, by the National Security Act of 1947. The National Security Act Amendments of 1949 established the DoD and made the Air Force a department within DoD. The overall mission of the Air Force is to defend the United States through control and exploitation of air and space.

The accompanying consolidated financial statements of the Air Force include the accounts of the general, special, deposit, and trust funds under the Air Force's control. The consolidated financial statements account for all funds for which the Air Force has responsibility except information relative to classified assets, programs, and operations has been excluded from the statements or otherwise aggregated and reported in such a manner that it is no longer classified. The audited

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**Financial Statements and Notes**

financial statements are presented on the accrual basis of accounting as required by DoD accounting policies. Financial statements and reports are prepared by the Defense Finance and Accounting Service - Denver Center, Directorate of Departmental Accounting (DFAS-DE/AD) based upon data provided by over 100 financial reporting systems, some of which are the General Accounting and Finance System (GAFS), Standard Base Supply System (SBSS), Medical Materiel Accounting System (MMAS), and major command unique systems which feed into general funds. In addition, feeder data are supplied by the Air Force Academy Accounting and Finance Office for the Cadet Fund, and by DFAS-DE/AD for the Gift Fund which is administered by DFAS-DE/AD. Other entities also send data for consolidation such as Army Corps of Engineers and Department of the Navy.

DFAS-DE/AD uses the Departmental On-Line Accounting and Reporting System (DOLARS) to consolidate and prepare Air Force level financial reports. Monthly, the Automated Digital Network (AUTODIN) or file transfer protocol (FTP) is used to transmit data from either the base, operating location, or major command, depending on the report. The data are programmatically validated by DOLARS' programs and then automatically updated in the departmental database. Data are also updated in the database through manual entries. Appropriation Status of Funds reports are prepared from this single, integrated database, thus enabling consistent, accurate, and timely reporting. Moreover, the data in the database are readily available for update and inquiry by departmental staff, Air Staff, and major command staffs. All data in the database have readily available audit trails.

The financial statements presented herein are derived from supply, maintenance and accounting records, utilizing the Air Force service-unique general ledger structure. A plan to accomplish initial tasks (phase one) required for a conversion to a transaction driven general ledger (using the DoD standard general ledger structure) was approved by DFAS-HQ. Additionally, the General Ledger Funds Control (GLFC) system is in development to blend the Air Force information management and DFAS financial systems into a comprehensive management information system.

The Air Force incorporates into the accounting systems internal controls, reconciliations, management by exception reports, and other analytical check and balance processes to enhance required general ledger controls.

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The following is a list of Air Force account numbers and titles:

<u>Air Force Account Number</u>	<u>Title</u>
57 * 8418	Air Force Cadet Fund
57 * 8928	Air Force General Gift Fund
57 * 3500	Military Personnel, AF
57 * 3700	Reserve Personnel, AF
57 * 3850	Air National Guard Personnel
57 * 3400	Operations and Maintenance (O&M), AF
57 * 3740	O&M Reserve
57 * 3840	O&M Air National Guard
57 * 3010	Aircraft Procurement
57 * 3020	Missile Procurement
57 * 3080	Other Procurement
57 * 3600	RDT&E, Air Force
57 * 3300	Military Construction, AF
57 * 3830	Military Construction, ANG
57 * 3730	Military Construction, Reserve
57 * 0704	Military Family Housing
57 * 3011	Procurement of Ammunition
57 * 5095	Wildlife Conservation, Military Reservations, Air Force (Special Fund Accounts)
57 * 3XXX	Budget Clearing Accounts
57 * 6XXX	Deposit Fund Accounts

**C. Budgets and Budgetary Accounting:**

The Air Force's activities are financed by general, trust, special, deposit, and revolving funds. These notes describe the attributes of these funds.

General fund accounts are used to record the amounts appropriated by Congress and the financial transactions utilizing the funds. The Air Force manages 16 general fund accounts: 7 are funded by annual year appropriations and 9 are funded by multi-year appropriations. These appropriations made available in FY 95 includes:

Appropriations Realized	\$74,712,617,000
Other	<u>&lt;357,781,000&gt;</u>
Appropriations Net of Adjustment	74,354,836,000
Return of equity to Treasury for closed accounts	<u>993,772,277</u>
Net Appropriations Available for FY 95	\$73,361,063,723

Trust fund accounts are used to record the receipt and expenditure of funds held in trust by the government for use in carrying out specific purposes or programs in accordance with the terms of a trust agreement or statute. Trust accounts include funds collected through gifts and bequests (as

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**Financial Statements and Notes**

well as interest earned on the investments of some of these gifts) and assets held for particular purposes. The Air Force maintains two trust fund accounts, totaling \$3,760,201 in assets.

Special fund accounts are credited with collections from specific sources that can only be used in accordance with specific provisions of law. The Air Force manages one special fund account, the Wildlife Conservation Program, totaling \$630,196 in assets. This special fund account had appropriations available of \$597,133.

Deposit funds are generally used to 1) hold funds whose distribution awaits legal determination or for which the Air Force acts as agent or custodian, and 2) account for unidentified remittances. The Air Force expressly requires all check collections to pass under the immediate control of one of these deposit funds upon receipt, regardless of source, if the ultimate recipient is unknown. The Air Force deposit fund accounts total \$53,760,698 in assets.

#### **D. Basis of Accounting:**

Transactions are recorded on an accrual basis of accounting, with the exception of the Cadet and Gift Trust Fund accounts (described in detail in a subsequent note) which are on a cash basis. Under the accrual basis, revenues are recognized when earned and expenses are recognized when liabilities are incurred, without regard to receipt or payment of cash. Budgetary accounting facilitates compliance with legal constraints and controls over the use of federal funds. All interfund balances and transactions were eliminated.

The financial statements are presented in accordance with the accounting principles and reporting standards contained in the DoD Financial Management Regulation (DoD 7000.14-R Volume I). There are, however, five areas in which the accounting systems do not currently comply with existing DoD accounting standards. These areas include:

(1) Chart of Accounts. Prior to capitalization by DFAS, the Air Force had not implemented the standard DoD General Funds General Ledger (GFGL) chart of accounts. DoD directives require that a general ledger system be established using the standard DoD chart of accounts to provide primary internal management information. This deficiency has been reported in the Air Force Federal Managers' Financial Integrity Act (FMFIA), Section 4, Conformance Review and Evaluation of Accounting Systems.

(2) General Ledger. Prior to capitalization by DFAS, the Air Force had not implemented a true transaction driven general ledger system to provide a consolidated source of financial management information for either management or financial statement purposes. To account for its resources, the Air Force utilizes an extensive number of external systems to account, control, and report on the status of its resources. Many of these systems are outside the accounting and finance network (i.e., budget and property systems) and the general ledger accounting process. This deficiency has been reported in the Air Force FMFIA, Section 4, Conformance Review and Evaluation of Accounting Systems. DFAS has initiated a project to integrate and modernize DFAS accounting systems into a comprehensive management system. The overall goal is to bring financial data for both general funds and Defense Business Operations Fund (DBOF) under general ledger control that complies with General Accounting Office (GAO) and OMB mandates, is transaction driven, and uses the DoD Uniform Chart of Accounts. The development of concepts

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began in September 1994 and was completed in October 1995. The GLFC project is scheduled for completion in 1998.

(3) Government Furnished Material (GFM) Costs. DFAS-DE has identified GFM as a deficiency in the FMFLA, Section 4, Conformance Review and Evaluation of Accounting Systems. See Note 15M(10).

(4) Inventory/Equipment. The Air Force uses different valuation methods for the various categories of materials and equipment contained in the Air Force inventory. Materials inventory and equipment items accounted for in logistics systems are valued at standard price. Generally, standard prices are based on prices paid for recently acquired items; plus surcharges for handling, distribution; and other costs which results in their being higher than historical cost. Real property installed equipment is valued at cost and is included as part of the real property facility cost basis. This inconsistency in valuation methods was initially documented in the GAO FY 88 financial audit report. The DoD Comptroller has directed an inventory valuation methodology which allows the Air Force to continue to use standard costs (latest acquisition costs) in logistics systems for equipment valuations and for valuations of inventory for financial statements. The Air Force has implemented this inventory valuation methodology.

(5) Capitalizing Aircraft and Missile GFM and Modifications Cost. The Air Force does not generally capitalize the cost of aircraft and missile contract modifications made after the initial acquisition (see Note 15M(2)).

**E. Revenues and Other Financing Sources:**

The Air Force is financed primarily through appropriations provided by Congress for annual and multi-year purposes. The following Treasury accounts are used to fund, execute, and report on total financial activity.

(1) General Funds. This grouping contains the bulk of congressional appropriations, including: operations: research, development, test and evaluation (RDT&E); and investment and construction accounts. Operations accounts represent those funds used for the pay of operating forces. These funds also finance the functional and administrative support needed to operate and maintain Air Force installations.

The Air Force conducts and contracts for RDT&E of advanced weapons systems which are normally expensed. The RDT&E programs support modernization of weapon systems through military research, exploratory development, and the development and testing of prototypes and full-scale preproduction of hardware.

Investment/construction accounts are used for specific purposes approved by and reportable to Congress. These accounts are used for the acquisition or construction of technology, property, and infrastructures.

Revenue and expenses were reduced by \$2,523,187,395, and receivables and payables were offset \$741,290,642, as a result of eliminating intra-Air Force transactions (see Note 29).

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(2) Trust Funds. The Air Force trust funds are endowment or revolving funds. These accounts are used to record the receipt and outlay of funds held in trust by the government for use in carrying out specific purposes or programs. The Air Force operates two trust funds. They are:

(a) The Air Force Gift Fund is an endowment fund where donors make conditional monetary gifts to the Air Force. Donations to the Air Force are recognized as a financial source upon acceptance of the donated asset, and a revenue is recorded for the value of the increase to the asset account. Obligations and expenditures are made against the Gift Fund for the purposes specified in the gift offer. The use or obligation of Gift Fund receipts is recorded on a cash basis. When specified in the gift offer, these funds are allowed to be invested in marketable securities. Donated property is disclosed in the financial statements.

(b) The Air Force Cadet Fund operates as a local deposit fund account. It is administered by the Superintendent of the Air Force Academy on behalf of the Academy cadets. Each month, monies are deposited into the account from checks and information provided by the Defense Joint Military Pay System (DJMS). The cadet pay office draws checks on this account to pay the various vendors and contractors at the Academy. The advance education funds which previously were processed through the Cadet Fund are now paid directly from the Military Personnel Appropriation (3500) and a repayment of indebtedness is established on the cadet Master Military Pay Account (MMPA) in DJMS.

Trust fund revenue of \$8,544,058 includes donations and gifts to the Gift Fund, and funds received from cadets to reimburse the Cadet Fund for items paid by the Cadet Fund on behalf of the cadets.

(3) Special Funds Receipt Accounts. These accounts are credited with receipts from specific sources, are earmarked by law for a particular purpose, and none of the funds are generated from operations. Special fund expenditure accounts are used to record appropriated amounts of special fund receipts to be expended for special programs in accordance with specific provisions of law.

(4) Deposit Fund Accounts. These accounts generally are used to 1) hold assets whose distribution awaits legal determination or for which the Air Force acts as agent or custodian, and 2) account for unidentified remittances. The Air Force expressly requires all check collections to pass under the immediate control of one of these deposit funds upon receipt, regardless of source, if the ultimate recipient is unknown.

For financial reporting purposes under accrual accounting, operating expenses for general fund activities are recognized in the period incurred. Expenditures for capital and other long-term assets are not recognized as expenses until consumed in the Department's operations. Unexpended appropriations are recorded as equity of the Air Force.

Certain expenses, such as annual and military leave earned but not taken, are not funded when accrued. Such expenses are financed in the period in which payment is required. Therefore, for the Department's general funds, an amount due from future financing sources (appropriations to be provided) is recognized as an offset to equity in the consolidated statement of financial position which is comprised of the accrued amount of such expenses at year-end.

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Annual and multi-year congressional appropriations, are supplemented, when authorized, with revenues generated by sales of goods or services through a reimbursable order process. This process allows the seller to increase funds available by the cost of the supplies and/or services ordered by the customer. The reimbursable order process promotes efficiency in providing products and services and it allows an accurate accounting of resources provided and applied. The authority to obligate is recognized (i.e., obligations may be recorded) when orders from a government entity are accepted or advances from a nonfederal entity are received. Obligation authority must be recorded before performance on an order begins. For financial reporting purposes under accrual accounting, revenue is recognized when earned. The cost of goods sold or services provided is recognized when expenses are incurred. Advances received prior to delivery of goods or services are treated as unearned revenue and recorded as a liability of the Air Force.

**F. Accounting for Intra-governmental Activities:**

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

The Air Force's proportionate share of public debt and related expenses of the federal government are not included. Debt issued by the federal government and the related interests costs are not apportioned to federal agencies. The Air Force'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 may ultimately be obtained through the issuance of public debt, interest costs were not capitalized since the Treasury does not allocate interest costs to the benefiting agencies.

The Air Force civilian employees participate in the Civil Service Retirement System (CSRS) and Federal Employees Retirement Systems (FERS) which includes the Thrift Savings Plan (TSP), while military personnel are covered by the Military Retirement System (MRS). Additionally, employees and personnel covered by FERS and MRS are also covered by Social Security. The Air Force funds a portion of pension benefits under these retirement systems but does not disclose the assets or actuarial data on the accumulated plan benefits or unfunded pension liabilities of its employees; the Office of Personnel Management (OPM) reports pension benefits and liabilities for CSRS, FERS and TSP, and DoD reports for MRS.

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In FY 95, the Air Force contributed the following amounts to the retirement plans and Social Security.

CSRS	\$227,380,464
FERS	272,789,726
MEDICARE	268,357,651
TSP	93,019,476
MRS	3,387,639,671
Social Security	<u>1,519,700,899</u>
<b>Total</b>	<b>5,768,887,887</b>

In FY 95, the Department or its components sold assets to foreign governments under the provisions of the Arms Export Control Act of 1976. Under the provisions of the Act, DoD has authority to sell defense articles and services to foreign countries, generally at no profit or loss to the U.S. government. Customers are required to make payments in advance to a trust fund maintained by the Department of the Treasury from which the Military Services are reimbursed for the cost of administering and executing the sales.

**G. Funds with the U.S. Treasury and Cash:**

The Treasury maintains Air Force appropriations in separate accounts in which it records warrants, receipts, and disbursements. During the fiscal year, the Air Force also has the use of various suspense accounts to record collections and disbursements which are rejected in the report edit process pending further research. Treasury requires suspense accounts be closed at year end prior to submission of September 30th reports. The Air Force operation and maintenance account is used to close most suspense accounts. Suspense balances of \$116,961,304 are reopened at the beginning of the next fiscal year. As of September 30, 1995, the Air Force had \$54,835,267,119 in funds with the Treasury.

As agents of the U.S. Treasury Department, disbursing officers (DO) maintain monthly Standard Form 1219, Statement of Accountability, that portray their cash accountability to the Treasury. Technically, the items making up this cash accountability are not Air Force assets. However, in 1992, the GAO held that since the cash accountability is under Air Force control, it should be included on the consolidated Air Force financial statements, with a corresponding liability to the Treasury Department. Beginning with financial statements for FY 92, accordingly, the consolidated total of DO cash accountability was included within totals reported for "unrestricted cash on hand." The amount of total DO cash accountability included in the FY 95 statement as a liability to Treasury is \$114,411,706.

The majority of DO's cash accountability is actual operating or accommodation/exchange "cash" either acquired by Treasury check issue or by collection from customers. However, portions of the total FY 95 cash accountability shown on the disbursing officer's Statement of Accountability, SF 1219, includes advances to contractors under advance payments pool agreements. These advances are reported as non-entity assets, other.

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**H. Foreign Currency:**

The Air Force purchases foreign currency to use in its operations, when appropriate. The Air Force does not purchase foreign currency for investment purposes.

The Air Force conducts a significant portion of its operations overseas. Gains and losses from foreign currency transactions for four general fund appropriations (operation and maintenance, military construction, family housing operation and maintenance, and family housing construction) are recognized and reported in the statement of operations. The gains or losses are computed as the variance between the current exchange rate at the date of payment and a budget rate established at the beginning of the fiscal year. During FY 95, the Air Force recognized a net loss of \$51,278,635 due to foreign currency transactions for the four appropriations. Similar gains and losses from other appropriations are not recognized in the Statement of Operations and Changes in Net Position. They are absorbed by budgetary transactions in which obligations are increased or decreased to reflect foreign currency fluctuations.

**I. Accounts Receivable:**

As presented in the Consolidated Statement of Financial Position, accounts receivable includes accounts, claims, and refunds receivable and advance payments to other entities. Allowances for uncollectible accounts are based upon analysis of collection experience by fund type. During FY 95, the Department wrote off approximately \$10,738,648 in uncollectible receivables. See Note 5 for current year receivables and allowances for doubtful accounts.

**J. Loans Receivable:** Not applicable.

**K. Inventories:**

Inventories, including operating supplies and nonconsumable items, are valued at latest acquisition cost as required by DoD accounting policies. Generally, these prices are based on prices paid for recently acquired items plus appropriate surcharges. No gains or losses are recognized in the Consolidated Statement of Operations as a result of changes in valuation for general fund operating supplies and materials. Such changes are reflected in the asset valuations and related invested capital as reported in the Statement of Financial Position. The Air Force reported no Inventory Held for Sale; however, Operating Supplies and Materials is valued at \$23,364,082,817.

**L. Investments in U.S. Government Securities:**

Investments in U.S. Government securities are reported at cost, net of unamortized premiums or discounts. Premiums or discounts are amortized into interest income over the term of the investment. The reporting entity's intent is to hold investments to maturity, unless they are needed to finance claims or otherwise sustain operations. No provision is made for unrealized gains or losses on these securities because, in the majority of cases, they are held to maturity.

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The Air Force Gift Fund was established to control and account for the disbursement and use of monies donated to the Air Force and the receipt of interest or dividends arising from investment of such donations. The Gift Fund accepts certain gifts offered by the public. Among these are monetary gifts which are accounted for by DFAS-DE. The amount of investments represents federal securities controlled by DFAS-DE. The related earnings are allocated to appropriate Air Force activities to be used in accordance with the directions of the donor. At September 30, 1995, \$850,000 of investments in U.S. securities were included in the Gift Fund balance with Treasury. This amount was not separately stated on the financial statements but included in the fund balance with Treasury.

### **M. Property and Equipment:**

Valuations for equipment, aircraft, missiles, and engines are not based on historical procurement costs. Rather, these assets and weapons systems are valued and reported at actual or average procurement costs. Equipment is valued at acquisition costs using federal stock categories. While no gains or losses are recognized in the Statement of Operations and Changes in Net Position for changes in average costs of equipment, such changes are reflected in asset valuations and related invested capital. Engineering and modification costs incurred subsequent to approval of the basic procurement contracts are valued at the contract price of the engineering change order, value engineering, or modification which extends the life of the asset or capability of the system, and any other cost of materials or services not included in the contract cost.

Land and facilities are valued at cost. Buildings are capitalized when constructed or at the date of acquisition. Improvements to land and buildings costing more than \$50,000 are capitalized. Audits of FY 91 and FY 92 financial statements have shown that documentation to support the recorded acquisition cost of many older properties is no longer available. Obtaining appraisals for older property for which original acquisition records are no longer available is not cost effective, especially considering the number and age of many of DoD's properties. As a reasonable solution to this dilemma, when original records to support the acquisition cost of property are no longer available, recorded valuations of property, or other available information if the value has not been formally recorded, could be permitted for financial statement purposes when such valuation represents the best available information. The Department has requested that the Federal Accounting Standards Advisory Board endorse the above policy until such time as other applicable accounting standards are issued by the Board.

Routine maintenance and repair costs are expensed when incurred. No depreciation has been recorded for general fund equipment and buildings (see Note 15).

**Capitalization of Assets:** The Air Force followed the criteria for capitalization of assets contained in DoD 7220.9-M. This guidance required capitalization of all assets with a useful life of 2 or more years and an acquisition cost of \$5,000 or more. In September 1992, the Air Force received direction from the Acting Comptroller of the Department of Defense to change this requirement (retroactively to October 1, 1991) to capitalize assets with a useful life of 2 years or more and an acquisition cost equal to or exceeding the expense/investment funding threshold used by Congress for appropriating DoD operating (expense) and procurement (investment) appropriations. With the enactment of the Department of Defense Appropriations Act of 1995, the current acquisition cost

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has been increased to \$50,000 or more. During FY 95 the Air Force changed the property, plant, and equipment systems, and regulatory documents to implement the \$50,000 threshold.

**Valuation of Assets:** All fixed assets, including land held in public domain, are valued at acquisition cost. Acquisition cost includes such costs as: purchase price, broker's commissions, fees for examining and recording the title, surveying, razing and removal costs (less salvage proceeds) of structures on the land, transportation, handling and storage, installation, interest, preparation, labor, engineering, appropriate share of the cost of equipment and facilities used in construction, inspections, supervision, legal recording fees, and other related costs of obtaining the property. When the acquisition cost can not be determined, fair market value at the time of acquisition is used.

The various criteria used to establish the fair market value are:

- a. Cash realized in transactions involving the same or similar assets,
- b. Quoted market prices,
- c. Fair market value of other assets or services received in exchange of property, or
- d. Independent appraisals.

Routine maintenance and repair costs are expensed when incurred.

**Base Closures:** Twenty-three bases have been officially closed or realigned including Pease AFB, NH in FY 91, Bergstrom AFB, TX; Carswell AFB, TX; Chanute AFB, IL; Eaker AFB, AR; England AFB, LA; George AFB, CA; Mather AFB, CA; Myrtle Beach, SC; Williams AFB, AZ; and Wurtsmith AFB, MI all in FY 93, Grissom AFB, IN; Homestead AFB, FL; Loring AFB, MA; Lowry AFB, CO; MacDill AFB, FL; Norton AFB, CA; Richards-Gebaur AFB, MO; and Rickenbacker AFB, OH all in FY 94, and Castle AFB, CA; Griffiss AFB, NY; KI Sawyer AFB, MI; and Plattsburgh AFB, NY in FY 95. Between FY 96 and FY 01 adjustments can be expected as a result of disposal transactions at these 23 closed or realigned installations or at any of the other 16 closure or realignment installations pending.

The Comprehensive Environmental Response, Compensation and Liability Act (CERCLA), section 120h, implementation has hampered the federal government's ability to deed property out of the federal inventory. Because of this limitation, 25,771 acres of property are under long-term lease and 9,023 acres of property are under interim lease which has allowed some economic recovery to begin. Four properties (2170 acres) have been transferred to other federal agencies; 1070 acres should appear as a reduction to the Air Force Real Property Inventory in FY 96. 1100 acres was removed during FY 94. Three parcels (17 acres) were assigned for disposal to other federal disposal agents which should reflect as an inventory decrease in FY 96. Only six properties have been sold and deeded to the new owners since the inception of the base closure program in 1988. These six properties yielded \$1,060,250 which will be deposited to the special Office of the Secretary of Defense Base Closure Account (BCA) in FY 96. There are another 25 sales pending which are expected to yield an additional \$25,130,000 as soon as deeds can legally be issued to the properties. Until deeds can be issued, the properties, with minor exception, have been leased to the future owners at no cost. Finally, two large Economic Development Conveyances were consummated, a 530 acre transaction at Norton AFB, CA (\$52M) and a 740 acre transaction at Lowry AFB, CO (\$32.5M). These two transactions granting liberal repayment and charging no interest should yield

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the full \$84,500,000 between now and the year 2010. With no fixed repayment schedule, the yield to the BCA will be based primarily on the success of the redevelopment efforts of the Local Redevelopment Authority (LRA).

No income from the sale of lease of real or related personal property was deposited into or redistributed from the special Office of the Secretary of Defense Base Closure Account (BCA), Parts I or II during FY 95. The accounts (Part I and II) were created by Public Law 100-526 (1988 Act) and Public Law 101-510 (1990 Act), respectively, to handle receipts and disbursements in connection with base closure, realignment and disposal.

**Medical Funding:** Beginning in FY 92, funding for all components in DoD was accomplished through the Defense Health Program appropriation, with an amount allocated to the Air Force. Any fixed assets purchased with these funds, if they met the capitalization criteria, were commingled with assets purchased with other Air Force appropriations, and are included in those amounts. Materiel in stores, real property, and equipment in the medical care program remain on the general funds financial statements.

### **N. Prepaid and Deferred Charges:**

Payments in advance of the receipt of goods and services are recorded as prepaid charges at the time of prepayment and recognized as expenditures/expenses when the related goods and services are received.

### **O. Leases:**

Air Force reported no commitment for operating leases and rental agreements (see Note 18). All leases are recorded as operating leases, contracted for annually, and paid by the annual operations and maintenance appropriation.

The Air Force owns substantially all of the facilities and real property used in its domestic operations. Capital assets overseas are normally funded with appropriated funds, but title is retained by the host country.

### **P. Budgetary Contingencies:**

By their nature, DoD accounting polices are a blend of budgetary and proprietary rules. Applicable directives require the Air Force to report and disclose contingencies in budgetary and proprietary accounts. Overall, unfunded liabilities cannot be liquidated without the enactment of an appropriation. Budgetary contingencies are indicated below. See Footnote 31 for proprietary contingencies (contingent liabilities) which include commitments.

**Budgetary Contingencies:** Air Force budgetary contingencies include undelivered orders outstanding and unfilled orders outstanding. See Footnote 1V for information on undelivered orders outstanding.

The DoD Accounting Manual, in conformance with requirements imposed by OMB, requires that all procurement accounts, military construction and RDT&E accounts report budgetary contingencies that meet the definition of budgetary commitments. Air Force also reports budgetary commitments for operation and maintenance accounts. Budgetary commitments are administrative reservations of appropriated funds. The purpose of budgetary commitments is to improve obligation accounting and reduce the possibility of the overobligation of appropriated funds.

Unfilled orders outstanding represent reimbursable orders received for which supplies or services have not been delivered to the ordering agency. Except for sale from inventory items, unfilled orders at fiscal yearend have been obligated. Unfilled orders outstanding at the end of FY 95 totalled \$1,289,945,916 in unexpired, expired, and closed accounts.

The National Defense Authorization Act for FY 92 enacted Sections 1174a and 1175, Title 10, United States Code which authorized the Special Separation Benefit (SSB) and Voluntary Separation Incentive (VSI) programs. These programs offer eligible military members special benefits associated with separation from active duty and voluntary appointment, enlistment or transfer to a Reserve component. The SSB transactions are paid from the current military personnel appropriation and expenditures for FY 95 were \$217,230,415. All VSI payments made after December 31, 1992, are paid from a "Voluntary Separation Incentive Fund" established by the Department of the Treasury. The fund is used to accumulate amounts needed to finance, on an actuarially sound basis, liabilities accrued under the VSI Program. The DoD Board of Actuaries determines the present value of the future benefits payable to persons who separate under VSI. The Board also determines an amortization schedule for liquidating these new unfunded liabilities. In January 1993, \$391.4 million was transferred to the VSI trust fund, which was expected to cover all VSI expenditures through January 1, 1995. The VSI expenditures for FY 95 were \$28,428,726.

Voluntary separation incentive payments (VSIP) to civilians during FY 95 were approximately \$71,307,000.

**Q. Accrued Leave:**

Civilian annual leave and military leave are accrued as earned and the accrued amounts are reduced as leave is taken. The balances for annual and military leave at the end of the fiscal year reflect current pay rates for the leave that is earned but not taken. Sick leave and other types of nonvested leave are expensed as taken. Each year, the balance in the accrued annual leave account is adjusted to reflect current pay rates.

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### **R. Equity:**

Equity consists of unexpended appropriations, invested capital, donations, and cumulative results of operations.

Unexpended appropriations represent amounts of authority which are unobligated and have not been rescinded or withdrawn, and amounts obligated but for which neither legal liabilities for payments have been incurred nor actual payments made. See note 20.G. for fund balance detail.

Invested capital, as presented in the consolidated statement of financial position, represents the value of the Department's capital assets which consists of operating materials and supplies and property and equipment.

Donations represent the value of donated assets on hand.

Cumulative results of operations for working capital funds represent the excess of revenues over expenses since fund inception, less refunds to customers and returns to the U.S. Treasury.

### **S. Aircraft and Satellite Crashes:**

The cost of aircraft which were either destroyed or damaged beyond repair due to aviation mishaps in FY 95 involved 31 aircraft valued at \$618 million. In FY 94, the cost of such aircraft was \$607 million. The related FY 95 Air Force cost for flight injuries was \$30 million. There were four missiles and one space satellite destroyed in FY 95 valued at \$45 million. The associated loss impacted both asset and equity accounts. No loss was separately recognized for aircraft damaged by accidents but were repairable. Costs associated with repair of such aircraft are recorded as operating expenses and generally funded from operation and maintenance appropriations.

### **T. Treaties for Use of Foreign Bases:**

The Air Force has the use of land, buildings, and other facilities which are located overseas and were obtained through various international treaties and agreements negotiated by the Department of State. Generally, treaty terms allow the Air Force continued use of these properties until the treaties expire. Capital investments in buildings, runways, aircraft shelters, and other facilities located on the overseas bases are capitalized. As of September 30, 1995, the Air Force had not finalized the cost values of buildings and facilities located in foreign countries. These fixed assets are subject to loss in the event the treaties are not renewed or other agreements are not reached which allow for the continued use by the Air Force. In the event these treaties or agreements are terminated, losses will be recorded for the value of nonretrievable capital assets.

In FY 91 two overseas bases, Torrejon, Spain, and Hellinikon, Greece, were closed. Funding for closing and relocation costs were provided through appropriations and North Atlantic Treaty Organization (NATO) funding. Operating expenses for overseas bases are included in the Consolidated Statement of Operations and Changes in Net Position.

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**U. Comparative Data.** Not applicable.

**V. Restatement of Prior Year Principal Statements:**

The Statement of Financial Position and Statement of Operations and Changes in Financial Position for FY 94 have been restated to permit the preparation of comparative statements due to significant changes in reporting requirements required by OMB.

**W. Undelivered Orders.**

Undelivered orders outstanding represent amounts ordered but not received and thus do not represent a liability for payment. Undelivered orders outstanding at the end of FY 95 totalled \$41,986,487,234 in unexpired, expired and closed accounts.

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**Note 2. Fund Balances with Treasury**

**A. Business Operations Fund (DoD Comptroller) and All Other Funds and Accounts**

	<u>Entity Assets</u>		
	Trust Funds	Revolving Funds	Appropriated Funds
Unobligated Balance Available:			
Available	\$2,346,632	-	\$10,905,907,401
Restricted	-	-	-
Reserve for Anticipated Resources	-	-	-
Obligated (but not expensed)	-	-	43,872,521,047
Unfunded Contract Authority	-	-	-
Unused Borrowing Authority	-	-	-
 Treasury Balance	<u>\$2,346,632</u>	<u>0</u>	<u>\$54,778,428,448</u>

	<u>Entity Assets</u>	
	Other Fund Types	Total
Unobligated Balance Available:		
Available	-	\$10,908,254,033
Restricted	-	-
Reserve for Anticipated Resources	-	-
Obligated (but not expensed)	-	43,872,521,047
Unfunded Contract Authority	-	-
Unused Borrowing Authority	-	-
 Treasury Balance	<u>0</u>	<u>\$54,780,775,080</u>

**B. Business Operations Fund Activities Below DoD Comptroller Level**

Not applicable

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**C. Business Operations Fund Activities and all Other Funds and Accounts**

<u>Non Entity Assets</u>					
	Trust Funds	Revolving Funds	Appropriated Funds	Other Fund Types	Total
Beginning Balance	-	-	\$642,654	\$53,598,083	\$54,240,737
Funds Collected (net)	-	-	88,686	162,614	251,300
Funds <Disbursed>	-	-	-	-	-
Ending Balance	<u>0</u>	<u>0</u>	<u>\$731,340</u>	<u>\$53,760,697</u>	<u>\$54,492,037</u>

D. Other Information. Trust Fund Balance with Treasury, \$2,346,632 includes \$1,752,552 of the Air Force Gift Fund held by the Treasury. Reports prior to FY 92 do not include the amount of cash held by Air Force disbursing officers. Past policy was that all cash belonged to the U.S. Treasury and was not considered as an asset of a DoD Component for external statement purposes. For FYs 92 and later, cash held by DoD disbursing officers are reported on DoD financial statements.

**Note 3. Cash, Foreign Currency and Other Monetary Assets**

	<u>Entity Assets</u>	<u>Nonentity Assets</u>
A. Cash	\$ -	\$99,172,015
B. Foreign Currency	-	14,618,793
C. Other Monetary Assets		
(1) Gold	-	-
(2) Special Drawing Rights	-	-
(3) US Reserves in the International Monetary Fund	-	-
(4) Other	-	-
(5) Total Other Monetary Assets	-	-
D. Total Cash, Foreign Currency and Other Monetary Assets	-	<u>\$113,790,808</u>
E. Other Information:		=====

**Note 4. Investments.** The Air Force did not have investments to report for FY 95.

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**Note 5. Accounts Receivable.**

	(1) Gross Amount Due	(2) Allow for Estimated Uncollect	(3) Allow Method Used (see below *)	(4) Net Amount Due
<b>A. Entity Receivables:</b>				
Intragovernmental- Receivables	\$1,362,858,593			\$1,362,858,593
Advances	<u>3,151,745</u>			<u>3,151,745</u>
Total Intragov	<u>1,366,010,338</u>			<u>1,366,010,338</u>
Public- Receivables	150,097,940	6,403,227		143,694,713
Refund Receivables	<u>45,215,530</u>	<u>2,304,082</u>		<u>42,911,448</u>
Subtotal	<u>195,313,470</u>	<u>8,707,309</u>		<u>186,606,161</u>
Advances	<u>8,121,479,314</u>	<u>0</u>		<u>8,121,479,314</u>
Total Public	<u>8,316,792,784</u>	<u>8,707,309</u>		<u>8,308,085,475</u>
Total Entity Rec	<u>\$9,682,803,122</u>	<u>\$8,707,309</u>		<u>\$9,674,095,813</u>
<b>B. Non-Entity Receivables:</b>				
Public Receivables	1,366,916,766	593,013,832		773,902,934
Cash Adv to Contr	<u>620,898</u>	<u>0</u>		<u>620,898</u>
Total Nonentity Rec	<u>\$1,367,537,664</u>	<u>\$593,013,832</u>		<u>\$774,523,832</u>

\* The departmental allowance for entity public receivables is computed each year. It is based on the average percent of write-offs to outstanding public accounts receivables for the last 5 years.

C. Other Information: As presented in the Consolidated Statement of Financial Position, accounts receivable include reimbursements receivable, and refund receivables such as out-of-service debts (amounts owed by former service members), contractor debt and unused travel tickets. In prior years, all advances were identified in the DOLARS system as public; even though there was a requirement to identify advances to federal sources. Effective FY 92, the amount for Intragovernmental Advances was taken from the GFGL. Beginning with FY 93 financial statements, Advances and Prepayments, Non-Federal includes advances to contractors under advance payments pool agreements. These payments are recorded on the disbursing officers' Statement of Accountability, SF 1219. See Note 29 for amounts associated with intrafund eliminations.

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**Miscellaneous Receivables and Interest and Penalties:** Accounts receivable balances extracted from DOLARS do not include the amount of miscellaneous receivables which result from interest, penalties, and administrative charges associated with the collection of delinquent accounts, merged appropriation accounts, and other miscellaneous receivables. Effective September 30, 1993, the remaining merged appropriation accounts were closed from the Treasury records. Receipts for merged appropriation accounts and for other miscellaneous receipts cannot be used to augment appropriations and any collections must be credited to a Treasury receipt account. Beginning in FY 93, miscellaneous receipts receivables are stated separately as nonfinancial resources transferable to Treasury and reported as liabilities to the Department of the Treasury.

The FY 94 net miscellaneous receivable total (as restated on the comparative statements) was \$137,217,184 and the FY 95 net total is \$167,967,116 (total receivables of \$760,850,697 less estimated uncollectibles of \$592,883,581). Both fiscal years include miscellaneous receipts, interest, penalties, and administrative charges. The FY 94 total receivables amount includes \$502,862,048 for merged and closed appropriation accounts which were cancelled and the FY 95 total receivables amount includes \$559,444,985 for merged and closed appropriations.

**Refund Receivable Claims Against Contractors:** As of September 30, 1995, the Air Force had claims against contractors valued at \$213,485,533. These contractor debts are deferred payment agreements and may result in valid receivables of the Air Force. The majority of these debts resulted from unliquidated progress payments, defective pricing, and breach of contract. Deferred payment agreements are an interim financial arrangement between the contractor and the government to defer the government's right to prompt payment from the contractor of the indebtedness, pending a decision by the ASBCA, and in no way releases or waives any other existing rights or remedies of the federal government. When the government (contracting office) issues a demand for payment of indebtedness, the contractor has a right to request that payment of the indebtedness be deferred pending disposition of its appeal to the ASBCA. In addition to the deferred payment agreements, \$605,523,358 is payable to the Foreign Military Sales Trust Fund upon collection.

**Allowance for Doubtful Accounts:** Although required by directives, no allowance for estimated uncollectible federal accounts receivable is recorded since data to compute an allowance does not currently exist. For the current year, the allowance for entity public receivables is computed at \$8,707,309. The Departmental allowance for refund receivables of \$592,883,581 for closed accounts is set equal to the receivables, or 100 percent, as it is not possible to adequately estimate the amount or timing of collections. If collected after the appropriation closes, any collections would be made to the U.S. Treasury with no benefit to the Air Force. Reported bad debt expense is sum of bad debt write offs and current year change in allowance.

**Advances:** Advances includes progress payments to contractors previously reported as work in progress. The reliability of this data is under review.

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The non-entity public receivables of \$1,366,916,766 and the related allowance of \$593,013,832 consists of the following:

	Receivable	Allowance	Note	Net Due
Closed Approp	\$559,444,985	\$559,444,985	A	0
Interest, Penalties & Admin Fees	186,234,690	29,797,550	B, C	156,437,140
Miscellaneous	15,713,733	3,771,297	B, C	11,942,436
Foreign Mil Sales Defer Pay Agree	605,523,358	0	D	605,523,358
<b>Total</b>	<b>\$1,366,916,766</b>	<b>\$593,013,832</b>		<b>\$773,902,934</b>

**Note A.** Allowance of 100 percent used as it is not possible to adequately estimate collections, and amounts eventually collected will be deposited to credit of U.S. Treasury, not the Air Force.

**Note B.** Allowance percent of 16 percent for interest, penalties, and administrative charges and 24% for miscellaneous accounts receivable are based on average percent of write-offs to yearend balances.

**Note C.** Net amount due at collection will be deposited to credit of U.S. Treasury, not the Air Force. Liabilities include an offsetting amount payable to U.S. Treasury for net amount due.

**Note D.** No allowance is set up for the deferred payment agreement amount. It is reported to disclose the fiduciary responsibility of the Air Force. Liabilities include an offsetting amount, as collections will not benefit the Air Force General Funds.

**Negative Unliquidated Obligations (NUOs):** Unmatched payments often create negative unliquidated obligations. A negative unliquidated obligation can occur (at the accountable station) when contractor accounting record payment data at one location (i.e., DFAS-Columbus Center) do not match the data in the actual accounting record at the accountable station (i.e., DAO at individual Air Force location). Differences require reconciliation to correctly account for the transaction. Citing the wrong fiscal year, contract line, appropriation, or agency, can cause unmatched payments. The negative unliquidated obligations at the accountable station may also be duplicate vendor payments.

The DFAS-Columbus Center makes disbursements and collections citing funds that belong to other Air Force accountable stations. The process facilitates prompt payments. Because the Columbus Center directly charges the appropriations, accountable stations do not reimburse the Columbus Center. When the Columbus Center makes an incorrect contract payment and the payment amount exceeds total available obligations, the result is a negative unliquidated obligation at the related accountable station.

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Efforts to correct these problems resulted in a downward trend during the fiscal year. At the end of FY 95, \$546 million was reported at accounting classification reference number (ACRN) level (gross) compared to \$2.1 billion in FY 94. Of the \$546 million in NULOs, \$163 million were 0 to 90 days old, \$84 million were 91 to 180 days old, and \$299 million were over 180 days old.

**Note 6. Other Assets.**

Cash advances to contractors totals \$620,898.

**Note 7. Loans and Loan Guarantees, Non-Federal Borrowers.**

The Air Force did not have loans or loan guarantees to report for FY 95. See Note 1.J.

**Note 8. Inventory, Net.**

The Air Force did not report inventory categories including inventories held for current sale, inventories held in reserve for future sale, excess, obsolete and unserviceable inventories, and inventories held for repair.

**Note 9. Work in Process (Personal Property).**

The Air Force has no work in process. Progress payments to contractors previously reported under this category is now in Advances and Prepayments, Entity Assets. The reliability of this data is under review.

**Note 10. Operating Materials and Supplies (OM&S), Net:**

A. Categories:	
Material in Transit	\$22,782,626
Material in Storage	23,804,607,966
Excess Property	<u>109,072,274</u>
 Total	 \$23,936,462,866 =====

B. Restrictions on operating materials and supplies: The value reported for OM&S includes War Reserve Materiel and War Readiness Spare Kits inventories.

C. Other Information:

As of September 30, 1995, the values reported in Materiel on Hand - Ammunition were obtained from the Combat Ammunition System (CAS-A) located at Hill AFB. The total dollar amounts for FY 95 in general ledger subsidiary accounts (GLSAs) 14643 (ammunition, Air Force stored) and 14644 (ammunition stored with other government agencies) were \$5,175,869,562.44 and \$1,282,932,541.50, respectively. The products/values obtained from this system were forwarded to DFAS-DE for additional review. During this review, items determined to be duplicate were deleted. This same process was used in FYs 93 and 94 to report costs and data to the appropriate GFGL

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account. Previously, for FY 92 and prior fiscal years GFGL reporting, ammunition was reported using the Combat Ammunition System (CAS) - Base (B) at those installations which had converted to CAS-B.

The general funds general ledger account balances for GLSAs 14643 - Ammunition, Air Force Stored, and 14644 - Ammunition Stored With Other Government Agencies, were obtained by using the CAS-A report provided to us from OOALC/LIWO, Hill AFB, Utah, and is reconciled to the total inventory value of \$6,458,802,103.94. This information is on file in DFAS-DE/ANBG. The CAS-A report contains the Air Force munitions value for fiscal year 1995, both stored at Air Force installations and other DoD government agencies (Army,Navy).

For GLSA 14644, dollar values reported for assets (munitions) stored at Army and Navy depots are not current. In September, while loading the depot assets, it became apparent that the hardware being used was not going to handle the workload of the additional data. Consequently, depot data updates were suspended until they could convert to a new hardware platform. CAS-A is currently in Quality Test and Evaluation II phase and has not reestablished the interface required with the depots. It is anticipated that this interface will be completed in March 1996.

For GLSA 14643, a number of bases are currently in the process of converting from SBSS to CAS-B. The conversion is a manual process and gives limited visibility during implementation. Consequently, the most accurate information possible is also not available for these bases (10 bases). In addition, as the bases are converted, a complete inventory is taken and CAS-B is updated accordingly. A major proportion of the difference reported between the 1994 and 1995 figures (approximately \$8.0 billion decrease) can be attributed to the Air Force doing a more accurate reconciliation of the commands munitions inventory and not having all available information in the CAS-B system which feeds CAS-A.

**Note 11. Stockpile Materials.**

The Air Force did not report stockpile materials.

**Note 12. Seized Property.**

The Air Force did not report seized property.

**Note 13. Forfeited Property, Net.**

The Air Force did not report forfeited property.

**Note 14. Goods Held Under Price Support and Stabilization Programs, Net.**

The Air Force did not report goods held under price support and stabilization programs.

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**Note 15. Property, Plant and Equipment, Net.  
(Thousands)**

Classes of Fixed Assets:	(1) Depreciation Method	(2) Service Life	(3) Acqui sition Value	(4) Accumulated Depreciation	(5) Net Book Value
A. Land		See	\$286,262		\$286,262
B. Structures, Facilities, & Leasehold Improvements		Notes 1-D & 1-M	38,797,002	38,797,002	
C. Military Equipment			191,576,617	191,576,617	
D. ADP Software					
E. Equipment					
F. Assets Under Capital Lease					
G. Other					
H. Natural Resources					
I. Construction in Progress			<u>3,818,434</u>	<u>3,818,434</u>	
Total			234,478,315 -----	233,478,315 -----	

**J. Other Information:**

(1) Increases in the capitalization criteria to \$50,000 or more as required by the Department of Defense Appropriations Act of 1995 resulted in decapitalization (decrease) in various property, plant and equipment assets.

(2) Weapon System Valuation Project. During FY 92, the Air Force began a project to revalue the recorded costs of weapon systems. The basic thrust of the project was to update the weapon systems listed in the Air Force Materiel Command (AFMC) technical manual, TO 00-25-30, Unit Cost of Aircraft, Guided Missiles, and Engines. This publication was last revised on May 15, 1983. However, as of September 30, 1995, weapon systems still had not been revalued based upon their acquisition cost. Major computer system changes would be required to revise present weapon system valuation procedures. In February 1995, the Federal Accounting Standards Advisory Board (FASAB) issued its proposed Statement on Accounting for Property, Plant, and Equipment. According to this document, weapon systems may be reported through a stewardship report in the future rather than on financial statements required by the CFO Act.

(3) Donated Real Property (nonmonetary). Donated real property value is the estimated value of any right, title, or interest in land and buildings, fixed improvements, utilities, and other permanent type additions to land donated to the Air Force. The balance reported at the end of FY 94 was \$256,352,435, and at the end of FY 95 was \$283,815,282.

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(4) Other Donations to the Air Force (nonmonetary).

a. Artwork: Air Force physically accounts for approximately 7,700 pieces of artwork although no value was established; any omitted amount is immaterial for financial reporting purposes.

b. Museum Items: Items donated to the Air Force Museum Program are recorded in the financial records with all other museum items. The Colonel Richard Gimbel Aeronautical Collection at the United States Air Force Academy is separately maintained by the Academy.

c. Foreign Gifts: The value of foreign gifts is not recorded in the financial statements because Air Force ownership of these gifts was not established.

(5) Work-in-Process for satellites was not identified and accounted for separately. Expenditures for this may be commingled with other account expenditures. Costs for each satellite are not tracked by unique vehicle. When a contract is completed, total costs are distributed to the vehicles covered in the contract.

(6) Construction-in-progress (real property) costs are obtained from the Base Civil Engineers (BCE) Current Month Cost Report (for ACs 80010, 83000, and 84000) and the Allotment Ledger (for Military Family Housing (MFH) projects). Construction-in-progress costs are also collected from the Army Corps of Engineers and the Navy Facilities Engineering Command for Air Force funded projects. These costs are entered into the general ledger by the DFAS Denver Center. Work in process for personal property is reported on line 1.e. of the Statement of Financial Position.

(7) Aircraft and missiles having "no operational value", and awaiting salvage, e.g., stripped B-52s, should be valued at their scrap value. In response to FY 92 audits, HQ AFMC/FM agreed to establish aircraft values at various levels from fully operational to scrap, thus reporting more accurate asset values. However, this still has not yet been accomplished.

(a) During FY 95, 666 aircraft valued at \$3.5 billion were terminated from the Air Force inventory. Additionally, 37 missiles valued at \$200 million were terminated from the Air Force inventory.

(b) As of September 30, 1995, the Air Force Materiel Command had approximately 3,252 aircraft which included 2,002 non-operational aircraft valued at \$9.3 billion in various stages of operational readiness. Additionally, of the 2,059 missiles assigned to AFMC, 1,148 missiles valued at \$621 million were not operational. However, these non-operational aircraft and missiles were included in the Air Force active inventory as fully operational. Additionally, audit findings on the FY 94 financial statements revealed that approximately 176 B-52 aircraft were reported in both the aircraft general ledger account and the excess and surplus property general ledger account. Accordingly, general ledger account 141 was overstated by \$1.8 billion and general ledger account 147 was overstated by \$1.25 million. These overstated values were corrected in the FY 94 accounting records.

(8) Uninstalled Engines - Aircraft and Guided Missiles vs Materiel in Transit: Currently, values reported for this account are obtained from the Comprehensive Engine Management System

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(CEMS) located at Tinker AFB. The values obtained are reported by Tinker AFB to DFAS-DE/ADC where they are reviewed for accuracy. Messages to the installations that handle uninstalled engines have directed that engines considered intransit are included in the uninstalled engine account. CEMS calculates the value of engines and engine modules in the Air Force inventory by multiplying the quantity and unit cost of type-model-series modification. CEMS was found deficient in that unit cost are based on standard cost; additionally, crashed, cannibalized, and scrap engines were carried at full value instead of their decreased value. A \$773,000,000 reduction in general ledger accounts 143 and 147 was entered into accounting records as prior period adjustments for FY 94.

(9) In the past the excess and surplus property general ledger account (GLA 147) was valued at acquisition cost. However, based upon the intent of a recommendation from Air Force Audit Agency, the amount reported on the FY 95 financial statements is a residual value of 2.5 percent of the acquisition cost. This is the same method used for the Defense Business Operating Fund general ledger. Therefore, the amount reported for FY 95 is \$109,072,274.

(10) Government furnished material (GFM) included in the financial statements are based on data received from the Defense Logistics Agency (DLA), which receives the data from defense contractors. The reliability of this data is currently under study.

**Note 16. Debt.**

The Air Force did not report borrowing from the Treasury, borrowing from the Federal Financing Bank, borrowing from other federal agencies, and agency debt issued by Federal Housing Administration or Tennessee Valley Authority bonds.

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**Note 17. Other Liabilities.**

**A. Other Liabilities Covered by Budgetary Resources:**

	Non Current <u>Liab.</u>	Current Liab.	Total
1. Intragovernmental:			
Unearned Revenue		\$725,141,697	\$725,141,697
DAO Treasury Cash		<u>114,411,705</u>	<u>114,411,705</u>
Total		\$839,553,402	\$839,553,402

The Treasury cash held by the DAOs includes \$620,898 in advances to contractors (see Note 3).

	Non Current <u>Liab.</u>	Current Liab.	Total
2. Governmental:			
Unearned Revenue		\$2,357,056	\$2,357,056

**B. Other Information.**

**C. Other Liabilities Not Covered by Budgetary Resources:**

	Non- Current <u>Liab.</u>	Current Liab.	Total
1. Intragovernmental			
Accrued Unfunded Exp			0
Total			0

	Non- Current <u>Liab.</u>	Current Liab.	Total
2. Governmental:			
Accrued Unfunded Exp:			
Accrued Annual Leave		\$613,754,653	
Accrued Military Leave		974,187,574	
Closed Years Accruals		<u>225,029,502</u>	
Total			\$1,812,971,729
			=====

**D. Other Information.**

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**Note 18 Leases.** The Air Force has use of leased land, buildings, and other facilities, all of which are leased under operating lease agreements. All Air Force leases are operating leases because they are contracted for annually (with a possible 4 year renewal), and paid for with the annual O&M appropriation. Thus, a capital lease amount is not reported. The following estimates are derived from the Work Space Management Plan and Budget Justification (Report Control No. 0323-GSA-XX), and the FY 95 amount is reported as part of current expenses reflected in Note 23.

<u>Fiscal Year</u>	<u>Land &amp; Building</u>
Year 1995	\$ 52,998,000
Year 1996	47,801,000
Year 1997	<u>49,190,000</u>
Total Lease Payments	\$149,989,000 -----

**Note 19. Pensions and Other Actuarial Liabilities**

See Note 1(F).

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**Note 20. Net Position**

	Revolving Trust Fund	Other Trust Funds	Appropriated Funds	Total Funds
A.				
Unexpended Appropriations				
(1) Unobligated				
a. Available			\$10,722,931,488	\$10,722,931,488
b. Unavailable			<1,058,403,825>	<1,058,403,825>
(2) Undel Orders			<u>41,203,116,996</u>	<u>41,203,116,996</u>
Total			50,867,644,659	50,867,644,659
B.				
Invested Capital			266,433,655,505	266,433,655,505
C.				
Cum Result of Operations				
D.				
Other	\$1,709,908	\$4,085		\$1,713,993
E.				
Future Funding Requirements; See G. (3) below			<1,774,157,966>	<1,774,157,966>
F.				
Total	<u>\$1,709,908</u>	<u>\$4,085</u>	<u>\$315,527,142,198</u>	<u>\$315,528,856,191</u>

G. Other Information:

The Air Force's equity, as presented above, consists of unexpended appropriations, invested capital, and other future funding requirements:

(1) Unexpended appropriations and other represent amounts of funding authority which were not obligated, rescinded or withheld pending withdrawal, and amounts obligated but unpaid. (More specifically, unexpended appropriation balances are those amounts of currently available funds which are not classified as accrued expenditures unpaid or accrued expenditures paid.)

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Other consists of:

Revolving Trust Funds	
Cadet Trust Fund	\$4,085
Other Trust Fund (Gift)	<u>1,709,908</u>
Total Trust Funds	\$1,713,993

Unexpended appropriations consist of:

Appropriated Funds	
General Funds	
Operating Appropriations	
RDT&E	9,237,449,362
Operation and Maintenance, AF	8,401,310,120
Military Family Housing O&M	401,980,319
Operation and Maintenance, ANG	655,116,977
Operation and Maintenance, Reserve	406,351,630
Reserve Personnel	100,030,421
Military Personnel	107,199,820
National Guard Personnel, AF	<u>53,081,708</u>
Unexpended Operating Appropriations	<u>\$19,362,520,357</u>
Capital Appropriations	
Aircraft Procurement	\$17,731,177,342
Other Procurement	5,744,850,990
Missile Procurement	5,394,976,654
Military Construction	1,410,715,773
Military Construction, ANG	498,642,824
Family Housing, Construction	425,092,859
Military Construction, AF Reserve	89,975,297
Ammunitions Procurement	<u>209,062,367</u>
Unexpended Capital Appropriations	<u>\$31,504,494,106</u>
Total General Funds Unexpended Appropriations	\$50,867,014,463
Special Funds-	
Conservation Programs on Military Reservations (Wildlife)	<u>630,196</u>
Total Unexpended Appropriations	\$50,867,644,659

(2) Invested capital, as presented in the Consolidated Statement of Financial Position, represents the value of the Air Force's capital assets. These capital assets are classified as work in progress (personal property), operating materials and supplies, and property and equipment. Increases to capital assets and invested capital are recorded when such capital assets are acquired or constructed (See Note 15), or when asset valuations increase as a result of increases in standard prices/costs. Decreases occur when such capital assets are consumed in operations or otherwise disposed of. Assets transferred without reimbursement similarly affect capital assets and the contra invested capital amount.

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(3) Future funding requirements represents the accumulated effect of unfunded expenses net of specific receivables that upon collection will reverse budgetary authority (see Note 32).

**NOTE 21. Taxes**

The Air Force did not report tax revenues.

**Note 22. Other Revenues and Financing Sources:**

**A. Other Revenues and Financing Sources:**

Change in Claims against contractors and Others	\$36,314,510
Donations to the Gift Fund and other revenue to the Trust Funds	<u>912,565</u>
Other Revenues and Financing Sources	\$37,227,075
	=====

B. Other Information: See Note 5.C., Allowance for Doubtful Accounts, for further information on claims against contractors. See Note 1.E.2.a for further information on donations to the Gift Fund.

**Note 23. Program or Operating Expenses:**

**A. Operating Expenses:**

1. General Funds	\$54,628,409,970
2. Special Funds	408,813
3. Trust Funds	<u>477,859</u>
Total (Line 9)	\$54,629,296,642

**B. Operating Expenses for General Funds:**

1. Operation and Maintenance, AF	
a. Personnel Compensation	\$2,880,907,675
b. Personnel Benefits	770,402,202
c. Travel and Transportation of Persons	688,235,984
d. Transportation of Things	380,334,193
e. Rent, Communications and Utilities	788,817,563
f. Printing and Reproduction	47,520,798
g. Other Services	8,489,249,464
h. Supplies and Materials	3,978,141,824
i. Equipment	632,911,649
j. Land and Structures	38,858
k. Grants, Subsidies, and Contributions	35,591,374
l. Insurance Claims and Indemnities	67,388,133
m. Interest and Dividends	3,285,052
n. Unclassified	<u>57,859,371</u>
Total	<u>18,820,684,140</u>

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2. Operation and Maintenance, Air Nat Guard	
a. Personnel Compensation	910,248,859
b. Personnel Benefits	219,574,308
c. Travel and Transportation of Persons	41,051,868
d. Transportation of Things	5,659,366
e. Rent, Communications and Utilities	41,595,853
f. Printing and Reproduction	1,272,270
g. Other Services	618,851,776
h. Supplies and Materials	821,851,405
i. Grants, Subsidies, and Contributions	6,452
j. Insurance Claims and Indemnities	(18,641,702)
k. Interest and Dividends	64,829
l. Unclassified	12,407
m. Equipment	<u>75,778,923</u>
Total	<u>2,717,326,614</u>
3. Operation and Maintenance, AF Reserve	
a. Personnel Compensation	\$543,608,569
b. Personnel Benefits	134,057,861
c. Travel and Transportation of Persons	17,573,015
d. Transportation of Things	1,325,995
e. Rent, Communications and Utilities	19,549,550
f. Printing and Reproduction	2,301,200
g. Other Services	276,924,174
h. Supplies and Materials	368,009,086
i. Equipment	41,611,352
j. Grants, Subsidies, and Contributions	35,399
k. Insurance Claims and Indemnities	3,471,814
l. Interest and Dividends	34,725
m. Unclassified	<u>4,452,140</u>
Total	<u>1,412,954,880</u>
4. Operation and Maintenance, Military Family Housing	
a. Personnel Compensation	66,134,780
b. Personnel Benefits	1,891,034
c. Travel and Transportation of Persons	2,227,196
d. Transportation of Things	3,182,741
e. Rent, Communications and Utilities	230,047,504
f. Printing and Reproduction	55,224
g. Other Services	420,228,798
h. Supplies and Materials	46,119,327
i. Equipment	22,479,695
j. Grants, Subsidies, and Contributions	549,677
k. Insurance Claims and Indemnities	107,658
l. Refunds	26,034
m. Unclassified	<u>13,416,860</u>
Total	<u>806,466,528</u>

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5. Operation and Maintenance, Research, Development, Test and Evaluation	
a. Personnel Compensation	493,928,652
b. Personnel Benefits	107,487,611
c. Travel and Transportation of Persons	40,931,419
d. Transportation of Things	2,798,403
e. Rent, Communications and Utilities	54,727,448
f. Printing and Reproduction	1,688,121
g. Other Services	780,283,324
h. Supplies and Materials	197,776,877
i. Equipment	110,322,233
j. Land and Structures	-
k. Grants, Subsidies, and Contributions	4,722
l. Insurance Claims and Indemnities	-
m. Interest and Dividends	133,505
n. Unclassified	
Total	<u>1,790,082,315</u>
6. Research, Development, Test, and Evaluation other than Operations and Maintenance	
a. Projects	<u>9,545,269,433</u>
Total	<u>11,335,351,748</u>
7. Military Personnel	
1. Active Duty	
Unclassified	
Pay and Allowance - Officers	4,259,677,668
Basic Allowance, S, FSA, Ret Pay - Off	1,576,032,985
Pay and Allowance - Enlisted	7,335,986,105
VHA, FSA, Employers Social Security	2,762,216,530
Pay and Allowance - Cadets	35,793,000
Subsistence - Enlisted	688,620,945
PCS - Officer and Enlisted	784,560,041
Other Military Personnel Costs	<u>92,303,000</u>
Total	<u>17,535,190,274</u>
8. Reserve Personnel	
Reserve Personnel	616,506,466
Full Time Act Duty - PCS - Travel	64,369,732
Officer Training	42,715,451
Refunds - Transportation	(39,695)
Unclassified	<u>79,537</u>
Total	<u>723,631,491</u>
9. National Guard Personnel	
Unclassified	(3,263)
Basic Pay	603,886,400
Other Training and Support	692,124,846
Refunds - Transportation	<u>(2,006,566)</u>
Total	<u>1,294,001,417</u>

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10. Total General Funds	54,645,607,092
<Less>: Redistribution for Bad Debt Write-off	<10,738,648>
Interest, and Penalties and Discounts Lost	<6,449,474>
 Total General Fund Operating Expenses	 \$54,628,418,970 =====

D. Expenses of Capital Appropriations are listed in Note 31.

**Note 24. Cost of Goods and Services Sold.**

The Air Force did not have cost of goods and services sold to report for FY 95. However, reimbursable program costs are shown in this category and are offset by earnings from the reimbursable program on line 2.

**Note 25. Other Expenses.**

A. Other Expenses:

(1) Equipment lost in crashes	\$663,602,723
(2) Unfunded expense - accrued leave	126,159,091
(3) Unfunded expense - M and closed year payables change	80,745,916
(4) Discounts lost	<u>2,989,474</u>
 Total	 \$873,497,204 <u>                    </u>

B. Other Information:

**Note 26 - Extraordinary Items and Note 27 - Prior Period Adjustments.**

Subsequent to the issuance of financial statements for the Department of the Air Force as of September 30, 1994, adjustments were made to the amounts presented. These adjustments were necessitated by audit findings and other work. If a single period statement was presented, these adjustments would reflect adjustments of the opening balance of net position (September 30, 1994) by presenting prior period adjustments. As comparative period statements are presented, the previously issued statements as of September 30, 1994 were restated to include the subsequent adjustments.

The net adjustments and their net affect on the previously issued statements as of September 30, 1994, are as follows:

1. Corrected overstatement of operating materials and supplies by \$1,234,231,000.

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- 2. Corrected overstatement of property, plant, and equipment by \$3,834,095,907.
- 3. Corrected overstatement of invested capital by \$5,068,326,907 (sum of items 1 and 2).

**Note 28. Non-Operating Changes - (Transfers and Donations)**

**A. Increases**

(1) Transfers in	\$ -
(2) Donations received	-
(3) Other increases	-
(4) Total increases	<u>-</u>

**B. Decreases**

(1) Transfers Out:	
(a) Return of closed year authority	993,772,277
(2) Donations	-
(3) Other Decreases	<u>1,650,536,350</u>
(4) Total Decreases	<u>2,644,308,627</u>

C. Net Non Operating Changes \$2,644,308,627

**D. Other Information:**

Other decreases includes:

Net change, or increase, in invested capital. See Note 30.	\$1,664,620,493
Excess of current year expenditures over current year expenditures in appropriations made available in current year, net of adjustments:	
Available current year appropriation	\$74,355,433.133
Less expenditures, current and prior year appropriations	<u>77,670,589.976</u>
Net decrease	<u>3,315,156,843</u>
	<u>\$1,650,536,350</u>

As the general fund includes one year, two year, five year, and no year appropriations, these were available unexpended appropriations brought forward from FY 94 to cover the excess of FY 95 expenditures over FY 95 appropriations made available.

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**Note 29. Intrafund Eliminations.**

	<u>Accounts Receivables</u>	<u>Revenues</u>
	<u>Accounts Payable</u>	<u>Expenses</u>
General Funds	\$741,290,642	\$2,523,187,395
Deposit Funds	0	0
Special Funds	0	0
Trust Funds	0	0

Intrafund transactions relate to only Air Force funds and enter the accounting records as accounts receivable and revenues. It is presumed that an equal amount of accounts payable and expenses were entered on the accounting records. Consequently, those amounts can be eliminated from the financial statements. Intrafund eliminations are discussed on Note 1.E.1.

**Note 30. Proprietary Contingencies (contingent liabilities)**

**Proprietary Contingencies:** Proprietary contingencies are commonly referred to as contingent liabilities. If they meet certain requirements, proprietary contingencies are either disclosed in the notes to the financial statements or recorded as liabilities in the principal financial statements. Proprietary contingencies are indicated below. See Footnote 1P for budgetary contingencies.

The Air Force has a total of \$4,019,677,347 as commitments at the end of FY 95 in expired, unexpired, and closed accounts. This amount is not reported in financial statements and includes contract award fees, contract disputes, and commitments that should have been deleted at the end of FY 95.

Unfunded liabilities from "M" and closed years amount to \$225,029,500 (see Note 32 for future funding requirements). It is reasonably possible that this liability may be incurred.

The Air Force is party to various legal and administrative claims brought against it. Most are tort claims initiated by individuals addressing aircraft and vehicle accidents, medical malpractice, property and environmental damages resulting from Air Force activities, and contract disputes.

Certain legal actions to which the Air Force is named a party are administered and, in some instances litigated, by other Federal agencies. Legal actions to which the Air Force is a litigant are covered by the Federal Tort Claims Act and Chapter 163 (Military Claims) of Title 10, United States Code (U.S.C.). Contingent liabilities under the Tort Claims Act and Chapter 163, Title 10 U.S.C., are \$2,500 and \$100,000 respectively, per occurrence. Settlements in excess of these amounts are paid from the Treasury's Claims, Judgments and Relief Acts Fund; under these situations the Treasury's Claims, Judgments and Relief Acts Fund is not reimbursed by Air Force appropriations, and contingent liabilities arising from legal actions against the Air Force will not materially affect its operations or financial condition. However, the Air Force must reimburse the Treasury's Claims, Judgments and Relief Acts Fund for claims filed under the Contract Disputes Act.

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The Air Force's potential liability for all civil law and litigation claims (including claims both over and under \$100 million) outstanding as of September 30, 1995 may amount to \$949 million.

Claims under \$100 million each amounted to approximately \$649 million. However, it is uncertain that these claims will ever accrue to the Air Force and thus are not reflected in the financial statements. In addition to the fact that many cases simply lack merit, most claims, even if successful, will not be paid from Air Force accounts. Rather, judgments are ordinarily paid from the GAO Judgment Fund, not from Air Force accounts. In many cases involving attorney fees, the amounts are not known until the last appeal is taken.

The Legal Representation Letter describes contingent liabilities over \$100 million, which will probably be paid from the Treasury's Claims, Judgments and Relief Acts Fund, and thus, are not reflected in the Air Force financial statements. In FY 95 there was one pending case involving more than \$100 million in which the Department of the Air Force was a party. Since Air Force appropriations do not necessarily pay for all judgments or settlements for cases, and the probability of payment is unknown, this pending case is not reflected in the financial statements. This case, which has a total dollar value of approximately \$300 million, is presently in litigation.

As of September 30, 1995, the Air Force was a party to 388 contract appeals before the Armed Services Board of Contract Appeals. The total dollar value of these claims was approximately \$1 billion which included \$783,734,798 in contractor claims. Such claims are funded primarily from Air Force appropriations.

The Air Force is responsible for environmental cleanup. This responsibility is programmed into the Air Force 6 year defense plan. The total cost to the Air Force is estimated at \$7.9 billion between 1994 and 2030, however, the probability of actual disbursement is not known. In FY 94, the Air Force disbursed approximately \$513 million, and disbursed approximately \$367 million in FY 95.

Future workers' compensation benefits pertaining to the Federal Employees' Compensation Act (FECA) is estimated at \$1 billion for the next 23 years. The probability of this contingent liability is not known, so the \$1 billion is not included in the financial statements. However, annual FECA disbursements are approximately \$200 million, and are included in the financial statements.

### **Note 31. Other Disclosures.**

**Accrued Expenditure Report:** As required by the DoD Accounting Manual, Chapter 27, Accounts Payable, Public includes \$3,042,892,382 of Accrued Expenditures Unpaid from the HAF-ACF(M)7152 report received from the Columbus Center relating to central procurement. The report reflects outstanding accounts payable, invoices on hand but unmatched to accounts payable, recoupments of progress payments, and withholding on cost/fee vouchers because of nonreceipt of patent clearances.

**Canceled Balances:** All unliquidated balances associated with the closed account have been canceled in accordance with Public Law 101-510. Canceled accrued expenditures unpaid are reflected in the financial statements as unfunded liabilities. Canceled undelivered orders

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outstanding are not included in the financial statements, however, these orders may result in future expenditures. Canceled receivables are included in the Air Force Statement of Financial Position.

**Cadet Fund:** The only equity in the Cadet Fund is the Cadet Emergency Leave Fund totaling \$4,085 as of September 30, 1995. The Cadet Emergency Leave Fund receives its money from a one-time collection from each freshman cadet. The Cadet Fund receives a check from DFAS-DE which represents funds from the cadets to pay vendors who perform services for the cadets (e.g., dry cleaning, tailors, and barbers). All dollars received by the Cadet Fund are disbursed out for support of cadets.

**UNMATCHED DISBURSEMENTS, NEGATIVE UNLIQUIDATED OBLIGATIONS, AND AGED IN-TRANSIT DISBURSEMENTS**

Treasury Index 57

Air Force Appropriations	June 1994	September 1995 ***	Change	Percent Change
Unmatched Disbursements	N/A*	\$766,320	N/A*	N/A*
Negative Unliquidated Obligations**	N/A*	325,545	N/A*	N/A*
Aged In-Transit Disbursements	N/A*	1,783,872	N/A*	N/A*
Totals	<u>N/A*</u>	<u>\$2,875,737</u>	<u>N/A*</u>	<u>N/A*</u>

\*1994 data is unavailable since the amounts are not broken out between DBOF, FMS, and General Funds (Air Force, and OSD allocations to Air Force). However, overall these aggregate problem disbursements as of June 30, 1994 were \$8,219 million. Aggregate problem disbursements as of September 30, 1995 were \$4,656 million, reflecting a reduction of \$3,563 million.

\*\*Represents all negative balances not obligated including deferred items awaiting correction from paying station or awaiting funding.

\*\*\*All dollar amounts above apply only to general funds.

The problem disbursement amount represents less than one percent of the Air Force total assets. The DFAS and customers are making concerted efforts to reduce problem disbursements, including pre-validation of obligations before disbursements (Public Law 103-335).

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**Net Change in Invested Capital.**

The overall change in invested capital for FY 95 was an increase of \$1,664,620,493, and for FY 94 as restated an increase of \$4,531,030,938. It is computed as the change from the previous years sum of progress payments to contractors, operating materials and supplies, and property and equipment. It is included in non-operating changes reported on line 23 of the statement of operations and changes in net position. The Air Force general ledger system does not allow for detailed tracking and presentation of the various causes of changes in invested capital. Moreover, the present system does not allow for reconciling total appropriations from the capital appropriations discussed below and amounts capitalized in the general funds general ledger.

The current budgetary and accounting process under which the Air Force operates does not distinguish between capital and operating expenses within appropriations. Therefore, appropriations were classified as either operating appropriations or capital appropriations for financial statement reporting purposes. Expenditures from capital appropriations were \$23,024,574,071 for the year. Accrued expenditures, by capital appropriation are as follows (the amounts for appropriations classified as operating appropriations are listed in Note 23):

Aircraft Procurement (3010)	\$8,804,346,861
Procurement of Ammunition, AF (3011)	77,284,633
Other Procurement (3080)	7,896,952,226
Missile Procurement (3020)	4,679,797,617
Military Construction (3300)	988,095,635
Military Construction, ANG (3830)	231,023,576
Family Housing, Construction (0704)	268,162,579
Military Construction, AF Reserve (3730)	<u>78,210,944</u>
Total Capital Accrued Expenditures	\$23,024,574,071
	=====

This total expenditure amount does not automatically increase invested capital for a like amount. Only expenditures from an appropriation meeting the current capitalization guidelines and dollar threshold of \$50,000 will increase the value of property, plant and equipment. Only expenditures for items of a nature included in operating material and supplies, and not consumed in the current year, will increase the value of inventories not held for sale.

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**Future Funding Requirements.**

Future funding requirements consist of:

Liabilities not covered by budgetary resources:

Accrued annual leave	\$613,754,653
Accrued military leave	974,187,574
Closed years accruals	<u>225,029,502</u>
	1,812,971,729

<Less>: Other assets, advances and prepayments that will go to Air Force budgetary authority upon collection, net of allowance	<u>&lt;38,813,753&gt;</u>
	\$1,774,157,966
	=====

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***DEPARTMENT OF THE  
AIR FORCE***

***GENERAL FUNDS***

***SUPPLEMENTAL***

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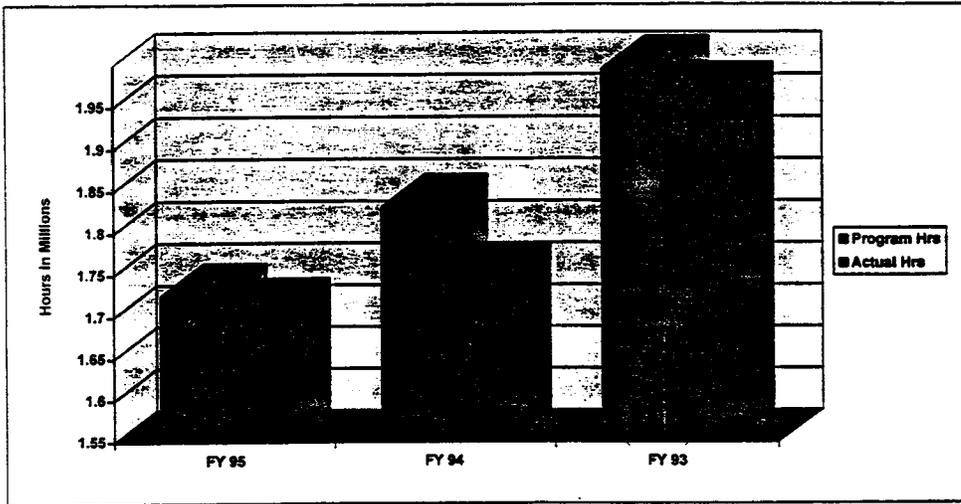
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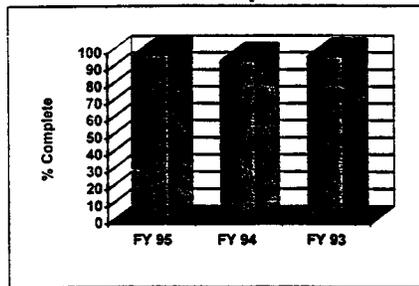
FLYING HOURS PROGRAM

Hours



Hours in millions	FY 95	FY 94	FY 93
Program Hrs	1.726	1.832	1.995
Actual Hrs.	1.709	1.750	1.964
% Complete	99.4	95.5	98.4

Percent Complete



Percent completion varies due to numerous factors such as fact-of-life program changes during the year, weapon systems retirements, conversion of hours between weapon systems, and aircraft grounding.

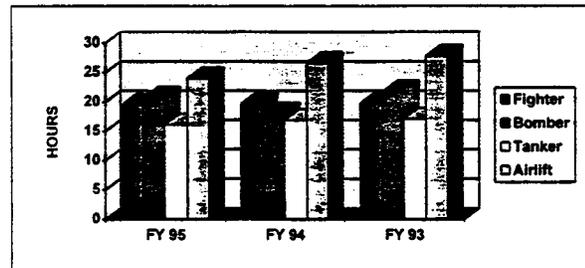
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HOURS PER CREW PER MONTH (HCM)



	FY 95	FY 94	FY 93
Fighter	19.9	19.7	19.8
Bomber	20.7	18.0	21.7
Tanker	16.1	16.9	17.1
Airlift	24.0	26.6	27.8

HCM reflects the number of flying hours programmed per aircrew for a 30-day period. Variances among the groupings are due to differences in mission profiles and training requirements for different categories of aircraft. These variances are also the reason data are depicted by category versus an overall composite Air Force HCM.

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**OPERATION AND MAINTENANCE FUNDS IN SUPPORT OF  
FLYING HOURS PROGRAM**

(000's)

	<b>FY 95</b>	<b>FY 94</b>	<b>FY 93</b>
Systems Support	\$ 136,121	\$ 214,975	\$ 175,594
General Support	179,868	212,461	215,789
Depot Level Reparables (DLRs)	1,409,725	1,469,764	1,034,827
Aviation Fuels	986,834	1,203,048	1,168,978
<b>TOTAL</b>	<b>\$2,712,548</b>	<b>\$3,100,248</b>	<b>\$2,595,188</b>

- FY 93 - FY 94 DLR increase was due to a +25.5% price change, the implementation of two-level maintenance, and the transfer of the Air Force Mobility Command out of the Defense Business Operations Fund in FY 94
- FY 94 - FY 95 DLR decrease is due to a -6.3% price change
- FY 94 - FY 95 aviation fuels decrease is due to a -12.3% price change, command flying hour underfly/program changes, and an increase in assistance-in-kind

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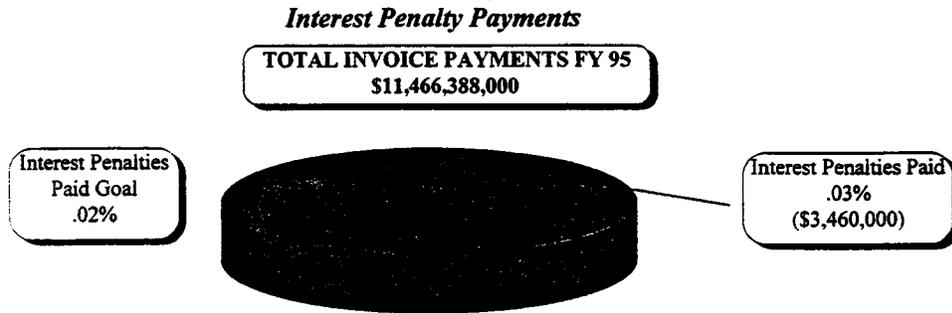
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• Prompt Payment Act (PPA)

Interest penalty payments are paid to commercial vendors when their invoices are paid late. The Air Force, in conjunction with DFAS, is close to achieving its goal in this area:



**Lost Discounts**

Cash management principles require vendors not be paid early, but that all cost-effective discounts are taken.



DFAS has instituted a number of changes aimed at solving these problems. Among those changes are increases in temporary hires, changes in procedures, and more efforts to clean up databases at Air Force bases about to be consolidated.

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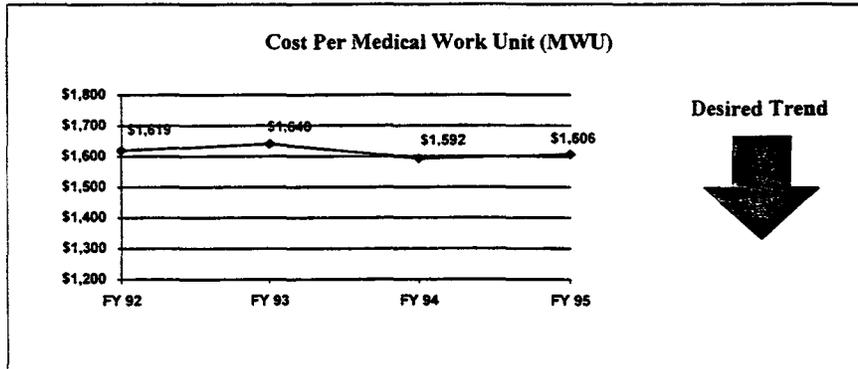
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ANALYSIS OF HEALTH CARE STANDARD

The Air Force has undergone a major shift in the manner we provide resources to our Air Force hospitals and clinics. Capitation budgeting became a reality for all Air Force facilities in FY 94 and continued in FY 95. Capitation is simply a dollar amount provided to the facility to meet the health care needs of eligible beneficiaries or users in their locale. The capitation resource model is primarily based on population served with the exception of mission-oriented requirements or directed programs. The performance incentives change under capitation budgeting to limiting expensive, unnecessary care and keeping the population healthy and out of the hospital.

Past performance indicators rewarded ever higher utilization of clinics and hospitals. The more visits or bed days a facility generated led to higher budgets, regardless of population served. Under capitation budgeting these negative incentives are removed. The incentive under capitation budgeting is to meet the health needs of the population in the most cost effective manner possible. The Air Force is committed to total operational forces support incorporating sound economic principles, delivering compassionate care with fiscal resolve.

The Air Force Surgeon General measures success in making efficient use of medical resources in three ways:



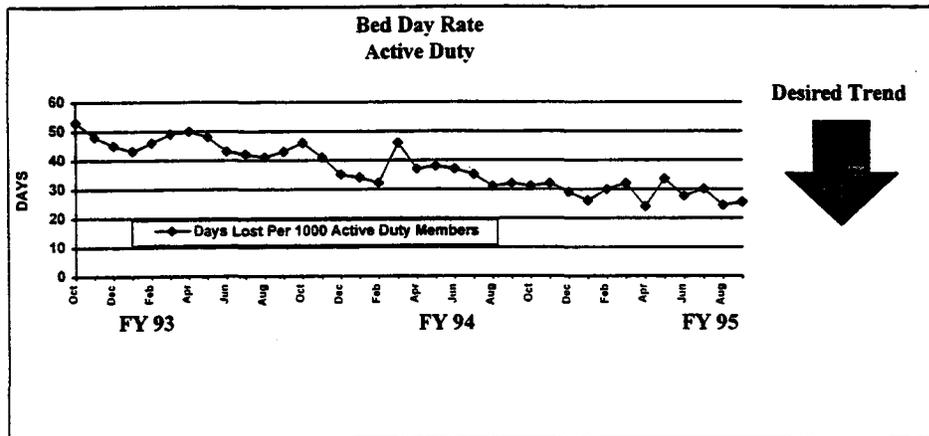
The current trend in Cost Per MWU begins to reflect some of the efficiencies introduced into health care delivery management, such as the transition to ambulatory surgical units and settings, Prime Vendor arrangements requiring less investment in inventory, and arrangements leading to better health care delivery settings such as right sizing and external partnership programs.

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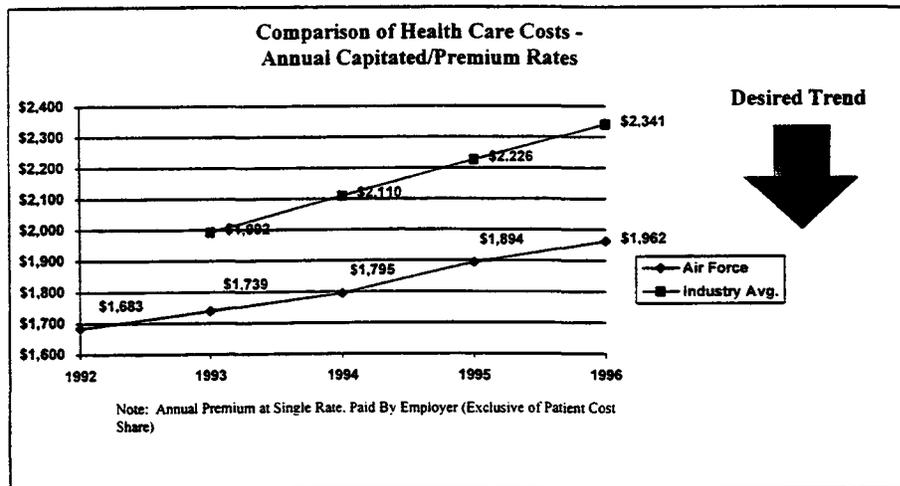
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To determine the health status of active duty forces, the bed day rate is used. The Retrospective Case Mix Analysis System and Defense Medical Information System are used to determine bed days and population. The bed day rate is the monthly inpatient bed days per 1000 active duty members. The goal is a downward trend, which reflects fewer duty days lost due to hospitalization.



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The comparison of health care costs with civilian fee-for-service programs and HMOs allows the Air Force to measure our competitive position in the health care marketplace, make a comparison of civilian programs with similar benefits packages, and reflect the impact of the TRICARE Support Contracts setting and other costs associated with the delivery of care. More importantly, this measure is in concert with our focus on wellness and preventative care. Note: This measure is based on the most recent OASD(HA) estimate of the cost per Air Force "USER" and FY95/FY96 capitated allocations. Additionally, it includes only O&M, CHAMPUS, and MILPERS costs. It excludes MILCON, investment equipment, or other overhead costs such as depreciation.

The major reasons for differences between the Air Force and civilian programs are:

1. Transition to system-wide capitation; incentive changes
2. Implementation of utilization management and review
3. TRICARE deployment which includes fixed-price contracts
4. Concerted efforts to transition to ambulatory care settings
5. Better emphasis on less inventory
6. Technology insertion -- increased access
7. Innovative health care delivery arrangements such as right sizing, external partnership programs, VA joint ventures

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#### *REAL PROPERTY MAINTENANCE ACTIVITIES (RPMA) PROGRAM*

The Air Force Plant Replacement Value (PRV) as of the middle of FY 95 has been calculated at \$185.54 billion. The Commander's Facilities Assessment (CFA) Real Property Maintenance (RPM) requirements for the active Air Force are \$807 million in Level I (Unsatisfactory) and \$2,826 million in Level II (Degraded). These are from the 1993 CFA baseline survey.

PRV is the amount of money required to replace the Air Force's active, guard, and reserve physical plant (facility for facility, mile of road for mile of road, etc.) in FY 95 dollars. The figure is calculated using the official Air Force real property records consisting of over 450,000 individual facility records. Information extracted from the records include the scope, unit of measure, facility category code, and description of each facility. The PRV model takes into account the unit cost for the type of facility, a facility size adjustment factor, area cost factors, a percentage for site preparation, design, and construction management. The PRV has been adjusted for all known base closures, realignments, and transfers through July 1995. Out-year projections are also calculated using approved inflation factors. PRV includes both vertical facilities, as well as those not measured by square feet (i.e., utility systems, air field pavements, and roadways) which account for upwards of 35% of the total value. The figure above does not include the military family housing PRV or PRV for three Air Force installations funded from research, development, test, and evaluation (RDT&E) appropriations.

The Commander's Facility Assessment (CFA) enables installation commanders to link facility performance directly with mission requirements to ensure proper resource allocation for facility maintenance, repair, and construction. The methodology first requires installation commanders to assess facility deficiencies. The commander then assesses the capability of the facilities and infrastructure to support the installation's mission. From this assessment the facilities and infrastructure are rated using the following rating definitions:

Level I (Unsatisfactory) - The condition and quality of the facility or infrastructure inhibit mission readiness and contribute to substandard quality of life.

Level II (Degraded) - The condition and quality of the facility or infrastructure impairs mission readiness and contributes to poor quality of life.

Level III (Adequate) - The facility or infrastructure is generally adequate, but investments are required to increase productivity and drive down O&M costs.

CFA requirements are programmed and funded based on deficiency levels. Current funding levels will enable the Air Force to buy out Level I requirements and significantly reduce the Level II deficiencies. All CFA requirements are validated annually. CFA does not include an estimate of deterioration of effects of unannounced base closures.

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**FINANCIAL ATTRIBUTES OF DoD ENTITIES  
FY 95  
AIR FORCE TRUST FUNDS**

<b>Operating Costs Attribute:</b>	<b>Trust Fund Consolidated 1995</b>	<b>Trust Fund Consolidated 1994</b>
<b>Current Dollars:</b>		
• Total Costs and Expenses(Statement of Operations, line 15)	\$8,109,352	\$6,647,000
• Revenues and Reimbursements (Statement of Operations, line 8c)	8,544,058	6,183,000
• Net Operating Costs(Statement of Operations,line 16)	<434,706>	464,000
• Annual Percentage Change	7%	<56%>
<b>1991 Constant Dollars (factor 1995 = .75) (factor 1994 = .79)</b>		
• Net Operating Costs	326,030	366,560
• Annual Percentage Change	12%	<58%>

**Narrative:**

This attribute represents how much it costs to operate a program. The cost of operating a program is its net operating cost, which is equal to the program's total expenses and losses, minus its revenues and reimbursements.

The Air Force Trust Fund is composed of the Cadet Fund and the Gift Fund. The Trust Fund is used to record the receipt and outlay of funds held in trust by the government for use in carrying out specific purposes or programs. The trust funds operate on a cash basis. In FY 95, revenues exceeded expenses by \$434,706. In FY 94, expenses exceeded revenues by \$464,000.

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**FINANCIAL ATTRIBUTES OF DoD ENTITIES  
FY 95  
AIR FORCE TRUST FUNDS**

<b>Operating Results Attribute:</b>	<b>Trust Fund Consolidated 1995</b>	<b>Trust Fund Consolidated 1994</b>
• Revenues:		
• Federal sources	0	0
• Public sources	\$7,631,493	\$5,777,000
• Other (Statement of Operations, line 6)	912,565	407,000
• Total Revenues (Statement of Operations, line 8a)	8,544,058	6,184,000
• Expenses and Losses (Statement of Operations, lines 15 + 17)	8,109,352	6,647,000
• Net Operating Income (Deficit) (St. of Operations, lines 8 + 18)	434,706	<464,000>
• Additional Appropriations (St. of Operations, line 1)	0	0
• Operating Surplus (Deficit) (St. of Operations, lines 1 + 8 + 18)	434,706	<464,000>

**Narrative:**

This attribute identifies whether a program's operations resulted in an excess of expenses over revenues and appropriations or vice versa. A program's operating results for a fiscal year are measured by calculating the difference between the net operating cost and the amount of funds appropriated to the program for that fiscal year.

The Air Force Trust Fund is composed of the Cadet Fund and the Gift Fund. The Trust Fund is used to record the receipt and outlay of funds held in trust by the government for use in carrying out specific purposes or programs. The trust funds operate on a cash basis. In FY 95, the Trust Fund had an operating gain of \$434,706. In FY 94, the Trust Fund had an operating loss of \$464,000.

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FINANCIAL ATTRIBUTES OF DoD ENTITIES  
FY 95  
AIR FORCE TRUST FUNDS

Financial Conditions Attribute:	Trust Fund Consolidated 1995	Trust Fund Consolidated 1994
• Available Sources of Cash (Statement of Financial Position, line 1a(1) thru (d))	\$2,346,632	\$1,698,000
• Future Requirements for Cash (St. of Fin. Position, line 1a(1) (a)-(d) + line 7e)	0	2,105,000
• Cash Surplus (Shortfall) (St. of Fin. Position, line 7c)	0	0
• Total Assets (St. of Fin. Position, line 3)	3,760,201	2,650,000
• Total Liabilities (St. of Fin. Position, line 6)	2,046,208	1,371,000
• Asset to Debt Ratio	1.84	1.93

Narrative:

This attribute is defined as the financial health of a program and its inherent ability to generate financial resources to maintain its operations and meet its financial obligations, when they are due, without considering financial assistance (such as additional appropriations). The debt-to-asset ratio can be used to test a program's solvency.

The Cadet Fund and Gift Fund did not acquire their assets through debt. Gifts or capital are donated to the Trust Fund; this increases the equity accounts, not the liability accounts.

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**FINANCIAL ATTRIBUTES OF DoD ENTITIES  
FY 95  
AIR FORCE - OTHER FUNDS AND ACCOUNTS  
GENERAL FUNDS**

<b>Capital Investment Attributes:</b>	<b>1995</b>	<b>1994</b>
• Purchase of Property, Plant & Equipment	\$23,024,574,071	\$25,322,130,000
• Less: Sales of Property, Plant and Equipment (data unreliable)	0	0
• Net Cost of Capital Assets	23,024,574,071	25,322,130,000
• Average Balance of Capital Assets (Statement of Financial Position, line 2d)	265,383,736,589	132,971,734,462
• % of Acquisition to Book Value	6%	10%
1990 Constant Dollars		
• (factor 1995 - .762)		
• (factor 1994 - .830)		
• Net Cost of Capital Assets	17,544,725,442	21,017,367,900
• % of Acquisitions to Book Value	8%	8%

**Narrative:**

This attribute represents the money a program spends for the acquisition of long-term assets such as land, buildings, equipment, and other facilities. Capital investments of a program are measured by determining the net cost, which equals the gross amount of expenditures made to acquire long-term physical and financial assets, less capital recovered from the disposition of long-term assets.

The General Fund finances the functional and administrative support required to operate and maintain Air Force installations. In FY 95, the General Fund increased its property, plant, and equipment by 6 percent, and in FY 94 by 10 percent.

Appendix B. AFAA Report, "Opinion on Fiscal Year 1995 Air Force Consolidated Financial Statements"

**Project 95053001**

**Financial Statements and Notes**

**Supplemental**

**FINANCIAL ATTRIBUTES OF DoD ENTITIES  
FY 95  
AIR FORCE - COMPONENT OF OTHER FUNDS AND ACCOUNTS  
DEPOSIT FUNDS**

<b>Financial Condition Attribute:</b>	<b>1995</b>	<b>1994</b>
• Available Sources of Cash	\$53,761,000	\$53,598,000
• (Statement of Financial Position, lines 1a(1) (a)-(d) + 2a (1))		
• Future Requirements for Cash (Statement of Financial Position, lines 1a(1) (a) - 1d+7e)	53,761,000	53,598,000
• Cash Surplus (Shortfall) (Statement of Financial Position, line 7c)	0	0
• Total Assets (Statement of Financial Position, line 3)	53,761,000	53,598,000
• Total Liabilities (Statement of Financial Position, line 6)	53,761,000	53,598,000
• Asset to Debt Ratio	1	1

**Narrative:**

This attribute is defined as the financial health of a program and its inherent ability to generate financial resources to maintain its operations and meet its financial obligations, when they are due, without considering financial assistance (such as additional appropriations). The debt to asset ratio can be used to test a program's solvency.

Deposit Funds are used to (a) hold assets whose distribution awaits legal determination or for which the Air Force acts as agent or custodian, and (b) account for unidentified remittances. In the Deposit Fund, assets acquired are either held for others, or for-self. This fund does not accumulate equity, thus the debt to asset ratio of 1.

**Appendix B. AFAA Report, "Opinion on Fiscal Year 1995 Air Force Consolidated  
Financial Statements"**

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**Financial Statements and Notes**

**Project 95053001**

**Supplemental**

**Appendix B. AFAA Report, "Opinion on Fiscal Year 1995 Air Force Consolidated Financial Statements"**

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Project 95053001

VERBATIM MANAGEMENT COMMENTS



Office of the Assistant Secretary

DEPARTMENT OF THE AIR FORCE  
WASHINGTON, DC

27 FEB 1996

MEMORANDUM FOR SAF/AG

FROM: SAF/FM

SUBJECT: Management Comments to the Air Force Audit Agency (AFAA) Draft Report of Audit, Opinion on Fiscal Year 1995 Air Force Consolidated Financial Statements (Project 95053001)

We appreciate the opportunity to review this report and provide our comments. We have limited our comments to this consolidated opinion report and may provide specific comments on other reports as we review them.

We agree with the basis for your position that you are unable to express an opinion on the reliability of the Air Force financial statements for fiscal year 1995. As your report suggests, we will not achieve an unqualified audit opinion on our financial statements until the Defense Finance and Accounting Service (DFAS) and the Air Force improve a large number of accounting systems and resolve other accounting related issues. Unfortunately, the systems issues will take a number of years to resolve. However, we feel we are making progress and will continue to do so in the future.

As you indicated in paragraph 6 of your opinion, the Air Force, DoD, and DFAS already have undertaken a number of management initiatives aimed at improving our financial data and statements. We are firmly committed to having auditable financial statements, and to improving our financial reporting. We will continue to work with AFAA, DFAS, and other groups to implement corrective actions as quickly as possible in order to bring about those improvements.

A handwritten signature in cursive script that reads "John W. Beach".

JOHN W. BEACH  
Principal Deputy Assistant Secretary  
of the Air Force (Financial Management)

Appendix B. AFAA Report, "Opinion on Fiscal Year 1995 Air Force Consolidated Financial Statements"

Project 95053001

Verbatim Management Comments



DEFENSE FINANCE AND ACCOUNTING SERVICE

1931 JEFFERSON DAVIS HIGHWAY  
ARLINGTON, VA 22240-5291

FEB 28 1996

DFAS-HQ/GC

MEMORANDUM FOR AUDITOR GENERAL, DEPARTMENT OF THE AIR FORCE

SUBJECT: Management Comments on Air Force Audit Agency (AFAA)  
Audit Report, "Opinion on Fiscal Year 1995 Air Force  
Consolidated Financial Statements"  
(Project No. 95053001)

We initially contemplated providing an interim response as we did to last year's report, however, we are providing our best effort and will provide additional comments where necessary on the final report. Attached are our detailed management comments to the subject report. In addition to our comments concerning the content of the report, we find it imperative that we also comment on the audit process. Specifically, our Denver Center was given only 3 days to respond to the draft report because of the Office of Management and Budget mandate for AFAA to publish the report by March 1, 1996. We believe issues of the magnitude described in the report deserve a more thoughtful and complete evaluation than can be afforded in 3 days. Also, as a result of the AFAA exit briefing with our Denver Center personnel, we were provided eleven revised pages of the draft report on February 26, 1996, the day our response was due to AFAA. Additionally, we have not received and reviewed all of the component audits which provide the detail to this audit opinion report.

My point of contact for this project is Mr. Charles McIntosh on DSN 327-5105 or (703) 607-5105.

*Thomas F. McCarty*  
for Thomas F. McCarty  
Deputy Director for General  
Accounting

Attachment

Appendix B. AFAA Report, "Opinion on Fiscal Year 1995 Air Force Consolidated Financial Statements"

Verbatim Management Comments

Project 95053001

SUBJECT: Management Comments on Air Force Audit Agency (AFAA) Audit Report, "Opinion on Fiscal Year 1995 Air Force Consolidated Financial Statements" (Project No. 95053001)

The following comments outline specific planned actions to eliminate as many repeat non-compliance issues as possible. Some of the planned actions involve the Air Force and must be coordinated with them. Due to the extremely short time frame we were given to respond to the draft report, we were unable to coordinate this response with the Air Force beforehand. Finally, we also explain our position for several issues in the subject report that we disagree with. It may be that the summarized presentation of some of the issues in the opinion report makes the issues appear different from the presentation in the individual reports. Conversely, we do not agree with some specific issues.

Planned actions: We are extremely concerned that the AFAA continues to disclose areas where DFAS-DE and Air Force personnel do not comply with existing policy or regulations. In some cases, they identified repeat conditions. Therefore, we plan to meet with the Air Force and discuss options for ensuring we comply with internal control requirements.

1. If the Air Force agrees, we will assign senior accountants to work with the functional areas that provide material balances on the financial statements in an attempt to ensure non-compliance deficiencies are not repeated in FY 96. For example:

a. We already made a proposal to the Air Force Space command that they rely on the Air Force Materiel Command (AFMC) to report capitalized satellite values. Doing so will eliminate duplicate reporting by both Space Command and AFMC.

b. Likewise, we will assist the Los Angeles Systems Program Office in developing and supporting satellite launch costs that should be capitalized by AFMC.

c. We will work with AFMC to develop procedures to fully disclose and accurately report excess and surplus property.

d. We are already working with AFMC to ensure we obtain accurate munitions year-end values for FY 96.

2. We will also task the accounting offices to report their status in correcting deficiencies identified in field-level reports relating to accounts receivables, accounts payable, expenses, and obligations. Furthermore, we will task the accounting offices to evaluate compliance in the foregoing areas as part of their embedded quality assurance programs and report

Appendix B. AFAA Report, "Opinion on Fiscal Year 1995 Air Force Consolidated Financial Statements"

**Project 95053001**

**Verbatim Management Comments**

the results to DFAS-DE. We will assist those areas who report they are unable to comply with regulatory requirements.

3. Finally, after we take action to correct a one time occurrence of a deficiency, we will follow-up to ensure the deficiency is actually corrected and is not repeated in FY 96.

Areas Where Summarized Issues Do Not Accurately Describe the Problem:

1. Many of the unreconciled differences identified by the AFAA are eventually resolved. We have also established procedures with the Air Force to obligate unmatched differences once we determine further research is unproductive. Furthermore, we believe that fund control data represent the most reliable source for financial statement account balances that we currently have. Moreover, the \$1.1 billion of differences represent 0.34 percent of total assets reported in the financial statements, an amount we believe is immaterial. Finally, we are developing a cash reporting system that will eventually eliminate the cause of all differences. The system is planned to be fully operational within 24 months.

2. We are concerned that the AFAA continues to state that the Air Force has not reported materially nonconforming accounting systems under the Federal Managers' Financial Integrity Act (FMFIA). Previously, the AFAA identified 31 systems they felt should be included in our inventory of FMFIA systems and evaluated under Section IV criteria. We were not given sufficient evidence to determine if we agreed and subsequently nonconcurred with the AFAA. As part of the mediation agreement with the AFAA and DoD Inspector General, DFAS-DE and the Air Force embarked on an effort to evaluate the 31 systems in questions. In addition, other systems were subsequently added to the evaluation process. A contractor determined whether the systems in question should be evaluated using Section 4 criteria and recommended who should own the systems. The contractor evaluated three of the four systems identified by the AFAA and concluded two were feeder systems falling under Section 2 criteria and one was a financial management system falling under Section 4 criteria. The contractor also recommended that all three systems should be owned by the Air Force. The contractor determination was not completed until after the FY 95 FMFIA report was prepared. The Air Force is now evaluating the systems against appropriate FMFIA criteria and should be capable of reporting their conformance during the FY 96 FMFIA process. Therefore, we do believe that the Air Force should have reported the systems under FMFIA Section 4 in FY 95.

3. We agree with the AFAA statement that, "The Air Force could not determine the correct amount of Air Force owned munitions to report to DFAS-DE. We reported the only amount provided to us by the Air Force. When we questioned why the

Appendix B. AFAA Report, "Opinion on Fiscal Year 1995 Air Force Consolidated Financial Statements"

Verbatim Management Comments

Project 95053001

FY 95 balance was dramatically lower than FY 94, we were told the Air Force was performing 100 percent inventories of the assets and this year's balance was more accurate. The AFAA did not establish which amount should have been reported. To preclude a repeat condition, we are working closely with the Air Force to ensure we obtain supportable end-of-year balances for FY 96.

4. The AFAA states DFAS-DE personnel made \$3.3 billion of adjustments without researching the basis for the adjustments. During FY 95, DFAS-DE deleted the requirement that accounting personnel research variances between amounts reported by the Air Force supply personnel on the Computation of On-Hand Investment Inventory Reconciliation List and amounts included in the general ledger. We removed the requirement because DFAS-DE personnel could not explain causes for the variances between supply and accounting records. We believe the AFAA statement that the operating materials and supplies line item on the Air Force financial statements were inaccurate because DFAS-DE personnel did not reconcile the differences tries to make a cause and effect relationship that is not supported by the facts. Since we reported the balances provided by the Air Force personnel responsible for managing the inventories, we believe the amounts were correct. If the AFAA determines the amounts reported to DFAS-DE were in error, we will adjust the statements accordingly.

5. We are attempting to review a report for Government Furnished Property (GFP) that was provided to us needing an almost immediate response. We believe the assertion that we under reported GFP by \$33.9 billion may not be entirely correct.

a. We do report Research Development Testing & Evaluation and supplies and equipment values as acknowledged by the AFAA. However, we do not use all contract purpose codes for the reasons that follow:

(1) The total amount of GFP identified by the AFAA includes amounts that should be reported in the Defense Business Operations Fund and Foreign Military Sales financial statements.

(2) The amounts reported by AFAA include values for satellites; aircraft; real property; maintenance, repairs, modification, or rebuilding; and, computer assets that we currently report using a variety of sources.

(3) The amounts reported by the AFAA include capitalized assets using a \$15,000 criteria versus the \$50,000 criteria we use for general funds assets.

b. We also do not agree with the cause for the problem identified by the AFAA. We are not supposed to have a separate system to record, track, and report GFP. According to the Defense Federal Acquisition Regulation Supplement, DFAS-DE and the Air Force are supposed to receive GFP values from the

Appendix B. AFAA Report, "Opinion on Fiscal Year 1995 Air Force Consolidated Financial Statements"

**Project 95053001**

**Verbatim Management Comments**

Defense Logistics Agency (DLA). We do in fact rely upon amounts reported by DLA for those balances we reported as GFP.

6. The AFAA stated "none of the 16 accounting offices reviewed promptly paid all Air Force debts as intended by the Prompt Pay Act." While we did not make all payments on time, our FY 95 Prompt Pay Act (PPA) statistics indicate we made over 95 percent of the payments subject to the PPA on time. We also disagree with the AFAA statement that the Air Force paid \$3.46 million in prompt pay interest because accounting personnel did not properly date stamp some invoices or understand the appropriate date for making payments. For example, factors other than paying office delays, e.g., lack of receiving reports being provided to accounting personnel, caused over 48 percent of PPA interest. Moreover, over 99 percent of the accounting office delays were caused by computer or other systems processing problems.

Areas of Disagreement:

1. We do not agree that unmatched recoupments of progress payments should be treated as recommended by the AFAA. The report infers that unmatched recoupments may be invalid but does not support the opinion with any hard evidence. Further, the AFAA states we may have significantly understated progress payments by offsetting them with unmatched recoupments. Again, the AFAA did not provide any evidence that progress payments were in fact understated on the financial statements. The fact that we recouped progress payments at the Air Force level means progress payments overall should be reduced. If the AFAA offers evidence that unmatched recoupments are invalid, we will adjust the financial statements accordingly.

2. We categorically disagree with the assertion that we did not properly analyze a \$6.9 billion decrease in munitions between FY 94 and FY 95. When we received the munitions end-of-year balance we questioned why it had decreased so much. The Air Force office providing the balance stated the FY 95 balance was more accurate because they were performing 100 percent inventories of the munitions. We had no basis to challenge the reasons given to us.

Project 95053001

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### ADDITIONAL AUDIT COMMENTS

1. These additional comments address the DFAS response to our opinion report. We must note that different decisions on the issues DFAS raised would not impact our disclaimer of opinion. The financial systems and associated internal controls remain inadequate and cannot produce reliable financial information.
2. We share DFAS concerns regarding the compressed timeframes. However, the 1 March deadline for producing audited financial statements is mandated by the Government Management Reform Act of 1994. We provided our draft opinion report to DFAS on 16 February 1996 and requested responses by 26 February 1996. These short suspenses were also due, in part, because DFAS did not provide financial statements for audit evaluation until 20 December 1995. We also recognize the limited time provided for analyzing the supporting reports. However, we repeatedly discussed our audit results with DFAS officials during the separate audits of specific accounts. Between 18 January and 23 February we briefed DFAS management on nine separate occasions regarding the results of our account balance audits. Furthermore, in the 23 February meeting we discussed all of the issues included in the opinion report with the DFAS-DE Director and his senior staff.
3. In some cases, the DFAS comments do not accurately portray our position. For example, we did not assert that the GFP balance is understated by \$33.9 billion. As stated in the report and emphasized during prior discussions with DFAS-DE, a \$33.9 billion variance exists between the amount reported in the financial statements and the amount contractors reported to the Defense Logistics Agency. DFAS also indicates they will adjust the statements when we prove that \$3.3 billion of unsupported adjustments are in error. We believe it is incumbent on management to properly research and support their adjustments. DFAS also questioned the propriety of reporting the \$1.1 billion in mismatches between disbursement and collection data. We believe \$1.1 billion of mismatches is significant but more importantly, the mismatches were only one of several problems we noted with fund control data to include over \$227 million of invalid, inadequately supported, and inaccurate accounts receivable, accounts payable, expenses, and obligations.
4. In summary, we appreciate the efforts DFAS and the Air Force have made to improve financial reporting. We will work with DFAS in addressing the issues included in their comments as we continue processing supporting reports covering specific accounts.

**Appendix B. AFAA Report, "Opinion on Fiscal Year 1995 Air Force Consolidated Financial Statements"**

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Project 95053001

**FINAL REPORT DISTRIBUTION**

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DFAS-DE	AMC
DFAS-HQ	ANGRC
NGB/CF	PACAF
	USAFA
Army Audit Agency	USAFE
AU Library	Units/Orgs Audited
DLSIE	
DoD Comptroller	
DoDIG-Library	
GAO	
GAO-Denver	
Naval Audit Service	
OAIG-AUD	
OAIG-P&O	
OAIG-AUD-FA	
OAIG-AUD-FC	
OAIG-AUD-FD	
OAIG-AUD-APTS	

**FREEDOM OF INFORMATION ACT**

The disclosure/denial authority prescribed in AFPD 65-3 will make all decisions relative to release of this report to the public.

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## Appendix C. Scope and Methodology

**Audit Work Performed.** To fulfill our responsibilities under the Chief Financial Officers Act of 1990, as amended by the Federal Financial Management Act of 1994, for determining the accuracy and completeness of the independent audit conducted by the AFAA, we evaluated the AFAA's qualifications and independence, reviewed the AFAA's audit approach, and monitored audit progress at key points.

**Evaluation of AFAA Qualifications and Independence.** Our determination of the AFAA's qualifications and independence was based on a lengthy and continuous association between the Inspector General (IG), DoD, and the AFAA. In addition, IG, DoD, Report No. APO 95-010, "Report on the Oversight Review of the Organization and Staffing of the DoD Audit Organizations for Audits of Financial Statements," dated July 19, 1995, concluded that the Military Department audit organizations have qualified and experienced staff and that the decision to use them in financial statement audits was wise.

We also relied on July 24, 1992, correspondence from the General Accounting Office, Assistant Comptroller General, Accounting and Financial Management Division, which raised no objections to the IG, DoD, using the work of the Defense audit agencies in discharging its responsibilities for the audits of the financial statements of the various Military Departments.

**Review of the AFAA Audit Approach.** We used the "Federal Financial Statement Audit Manual," issued by the President's Council on Integrity and Efficiency, as criteria for reviewing the AFAA audit approach. Specifically, we reviewed the following: the notification letter, opening conference documentation, strategy formulation, the entity profile, the general risk analysis, and audit programs. We reviewed additional planning documentation that we deemed necessary to accomplish the audit objective.

**Monitoring of Audit Progress at Key Points.** Through the IG, DoD, Integrated Audit Process Team and the Executive Steering Committee, we provided a forum for a centrally-managed exchange of guidance and information in conducting the audits of the FY 1995 Air Force consolidated financial statements. This will lead to a focused DoD-wide audit of the DoD consolidated financial statements, to include the supporting financial statements of the major DoD Components. The AFAA audit of the Air Force financial statements will constitute a significant portion of this DoD-wide audit effort. We also reviewed and commented on each AFAA draft audit report, including the audit opinion report, that was issued in relation to the audit of the FY 1995 Air Force consolidated financial statements.

## Appendix C. Scope and Methodology

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**Audit Period, Standards, and Locations.** We performed this financial audit from May 16, 1995, through March 15, 1996. The audit was made in accordance with auditing standards issued by the Comptroller General of the United States, as implemented by the IG, DoD. We did not use computer-processed data or statistical sampling procedures to conduct this audit. Appendix D lists the organizations we visited or contacted.

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## **Appendix D. Organizations Visited or Contacted**

### **Department of the Air Force**

Auditor General, Department of the Air Force, Washington, DC  
Assistant Auditor General, Operations, Arlington, VA  
Assistant Auditor General, Financial and Support Audits,  
March Air Force Base, CA

### **Other Defense Organizations**

Defense Finance and Accounting Service, Arlington, VA  
Defense Finance and Accounting Service Denver Center, Denver, CO

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## **Appendix E. Report Distribution**

### **Office of the Secretary of Defense**

Under Secretary of Defense (Acquisition and Technology)  
  Director, Defense Logistics Studies Information Exchange  
Under Secretary of Defense (Comptroller)  
  Deputy Chief Financial Officer  
  Director, Accounting Policy  
  Deputy Comptroller (Program/Budget)  
Assistant to the Secretary of Defense (Public Affairs)

### **Department of the Army**

Auditor General, Department of the Army

### **Department of the Navy**

Assistant Secretary of the Navy (Financial Management and Comptroller)  
Auditor General, Department of the Navy

### **Department of the Air Force**

Assistant Secretary of the Air Force (Financial Management and Comptroller)  
Auditor General, Department of the Air Force

### **Other Defense Organizations**

Director, Defense Contract Audit Agency  
Director, Defense Finance and Accounting Service  
Director, Defense Investigative Service  
Chief, Internal Review Group, Defense Logistics Agency  
Director, National Security Agency  
  Inspector General, National Security Agency

## Non-Defense Federal Organizations

Office of Management and Budget  
Technical Information Center, National Security and International Affairs Division,  
General Accounting Office  
Inspector General, Department of Education

Chairman and ranking minority member of each of the following congressional committees and subcommittees:

Senate Committee on Appropriations  
Senate Subcommittee on Defense, Committee on Appropriations  
Senate Committee on Armed Services  
Senate Committee on Governmental Affairs  
House Committee on Appropriations  
House Subcommittee on National Security, Committee on Appropriations  
House Committee on Government Reform and Oversight  
House Subcommittee on National Security, International Affairs, and Criminal  
Justice, Committee on Government Reform and Oversight  
House Committee on National Security

## **Audit Team Members**

This report was prepared by the Finance and Accounting Directorate, Office of the Assistant Inspector General for Auditing, DoD.

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