# United States Air Force

## Annual Financial Statement

2003

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SECRETARY OF THE AIR FORCE
WASHINGTON

January 2004

**Message from the Secretary of the Air Force**

Fiscal Year 2003 will live as a landmark success for the United States Air Force. Already answering the call to serve around the world and at home, the men and women of the Air Force again responded with professionalism and dedication to deliver decisive air and space power for our operations in Afghanistan and Iraq. It is with great pride that I note the Air Force met this challenge with unprecedented success while also securing our homeland in OPERATION NOBLE EAGLE and continuing our global fight against terrorism. As they have done time and time again, America's airmen proved they are the cornerstones of the most powerful and ready force in our service's storied history.

These successes and our support to our talented airmen required expert management of our financial resources. The Assistant Secretary for Financial Management has mobilized a forward-looking team focused on delivering sophisticated and timely support to our warfighters, from training and weapons systems to the welfare of Air Force families. The successes of Fiscal Year 2003 would not have been possible without our continuing innovation in all aspects of Air Force financial management. Just as our warfighters continue to hone their skills, we must continue to provide financial services and programs that are every bit as transformational as the warfighting concepts and systems they support. To do so, I encourage you to pay special attention to Air Force Financial Management Transformation efforts and our focus on performance-based management.

We are leading force-wide initiatives to leverage technology, best management practices, and the good ideas of Air Force people to constantly improve our support of all Air Force operations. Our efforts will be Chief Financial Officer (CFO) Act compliant, and this statement fulfills the requirements of the CFO Act. The statement documents the expenditures devoted to our General Fund and Working Capital Fund activities.

We are committed to expert leadership, management, and accountability in our finances as a fundamental part of providing for the world's preeminent air and space power. Air Force people and the people of the United States of America deserve nothing less.

DEPARTMENT OF THE AIR FORCE
WASHINGTON DC
OFFICE OF THE ASSISTANT SECRETARY

January 2004

**Message from the**
**Assistant Secretary of the Air Force,**
**Financial Management and Comptroller**

Even considering the impressive accomplishments of the recent past, this year has been extraordinary. Our Air Force financial management team across the enterprise supported OPERATION IRAQI FREEDOM with innovative and timely financial services to our warfighters. Just as our airmen fighting abroad and protecting at home found new and better ways to accomplish their demanding missions, we did also and provided them with the world-class financial support they deserve.

An important key to this has been the work of our Transformation Program Management Office and the extended transformation efforts across the Air Force. What was until the beginning of FY 2003 a nascent idea has proven to be profoundly valuable. Gaining the insight of everyone from combat pilots to depot maintenance personnel, we have successfully institutionalized a process of continuous improvement. To name but a few examples, we have improved web-based services for better support to deployed airmen at lower cost, we are delivering more sophisticated financial management decision support services, and we are reducing our procurement cycle times and more closely linking acquisition decisions with warfighter requirements. You will read about even more examples in this report. In sum, we are making considerable progress by listening to our customers, leveraging technology, and reducing costs.

We are off to a great start—but it is just the start. We are determined to continue the process of transformation not only to enhance but also to revolutionize the way we do business. This involves a completely different approach to decision-making, from defining our requirements to shaping our work force. The dynamic threat environment we face today demands we deliver fast, flexible, agile, and sophisticated financial services using people, processes, and systems that are integrated and capability-focused.

This statement provides both broad summaries and financial specifics of our efforts in FY 2003, fulfills the requirements of the Chief Financial Officer (CFO) Act, and documents the expenditures devoted to our General Fund and Working Capital Fund activities. It also briefly reviews selected performance measures established as part of the Government Performance and Results Act.

We are justly proud of Air Force men and women serving around the world. We must continue to match their transformation in warfighting and technology with a transformation in financial management and business practices. Synchronizing these revolutions is vital to the Air Force and to the United States of America.

*Financing the Fight*

# General Funds Overview

## Air Force in Action

As America and the world celebrate the 100th anniversary of powered flight, a sense of amazement comes to all who consider the tremendous advances and innovations represented by this anniversary. In no sphere is this amazement more justified, in no arena has the promise of Kitty Hawk been more fulfilled, than in the transformation and operations of the U.S. Air Force in FY 2003. The past year has seen the Air Force continue the war on terrorism, remain a vital part of homeland defense efforts and guarantee the welfare of airmen—responding with dedication and professionalism to serious and looming threats to American security.

Operation IRAQI FREEDOM (OIF) opened with the "shock and awe" of American air power, and throughout OIF the Air Force has been both spear and shield, working in complete concert with joint forces to first sweep a brutal tyrant from the scene, then to work to secure a ravaged land. From the power of B-2 precision weapons to the mobility of a C-17 airdrop of an airborne brigade, from global communications and intelligence to heroic efforts to quickly establish forward bases, OIF illustrates the integration of Air Force people and technology to achieve historically unprecedented air and space capabilities.

Even as these Air Force capabilities were employed in Iraq, so did they continue and expand in other key areas. Ongoing Operation ENDURING FREEDOM efforts as part of the global war on terrorism continued in Afghanistan with missions across the spectrum, from combat operations to humanitarian support, illustrating Air Force abilities to access and succeed in one of the most remote areas of the world. Operation NOBLE EAGLE continued as the Air Force rose to protect the homeland with reassuring power and surveillance over key areas of America.

Success in these and many other operations around the world proved repeatedly the vital role of the Air Force in the defense of America. In sustaining this irreplaceable role, the training and development of professional airmen, the cultivation of key technologies for warfighter employment, and the integration of all into operational capability conclusively bore out the value of continued and expanded Air Force Transformation.

> *"For those who have gone before us, who have given their lives so that we could have the greatest Air Force on Earth, so that we could enjoy the wonders of freedom and liberty, we pledge our best."*
>
> **General John Jumper, USAF**
> **Chief of Staff**

Some of the current real threats to American security had been imagined in the recent past, but many were new and unimagined. The Air Force must and is adapting to this new world by recognizing a broader spectrum of conflict, new categories of extant and potential enemies and the importance of forward-looking thinking and planning. Air Force Transformation efforts are aimed at moving ahead to ensure evermore dynamic, versatile and adaptable air and space power with the capability and agility to decisively face and defeat future threats to America.

In FY 2003, the Air Force left no doubt as to its status as the world's—indeed, history's—preeminent air and space power. Regardless of weather, darkness, distance, season or foe, the Air Force delivered peril to enemies and assurance to friends. Americans, dealing with the maelstrom of a changing world, can rest both at home and abroad, secure in the knowledge that there is protection above.

## Air Force Organizations

In FY 2003, Air Force active duty members, Air National Guardsmen, Reservists and civilians responded to unprecedented challenges with unprecedented performance. Calling upon the Air Force Core Values of "Integrity First—Service Before Self—Excellence In All That We Do," Air Force people proved time and time again, around the world, that they comprise the world's preeminent air and space power.

The integrated components of the Air and Space Expeditionary Force were involved in operations ranging from major theater war to homeland security to humanitarian relief. Air Force people and organizations did this with effectiveness and efficiency heretofore unseen in air and space operations—all while constantly preparing to face the challenges of the future.

### Major Commands, Direct Reporting Units and Field Operating Agencies

#### Major Commands

The Air Force is organizationally aligned into 10 Major Commands (MAJCOMs, including the Air Force Reserve and the Air National Guard). A MAJCOM represents a subdivision of the Air Force assigned one or more elements of the Air Force mission, and is subordinate to Headquarters Air Force (HAF). Bases and installations fall under MAJCOMs.

#### Direct Reporting Units

Direct Reporting Units (DRUs) are single-mission organizations that report directly to HAF.

#### Field Operating Agencies

Field Operating Agencies (FOAs) execute responsibilities under the organizational aegis of a functional manager at HAF.

## Fiscal Year 2003 Results

### Budget by Appropriation Categories

Six major appropriation categories comprised the Air Force FY 2003 budget, as follows:

- Operations and Maintenance (O&M): Pays the salaries and benefits of civilian employees and other day-to-day operating costs (e.g., fuel, spare parts).
- Military Personnel (MILPERS): Finances the salaries and benefits of uniformed personnel.
- Procurement (PROC): Funds Air Force investment in major systems.
- Research, Development, Test, and Evaluation (RDT&E): Funds system development.
- Military Construction (MILCON): Pays for facilities construction.
- Military Family Housing (MFH): Provides for the operation, maintenance and construction of housing units.

# Performance Measures

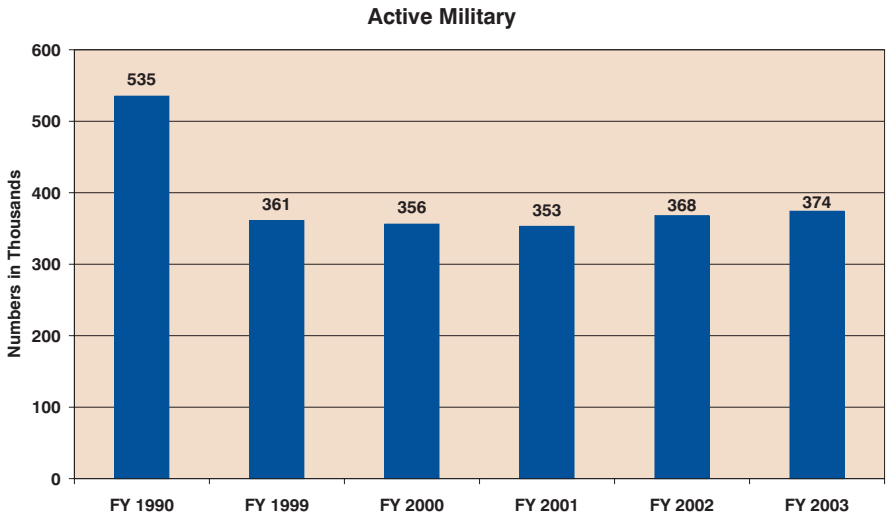
## Quality People

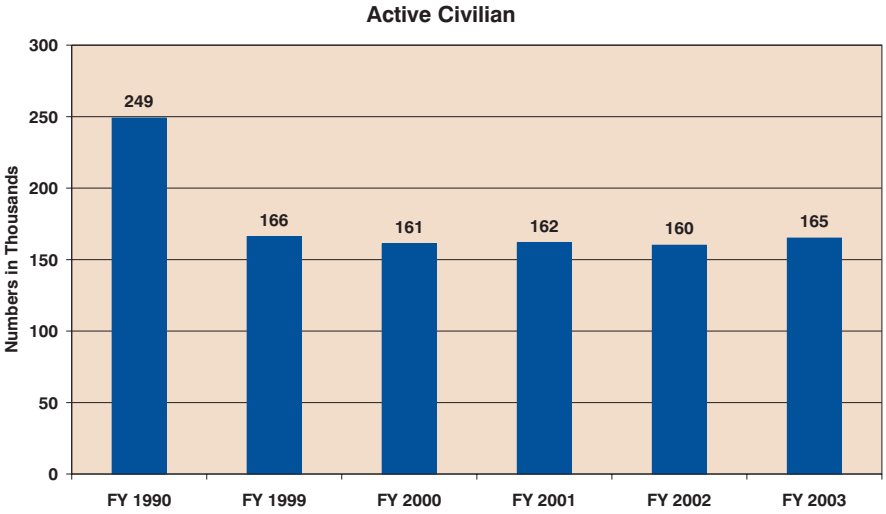
The Air Force's most important resource is its people. It is Air Force airmen, whether they are civilian, enlisted, or officer, who fight and win America's air wars and guarantee air and space dominance. They must be determined, mission-focused, and fully energized. The Air Force relies on a highly skilled, educated, and technologically superior force to function as an effective warfighting team.

Increasing demands for U.S. military presence around the globe, whether participating in the Global War on Terrorism, or contributing to the war effort in Iraq, continue to increase Air Force operations tempo. Despite these demands, Air Force members proudly serve their country and senior Air Force leaders value their service and readily undertake the obligation to care for them and their families.

The Active Military chart shows a leveling trend over the last 4 years, although active strength has declined approximately 31 percent from 1990 levels.

The Active Civilian chart shows that civilian population trends in the active Air Force have declined by more than 30 percent since FY 1990. Due to personnel drawdowns of the past decade, new hires have been limited. Moreover, many experienced employees have moved on to other jobs or have taken advantage of early retirement options. As a result, 42 percent of Air Force civilian personnel will be eligible to retire in the next 5 years. The Air Force is taking necessary steps to reshape the civilian force to ensure future availability of sufficient and experienced personnel with the requisite skills to fill the positions.



The reserve component, consisting of the Air Force Reserve and the Air National Guard, is an integral part of the Total Force. These personnel are integrated into all mission areas and nearly half of the mission-oriented squadrons in the total Air Force are in the reserve components. A majority of the Air Force's vital air refueling capability is in the Air National Guard and Air Force Reserve.

For all personnel, the Air Force ranks quality of life (QoL) as one of its top priorities. Air Force QoL initiatives acknowledge the intense demands placed on the mission-focused total force. The Air Force has and will, with the continued support of Congress, pursue adequate manpower; improve workplace environments; seek fair and competitive compensation and benefits; balance deployments and exercise schedules; provide safe, affordable, and adequate housing; enhance community and family programs; improve educational opportunities; and provide quality health care. Efforts to compensate the Air Force total force continued with the FY03 National Defense Authorization Act (NDAA). As a result, key legislation directly impacting total force pay and compensation, travel and transportation entitlements, and retirement and education programs were authorized and implemented over FY 2003.

Enhancing community and family programs is a crucial link between members, families and leadership creating the necessary support to encourage retention. In 2001, the Air Force began taking a more collaborative approach to community and family service delivery by creating Community Action Information Boards (CAIB) and Integrated Delivery System (IDS) working groups at the Air Staff, MAJCOM, and Installation levels. The CAIB brings together senior leaders to identify and resolve individual issues that impact the readiness of Air Force members and their families, promote the Air Force as a positive way of life, and enhance members' and families' ability to function as productive members of the Air Force community. The emphasis is on positive actions and programs that strengthen force readiness through a sense of community and assist Air Force members and civilians, their families and communities to thrive and successfully manage the demands of military life. Established as the action arm of the CAIB, the IDS working group brings together all community and family agencies to ensure our military members and their families have access to the services and activities they need. Additionally, Family Support Centers continue to meet individual and family needs by distributing information concerning all aspects of Air Force life and through AF Crossroads, the official family and community website for the Air Force.

## Recruiting

In FY 2003, the Air Force was slightly over end-strength requirements. The Air Force exceeded its FY 2003 recruiting goal of 37,000, sending 37,144 people to basic training. Further, the Air Force enters FY 2004 with a solid Delayed Entry Program under which 43% of the FY 2004 accession needs are already under contract and scheduled to enter active duty during the next year.

The Air Force exceeded its FY 2003 recruiting goal not by lowering standards, but by intensifying efforts to promote the benefits of the Air Force. This success, in the face of stiff competition from the private sector and an increased propensity to pursue civilian college opportunities, is the result of hard work and well-orchestrated approaches. Such success reflects a combination of measures—more recruiters on the street, a focused television advertising campaign, and higher enlistment bonuses. These are all important tools to maintaining a high-quality force, and the Air Force will continue to make recruiting a top priority.

In support of its recruiting mission, the Air Force:

- Increased the number of production recruiters from 1,085 at the beginning of FY 1999 to 1,610 by the end of FY 2003.
- Instituted an aggressive advertising campaign to include a full year of national television advertising.
- Kept pace in cyberspace, modernizing the innovative USAF web site to promote a better understanding of the Air Force overall, effectively reaching the Internet generation.

The need to recruit qualified men and women, both military and civilian, to serve in the Air Force remains as important today as it was when the service was established. A service population reflective of the strengths of a diverse America will provide the necessary new talent required for today's unique challenges. As the Air Force succeeds in sending its message to young people across the nation, the nation can be confident in a positive, high-quality response. For instance, more than 99% of those enlisting are high school graduates.

## Education and Training

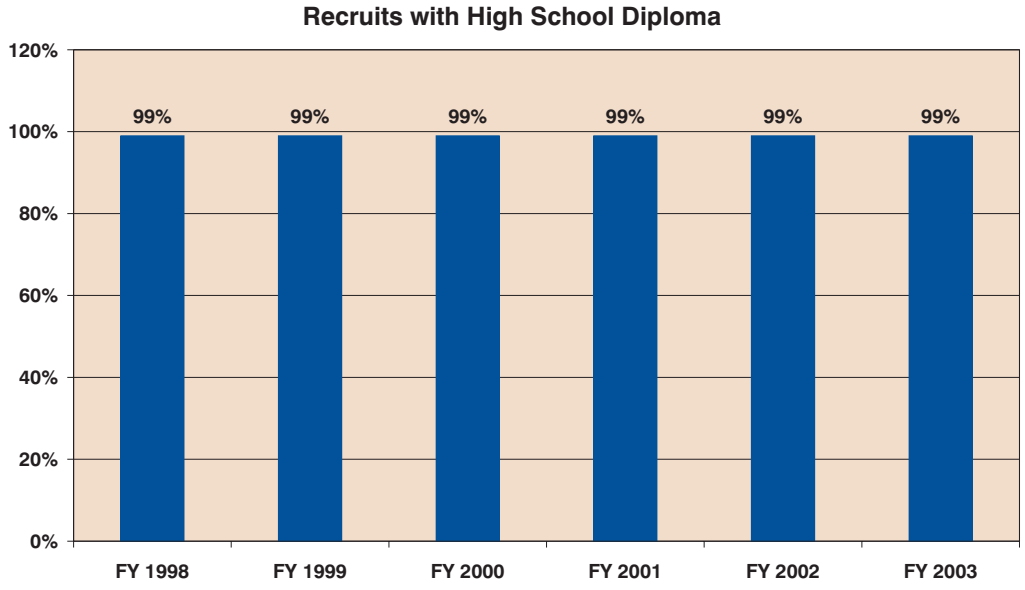
Recruiting good people into the Air Force is just the beginning. They need training to perform highly technical work—the basis of the Air Force's record of military success. The Air Force continues to offer professional military education (PME) programs that span the careers of all members. From Airman Leadership School to the Air War College, PME provides opportunities to all Air Force personnel, granting them the skills and knowledge they need to manage Air Force resources and to operate weapons systems.

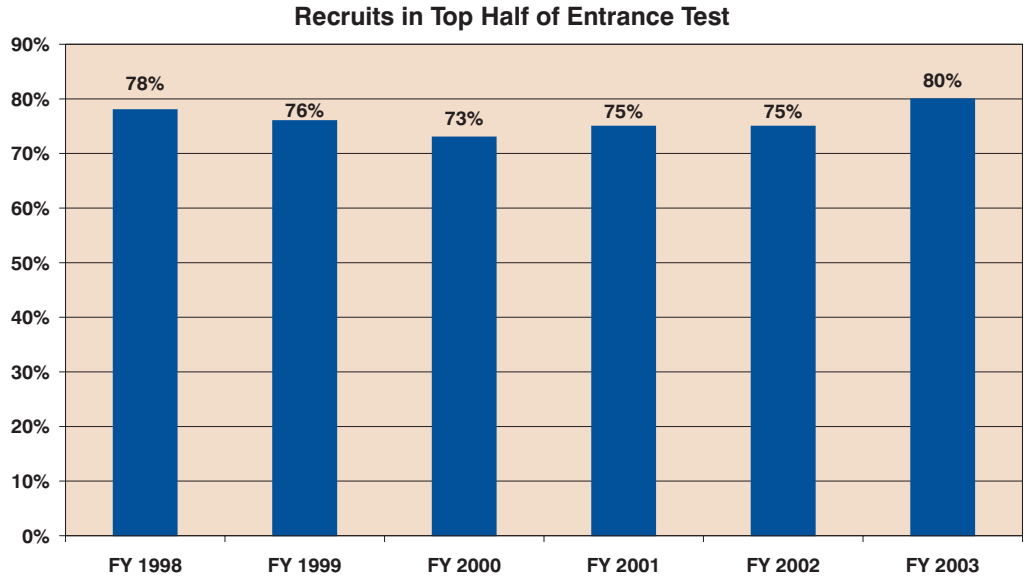
The newest PME course, the Air and Space Basic Course (ASBC) offered at Maxwell Air Force Base, Alabama, is designed to meet the needs of newly commissioned officers and selected civilian interns. At the direction of Air Force leadership, the ASBC and USAF Senior NCO Academy launched an historic Combined Ops Initiative, leveraging officer and enlisted PME in providing an order of magnitude improvement in followership, leadership, and mentoring. The week-long merger brings lieutenants and senior NCOs together in joint classroom discussions, wargaming laboratory, and field exercises. A post-graduation survey of junior grade officer and senior NCO students showed an appreciation of valuable lessons learned, improved understanding of respective roles, increased need for effective communication skills, and an emphasis on support for professional relationships.

Technical training courses are also a vital part of Air Force training, instructing new and retraining airmen on the fundamentals of their new career areas and the detailed tasks they will face. For example, the 51-day Security Forces Apprentice course teaches airmen all aspects of their multi-faceted career field missions—missions they will perform around the globe. In addition, the Community College of the Air Force (CCAF) offers numerous courses leading to an Associates degree and had awarded 243,899 degrees at the close of FY 2003.

In FY 2003, in a groundbreaking education initiative, 11 Air Force enlisted members were admitted to the Air Force Institute of Technology (AFIT) in highly technical areas in pursuit of a master's degree. Given the greater emphasis on a more technical Air Force, enlisted members will share in the responsibility to "meet the challenge" in the immediate years ahead by studying at a preeminent institution.

A new officer education development program was developed to better educate officers based on specific career phases and Air Force needs. The model will permit short modular course completion, specific technical training needs, and PME at sequenced points "just in time" for individual and Air Force requirements. This model incorporates best business practices in using resources when and where needed.



## Retention

Enlisted retention rates were uncharacteristically high in FY 2002 due to Stop Loss. As such, the Air Force expects to meet two of the goals ending FY 2003 with a 61% reenlistment rate for first-term personnel, 73% for second-term personnel and 95% for career airmen.

To help retain critical skills, in Apr 02 the Air Force completed its initial re-recruiting program. The program concentrated on development engineers entering critical decision points. The Air Force is seeking to institutionalize the re-recruiting program as a retention initiative and expand it to other critical Air Force specialties. In FY 2003, the Air Force announced the Critical Skill Retention Bonus (CSRB) program for five designated critical officer skills. Payment of CSRB is viewed as an important retention tool for these career fields—all of which have been facing the lowest retention rates in the Air Force for several years.

The Air Force Reserve met its end strength goal of 100 percent.

## Rated Retention

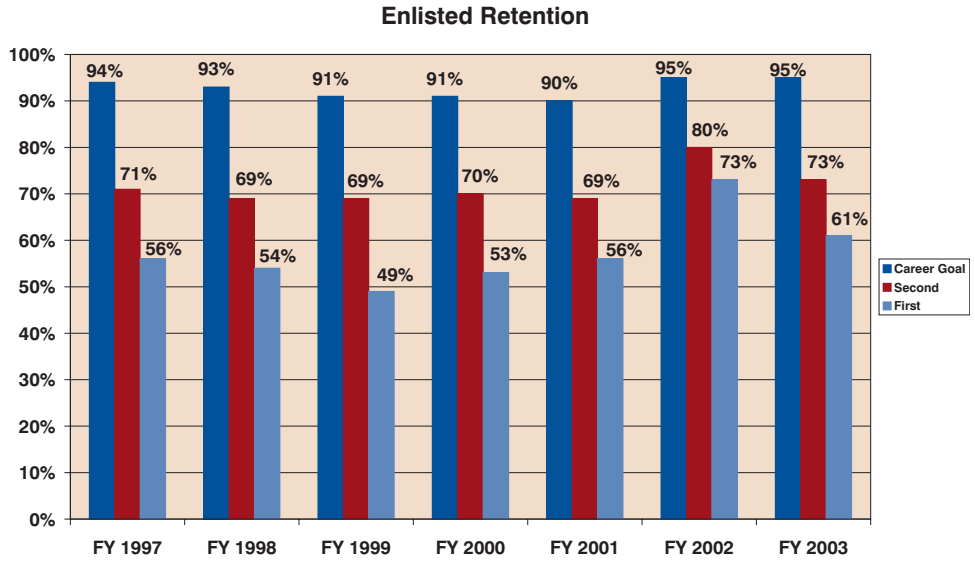
A special subset of the retention challenge is maintaining the health of the rated force in order to preserve the warfighting capability of the Air Force. The Air Force boasts the world's most efficient and talented support force, combined with technologically superior, integrated air and space systems. However, retention of skilled pilots, navigators, and Air Battle Managers (ABMs) remains crucial to accomplishing operational missions. Further, at a cost of several million dollars to train and season, a veteran pilot is the Air Force's most expensive personnel asset. Prior to September 11, 2001, a strong economy and unprecedented airline hiring, along with continued high operations tempo, contributed by the end of FY 2001 to a shortage of approximately 1,200 pilots—9% of the requirement. In FY 2002 the pilot shortfall dropped to approximately 600 pilots, or 5% of the requirement. By the end of FY 2003, the pilot shortfall is approximately 400 pilots, or 3% of the requirement. This short-term increase is attributable to the short-term decline in airline pilot hiring combined with the positive retention effects of Air Force initiatives such as Aviator Continuation Pay (ACP) in addition to the Permanent Rated Recall and Rated Retired Recall programs. In FY 2003 the pilot long-term bonus "take

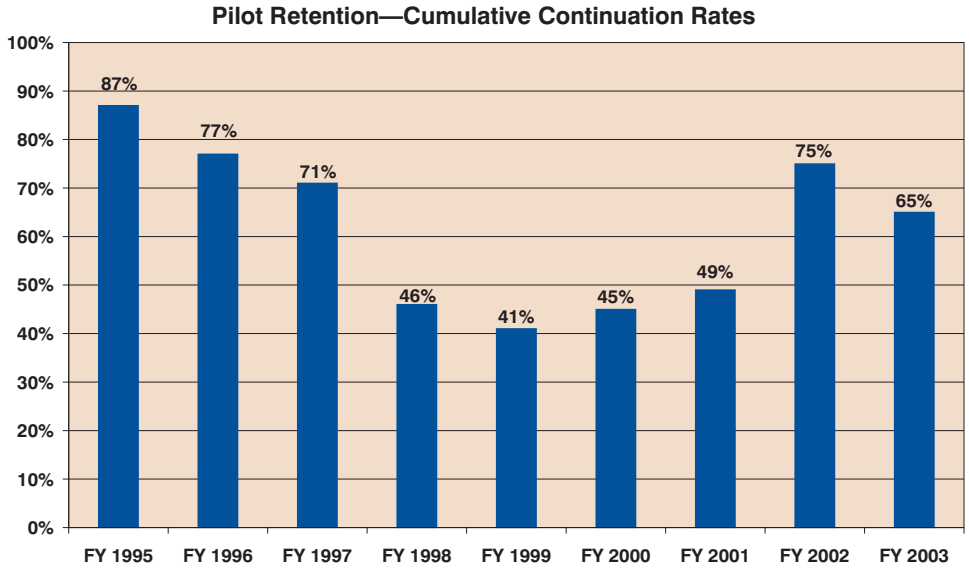
rate" (our best indicator of pilot retention trends) was approximately 61%. This is an increase from a 47% "take rate" during FY 2002. The total "take rate" for initially eligible pilots was also up for FY 2003 at 67% compared to 58% in FY 2002. However, because there are fewer initially eligible pilots in this year group (due to production in the mid-1990s) significant retention challenges remain. In fact, Air Force inventory forecasts estimate pilot shortfalls of 600-900 pilots through FY 2010. While airline hiring by the major airlines has shrunk in the short term following September 11th (from 4,000 new hires in FY 2001 to approximately 600 in FY 2003), two important points need to be considered: 1) that during lean economic times the airlines tend to hire a higher percentage of former military pilots (up to 75%) and 2) that the long range forecast of airline hiring shows significant increases in the coming years, due to a variety of factors, not the least of which is a significant airline pilot retirement bubble beginning

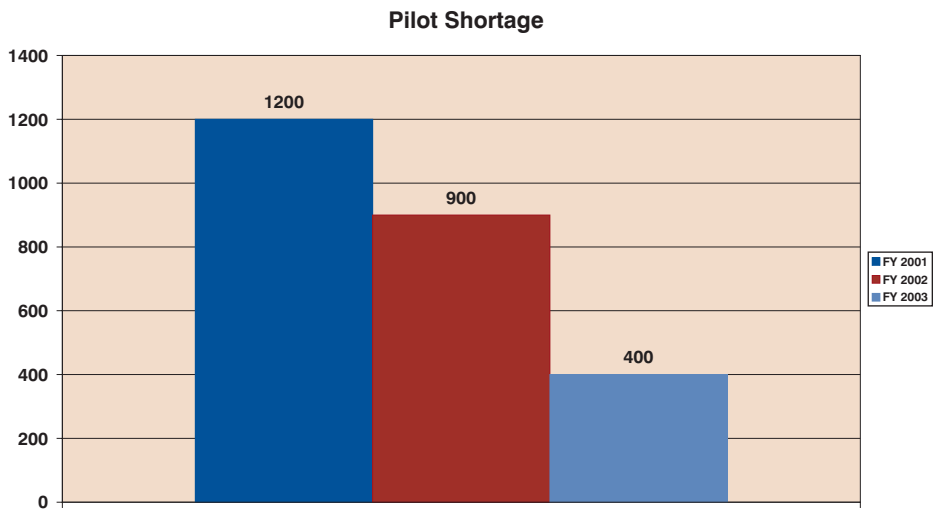
in 2005. As such, pilot retention will continue to be a significant issue for the long-term health of Air Force warfighting capability.

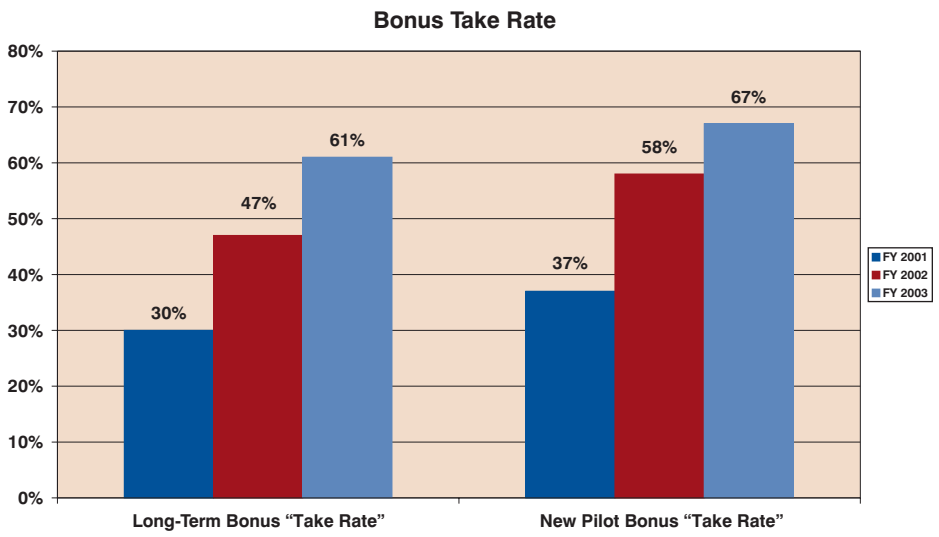
Until the bonus was offered, 30% of the navigator force was retirement eligible in the following two years and nearly half could have retired within 4 years. At mid-FY 2003, half of those navigators accepted bonus agreements cutting the retirement eligible pool by 50%. The bonus influenced navigators to stay in the service longer and provided relief for HQ staff pilot shortfalls (HQ level staff manning raised overall to 76% while pilot rated staff positions were manned at 58%). ABM shortfalls were no less acute as ABM inventory was estimated to be approximately 11% short of requirements at a time during which the demand for their expertise at home and abroad was greatest. ABMs are a resource critical to Air Force warfighting capabilities as they operate in low-density/high demand missions and aircraft (AWACS, JSTARS, and GTACS). The ABM bonus has been a great success with an aggressive "take rate" of approximately 75% for FY 2003. As a result, initial indications are that the ABM ACP has accelerated ABM inventory wellness by three full years.

Overall, the Air Force's integrated focus on retention initiatives will continue to emphasize long-term rather than short-term retention. Initiative options include: increasing active duty service commitments, increasing compensation, managing operations tempo, and enhancing quality of life programs.






## Operational Performance

### Air Force Flying Hour Program

The Air Force flying hour program was developed to provide training opportunities to prepare units to support their mission to the warfighting commanders. The execution of the President's Budget (PB) flying hour program is impacted by contingency operation support, maintenance issues, fact-of-life impacts, aircraft flight operations suspensions, aircraft delivery delays, weapon system retirements and approved program changes. Though the execution of the flying hour program does not define unit readiness, it can be a forward indicator of possible readiness issues. The MAJCOMs determine the reasons for execution deviations to required courses of action may be determined. Additionally, these evaluations provide insight into possible future-year requirements.

FY 2003 flying hour program execution significantly increased compared to the FY 2003 PB, particularly in the fighters, bombers and tankers, to an overall execution rate of 101.9%. The execution was impacted by the support of contingencies—OPERATION ENDURING FREEDOM and OPERATION IRAQI FREEDOM.

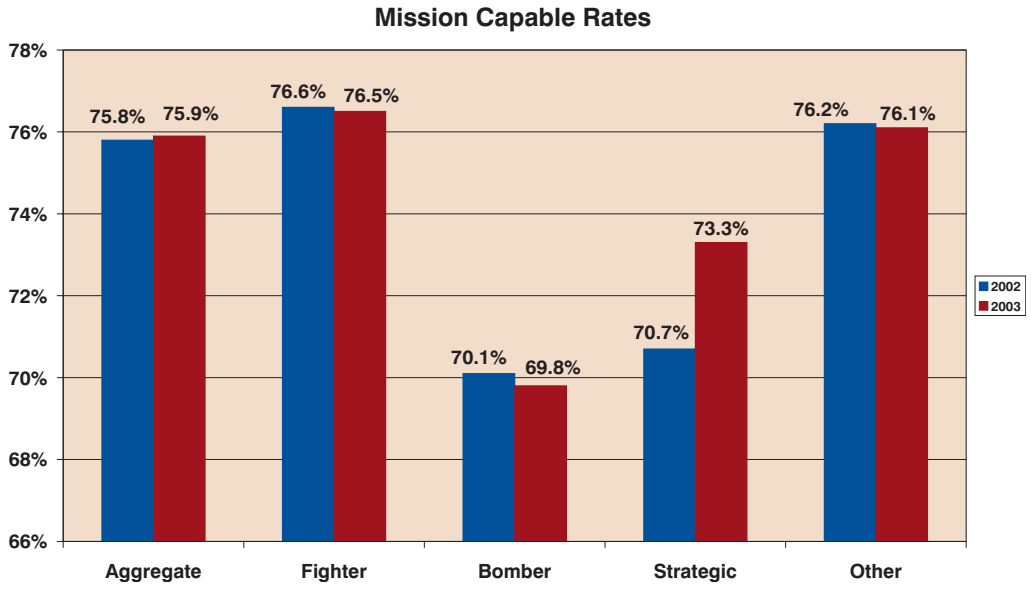
Flying hour program execution includes active Air Force Congressionally-funded O&M hours. They do not include incrementally funded contingency support hours, Transportation Working Capital Fund hours, foreign national reimbursable training hours, Special Operations hours and RDT&E hours.

## Weapon System Performance

The Air Force uses a variety of metrics to gauge the performance of its weapon systems and organizations. They are barometers for measuring the effectiveness of organizational structures, training, manpower and equipment levels, quality of spare parts, maintenance actions, and a variety of other indicators of the Air Force's ability to provide mission-ready weapon systems to the warfighter. Chief among these performance metrics are Mission Capable rates, Non-Mission Capable rates, Cannibalization rates, and engine and supply measures.

### Mission Capable Rates

Mission Capable (MC) rates are perhaps the best-known yardstick for measuring the readiness of Air Force aircraft. MC rates reflect the percentage of aircraft, by fleet that is capable of performing at least one of their assigned missions. The FY 2003 aggregate MC rate of 75.9% is a slight improvement over the FY 2002 rate, and is based on a combined MC rate of A/O-10, B-1, B-2, B-52, C-141, C-5, C-17, E-3, F-15, F-15E, F-16, F-117, HC-130, KC-10, KC-135, HH-60, RQ-1, and U-2 aircraft. MC rates categorized into Fighter, Bomber, Strategic, and Other are drawn from the aggregate fleet above. The FY 2003 MC rates for Fighters, Bombers and Other categories showed a slight drop from FY 2002 rates, while the Strategic fleet saw a 4% increase in MC rates.




### Non-Mission Capable Rates

Total Non-Mission Capable for Maintenance (TNMCM) is a measure of a maintenance organization's ability to fix aircraft quickly and accurately and Total Non-Mission Capable for Supply (TNMCS) measures spare parts availability. The FY 2003 aggregate fleet TNMCM rate remains unchanged at 19.3%, the lowest rate since FY 1997. TNMCS rates for the same period decreased from 11.7% to 10.7%, representing a 9% improvement in delivering critical aircraft parts.

### Other Key Metrics

Cannibalization (CANN) rates reflect the number of cannibalization actions that occur per 100 sorties for a particular weapon system. The aggregate CANN rate for FY 2003 dropped 15% from the FY 02 rate of 9.4 actions per 100 sorties. The FY 2003 rate of 8.8 CANNs per 100 sorties represents the lowest CANN rate since FY 95. Engine Not-Mission Capable-Supply (ENMCS) rate for Air Force engines dropped from 13.2% to 10.1%, a remarkable 23% improvement. Major improvements were seen in engines powering F-15, F-16, F-117, C-17 and A-10 aircraft. Improving

War Readiness Engine (WRE) numbers complemented the improved ENMCS rates as the number of WRE engines increased despite the high wartime operational tempo. The same engines that drove improvements in ENMCS rates were responsible for an increase of 97 WRE engines above FY 2002 levels. Investments in engine modifications, spare parts, and reliability-centered maintenance continued to pay "quality" dividends throughout FY03. Engines powering the B-1, B-52, F-15, F-16, and B-2 reached record setting on-wing operating times.

Aircraft MC rates are but one indicator of enhanced weapon system readiness. Measuring the efficiency of our depot program is equally important to increasing the availability of aircraft to operational units. While programmed depot maintenance and fleet modernization activities are critical to maintaining mission-ready aircraft, the Air Force strives to make continual improvements in business practices designed to increase the availability of aircraft to operational units. Evidence of the success of those efforts is the fact that the number of aircraft in depot fell in FY 03 to 452 compared with the FY 2000 high of 557. For example, the number of KC-135s in depot fell to less than 90 aircraft in FY 03, down from 176 aircraft in FY 2000. Aircraft that are not in depot are on the flight line supporting operational missions.

Air Force weapon system performance measures for FY 2003 provide a snap-shot of the efforts of the logistics community to support and provide combat-capable forces that are organized, trained and equipped to provide efficient and effective combat and combat support efforts across the full spectrum of military operations.

## Financing the Fight

The Air Force business transformation vision for the future is a single, capability-focused enterprise, with the common goal of serving the warfighter's needs and one that closes the seams dividing our capabilities today.

## Financial Management Transformation

Air Force Financial Management is continuing to make strides toward its vision of being strategic partners with Air Force commanders and decision-makers. In 2003, the first phase of transformation initiatives were put into motion with the establishment of 14 transformation teams and participation across the Financial

Management community. Additionally, initiative task forces represent nearly every MAJCOM and a broad cross-section of our Air Force installations. The establishment of the Financial Management Transformation Program Management Office (SAF/FMT) provided assistance in linking the overall Financial Management Strategy to the initiative task force teams and the MAJCOMs. This office also played a key role in leading the development of the Air Force Financial Management Strategic Plan (the Strategic Plan) for 2003-2008. The purpose of the Strategic Plan is to provide a roadmap that translates the lofty aspirations of the vision into concrete, actionable, and measurable steps. It communicates priorities, focuses our effort, and serves as a filter to help where to invest our time.

The President's Management Agenda (PMA), August 2001, provides the broad government-wide framework from which the Strategic Plan flows. The PMA identifies five broad initiatives:

- Strategic management of human capital
- Competitive sourcing
- Improved financial government
- Expanded electronic government
- Budget and performance integration

The Strategic Plan flows the PMA initiatives into a series of 17 strategic objectives, each of which corresponds to three themes—Air Force financial management's top priorities:

- **Warfighter Support:** Centered on developing an expeditionary-focused FM workforce (military and

civilian) trained and prepared to support deployed commanders and members.

- **Strategic Resourcing and Cost Management:** Maximizing resource effectiveness and cost efficiency by linking systems and resourcing strategies to measurable performance.
- **Information Integration and Reliability:** Providing relevant, timely, accurate and reliable financial information that supports decision-making.

Within these themes, each initiative will be evaluated from the perspective of the mission, the customer, internal processes and our people. Following are the major initiatives that are being undertaken in an effort to reach our vision.

## Establishment of the Information Technology Directorate

The Air Force has recognized the need for a single source of data, standardization, and governance across functional communities. To that end, during FY 2003, SAF/FM championed the organization of the Financial Management Information Systems & Technology Directorate (SAF/FMPT).

SAF/FMPT has laid out four primary goals which include developing a financial management enterprise architecture, establishing a single authoritative source of data, fielding a commercial-off-the-shelf (COTS) product for accounting and finance and lastly, to develop a new budget formulation system for the Air Force. Additionally, a new information technology (IT) portfolio management process for accounting and finance as well as budgeting systems will be implemented to help reduce the amount of duplicative and stand alone financial management systems throughout the Air Force.

The budget/financial execution systems effort is based at Maxwell AFB, AL, Gunter Annex, while the accounting and financial management portfolio is managed out of Wright-Patterson AFB, OH. The guidance provided by FMPT will assist in transitioning the Financial Management community toward a single authoritative source of data, which can provide leadership with critical decision support information.

## Establishment of a Workforce Management Office

The goals set forth in the April 2002 Air Force Financial Management Vision Statement provided the genesis for the requirement to ensure the effective and efficient management of the Financial Management workforce. In FY 2003 the Workforce Management Directorate (SAF/FMPW) was established with the mission to serve and support our Air Force financial management workforce and organizations to optimally achieve Air Force needs. In order to support this mission, FMPW has partnered with internal FM offices and our Air Force Personnel community to set forth revised Force Development Programs. Additionally, significant accomplishments have been achieved toward ensuring that education, training and development of the workforce are aligned with the SAF/FM vision statement.

## Air Force Customer Service Concept—Military Pay

Air Force personnel are our most important resource and the Air Force must make every effort to provide outstanding customer service in our Personnel and Financial Services Offices. The initiative is a three-phased approach to provide "one-stop shopping" for customer services, delivering service to customers anytime, anywhere through use of the worldwide web and interactive voice response technology. Taking advantage of available technology, services will be provided using the web via the AF Portal, contact centers under a single 800 number and a front-line cadre of customer service providers. The consolidation of myPay and the Air Force Personnel Center's virtual MPF and virtual CPF under the AF Portal is a major step toward improving service to the customer. A key enabler for the initiative is to ensure all members have access to web-based applications; self-service kiosks strategically deployed throughout an installation are one method of ensuring easy access to payroll and personnel applications. Additionally, migration from paper-based process-

es to electronic processes will further streamline customer service operations.

### Vendor/Commercial Pay Concept

The current process for vendor payment is complex and fragmented, with multiple stakeholders, and relies heavily on manual transaction processing. Contractual payments require the requesting activity to submit a purchase request, the contracting function to award the contract, the vendor to fill the order and submit an invoice, the requesting activity to receive and accept the goods, and the paying office to make payment on the invoice. The excessive billing costs are primarily attributable to manual processing. During 2003, the Vendor/Commercial Pay task force began introducing widespread eCommerce to the Air Force using the Wide Area Workflow system that was piloted in the Pacific theater and in Air Education and Training Command. Using this system, the Air Force, DFAS and vendors will submit and receive the vast majority of transactions associated with bidding on a contract, billing for the goods or services, verifying receipt, and payment via the internet. This process will save countless manhours and greatly reduce transaction errors, which have in the past accounted for a substantial portion of the lost discounts and interest penalty payments.

### Reengineer Wing/Unit Level Decision Support

The wing and unit level Financial Analysis offices are the building blocks for Air Force budgets. All too often these offices have spent an inordinate amount of time in bookkeeping, enforcement of budget rules, preparing budget documents and briefing staff members. While each of these activities is important, the higher value to the Air Force is the analysis and decision support they provide to their commanders and senior leaders. In phase one of this initiative, the task force is providing a tool to all Air Force bases to speed the loading of budget targets in the accounting system. This is expected to permit over 15,000 manhours, presently used for clerical work, to be diverted to the analytical efforts our commanders are demanding. In the coming year, this group will work toward reengineering resource management at the wing/unit level and streamlining the financial plan, both of which are expected to make significant progress towards reducing transaction-based workload.

### Reengineer Acquisition Decision Support

The Air Force Cost process must provide enhanced decision support for acquisition decisions based on analysis that correctly balances warfighting requirements, available resources and risk. During Phase 1, the task force thoroughly reviewed the current cost processes, evaluated best practices from government and industry, and examined the cost tools available for use. In Phase 2 of the project, the task force will reengineer FM processes and practices to maximize stability of acquisition funds, better support evolutionary acquisition and spiral development, maximize flexibility in funds management, and develop a process that allows for prioritization of Air Force acquisition programs. Pilot programs are currently underway which are working towards achieving a shortened cost estimating process while improving estimate quality.

### Combat Comptroller Concept

Supporting deployed operations around the world during peacetime, contingencies and war is a critical priority for financial management personnel. To make these operations more efficient, the task force is aiming to remove accounting transaction processing from the theater, decrease accounting reconciliation cycle time, and reduce cash/check handling. Already the Air Force has introduced a Knowledge Management link to be used by deployed personnel, streamlined electronic transfer of funds into deployed theaters, standardized routine deployment processes, and improved training. The Air Force is preparing to introduce more electronic banking such as ATMs where possible, and stored value cards at other locations. These will permit purchases from Services or the BX without the use of cash. The task force is also attempting to shift more accounting work from the theater to a central back shop. The Central Processing Site pilot consolidates the accounting pro-

cessing and reconciliation at a single stateside location. While this will not immediately reduce the requirement for deployed personnel, it is step one of a multi-generational plan to do just that. Eventually, the task force expects to see hand-held devices in the field, which directly transmit purchase requests and other documents to this central accounting shop. In Phase 2, there are continued efforts toward evaluating and improving support at deployed locations to include developing a standardized FM CONOPS.

## Reengineer the Air Force—DFAS Relationship

The Air Force is jointly working with the Defense Finance and Accounting Service (DFAS) to ensure our customers are provided with quality services and timely accurate information. In Phase 1 of this initiative, the task force has examined two key processes for internal governmental accounting and found significant opportunities for improvement. In one pilot, accuracy of accounting records was dramatically improved at the two pilot bases and substantial funds, which had been unnecessarily obligated for excessive periods of time, were made available to commanders for key warfighting requirements. The second pilot brings together Financial Management, Contracting and DFAS to reduce costs associated with intergovernmental purchases. Through the active partnership with Contracting, significant amounts of surcharges from other governmental agencies will be avoided and better contractual decisions will be made. In Phase 2 of this initiative, the process of accounting for commercial purchases will be examined. The initiative seeks to optimize the writing of contracts to not only provide the good or service at the lowest cost, but to simplify the billing, payment and accounting associated with it.

## Financial Management Knowledge Management Concept

Air Force downsizing, reorganizations and personnel cuts indicate that we are beyond "doing more with less." World-class financial tools are needed to help financial management professionals become more productive, enhance their skills and continue to become strategic partners with commanders and leaders at all levels. Knowledge Management will do this by revolutionizing the way the Air Force trains, supports and develops Financial Management personnel. It will capture and make available for reuse, a wide variety of corporate knowledge from across the entire financial management community. Hosted on Air Force Knowledge Now, the knowledge management system is organized into Communities of Practice that correspond to the way we do business. For example, there are Communities of Practice for Cost, Budget, Accounting and Finance, Policy, Automated Tools and others. This system offers a sophisticated online Wisdom and Advice feature, document management capabilities, and various collaboration tools such as online forums. The first phase of this initiative built the infrastructure and began to populate it with data. Subsequent efforts will include additional technical innovation tools, an expanded user base, additional Communities of Practice, and expanded knowledge content.

# Air Force Working Capital Fund

*"Working capital funds provide a financial structure that is intended to promote total cost visibility and full cost recovery of support services. The funds are structured around functions that provide goods and services to customers throughout DoD. Managers of these functions prepare their proposed budgets based on anticipated workload and expenses. At the same time, fund customers include in their budgets their planned requirements for goods and services from the various functions. These budgets are submitted to the Components, and the budget process sets rates for each function. Rates are keyed to a unit of output that is unique to each function. The rates are stabilized for the budget year and are intended to ensure that customers pay for the full cost of goods and services they receive from the functions."*

**—Department of Defense (DoD) Costing**

## Working Capital Fund Concept

### Air Force Materiel Command Focus on the Warfighter

Air Force Materiel Command (AFMC) supports Air Force warfighters and operations via three major business areas that all operate as revolving funds, i.e., they charge users for the goods and services they provide.

**Depot Maintenance Activity Group (DMAG):** The DMAG is responsible for maintenance and repair of systems and spare parts while striving to meet or exceed required standards for quality, timeliness and cost. Repair and overhaul is accomplished by both Air Force Materiel Command (AFMC) depots and contract operations.

**Supply Management Activity Group (SMAG):** The SMAG provides inventory management of spare parts and associated logistics support services. The major components of SMAG include:

- **Materiel Support Division (MSD):** The principal products of MSD are reparable spare parts and assemblies unique to Air Force weapon systems, i.e., those spare parts that can be repaired. The sale of reparable parts represents about 90 percent of total sales. The remainder represents sales of some consumable items, i.e., items disposed of when they fail. Although most consumable items have been transferred to the Defense Logistics Agency (DLA) for management, items designated as design unstable remain on the AFMC product list.
- **General Support Division (GSD):** The GSD provides both Air Force and non-Air Force customer's inventory management of the consumable spare parts that were transferred to DLA.
- **Medical/Dental:** The Surgeon General of the Air Force is responsible for the overall management of the Medical/Dental Division. The Medical/Dental division purchases large quantities of medical commodities in order to sell small quantities directly to the consumer, thereby providing effective support necessary to maintain established norms in the health care of USAF active military, retirees, and their dependents.
- **AF Academy:** The Air Force Academy Cadet Issue Division finances the purchase of uniforms, uniform accessories, and computers for sale to cadets. The division's customer base includes more than 4,000 cadets who receive distinctive uniforms procured from a number of domestic manufacturing contractors.

**Information Services Activity Group (ISAG):** The ISAG provides technological support for all levels of information systems, from development of leading-edge technologies to the maintenance and modification of older legacy systems. It offers comprehensive support to its customers, including the development, maintenance, integration, and sustainment of their combat support information systems.

*"Every sortie launched, every target confirmed, every bomb dropped and every radio message completed in support of our war on terrorism happens because AFMC people continue to anticipate and meet the needs of America's warfighters."*

**Gen. Lester L. Lyles**
**Former Commander, AFMC**

## Sustained Exceptional Logistics Support to the Warfighter—OPERATION IRAQI FREEDOM

When the call came to support OPERATION IRAQI FREEDOM (OIF), the men and women of the Air Force Materiel Command (AFMC) responded.

Extraordinary efforts included accelerating testing and fielding of new technologies, standing up new units, and deploying to the CENTCOM Area of Responsibility. AFMC personnel stepped forward and showed their dedication in working toward a common goal—supporting the warfighter. AFMC men and women worked harder than ever to make sure America's warfighters had the capabilities they needed to carry out their missions. Warfighter sustainment experts worked around the clock to get mission-critical parts to deployed people across the globe. They fostered and maintained the mentality that there is nobody more important than the person flying the mission and the person fixing the aircraft.

Throughout the war, the Air Force showed the fourth straight year of improvements across major readiness indicators. The right application of AFMC/LG involvement was needed to produce these results, including direct shipments from vendors to warfighters and finding the fastest transportation routes. At the height of the war there were about 10,000 shipments per week, with around 82,000 requisitions filled overall. Aggressive work and coordination between AFMC, Air Mobility Command, and commercial carriers led to this success.

Supply Chain Managers (SCMs) ensured high-level visibility on critical spares and leveraged the supply chain to reduce customer wait time. Parts constraints were quickly resolved by the collaboration of contracting offices and contractors, manufacturers, funds/budget managers, and SCMs. Therefore, in FY 2003 Total Non-Mission Capable Due to Supply (TNMCS) rates were the lowest since FY 1997, and were only 11 percent for premier weapon systems. In fact, there was no sortie lost due to lack of parts or munitions. TNMCS improvements during OIF were driven by mobilization of Air Force Reserve forces and the Air National Guard, 24/7 deployed operations, and deferred scheduled maintenance for non-critical items. Furthermore, cannibalization actions were reduced 43 percent in FY 2003, with April 2003 showing the best monthly cannibalization rate ever recorded.

AFMC warfighter support continues to improve, as shown by Mission Capable (MICAP) hours (hours accrued until warfighter order is filled) at its lowest historical level. In fact, MICAP hours for April FY 2003 were at the lowest level since MICAP metric tracking began (May 2000), leading to mission capable rates in FY 2003 at the highest levels since July 1996. Great improvements were also made in Logistics Response Times (LRT, the entire pipeline from requisition to base level customer receipt). Prior to 9/11 the average was 37 days, but during OIF the average improved to 33.4 days. In addition to LRT improvements, issue and stockage effectiveness times have also moved in positive directions. Engine readiness is at the highest levels since the Gulf War. FY 2003 engine production continued to run above budgeted goals.

Improving mission capable rates for aircraft and engines were not the only ways AFMC enhanced Air Force combat power. More aircraft were made available to

the warfighter, depot production was above target in FY 2003 and on-time-due-date performance continued to trend upwards. In fact, AFMC averaged 44 days earlier than scheduled on aircraft delivery. As a result, in FY 2003 the warfighter had 20 percent more aircraft than 3 years ago.

AFMC people indeed rose to the challenge of OIF, as they continue to do for OPERATION NOBLE EAGLE and OPERATION ENDURING FREEDOM. Simply, by doing the critical work of supply, maintenance and logistics better and faster, AFMC dramatically illustrated improved support to Air Force warfighters.

## Transformation Efforts

As AFMC success in OIF shows, transformation of Air Force operations and enterprise processes has already yielded impressive results, but this transformation must continue and expand to enable the flexible, responsive force needed to face future challenges. Even as the Air Force transformation process streamlines acquisition and contracting procedures at the highest levels of the Air Force, so also must transformation opportunities be acted on at every level—from headquarters to the flight-line airman.

AFMC, as the key Major Command in acquiring, supplying, maintaining and delivering Air Force material and equipment, clearly met this challenge head-on in FY 2003. AFMC undertook across-the-board initiatives to increase efficiency and reduce costs, all with the focus

on support to Air Force warfighters and operations. Every aspect of AFMC processes is open to review, and the Air Force has already benefited with in-place initiatives to provide more effective support. All AFMC functions and activities are involved, and the results in FY 2003 ranged from improving depot maintenance procedures to the integration of supply chain functions and reshaping to free military positions for warfighting roles to taking advantage of inherent civilian expertise. A review of AFMC activity group transformation efforts includes:

### DMAG Transformation

A number of Depot Maintenance Reengineering and Transformation initiatives have been approved. The expected results from these initiatives equate to improved readiness and support to the warfighter, improvement in execution year financial results, and improved processes.

In Depot Maintenance Transformation (DMT), AFMC has chartered a Business Process Reengineering (BPR) team to integrate process improvement efforts on the shop floor with production support processes and to determine the most effective Maintenance, Repair, and Overhaul (MRO) information system enabler. This results in a "lean" focus on production and production support, and each production line will implement 6S (sort, straighten, scrub, standardize, safety, and sustain), reconfigure into production cells, and construct a tailored logistics support plan that will provide all materials and tools at point of use. DMAG will have enterprise processes that will be more effective and efficient, and will establish Production Support Cells (PSC) that will support and be located on the shop floor. Production shop floor change has already begun in some areas.

Eighty percent of all production lines will be converted to cellular flow by the end of 2004.

As a result, future depot maintenance will incorporate:

- Single piece cellular flow
- All resources at point of use at time of need
- Flexible workforce
- Standard work
- Visual controls
- One easy-to-use information system
- Right-sized, state of the art, facilities/equipment
- Alignment of responsibility, authority, and accountability
- Pro-active planning and scheduling of workload in anticipation of customer requirements

## SMAG Transformation Initiatives

The SMAG is implementing a major redesign of the spares supply process through a set of initiatives designed to improve support to the warfighter. These initiatives will result in a fundamental reshaping of the internal management processes and data systems used on a daily basis to buy, repair, and distribute the thousands of different items needed to maintain weapon systems in a mission-capable (MC) status. Five primary initiatives address key areas of opportunity within the spares process.

- Purchasing and Supply Chain Management (PSCM)—When implemented, PSCM will integrate purchasing and supply processes into a single end-to-end process that spans the Air Force supply system, reducing supply chain operating costs and improving warfighter readiness.
- Weapon System Supply Chain Management (WS SCM)—WS SCM utilizes the private sector and sister services best practice of creating a supply chain manager position that reports directly to the "CEO" or the Air Force equivalent, System Program Director (SPD). It integrates the weapon system supply chain to maximize spares support to achieve weapon system availability.
- Logistics Enterprise Architecture (LOGEA)—LOGEA is an initiative to develop a single authoritative strategic map of future Logistics business practices, systems, and organizations. It is a single authoritative source defining operating and systems models, aligns business and IT initiatives, and provides a vehicle to ensure transformation coordination across the Air Force and outside the Air Force.
- Advanced Planning System (APS)—APS aims to improve the process of translating warfighter needs into executable logistics system support plans and schedules. By emphasizing collaboration with customers and suppliers, it seeks to optimize activities and resources across the Air Force supply chain.
- FY 04 Metrics Way Ahead—HQ AFMC/LG recognizes Aircraft Availability (AA) as the organizational focus and is implementing a new approach to the FY 04 Supply Performance Metrics. Metrics that

show a high correlation to AA, known as Performance Measures, will be formally reported. These measures include MICAP Hours and Customer Wait Time (CWT).

### ISAG Transformation Initiatives

In response to changes in Air Force structure and operations, technology, customer needs and to take better advantage of industry core competencies, the ISAG is reshaping itself to meet future information technology requirements for the warfighter. The end result is an organization that is more net-centric, building an object-oriented skills base, and concentrating on architecture, integration, and independent testing to assure top performance and interoperability in the systems we deploy to our warfighters. One key in this reshaping involves releasing military positions to be used in other warfighting roles as well as partnering with industry providers for the development of systems while leveraging our unparalleled acquisition and engineering expertise.

In sum and across activity groups, AFMC recognizes that Air Force transformation is a process that cannot rest on its laurels. As such, AFMC is pressing ahead with transformation initiatives, expanding the implementation of good ideas and improved procedures and empowering all AFMC people to contribute to better ways of doing business for the Air Force.

## Air Force Working Capital Fund (AFWCF) Overview

The Air Force Materiel Command (AFMC) accounts for more than 95 percent of Air Force Working Capital Fund (AFWCF) revenue and expense activity (excluding the Transportation Working Capital Fund, which is managed by the United States Transportation Command). The AFWCF consists of three functions: Supply Management, Depot Maintenance, and Information Services. These functions, referred to as activity groups, supply their singular goods and services to Air Force and DoD customers. Supply Management provides inventory management for spare parts and associated logistics support services to fulfill Air Force needs during war and peacetime. Depot Maintenance provides economical and responsive repair, overhaul, and modification of aircraft, missiles, engines, other major end items, and their associated components. The Information Services business area provides for the

maintenance and development of automated information systems for information-related activities of the Air Force, Department of Defense (DoD), along with certain other Government agencies.

Working Capital Funds (WCFs) allow the Air Force to accomplish the following:

- Ensure readiness through reduced support costs, stabilized rates, and customer service
- Focus management attention on net results, including costs and performance
- Identify the total cost of providing support products and services
- Establish strong customer/provider relationships

### Funding Authority

The Office of the Under Secretary of Defense (Comptroller) (OUSD(C)), through the Assistant Secretary of the Air Force (Financial Management and Comptroller) (SAF/FM), allocates to activity groups their annual cost authority. Specific capital investment targets are established to support the replacement and modernization of equipment and other capital assets through the budget, obligation, and procurement processes.

### Cash Management

DoD cash management policy recommends maintaining the minimum cash balance necessary to meet both operational requirements and disbursements in support of the capital program. Cash generated from operations is the primary means of maintaining adequate cash levels. The ability to generate cash is dependent on setting rates to recover full costs, including prior-year losses,

accurately projecting workloads, and meeting established operational goals.

Effective cash management is directly dependent on the availability of accurate and timely data on cash levels and operational results. Cash levels should be maintained to cover at least seven to 10 days of operational costs as well as cash adequate to meet six months of capital disbursements. The recommended cash range for FY 2003, the FY 2003 result, and the FY 2004 goal are below.

Cash management efforts continue to focus on analyzing data and developing tools to identify changes in cash. Monthly, AFMC prepares a statement of sources and uses of cash and use these statements to identify areas of cash increases and drains.

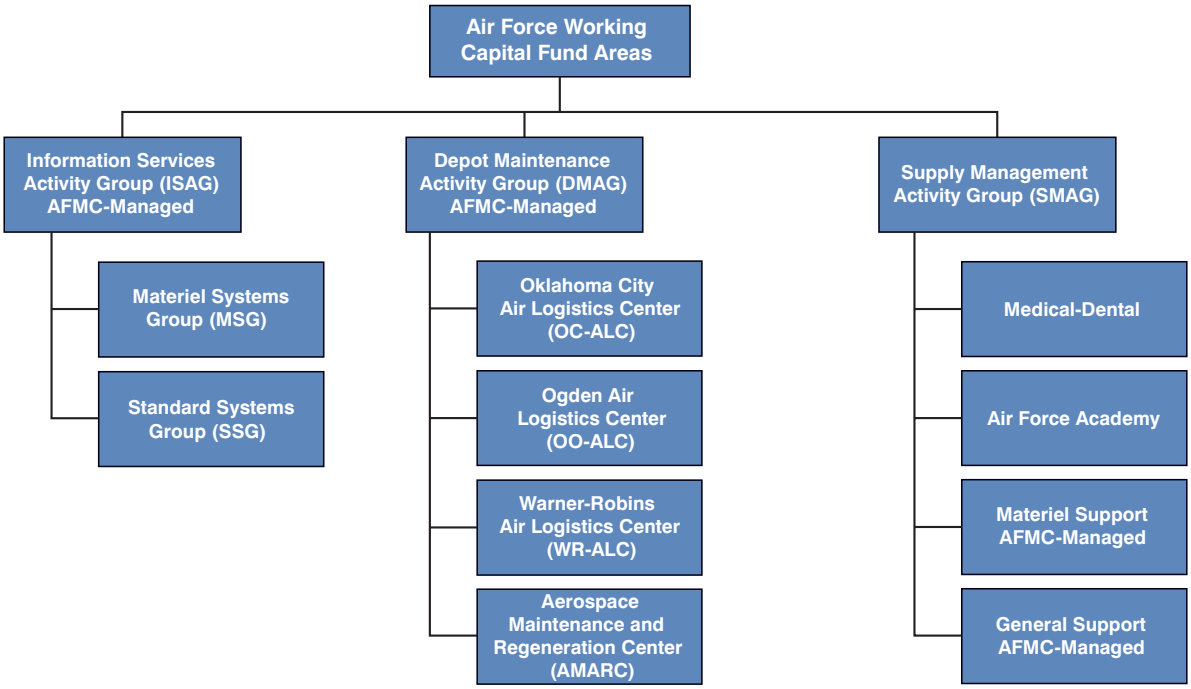
**AF Working Capital Fund Cash Performance Measure**

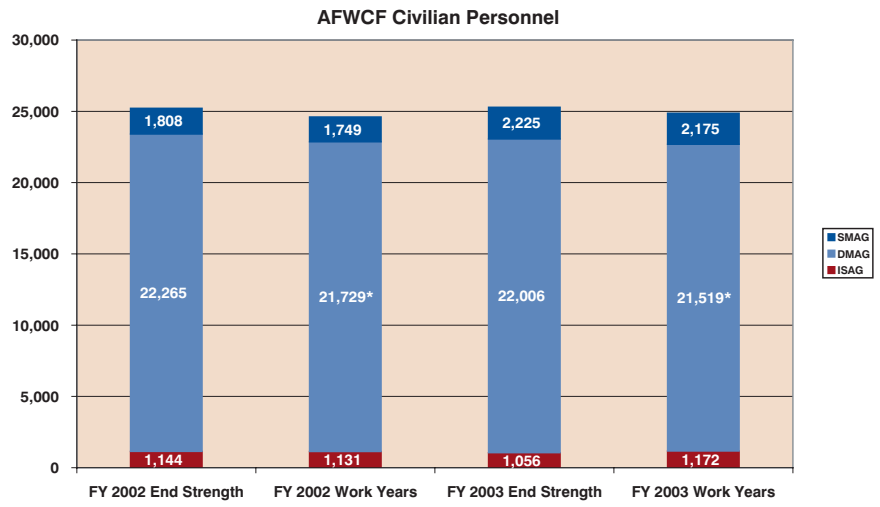
| Activity Group | FY 2003 Goal* | FY 2003 Result** | FY 2004 Goal* |
|---|---|---|---|
| DMAG | $199.5 M | $352.7 M | $299.7 M |
| SMAG | $143.5 M | $316.5 M | $399.5 M |
| ISAG | $41.2 M | $50.4 M | $52.6 M |
| Transportation | $860.0 M | $1,742.2 M | $304.0 M |
| Other | $29.0 M | $13.2 M | $29.0 M |
| Total | $1,273.2 M | $2,475.0 M | $1,084.8 M |

*Source: *FY04 PB, **30 September 03 Financial Data*

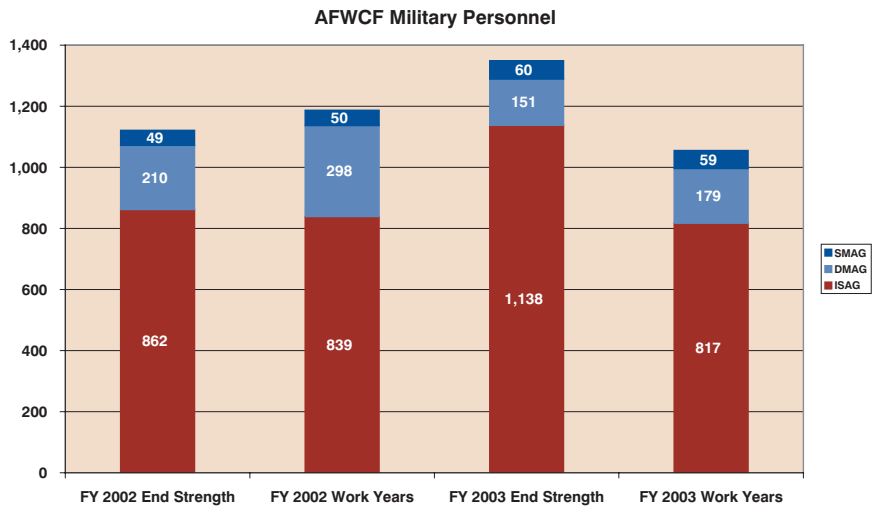
## Air Force Working Capital Fund Organization

**Air Force Working Capital Fund Activity Groups and Divisions**

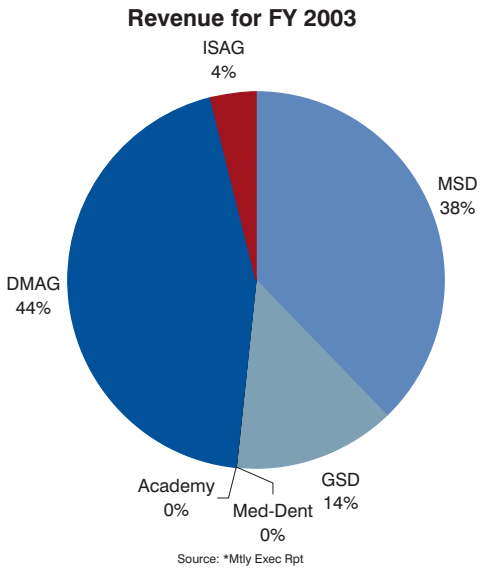




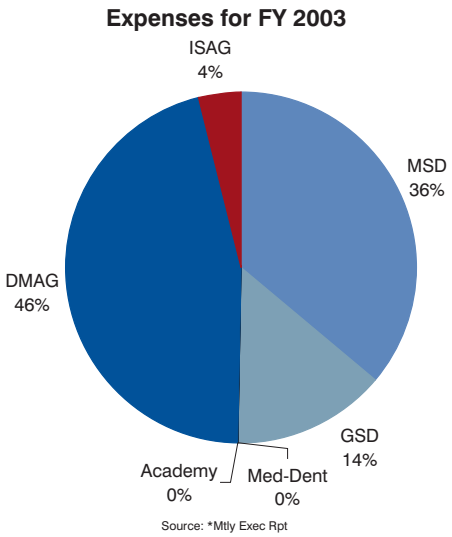

* Excludes Overtime
FY03 SOURCE: SMAG and ISAG FY04 PB, DMAG 8203 Rpt.




FY03 SOURCE: SMAG and ISAG FY04 PB, DMAG 8203 Rpt.




Source: *Mtly Exec Rpt




Source: *Mtly Exec Rpt

## Depot Maintenance Activity Group

The Depot Maintenance Activity Group (DMAG) repairs systems and spare parts which support the warfighter in peacetime and provide sustainment to combat forces in wartime. In peacetime, DMAG enhances readiness by efficiently and economically repairing, overhauling, and modifying aircraft, engines, missiles, components, and software to meet the warfighter demands. During wartime or contingencies, the group shifts to surge repair operations and realign capacity to support the warfighter's immediate needs.

### Mission Statement

Support an Air and Space Expeditionary Force by providing repair systems and spare parts that ensure readiness in peacetime and provide sustainment to combat forces in wartime.

### Customers, Products and Services

DMAG provides major overhaul and repair of systems and spare parts while striving to meet or exceed required standards for quality, timeliness, and cost. Both the Air Force Material Command (AFMC) depots and contract operations accomplish these goals.

Depot maintenance supports customers across the Air Force. In addition to supporting the warfighter with depot level repair of weapon systems, DMAG provides storage, reclamation, and regeneration for equipment not currently used by the active forces of all military services. This work is done at the Aerospace Maintenance and Regeneration Center at Davis Monthan AFB, Arizona.

The Depot Maintenance Activity Group has two principal objectives. The first objective is to provide organic and contract depot repair capability for fielded and emerging weapon systems, so warfighters have needed mission-essential equipment. Secondly, DMAG ensures the ability to rapidly respond to warfighter requirements driven by contingency operations. This requires both short and long term strategies, and the depot maintenance strategic plan guides the DMAG to have the right workload capacity and capability to meet depot maintenance: (a) peacetime support; (b) surge and (c) core requirements.

### Depot Maintenance Accounting and Production System (DMAPS)

DMAPS is an integrated suite of systems providing improved financial, production and material functions in support of warfighter needs for quality organic depot maintenance. During Fiscal Year 2003, AFMC completed implementation of the financial portion of the DMAPS. This followed successful implementation of production functions in Fiscal Year 2002. DMAPS brings substantial improvement to financial management and reporting for organic depot maintenance activities, to include substantial compliance with legislative requirements, such as the Chief Financial Officers (CFO) Act. The integrated suite of systems provides AFMC the capability to capture actual and planned direct material and direct labor at the task level and report this on a daily basis. DMAPS also provides the capability to apply overhead and general and administrative expenses on a planned dollar rate per direct labor hour, giving organic depot maintenance activities the capability to look at production cost on a daily basis at the task level. Other benefits include a standard DoD financial reporting system, a fully automated billing process, reduction of some legacy systems and a consolidated fund control process.

### Customer Support Performance Measures

Customer Support Performance Measures for DMAG consist primarily of Production Performance Measures that are used to assess cost, schedule and quality of the DMAG output. These are designed to achieve accountability at the appropriate depot maintenance level, the Depot Maintenance Manager. They measure compliance with DMAG goals.

| Organic Depot Maintenance<br>Customer Support Performance Measures | | | |
|---|---|---|---|
| **Measure** | **FY 2003 Goal*** | **FY 2003 Result**** | **FY 2004 Goal****** |
| **Organic Production Hours (DPSH)** | 22,083 K | 23,302K** | 22,136K |
| **Aircraft Days Held Index (yr)** | ≤1.0 | 1.02 | ≤1.0 |
| **Aircraft Due Date Performance** | ≥90 Percent | 78 Percent | ≥90 Percent |
| **Aircraft Quality Defect Rate (18 mo avg)** | Varies by MDS | 0.21*** | Varies by MDS |
| **Engine Quality Defect Free Percentage** | Varies by engine | 0.04*** | Varies by engine |
| **Exchangeable Quality Defect Rate (Defects per item)** | 0.03 | 0.020*** | 0.03 |

*Source: *FY03 Depot Maint Mission Area Ops Plan, **30 Sep 03 Execution Data, ***Oct 02-Jun 03, **** FY04 PB*

**Organic Production Hours:** The maintenance hours necessary to produce a product (i.e., aircraft, engines, spares, software, etc.) or to provide a service.

**Aircraft Days Held Index:** The length of time that the depot or depot maintenance contractor possesses aircraft for maintenance or modifications.

**Aircraft Due Date Performance:** The ability of the depot and depot maintenance contractors to produce aircraft according to schedule.

**Aircraft Quality Defect Rate:** The ability of the depot and depot maintenance contractors to produce defect-free aircraft, ready for use by the customer.

**Engine Quality Defect Rate:** The ability of the depot to produce engines that are defect free and ready for use by the customer.

**Exchangeable Quality Defect Rate:** The ability of the depot, to produce components that are defect free and ready to use by the customer.

## Financial Performance Measures

Financial Performance Indicators assess the financial performance of the DMAG. They are designed to achieve accountability at the appropriate level and measure compliance with DMAG objectives.

The following represent the DMAG Financial Performance Indicators for Organic. We are currently in the process of realigning the Contract DMAG program, to provide a more direct relation between customers and repair contractors:

| Depot Maintenance<br>Financial Performance Measures | | | |
|---|---|---|---|
| **Measure** | **FY 2003 Goal*** | **FY 2003 Results**** | **FY 2004 Goal*** |
| **Organic Net Operating Result (NOR)** | ($173.8) M | ($116.9) M*** | $107.2 M |
| **Organic Expense Rate** | $193.05 | $184.86 | $221.12 |

*Source: *FY03 = 04PB excluding $109M planned reimbursement not provided during execution **FY03 30 Sep 03 Financial Data*
*****$70M of the FY03 loss was a duplication of losses also reported in FY02*

**Organic Net Operating Result:** The profit or loss from annual operations and is based on work performed. Revenue includes amounts earned from stabilized sales rates and reimbursements. The goal of the fund is to break even over the long run.

**Organic Expense Rate:** Estimated cost per hour for work produced including all labor, material and business operations costs. It provides managers visibility of cost trends.

## Supply Management Activity Group

### Mission Statement

The SMAG provides policy, guidance, and resources to meet Air Force needs for spare parts. SMAG manages approximately two million items including weapon systems spare parts, medical/dental supplies and equipment, and items used for non-weapon systems applications. Materiel procured from vendors held in inventory is for sale to authorized customers.

SMAG consists of four divisions: the Materiel Support Division (MSD), General Support Division (GSD), Medical/Dental Division, and Air Force Academy Cadet Issue Division. The Air Force Materiel Command (AFMC) manages MSD and GSD. The United States Air Force Headquarters (HQ USAF) manages the Medical/Dental Division and Air Force Academy Cadet Issue Division. Since the onset of FY 2002, Headquarters Defense Logistics Agency/Defense Energy Service Center assumed management of the Fuels Division.

MSD is responsible for Air Force-managed, depot-level reparable spare parts and some consumable spares. The principal products of MSD are serviceable spare parts and assemblies unique to Air Force weapon systems.

The Retail Operations of the Air Force Working Capital Fund is comprised of the General Support, Medical Dental, and United States Air Force Academy Divisions. Although each division operates independently they all purchase large quantities of commodities in order to sell small quantities directly to the ultimate consumer (supporting the warfighter). Large bulk buys allow them to take advantage of the economies of scale and achieve significant cost savings. Additionally, each division concentrates its efforts in a specific area of expertise.

GSD items support installation maintenance and administrative functions, field and depot maintenance of aircraft and other systems. GSD supports more than 150 Air Force installations throughout the world.

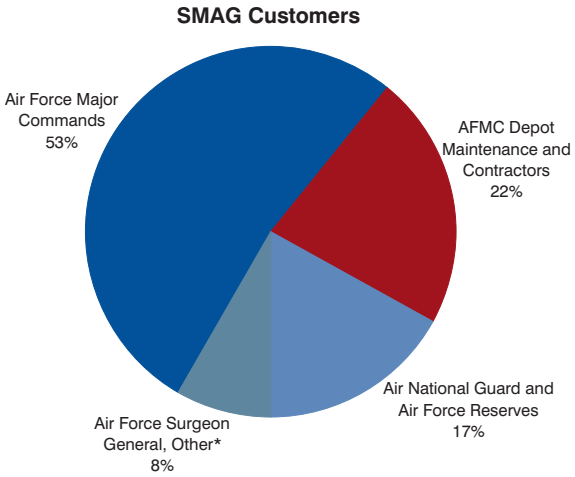
The Surgeon General of the Air Force is responsible for the overall management of the Medical/Dental Division. This peacetime operating authority provides the effective support necessary to maintain established norms in the health care of USAF active military, retirees, and their dependents. The war reserve materiel (WRM) requirement of this division is to provide medical supplies and equipment vital to support forces in combat and contingency operations.

The Air Force Academy Cadet Issue Division finances the purchase of uniforms, uniform accessories, and computers for sale to cadets. The division's customer base includes more than 4,000 cadets who receive distinctive uniforms procured from a number of domestic manufacturing contractors.

### Customers, Products, and Services

In addition to the management of various inventories, the SMAG provides a wide range of logistics support services, including requirements forecasting, item introduction, cataloging, provisioning, procurement, repair, technical support, data management, item disposal, distribution management, and transportation.

SMAG provides support to a variety of customers. During FY 2003, the customer base consisted primarily of the following:




*Other military services within the DoD, other agencies within the Federal Government, and Foreign Military Sales (FMS). Source: Mtly Exec Rpt

The supply business also provides initial provisioning support to the Air Force Acquisition Executive.

## Customer Support Performance Measures

SMAG evaluated customer support performance of Air Force managed items for FY 2003 based on the following indicators. These indicators provide feedback to allow managers to assess quality of spares support provided and plan corrective action when needed. General Support Division reports these indicators at the base level not at the aggregate level. As a result of the FY 2004 Metrics Way Ahead initiative, future performance measures will be reported on MICAP Hours and CWT. Issue Effectiveness (IE), Stockage Effectiveness (SE), Logistics Response Time (LRT), and Backorders are now Process Indicators and will only be referenced as part of root-cause analysis.

**Materiel Support Division**
**Customer Support Performance Measures**

| Measure | FY 2003 Goal* | FY 2003 Result** | FY 2004 Goal*** |
|---|---|---|---|
| **Issue Effectiveness (IE)** | 65.1 Percent | 69.3 Percent | No Goal |
| **Stockage Effectiveness (SE)** | 74.4 Percent | 76.5 Percent | No Goal |
| **Logistics Response Time (LRT)** | 35.3 Days | 26.9 Days | No Goal |
| **Backorder Reduction** | 177,281 Units | 288,644 Units | No Goal |
| **MICAP** | 3,139,459 Hours | 2,216,802 Hours | 2,181,437 |
| **CWT** | No Goal | 8.52 Days | 8.34 Days |

*Source: *FY03 Supply Mgnt Mission Area Ops Plan, **30 Sep 03 Execution Data, ***FY04 Sustainment Mission Area Ops Plan for Supply*

**Issue Effectiveness (IE):** IE reflects the percentage of time base supply satisfies base demands with stock off the shelf, irrespective of authorized stock levels. The IE supports the AFMC Expeditionary Combat Support Enabling Task to "equip and sustain the war fighter with reach back capability to the latest available technology and resources."

**Stockage Effectiveness (SE):** SE represents the percentage of time base supply satisfies base demands with stock off the shelf, for items with authorized stock levels only.

**Logistics Response Time (LRT):** LRT measures the average time taken to satisfy customer (base supply or depot retail) requisitions for those Air Force managed items that were not immediately available.

**Backorders:** A backorder is a demand placed on the Air Force supply system that cannot be immediately satisfied from existing inventory. The SMAG strives to reduce backorders by having parts on the shelf for immediate issue and increasing war fighter readiness.

**Mission Capability (MICAP) Hours:** A MICAP backorder is a demand placed on the supply system that cannot be immediately satisfied from existing inventory and has been designated as affecting mission capability by the customer. MICAP hours are accrued until the order is filled. The SMAG strives to reduce MICAP hours by having parts on the shelf for immediate issue and thus increasing operational readiness.

## Financial Performance Measures

SMAG measures financial performance based on the following indicators shown for MSD and GSD. These indicators allow effective and efficient utilization of funding to support customer needs, while providing vital information needed for accurate budget forecasts.

| Supply Management<br>Financial Performance Measures<br>Materiel Support Division | | | |
|---|---|---|---|
| **Measure** | **FY 2003 Goal*** | **FY 2003 Result**** | **FY 2004 Goal* (05 BER)** |
| **Revenue** | $6114.2 M | $6,596.8 M | $6,656.8 M |
| **Expenses** | $6013.5 M | $6,170.2 M | $6,511.7 M |
| **Net Operating Result (NOR)** | $100.7 M | $426.6 M | $145.1 M |
| **Unit Cost Target (UCT)** | 1.030 | 1.050 | 1.000 |

*Source: *FY04 PB, **30 September 03 Financial Data (CFIS)*

| Supply Management<br>Financial Performance Measures<br>General Support Division | | | |
|---|---|---|---|
| **Measure** | **FY 2003 Goal*** | **FY 2003 Result**** | **FY 2004 Goal*** |
| **Revenue** | $2,088.1 M | $2,451.8 M | $2,379.0 M |
| **Expenses** | $2,088.1 M | $2,397.5 M | $2260.2 M |
| **Net Operating Result (NOR)** | $0 M | $54.4 M | $118.8 M |
| **Unit Cost Target (UCT)** | 1.000 | 1.077 | 1.000 |

*Source: *FY04 PB, **30 September 03 Financial Data (CFIS)*

**Revenue:** Revenues are amounts earned as a result of normal operations and usually result from sale of, or reimbursements for, goods and services provided to DoD activities, other federal government agencies and the public.

**Expenses:** Expenses are the use of resources during an accounting period in carrying out the DoD's mission. They occur from rendering services, delivering or producing goods, or carrying out other mission related activities and relate to normal operating activities.

**Net Operating Result (NOR):** The NOR is the difference between revenue and expenses, i.e., a bottom-line profit and loss indicator. The NOR objective of an activity group is to break even over a two-year budget cycle. Setting rates that effectively offset the prior year net profit or loss accomplishes this.

**Unit Cost Target (UCT):** UCT is a limitation imposed by the Office of the Under Secretary of Defense (Comptroller) on the annual operating budget (AOB), restricting obligations to a percentage of gross sales. The AOB is the funding document providing the authority to incur costs. The UCT is determined by dividing costs by sales. Another description is the ratio of obligations to gross sales. A definition for costs is an obligation (excluding initial and capital expenses) and credit returns.

## Information Services Activity Group

The Information Services Activity Group (ISAG) was established to develop and maintain automated information systems for specific Air Force, DoD, and other Government agencies. Two Air Force entities act as one information technology provider activity under the command of the Air Force Materiel Command, Electronic Systems Center (ESC), at Hanscom Air Force Base (AFB), Massachusetts. The two entities are the Materiel Systems Group (MSG), located at Wright-Patterson AFB, Ohio, and the Standard Systems Group (SSG) located at Maxwell AFB-Gunter Annex, Alabama.

### Mission Statement

Develop, acquire, integrate, implement, protect and sustain combat support information systems for the United States Air Force and Department of Defense customers.

### Customers, Products, and Services

ISAG provides information products and services via two business lines—the information technology solutions line (rate based) and the commercial information technology (surcharge) line.

The information technology solutions business line develops, acquires, and sustains automated information systems in two target markets: 1) AFMC-level supply management and depot maintenance information systems and 2) Air Force-wide, standardized support systems. This includes a 24-hour, seven-day help desk for customers to call for hardware and software support. The ISAG provides their service based on service-level agreements (SLAs) with known customers which specify how many direct billable hours of service per year

will be sold to the customer and at what cost per billable hour.

The commercial information technology business line provides computer hardware, software, peripheral equipment and related services to the Department of the Air Force, other agencies including DoD, and private parties (as authorized by law) through their web-based "Virtual Superstore" called "AFWay." Thousands of customers across the Air Force and DoD enjoy one-stop shopping from the online catalog of computer and computer-related products and services. For providing this service, the commercial information technology line collects a small surcharge, which is embedded into the price of the item, on equipment and services sold.

### Customer Support Performance Measures

ISAG measures the quality of support to its consumer base using several performance indicators. Critical to the ISAG customer is the timeliness of software releases required to either fix deficiency reports or to make enhancements to the software. In addition, the ISAG customers demand timely resolution to their software problems or discrepancies.

**Information Services**
**Customer Support Performance Measures**

| Measure | FY 2003 Goal* | FY 2003 Result** | FY 2004 Goal*** |
|---|---|---|---|
| **Software Releases** | 95 Percent | 99 Percent | TBD |
| **Priority 1 Deficiency Reports** | 66 Percent | 92 Percent | TBD |
| **Priority 2 Deficiency Reports** | 75 Percent | 96 Percent | TBD |

Source: *ODA Internal Goal/Metric, **Mtly Exec Rpt

*** Due to ongoing transformation efforts, ISAG has suspended reporting of these Non-Financial Metrics. Once transformation is complete, a joint MSG/SSG team will attempt to design metrics that better support a netcentric philosophy and will reflect a balanced scorecard approach.

**Software Releases:** The percentage of software which is delivered on time.

**Priority 1 Deficiency Reports:** Percentage of reported priority 1 software deficiencies resolved within 48 hours. Priority 1 software deficiencies are those deficiencies which if not resolved, will prevent the accomplishment of an essential mission capability.

**Priority 2 Deficiency Reports:** Percentage of reported priority 2 software deficiencies resolved within 45 days. Priority 2 software deficiencies are those deficiencies which if not resolved, will affect technical, cost, schedule risks to the project or to the life cycle support of the system, and no workaround is known.

## Financial Performance Measures

| Information Services<br>Financial Performance Measures | | | |
|---|---|---|---|
| **Measure** | **FY 2003 Goal*** | **FY 2003 Result**** | **FY 2004 Goal*** |
| **Revenue** | $608.0 M | $658.5 M | $641.4 M |
| **Cost of Operations (Expenses)** | $613.2 M | $675.2 M | $631.3 M |
| **Net Operating Result (NOR)** | ($5.2) M | ($16.7) M | $10.1 M |

*Source: *FY04 PB, **30 Sep 03 Financial Data*

**Revenue:** Revenue is earned through the sale of direct billable labor hours at the ISAG composite rate; direct reimbursements for pass-through contract efforts and extraordinary expenses (e.g., mission-unique travel, equipment, and supplies); and the collection of commercial information technology surcharges.

**Cost of Operations (Expenses):** Cost of operations (expenses) measures the resources consumed in filling customer orders. These costs include labor and non-labor expenses, both direct and overhead.

**Net Operating Result (NOR):** The NOR is the difference between revenue and expenses, i.e., a bottom-line profit and loss indicator. The NOR objective of an activity group is to break even over a two-year budget cycle. Setting rates that effectively offset the prior year net profit or loss accomplishes this.

United States Air Force

# Fiscal Year 2003
# Annual Financial Statements

## Limitations of the Financial Statements

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

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

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

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

The Federal Accounting Standards Advisory Board (FASAB) amended the Statement of Federal Financial Accounting Standard No. 6 to require the capitalization and depreciation of military equipment (formerly known as National Defense Property, Plant and Equipment) for fiscal years (FY) 2003 and beyond, and encouraged early implementation. Accordingly, the Department began the process of developing and reporting values for these assets in notes to the Balance Sheet, beginning in FY 2002.

# Principal Statements

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# Consolidated Balance Sheet—General Funds

As of September 30, 2003 and 2002 ($ in Thousands)

| | 2003 Consolidated | 2002 Consolidated |
|---|---|---|
| **1. ASSETS (Note 2)** | | |
| A. Intragovernmental: | | |
| 1. Fund Balance with Treasury (Note 3) | | |
| a. Entity | $ 59,714,038 | $ 47,888,000 |
| b. Non-Entity Seized Iraqi Cash | 0 | 0 |
| c. Non-Entity-Other | 52,503 | 54,750 |
| 2. Investments (Note 4) | 712 | 708 |
| 3. Accounts Receivable (Note 5) | 541,429 | 443,154 |
| 4. Other Assets (Note 6) | 339,093 | 4,989 |
| 5. Total Intragovernmental Assets | $ 60,647,775 | $ 48,391,601 |
| B. Cash and Other Monetary Assets (Note 7) | $ 147,926 | $ 140,645 |
| C. Accounts Receivable (Note 5) | 772,500 | 1,017,910 |
| D. Loans Receivable (Note 8) | 0 | 0 |
| E. Inventory and Related Property (Note 9) | 51,815,831 | 28,817,564 |
| F. General Property, Plant and Equipment (Note 10) | 112,786,130 | 24,247,152 |
| G. Investments (Note 4) | 0 | 0 |
| H. Other Assets (Note 6) | 9,912,151 | 7,535,914 |
| **2. TOTAL ASSETS** | $ 236,082,313 | $ 110,150,786 |
| **3. LIABILITIES (Note 11)** | | |
| A. Intragovernmental: | | |
| 1. Accounts Payable (Note 12) | $ 1,413,940 | $ 1,124,733 |
| 2. Debt (Note 13) | 0 | 134 |
| 3. Environmental Liabilities (Note 14) | 0 | 0 |
| 4. Other Liabilities (Note 15 & Note 16) | 1,623,905 | 2,179,087 |
| 5. Total Intragovernmental Liabilities | $ 3,037,845 | $ 3,303,954 |
| B. Accounts Payable (Note 12) | $ 7,080,909 | $ 6,206,967 |
| C. Military Retirement Benefits and Other Employment-Related Actuarial Liabilities (Note 17) | 1,262,267 | 1,211,045 |
| D. Environmental Liabilities (Note 14) | 8,110,403 | 8,454,564 |
| E. Loan Guarantee Liability (Note 8) | 0 | 0 |
| F. Other Liabilities (Note 15 & Note 16) | 4,520,888 | 3,987,188 |
| G. Debt Held by Public (Note 13) | 0 | 0 |
| **4. TOTAL LIABILITIES** | $ 24,012,312 | $ 23,163,718 |
| **5. NET POSITION** | | |
| A. Unexpended Appropriations (Note 18) | $ 50,742,317 | $ 39,543,850 |
| B. Cumulative Results of Operations | 161,327,684 | 47,443,218 |
| **6. TOTAL NET POSITION** | $ 212,070,001 | $ 86,987,068 |
| **7. TOTAL LIABILITIES AND NET POSITION** | $ 236,082,313 | $ 110,150,786 |

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

# Consolidated Statement of Net Cost—General Funds

For the years ended September 30, 2003 and 2002 ($ in Thousands)

| | 2003 Consolidated | 2002 Consolidated |
|---|---|---|
| **1. Program Costs** | | |
| A. Intragovernmental Gross Costs | $ 26,846,664 | $ 21,820,712 |
| B. (Less: Intragovernmental Earned Revenue) | -3,986,411 | -2,327,324 |
| C. Intragovernmental Net Costs | $ 22,860,253 | $ 19,493,388 |
| D. Gross Costs With the Public | 99,803,267 | 72,927,138 |
| E. (Less: Earned Revenue From the Public) | -836,158 | -680,711 |
| F. Net Costs With the Public | $ 98,967,109 | $ 72,246,427 |
| G. Total Net Cost | $ 121,827,362 | $ 91,739,815 |
| **2. Cost Not Assigned to Programs** | 0 | 0 |
| **3. (Less:Earned Revenue Not Attributable to Programs)** | 0 | 0 |
| **4. Net Cost of Operations** | $ 121,827,362 | $ 91,739,815 |



*The accompanying notes are an integral part of the financial statements. See notes 1 and 19.*

# Consolidated Statement of Changes in Net Position—General Funds

For the years ended September 30, 2003 and 2002 ($ in Thousands)

| | 2003 Consolidated | 2002 Consolidated |
|---|---|---|
| **CUMULATIVE RESULTS OF OPERATIONS** | | |
| **1. Beginning Balances** | $ 47,443,218 | $ 70,732,397 |
| **2. Prior period adjustments (+/-)** | 122,475,076 | -31,869,730 |
| **3. Beginning Balances, as adjusted** | 169,918,294 | 38,862,667 |
| **4. Budgetary Financing Sources:** | | |
| 4.A. Appropriations received | 0 | 0 |
| 4.B. Appropriations transferred-in/out (+/-) | 0 | 0 |
| 4.C. Other adjustments (rescissions, etc) (+/-) | 0 | 0 |
| 4.D. Appropriations used | 113,384,126 | 99,437,408 |
| 4.E. Nonexchange revenue | 0 | 0 |
| 4.F. Donations and forfeitures of cash and cash equivalents | 9,096 | 12,682 |
| 4.G. Transfers-in/out without reimbursement (+/-) | 0 | 0 |
| 4.H. Other budgetary financing sources (+/-) | -678,772 | 246,474 |
| **5. Other Financing Sources:** | | |
| 5.A. Donations and forfeitures of property | 0 | 0 |
| 5.B. Transfers-in/out without reimbursement (+/-) | -110,688 | 26,728 |
| 5.C. Imputed financing from costs absorbed by others | 632,990 | 597,076 |
| 5.D. Other (+/-) | 0 | 0 |
| **6. Total Financing Sources** | 113,236,752 | 100,320,368 |
| **7. Net Cost of Operations (+/-)** | 121,827,362 | 91,739,815 |
| **8. Ending Balances** | $ 161,327,684 | $ 47,443,220 |
| **UNEXPENDED APPROPRIATIONS** | | |
| **1. Beginning Balances** | $ 39,543,850 | $ 39,006,789 |
| **2. Prior period adjustments (+/-)** | 0 | 0 |
| **3. Beginning Balances, as adjusted** | 39,543,850 | 39,006,789 |
| **4. Budgetary Financing Sources:** | | |
| 4.A. Appropriations received | 124,225,931 | 96,952,072 |
| 4.B. Appropriations transferred-in/out (+/-) | 2,179,806 | 5,084,803 |
| 4.C. Other adjustments (rescissions, etc) (+/-) | -1,823,144 | -2,062,406 |
| 4.D. Appropriations used | -113,384,126 | -99,437,408 |
| 4.E. Nonexchange revenue | 0 | 0 |
| 4.F. Donations and forfeitures of cash and cash equivalents | 0 | 0 |
| 4.G. Transfers-in/out without reimbursement (+/-) | 0 | 0 |
| 4.H. Other budgetary financing sources (+/-) | 0 | 0 |
| **5. Other Financing Sources:** | | |
| 5.A. Donations and forfeitures of property | 0 | 0 |
| 5.B. Transfers-in/out without reimbursement (+/-) | 0 | 0 |
| 5.C. Imputed financing from costs absorbed by others | 0 | 0 |
| 5.D. Other (+/-) | 0 | 0 |
| **6. Total Financing Sources** | 11,198,467 | 537,061 |
| **7. Net Cost of Operations (+/-)** | 0 | 0 |
| **8. Ending Balances** | $ 50,742,317 | $ 39,543,850 |

*The accompanying notes are an integral part of the financial statements. See notes 1 and 20.*

# Combined Statement of Budgetary Resources—General Funds

For the years ended September 30, 2003 and 2002 ($ in Thousands)

| | 2003 Combined | 2002 Combined |
|---|---|---|
| **BUDGETARY FINANCING ACCOUNTS** | | |
| **BUDGETARY RESOURCES** | | |
| 1. Budget Authority: | | |
| 1a. Appropriations received | $ 124,235,723 | $ 96,329,855 |
| 1b. Borrowing authority | 0 | 0 |
| 1c. Contract authority | 0 | 0 |
| 1d. Net transfers (+/-) | 1,888,215 | 4,954,597 |
| 1e. Other | 0 | 0 |
| 2. Unobligated balance: | | |
| 2a. Beginning of period | 6,066,510 | 7,203,289 |
| 2b. Net transfers, actual (+/-) | 291,591 | 130,206 |
| 2c. Anticipated Transfers balances | 0 | 0 |
| 3. Spending authority from offsetting collections: | | |
| 3a. Earned | 0 | 0 |
| 1. Collected | 7,802,547 | 6,551,584 |
| 2. Receivable from Federal sources | -322,918 | 274,507 |
| 3b. Change in unfilled customer orders | 0 | 0 |
| 1. Advance received | 213,465 | 106,478 |
| 2. Without advance from Federal sources | 472,167 | -1,182 |
| 3c. Anticipated for the rest of year, without advances | 0 | 0 |
| 3d. Transfers from trust funds | 0 | 0 |
| 3e. Subtotal | 8,165,261 | 6,931,387 |
| 4. Recoveries of prior year obligations | 1,955,959 | 1,051,593 |
| 5. Temporarily not available pursuant to Public Law | 0 | 0 |
| 6. Permanently not available | -1,806,362 | -2,062,413 |
| **7. Total Budgetary Resources** | $ 140,796,897 | $ 114,538,514 |
| **STATUS OF BUDGETARY RESOURCES** | | |
| 8. Obligations incurred: | $ | |
| 8a. Direct | $ 123,375,566 | $ 100,622,101 |
| 8b. Reimbursable | 8,231,386 | 7,849,904 |
| 8c. Subtotal | 131,606,952 | 108,472,005 |
| 9. Unobligated balance: | | |
| 9a. Apportioned | 8,320,595 | 5,268,178 |
| 9b. Exempt from apportionment | 2,573 | 4,607 |
| 9c. Other available | -1 | -1 |
| 10. Unobligated Balances Not Available | 866,778 | 793,725 |
| **11. Total, Status of Budgetary Resources** | $ 140,796,897 | $ 114,538,514 |
| **RELATIONSHIP OF OBLIGATIONS TO OUTLAYS:** | | |
| 12. Obligated Balance, Net - beginning of period | $ 41,822,195 | $ 37,049,171 |
| 13. Obligated Balance transferred, net (+/-) | 0 | 0 |
| 14. Obligated Balance, Net - end of period: | | |
| 14a. Accounts receivable | -1,159,047 | -1,481,965 |
| 14b. Unfilled customer order from Federal sources | -937,374 | -465,207 |
| 14c. Undelivered orders | 42,168,646 | 34,030,703 |
| 14d. Accounts payable | 10,469,360 | 9,738,663 |
| 15. Outlays: | | |
| 15a. Disbursements | 120,782,356 | 102,374,064 |
| 15b. Collections | -8,016,013 | -6,658,063 |
| 15c. Subtotal | 112,766,343 | 95,716,001 |
| 16. Less: Offsetting receipts | -156,704 | -121,154 |
| **17. Net Outlays** | $ 112,609,639 | $ 95,594,847 |

*The accompanying notes are an integral part of the financial statements. See notes 1 and 21.*

# Combined Statement of Financing—General Funds

For the years ended September 30, 2003 and 2002 ($ in Thousands)

| | 2003 Combined | 2002 Combined |
|---|---|---|
| **Resources Used to Finance Activities:** | | |
| Budgetary Resources Obligated | | |
| 1. Obligations incurred | $ 131,606,952 | $ 108,472,005 |
| 2. Less: Spending authority from offsetting collections and recoveries (-) | -10,121,221 | -7,982,980 |
| 3. Obligations net of offsetting collections and recoveries | 121,485,731 | 100,489,025 |
| 4. Less: Offsetting receipts (-) | -156,704 | -121,154 |
| 5. Net obligations | 121,329,027 | 100,367,871 |
| Other Resources | | |
| 6. Donations and forfeitures of property | 0 | 0 |
| 7. Transfers in/out without reimbursement (+/-) | -110,688 | 26,727 |
| 8. Imputed financing from costs absorbed by others | 632,992 | 597,076 |
| 9. Other (+/-) | 0 | 0 |
| 10. Net other resources used to finance activities | 522,304 | 623,803 |
| **11. Total resources used to finance activities** | 121,851,331 | 100,991,674 |
| **Resources Used to Finance Items not Part of the Net Cost of Operations** | | |
| 12. Change in budgetary resources obligated for goods, services and benefits ordered but not yet provided | | |
| 12a. Undelivered Orders (-) | -8,331,143 | -2,222,784 |
| 12b. Unfilled Customer Orders | 685,633 | 105,295 |
| 13. Resources that fund expenses recognized in prior periods | 0 | -651,941 |
| 14. Budgetary offsetting collections and receipts that do not affect net cost of operations | 9,106 | 0 |
| 15. Resources that finance the acquisition of assets | -19,120,713 | -10,859,967 |
| 16. Other resources or adjustments to net obligated resources that do not affect net cost of operations | | |
| 16a. Less: Trust or Special Fund Receipts Related to Exchange in the Entity's Budget (-) | 0 | 0 |
| 16b. Other (+/-) | 110,688 | 0 |
| **17. Total resources used to finance items not part of the net cost of operations** | -26,646,429 | -13,629,397 |
| **18. Total resources used to finance the net cost of operations** | 95,204,902 | 87,362,277 |
| **Components of the Net Cost of Operations that will not Require or Generate Resources in the Current Period:** | | |
| Components Requiring or Generating Resources in Future Periods: | | |
| 19. Increase in annual leave liability | 478,341 | -71,316 |
| 20. Increase in environmental and disposal liability | -344,161 | 1,117,408 |
| 21. Upward/Downward reestimates of credit subsidy expense (+/-) | 0 | 0 |
| 22. Increase in exchange revenue receivable from the the public (-) | 0 | 0 |
| 23. Other (+/-) | 14,770 | 73,202 |
| 24. Total components of Net Cost of Operations that will require or generate resources in future periods | 148,950 | 1,119,294 |
| Components not Requiring or Generating Resources: | | |
| 25. Depreciation and amortization | 13,282,864 | 1,795,095 |
| 26. Revaluation of assets or liabilities (+/-) | 1,641,043 | 3,715,480 |
| 27. Other (+/-) | 11,549,603 | -2,252,331 |
| 28. Total components of Net Cost of Operations that will not require or generate resources | 26,473,510 | 3,258,244 |
| **29. Total components of net cost of operations that will not require or generate resources in the current period** | 26,622,460 | 4,377,538 |
| **30. Net Cost of Operations** | 121,827,362 | 91,739,815 |

*The accompanying notes are an integral part of the financial statements. See notes 1 and 22.*

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# Footnotes to the Principal Statements

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# Note 1. Significant Accounting Policies

## 1.A. Basis of Presentation

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

The Air Force is unable to implement fully all elements of Federal GAAP and the OMB Bulletin No. 01-09 due to limitations of both its financial and nonfinancial processes and feeder systems. Reported values and information for the Air Force's major asset and liability categories are derived largely from the nonfinancial inventory and logistic feeder systems. These systems were designed to support reporting requirements focusing on maintaining accountability over assets and reporting the status of federal appropriations rather than preparing financial statements in accordance with Federal GAAP. As a result, the Air Force currently cannot implement every aspect of GAAP and the OMB Bulletin No. 01-09. The Air Force continues to implement process and system improvements addressing the limitation of its financial and nonfinancial feeder systems.

The Air Force continues to enter material amounts of unsupported accounting entries. Financial and non-financial feeder systems continue to lack sufficient customer identification necessary to accurately process eliminations. The issue has been addressed as part of the Air Force plan for gaining a favorable opinion by FY 2007. This was also disclosed in the DoD Agency wide Footnote 1.

A more detailed explanation of these financial statement elements is provided in the applicable note.

## 1.B. Mission of the 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 Department of Defense (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 accounts used to prepare the statements are classified as entity/nonentity. Entity accounts consist of resources the agency has authority to decide how to use or is legally obligated to use to meet entity obligations. Nonentity accounts are assets held by an entity but are not available for use in operations.

The Air Force incorporates internal controls, reconciliations, management by exception reports, and other management control information into the accounting systems.

When possible, the financial statements are presented on the accrual basis of accounting as required by federal accounting standards.

Following is a list of Air Force account numbers and titles (all accounts are entity accounts unless otherwise noted):

| Air Force Account Number | Title |
|---|---|
| 57 * 0704 | Military Family Housing (O&M and Construction), Air Force |
| 57 * 0810 | Environmental Restoration, Air Force |
| 57 * 1999 | Unclassified Receipts and Expenditures, Air Force |
| 57 * 3010 | Aircraft Procurement, Air Force |
| 57 * 3011 | Procurement of Ammunition, Air Force |
| 57 * 3020 | Missile Procurement, Air Force |
| 57 * 3080 | Other Procurement, Air Force |
| 57 * 3300 | Military Construction, Air Force |
| 57 * 3400 | Operation and Maintenance (O&M), Air Force |
| 57 * 3500 | Military Personnel, Air Force |
| 57 * 3600 | Research, Development, Testing, and Evaluation (RDT&E), AF |
| 57 * 3700 | Personnel, Air Force Reserve |
| 57 * 3730 | Military Construction, Air Force Reserve |
| 57 * 3740 | Operation and Maintenance (O&M), Air Force Reserve |
| 57 * 3830 | Military Construction, Air National Guard |
| 57 * 3840 | Operation and Maintenance (O&M), Air National Guard |
| 57 * 3850 | Personnel, Air National Guard |
| 57 X 5095 | Wildlife Conservation, etc., Military Reservations, Air Force |
| 57 X 8418 | Air Force Cadet Fund |
| 57 X 8928 | Air Force General Gift Fund |
| 57 * 3XXX | Budget Clearing Accounts |
| 57 * 6XXX (Nonentity) | Deposit Fund Accounts |

## 1.C. Appropriations and Funds

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

- General funds are used for financial transactions arising under congressional appropriations, including personnel, operation and maintenance, research and development, procurement, and construction accounts.
- Working Capital fund activities are reported in a separate set of audited financial statements and related footnotes.
- Trust funds represent the receipt and expenditure of funds held in trust by the Air Force for use in carrying out specific purposes or programs in accordance with the terms of the donor, trust agreement, or statute.
- Special funds account for Air Force receipts earmarked for a specific purpose.
- Deposit funds generally are used to: (1) hold assets for which the Air Force is acting as an agent or a custodian or whose distribution awaits legal determination, or (2) account for unidentified remittances.

## 1.D. Basis of Accounting

The Air Force generally records transactions on a budgetary basis and not an accrual accounting basis as is required by Federal GAAP. For FY 2003, the Air Force's financial management systems are unable to meet all of the requirements for full accrual accounting. Many of the Air Force's financial and nonfinancial feeder systems and processes were designed and implemented prior to the issuance of Federal GAAP for federal agencies and, therefore, were not designed to collect and record financial information on the full accrual accounting basis as required by Federal GAAP. The Air Force has undertaken efforts to determine the actions required to bring its financial and nonfinancial feeder systems and processes into compliance with all elements of Federal GAAP. One such action is the current revision of its accounting systems to record transactions based on the United States Government Standard General Ledger (USSGL). Until such time as all of the Air Force's financial and nonfinancial feeder systems and processes are updated to collect and report financial information as required by Federal GAAP, the Air Force's financial data will be based on budgetary transactions (obligations, disbursements, and collections), transactions from nonfinancial feeder systems, and adjusted for known accruals of major items such as payroll expenses, accounts payable, and environmental liabilities. However, when possible, the financial statements are presented on the accrual basis of accounting as required. One example of information presented on the budgetary basis is the data on the Statement of Net Cost (SONC). Much of this information is based on obligations and disbursements and may not always represent all accrued costs.

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

## 1.E. Revenues and Other Financing Sources

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

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

## 1.F. Recognition of Expenses

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

Certain expenses, such as annual and military leave earned but not taken, are financed in the period in which payment is made.

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

## 1.G. Accounting for Intra-governmental Activities

The 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 transactions applicable to the Air Force as though the agency was 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 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 budget appropriations. To the extent this financing ultimately may have been obtained through the issuance of public debt, interest costs have not been capitalized since the Department of the Treasury does not allocate such interest costs to the benefiting agencies.

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

To prepare reliable financial statements, transactions occurring between components or activities within the Air Force must be eliminated. However, the Air Force, as well as the rest of the federal government, cannot accurately identify all intragovernment transactions by customer. The Defense Finance and Accounting Service (DFAS) is responsible for eliminating transactions between components or activities of the Air Force. For FYs 1999 and beyond, seller entities within the Department provided summary seller-side balances for revenue, accounts receivable, and unearned revenue to the buyer-side internal DoD accounting offices. In most cases, the buyer-side records have been adjusted to recognize unrecorded costs and accounts payable. Intra-Air Force balances were then eliminated.

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

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

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

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

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

In addition, the DFAS sites and USACE Finance Center submit reports to the Department of the Treasury, by appropriation, on interagency transfers, collections received, and disbursements issued. The Department of the Treasury then records this information to the applicable Fund Balance with Treasury (FBWT) account maintained in the Treasury's system. Differences between the Air Force's recorded balance in the FBWT accounts and Treasury's FBWT accounts sometimes result and are subsequently reconciled. Material disclosures are provided at Note 3. Differences between accounting offices' detail-level records and Treasury's FBWT accounts are disclosed in Note 21.B, specifically, differences caused by in-transit disbursements and unmatched disbursements (where the specific disbursement has not been recorded in the appropriate accounting offices' detail-level records).

## 1.J. Foreign Currency

The Air Force conducts a significant portion of its operations overseas. The Congress established a special account to handle gains and losses from foreign currency transactions for five general fund appropriations (operation and maintenance, military personnel, military construction, family housing operation and maintenance, and family housing construction). Gains and losses are computed as the variance between the exchange rate current at the date of payment and a budget rate established at the beginning of each fiscal year. Foreign currency fluctuations related to other appropriations require adjustment to the original obligation amount at the time of payment. These currency fluctuations are not identified separately. Material disclosures are provided at Note 7.

## 1.K. Accounts Receivable

As presented in the Balance Sheet statement, accounts receivable include accounts, claims, and refunds receivable from other federal entities or from the public. Allowances for uncollectable accounts due from the public are based upon analysis of collection experience by fund type. The Department does not recognize an allowance for estimated uncollectable amounts from other federal agencies. Claims against other federal agencies are to be resolved between the agencies. Material disclosures are provided at Note 5.

## 1.L. Loans Receivable. As Applicable.

Not applicable.

## 1.M. Inventories and Related Property

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

and upgrades. Likewise, military equipment (previously referred to as National Defense Property, Plant, and Equipment) also includes items which will now be classified as Operating Materials and Supplies.

Implementation of the new accounting principles requires the adjustment of the October 1, 2002, Operating Materials and Supplies balance to recognize the investment, accumulated depreciation, and net book value of military equipment that previously had been expensed and is discussed further in Note 9.

The related property portion of the amount reported on the Inventory and Related Property line includes OM&S. The OM&S are reported at approximate historical cost using Standard Price (SP).

The Air Force uses the Standard Price method because its Operating Materials and Supplies (OM&S) systems were designed for material management rather than accounting. The systems provide accountability and visibility over inventory items. They do not maintain the historical cost data necessary to comply with SFFAS No. 3, "Accounting for Inventory and Related Property." Neither can they directly produce financial transactions using the United States Government Standard General Ledger (USSGL), as required by the Federal Financial Management Improvement Act of 1996 (P.L 104-208). DoD is transitioning to a Moving Average Cost methodology for valuing inventory that, when fully implemented, will allow the Air Force to comply with SFFAS No. 3.

SFFAS No. 3 distinguishes between "inventory held for use" and "inventory held in reserve for future use." There is no management or valuation difference between the two USSGL accounts. Further, the DoD manages only military or government-specific material under normal conditions. Items commonly used in, and available from the commercial sector are not managed in the DoD material management activities. Operational cycles are irregular, and the military risks associated with stock-out positions have no commercial parallel. The DoD holds material based on military need and support for contingencies. Therefore, the Air Force does not attempt to account separately for items held for current or future use.

Related property includes Operating Materials and Supplies (OM&S) and stockpile materials. The OM&S, including munitions not held for use, are valued at SP. Ammunition and munitions are treated as OM&S. For the most part, the Air Force is using the consumption method of accounting for OM&S, expensing material when it is issued to the end user.

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

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

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

Investments in U.S. Treasury securities are reported at cost, net of unamortized premiums or discounts. Premiums or discounts are amortized into interest income over the term of the investment using the effective interest rate method or other method if similar results are obtained. The Air Force's intent is to hold investments to maturity, unless needed to finance claims or otherwise sustain operations. Consequently, a provision is not made for unrealized gains or losses on these securities. Related earnings are allocated to appropriate Air Force activities to be used in accordance with the directions of the donor. Material disclosures are provided at Note 4.

The Air Force invests in both marketable and non-marketable securities. Marketable securities are investments trading on a public market. The two types of non-marketable securities are par value and market based Intragovernmental securities. The Bureau of Public Debt issues non-marketable Par Value Intragovernmental

Securities. Non-marketable, Market Based Intragovernmental Securities mimic marketable securities, but are not traded publicly. See Note 4 for material disclosures.

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

Statement of Federal Financial Accounting Standards No. 23, Eliminating the Category National Defense Property, Plant, and Equipment, establishes new generally accepted accounting principles for valuing and reporting military equipment (e.g. ships, aircraft, combat vehicles, weapons) in federal financial statements. The standard requires the capitalization and depreciation of the cost of military equipment, including the cost of modifications and upgrades, for accounting periods beginning after September 30, 2002.

Until this change in accounting principle, the acquisition costs for military equipment were classified as National Defense Property, Plant, and Equipment (PP&E) and were expensed in the period incurred. Implementation of this new accounting principle required the Department to adjust the October 1, 2002 General PP&E balance to recognize the investment, accumulated depreciation, and net book value of military equipment that previously had been expensed. As discussed further in Note 10, General PP&E, the adjustment was based on data provided by the Bureau of Economic Analysis at the Department of Commerce.

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

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

To bring the Air Force into fuller compliance with federal accounting standards, DoD has issued new property accountability and reporting regulations that require the DoD Components to maintain, in DoD Component property systems, information on all property furnished to contractors. This action and other DoD proposed actions are structured to capture and report the information necessary for compliance with federal accounting standards.

Material disclosures are provided at Note 10.

## 1.P. Advances and Prepayments

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

## 1.Q. Leases

Generally, lease payments are for the rental of equipment vehicles and operating facilities and are classified as either capital or operating leases. When a lease essentially is equivalent to an installment purchase of property (a capital lease) the Air Force records the applicable asset and liability if the value equals or exceeds the current DoD capitalization threshold. The Air Force records the amounts as the lesser of the present value of the rental and other lease payments during the lease term (excluding portions representing executory costs paid to the lessor) or the asset's fair

value. The Air Force deems the use of estimates for these costs as adequate and appropriate due to the relatively low dollar value of capital leases. Imputed interest was necessary to reduce net minimum lease payments to present value calculated at the incremental borrowing rate at the inception of the leases. Leases that do not transfer substantially all of the benefits or risks of ownership are classified as operating leases and are expensed over the period of the lease.

## 1.R. Other Assets

The Air Force conducts business with commercial contractors under two primary types of contracts: fixed price and cost reimbursable. In order to alleviate the potential financial burden on the contractor that long-term contracts can cause, the Air Force provides financing payments. One type of financing payment for real property is based on the percentage of completion. In accordance with the SFFAS No. 1, "Accounting for Selected Assets and Liabilities,' such payments are treated as construction in progress and reported on the General PP&E line and in Note 10, General PP&E, Net. In addition, based on the Federal Acquisition Regulation, the Air Force makes financing payments under fixed price contracts not based on percentage of completion. The Air Force reports these financing payments as advances or prepayments in the "Other Assets" line item. The Air Force treats these payments as advances or prepayments because the Air Force becomes liable only after the contractor delivers the goods. If the contractor does not deliver a satisfactory product, the Air Force is not obligated to reimburse the contractor and the contractor is liable to repay the Air Force for the full amount of the advance. The DoD has completed a review of applicable federal accounting standards; public laws on contract financing; Federal Acquisition Regulation Parts 32, 49, and 52; and the OMB guidance in 5 Code of Federal Regulations Part 1315, "Prompt Payment." The DoD has concluded that SFFAS No. 1 does not address fully or adequately the subject of progress payment accounting and is considering what action is appropriate.

## 1.S. Contingencies and Other Liabilities

The SFFAS No. 5, "Accounting for Liabilities of the Federal Government," defines a contingency as an existing condition, situation, or set of circumstances that involves an uncertainty as to possible gain or loss to the Air Force. The uncertainty will be resolved when one or more future events occur or fail to occur. A contingency is recognized as a liability when a past event or exchange transaction has occurred, a future loss is probable and the amount of loss can be reasonably estimated. Financial statement reporting is limited to disclosure when conditions for liability recognition do not exist but there is at least a reasonable possibility that a loss or additional loss will be incurred. Examples of loss contingencies include the collectability of receivables, pending or threatened litigation, and possible claims and assessments. The Air Force's loss contingencies arising as a result of pending or threatened litigation or claims and assessments occur due to events such as aircraft and vehicle accidents, medical malpractice, property or environmental damages, and contract disputes.

Other liabilities arise as a result of anticipated disposal costs for the Air Force's assets and are classified as either environmental or non-environmental. The recognition of an anticipated environmental disposal liability commences when the asset is placed into service, consistent with SFFAS No. 6, "Accounting for Property, Plant, and Equipment." Based upon the Air Force's policies and consistent with SFFAS No. 5, "Accounting for Liabilities of Federal Government," a non-environmental disposal liability is recognized for an asset when management makes a decision to dispose of the asset. The Department has agreed to the recognition of the nonenvironmental disposal liability for nuclear-powered assets when the asset is placed in service. Such amounts are developed in conjunction with and not easily identifiable separately from environmental disposal costs. Material disclosures are provided at Notes 14 and 15.

## 1.T. Accrued Leave

Civilian annual leave and military leave balances that have been accrued and not used prior to the balance sheet date are reported as liabilities. The liability reported at the end of the fiscal year reflects current pay rates.

## 1.U. Net Position

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

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

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

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

## 1.W. Comparative Data

The Financial Statements and accompanying Notes to the Financial Statements report the financial position and results of operations for FY 2003. Financial statement fluctuations greater than 2 percent of total assets on the Balance Sheet and/or greater than 10 percent between FY 2002 and FY 2003 are explained within the Notes to the Financial Statements.

## 1.X. Unexpended Obligations

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

## Note 2. Nonentity and Entity Assets

| As of September 30, (Amounts in thousands) | 2003 Nonentity | 2003 Entity | 2003 Total | 2002 Non-Entity Assets |
|---|---|---|---|---|
| **1. Intra-governmental Assets:** | | | | |
| A. Fund Balance with Treasury | $ 52,503 | $ 59,714,038 | $ 59,766,541 | $ 54,750 |
| B. Investments | 0 | 712 | 712 | 0 |
| C. Accounts Receivable | -2,580 | 544,008 | 541,428 | 10,913 |
| D. Other Assets | 0 | 339,093 | 339,093 | 0 |
| E. Total Intra-governmental Assets | $ 49,923 | $ 60,597,851 | $ 60,647,774 | $ 65,663 |
| **2. Non-Federal Assets:** | | | | |
| A. Cash and Other Monetary Assets | $ 147,926 | $ 0 | $ 147,926 | $ 140,645 |
| B. Accounts Receivable | 289,787 | 482,713 | 772,500 | 711,546 |
| C. Loans Receivable | 0 | 0 | 0 | 0 |
| D. Inventory & Related Property | 0 | 51,815,832 | 51,815,832 | 0 |
| E. General Property, Plant and Equipment | 0 | 112,786,131 | 112,786,131 | 0 |
| F. Other Assets | 125,940 | 9,786,211 | 9,912,151 | 125,064 |
| G. Total Non-Federal Assets | $ 563,653 | $ 174,870,887 | $ 175,434,540 | $ 977,255 |
| **3. Total Assets:** | $ 613,576 | $ 235,468,738 | $ 236,082,314 | $ 1,042,918 |

## Other Information

### Relevant Information for Comprehension

Assets are categorized as:

- Entity assets consist of resources that the agency has the authority to use, or where management is legally obligated to use funds, to meet entity obligations.
- Nonentity assets are assets held by an entity, but are not available for use in the operations of the entity. The $125,940,237.53 in Other Nonentity Assets are advances to the contractor as reported on the Statement of Accountability (SF 1219) and are part of an advance payment pool agreement with the Massachusetts Institute of Technology or other non-profit institutions. Nonentity Fund Balance With Treasury represents amounts in Air Force deposit and suspense accounts that are not available for Air Force use. Nonentity Accounts Receivables, both Intra-governmental and Non-Federal, represents receivables in cancelled year appropriations that, when collected, go to the Treasury as miscellaneous receipts. The Nonentity Non-Federal Accounts Receivable amount also includes interest receivables on aged debt. Nonentity Cash and Other Monetary Assets represent disbursing officers cash and undeposited collections as reported on the Statement of Accountability. These assets are held by the Air Force disbursing officers as an agent of the Treasury.

### Note Reference

For Additional Line Item discussion, see:

- Note 3, Fund Balance with Treasury
- Note 4, Investments
- Note 5, Accounts Receivable
- Note 6, Other Assets
- Note 7, Cash and Other Monetary Assets
- Note 8, Direct Loan and/or Loan Guarantee Programs
- Note 9, Inventory and Related Property Operating Materials and Supplies, Net
- Note 10, General PP&E, Net

## Note 3. Fund Balance with Treasury

| As of September 30, | 2003 | 2002 |
|---|---|---|
| (Amounts in thousands) | | |
| **1. Fund Balances:** | | |
| A. Appropriated Funds | $ 59,726,905 | $ 47,889,092 |
| B. Revolving Funds | 0 | 0 |
| C. Trust Funds | 3,942 | 11,746 |
| D. Other Fund Types | 35,694 | 41,912 |
| E. Total Fund Balances | $ 59,766,541 | $ 47,942,750 |
| **2. Fund Balances Per Treasury Versus Agency:** | | |
| A. Fund Balance per Treasury | $ 59,766,541 | $ 47,942,751 |
| B. Fund Balance per | 59,766,541 | 47,942,750 |
| C. Reconciling Amount | $ 0 | $ 1 |

## Other Information Related to Fund Balance with Treasury

### Fluctuations

The Appropriated Funds increase of $11,837,813 thousand is directly tied to the supplemental funding received for the Global War on Terrorism (GWOT).

The Trust Fund decrease of $7,804 thousand from year-end FY 2002 results from monies being spent by the Air Force Gift Fund. The Air Force Museum Foundation allocated gift funds to construct a building to be used by the Air & Space Museum located at Wright-Patterson Air Force Base.

The Other Fund Types decrease of $6,218 thousand from year-end FY 2002 is related to the decrease in amounts found in deposit funds. Deposit funds are used as temporary accounts to hold amounts to eventually pay for state and local income taxes, savings bonds, charitable contributions, and employees' organizational dues. The amount held in deposit funds is associated with the timing difference as these deposit funds are held until paid to the appropriate agencies on a quarterly basis.

### Other Information Related to Fund Balance with Treasury

- **Air Force Cadet Fund**—The Cadet Fund is a Revolving Trust Fund account maintained for the benefit of the US Air Force Academy Cadets. The appropriation was initially funded at its inception. From that point on the fund was to be self-sufficient. Collections are received at least equal to any disbursements, and the account revolves funds through the disbursement and collection process with no requirement for additional appropriated funding. The Cadet Fund is an X year account, meaning there is no time limit on obligations.

- **Intragovernmental Paying and Collecting (IPAC)**—The Intragovernmental Payment and Collection (IPAC) differences are reconcilable differences that represent amounts reported by Treasury but not reported by the organization. As of September 30, 2003, there was no IPAC differences over 180 days old. As of September 30, 2002, there was $1,069 thousand of IPAC differences greater than 180 days old. A majority of the differences represent internal DoD transactions and therefore, do not affect the Fund Balance With Treasury (FBWT) at the DoD consolidated level. For individual entity level statements however, these differences would affect the amount reported for FBWT. The Department is working with the DFAS sites, and the Department of Treasury, and a Treasury Department contractor to develop an automated tool to aid in reconciling the Treasury's Statement of Differences. The accounting and paying centers established metrics and implemented monthly reporting requirements for FY 2001. These actions will aid the Air Force in clearing the old balances and establishing better internal controls over the IPAC process.

- **Check Issue Discrepancy**—DFAS is in the process of collecting information for all check issue discrepancy data unsupportable because: (1) records have been lost during deactivation of disbursing offices; (2) the Treasury may not assist in research efforts for transactions over 1-year old; or (3) corrections were processed for transactions that Treasury removed from the check comparison report. Transactions that have no supporting documentation due to one of the preceding situations shall be provided to the Department of the Treasury with a request to remove them from the Treasury Check Comparison Report. The vast majority of the remaining check issue discrepancies are a result of timing differences between the Air Force and the Department of the Treasury for processing checks. The Department does not require that the DoT remove any amounts from the check-issue comparison report since $9,339 thousand was written off during FY2003 to bring the check-issue report balance to $0. Further, no empirical evidence has been presented that demonstrates check issue discrepancies adversely affect the FBWT.

### Note Reference

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

## Note 4. Investments

| As of September 30, | 2003 | | | | | 2002 |
|---|---|---|---|---|---|---|
| | Cost | Amortization Method | Amortized (Premium/ Discount) | Investments, Net | Market Value Disclosure | Investments, Net |
| (Amounts in thousands) | | | | | | |
| **1. Intra-governmental Securities**: | | | | | | |
| A. Marketable | $ 0 | | $ 0 | $ 0 | $ 0 | $ 0 |
| B. Non-Marketable, Par Value | 0 | | 0 | 0 | 0 | 0 |
| C. Non-Marketable, Market-Based | 714 | | (2) | 712 | 0 | 708 |
| D. Subtotal | $ 714 | | $ (2) | $ 712 | $ 0 | $ 708 |
| E. Accrued Interest | $ 0 | | | $ 0 | $ 0 | $ 0 |
| F. Total Intragovernmental Securities | $ 714 | | $ (2) | $ 712 | $ 0 | $ 708 |
| **2. Other Investments:** | $ 0 | | 0 | $ 0 | 0 | $ 0 |

## Other Information

### Fluctuations

The Air Force Gift Fund cash donations that are not going to be used in the immediate future to fund donor designated projects are invested in marketable securities with Treasury. Increases and decreases in the investment cost amount reflect the changes in those investments.

### Relevant Information for Comprehension

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

### Note Reference

See Note Disclosure 1.N., Investments in U.S. Treasury, for additional Air Force policies governing Investments in U.S. Treasury Securities.

# Note 5. Accounts Receivable

| As of September 30, | 2003 | | | 2002 |
|---|---|---|---|---|
| | Gross Amount Due | Allowance for Estimated Uncollectibles | Accounts Receivable, Net | Accounts Receivable, Net |
| (Amounts in thousands) | | | | |
| **1. Intra-governmental Receivables:** | $ 541,429 | N/A | $ 541,429 | $ 443,154 |
| **2. Non-Federal Receivables (From the Public):** | $ 1,003,810 | $ (231,310) | $ 772,500 | $ 1,017,910 |
| **3. Total Accounts Receivable:** | $ 1,545,239 | $ (231,310) | $ 1,313,929 | $ 1,461,064 |

## Allowance Method

The total allowance method is determined at the Air Force departmental level. These departmental level amounts are derived as follows: for closed years receivables and deferred debts in litigation, an allowance rate of 50 percent results in an estimated allowance of $218,408 thousand. Interest allowance of $7,128 thousand is calculated using an average percent of writeoffs to outstanding public accounts receivable over a five-year period starting with FY 1999 data. For Air Force entity receivables, the allowance is computed each year based on the average percent of writeoffs to outstanding public accounts receivable for the last five years resulting in an estimated allowance of $5,774 thousand.

## Other Information

### Relevant Information for Comprehension

As presented on the Consolidated Balance Sheet, accounts receivable include reimbursements receivable and refunds receivable such as out-of-service debts (amounts owed by former service members), contractor debt, and unused travel tickets. It also includes net interest receivable per DoD FMR Vol. 6B guidance. Canceled accounts receivables are reported as nonentity receivables because these amounts are deposited into a Treasury miscellaneous receipt account when collected. A reconciliation between Report on Receivables Due from the Public and the Balance Sheet was accomplished. The differences between the Balance Sheet (line 1C) and Report on Receivables Due from the Public (line 7) include the allowance for estimated receivables that will be uncollected of $231,310 thousand and undistributed collections of $2,905 thousand. Undistributed collections are prorated between public and intragovernmental receivables on the balance sheet based on the percentages of distributed receivables. This reconciliation is performed to ensure the financial statements are in agreement with the public receivables reported to the Department of Treasury.

#### Fluctuations

Intragovernmental Receivables before eliminations decreased by $400,913 thousand from September 2002. We attribute this to the increased focus on reducing accounts receivable balances within DoD agencies. The increase on the financial statement of $98,274 thousand is after intragovernmental Air Force eliminations.

| | **Sep 2003** | **Sep 2002** | **$ Change** |
|---|---|---|---|
| A/R Government before Eliminations | $932,969 | $1,333,882 | $<400,913> |
| Less Intra AF Eliminations | $391,541 | $890,728 | $<499,187> |
| Total | $541,428 | $443,154 | $98,274 |

*(Both columns reflect data in thousands)*

Debts were collected since September 2002 for Air Force Operation & Maintenance funds owed by the Air National Guard of $62,298 thousand, Air Mobility Command of $24,754 thousand, Intrafund Reimbursement of $91,726 thousand, and Air Force Reserve of $91,924 thousand. Debts were collected for Air Force Research, Development, Testing & Evaluation funds owed by Program Management & Support of $45,700 thousand and the Office of the

Secretary of Defense (OSD) of $28,300 thousand. The true change in actual receivable balances is a decrease of $400,913 thousand that we believe is attributable to increased focus on collecting debt since FY 2002. The $499,187 thousand change is elimination activity between Air Force Active, Air Force Reserve, and Air National Guard appropriations.

Public accounts receivables decreased $245,410 thousand since September 2002. Since FY 2002, there is an increased focus on ensuring that all debt is reflected in the accounting records. The overall net decrease during the year resulted from the reversal of a debt worth $299,123 thousand for contract debt against Johnson Controls World Services, Inc (JCWS). This debt was previously in litigation. Memorandum from SAF/FMPB gave the authority to remove the JCWS debt from the Air Force receivables records and reports. The litigation has been settled but it is still unknown the exact amount the Air Force will receive. It is known that the amount will be substantially less than the receivable amount that was booked prior to September 2003. The exact amount of money to be collected by the government from JCWS is still undetermined due to questions related to offsets, closed account legislation, and other issued according to the memorandum.

Another decrease is the over reporting of General Electric (GE) debt at DFAS-Denver departmental level and in the Contractor Debt System worth $316,236 thousand. For year-end 2002, GE debt was reported at DFAS-Denver based on information provided by the Defense Contract Management Agency (DCMA) not realizing the same debt was reported on the Monthly Receivable Management Report (MDMR) file at DFAS-Columbus. The MDMR file reported these debts under a case number instead of using the GE contract numbers as reported by DCMA causing a duplicate reporting of debts.

Public accounts receivables debts in the Contractor Debt System - Columbus (CDS) increased overall by $193,789 thousand since FY 2002. Debts processed in the Mechanization of Contract Administration Services (MOCAS) contract payments increased by $6,810 thousand since September 2002. The reporting of these debts resulted from an OSD initiative to ensure the accountability of all debt on all Services' financial statements. The remaining $169,350 thousand increase results from public accounts receivables reported on the Air Force field sites base-level accounting systems and off-line receivables consolidated at the Denver center.

### Accounts Receivable Over 180 Days

Intragovernmental receivables over 180 days reported on the Quarterly Receivable Report (QRR) are $43,098 thousand. Public receivables over 180 days reported on the QRR is $131,541 thousand excluding $501,736 thousand reported in litigation. Debts in litigation are being pursued in court for collection as such are not subject to write-off or other active collection procedures.

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

### Allocation of Undistributed Collections

The Department of Defense policy is to allocate supported undistributed collections between federal and non-federal categories based on the percentage of Federal and Non-federal Accounts Receivable. Unsupported, undistributed collections should be recorded in the United States Standard General Ledger (USSGL) account 2400, Liability for Deposit Funds, Clearing Accounts and Undeposited Collections. The Air Force follows this allocation procedure.

## Note Reference

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

# Note 6. Other Assets

| As of September 30, | 2003 | 2002 |
|---|---|---|
| (Amounts in thousands) | | |
| **1. Intra-governmental Other Assets:** | | |
| A. Advances and Prepayments | $ 339,093 | $ 4,988 |
| B. Other Assets | 0 | 0 |
| C. Total Intra-governmental Other Assets | $ 339,093 | $ 4,988 |
| **2. Non-Federal Other Assets:** | | |
| A. Outstanding Contract Financing Payments | $ 9,645,299 | $ 7,275,853 |
| B. Other Assets (With the Public) | 266,852 | 260,062 |
| C. Total Non-Federal Other Assets | $ 9,912,151 | $ 7,535,915 |
| **3. Total Other Assets:** | $ 10,251,244 | $ 7,540,903 |

## Other Information Related to Other Assets

### Fluctuations

Advances and Prepayments on line 1.A. increased $334,111 thousand from September 2002. Amounts are recorded based upon elimination data as provided by Air Force trading partners. The increase includes $314,422 thousand, reported by the Air Force Depot Maintenance Activity Group.

The comparison of FY 2003 to FY 2002 for Advances and Prepayments (in thousands):

| | FY 2003 | FY 2002 |
|---|---|---|
| Government advances before accrual | 56.3 | 286.4 |
| Accruals to match seller data | 721,476.9 | 79,927.6 |
| | 721,533.2 | 80,214.0 |
| Less intra Air Force eliminations | 382,739.9 | 75,225.8 |
| Reported advances and prepayments | 339,093.3 | 4,988.2 |

Outstanding Contract Financing Payments increased 33 percent from $7,275,853 thousand to $9,645,299 thousand as reported for FY 2002 and FY 2003 respectively. The increase is predominantly attributed to additional progress payments for the F-22 program, which is experiencing an increase in production.

## Relevant Information for Comprehension

### Other Assets

The $266,852 thousand on line 2.B. is composed of $134,311 thousand in travel advances, $125,610 thousand in advances to contractors as reported on the SF 1219, Statement of Accountability, and $6,931 thousand in other advances to contractors.

Advances to the contractor as reported on the SF 1219, Statement of Accountability, are payments as part of an advance payment pool agreement with Massachusetts Institute of Technology or other non-profit institutions. Advance payment pool agreements are used for the financing of cost-type contracts with non-profit educational or research institutions for experimental, or research and development work, when several contracts or a series of contracts require financing by advance payments.

### Outstanding Contract Financing Payments

The Air Force reports, as an advance and prepayment, all outstanding financing payments for fixed-price contracts that are not based on percentage or stage of completion. Under the contract terms, the Air Force becomes liable only after the contractor delivers the goods in conformance with the contract terms. If the contractor does not deliv-

er a satisfactory product, the Air Force is not obligated to reimburse the contractor for its cost and the contractor is liable to repay the Air Force for the full amount of the outstanding contract finance payments.

### Note Reference

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

## Note 7. Cash and Other Monetary Assets

| As of September 30, | 2003 | 2002 |
|---|---|---|
| (Amounts in thousands) | | |
| 1. Cash | $ 136,195 | $ 116,261 |
| 2. Foreign Currency (non-purchased) | 11,731 | 24,385 |
| 3. Other Monetary Assets | 0 | 0 |
| 4. Total Cash, Foreign Currency, and Other Monetary Assets | $ 147,926 | $ 140,646 |

- Cash—The total of cash resources under the control of the Air Force, which includes coin, paper currency, negotiable instruments, and amounts on deposit in banks and other financial institutions. Cash available for agency use should include petty cash funds and cash held in revolving funds which will not be transferred into the U.S. Government General Fund.
- Foreign Currency—consists of the total U.S. dollar equivalent of non-purchased foreign currencies held in foreign currency fund accounts.
- Other Monetary Assets—includes gold, special drawing rights, and U.S. Reserves in the International Monetary Fund. This category is principally for use by the Department of the Treasury.

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

### Fluctuations

Cash and Foreign Currency increased during FY 2003 due to the requirements associated with Operation Enduring Freedom and Operation Iraqi Freedom. Those requirements have now subsided and both Cash and Foreign Currency have returned to pre-war levels. An ongoing effort to replace foreign currency contracts with U.S. Dollar contracts however, has caused an increased need for U.S. dollars and a corresponding decrease in foreign currency requirements.

### Relevant Information for Comprehension

Cash and Foreign Currency reported is primarily cash held by Disbursing Officers to carry out their paying, collecting and foreign currency accommodation exchange mission. The primary source of the amounts reported is the Standard Form 1219, Statements of Accountability reported by DoD Disbursing Officers.

Foreign Currency is valued using the Department of Treasury Prevailing Rate of Exchange. This rate is the most favorable rate that would legally be available to the U.S. Government's acquisition of foreign currency for its official disbursements and provide currency for exchange of U.S. dollars for troops.

### Note Reference

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

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

## Direct Loan and/or Loan Guarantee Programs

The entity operates the following direct loan and/or Loan guarantee program(s):

- Military Housing Privatization Initiative
- Direct Loan Or Loan Guarantee Program Title

## Other Information

Not applicable.

# Note 9. Inventory and Related Property

| As of September 30, | 2003 | 2002 |
|---|---|---|
| (Amounts in thousands) | | |
| 1. Inventory, Net | $ 0 | $ 0 |
| 2. Operating Materials & Supplies, Net | 51,815,831 | 28,817,563 |
| 3. Stockpile Materials, Net | 0 | 0 |
| 4. Total | $ 51,815,831 | $ 28,817,563 |

# Note 9.A. Inventory, Net

Not applicable.

# Note 9B. Operating Materials and Supplies, Net

| As of September 30, | 2003 | | | 2002 | |
|---|---|---|---|---|---|
| | OM&S Gross Value | Revaluation Allowance | OM&S, Net | OM&S, Net | Valuation Method |
| (Amounts in thousands) | | | | | |
| **1. OM&S Categories:** | | | | | |
| A. Held for Use | $ 38,860,094 | $ 0 | $ 38,860,094 | $ 23,779,740 | SP |
| B. Held for Repair | 12,955,737 | 0 | 12,955,737 | 5,037,823 | SP |
| C. Excess, Obsolete, and Unserviceable | 2,042,114 | -2,042,114 | 0 | 0 | |
| D. Total | $ 53,857,945 | $ -2,042,114 | $ 51,815,831 | $ 28,817,563 | NRV |

**Legend for Valuation Methods:**

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

## Restrictions on OM&S

Not applicable.

## Other Information

### Fluctuations

The major fluctuation between the comparative periods for OM&S was the result of the Air Force complying with the change in accounting principle regarding military equipment which was effective for accounting periods beginning after September 30, 2002. Until the change, some OM&S (aircraft engines, missile engines, electronic pods, and cruise missiles) were considered National PP&E and were expensed at the time of acquisition. This change in accounting principles resulted in an increase in OM&S of approximately $18,597,641 thousand.

The Air Force has a significant increase in the amounts reported as OM&S by the FX accounts and contractor ($1,237,992 thousand). This was due in part to a) increase in program build up, and b) better reporting by the account managers.

The Air Force also reported a significant increase in the amounts reported for munitions, $1,590,025 thousand. This was due, in part, to increased accountability and validating that duplicate data did not reside in two different systems. In FY 2002, munitions data that resided in the Financial Inventory Accounting and Billing System (FIABS) was also considered to be in the Combat Ammunitions System (CAS). Therefore, an adjustment to the CAS data was made using the FIABS data to avoid duplicate reporting. After some additional reviews, this assumption appears to be invalid. Therefore, no adjustment was made to the CAS data for determining which system will report munitions and which national stock numbers are considered to be munitions. Further, the Combat Ammunition System is undergoing a major system modification that will provide better accountability of all Air Force munitions items.

## Information related to OM&S

### General Composition of Operating Materials and Supplies

Operating Materials and Supplies include spare and repair parts, ammunition, tactical missiles, aircraft configuration pods, and centrally managed aircraft engines.

### Balances

In addition to the account balances shown in Table 9.B., the Federal accounting standard requires disclosure of the amount of OM&S held for future use. Except for an immaterial amount of munitions, the Air Force does not have any items considered held for future use.

### Decision Criteria for Identifying the Category to Which OM&S is Assigned

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

The category “Held for Use” includes all issuable materials and is coded within each supply or inventory system as condition codes

The Category “Excess, Obsolete, and Unserviceable” includes all material assigned condition codes H, P & S. The Category “Held for Repair” relates to impaired assets and includes all other condition codes as defined by the Military Standard Transaction Reporting and Accounting Procedures Manual (DoD 4000.25-2-M).

### Changes in the Criteria for Identifying the Category to Which OM&S is Assigned

The category “Held for Use” includes all issuable material. The category “Held for Repair” includes all economically reparable material. Before FY 2002, the Department showed potentially redistributable material, regardless of condition, as “Excess, Obsolete, and Unserviceable”.

The Air Force has not yet implemented “moving average cost,” the DoD approved methodology for reporting historical cost, within any of the supply or inventory accounting systems for OM&S. Consequently, all OM&S assets are valued at standard price, with an allowance for “Excess, Obsolete and Unserviceable.” Under current DoD policy, no allowance is used for serviceable ready to issue items (category “Held for Use”). An allowance equal to 100 percent of standard price however, is used for the category “Excess, Obsolete and Unserviceable.” This allowance results in a net book value of zero which is considered appropriate because the items are coded condemned and therefore have no intrinsic value to the Air Force. The category “Held for Repair” represents suspended, unserviceable (but reparable) items which have a value to the Air Force but that value is less than the items “Held for Use” and greater than “Excess, Obsolete and Unserviceable” items. To date, OSD has not provided sufficient guidance or policy to the Air

Force on the methodology for computing an allowance for "Held for Repair"; therefore, "Held for Repair" is reported at full standard price.

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

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

## Operating Materials and Supplies (OM&S) Value

The OM&S data reported on the financial statements are derived from logistics systems designed for material management purposes. These systems do not maintain the historical cost data necessary to comply with the valuation requirements of the Statement of Federal Financial Accounting Standards (SFFAS) No. 3, "Accounting for Inventory and Related Property." In addition, while these logistics systems provide management information on the accountability and visibility over OM&S items, they do not directly support the categorization of OM&S as held for use, held in reserve for future use, held for repair, or excess, obsolete, and unserviceable. The DoD manages only military- or government-specific material under normal circumstances. Material includes material held due to operational economies. Similarly, material held for use includes material held due to a managerial determination that is should be retained to support departmental contingencies. All OM&S assets are valued at standard price, with an allowance for "Excess, Obsolete, and Unserviceable."

Items commonly used in and available from the commercial sector are not managed in the DoD material management activities. Further, unlike the commercial sector, the Department's operational cycles, based on national need, are irregular. In addition, the military risks associated with stock-out positions (e.g., weapon systems that are not mission capable due to lack of supplies) are totally different from a commercial activity's risk of losing sales. Therefore, the Department does not attempt to account separately for items held for current or future use.

For the most part, the Air Force is using the consumption method of accounting for OM&S, since OM&S is defined in the SFFAS

No. 3 as material which has not yet been issued to the end user. Once issued, the material is expensed. As stated above, current financial and logistics systems cannot fully support the consumption method. According to Federal accounting standards, the consumption method of accounting should be used to account for OM&S unless (1) the amount of OM&S is not significant, (2) OM&S are in the hands of the end-user for use in normal operations, or (3) it is cost-beneficial to expense OM&S when purchased (purchase method).

## Note Reference

See Note Disclosure 1.M., Significant Accounting Policies, for additional discussion on financial reporting requirements and DoD policies governing inventory and related property.

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

## Other Air Force Disclosures

The Air Force provided only minimal accounting data for OM&S that can be used to prepare the financial statements. In most cases, the data provided consisted of only beginning and ending balances for each of the asset accounts "Held for Use; Excess, Obsolete, Unserviceable; and Held for Repair. In other cases, the data provided consisted of only beginning balances, and serviceable and unserviceable ending balances. Without the required additional data (acquisitions, transfers in, amounts consumed, transfers out, trading partner data, etc), DFAS could only report the "net

change" between prior period ending balances and the values reported as current period ending balances. Although, the required additional data is available in some Air Force supply systems, the DFAS general fund accounting system was not developed to receive and translate the transaction codes to report the data. To correct this problem, DFAS is making changes to some accounting systems, and implementing standard interfaces between the Air Force feeder systems and the accounting systems.

Although, the Air Force OM&S systems, in most cases, capture some trading partner data at the transaction-level, there are no electronic interfaces between the Air Force OM&S feeder systems and DFAS accounting systems that can be used to report the data for all items transferred to and from other DoD and Federal Agencies. Consequently, intragovernmental transactions (trading partner data) could not be reconciled. The Air Force and DFAS are in the process of developing processes, methodologies and standard electronic interfaces that will allow the intragovernmental transactions to be reported monthly to the General Accounting and Finance System - Rehost.

## Note 9.C. Stockpile Materials, Net

Not applicable.

## Note 10. General PP&E, Net

| As of September 30, | 2003 | | | | | 2002 |
|---|---|---|---|---|---|---|
| | Depreciation/ Amortization Method | Service Life | Acquisition Value | (Accumulated Depreciation/ Amortization) | Net Book Value | Prior FY Net Book Value |
| (Amounts in thousands) | | | | | | |
| **1. Major Asset Classes:** | | | | | | |
| A. Land | N/A | N/A | $ 416,975 | $ N/A | $ 416,975 | $ 364,091 |
| B. Buildings, Structures, Facilities | S/L | 20 Or 40 | 40,887,338 | (23,620,812) | 17,266,526 | 16,274,354 |
| C. Leasehold Improvements | S/L | lease term | 0 | 0 | 0 | 0 |
| D. Software | S/L | 2-5 or 10 | 23,806 | (24) | 23,782 | 23,715 |
| E. Equipment | S/L | 5 or 10 | 307,451,367 | (215,084,060) | 92,367,307 | 4,701,110 |
| F. Assets Under Capital Lease [1] | S/L | 20 | 409,498 | (221,473) | 188,025 | 203,005 |
| G. Construction-in-Progress | N/A | N/A | 2,523,416 | N/A | 2,523,416 | 2,679,945 |
| H. Other | | | 99 | 0 | 99 | 932 |
| I. Total General PP&E | | | $ 351,712,499 | $ (238,926,369) | $ 112,786,130 | $ 24,247,152 |

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

Legend for Valuation Methods:

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

## Other Information

### Fluctuations

The Air Force in FY 2003, reported an estimated fair market value on land not acquired for, or in connection with General PP&E. This stewardship land was then added to the General land category in error instead of being retained in the Stewardship Land Category. The Air Force advised DFAS that this problem would be corrected in FY 2004. Therefore, an adjustment will be made to the land category when reported by ACES, the real property system.

The Federal Accounting Standards Advisory Board issued Statement of Federal Financial Accounting Standards No. 23, Eliminating the Category National Defense Property, Plant and Equipment, in May 2003. This standard, which is effective for accounting periods beginning after September 30, 2002, establishes Generally Accepted Accounting Principles for valuing and reporting military equipment (e.g. aircraft, satellites, and intercontinental ballistic missiles) in federal financial statements. The Standard requires the capitalization and depreciation of the cost of military equipment, including the cost of modifications and upgrades.

The Department has determined that it is not practicable at this time to accumulate from internal records the information necessary to value military equipment in accordance with generally accepted accounting principles, because the Department is currently working to revise its accounting processes and systems to support the informational

needs of management and compliance with generally accepted accounting principles. In the interim, the Department will base the value of military equipment for financial statement presentation purposes on data provided by the Bureau of Economic Analysis (BEA), Department of Commerce.

The data provided by BEA consists of investment and net book value data for 84 groups of equipment such as aircraft, ships, and combat vehicles. BEA uses Department budget data for equipment acquisitions and actual quantities of equipment items delivered to calculate the Department's annual investment in equipment, after recognizing any equipment transfers or war losses. The Department adjusted BEA data to eliminate equipment items that are not accounted for as military equipment such as spares, munitions, and inventory items, which are accounted for and reported as Inventory and Related Property.

The value of the BEA data provided by the Department to the Air Force to be included in the financial statements for the 4th Quarter 2003 amounted to approximately $292,420,000 thousand less accumulated depreciation of $204,890,000 thousand for a net realized book value of $87,530,000 thousand. A prior period adjustment (not restated) was made to account for prior years military equipment acquisitions and depreciation plus an adjustment to report current year acquisitions and depreciation expense.

The Other asset class on line 1.H. decreased by $833 thousand since September 2002. The Other category represents the timing in harvesting timber. The value of timber is only reported when there is a signed contract to cut the timber and specifies an actual value for the timber to be cut. This value decreases during the year until new contracts are established during the beginning of the next fiscal year.

## Relevant Information for Comprehension

Personal property in the Air Force consists of General Equipment, Automated Data Processing (ADP) hardware, Medical Equipment, Special Tools and Test Equipment (ST/STE) and Military Equipment.

## Other Air Force Disclosures

The Air Force used FY 2002 ending data for Special Tools, Special Test Equipment (ST/STE) and for Medical Equipment for the FY 2003 4th Quarter reports. The FY 2002 values were used because: a) the two systems previously used to report ST/STE have been turned off and are scheduled to be replaced by AFEMS by the end of FY 2003, and b) the MEDLOG system cannot provide a 4th Quarter FY 2003 update. This system is scheduled to be replaced by the Department's Medical Logistics Supply Support (DMLSS) system in FY 2004.

The Air Force used the 2nd Qtr 2003 ending balances to report the value of assets that had not passed the required edit checks (missing historical cost, acquisition dates or serial numbers) and therefore had not been included in the values reported by the Air Force Equipment Management System (AFEMS) for the 4th Quarter FY2003 reports. This data was used because the processes previously established to report this data could not be relied on due to unexplained large fluctuations. The Air Force is currently working this "in suspense" data problem to assure that all assets are properly recorded and depreciated by AFEMS for the audited financial statements at year end.

The value of the Air Force's General PP&E real property in the possession of contractors is included in the values reported above for the Major Asset Classes of Land and Buildings, Structures, and Facilities. The value of General PP&E personal property (Major Asset Classes of Software and Equipment) does not include all of the General PP&E above the DoD capitalization threshold in the possession of contractors. The net book amount of such property is immaterial in relation to the total General PP&E net book value. In accordance with an approved strategy with the OMB, the General Accounting Office and the Inspector General, DOD, the Department is developing new policies and a contractor reporting process to capture General PP&E information for future reporting purposes for compliance with Generally Accepted Accounting Principles.

## Note Reference

See Note Disclosure 1.O., Significant Accounting Policies for additional discussion on financial reporting requirements and DoD policies governing General Property, Plant and Equipment (PP&E).

# Note 10.A. Assets Under Capital Lease

| As of September 30, | 2003 | 2002 |
|---|---|---|
| (Amounts in thousands) | | |
| **1. Entity as Lessee, Assets Under Capital Lease:** | | |
| A. Land and Buildings | $ 408,540 | $ 408,540 |
| B. Equipment | 958 | 958 |
| C. Other | 0 | 0 |
| D. Accumulated Amortization | (221,473) | (206,493) |
| E. Total Capital Leases | $ 188,025 | $ 203,005 |

## Description of Lease Arrangements

The Air Force is the leasee in twelve capital leases. Eleven are for Military Family Housing acquired through Section 801 Family Housing Program, and one is for a piece of medical equipment. The leased items are capitalized and reported as an asset when the costs of the items exceed the capitalization threshold. Leased items not meeting the capitalization threshold are expensed. All leases prior to FY 1992 are funded on a fiscal year basis. This correlates to six of the Military Family Housing Leases.

## Other Information

Not applicable.

# Note 11. Liabilities Not Covered and Covered by Budgetary Resources

| As of September 30, | 2003 | | | 2002 |
|---|---|---|---|---|
| (Amounts in thousands) | Covered by Budgetary Resources | Not Covered by Budgetary Resources | Total | Not Covered by Budgetary Resources |
| **1. Intra-governmental Liabilities:** | | | | |
| A. Accounts Payable | $ 1,413,940 | $ 0 | $ 1,413,940 | $ 3,957 |
| B. Debt | 0 | 0 | 0 | 134 |
| C. Environmental Liabilities | 0 | 0 | 0 | 0 |
| D. Other | 924,648 | 699,256 | 1,623,904 | 609,275 |
| E. Total Intra-governmental Liabilities | $ 2,338,588 | $ 699,256 | $ 3,037,844 | $ 613,366 |
| **2. Non-Federal Liabilities:** | | | | |
| A. Accounts Payable | $ 7,080,910 | $ 0 | $ 7,080,910 | $ 0 |
| B. Military Retirement Benefits and Other Employment-Related Actuarial Liabilities | 0 | 1,262,268 | 1,262,268 | 1,211,045 |
| C. Environmental Liabilities | 549,849 | 7,560,554 | 8,110,403 | 8,454,564 |
| D. Loan Guarantee Liability | 0 | 0 | 0 | 0 |
| E. Other Liabilities | 1,598,648 | 2,922,241 | 4,520,889 | 2,454,562 |
| F. Total Non-Federal Liabilities | $ 9,229,407 | $ 11,745,063 | $ 20,974,470 | $ 12,120,171 |
| **3. Total Liabilities:** | $ 11,567,995 | $ 12,444,319 | $ 24,012,314 | $ 12,733,537 |

## Other Information

### Liabilities Not Covered and Covered by Budgetary Resources

Liabilities that are not considered covered by realized budgetary resources as of the Balance Sheet date. Budgetary resources encompass the following:

- New budget authority.
- Spending authority from offsetting collections (credited to an appropriation or fund account).
- Recoveries of unexpired budget authority through downward adjustments of prior-year obligations.
- Unobligated balances of budgetary resources at the beginning of the year or net transfers of prior-year balances during the year.
- Borrowing authority or permanent indefinite appropriations, which have been enacted and signed into law as of the Balance Sheet date, provided that the resources may be apportioned by the OMB without further action by the Congress or without a contingency first having to be met.

### Liabilities Covered by Budgetary Resources

Resources incurred by the reporting entity which are covered by realized budget resources as of the Balance Sheet date. Budgetary resources encompass not only new budget authority, but also other resources available to cover liabilities for specified purposes in a given year. Available budgetary resources include the following:

- New budget authority.
- Spending authority from offsetting collections (credited to an appropriation or fund account).
- Recoveries of unexpired budget authority through downward adjustments of prior-year obligations.
- Unobligated balances of budgetary resources at the beginning of the year or net transfers of prior-year balances during the year.
- Borrowing authority or permanent indefinite appropriations, which have been enacted and signed into law as of the Balance Sheet date, provided that the resources may be apportioned by the OMB without further action by the Congress or without a contingency first having to be met.

## Fluctuations and Abnormalities

Explanations for fluctuations are explained in the individual footnotes. See "Note Reference" section below for the related footnotes.

## Information Related to Liabilities Covered by Budgetary Resources

### Other Liability Disclosures

Other Intragovernmental Liabilities Covered by Budgetary Resources consists of $145,290 thousand in advances from others, $23,503 thousand in deposit fund liabilities, $449,282 thousand in resources payable to treasury relative to cancelled accounts receivable, $273,536 thousand in Disbursing Officer cash liability, and $33,037 thousand in government contributions for employee benefits.

Other Nonfederal Liabilities Covered by Budgetary Resources consists of $1,289,522 thousand in accrued payroll and benefits liabilities for military and civilians, $5,143 thousand in Temporary Early Retirement Authority liabilities, $206,764 thousand in capital lease liabilities, $68,038 thousand in advances from others, and $29,181 thousand in liabilities for deposit fund clearing accounts and undeposited collections.

## Information Related to Liabilities Not Covered by Budgetary Resources

### Other Liability Disclosures

Other Intragovernmental Liabilities Not Covered by Budgetary Resources consists of $252,090 thousand in judgement fund liabilities, $304,751 thousand in Federal Employees Compensation Act (FECA) reimbursement to the

Department of Labor (DoL), $27,488 thousand in unemployment compensation liabilities, $3,249 thousand in education benefit liabilities, and $111,677 thousand in custodial liabilities.

Other Nonfederal Liabilities Not Covered by Budgetary Resources consists of $445,939 thousand in accounts payable cancelled appropriations, $76,569 thousand in nonenvironmental disposal liabilities, $57,037 thousand in capital lease liabilities, $189,231 thousand in contingent liabilities, $2,152,620 thousand in accrued annual leave liabilities for military and civilians, and $845 thousand in accrued interest liability.

## Note Reference

For Additional Line Item discussion, see:

- Note 12, Accounts Payable
- Note 13, Debt
- Note 14, Environmental Liabilities and Disposal Liabilities
- Note 15, Other Liabilities
- Note 16, Commitments and Contingencies
- Note 17, Military Retirement Benefits and Other Employment Related Actuarial Liabilities
- Note 21B, Disclosures Related to Problem Disbursements, Intransit Disbursements and Suspense/Budget Clearing Accounts

# Note 12. Accounts Payable

| As of September 30, | 2003 | | | 2002 |
|---|---|---|---|---|
| (Amounts in thousands) | Accounts Payable | Interest, Penalties, and Administrative Fees | Total | Total |
| **1. Intra-governmental Payables:** | $ 1,413,940 | N/A | $ 1,413,940 | $ 1,124,734 |
| **2. Non-Federal Payables (to the Public):** | $ 7,080,909 | $ 0 | $ 7,080,909 | $ 6,206,966 |
| **3. Total** | $ 8,494,849 | $ 0 | $ 8,494,849 | $ 7,331,700 |

## Other Information

Intragovernmental accounts payable consists of amounts owed to other federal agencies for goods or services ordered and received but not yet paid. Interest, penalties, and administrative fees are not applicable to intragovernmental payables. Nonfederal Payables (to the Public) are payments to nonfederal governmental entities.

## Other Information Related to Accounts Payable

### Fluctuations

Intragovernmental accounts payable increased $289,206 thousand. This was directly affected by the elimination process, which requires the accrual of accounts payables to agree with Air Force trading partner seller data.

Comparison prior to eliminations:

| | **Sep 2003** (in thousands) | **Sep 2002** (in thousands) | **$ Change** (in thousands) |
|---|---|---|---|
| Intragovernmental accounts payable before eliminations | $1,805,481 | $2,015,462 | $(209,981) |
| Less Intra Air Force eliminations | $391,541 | $890,728 | $499,187 |
| **Total** | **$1,413,940** | **$1,124,734** | **$289,206** |

Accounts payable public increased by $873,944 thousand. Other Procurement—Air Force program entity reflects a $283,528 thousand increase in public accounts payable, Aircraft Procurement—Air Force program entity reflects a $520,041 thousand decrease in public accounts payable, Missile Procurement—Air Force program entity reflects a $174,509 thousand increase in public accounts payable, Other Procurement—Air Force program reflects a $707,741 thousand increase in public accounts payable and Operations and Maintenance—Air Force program entity shows an increase in public accounts payable of $498,421 thousand. The remaining $13,314 thousand increase is shared by a number of other program entities. Over 90 percent of the $873,944 thousand increase can be attributed to classified Air Force Special Programs. Further information regarding that portion is not available.

### Intragovernmental Eliminations

For the majority of intra-agency sales, the Air Force's feeder and DFAS accounting systems do not capture trading partner data at the transaction level in a manner that facilitates trading partner aggregations. Therefore, the Air Force was unable to reconcile intragovernmental accounts payable to the related intragovernmental accounts receivable that generated the payable. The DoD and Air Force intend to develop long-term systems improvements that will include sufficient up-front edits and controls to eliminate the need for after-the-fact reconciliations. The volume of intragovernmental transactions is so large that after-the-fact reconciliation can not be accomplished with the existing or foreseeable resources.

The DoD summary level seller accounts receivables were compared to the Air Force accounts payable. An adjustment was posted to the Air Force accounts payable based on the comparison with the accounts receivable of the DoD components providing goods or services to the Air Force. Positive differences were treated as unrecognized accounts payable and in the case of the Air Force, accounts payable were adjusted upwards in the amount of $986,462 thousand.

### Allocation of Undistributed Disbursements

The Department of Defense policy is to allocate supported undistributed disbursements between federal and nonfederal categories based on the percentage of Federal and Nonfederal accounts payable. Unsupported undistributed disbursements should be recorded in United States Standard General Ledger (USSGL) account 2120, Disbursements in Transit. The Air Force followed this allocation policy.

### Note Reference

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

## Note 13. Debt

| As of September 30, | 2003 | | | 2002 |
|---|---|---|---|---|
| (Amounts in thousands) | Beginning Balance | Net Borrowings | Ending Balance | Ending Balance |
| **Agency Debt:** | | | | |
| Debt to Other Federal Agencies | 0 | 0 | 0 | 134 |
| **Total Debt:** | $ 0 | $ 0 | $ 0 | $ 134 |
| **Classification of Debt:** | | | | |
| Intragovernmental Total Debt | | | $ 0 | $ 134 |

## Other Information

### Relevant Information for Comprehension

**Fluctuation.** Education benefits that are provided for certain involuntary and voluntary separatees are paid from the DoD Education Benefit Fund. The Air Force portion of the unfunded interest liability for education benefits for FY

2003 of $67.2 thousand is now being reported as Other Intragovernmental Liabilities. For FY 2002, the unfunded interest liability of $134.1 thousand was reported as Debt.

### Note Reference

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

## Note 14. Environmental Liabilities and Disposal Liabilities

| As of September 30, (Amounts in thousands) | 2003 | | | 2002 |
|---|---|---|---|---|
| | Current Liability | Noncurrent Liability | Total | Total |
| **Environmental Liabilities:** | | | | |
| Non-Federal: | | | | |
| Accrued Environmental Restoration (DERP funded) Costs: | | | | |
| Active Installations—Environmental Restoration (ER) | $ 384,307 | $ 4,517,581 | $ 4,901,888 | $ 5,237,429 |
| Active Installations—ER for Closed Ranges | 0 | 838,172 | 838,172 | 705,700 |
| Other Accrued Environmental Costs (Non-DERP funds) | | | | |
| Active Installations—Environmental Corrective Action | 0 | 204,341 | 204,341 | 175,043 |
| Active Installations—Environmental Closure Requirements | 0 | 66,454 | 66,454 | 65,182 |
| Base Realignment and Closure (BRAC) | | | | |
| BRAC Installations—Environmental Restoration (ER) | 75,153 | 1,833,847 | 1,909,000 | 2,083,724 |
| BRAC Installations—ER for Transferring Ranges | 0 | 0 | 0 | 0 |
| BRAC Installations—Environmental Corrective Action | 5,139 | 134,817 | 139,956 | 136,198 |
| Environmental Disposal for Weapons Systems Programs | | | | |
| Other National Defense Weapons Systems | 0 | 50,592 | 50,592 | 51,288 |
| **Total Non-Federal Environmental Liabilities:** | $ 464,599 | $ 7,645,804 | $ 8,110,403 | $ 8,454,564 |

## Other Information Related to Environmental Liabilities

### Fluctuations

Accrued Environmental Restoration Costs (DERP funded) Active Installations - Environmental Restoration for Closed Ranges increased $132,472 thousand, or 19 percent, from $705,700 thousand to $838,172 thousand as reported for FY 2002 and FY 2003 respectively. This increase is a result of the identification of 19 additional areas.

Other Accrued Environmental Costs (Non-DERP funds) Active Installations - Environmental Corrective Action increased $29,298 thousand, or 17 percent, from $175,043 thousand to $204,341 thousand as reported for FY 2002 and FY 2003 respectively. The total liability reported for September 30, 2002 was $175,043 thousand, however one figure was inadvertently reported in actual dollars rather than thousands. Had total cost to complete been reported correctly, the total liability would have been $169,800 thousand. The total liability for the non-DERP, Non-BRAC cleanup results in a 19 percent increase from the corrected figure of $169,800 thousand as of September 30, 2002 to $204,341 thousand as of September 30, 2003. The total change of $34,541 thousand is comprised of a decrease of $18,418 thousand in expenditures, an increase of $2,348 thousand in revaluations, and an increase of $50,611 which reflects identification of 168 new sites during FY 2003. The total number of non-DERP, non-BRAC cleanup sites grew from 712 as of September 30, 2002 to 715 at September 30, 2003, which indicates that 165 sites were eliminated during the fiscal year.

## General Disclosures

### Accrued Environmental Restoration Costs (DERP funded) Active Installations—Environmental Restoration and Other Accrued Environmental Costs (Non-DERP funds) Active Installations—Environmental Corrective Action

Environmental cleanup liabilities are incurred in connection with the Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA) and the Resource Conservation and Recovery Act (RCRA). Cost estimates are performed using the Remedial Action Cost Engineering and Requirements System (RACER) unless there is a historic comparable project, or there is a specific bid or independent government cost estimate for the project. The liability amount is composed of the sum of several stages of activity and not necessarily contained in a single estimate or contract.

The change in environmental cleanup liability during a reporting period is comprised of revaluations of the cost-to-complete cleanup of sites that existed at the beginning of the period plus the cost-to-complete cleanup for new sites introduced during the reporting period, less amounts expensed in the program during the reporting period. The beginning environmental cleanup liability plus the cost-to-complete new sites added during the period, plus or minus changes in cost-to-complete estimates (revaluations) during the period is equal to the ending environmental cleanup liability for the period. Because the Defense Environmental Restoration Program (DERP) is accounted for as a totally self-contained program, all direct and indirect costs of the program are captured and reported.

Non-DERP non-Base Realignment and Closure (non-BRAC) environmental cleanup liabilities represent corrective actions required under RCRA law. These environmental cleanup liabilities are estimated in the same manner as DERP environmental cleanup liabilities. The change in non-DERP non-BRAC environmental cleanup liabilities during a reporting period is comprised of revaluations of the cost-to-complete for sites that existed at the beginning of the period plus the cost-to-complete for new sites added during the reporting period less amounts expensed during the period. Because the non-DERP non-BRAC environmental cleanup activity is a part of general funding achieved using 3400 appropriation funds, there is no special accounting for the costs of the entire program. Therefore, the costs captured for the non-DERP non-BRAC environmental cleanup reflect only direct costs. Because this program was not tracked and appropriated specifically there was no accounting specific to this program. Expense codes for this program were established in 1999 and implemented in fiscal year 2000. Therefore, the expense portion of the estimate has no significant history. Because of the lack of expense history for the program, there is no reliable data for estimating the current portion of the non-DERP non-BRAC environmental cleanup liability. It is believed that the current portion of the environmental cleanup liability in this area is relatively small and not material in the classification of liabilities. Because the non-DERP non-BRAC environmental cleanup liabilities are only estimated between 1 July and 1 September of each year, there is no significant change other than at fiscal year end for non-DERP non-BRAC environmental liabilities. On less than an annual basis the only change to the liability estimate in this area is the amount recorded as expensed during the reporting period.

### Accrued Environmental Restoration Costs (DERP funded) Active Installations—Environmental Restorations for Closed Ranges

The environmental cleanup of military ranges is governed by the "Military Munitions Rule" in 40 CFR 266.201. Environmental cleanup liabilities on ranges refer only to munitions related activities. Other actions are captured under the DERP, BRAC and non-DERP non-BRAC environmental cleanup categories. Additionally, environmental cleanup liabilities are reported only for closed ranges. The Air Force had 509 ranges at September 30, 2002 of which 268 are considered operational ranges. The environmental cleanup liability is reported only for closed ranges that number 260 as of September 30, 2003 (236 closed, 18 transferred, 6 transferring).

Environmental cleanup areas within a closed range are referred to as "munitions response areas" (MRAs). As studies are done to find munitions related contamination on closed ranges the number of sites is expected to rise. At September 30, 2002 there were 241 areas comprised of closed ranges that resulted in an estimated environmental

cleanup liability of about $705,700 thousand and has increased to 260 areas with an estimated cost of $838,172 thousand at September 30, 2003. As investigations progress, the number of sites will increase to reflect specific areas of polluted and non-polluted sites. The Air Force expects the number of sites reported to increase as pollution is discovered and sites are defined in areas less than the total boundary of the closed range. For example, one closed range of 100 acres may become three sites - one of five acres with pollution A, one of 15 acres with pollution B and the remaining 80 acres with no pollution found. Thus, one closed range becomes three sites and each site has its own cost-to-complete cleanup estimate. The sum of the individual site cost-to-complete cleanup becomes the environmental cleanup liability for closed ranges. Current policy is to investigate all closed ranges by the end of 2007. The environmental cleanup for closed ranges is in its infancy and the total liability is expected to increase significantly over the coming years as investigations progress.

Although there are no stated standards for the environmental cleanup of closed ranges, the Air Force has implemented the cleanup standards used by the Formerly Used Defense Site (FUDS) operation to determine a cost-to-complete for the environmental cleanup. Over time implementation of these standards of cleanup are highly likely to change and are expected to vary significantly from site to site depending upon the specific site related terrain and geology. For example, the standard cleanup levels for FUDS may not apply in the situation of a dense rain forest because the standard would require the complete destruction of the forest to achieve the cleanup standards established. It is expected that there will be significant changes in the cleanup standards that eventually will be applied on a case by case basis for munitions response requirements.

As investigations progress it is expected the environmental cleanup liability for closed ranges will increase materially. The liability for environmental cleanup will reflect direct costs. Also, the lack of any history of expenses for the environmental cleanup will make it impossible to estimate current liabilities reliably for some time.

### Other Accrued Environmental Costs (Non-DERP funds) Active Installations—Environmental Closure Requirements

Environmental closure liabilities are incurred under RCRA with the cost-to-complete closure reported for RCRA permitted facilities. Cost estimates are prepared under assumptions of a “clean close” as defined in the RCRA law and estimated using RACER in the absence of a specific contract cost or bid. The specific facilities reported cover permitted landfills, underground storage tanks (USTs) and treatment, storage and disposal facilities (TSDFs).

The current accounting system does not capture expenses of environmental closures. Therefore, environmental closure liabilities are reversed at the end of each year and replaced with the most recent cost-to-complete closure estimate. Disposal liabilities are presented as an accrued amount for the life of the RCRA permitted facilities and the total liability is presented in the year end narrative. The accounting standard requires full cost be recognized for closure liability. Closure liabilities recognized by the Air Force cover only direct costs. There is no reliable cost accounting system to determine indirect closure costs. This is not considered material in the cost estimates because indirect costs incurred would not happen for at least 20 years and in many cases far beyond 20 years. The present value of such costs would be negligible in recognition of closure liabilities.

The environmental closure liability for landfills is based on the proportion of the landfill used as of the reporting date. This estimate includes the cost of capping the fill, as well as, 30 years of monitoring required by Federal regulations.

Reporting of landfill closure liability is not in conformance with the accounting standard. The standard would recognize all future costs regardless of timing. The Air Force recognizes only the initial closure. A landfill cap typically requires replacement every 20 to 40 years. An estimation of current costs based on all future costs, regardless of timing, would result in an infinite liability. This appears meaningless and not the intent of the standard. Therefore, the Air Force reports only the cost of the initial cap required to close a landfill. The Air Force believes this reporting is more meaningful. The present value of the future caps, those after the initial cap, would be negligible.

UST closure liabilities are based on an assumed life of 20 years and two years of monitoring with closure costs estimated for a "clean close." "Clean close" is defined in the Federal regulations.

TSDF closure liabilities are based on an assumed life of 30 years. Disposal costs include two years of monitoring with closure costs estimated for a "clean close." "Clean close" is defined in the Federal regulations.

### Base Realignment and Closure (BRAC) Installations—Environmental Restoration and Environmental Corrective Action

For FY 2003, the Air Force has estimated and reported its BRAC environmental future liabilities. The Air Force Real Property Agency (AFRPA) estimates a $2,048,955 thousand total environmental liability as of September 30, 2003. This amount includes all cleanup requirements to meet applicable laws and regulatory requirements and to transfer property. However, this amount does not include Land Use Control/Institutional Control costs beyond system operations associated with property transfer. Cost estimates are assigned to current operating periods using the Remedial Action Cost Engineering and Requirements System (RACER).

### Environmental Disposal for Weapons Systems Programs—Other National Defense Weapon Systems

The September 20, 2003 environmental disposal liability of $50,592 thousand in Other National Defense Weapon Systems includes strategic and tactical active missiles, inactive missiles, and missile motors. The Air Force identified $48,636 thousand in environmental liability for the disposal of the Minuteman III and Peacekeeper strategic missile motors and $1,956 thousand for the disposal of tactical active and inactive missiles.

### Reporting of Estimates

Our financial statements are prepared in accordance with accounting principles generally accepted in the United States ("GAAP"). These accounting principles require us to make certain estimates, judgments and assumptions. We believe that the estimates, judgments and assumptions upon which we rely are reasonable based upon information available to us at the time that these estimates, judgments and assumptions are made. These estimates, judgments and assumptions can affect the reported amounts of environmental liabilities as of the date of the financial statements.

Our financial statements would be affected to the extent there are material differences between these estimates and actual results. In many cases, the accounting treatment of a particular transaction specifically is dictated by the Department of Defense Financial Management Regulations and does not require management's judgment in its application. There also are areas in which management judgment in selecting any available alternative could produce a materially different result.

## Other Air Force Disclosures

### Other Accrued Environmental Costs (Non-DERP funds) Active Installations—Environmental Closure Requirements

The recognized closure liability for Resource Conservation and Recovery Act (RCRA) permitted facilities combine treatment, storage, and disposal facilities (TSDFs) for hazardous waste, landfills, and underground storage tanks (USTs) increased from $65,182 thousand to $66,454 thousand during fiscal year 2003. The total liability, however, decreased significantly. The decrease in total liability was due to an incorrect figure reported at September 30, 2002. The total closure liability for TSDF's reported September 30, 2002 was $226,100 thousand. The total at September 30, 2003 is $13,400 thousand, significantly lower because two of last year's figures inadvertently were reported in actual dollars rather than thousands. Had total closure liability at September 30, 2002 been reported correctly, the total TSDF liability only would have been $14,800 thousand. The components for the ending liability figures for FY 2002 and FY 2003 are shown below. The recognized liability is the amount reflected on the financial statements.

| | FY 2003 (amounts in thousands) | | FY 2002 (amounts in thousands) | |
|---|---|---|---|---|
| | *Total* | *Recognized* | *Total* | *Recognized* |
| TSDFs | $13,400 | $5,000 | $226,100 | $39,700 |
| Landfills | $132,100 | $35,454 | $80,000 | $16,700 |
| USTs | $51,200 | $26,000 | $75,300 | $8,782 |
| **Total** | **$196,700** | **$66,454** | **$381,400** | **$65,182** |

The increase in recognized liability reflects reporting of additional USTs, and landfills not reported previously. Closure liabilities reflect a continued refinement and re-evaluation of cost estimating procedures and data fidelity. More installations have implemented the validated, verified and accredited cost-estimating tool (RACER). Overall, TSDF and UST liability decreased, and landfill closure liability increased due to the identification of three previously unreported landfills.

## Note Reference

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

# Note 15.A. Other Liabilities

| As of September 30, | 2003 | | | 2002 |
|---|---|---|---|---|
| (Amounts in thousands) | Current Liability | Noncurrent Liability | Total | Total |
| **Intra-governmental:** | | | | |
| Advances from Others | $ 145,290 | $ 0 | $ 145,290 | $ 213,843 |
| Deposit Funds and Suspense Account Liabilities | 23,503 | 0 | 23,503 | 15,596 |
| Resources Payable to Treasury | 0 | 0 | 0 | 1,006,978 |
| Disbursing Officer Cash | 273,536 | 0 | 273,536 | 265,295 |
| Judgement Fund Liabilities | 149,054 | 103,037 | 252,091 | 303,600 |
| FECA Reimbursement to the Department of Labor | 132,538 | 172,212 | 304,750 | 305,675 |
| Other Liabilities | 624,734 | 0 | 624,734 | 68,101 |
| Total Intra-governmental Other Liabilities | $ 1,348,655 | $ 275,249 | $ 1,623,904 | $ 2,179,088 |
| **Non-Federal:** | | | | |
| Accrued Funded Payroll and Benefits | $ 1,289,522 | $ 0 | $ 1,289,522 | $ 1,166,899 |
| Advances from Others | 68,038 | 0 | 68,038 | 93,234 |
| Deposit Funds and Suspense Accounts | 29,181 | 0 | 29,181 | 39,154 |
| Temporary Early Retirement Authority | 1,827 | 3,316 | 5,143 | 16,900 |
| Nonenvironmental Disposal Liabilities: | | | | |
| Excess/Obsolete Structures | 55,487 | 15,202 | 70,689 | 62,581 |
| Conventional Munitions Disposal | 0 | 5,880 | 5,880 | 0 |
| Other | 0 | 0 | 0 | 0 |
| Accounts Payable—Cancelled Appropriations | 358,656 | 87,282 | 445,938 | 452,919 |
| Accrued Unfunded Annual Leave | 2,152,620 | 0 | 2,152,620 | 1,674,276 |
| Capital Lease Liability | 31,458 | 232,344 | 263,802 | 279,418 |
| Other Liabilities | 845 | 189,231 | 190,076 | 201,806 |
| **Total Non-Federal Other Liabilities** | $ 3,987,634 | $ 533,255 | $ 4,520,889 | $ 3,987,187 |
| **Total Other Liabilities:** | $ 5,336,289 | $ 808,504 | $ 6,144,793 | $ 6,166,275 |

## Other Information Pertaining to Other Liabilities

### Intragovernmental Fluctuations

The $68,553 thousand decrease in Advances from Others on Line 1.A. in comparison to 30 September 2002 is due to the timing of the receipt and execution of orders which causes variations in the year-end balances.

The deposit funds and suspense account liabilities on Line 1.C. increase of $7,907 thousand is related to Intragovernmental Paying and Collection (IPAC) transactions that are initially posted to account 57 F 3885 and the Military Thrift Saving Plan posted to account 57 F 3882. IPAC transactions are aged and monitored to ensure they are cleared timely. The Military Thrift Saving Plan represents a timing difference as the National Finance Center post amounts into each military member's account.

The Resources Payable to Treasury on Line 1.D. decreased by $1,006,978 thousand due to the reclassification of cancelled authority for recording accounts receivables. DFAS-Denver was the only Center using USSGL 2970, Resources Payable to Treasury, as the contra to receivables in cancelled accounts. Amount if collected will go to Treasury as miscellaneous receipts. This was the contra account provided to us to use when populating the CFO Reporting System with posting logic. According to draft guidance from DFAS-Arlington, the accounting for expired and cancelled authority for other than special and trust funds should be reported under USSGL 2990, Other Liabilities. USSGL 2990 cross walk to Other Liabilities on the Balance Sheet and Line 1.K. on Note 15A.

The $8,241 thousand increase in Disbursing Officer Cash on Line 1.E. is primarily attributed to war effort requirements in support of Operation Iraqi Freedom.

Balances in Accounts Payable - Cancelled Appropriations on Line 1.G. for $220,667 thousand was reclassified from federal to non-federal for elimination balancing. Cancelled accounts payable based on accounts receivable data between trading partners within government if collected will go to the Treasury as miscellaneous receipts. Therefore, you have to reclassify cancelled accounts payable to non-federal.

Judgement Fund liabilities of $252,091 thousand result from contractor claims under the Contract Disputes Act on Air Force contracts that have been adjudicated by a court or a board in favor of the contractor. Initially, the Department of the Treasury pays the monetary awards to the contractor. The Air Force must subsequently reimburse the Treasury's Judgement Fund for the amount that was paid to the contractors. The decrease during FY 2003 is due to the Air Force paying approximately $52,509 thousand more to Treasury on debts owed than Treasury billed to the Air Force in new debts.

No seller data was matched to Air Force closed account payables. Therefore, all cancelled accounts payables are reported as public.

## Other Liabilities

Other Liabilities includes unsupported undistributed collections which are recorded in United States Standard General Ledger (USSGL) account 2400, Liability for Deposit Funds, Clearing Accounts, and Undeposited Collections.

The Other Liabilities on Line 1.K. increase of $525,901 thousand represents $33,037 thousand in government contribution of employee benefits, $27,489 thousand in other unfunded unemployment compensation liabilities. The reclassification of Resources Payable to Treasury increased by $449,288 thousand to report cancelled authority for recording accounts receivables appear in Other Liabilities.

## Non-Federal Fluctuations

The increase of $122,623 thousand in accrued funded payroll and benefits from 30 September 2002 is due to the increase in the number of military personnel when Air Force Reserve and Air National Guard military personnel were activated in support of the war effort.

The decrease of $25,196 thousand in Advances from Others on Line 2.B. is due to the timing of the receipt and execution of orders primarily from Non-Federal sources.

The decrease of $9,973 thousand in deposit funds is associated with the timing difference as these deposit funds are posted to 57 X 6*** account until paid after each quarter. Deposit funds are used as temporary accounts to hold

amounts that eventually pay for state and local income taxes, savings bonds, charitable contributions, and employees' organizational dues.

The Temporary Early Retirement Authority (TERA) liabilities decrease of $11,757 thousand is due to the termination of the program in FY 2002.

The Accounts Payable - Cancelled Appropriations on Line 2.I. decreased by $6,974 thousand. Amounts are reduced as the liability is liquidated using current year funds.

The increase of $478,344 thousand in the accrued unfunded annual leave is the result of increases in military and civilian leave balances. The increase in military leave is impacted by the activation of military personnel in support of the war in Iraq, because the use of leave is restricted during a war.

Nonenvironmental Disposal Liabilities - Excess/Obsolete Structures increased $8,108 thousand, or 13 percent, from $62,581 thousand to $70,689 thousand as reported for FY 2002 and FY 2003 respectively. This change was in accordance with disposal plans directed by the Defense Reform Initiative Directive No. 36, dated May 5, 1998.

Nonenvironmental Disposal Liabilities - Conventional Munitions Disposal increased $5,880 thousand. Previously, this liability was only disclosed in the notes, but for FY 2003 it is included in the audited financial statements.

## Other Liabilities

The amount of $190,076 thousand represents legal contingencies of $189,231 thousand and accrued interest liability of $845 thousand.

The recorded estimated probable liability amount of $25,183 thousand has been included in the accompanying financial statements for open contractor claims greater than $100,000 and neither under appeal nor in litigation. In addition to the contractor claims under appeal and the open contractor claims for an amount greater than $100,000, the Air Force was party to numerous other contractor claims in amounts less than $100,000 per claim. These claims are a routine part of the contracting business and are typically resolved through mutual agreement between the contracting officer and the contractor. Because of the routine nature of these claims, no requirement exists for a consolidated tracking mechanism to record the amount of each claim, the number of open claims, or the probability of the claim being settled in favor of the claimant. The potential liability arising from these claims in aggregate would not materially affect the operations or financial condition of the Air Force. A reasonably possible liability is estimated at $9,447 thousand and is not included in the reported amount.

The total estimated probable liability for claims and litigation against the Air Force handled by the Civil Law and Litigation Directorate, as of June 30, 2003, was valued at $153,358 thousand and has been included in the accompanying financial statements. As of Sept 30, 2003, the Air Force was party to 4,157 claims and litigation actions. This liability dollar amount recorded in the financial statements is an estimate based on the weighted average payout rate for the previous three years. A reasonably possible liability is estimated at $244,739 thousand and is not included in the reported amount. Neither past payments nor the current contingent liability estimate provides a basis for accurately projecting the results of any individual lawsuit or claim. It is uncertain that claims will ever accrue to the Air Force. In addition, many claims and lawsuits, even if successful, will not be paid out of Air Force Funds. Rather, judgements over $100,000 are ordinarily paid from the Judgement Fund, not from Air Force accounts even though claims were the result of Air Force operations. In many cases involving attorney fees, the amounts are not known until the last appeal is concluded.

As of Sept 30, 2003, the Air Force was a party to 68 contract appeals before the Armed Services Board of Contract Appeals (ASBCA). The probable amount of loss from contractor claims of $10,689 thousand has been included in the financial statements. The contractor claims involve unique circumstances, which are considered by the ASBCA in for-

mulating decisions on the cases. Such claims are funded primarily from Air Force appropriations. A reasonably possible liability is estimated at $11,486 thousand and is not included in the reported amount.

## Other Disclosures

### Intragovernmental Reconciliation for Fiduciary Transactions with DoL and OPM

With respect to the major fiduciary balances with the OPM and the DoL, the Air Force was able to reconcile with the OPM and the DoL. During these reconciliations immaterial differences were identified.

# Note 15.B. Capital Lease Liability

| As of September 30, | 2003 | | | | 2002 |
|---|---|---|---|---|---|
| | Asset Category | | | | |
| (Amounts in Thousands) | Land and Buildings | Equipment | Other | Total | Total |
| **1. Future Payments Due:** | | | | | |
| A. 2004 | $ 45,433 | $ 167 | $ 0 | $ 45,600 | $ 45,600 |
| B. 2005 | 45,433 | 42 | 0 | 45,475 | 45,600 |
| C. 2006 | 45,152 | 0 | 0 | 45,152 | 45,433 |
| D. 2007 | 42,056 | 0 | 0 | 42,056 | 45,152 |
| E. 2008 | 38,978 | 0 | 0 | 38,978 | 42,056 |
| F. After 5 Years | 165,138 | 0 | 0 | 165,138 | 192,757 |
| G. Total Future Lease Payments Due | $ 382,190 | $ 209 | $ 0 | $ 382,399 | $ 416,598 |
| H. Less: Imputed Interest Executory Costs | 118,587 | 9 | 0 | 118,596 | 137,180 |
| I. Net Capital Lease Liability | $ 263,603 | $ 200 | $ 0 | $ 263,803 | $ 279,418 |
| **2. Capital Lease Liabilities Covered by Budgetary Resources:** | | | | $ 299,510 | $ 323,439 |
| **3. Capital Lease Liabilities Not Covered by Budgetary Resources:** | | | | $ 82,679 | $ 93,159 |

## Other Information

The Air Force is the leasee in twelve capital leases. Eleven are for family housing and one is for a piece of equipment. Six of the military housing leases were awarded prior to FY 1992 and are funded on a FY basis.

# Note 16. Commitments and Contingencies

## Disclosures Related to Commitments and Contingencies

### Relevant Information for Comprehension

The Commitments and Contingencies consist of the following reasonably possible liabilities:

| | |
|---|---|
| Contractual Actions: | |
| Contractor Claims | $9,447 Thousand |
| Appeals before Armed Services Board of Contract Appeals (ASBCA) | $11,486 Thousand |
| | $20,933 Thousand |
| Claims and Litigation from Civil Law: | $244,739 Thousand |
| **Total** | **$265,672 Thousand** |

### Note Reference

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

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

| As of September 30, (Amounts in Thousands) | 2003 | | | | 2002 |
|---|---|---|---|---|---|
| | Actuarial Present Value of Projected Plan Benefits | Assumed Interest Rate (%) | (Less: Assets Available to Pay Benefits) | Unfunded Actuarial Liability | Unfunded Actuarial Liability |
| FECA | $ 1,262,267 | | $ 0 | $ 1,262,267 | $ 1,211,045 |
| **Total Military Retirement Benefits and Other Employment Related Actuarial Liabilities** | **$ 1,262,267** | | **$ 0** | **$ 1,262,267** | **$ 1,211,045** |

## Military Retirement Pensions—Assumptions

The portion of the military retirement benefits actuarial liability applicable to the Department of the Air Force is reported on the financial statements of the Military Retirement Fund.

## Military Retirement Health Benefits—Assumptions

Health benefits are funded centrally at the DoD level. As such, the portion of the health benefits actuarial liability that is applicable to the Air Force is reported only on the DoD Agency-wide financial statements.

## Federal Employees' Compensation Act (FECA)—Assumptions and Actuarial Cost Method Used

The Air Force's actuarial liability for workers' compensation benefits is developed by the Department of Labor and provided to the Air Force at the end of each fiscal year. The liability includes the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases. The liability is determined using a method that utilizes historical benefit payment patterns to predict the ultimate payments. The projected annual benefit payments are then discounted to the present value using the OMB's economic assumptions for 10-year U.S. Treasury notes and bonds. Cost-of-living adjustments and medical inflation factors are also applied to the calculation of projected future benefits. Interest rate assumptions utilized for discounting were as follows:

**2003**

3.84% in Year 1

4.35% in Year 2 and thereafter

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

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

| CBY | COLA | CPIM |
|---|---|---|
| 2004 | 2.3% | 3.21% |
| 2005 | 2.00% | 3.54% |
| 2006 | 1.83% | 3.64% |
| 2007 | 1.97% | 3.80% |
| 2008+ | 2.17% | 3.92% |

The model's resulting projections were analyzed to insure that the estimates were reliable. The analysis was based on two tests: (1) a comparison of the percentage change in the liability amount by agency to the percentage change in

the actual payments, and (2) a comparison of the ratio of the estimated liability to the actual payment of the beginning year calculated for the current projection to the liability-payment ratio calculated for the prior projection.

### Note Reference

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

## Note 18. Unexpended Appropriations

| As of September 30, | 2003 | 2002 |
|---|---|---|
| (Amounts in Thousands) | | |
| **1. Unexpended Appropriations:** | | |
| A. Unobligated, Available | $ 8,323,168 | $ 5,272,785 |
| B. Unobligated, Unavailable | 1,571,907 | 1,185,935 |
| C. Unexpended Obligations | 40,847,242 | 33,085,130 |
| D. Total Unexpended Appropriations | $ 50,742,317 | $ 39,543,850 |

### Other Information Pertaining to Unexpended Appropriations

### Fluctuations

Unexpended appropriation increased $11,198,466 thousand since EOY 2002. This increase is directly associated with the increase in budget authority received by the Air Force for FY 2003 and the status of execution as a result of Operation Iraqi Freedom.

### Relevant Information for Comprehension

Unexpended obligations reported as a component of Unexpended Appropriations include both Undelivered Orders-Unpaid and Undelivered Orders-Paid only for direct appropriated funds. This amount is distinct from Change in Amount of Goods, Services, and Benefits Ordered but Not Yet Received line of the Statement of Financing, which includes the change during the fiscal year in unexpended obligations against budget authority from all sources.

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

### Disclosures Related to the Statement of Net Cost

### Statement of Net Cost

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

### Reporting Entities

The amounts presented in the SoNC are based on obligations and disbursements and therefore may not in all cases report actual accrued costs. The Air Force generally records transactions on a cash basis and not an accrual basis as is required by the generally accepted accounting principles. Therefore, the Air Force systems do not capture actual costs. As such, information presented in the SoNC is based on budgetary obligations, disbursements and collection transactions, as well as non-financial feeder systems; then adjusted to record known accruals for major items such as payroll expenses, accounts payable, and environmental liabilities.

### Fluctuations and Abnormalities

The 23 percent increase in Intragovernmental Gross Cost and 36 percent in Public Net Costs is due to the 23 percent increase in Budget Authority as reflected on the Statement of Budgetary Resources. The increase is primarily tied to supplemental funding for Global War on Terrorism.

The increase in Gross Cost with the Public can be attributed to the increase in depreciation expense resulting from the inclusion of National Defense Property Plant and Equipment and an increase in real property depreciation as reported in the Automated Civil Engineering System (ACES). Further, increased consumption of Operating Material and Supplies such as munitions, and decreases in the value of Other General Property, Plant and Equipment assets contributed to the change.

The increase in Intragovernmental and Public Earned Revenue can be attributed to an increase of 18 percent in reimbursable authority. Despite the fact that intragovernmental earned revenue increased 71 percent, as reflected on the comparative Net Cost Statement, actual government revenue only increase by 8 percent. Intra-Air Force reimbursable activity decreased and reimbursable activity with other intragovernmental activities increased which resulted in a 70 percent change in eliminations on the Air Force Net Cost statement.

Imputed Cost and Expenses for the Judgement Fund decreased in value by $22,705 thousand due to the number of Air Force cases requiring payment by the U.S. Treasury.

The abnormal amount of intragovernmental net costs on the Consolidating Statement of Net Cost for Research, Development, Test & Evaluation Program is attributable to intragovernmental revenue per Air Force seller side records being higher than intragovernmental expenses in the Air Force accounting records. This situation existed prior to adjustments for other seller side data. Further analysis of Air Force accounting data is required.

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

Not applicable.

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

Not applicable.

## Note 19.D. Imputed Expenses

| As of September 30, | 2003 | 2002 |
|---|---|---|
| (Amount in thousands) | | |
| **Civilian (e.g.,CSRS/FERS) Retirement** | $ 254,229 | $ 193,271 |
| **Civilian Health** | 338,180 | 340,583 |
| **Civilian Life Insurance** | 1,249 | 1,184 |
| **Judgment Fund** | 39,334 | 62,038 |
| **Total Imputed Expenses** | $ 632,992 | $ 597,076 |

### Other Information

#### Fluctuations

The Civilian Retirement imputed expense increased $60,958 thousand, or 32 percent, from $193,271 thousand to $254,229 thousand as reported for FY 2002 and FY 2003 respectively. The major factors contributing to this fluctuation are an increase in the cost factors computed by the Office of Personnel Management (OPM), an increase in the gross basic pay for the Federal Employees' Retirement System (FERS), and a decrease in the employer contribution rate for the Civil Service Retirement System (CSRS). For the first time, an imputed cost is recognized for FERS.

#### Information Related to Imputed Expenses

The total Civilian Retirement imputed expense of $254,229 thousand is comprised of $230,951 thousand for the Civil Service Retirement System (CSRS) and $23,278 thousand for the Federal Employees' Retirement System (FERS).

The imputed expenses are equal to the imputed revenue recognized on the Statement of Changes in Net Position and disclosed in detail in Note 20.

## Note 19.E. Benefit Program Expenses

Not applicable.

## Note 19.F. Exchange Revenue

### Disclosures Related to the Exchange Revenue

Exchange Revenue arises when a Government entity provides goods and services to the public or to another Government for a price—"earned revenue." Exchange revenue includes most user charges other than taxes, i.e., regulatory user charges.

Goods and services provided through reimbursable programs to the public or another U.S. Government entity (intra-Air Force, intra-DoD or other federal entity) is provided at cost. Such reimbursable sales are reported as earned revenues. Costs are equal to the amount reported as earned. Since FY 2000 sales to the Foreign Military Trust Fund and related cost of sales have been reclassified as nonfederal, transactions with the public, rather than intragovernmental transactions as in years prior.

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

Not applicable.

## Note 19.H. Stewardship Assets

### Disclosures Related to Stewardship Assets

Stewardship assets include Heritage Assets, Stewardship Land, Nonfederal Physical Property, and Investments in Research and Development. The current year cost of acquiring, constructing, improving, reconstructing, or renovating heritage assets; costs of acquiring stewardship land; and costs to prepare stewardship land for its intended use are required to be recognized and disclosed in the SoNC or the notes if occurring. Such costs, if any, are not separately identifiable and are not believed to be material.

## Note 19.I. Intra-governmental Revenue and Expense

### Disclosures Related to Intra-governmental Revenue and Expense

#### Intragovernmental Revenue

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

#### Intragovernmental Operating Expenses

The Air Force's operating expenses were adjusted based on a comparison between the Air Force's accounts payable and the DoD summary level seller accounts receivables. An adjustment was posted to accounts payable and operating expenses to reflect unrecognized accounts payable and operating expenses. The operating expenses of the Air Force were adjusted upwards in the amount of $986,462 thousand.

## Note 19.J. Suborganization Program Costs

The Department of Defense (DoD) identifies programs based on the nine major appropriation groups provided by the Congress. The Department is in the process of reviewing available data and attempting to develop a cost reporting methodology that fulfills the need for cost information required by SFFAS No. 4 to keep the financial statements from becoming overly voluminous.

Until cost-allocating processes and expanded intra-DoD eliminating capabilities are incorporated into the accounting processes, the usefulness of further suborganization-reported (major command) net costs is limited. This limitation is the reason that no additional statements of suborganization costs at lower levels are presented with these statements.

The DoD is unable to accumulate costs for major programs based on performance measures identified under requirements of the Government Performance and Results Act because current financial processes and systems do not capture and report this type of cost information. Until the processes and systems are upgraded, the DoD as a whole will break out programs by major appropriation groupings.

The SoNC format requires reporting program costs by costs incurred with intragovernmental and public entities. Although overall program costs are believed to be fairly stated, the cost allocations between intragovernmental and public entities that were based on available vendor-type data may not be totally accurate.

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

| As of September 30, | Cumulative Results of Operations 2003 | Unexpended Appropriations 2003 | Cumulative Results of Operations 2002 | Unexpended Appropriations 2002 |
|---|---|---|---|---|
| (Amounts in thousands) | | | | |
| **1. Prior Period Adjustments Increases (Decreases) to Net Position** | | | | |
| **Beginning Balance:** | | | | |
| A. Changes in Accounting Standards | $ 122,475,076 | $ 0 | $ 0 | $ 0 |
| B. Errors and Omissions in Prior Year Accounting Reports | 0 | 0 | -31,869,730 | 0 |
| C. Other Prior Period Adjustments | 0 | 0 | 0 | 0 |
| D. Total Prior Period Adjustments | $ 122,475,076 | $ 0 | $ -31,869,730 | $ 0 |
| **2. Imputed Financing:** | | | | |
| A. Civilian CSRS/FERS Retirement | $ 254,229 | $ 0 | $ 193,271 | $ 0 |
| B. Civilian Health | 338,180 | 0 | 340,583 | 0 |
| C. Civilian Life Insurance | 1,249 | 0 | 1,184 | 0 |
| D. Military Retirement Pension | 0 | 0 | 0 | 0 |
| E. Military Retirement Health | 0 | 0 | 0 | 0 |
| F. Judgment Fund | 39,334 | 0 | 62,038 | 0 |
| G. Total Imputed Financing | $ 632,992 | $ 0 | $ 597,076 | $ 0 |

## Other Information

### Relevant Information for Comprehension

The Federal Accounting Standards Advisory Board issued Statement of Federal Financial Accounting Standards No. 23, Eliminating the Category National Defense Property, Plant and Equipment, in May 2003. This standard requires the capitalization and depreciation of the cost of military equipment. This data was included in the statements through a prior period adjustment.

### Imputed Financing

The amounts remitted to OPM by and for employees covered by Civil Service Retirement System (CSRS), Federal Employees' Retirement System (FERS), Federal Employees' Health Benefits Program (FEHB) and the Federal

Employee Group Life Insurance Program (FEGLI) do not fully cover the Government's cost to provide these benefits. An imputed cost is recognized as the difference between the Government's cost of providing these benefits to the employees and contributions made by and for them. The Office of Personnel Management (OPM) provides the cost factors to DFAS for computation of imputed financing cost. The DFAS provides the costs to the Office of the Under Secretary of Defense (Personnel and Readiness) (OUSD (P&R)) for validation. Approved imputed costs are provided to the reporting components for inclusion in their financial statements.

The total Civilian Retirement imputed financing of $254,229 thousand is comprised of $230,951 thousand for Civil Service Retirement System (CSRS) and $23,278 thousand for the Federal Employees' Retirement System (FERS).

The imputed revenue is equal to the imputed expense recognized in the Statement of Net Cost and disclosed in detail in Note 19D.

## Note 21.A. Disclosures Related to the Statement of Budgetary Resources

| As of September 30, | 2003 | 2002 |
|---|---|---|
| (Amounts in thousands) | | |
| 1. Net Amount of Budgetary Resources Obligated for Undelivered Orders at the End of the Period | $ 42,556,665 | $ 34,775,371 |
| 2. Available Borrowing and Contract Authority at the End of the Period | 0 | 0 |

### Other Information

#### Fluctuations

Comparison of FY 2003 to FY 2002 Statement of Budgetary Resources not required for the year-end statements.

#### Other Information Related to the Statement of Budgetary Resources

The amount of direct obligations incurred and apportioned under category A is $73,187,072 thousand, category B is $50,177,235 thousand, and exempt is $11,259 thousand. For reimbursable obligations incurred and apportioned category A is $5,244,197 thousand, category B is $2,975,642 thousand and exempt is $11,547 thousand.

Unexpended Obligations presented in the Statement of Budgetary Resources (SBR) includes Unexpended Obligations for both direct and reimbursable funds. The Department has not fully implemented the U.S. Standard General Ledger (USSGL) in all operational accounting systems.

The statement does not include any amounts for which the Department of Treasury is willing to accept corrections to canceled appropriation amounts, in accordance with SFFAS Number 1.

Adjustments in funds that are temporarily not available pursuant to Public Law, and those that are permanently not available (included in the Adjustments line on the SBR), are not included in Spending Authority from Offsetting Collections and Adjustments line of the SBR or the Spending Authority for Offsetting Collections and Adjustments line of the Statement of Financing.

Due to accounting system deficiencies, the proper amount of intra agency eliminations for this statement cannot be determined.

Accounting systems currently do not provide or capture data needed for obligations incurred and recoveries of prior year obligations in accordance with OMB Circular A-11, "Instructions on Budget Execution" requirements. Although DFAS Denver Center developed an alternative methodology to calculate these items, the auditors and DFAS Denver Center concurs this methodology also distorts the obligation figures. As a result, the amount of distortion cannot be reliably determined, and may or may not be material.

Disaggregated SBR are included in the Required Supplementary Information section of the statements. The abnormal balance on line 15b of the disaggregated SBR is the current year correction of an erroneous collection reported during FY 2002.

## Note 21.B. Disclosures Related to Problem Disbursements, In-transit Disbursements and Suspense/Budget Clearing Accounts

| As of September 30, | Sep-01 | Sep-02 | Sep-03 | (Decrease)/Increase from 2002 to 2003 |
|---|---|---|---|---|
| (Amounts in thousands) | | | | |
| **Total Problem Disbursements** | | | | |
| Absolute Unmatched Disbursements | $ 23,300 | $ 11,685 | $ 7,813 | $ (3,872) |
| Negative Unliquidated Obligations | 22,722 | 10,232 | 12,436 | 2,204 |
| **Total In-transit Disbursements, Net** | $ 2,271,948 | $ 1,320,627 | $ 1,111,274 | $ (209,353) |

### Other Information Related to Problem Disbursements and In-transit Disbursements

The Air Force has $20,248 thousand in problem disbursements and $1,111,274 thousand in in-transit disbursements that represent disbursements of Air Force funds that have been reported by a disbursing station to the Department of the Treasury but have not yet been precisely matched against the specific source obligation giving rise to the disbursements. For the most part, these payments have been made using available funds and based on valid receiving reports for goods and services delivered under valid contracts. The problem disbursements and in-transit disbursements arise when the various contracting, disbursing, and accounting systems fail to match the data necessary to properly account for the disbursement transactions in all applicable accounting systems. Defense Finance and Accounting Service has efforts underway to improve the systems and to resolve all previous problem disbursements and to process all in-transit disbursements. As of September 30, 2003, these efforts resulted in a $1,668,508.24 decrease in reported problem disbursements since September 2002; and in-transit disbursements have decreased by $209,353,185.29. The amount over 120 days old for UMDs is $110,951.71 and NULOs is $475,000.67. The amount over 180 days old for UMDs is $81,602.39, for NULOs is $409,206.41, and for In-transits is $12,204,352.07. The absolute value of in-transit disbursements is $3,903,424,469.55.

**Suspense/Budget Clearing Accounts, Net**

| Account | Sep-01 | Sep-02 | Sep-03 | (Decrease)/Increase |
|---|---|---|---|---|
| F3875 | $ 30,874 | $ 398,084 | $ (364,737) | $ (762,821) |
| F3880 | 35 | (62) | (2,343) | (2,281) |
| F3882 | 0 | 0 | (16,526) | (16,526) |
| F3885 | (477,440) | (193,678) | 8,785 | 202,463 |
| F3886 | 5 | 0 | 0 | 0 |
| **Total** | $ (446,526) | $ 204,344 | $ (374,821) | $ (579,165) |

### Other Information Related to Suspense/Budget Clearing Accounts:

Air Force has made a concerted effort to reduce balances in the suspense and budget clearing accounts, and to establish an accurate and consistent use of these accounts. The information presented indicates the significant reductions (with the exceptions noted below) that the Air Force has achieved in the various suspense/budget clearing accounts.

The increase in account F3875 from September FY 2002 to September FY 2003 is due to many variables. They are all placed in various suspense accounts such as Agricultural/Grazing Leases and Withheld FICA/FITW Medicare Taxes for Military that are collected in and released at various times.

The decrease in account F3880 from September FY2002 to September FY 2003 is due to Recertified Check Payments which are credits from Treasury for cancelled checks not yet being put back into the original appropriations and 1081 completion.

Suspense account F3882 began in 1st quarter of FY 2003 as the Military Thrift Saving Plan came into existence starting October 2002. The ($3,971) thousand represents a timing difference as the National Finance Center post amounts into each member's account. They are consolidated and posted to Treasury before the Air Force can post the amounts in the military accounting system in the following month.

The increase in account F3885 from September FY2002 to September FY 2003 is due to Intragovernmental Payment and Collection (IPAC) transactions received during the last business day of the month. They are placed in a suspense account until they can be researched and assigned a valid appropriation, which will fluctuated from each reporting period depending upon the amount processed to the Treasury at that time.

# Note 22. Disclosures Related to the Statement of Financing

## Disclosures Related to the Statement of Financing

The objective of the Statement of Financing is to reconcile the difference between budgetary obligations and the net cost of operations reported. It is presented as combined or combining statements rather than consolidated statements due to intragovernmental transactions not being eliminated. Due to the Department of the Air Force's financial system limitations, budgetary data is not in agreement with proprietary expenses and assets capitalized. Differences between budgetary and proprietary data are a previously identified deficiency.

Note 1A and Note 1F provide additional detail.

## Other Information Related to the Statement of Financing

Components Requiring or Generating Resources in the Future, Other, consists of $(6,980) thousand in closed year payables, $(51,509) thousand in judgement fund liabilities, $(842) thousand in education benefits for involuntary separatees, $13,988 thousand in nonenvironmental disposal liabilities, $(5,942) thousand in capital lease liabilities, $(12,046) thousand in contingent liabilities, $315 thousand in interest accrued liability, $51,223 thousand in changes in actuarial liabilities, and $26,564 thousand in Federal Employees Compensation Act (FECA) reimbursement to the Department of Labor. Components Not Requiring or Generating Resources, Other, consists of $1,984 thousand in bad debt expense and $11,547,618 thousand in other expenses.

The components and amount of liabilities not covered by budgetary resources are disclosed in Note 11. Liabilities Not Covered and Covered by Budgetary Resources.

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

Budgetary data is not in agreement with Proprietary Expenses and Asset Capitalized. This causes a difference in Net Cost between the Statement of Net Cost and the Statement of Financing. The amount on the Resources that finance the acquisition of assets line has been adjusted $303,216 thousand to resolve differences.

# Note 23. Disclosures Related to the Statement of Custodial Activity

Not applicable.

# Note 24.A. Other Disclosures

**ENTITY AS LESSEE—Operating Leases**

| As of September 30, (Amounts in thousands) | 2003 | | | | 2002 |
|---|---|---|---|---|---|
| B. Future Payments Due: *Fiscal Year* | Land and Buildings | Equipment | Other | Total | Total |
| 2004 | $ 59 | $ 1,263 | $ 76 | $ 1,398 | $ 2,045 |
| 2005 | 75 | 558 | 106 | 739 | 1,582 |
| 2006 | 82 | 376 | 0 | 458 | 906 |
| 2007 | 87 | 0 | 0 | 87 | 538 |
| 2008 | 85 | 0 | 0 | 85 | 0 |
| After 5 Years | 87 | 0 | 0 | 87 | 0 |
| Total Future Lease Payments Due | $ 475 | $ 2,197 | $ 182 | $ 2,854 | $ 5,071 |

## Fluctuations and Abnormalities

The increase in Operating Leases from FY 02 to FY 03 is due to an increase in the number of high cost leases entered into by the Air Force.

## Definitions

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

Land and Buildings Leases consist of:

- Description of Leases: The figures represent operating leased facilities in the U.S. and overseas applicable to active Air Force, Air Force Reserve and Air Force National Guard.

Equipment Leases consist of :

- Description of Leases: Operating leases for medical equipment are one year leases with four option years. Each year, facilities must specifically exercise the option to continue the lease. The operating leases contain an option to purchase allow the government to purchase the equipment a fair market value at the end of the lease period.

Other Leases consist of :

- Description of Leases: Operating Leases for Motor Vehicles are essentially one year leases funded in appropriation 3400 (O&M). As the out year estimates indicate, Air Force expects to continue to reduce the level of owned assets, while increasing the number of operational leases. Air Force will continue to displace commercial leases in favor of IFMS (General Services Administration) leases because IFMS leases are typically more economical.

# Note 24.B. Other Disclosures

Interest Payable: DFAS Columbus has accumulated prompt payment interest of approximately $845 thousand during FY 2003 for Air Force contracts.

Undistributed Collections and Disbursements: Accounts receivable and payable are adjusted for undistributed collections and disbursements. These transactions represent the Air Force's in-float (undistributed) collections and disbursements for transactions that were reported by a disbursing station but not recorded by the appropriate accountable station. Undistributed amounts are prorated by appropriation based on the percentage of distributed government and public receivables and payables.

Canceled Balances: All unliquidated balances associated with closed accounts 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 outstanding are not included in the financial statements; however, these orders may result in future expenditures.

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# Consolidating and Combining Statements

# Consolidating Balance Sheet—General Funds

As of September 30, 2003 and 2002 ($ in thousands)

| | Air Force Active | Air Force Reserve | Air National Guard |
|---|---|---|---|
| **ASSETS (Note 2)** | | | |
| Intragovernmental: | | | |
| Fund Balance with Treasury (Note 3) | | | |
| Entity | $ 56,397,291 | $ 1,050,436 | $ 2,266,311 |
| Non-Entity Seized Iraqi Cash | 0 | 0 | 0 |
| Non-Entity-Other | 52,503 | 0 | 0 |
| Investments (Note 4) | 712 | 0 | 0 |
| Accounts Receivable (Note 5) | 704,929 | 61,054 | 166,987 |
| Other Assets (Note 6) | 56 | 0 | 0 |
| Total Intragovernmental Assets | $ 57,155,491 | $ 1,111,490 | $ 2,433,298 |
| Cash and Other Monetary Assets (Note 7) | $ 147,926 | $ 0 | $ 0 |
| Accounts Receivable (Note 5) | 746,348 | 9,264 | 16,888 |
| Loans Receivable (Note 8) | 0 | 0 | 0 |
| Inventory and Related Property (Note 9) | 46,990,655 | 726,348 | 4,098,828 |
| General Property, Plant and Equipment (Note 10) | 108,020,196 | 1,022,240 | 3,743,694 |
| Investments (Note 4) | 0 | 0 | 0 |
| Other Assets (Note 6) | 9,872,418 | 4,613 | 35,120 |
| **TOTAL ASSETS** | $ 222,933,034 | $ 2,873,955 | $ 10,327,828 |
| **LIABILITIES (Note 11)** | | | |
| Intragovernmental: | | | |
| Accounts Payable (Note 12) | $ 640,199 | $ 19,019 | $ 92,223 |
| Debt (Note 13) | 0 | 0 | 0 |
| Environmental Liabilities (Note 14) | 0 | 0 | 0 |
| Other Liabilities (Note 15 & Note 16) | 2,206,526 | 6,087 | 14,399 |
| Total Intragovernmental Liabilities | $ 2,846,725 | $ 25,106 | $ 106,622 |
| Accounts Payable (Note 12) | $ 6,665,407 | $ 120,585 | $ 300,195 |
| Military Retirement Benefits and Other Employment-Related Actuarial Liabilities (Note 17) | 904,570 | 133,221 | 224,476 |
| Environmental Liabilities (Note 14) | 8,110,403 | 0 | 0 |
| Loan Guarantee Liability (Note 8) | 0 | 0 | 0 |
| Other Liabilities (Note 15 and Note 16) | 4,202,249 | 43,125 | 54,847 |
| Debt Held by Public | 0 | 0 | 0 |
| **TOTAL LIABILITIES** | $ 22,729,354 | $ 322,037 | $ 686,140 |
| **NET POSITION** | | | |
| Unexpended Appropriations (Note 18) | $ 48,066,969 | $ 956,002 | $ 2,046,631 |
| Cumulative Results of Operations | 152,136,711 | 1,595,916 | 7,595,057 |
| **TOTAL NET POSITION** | $ 200,203,680 | $ 2,551,918 | $ 9,641,688 |
| **TOTAL LIABILITIES AND NET POSITION** | $ 222,933,034 | $ 2,873,955 | $ 10,327,828 |

| Component Level | Combined Total | Eliminations | 2003 Consolidated | 2002 Consolidated |
|---|---|---|---|---|
| $ 0 | $ 59,714,038 | $ 0 | $ 59,714,038 | $ 47,888,000 |
| 0 | 0 | 0 | 0 | 0 |
| 0 | 52,503 | 0 | 52,503 | 54,750 |
| 0 | 712 | 0 | 712 | 708 |
| -391,541 | 541,429 | 0 | 541,429 | 443,154 |
| 339,037 | 339,093 | 0 | 339,093 | 4,989 |
| $ -52,504 | $ 60,647,775 | $ 0 | $ 60,647,775 | $ 48,391,601 |
| $ 0 | $ 147,926 | $ 0 | $ 147,926 | $ 140,645 |
| 0 | 772,500 | 0 | 772,500 | 1,017,910 |
| 0 | 0 | 0 | 0 | 0 |
| 0 | 51,815,831 | 0 | 51,815,831 | 28,817,564 |
| 0 | 112,786,130 | 0 | 112,786,130 | 24,247,152 |
| 0 | 0 | 0 | 0 | 0 |
| 0 | 9,912,151 | 0 | 9,912,151 | 7,535,914 |
| $ -52,504 | $ 236,082,313 | $ 0 | $ 236,082,313 | $ 110,150,786 |
| | | | | |
| $ 662,499 | $ 1,413,940 | $ 0 | $ 1,413,940 | $ 1,124,733 |
| 0 | 0 | 0 | 0 | 134 |
| 0 | 0 | 0 | 0 | 0 |
| -603,107 | 1,623,905 | 0 | 1,623,905 | 2,179,087 |
| $ 59,392 | $ 3,037,845 | $ 0 | $ 3,037,845 | $ 3,303,954 |
| $ -5,278 | $ 7,080,909 | $ 0 | $ 7,080,909 | $ 6,206,967 |
| 0 | 1,262,267 | 0 | 1,262,267 | 1,211,045 |
| | | | | |
| 0 | 8,110,403 | 0 | 8,110,403 | 8,454,564 |
| 0 | 0 | 0 | 0 | 0 |
| 220,667 | 4,520,888 | 0 | 4,520,888 | 3,987,188 |
| 0 | 0 | 0 | 0 | 0 |
| $ 274,781 | $ 24,012,312 | $ 0 | $ 24,012,312 | $ 23,163,718 |
| | | | | |
| $ -327,285 | $ 50,742,317 | $ 0 | $ 50,742,317 | $ 39,543,850 |
| 0 | 161,327,684 | 0 | 161,327,684 | 47,443,218 |
| $ -327,285 | $ 212,070,001 | $ 0 | $ 212,070,001 | $ 86,987,068 |
| $ -52,504 | $ 236,082,313 | $ 0 | $ 236,082,313 | $ 110,150,786 |

# Consolidating Statement of Net Cost—General Funds

For the periods ended September 30, 2003 and 2002 ($ in thousands)

| | Air Force Active | Air Force Reserve | Air National Guard |
|---|---|---|---|
| **Program Costs** | | | |
| **A. Military Personnel** | | | |
| Intragovernmental Gross Costs | $ 360,388 | $ 110,469 | $ 249,508 |
| (Less: Intragovernmental Earned Revenue) | -297,366 | -5,494 | -39,508 |
| Intragovernmental Net Costs | $ 63,022 | $ 104,975 | $ 210,000 |
| Gross Costs With the Public | 25,540,585 | 1,027,347 | 1,780,958 |
| (Less: Earned Revenue From the Public) | -139,177 | 0 | -8,119 |
| Net Costs With the Public | $ 25,401,408 | $ 1,027,347 | $ 1,772,839 |
| Total Net Cost | $ 25,464,430 | $ 1,132,322 | $ 1,982,839 |
| **B. Operation and Maintenance** | 0 | | |
| Intragovernmental Gross Costs | $ 12,923,063 | $ 680,161 | $ 1,656,445 |
| (Less: Intragovernmental Earned Revenue) | -2,674,604 | -326,667 | -729,686 |
| Intragovernmental Net Costs | $ 10,248,459 | $ 353,494 | $ 926,759 |
| Gross Costs With the Public | 22,872,197 | 1,465,636 | 3,233,746 |
| (Less: Earned Revenue From the Public) | -420,864 | -882 | -103,463 |
| Net Costs With the Public | $ 22,451,333 | $ 1,464,754 | $ 3,130,283 |
| Total Net Cost | $ 32,699,792 | $ 1,818,248 | $ 4,057,042 |
| **C. Procurement** | 0 | | |
| Intragovernmental Gross Costs | $ 2,669 | $ 0 | $ 0 |
| (Less: Intragovernmental Earned Revenue) | -214,765 | 0 | 0 |
| Intragovernmental Net Costs | $ -212,096 | $ 0 | $ 0 |
| Gross Costs With the Public | 35,414,003 | 0 | 0 |
| (Less: Earned Revenue From the Public) | -13,188 | 0 | 0 |
| Net Costs With the Public | $ 35,400,815 | $ 0 | $ 0 |
| Total Net Cost | $ 35,188,719 | $ 0 | $ 0 |
| **D. Research, Development, Test & Evaluation** | 0 | | |
| Intragovernmental Gross Costs | $ 976,052 | $ 0 | $ 0 |
| (Less: Intragovernmental Earned Revenue) | -2,356,078 | 0 | 0 |
| Intragovernmental Net Costs | $ -1,380,026 | $ 0 | $ 0 |
| Gross Costs With the Public | 19,273,993 | 0 | 0 |
| (Less: Earned Revenue From the Public) | -138,222 | 0 | 0 |
| Net Costs With the Public | $ 19,135,771 | $ 0 | $ 0 |
| Total Net Cost | $ 17,755,745 | $ 0 | $ 0 |
| **E. Military Construction/Family Housing** | 0 | | |
| Intragovernmental Gross Costs | $ 140,951 | $ 715 | $ 4,823 |
| (Less: Intragovernmental Earned Revenue) | 0 | 0 | 0 |
| Intragovernmental Net Costs | $ 140,951 | $ 715 | $ 4,823 |
| Gross Costs With the Public | 1,042,131 | 31,856 | 166,872 |
| (Less: Earned Revenue From the Public) | 0 | 0 | 0 |
| Net Costs With the Public | $ 1,042,131 | $ 31,856 | $ 166,872 |
| Total Net Cost | $ 1,183,082 | $ 32,571 | $ 171,695 |
| **F. Other** | 0 | | |
| Intragovernmental Gross Costs | $ 12,548 | $ 0 | $ 0 |
| (Less: Intragovernmental Earned Revenue) | -32 | 0 | 0 |
| Intragovernmental Net Costs | $ 12,516 | $ 0 | $ 0 |
| Gross Costs With the Public | 13,320 | 0 | 0 |
| (Less: Earned Revenue From the Public) | -12,243 | 0 | 0 |
| Net Costs With the Public | $ 1,077 | $ 0 | $ 0 |
| Total Net Cost | $ 13,593 | $ 0 | $ 0 |
| **G. Total Program Costs** | 0 | | |
| Intragovernmental Gross Costs | $ 14,415,671 | $ 791,345 | $ 1,910,776 |
| (Less: Intragovernmental Earned Revenue) | -5,542,845 | -332,161 | -769,194 |
| Intragovernmental Net Costs | $ 8,872,826 | $ 459,184 | $ 1,141,582 |
| Gross Costs With the Public | 104,156,229 | 2,524,839 | 5,181,576 |
| (Less: Earned Revenue From the Public) | -723,694 | -882 | -111,582 |
| Net Costs With the Public | $ 103,432,535 | $ 2,523,957 | $ 5,069,994 |
| Total Net Cost | $ 112,305,361 | $ 2,983,141 | $ 6,211,576 |
| **Cost Not Assigned to Programs** | 0 | 0 | 0 |
| **(Less:Earned Revenue Not Attributable to Programs)** | 0 | 0 | 0 |
| **Net Cost of Operations** | $ 112,305,361 | $ 2,983,141 | $ 6,211,576 |

*The accompanying notes are an integral part of the financial statements. See notes 1 and 19.*

| Component Level | Combined Total | Eliminations | 2003 Consolidated | 2002 Consolidated |
|---|---|---|---|---|
| | $ 720,365 | $ 0 | $ 720,365 | $ 3,873,097 |
| | -342,368 | 0 | -342,368 | -152,854 |
| | $ 377,997 | $ 0 | $ 377,997 | $ 3,720,243 |
| | 28,348,890 | 0 | 28,348,890 | 20,842,052 |
| | -147,296 | 0 | -147,296 | -68,228 |
| | $ 28,201,594 | $ 0 | $ 28,201,594 | $ 20,773,824 |
| | $ 28,579,591 | $ 0 | $ 28,579,591 | $ 24,494,067 |
| | $ 15,259,669 | $ 0 | $ 15,259,669 | $ 17,472,658 |
| | -3,730,957 | 0 | -3,730,957 | -1,156,988 |
| | $ 11,528,712 | $ 0 | $ 11,528,712 | $ 16,315,670 |
| | 27,571,579 | 0 | 27,571,579 | 19,969,078 |
| | -525,209 | 0 | -525,209 | -481,777 |
| | $ 27,046,370 | $ 0 | $ 27,046,370 | $ 19,487,301 |
| | $ 38,575,082 | $ 0 | $ 38,575,082 | $ 35,802,971 |
| | $ 2,669 | $ 0 | $ 2,669 | $ 321,717 |
| | -214,765 | 0 | -214,765 | -153,067 |
| | $ -212,096 | $ 0 | $ -212,096 | $ 168,650 |
| | 35,414,003 | 0 | 35,414,003 | 16,329,627 |
| | -13,188 | 0 | -13,188 | -10,410 |
| | $ 35,400,815 | $ 0 | $ 35,400,815 | $ 16,319,217 |
| | $ 35,188,719 | $ 0 | $ 35,188,719 | $ 16,487,867 |
| | $ 976,052 | $ 0 | $ 976,052 | $ 136,722 |
| | -2,356,078 | 0 | -2,356,078 | -864,360 |
| | $ -1,380,026 | $ 0 | $ -1,380,026 | $ -727,638 |
| | 19,273,993 | 0 | 19,273,993 | 15,364,865 |
| | -138,222 | 0 | -138,222 | -113,063 |
| | $ 19,135,771 | $ 0 | $ 19,135,771 | $ 15,251,802 |
| | $ 17,755,745 | $ 0 | $ 17,755,745 | $ 14,524,164 |
| | $ 146,489 | $ 0 | $ 146,489 | $ 4,164 |
| | 0 | 0 | 0 | 0 |
| | $ 146,489 | $ 0 | $ 146,489 | $ 4,164 |
| | 1,240,859 | 0 | 1,240,859 | 417,431 |
| | 0 | 0 | 0 | 0 |
| | $ 1,240,859 | $ 0 | $ 1,240,859 | $ 417,431 |
| | $ 1,387,348 | $ 0 | $ 1,387,348 | $ 421,595 |
| $ 9,728,872 | $ 9,741,420 | $ 0 | $ 9,741,420 | $ 12,354 |
| 2,657,789 | 2,657,757 | 0 | 2,657,757 | -55 |
| $ 12,386,661 | $ 12,399,177 | $ 0 | $ 12,399,177 | $ 12,299 |
| -12,059,377 | -12,046,057 | 0 | -12,046,057 | 4,085 |
| 0 | -12,243 | 0 | -12,243 | -7,233 |
| $ -12,059,377 | $ -12,058,300 | $ 0 | $ -12,058,300 | $ -3,148 |
| $ 327,284 | $ 340,877 | $ 0 | $ 340,877 | $ 9,151 |
| $ 9,728,872 | $ 26,846,664 | $ 0 | $ 26,846,664 | $ 21,820,712 |
| 2,657,789 | -3,986,411 | 0 | -3,986,411 | -2,327,324 |
| $ 12,386,661 | $ 22,860,253 | $ 0 | $ 22,860,253 | $ 19,493,388 |
| -12,059,377 | 99,803,267 | 0 | 99,803,267 | 72,927,138 |
| 0 | -836,158 | 0 | -836,158 | -680,711 |
| $ -12,059,377 | $ 98,967,109 | $ 0 | $ 98,967,109 | $ 72,246,427 |
| $ 327,284 | $ 121,827,362 | $ 0 | $ 121,827,362 | $ 91,739,815 |
| 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 |
| $ 327,284 | $ 121,827,362 | $ 0 | $ 121,827,362 | $ 91,739,815 |

*The accompanying notes are an integral part of the financial statements. See notes 1 and 19.*

# Consolidating Statement of Changes in Net Position—General Funds

For the years ended September 30, 2003 and 2002 ($ in thousands)

| | Air Force Active | Air Force Reserve | Air National Guard |
|---|---|---|---|
| **CUMULATIVE RESULTS OF OPERATIONS** | | | |
| **Beginning Balances** | $ 43,431,324 | $ 708,722 | $ 3,303,172 |
| **Prior period adjustments (+/-)** | 118,827,668 | 611,906 | 3,035,502 |
| **Beginning Balances, as adjusted** | 162,258,992 | 1,320,628 | 6,338,674 |
| **Budgetary Financing Sources:** | | | |
| Appropriations received | 0 | 0 | 0 |
| Appropriations transferred-in/out (+/-) | 0 | 0 | 0 |
| Other adjustments (rescissions, etc) (+/-) | 0 | 0 | 0 |
| Appropriations used | 103,901,479 | 3,108,199 | 6,047,163 |
| Nonexchange revenue | 0 | 0 | 0 |
| Donations and forfeitures of cash and cash equivalents | 9,096 | 0 | 0 |
| Transfers-in/out without reimbursement (+/-) | 0 | 0 | 0 |
| Other budgetary financing sources (+/-) | 0 | 0 | 0 |
| **Other Financing Sources:** | | | |
| Donations and forfeitures of property | 0 | 0 | 0 |
| Transfers-in/out without reimbursement (+/-) | -2,360,484 | 150,229 | 1,420,795 |
| Imputed financing from costs absorbed by others | 632,990 | 0 | 0 |
| Other (+/-) | 0 | 0 | 0 |
| **Total Financing Sources** | 102,183,081 | 3,258,428 | 7,467,958 |
| **Net Cost of Operations (+/-)** | 112,305,361 | 2,983,141 | 6,211,576 |
| **Ending Balances** | $ 152,136,712 | $ 1,595,915 | $ 7,595,056 |
| **UNEXPENDED APPROPRIATIONS** | | | |
| **Beginning Balances** | $ 37,257,950 | $ 684,574 | $ 1,601,326 |
| **Prior period adjustments (+/-)** | 0 | 0 | 0 |
| **Beginning Balances, as adjusted** | 37,257,950 | 684,574 | 1,601,326 |
| **Budgetary Financing Sources:** | | | |
| Appropriations received | 114,277,138 | 3,484,834 | 6,463,959 |
| Appropriations transferred-in/out (+/-) | 2,135,606 | -50,761 | 94,961 |
| Other adjustments (rescissions, etc) (+/-) | -1,702,246 | -54,446 | -66,452 |
| Appropriations used | -103,901,479 | -3,108,199 | -6,047,163 |
| Nonexchange revenue | 0 | 0 | 0 |
| Donations and forfeitures of cash and cash equivalents | 0 | 0 | 0 |
| Transfers-in/out without reimbursement (+/-) | 0 | 0 | 0 |
| Other budgetary financing sources (+/-) | 0 | 0 | 0 |
| **Other Financing Sources:** | | | |
| Donations and forfeitures of property | 0 | 0 | 0 |
| Transfers-in/out without reimbursement (+/-) | 0 | 0 | 0 |
| Imputed financing from costs absorbed by others | 0 | 0 | 0 |
| Other (+/-) | 0 | 0 | 0 |
| **Total Financing Sources** | 10,809,019 | 271,428 | 445,305 |
| **Net Cost of Operations (+/-)** | 0 | 0 | 0 |
| **Ending Balances** | $ 48,066,969 | $ 956,002 | $ 2,046,631 |



*The accompanying notes are an integral part of the financial statements. See notes 1 and 20.*

| Component Level | Combined Total | Eliminations | 2003 Consolidated | 2002 Consolidated |
|---|---|---|---|---|
| $ 0 | $ 47,443,218 | $ 0 | $ 47,443,218 | $ 70,732,397 |
| 0 | 122,475,076 | 0 | 122,475,076 | -31,869,730 |
| 0 | 169,918,294 | 0 | 169,918,294 | 38,862,667 |
| | | | | |
| 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 |
| 327,285 | 113,384,126 | 0 | 113,384,126 | 99,437,408 |
| 0 | 0 | 0 | 0 | 0 |
| 0 | 9,096 | 0 | 9,096 | 12,682 |
| 0 | 0 | 0 | 0 | 0 |
| -678,772 | -678,772 | 0 | -678,772 | 246,474 |
| | | | | |
| 0 | 0 | 0 | 0 | 0 |
| 678,772 | -110,688 | 0 | -110,688 | 26,728 |
| 0 | 632,990 | 0 | 632,990 | 597,076 |
| 0 | 0 | 0 | 0 | 0 |
| 327,285 | 113,236,752 | 0 | 113,236,752 | 100,320,368 |
| 327,284 | 121,827,362 | 0 | 121,827,362 | 91,739,815 |
| $ 1 | $ 161,327,684 | $ 0 | $ 161,327,684 | $ 47,443,220 |
| | | | | |
| $ 0 | $ 39,543,850 | $ 0 | $ 39,543,850 | $ 39,006,789 |
| 0 | 0 | 0 | 0 | 0 |
| 0 | 39,543,850 | 0 | 39,543,850 | 39,006,789 |
| | | | | |
| 0 | 124,225,931 | 0 | 124,225,931 | 96,952,072 |
| 0 | 2,179,806 | 0 | 2,179,806 | 5,084,803 |
| 0 | -1,823,144 | 0 | -1,823,144 | -2,062,406 |
| -327,285 | -113,384,126 | 0 | -113,384,126 | -99,437,408 |
| 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 |
| | | | | |
| 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 |
| -327,285 | 11,198,467 | 0 | 11,198,467 | 537,061 |
| 0 | 0 | 0 | 0 | 0 |
| $ -327,285 | $ 50,742,317 | $ 0 | $ 50,742,317 | $ 39,543,850 |

*The accompanying notes are an integral part of the financial statements. See notes 1 and 20.*

# Combining Statement of Budgetary Resources—General Funds

For the years ended September 30, 2003 and 2002 ($ in thousands)

| | Air Force Active | Air Force Reserve |
|---|---|---|
| **BUDGETARY FINANCING ACCOUNTS** | | |
| **BUDGETARY RESOURCES** | | |
| Budget Authority: | | |
| Appropriations received | $ 114,286,930 | $ 3,484,834 |
| Borrowing authority | 0 | 0 |
| Contract authority | 0 | 0 |
| Net transfers (+/-) | 1,844,015 | -50,761 |
| Other | 0 | 0 |
| Unobligated balance: | | |
| Beginning of period | 5,679,549 | 113,745 |
| Net transfers, actual (+/-) | 291,591 | 0 |
| Anticipated Transfers Balances | 0 | 0 |
| Spending authority from offsetting collections: | | |
| Earned | 0 | 0 |
| Collected | 6,486,849 | 313,290 |
| Receivable from Federal sources | -221,039 | 19,753 |
| Change in unfilled customer orders | 0 | 0 |
| Advance received | 213,488 | 0 |
| Without advance from Federal sources | 471,878 | 0 |
| Anticipated for the rest of year, without advances | 0 | 0 |
| Transfers from trust funds | 0 | 0 |
| Subtotal | 6,951,176 | 333,043 |
| Recoveries of prior year obligations | 1,780,895 | 68,449 |
| Temporarily not available pursuant to Public Law | 0 | 0 |
| Permanently not available | -1,685,464 | -54,446 |
| **Total Budgetary Resources** | $ 129,148,692 | $ 3,894,864 |
| **STATUS OF BUDGETARY RESOURCES** | | |
| Obligations incurred: | | |
| Direct | $ 113,494,306 | $ 3,395,967 |
| Reimbursable | 6,992,486 | 335,988 |
| Subtotal | 120,486,792 | 3,731,955 |
| Unobligated balance: | | |
| Apportioned | 8,118,892 | 44,182 |
| Exempt from apportionment | 2,573 | 0 |
| Other available | 0 | 0 |
| Unobligated Balances Not Available | 540,435 | 118,727 |
| **Total, Status of Budgetary Resources** | $ 129,148,692 | $ 3,894,864 |
| **Relationship of Obligations to Outlays:** | | |
| Obligated Balance, Net - beginning of period | $ 39,649,646 | $ 784,727 |
| Obligated Balance transferred, net (+/-) | 0 | 0 |
| Obligated Balance, Net - end of period: | | |
| Accounts receivable | -941,384 | -61,674 |
| Unfilled customer order from Federal sources | -936,902 | 0 |
| Undelivered orders | 40,783,010 | 788,290 |
| Accounts payable | 8,848,157 | 160,912 |
| Outlays: | | |
| Disbursements | 110,351,823 | 3,540,953 |
| Collections | -6,700,337 | -313,290 |
| Subtotal | 103,651,486 | 3,227,663 |
| Less: Offsetting receipts | -156,704 | 0 |
| **Net Outlays** | $ 103,494,782 | $ 3,227,663 |

*The accompanying notes are an integral part of the financial statements. See notes 1 and 21.*

| Air National Guard | Component Level | 2003 Combined | 2002 Combined |
|---|---|---|---|
| $ 6,463,959 | $ 0 | $ 124,235,723 | $ 96,329,855 |
| 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 |
| 94,961 | 0 | 1,888,215 | 4,954,597 |
| 0 | 0 | 0 | 0 |
| 273,216 | 0 | 6,066,510 | 7,203,289 |
| 0 | 0 | 291,591 | 130,206 |
| 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 |
| 1,002,408 | 0 | 7,802,547 | 6,551,584 |
| -121,632 | 0 | -322,918 | 274,507 |
| 0 | 0 | 0 | 0 |
| -23 | 0 | 213,465 | 106,478 |
| 289 | 0 | 472,167 | -1,182 |
| 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 |
| 881,042 | 0 | 8,165,261 | 6,931,387 |
| 106,615 | 0 | 1,955,959 | 1,051,593 |
| 0 | 0 | 0 | 0 |
| -66,452 | 0 | -1,806,362 | -2,062,413 |
| $ 7,753,341 | $ 0 | $ 140,796,897 | $ 114,538,514 |
| $ 6,485,293 | $ 0 | $ 123,375,566 | $ 100,622,101 |
| 902,912 | 0 | 8,231,386 | 7,849,904 |
| 7,388,205 | 0 | 131,606,952 | 108,472,005 |
| 157,521 | 0 | 8,320,595 | 5,268,178 |
| 0 | 0 | 2,573 | 4,607 |
| -1 | 0 | -1 | -1 |
| 207,616 | 0 | 866,778 | 793,725 |
| $ 7,753,341 | $ 0 | $ 140,796,897 | $ 114,538,514 |
| $ 1,387,822 | $ 0 | $ 41,822,195 | $ 37,049,171 |
| 0 | 0 | 0 | 0 |
| -155,989 | 0 | -1,159,047 | -1,481,965 |
| -472 | 0 | -937,374 | -465,207 |
| 1,646,108 | -1,048,762 | 42,168,646 | 34,030,703 |
| 411,529 | 1,048,762 | 10,469,360 | 9,738,663 |
| 6,889,580 | 0 | 120,782,356 | 102,374,064 |
| -1,002,386 | 0 | -8,016,013 | -6,658,063 |
| 5,887,194 | 0 | 112,766,343 | 95,716,001 |
| 0 | 0 | -156,704 | -121,154 |
| $ 5,887,194 | $ 0 | $ 112,609,639 | $ 95,594,847 |

*The accompanying notes are an integral part of the financial statements. See notes 1 and 21.*

# Combining Statement of Financing—General Funds

For the years ended September 30, 2003 and 2002 ($ in thousands)

| | Air Force Active | Air Force Reserve |
|---|---|---|
| **Resources Used to Finance Activities:** | | |
| Budgetary Resources Obligated | | |
| Obligations incurred | $ 120,486,792 | $ 3,731,955 |
| Less: Spending authority from offsetting collections and recoveries (-) | -8,732,071 | -401,492 |
| Obligations net of offsetting collections and recoveries | 111,754,721 | 3,330,463 |
| Less: Offsetting receipts (-) | -156,704 | 0 |
| Net obligations | 111,598,017 | 3,330,463 |
| Other Resources | | |
| Donations and forfeitures of property | 0 | 0 |
| Transfers in/out without reimbursement (+/-) | -2,360,484 | 150,229 |
| Imputed financing from costs absorbed by others | 632,992 | 0 |
| Other (+/-) | 0 | 0 |
| Net other resources used to finance activities | -1,727,492 | 150,229 |
| **Total resources used to finance activities** | 109,870,525 | 3,480,692 |
| | | |
| **Resources Used to Finance Items not Part of the Net Cost of Operations** | | |
| Change in budgetary resources obligated for goods, services and benefits ordered but not yet provided | | |
| Undelivered Orders (-) | -8,150,890 | -169,048 |
| Unfilled Customer Orders | 685,366 | 0 |
| Resources that fund expenses recognized in prior periods | 0 | 0 |
| Budgetary offsetting collections and receipts that do not affect net cost of operations | 9,106 | 0 |
| Resources that finance the acquisition of assets | -18,839,045 | -164,394 |
| Other resources or adjustments to net obligated resources that do not affect net cost of operations | | |
| Less: Trust or Special Fund Receipts Related to Exchange in the | 0 | 0 |
| Other (+/-) | 2,360,484 | -150,229 |
| **Total resources used to finance items not part of the net cost of operations** | -23,934,979 | -483,671 |
| **Total resources used to finance the net cost of operations** | 85,935,546 | 2,997,021 |
| | | |
| **Components of the Net Cost of Operations that will not Require or Generate Resources in the Current Period:** | | |
| Components Requiring or Generating Resources in Future Periods: | | |
| Increase in annual leave liability | 469,832 | 7,374 |
| Increase in environmental and disposal liability | -344,161 | 0 |
| Upward/Downward reestimates of credit subsidy expense (+/-) | 0 | 0 |
| Increase in exchange revenue receivable from the the public (-) | 0 | 0 |
| Other (+/-) | 1,955 | 4,801 |
| Total components of Net Cost of Operations that will require or generate resources in future periods | 127,626 | 12,175 |
| Components not Requiring or Generating Resources: | | |
| Depreciation and amortization | 12,874,631 | 78,154 |
| Revaluation of assets or liabilities (+/-) | 1,607,548 | -22,448 |
| Other (+/-) | 11,760,010 | -81,761 |
| Total components of Net Cost of Operations that will not require or generate resources | 26,242,189 | -26,055 |
| **Total components of net cost of operations that will not require or generate resources in the current period** | 26,369,815 | -13,880 |
| **Net Cost of Operations** | 112,305,361 | 2,983,141 |



*The accompanying notes are an integral part of the financial statements. See notes 1 and 22.*

| Air National Guard | Component Level | 2003 Combined | 2002 Combined |
|---|---|---|---|
| $ 7,388,205 | $ 0 | $ 131,606,952 | $ 108,472,005 |
| -987,658 | 0 | -10,121,221 | -7,982,980 |
| 6,400,547 | 0 | 121,485,731 | 100,489,025 |
| 0 | 0 | -156,704 | -121,154 |
| 6,400,547 | 0 | 121,329,027 | 100,367,871 |
| 0 | 0 | 0 | 0 |
| 1,420,795 | 678,772 | -110,688 | 26,727 |
| 0 | 0 | 632,992 | 597,076 |
| 0 | 0 | 0 | 0 |
| 1,420,795 | 678,772 | 522,304 | 623,803 |
| 7,821,342 | 678,772 | 121,851,331 | 100,991,674 |
| -338,490 | 327,285 | -8,331,143 | -2,222,784 |
| 267 | 0 | 685,633 | 105,295 |
| 0 | 0 | 0 | -651,941 |
| 0 | 0 | 9,106 | 0 |
| -117,274 | 0 | -19,120,713 | -10,859,967 |
| 0 | 0 | 0 | 0 |
| -1,420,795 | -678,772 | 110,688 | 0 |
| -1,876,292 | -351,487 | -26,646,429 | -13,629,397 |
| 5,945,050 | 327,285 | 95,204,902 | 87,362,277 |
| 1,135 | 0 | 478,341 | -71,316 |
| 0 | 0 | -344,161 | 1,117,408 |
| 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 |
| 8,014 | 0 | 14,770 | 73,202 |
| 9,149 | 0 | 148,950 | 1,119,294 |
| 330,079 | 0 | 13,282,864 | 1,795,095 |
| 55,943 | 0 | 1,641,043 | 3,715,480 |
| -128,646 | 0 | 11,549,603 | -2,252,331 |
| 257,376 | 0 | 26,473,510 | 3,258,244 |
| 266,525 | 0 | 26,622,460 | 4,377,538 |
| 6,211,575 | 327,285 | 121,827,362 | 91,739,815 |

*The accompanying notes are an integral part of the financial statements. See notes 1 and 22.*

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# Required Supplementary Stewardship Information

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# National Defense Property, Plant and Equipment

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

**Heritage Assets**
For Fiscal Year Ended September 2003

| | Measurement Quantities | As of 10/01/02 | Additions | Deletions | As of 9/30/03 |
|---|---|---|---|---|---|
| Museums | Each | 18 | 0 | 0 | 18 |
| Monuments & Memorials | Each | 151 | 0 | 0 | 151 |
| Cemeteries | Sites | 39 | 0 | 0 | 39 |
| Archeological Sites | Sites | 1,685 | 0 | 0 | 1,685 |
| Buildings & Structures | Each | 4,074 | 0 | 0 | 4,074 |
| Major Collections | Each | 4 | 0 | 0 | 4 |

## 1. Museums

The Air Force Museum, located at Wright-Patterson Air Force Base, Ohio, houses the main collection of historical artifacts that are registered as historical property in the USAF Museum System. The other 17 Air Force museums are considered Air Force Field Museums or Heritage Centers, which also contain items of historical interest; some however, are specific to the general locality.

All remaining museums and Heritage Centers are reported in acceptable condition.

## 2. Monuments and Memorials

The memorials and monuments reported above, except for 28, are all located at the Air Force Academy in the Air Gardens and Honor Court. Most of these monuments and memorials honor specific individuals or cadet wings for various accomplishments. The remaining 28 memorials, all with costs that exceed $100,000, are located on various Air Force bases throughout the United States. All are reported in acceptable condition.

## 3. Cemeteries

The Air Force has administrative and curatorial responsibilities for 39 cemeteries on its bases. The cemeteries are maintained by the bases and are in good condition.

## 4. Archeological Sites

As of 30 September 2003, the AF has 1,685 archeological sites listed on or eligible for the National Register. The AF has 9,779 potentially eligible archeological sites, and 2,464 non-eligible archaeological sites, neither are listed on this report. The numbers of archaeological sites will increase yearly as the AF completes surveys in compliance with the National Historic Preservation Act. The number of archaeological sites on AF managed lands is reported each year in the Report to Congress on Federal Archaeological Activities (FY02 report submitted March 03). The identified sites are maintained in an acceptable condition.

## 5. Buildings and Structures

The Air Force currently considers 4,074 buildings and structures as heritage assets. Most of these buildings and structures are considered Multi-use Heritage Assets, and as such, have been reported as general Property, plant and equipment on the Balance Sheet. The buildings and structures are maintained by each base civil engineering group and are considered to be in good condition.

## 6. Major Collections

The Air Force has 4 significant or major collections consisting of: (a) the Air Force Art Collection, and (b) three collections at the Air Force Academy containing historical items and memorabilia as well as distinctive works of art. The curators for all major collections reported the contents to be in good condition. They further added that almost all of the materials are protected in an environment suitable for long-term storage. The overall condition of the collections in the museums is good; items are displayed and protected in accordance with the standards of Air Force Instruction 84-103, USAF Museum System.

**Stewardship Land**
For Fiscal Year Ended September 2003 (Acres in Thousands)

| (a) Land Use | (b) As of 10/01/02 | (c) Additions | (d) Deletions | (e) As of 9/30/03 |
|---|---|---|---|---|
| 1. Mission | 7,728 | 0 | 0 | 7,728 |
| 2. Parks and Historic Sites | - | | | - |
| Totals | 7,728 | 0 | 0 | 7,728 |

The Air Force has 7,728 acres of mission-essential land under their administration. Lands purchased by the Air Force with the intent to construct buildings or facilities are considered general PP&E and are reported on the balance sheet. All stewardship lands, as reported, are in acceptable condition, based on designated use.

**Nonfederal Physical Property**
Yearly Investment in State and Local Governments
For Fiscal Years 1999 through FY 2003 ($ in millions)

| Categories | FY 1999 | FY 2000 | FY 2001 | FY 2002 | FY 2003 |
|---|---|---|---|---|---|
| Funded Assets: | | | | | |
| National Defense Mission Related | $16.60 | $6.80 | $20.20 | $21.30 | $11.31 |
| Total | $16.60 | $6.80 | $20.20 | $21.30 | $11.31 |

The Air National Guard investments in non-federal physical property are strictly through the Military Construction Cooperative Agreements (MCCAs). These agreements involve the transfer of money only and allow joint participation with States, Counties, and Airport Authorities for construction or repair of airfield pavements and facilities required to support the flying mission assigned at these civilian airfields

Investment values included in this report are based on Nonfederal Physical Property outlays (expenditures). Outlays are used because current DoD systems are unable to capture and summarize costs in accordance with the Federal Accounting Standards requirements.

**Investments in Research and Development**
Yearly Investment in Research and Development
For Fiscal Years 1999 through 2003 ($ in millions)

| Categories | FY 1999 | FY 2000 | FY 2001 | FY 2002 | 2003 |
|---|---|---|---|---|---|
| 1. Basic Research | $187 | $206 | $203 | $208 | $141 |
| 2. Applied Research | 543 | 577 | 637 | 666 | 510 |
| 3. Development | | | | | |
| Advanced Technology Development | 456 | 554 | 545 | 492 | 399 |
| Advanced Component Development and Prototypes | 1,101 | 899 | 1,237 | 884 | 1,065 |
| System Development and Demonstration | 4,296 | 4,251 | 3,279 | 3,194 | 2,903 |
| Research, Development, Test and Evaluation Management Support | 1,034 | 768 | 777 | 769 | 597 |
| Operational Systems Development | 6,647 | 7,096 | 7,295 | 7,225 | 7,864 |
| Totals | $14,264 | $14,351 | $13,973 | $13,438 | $13,479 |

**Basic Research** is the systematic study to gain knowledge or understanding of the fundamental aspects of phenomena and of observable facts without specific applications, processes, or products in mind. Basic Research involves the gathering of a fuller knowledge or understanding of the subject under study. Major outputs are scientific studies and research papers.

**Applied Research** is the systematic study to gain knowledge or understanding necessary for determining the means by which a recognized and specific need may be met. It is the practical application of such knowledge or understanding for the purpose of meeting a recognized need. This research points toward specific military needs with a view toward developing and evaluating the feasibility and practicability of proposed solutions and determining their parameters. Major outputs are scientific studies, investigations, and research papers, hardware components, software codes, and limited construction of, or part of, a weapon system to include nonsystem specific development efforts.

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

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

2. Advanced Component Development and Prototypes evaluates integrated technologies in as realistic an operating environment as possible to assess the performance or cost reduction potential of advanced technology. Programs in this phase are generally system specific. Major outputs of Advanced Component Development and Prototypes are hardware and software components, or complete weapon systems, ready for operational and developmental testing and field use.

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

4. RDT&E Management Support is support for installations and operations for general research and development use. This category includes costs associated with test ranges, military construction maintenance support for laboratories, operations and maintenance of test aircraft and ships, and studies and analysis in support of the R&D program.

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

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

**Basic Research**—The Air Force's (AF) Basic Research program funded basic scientific disciplines that are core to developing future warfighting capabilities. Funding was provided to twelve different scientific project areas. These focused on atmospherics, biological sciences, chemistry, electronics, fluid mechanics, human performance, materials, mathematical and computer sciences, physics, propulsion, space sciences, and structures. (1) One example is the development of technology that could be the breakthrough for a new generation of computers (quantum computers). The AF Research Lab (AFRL) demonstrated the ability to stop light and release it again without losing any of its original characteristics. This development could lead to a breakthrough in nonlinear optics with applications from telecommunications to imaging, which could be useful in designing ultra-sensitive optical switches. (2) Another example, AFRL researchers developed a new mathematical theory that would result in a new radar wave that would aid in rapid and accurate target identification through foliage and beneath soil, better than any radar currently in use.

**Applied Research**—The AF's Applied Research program is developing technologies to support the air and space force of the future. Technology developments are focused in those areas that are essential to these warfighting capabilities. This investment strategy allows the AF to focus on those military-relevant technologies that are not being developed by industry. (1) One example is the F119 turbine engine case redesign using a new casting process, with a predicted lifecycle cost savings of 35 percent. The redesign makes extensive use of thin-wall castings in place of the

existing complex, multi-walled, and diffusion-bonded sheet metal assemblies. The AF is now looking at this technology for use on other aircraft engines. Example two, AFRL recently achieved a milestone in wireless Internet communications with the first commercial installation of the Space Communications Protocol Standards (SCPS) transport gateway over National Aeronautics and Space Administration's Advanced Communications Technology Satellite. The SCPS transport gateway offers up to several times the bandwidth utilization efficiency of the well-known internet protocols.

**Advanced Technology Development**—The AF's Advanced Technology Development program demonstrates, in a realistic operational environment, integrated sets of technology to prove military worth and utility. The first example was the AF and the Defense Advanced Research Projects Agency accomplishing the first Unmanned Combat Air Vehicle (UCAV) flight. This successful flight test demonstrated the command and control links between the aircraft and a mission-oriented ground station. Secondly, AFRL also demonstrated a 330 Gigahertz detector that operates at frequencies billions of times faster than the blink of an eye. This technology will be used to produce compact solid-state circuits operating at Terahertz frequencies. Likely technology application would be to enable a new generation of sensors to enhance homeland security.

**Demonstration and Validation**—The AF's Advanced Component Development and Prototypes (ACD&EP) programs are comprised of system specific advanced technology integration efforts accomplished in an operational environment to help expedite transition from the laboratory to operational use. Example of the AF's Demonstration and Validation effort is: The Command and Control System - Consolidated (CCS-C) program. The CCS-C will replace the aging S-Band Command and Control Segment (CCS) that is currently used for the command and control of Military Satellite Communications satellites (MILSATCOM) by the 50th Space Wing (50SW) at Schriever AFB. The CCS-C system selected will drastically reduce the sustainment costs that would have been needed to maintain the aging CCS and offers tremendous enhancements to ease our satellite operators' workload, enabling accurate and efficient control of MILSATCOM satellites. The system is scheduled to take over command and control of MILSATCOM satellites at the end of fiscal year 2004. In FY03, the AF awarded contracts for development of Transformational Communications Architecture and approved the program acquisition strategy and architecture. The Transformational Satcom Program (TSAT) will develop key technologies such as laser communications, internet-like communications protocols, and methods of dynamically allocating communications among users. The ultimate goal is a FY10 first launch of a transformational satellite.

**Engineering and Manufacturing Development**—The AF's System Demonstration and Engineering Development (SD&ED) efforts are development projects which have not received approval for full-production. Examples of AF EMD efforts are: (1) The Space Based Infrared System Increment 1 Mission Control Station (MCS) achieved initial operational capability on 18 December 2001. The MCS consolidates Defense Support Program operations at Buckley AFB, Colorado, reducing manpower by 58 percent and operations and maintenance costs by 25 percent. Subsequent upgrades to the MCS throughout fiscal year 2002 resulted in closure of the Air-Land Enhanced Reconnaissance and Targeting ALERT ground station on 25 September 2002, consolidating all space-based strategic and theater missile warning operations, realizing additional manpower and Operations and Maintenance funds savings. (2) Another example, The Fighter/Attack (F/A)-22 Program is developing the next generation air dominance fighter designed to penetrate enemy airspace and achieve a first look, first kill capability against multiple targets. The F/A-22's combination of stealth, supercruise, maneuverability, and integrated avionics, coupled with improved supportability, represents an exponential leap in warfighting capabilities and allows for the full realization of operational concepts that are vital to the 21st century Air Force. The F/A-22 will replace the F-15C as the frontline USAF air superiority fighter with initial operational capability planned for December 2005. The F/A-22 has been in Engineering and Manufacturing Development (EMD) since 1991 and is currently meeting or exceeding all Key Performance Parameters. Significant program accomplishments in fiscal year 2002 include:

- Continued 2nd full-scale airframe lifetime fatigue test
- Initiated avionics software Block 3.1.2 FT-3 flight testing

- Completed multiple supersonic AMRAAM and AIM-9 missile shots
- Exceeded 2000 flight test missions, logging in over 4100 hours on the EMD aircraft fleet

The F-35 Joint Strike Fighter (JSF) program is developing a family of strike fighter aircraft for the Air Force, Navy, Marine Corps and our allies, with maximum commonality among the variants to minimize life cycle costs. The AF Conventional Takeoff and Landing (CTOL) variant will be a multi-role, primary air-to-ground aircraft to replace the F-16 and A-10 and complement the F/A-22. While the F/A-22 will establish air dominance, the F-35-with its combination of stealth, large internal payloads and multi-spectral avionics-will provide persistent stealth and precision engagement to the future battlespace. The F-35 has been in System Development and Demonstration since 2001 and is currently meeting or exceeding all Key Performance Parameters. In fiscal year 2003, the program completed the Air System Preliminary Design Review and the Pratt & Whitney F135 Engine Critical Design Review and continued General Electric's development of a second, interchangeable engine (F136) for competition in production. Additionally, the program continued the International Commonality Effort to identify an ORD compliant configuration for international partners that maximizes commonality with the US baseline program consistent with National Disclosure Policy. The B-1B Defensive System Upgrade Program (DSUP) was canceled in December 2002 due to repeated cost and schedule over-runs. However, the AF continued to improve the B-1B's effectiveness through integration of new computers and advanced conventional weapons. Combined Developmental and Operational Testing (DT/OT) for the new computers completed in July, and dedicated operational testing completed in December 2002. Testing showed the computers met or exceeded all Key Performance Parameters and they were approved for full rate production in April 2003. Combined DT/OT flight test for the integration of JSOW and JASSM onto the B-1 began in September 2003 and is scheduled to complete in April 2004.

**Research, Development, Test and Evaluation Management Support**—The Air Force's Research, Development, Test and Evaluation (RDT&E) Management Support efforts include projects directed toward support of installation or operations required for general research and development use. Included would be test ranges, military construction, maintenance support of laboratories, operation and maintenance of test aircraft and ships, and studies and analysis in support of the research and development program. Example of AF RDT&E management support is: The Major Test and Evaluation Investment program, which funds the planning, improvements and modernization for three national asset test centers having over $10 billion of unique test facilities/capabilities operated and maintained by the AF for the Department of Defense (DoD) test and evaluation missions, and available to others having a requirement for their unique capabilities. Many efforts are contained within this program, but two examples are the Propulsion Wind Tunnel Upgrade at Arnold Engineering Development Center. This effort replaces outdated data acquisition, processing, and control systems and drive motors. The second is the Threat Simulator Development program, which supports many of the AF electronic Warfare Test Processes. Current projects focus on improved Low Radar Cross Section threat modeling and simulation, and enhanced infrared and radio frequency countermeasures testing.

**Operational Systems Development**—The AF's operational system efforts include projects in support of development acquisition programs or upgrades in System Demonstration and Development (SDD). Examples of operational systems development are: (1) AIM9X Sidewinder project, which improves seeker performance, infrared counter-countermeasures, and kinematics of the AIM-9M short range air-to-air missile. AIM-9X regains short, within visual range (WVR) first-shot, first-kill capability for the U.S. warfighter. Test and Evaluation efforts have been positive, 18 of 19 successful guided launches with 10 direct hits to target drones. Other notable accomplishments include completion of flight test activities, such as, Operations/Operational Evaluation (OPEVAL) and Developmental Test (DT) assist. Low Rate Initial Production (LRIP 3) contract was awarded November 2002. (2) Another example of Operational Systems Development is the Airborne Warning and Control System (AWACS) Block 40/45 system upgrade. Block 40/45 replaces the 1970's vintage mission computer system with an open system, LAN-based architecture. It also incorporates Multi-Sensor Integration of on-board and off-board sensors into a real-time database allowing for a "single target-single track" to be displayed to the operator and transmitted to the shooter. Block 40/45 also incorporates

an improved Data Link Infrastructure that decreases the latency of data link transmissions for high priority targets, thus allowing targets to be transmitted quickly to the shooter. This upgrade improves machine-to-machine interfaces that ultimately compress the kill chain timeline and postures the system to more easily integrate future modifications and support. These future modifications will support horizontal integration and network centric operations. Initial System Development and Design began this year. The first of a series of planned upgrades to the B-2 Spirit Bomber entered flight test in FY03. This bundled package of capability includes the upgraded, or "Smart" Bomb Rack Assembly; ability to drop the 500 lb Joint Direct Attack Munition (JDAM) Mark 82; ability to drop the Enhanced Guided Bomb Unit-28 (EGBU-28) bunker buster; and addition of improved voice and data communication via integration of a programmable UHF satellite communication terminal. Incorporation of this upgraded package into the fleet will begin in FY04. Development of an extended range variant of the Wind Corrected Munitions Dispenser (WCMD-ER) was initiated in FY03. The project extends the range and improves the accuracy of WCMD by adding a wing kit and integrating GPS into the tail kit for CBU-105 (anti-armor targets) and CBU-103 (soft and area targets) dispensers. Th Air Force Space program achieved nine successful launches of military satellites, utilizing Titan and Delta to launch Milstar-5 and -6, GPS IIR-8 and -9, DSCS A3 and B6, Coriolis, NOAA-M, and NROL-19. USAF launch ranges successfully supported 23 military, civil and commercial launches, and EELV completed three successful Atlas V launches and three successful Delta IV launches.

# Required Supplementary Information

# Disaggregated Statement of Budgetary Resources—General Funds

For the years ended September 30, 2003 and 2002 ($ in thousands)

| | Other | Research, Development, Test & Evaluation | Operation and Maintenance |
|---|---|---|---|
| **BUDGETARY RESOURCES** | | | |
| 1. Budget Authority: | | | |
| 1a. Appropriations received | $ 399,564,874 | $ 19,041,149,000 | $ 43,189,230,000 |
| 1b. Borrowing authority | 0 | 0 | 0 |
| 1c. Contract authority | 0 | 0 | 0 |
| 1d. Net transfers (+/-) | -387,587,000 | 23,596,000 | 1,112,746,000 |
| 1e. Other | 0 | 0 | 0 |
| 2. Unobligated balance: | | | |
| 2a. Beginning of period | 4,778,098 | 1,444,010,253 | 746,222,986 |
| 2b. Net transfers, actual (+/-) | 0 | 7,000,000 | 184,836,000 |
| 2c. Anticipated Transfers balances | 0 | 0 | 0 |
| 3. Spending authority from offsetting collections: | | | |
| 3a. Earned | 0 | 0 | 0 |
| 1. Collected | 11,312,448 | 2,563,027,895 | 4,591,770,723 |
| 2. Receivable from Federal sources | 234,914 | -68,727,346 | -335,605,805 |
| 3b. Change in unfilled customer orders | 0 | 0 | 0 |
| 1. Advance received | 0 | 153,420,819 | 54,810,939 |
| 2. Without advance from Federal sources | 0 | 39,310,033 | 403,302,336 |
| 3c. Anticipated for the rest of year, without advances | 0 | 0 | 0 |
| 3d. Transfers from trust funds | 0 | 0 | 0 |
| 3e. Subtotal | 11,547,363 | 2,687,031,401 | 4,714,278,193 |
| 4. Recoveries of prior year obligations | 26,197 | 99,801,336 | 788,941,102 |
| 5. Temporarily not available pursuant to Public Law | 0 | 0 | 0 |
| 6. Permanently not available | -2,186,000 | -295,743,692 | -620,909,907 |
| **7. Total Budgetary Resources** | $ 26,143,532 | $ 23,006,844,298 | $ 50,115,344,375 |
| **STATUS OF BUDGETARY RESOURCES** | | | |
| 8. Obligations incurred: | | | |
| 8a. Direct | 11,809,663 | 18,282,333,179 | 44,420,505,233 |
| 8b. Reimbursable | 11,547,363 | 2,718,067,428 | 4,834,930,030 |
| 8c. Subtotal | 23,357,026 | 21,000,400,607 | 49,255,435,263 |
| 9. Unobligated balance: | | | |
| 9a. Apportioned | 213,601 | 2,312,001,788 | 171,120,994 |
| 9b. Exempt from apportionment | 2,572,906 | 0 | 0 |
| 9c. Other available | 0 | 0 | 0 |
| 10. Unobligated Balances Not Available | 0 | -305,558,097 | 688,788,117 |
| **11. Total, Status of Budgetary Resources** | $ 26,143,532 | $ 23,006,844,298 | $ 50,115,344,375 |
| **RELATIONSHIP OF OBLIGATIONS TO OUTLAYS:** | | | |
| 12. Obligated Balance, Net - beginning of period | $ 8,058,878 | $ 6,210,426,030 | $ 12,614,633,349 |
| 13. Obligated Balance transferred, net (+/-) | 0 | 0 | 0 |
| 14. Obligated Balance, Net ? end of period: | | | |
| 14a. Accounts receivable | -234,914 | -240,872,139 | -786,074,916 |
| 14b. Unfilled customer order from Federal sources | 0 | -339,927,258 | -472,284,834 |
| 14c. Undelivered orders | -1,047,997,865 | 6,224,217,313 | 16,920,847,061 |
| 14d. Accounts payable | 1,050,526,755 | 1,510,066,910 | 2,594,840,283 |
| 15. Outlays: | | | |
| 15a. Disbursements | 28,860,816 | 19,986,957,789 | 42,756,103,384 |
| 15b. Collections | -11,312,448 | -2,716,448,714 | -4,646,581,662 |
| 15c. Subtotal | 17,548,368 | 17,270,509,075 | 38,109,521,722 |
| 16. Less: Offsetting receipts | 0 | 0 | 0 |
| **17. Net Outlays** | $ 17,548,368 | $ 17,270,509,075 | $ 38,109,521,722 |

| Procurement | Military Personnel | Military Construction/ Family Housing | 2003 Combined | 2002 Combined |
|---|---|---|---|---|
| $ 30,739,027,000 | $ 28,677,742,000 | $ 2,189,010,000 | $ 124,235,722,874 | $ 96,329,854,921 |
| 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 |
| 1,077,290,000 | 54,570,000 | 7,600,000 | 1,888,215,000 | 4,954,597,000 |
| 0 | 0 | 0 | 0 | 0 |
| 2,908,146,800 | 216,460,937 | 746,890,059 | 6,066,509,133 | 7,203,288,054 |
| 17,694,000 | 101,608,000 | -19,547,000 | 291,591,000 | 130,206,000 |
| 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 |
| 229,694,234 | 406,742,497 | -559 | 7,802,547,239 | 6,551,584,842 |
| -1,741,207 | 82,920,940 | 559 | -322,917,945 | 274,506,845 |
| 0 | 0 | 0 | 0 | 0 |
| 5,233,523 | 0 | 0 | 213,465,280 | 106,478,088 |
| 29,554,309 | 747 | 0 | 472,167,425 | -1,182,191 |
| 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 |
| 262,740,858 | 489,664,184 | 0 | 8,165,261,999 | 6,931,387,585 |
| 671,985,212 | 377,282,497 | 17,922,574 | 1,955,958,918 | 1,051,592,829 |
| 0 | 0 | 0 | 0 | 0 |
| -688,241,154 | -175,867,192 | -23,414,244 | -1,806,362,189 | -2,062,412,391 |
| $ 34,988,642,715 | $ 29,741,460,426 | $ 2,918,461,389 | $ 140,796,896,734 | $ 114,538,513,999 |
| 29,965,006,333 | 28,766,565,641 | 1,929,345,600 | 123,375,565,648 | 100,622,100,944 |
| 257,575,095 | 409,266,531 | 0 | 8,231,386,446 | 7,849,903,922 |
| 30,222,581,427 | 29,175,832,171 | 1,929,345,600 | 131,606,952,094 | 108,472,004,866 |
| 4,698,913,752 | 159,372,832 | 978,971,015 | 8,320,593,982 | 5,268,177,863 |
| 0 | 0 | 0 | 2,572,906 | 4,607,151 |
| 0 | 0 | 0 | 0 | 0 |
| 67,147,535 | 406,255,423 | 10,144,774 | 866,777,752 | 793,724,119 |
| $ 34,988,642,715 | $ 29,741,460,426 | $ 2,918,461,389 | $ 140,796,896,734 | $ 114,538,513,999 |
| $ 18,536,934,036 | $ 2,280,250,252 | $ 2,171,892,392 | $ 41,822,194,937 | $ 37,049,171,607 |
| 0 | 0 | 0 | 0 | 0 |
| -45,908,669 | -85,956,683 | 0 | -1,159,047,321 | -1,481,965,266 |
| -125,161,726 | -747 | 0 | -937,374,565 | -465,207,140 |
| 17,700,256,155 | 22,564,017 | 2,348,758,955 | 42,168,645,636 | 34,030,703,207 |
| 3,036,758,243 | 2,212,109,777 | 65,057,419 | 10,469,359,386 | 9,738,664,136 |
| 27,493,773,148 | 28,847,161,876 | 1,669,498,485 | 120,782,355,498 | 102,374,064,052 |
| -234,927,756 | -406,742,497 | 559 | -8,016,012,519 | -6,658,062,931 |
| 27,258,845,391 | 28,440,419,379 | 1,669,499,043 | 112,766,342,979 | 95,716,001,121 |
| 0 | -156,703,544 | 0 | -156,703,544 | -121,153,981 |
| $ 27,258,845,391 | $ 28,283,715,836 | $ 1,669,499,043 | $ 112,609,639,435 | $ 95,594,847,140 |

**General Property, Plant, and Equipment**
**Real Property Deferred Sustainment Tables**
As of September 30, 2003 ($ in thousands)

| | Annual Sustainment FY 2003 | | |
|---|---|---|---|
| Property Type | Required | Actual | Difference |
| Buildings and Structures (O&M) | 1,795,325 | 1,537,513 | $257,812 |
| Buildings and Structures (MFH) | 608,550 | 398,209 | 210,341 |
| Total | $2,403,875 | $1,935,722 | $468,153 |

## Notes

1. FY03 O&M Sustainment Required is based on Facilities Sustainment Model (FSM) 03 Total Force (Air Force Active, Air National Guard, and Air Force Reserve) requirements (per request of OUSD(AT&L) to use draft DoD Financial Management Regulation, Volume 6B, Chapter 12, dated Oct 2003) less the MILPERS contribution (49%).

2. Obligations and expenditures for the RDT&E Sustainment and Restoration & Modernization (SRM) funding are not available for FY03. Beginning in FY04, RDT&E SRM funding will be managed under two new Program Elements (65976F; 65978F). Prior to FY04, obligation and expenditure data was not separately tracked for SRM and was executed within a much larger Test Support Program Element. Real Property Deferred Sustainment information will be incorporated into the FY04 Annual Statement.

3. The table above does not include NAF sustainment funding information because the systems are not able to capture the requested data on the NAF program. AF/ILERP will work with AFSVA and AF/ILVF counterparts to include the requested information for the FY04 Financial Statement.

| | Annual Deferred Sustainment Trend | | |
|---|---|---|---|
| Property Type | FY 2001 | FY 2002 | FY 2003 |
| Buildings and Structures (O&M) | 128,740 | 592,629 | 257,812 |
| Buildings and Structures (MFH) | 239,730 | 215,999 | 210,341 |
| Total | $368,470 | $808,628 | $468,153 |

## Notes

1. MFH Deferred Sustainment is based upon a combination of historical expenditures for day-to-day maintenance and condition assessment surveys for MFH real property maintenance by contract. These requirements are part of the 1999 Family Housing Master Plan.

2. Reasons For Deferred Sustainment Change (O&M) Over 10% FY03-02

a. FY01 O&M Sustainment Actuals were estimated, using the FY01 methodology, at 85 percent of the total of all maintenance, repair, and minor construction. FY02 Sustainment requirements were programmed based on 1% of AF plant replacement value however, the FY02 O&M sustainment requirement used to determine the Deferred Sustainment trend was based (per request of OUSD(AT&L) to use draft DoD Financial Management Regulation, Volume 6B, Chapter 12, dated June 2002) on FSM 04 requirements, deflated to FY02. FY03 O&M Sustainment Required uses a different baseline/methodology (see note 1, Tab 12-3) from FY01 and FY02. Comparing the Deferred Sustainment amounts for these three years as shown in Table 12-4 is an “apples to oranges” comparison, and may be largely irrelevant from a statistical perspective since three different methodologies/baselines were used.

b. O&M Sustainment was initially underfunded for FY02 due primarily to a Program Budget Decision which redirected some Sustainment funds to other Air Force readiness requirements.

| | Restoration and Modernization Requirements | | |
|---|---|---|---|
| Property Type | FY 2001 | FY 2002 | Change |
| Buildings, Structures, and Utilities | $21,000,000 | 28,400,000 | $7,400,000 |

## Notes

1. The Air Force does not maintain data on the cost to C1 for all facilities. The Installations' Readiness Report (IRR) highlights cost to C2 but that does not include the total AF backlog. FY03 and FY02 R&M requirements for Table 12-5 were therefore estimated based upon an estimated Air Force backlog. This includes the total R&M Operation and Maintenance (O&M) requirement projected for each year and non-Military Family Housing (MFH) and MFH MILCON requirements to C2 from the FY02 and FY01 IRRs, respectively. FY02 IRR Costs to C2 breakdown is: $12.5B MILCON, $5.1B for Family Housing, and $2.9B for Transportation Working Capital Fund, Defense Logistics Agency, Non-Appropriated Funds, RDT&E (Research, Development, Test, and Evaluation), Medical, other non-O&M facilities (note: this information is not included in FY02 submission). The total FY03 O&M R&M backlog is $7.9B. All R&M MILCON numbers include new footprint because the available data does not allow distinguishing between new footprint and existing footprint.

2. Reasons For Change Over 10% FY03-02

a. FY03 Submission includes $2.9B of "other" facility costs to C2; this information was not included in FY02 submission.

b. FY03 O&M R&M requirements ($7.9B) increased 27% over FY02 ($6.3B).

### Real Property Condition Information

The readiness of Air Force facilities is assessed using the IRR. The IRR assigns C-ratings ranging from C-4 (worst) to C-1 (best) facilities aggregated in nine facility classes. The FY02 IRR identified that 66 percent of Air Force facility classes were rated C-4 or C-3 (i.e. below minimal acceptable performance).

**National Defense Property, Plant, and Equipment**
**Deferred Maintenance Amounts**
As of September 30, 2003 (Amounts in Thousands)

| | |
|---|---|
| Aircraft | $2,000 |
| Other Weapons Systems | 131,843 |
| **Total** | $133,843 |

The figures presented are actual deferred maintenance amounts for FY03. The figures include Active Air Force, Air National Guard, and the Air Force Reserve.

| Schedule, Part A<br>DoD Intra-governmental Asset Balances<br>($ in thousands) | Treasury Index | Fund Balance with Treasury | Accounts Receivable | Loans Receivable | Investments | Other |
|---|---|---|---|---|---|---|
| Executive Office of the President | 11 | | $6,111 | | | |
| Department of Agriculture | 12 | | $1,217 | | | |
| Department of Commerce | 13 | | $848 | | | |
| Department of the Interior | 14 | | $2,685 | | | |
| Department of Justice | 15 | | $7,984 | | | |
| Navy General Fund | 17 | | $18,746 | | | |
| United States Postal Service | 18 | | $135 | | | |
| Department of State | 19 | | $39,821 | | | |
| Department of the Treasury | 20 | $59,766,541 | $1,467 | | $712 | |
| Army General Fund | 21 | | $19,122 | | | $1,482 |
| Office of Personnel Management | 24 | | $1 | | | |
| Social Security Administration | 28 | | $59 | | | |
| Nuclear Regulatory Commission | 31 | | $80 | | | |
| Department of Veterans Affairs | 36 | | $534 | | | |
| General Service Administration | 47 | | $831 | | | |
| National Science Foundation | 49 | | $26,390 | | | |
| Central Intelligence Agency | 56 | | $41 | | | |
| Federal Emergency Management Agency | 58 | | $62 | | | |
| Environmental Protection Agency | 68 | | $72 | | | |
| Department of Transportation | 69 | | $26,856 | | | |
| Agency for International Development | 72 | | $9,009 | | | |
| Department of Health and Human Services | 75 | | $20 | | | |
| National Aeronautics and Space Administration | 80 | | $8,841 | | | |
| National Archives and Records Administration | 88 | | $25 | | | |
| Department of Energy | 89 | | $8,348 | | | |
| Department of Education | 91 | | $115 | | | |
| US Army Corps of Engineers | 96 | | $148 | | | |
| Other Defense Organizations General Funds | 97 | | $103,136 | | | |
| Other Defense Organizations Working Capital Funds | 97-4930 | | $183,757 | | | $17,039 |
| Army Working Capital Fund | 97-4930.001 | | | | | $643 |
| Navy Working Capital Fund | 97-4930.002 | | $236 | | | $133 |
| Air Force Working Capital Fund | 97-4930.003 | | $74,731 | | | $319,796 |
| ***Totals might not match reports*** | **TOTAL** | **$59,766,541** | **$541,428** | **$0** | **$712** | **$339,093** |

| Schedule, Part B<br>DoD Intra-governmental Entity Liabilities<br>($ in thousands) | Treasury Index | Accounts Payable | Debts/ Borrowings from Other Agencies | Other |
|---|---|---|---|---|
| Department of Commerce | 13 | | | $637 |
| Department of the Interior | 14 | | | $1 |
| Department of Justice | 15 | | | $0 |
| Department of Labor | 16 | | | $332,239 |
| Navy General Fund | 17 | $16,940 | | $6,006 |
| Department of the Treasury | 20 | | | $1,110,583 |
| Army General Fund | 21 | $183,527 | | $3,434 |
| Office of Personnel Management | 24 | | | $33,037 |
| Social Security Administration | 28 | | | $71 |
| General Service Administration | 47 | | | $779 |
| Department of Transportation | 69 | | | $851 |
| National Aeronautics and Space Administration | 80 | | | $8,250 |
| Department of Energy | 89 | | | $84,336 |
| US Army Corps of Engineers | 96 | $1,619 | | $0 |
| Other Defense Organizations General Funds | 97 | $135,329 | $0 | $43,675 |
| Other Defense Organizations Working Capital Funds | 97-4930 | $534,212 | | $4 |
| Army Working Capital Fund | 97-4930.001 | $4,453 | | |
| Navy Working Capital Fund | 97-4930.002 | $10,108 | | |
| Air Force Working Capital Fund | 97-4930.003 | $527,751 | | |
| ***Totals might not match reports*** | **TOTAL** | **$1,413,939** | **$0** | **$1,623,903** |

| Schedule, Part C<br>DoD Intra-governmental Revenue and Related Costs<br>($ in thousands) | Treasury Index | Earned Revenue |
|---|---|---|
| Executive Office of the President | 11 | $9,489 |
| Department of Agriculture | 12 | $12 |
| Department of Commerce | 13 | $11,492 |
| Department of the Interior | 14 | $1,131 |
| Department of Justice | 15 | $39,319 |
| Navy General Fund | 17 | $222,803 |
| United States Postal Service | 18 | $352 |
| Department of State | 19 | $29,439 |
| Department of the Treasury | 20 | $213,243 |
| Army General Fund | 21 | $219,632 |
| Social Security Administration | 28 | $2,305 |
| Nuclear Regulatory Commission | 31 | $223 |
| Department of Veterans Affairs | 36 | $569 |
| General Service Administration | 47 | $6,663 |
| National Science Foundation | 49 | $70,000 |
| Central Intelligence Agency | 56 | $414 |
| Federal Emergency Management Agency | 58 | $136 |
| Environmental Protection Agency | 68 | $367 |
| Department of Transportation | 69 | $131,989 |
| Agency for International Development | 72 | $17,636 |
| Department of Health and Human Services | 75 | $91 |
| National Aeronautics and Space Administration | 80 | $143,058 |
| Department of Housing and Urban Development | 86 | $4 |
| National Archives and Records Administration | 88 | $25 |
| Department of Energy | 89 | $30,340 |
| Department of Education | 91 | $425 |
| US Army Corps of Engineers | 96 | $425 |
| Other Defense Organizations General Funds | 97 | $1,325,903 |
| Other Defense Organizations Working Capital Funds | 97-4930 | $1,185,854 |
| Army Working Capital Fund | 97-4930.001 | $285 |
| Navy Working Capital Fund | 97-4930.002 | $15,359 |
| Air Force Working Capital Fund | 97-4930.003 | $332,273 |
| DoD Medicare-Eligible Retiree Health Care Fund | | $178,829 |
| ***Total might not match reports*** | **TOTAL** | **$4,190,085** |

| Schedule, Part E<br>DoD Intra-governmental Non-exchange Revenues<br>($ in thousands) | Treasury Index | Transfers In | Transfers Out |
|---|---|---|---|
| Unidentifiable Federal Agency Entity (Other than DoD entities) | 0 | | $0 |
| Navy General Fund | 17 | | $6,589 |
| Army General Fund | 21 | | $108,474 |
| US Army Corps of Engineers | 96 | $1 | |
| Other Defense Organizations General Funds | 97 | $11,212 | |
| Other Defense Organizations Working Capital Funds | 97-4930 | $2,731 | $93,918 |
| Air Force Working Capital Fund | 97-4930.003 | $85,097 | $748 |
| ***Totals might not match reports*** | **TOTAL** | **$99,041** | **$209,729** |

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# Audit Opinion

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

December 4, 2003

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

SUBJECT: Independent Auditor's Report on the Air Force General Funds Fiscal Year 2003 Principal Financial Statements (Report No. D-2004-026)

The Chief Financial Officers Act of 1990, as amended, requires the Inspector General of the Department of Defense to audit the accompanying Consolidated Balance Sheet of the Air Force General Funds as of September 30, 2003 and 2002, the related Consolidated Statements of Net Cost and Changes in Net Position, and the Combined Statements of Financing[1] and Budgetary Resources for the fiscal years then ended. These financial statements are the responsibility of Air Force management. The Air Force is also responsible for implementing effective internal control and for complying with laws and regulations. We are including the required reports on internal control and compliance with laws and regulations.

## Disclaimer of Opinion on the Financial Statements

The Assistant Secretary of the Air Force (Financial Management and Comptroller) acknowledged that the Air Force previously identified material weaknesses in internal control and instances of noncompliance with laws and regulations that continue to affect the current period. As a result of those conditions, management acknowledged that the financial data reported in the financial statements were unreliable. Therefore, we did not perform auditing procedures to support material amounts on the financial statements. In addition, other auditing procedures were not performed because Section 1008(d) of the FY 2002 National Defense Authorization Act requires the Inspector General of the Department of Defense to perform only the audit procedures required by generally accepted government auditing standards that are consistent with the representations made by management. These material deficiencies also affect the reliability of certain other information contained in the accompanying Management's Discussion and Analysis and certain other information—much of which is taken from the same data sources as the principal financial statements.[2] These deficiencies would have precluded an

[1] The Office of Management and Budget requires a Consolidated Statement of Financing, instead of the Combined Statement of Financing prepared by the Air Force.

[2] Other information includes the Supporting Consolidating and Combining Financial Statements, Required Supplementary Stewardship Information, Required Supplementary Information, and Other Accompanying Information.

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

audit opinion. As described above, we are unable to express, and we do not express, an opinion on the referenced financial statements and other information.

## Summary of Internal Control

In planning and performing our audit, we considered the Air Force internal control over financial reporting and compliance. We did this to determine our procedures for auditing the financial statements and to comply with Office of Management and Budget guidance, but not to express an opinion on internal control. Accordingly, we do not express an opinion on internal control over financial reporting and compliance because previously identified reportable conditions,[3] all of which are material, continue to exist in the following areas.

- Air Force financial management systems,
- Intragovernmental Transactions,
- Fund Balance With Treasury and problem disbursements,
- accounting entries,
- operating materials & supplies,
- government furnished material and contractor acquired material,
- General Property, Plant, & Equipment (PP&E),
- Environmental Liabilities,
- Statement of Net Cost, and
- Statement of Financing.

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

## Summary of Compliance with Laws and Regulations

Our work to determine compliance with selected provisions of the applicable laws and regulations was limited because management acknowledged instances of noncompliance, and previously reported instances of noncompliance continue to exist in the following areas.

- Federal financial management systems requirements,

---

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

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

- generally accepted accounting principles, and
- United States Government Standard General Ledger.

Therefore, we did not determine whether Air Force was in compliance with all applicable laws and regulations related to financial reporting. See the Attachment for additional details on compliance with laws and regulations.

In order for DoD to comply with statutory reporting requirements and applicable financial systems requirements, the Under Secretary of Defense (Comptroller)/Chief Financial Officer is developing the DoD-wide Business Enterprise Architecture. Until the architecture is fully developed and implemented, the Air Force will be unable to fully comply with the statutory reporting requirements.

We caution that other noncompliance may have occurred and not been detected. Further, the results of our limited procedures may not be sufficient for other purposes. Our objective was not to express an opinion on compliance with applicable laws and regulations.

## Management Responsibility

Management is responsible for:

- preparing the financial statements in conformity with generally accepted accounting principles,
- establishing, maintaining, and assessing internal control to provide reasonable assurance that the broad control objectives of the Federal Managers' Financial Integrity Act (FMFIA) of 1982 are met,
- ensuring that Air Force financial management systems substantially comply with Federal Financial Management Improvement Act (FFMIA) of 1996 requirements, and
- complying with applicable laws and regulations.

Paul J. Granetto

Paul J. Granetto, CPA
Director
Defense Financial Auditing
Service

Attachment
as stated

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

# Reports on Internal Control and Compliance with Laws and Regulations

## Internal Control

Management is responsible for implementing effective internal control and for providing reasonable assurance that accounting data are accumulated, recorded, and reported properly; and that assets are safeguarded. We did not perform tests of internal control over financial reporting for the Air Force, and we did not obtain sufficient evidence to support or express an opinion on internal control. We limited our audit tests because previously identified reportable conditions, all of which are material, continue to exist in the following areas. These material internal control weaknesses significantly impair the ability of Air Force to detect and prevent fraud or theft of assets. A high risk of material misstatements will continue to exist until the internal control deficiencies are corrected.

### Air Force Financial Management Systems

- The Air Force had not implemented the U.S. Government Standard General Ledger at the transaction level, therefore, internal control over recording transactions was not sufficient to ensure that all valid transactions were accurately recorded. In addition, all recorded transactions were not accurately reported in the financial statements. For details, see Note 1.D. to the financial statements.

- The financial management systems could not report financial data in compliance with generally accepted accounting principles and OMB Bulletin 01-09, "Form and Content of Agency Financial Statements," September 25, 2001, due to limitations in the financial management processes and systems. For details, see Note 1.A. to the financial statements.

- The Air Force generally records transactions on a cash (budgetary) basis and not on an accrual basis as required by generally accepted accounting principles. The amounts presented in the Consolidated Statement of Net Cost are based on budgetary obligations and disbursements and collection transactions, and are adjusted to record known accruals for major items and known imputed expenses. For details, see Note 1.D. to the financial statements.

- The Air Force does not calculate or recognize an allowance for estimated uncollectible amounts with other Federal agencies. For details, see Note 1.K. to the financial statements.

### Intragovernmental Transactions

- Air Force internal control was not sufficient to ensure that all intragovernmental accounts receivable, accounts payable, and revenue transactions were eliminated. For details, see Note 1.G. to the financial statements.

- The Air Force was unable to reconcile intragovernmental accounts receivable or accounts payable, or reconcile intragovernmental revenue balances with its trading partners. For details, see Notes 5, 12, & 19.E. to the financial statements.

Attachment

**Fund Balance With Treasury and Problem Disbursements, Collections, & Obligations**

- At the end of FY 2003, the Air Force had $1.13 billion in problem disbursements and in-transit disbursements that have been reported by a disbursing station to the Department of the Treasury, but have not yet been precisely matched against the specific source obligation. Among other financial statement line items, this condition adversely affects the reliability of the reported value of the Air Force General Funds Balance Sheet line item, Fund Balance with Treasury. For details, see Note 21.B. to the financial statements.

- Internal control was not sufficient to provide obligations incurred and recoveries of prior year obligations in accordance with governing directives. For details, see Note 21.A. to the financial statements.

- Internal control over matching disbursements to respective obligations, and collections to respective receivables, was not sufficient to ensure all disbursements were valid and that accounts receivable and accounts payable balances were accurately stated. For details, see Note 24.B. to the financial statements.

**Accounting Entries**

The Air Force had not implemented adequate procedures to support and document all journal vouchers in the Air Force General Funds. For details, see Note 1.A. to the financial statements.

**Operating Material and Supplies**

The Air Force had not recorded operating materials and supplies in conformance with Statement of Federal Financial Accounting Standards No. 3, "Accounting for Inventory and Related Property." Internal control was not sufficient to ensure that operating materials and supplies were correctly reported. For details, see Note 9.B. to the financial statements.

**Government Furnished Material and Contractor Acquired Material**

Internal control was not sufficient to include all contractor-controlled, Government-furnished material in the financial records. For details, see Note 1.O. and 9.B. to the financial statements.

**General Property, Plant, & Equipment**

- The Department of Defense has not reported the cost of Military Equipment in accordance with generally accepted accounting standards due to an absence of detailed cost information for Military Equipment acquired over many decades. For details, see Note 10 to the financial statements.

- The Air Force has not implemented adequate controls to ensure real property account balances are accurate. Real property accounts were adjusted without supporting documentation and depreciation expense was not calculated properly.

**Environmental Liabilities**

Material uncertainties exist related to environmental cleanup liabilities due to incomplete documentation for cleanup costs. For details, see Note 14 to the financial statements.

**Statement of Net Cost**

The Air Force does not accumulate cost information as required by generally accepted accounting principles. The Air Force identifies costs in the Consolidated Statement of Net Cost based on the major appropriation groups funded by Congress instead of being based on major programs and activities as set forth in Statement of Federal Financial Accounting Standards No. 4, "Managerial Cost Accounting Concepts and Standards for the Federal Government." For details, see Note 1.D. to the financial statements.

**Statement of Financing**

- The Air Force cannot reconcile budgetary data with proprietary expenses and assets capitalized without making unsupported adjustments to resolve differences. For details, see Note 22 to the financial statements. In addition, the Air Force prepared the Statement of Financing on a combined basis, instead of the consolidated basis required by OMB Bulletin No. 01-09, "Form and Content of Agency Financial Statements."
- Other financing sources reported by the Air Force did not include non-monetary support provided by U.S. Allies for common defense and mutual security. For details, see Note 1.E. to the financial statements.

## Compliance with Laws and Regulations

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

The Air Force is required to comply with the following financial management systems reporting requirements.

The Federal Financial Management Improvement Act of 1996 requires Air Force to establish and maintain financial management systems that comply substantially with the Federal financial management system requirements, applicable generally accepted accounting principles, and the United States Government Standard General Ledger at the transaction level. In addition, the Federal Managers' Financial Integrity Act of 1982 requires Air Force to evaluate the systems and to annually report whether those systems are in compliance with applicable requirements. The Chief Financial Officers Act of 1990 requires DoD to prepare a 5-year Financial Management Plan describing activities that DoD will conduct during the next 5 years to improve financial management.

The Air Force acknowledged that many of its critical financial management and feeder systems do not comply substantially with the Federal financial management systems requirements, generally accepted accounting principles, and the U.S. Government Standard General Ledger at the transaction level. In an attempt to comply with statutory reporting requirements and applicable financial systems requirements, DoD is developing a DoD-wide Business Enterprise Architecture. The architecture is intended to provide a "blueprint" of the Department's financial management systems and processes to initiate a comprehensive financial management reform

effort. Until the architecture is fully developed and implemented, Air Force will be unable to fully comply with the statutory reporting requirements. Therefore, we did not perform tests of compliance for these requirements.

## Audit Disclosures

Based on audit procedures performed, we obtained a limited understanding of internal control. However, we were unable to obtain sufficient understanding of internal control in order to plan the audit and to determine the nature, timing, and extent of tests to be performed.

The Assistant Secretary of the Air Force (Financial Management and Comptroller) acknowledged to us on June 20, 2003, that the Air Force General Funds financial management systems do not comply substantially with Federal financial management system requirements, generally accepted accounting principles, the U.S. Government Standard General Ledger at the transaction level. These deficiencies in Air Force critical financial feeder systems limited its ability to present information accurately and in conformance with generally accepted accounting principles. As a result, we were unable to obtain adequate evidential matter to form or express an opinion on the financial statements, internal control, and compliance with laws and regulations. Furthermore, we were unable to design the audit to provide reasonable assurance of detecting material misstatements resulting from violations of contracts or grant agreements that have a direct and material effect of financial statement amounts.

In addition, we were unable to conduct sufficient audit follow-up work related to the deficiencies identified in the FY 2002 Air Force financial statement audit. Finally, we did not perform audit tests of Air Force compliance with certain provisions of the Antideficiency Act, Debt Collection Improvement Act, Federal Credit Reform Act, Pay and Allowance System for Civilian Employees, and the Prompt Payment Act.

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

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## Working Capital Funds

# Principal Statements

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# Consolidated Balance Sheet—Working Capital Fund

As of September 30, 2003 and 2002 ($ in thousands)

| | 2003 Consolidated | 2002 Consolidated |
|---|---|---|
| **1. ASSETS (Note 2)** | | |
| A. Intragovernmental: | | |
| 1. Fund Balance with Treasury (Note 3) | | |
| a. Entity | $ 732,842 | $ 463,312 |
| b. Non-Entity Seized Iraqi Cash | 0 | 0 |
| c. Non-Entity-Other | 0 | 0 |
| 2. Investments (Note 4) | 0 | 0 |
| 3. Accounts Receivable (Note 5) | 605,077 | 628,025 |
| 4. Other Assets (Note 6) | 3 | 0 |
| 5. Total Intragovernmental Assets | $ 1,337,922 | $ 1,091,337 |
| B. Cash and Other Monetary Assets (Note 7) | $ 0 | $ 4 |
| C. Accounts Receivable (Note 5) | 167,764 | 15,847 |
| D. Loans Receivable (Note 8) | 0 | 0 |
| E. Inventory and Related Property (Note 9) | 11,154,540 | 13,991,959 |
| F. General Property, Plant and Equipment (Note 10) | 1,329,629 | 1,320,809 |
| G. Investments (Note 4) | 0 | 0 |
| H. Other Assets (Note 6) | 380,362 | 530,335 |
| **2. TOTAL ASSETS** | $ 14,370,217 | $ 16,950,291 |
| **3. LIABILITIES (Note 11)** | | |
| A. Intragovernmental: | | |
| 1. Accounts Payable (Note 12) | $ 231,725 | $ 154,696 |
| 2. Debt (Note 13) | 0 | 0 |
| 3. Environmental Liabilities (Note 14) | 0 | 0 |
| 4. Other Liabilities (Note 15 & Note 16) | 345,437 | 11,384 |
| 5. Total Intragovernmental Liabilities | $ 577,162 | $ 166,080 |
| B. Accounts Payable (Note 12) | $ 88,984 | $ 1,791,467 |
| C. Military Retirement Benefits and Other Employment-Related Actuarial Liabilities (Note 17) | 275,132 | 247,750 |
| D. Environmental Liabilities (Note 14) | 0 | 0 |
| E. Loan Guarantee Liability (Note 8) | 0 | 0 |
| F. Other Liabilities (Note 15 & Note 16) | 1,891,851 | 3,151,129 |
| G. Debt Held by Public (Note 13) | 0 | 0 |
| **4. TOTAL LIABILITIES** | $ 2,833,129 | $ 5,356,426 |
| **5. NET POSITION** | | |
| A. Unexpended Appropriations (Note 18) | $ 0 | $ 0 |
| B. Cumulative Results of Operations | 11,537,088 | 11,593,865 |
| **6. TOTAL NET POSITION** | $ 11,537,088 | $ 11,593,865 |
| **7. TOTAL LIABILITIES AND NET POSITION** | $ 14,370,217 | $ 16,950,291 |

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

# Consolidated Statement of Net Cost—Working Capital Fund

For the years ended September 30, 2003 and 2002 ($ in thousands)

| | 2003 Consolidated | 2002 Consolidated |
|---|---|---|
| **1. Program Costs** | | |
| A. Intragovernmental Gross Costs | $ 5,448,310 | $ 4,864,103 |
| B. (Less: Intragovernmental Earned Revenue) | -13,317,788 | -10,907,401 |
| C. Intragovernmental Net Costs | $ -7,869,478 | $ -6,043,298 |
| D. Gross Costs With the Public | 8,224,828 | 5,367,308 |
| E. (Less: Earned Revenue From the Public) | -393,889 | -308,024 |
| F. Net Costs With the Public | $ 7,830,939 | $ 5,059,284 |
| G. Total Net Cost | $ -38,539 | $ -984,014 |
| **2. Cost Not Assigned to Programs** | 0 | 0 |
| **3. (Less:Earned Revenue Not Attributable to Programs)** | 0 | 0 |
| **4. Net Cost of Operations** | $ -38,539 | $ -984,014 |



*The accompanying notes are an integral part of the financial statements. See notes 1 and 19.*

# Consolidated Statement of Changes in Net Position—Working Capital Fund

For the years ended September 30, 2003 and 2002 ($ in thousands)

| | 2003 Consolidated | 2002 Consolidated |
|---|---|---|
| **CUMULATIVE RESULTS OF OPERATIONS** | | |
| **1. Beginning Balances** | $ 11,593,865 | $ 8,784,032 |
| **2. Prior period adjustments (+/-)** | -55,128 | 1,628,844 |
| **3. Beginning Balances, as adjusted** | 11,538,737 | 10,412,876 |
| **4. Budgetary Financing Sources:** | | |
| 4.A. Appropriations received | 0 | 0 |
| 4.B. Appropriations transferred-in/out (+/-) | 0 | 0 |
| 4.C. Other adjustments (rescissions, etc) (+/-) | 0 | 0 |
| 4.D. Appropriations used | 23,956 | 32,886 |
| 4.E. Nonexchange revenue | 0 | 0 |
| 4.F. Donations and forfeitures of cash and cash equivalents | 0 | 0 |
| 4.G. Transfers-in/out without reimbursement (+/-) | 0 | 0 |
| 4.H. Other budgetary financing sources (+/-) | 0 | 0 |
| **5. Other Financing Sources:** | | |
| 5.A. Donations and forfeitures of property | 0 | 0 |
| 5.B. Transfers-in/out without reimbursement (+/-) | -209,350 | 36,886 |
| 5.C. Imputed financing from costs absorbed by others | 145,206 | 127,203 |
| 5.D. Other (+/-) | 0 | 0 |
| **6. Total Financing Sources** | -40,188 | 196,975 |
| **7. Net Cost of Operations (+/-)** | -38,539 | -984,014 |
| **8. Ending Balances** | $ 11,537,088 | $ 11,593,865 |
| | | |
| **UNEXPENDED APPROPRIATIONS** | | |
| **1. Beginning Balances** | $ 0 | $ 0 |
| **2. Prior period adjustments (+/-)** | 0 | 0 |
| **3. Beginning Balances, as adjusted** | 0 | 0 |
| **4. Budgetary Financing Sources:** | | |
| 4.A. Appropriations received | 23956 | 32886 |
| 4.B. Appropriations transferred-in/out (+/-) | 0 | 0 |
| 4.C. Other adjustments (rescissions, etc) (+/-) | 0 | 0 |
| 4.D. Appropriations used | -23956 | -32886 |
| 4.E. Nonexchange revenue | 0 | 0 |
| 4.F. Donations and forfeitures of cash and cash equivalents | 0 | 0 |
| 4.G. Transfers-in/out without reimbursement (+/-) | 0 | 0 |
| 4.H. Other budgetary financing sources (+/-) | 0 | 0 |
| **5. Other Financing Sources:** | | |
| 5.A. Donations and forfeitures of property | 0 | 0 |
| 5.B. Transfers-in/out without reimbursement (+/-) | 0 | 0 |
| 5.C. Imputed financing from costs absorbed by others | 0 | 0 |
| 5.D. Other (+/-) | 0 | 0 |
| **6. Total Financing Sources** | 0 | 0 |
| **7. Net Cost of Operations (+/-)** | 0 | 0 |
| **8. Ending Balances** | $ 0 | $ 0 |

*The accompanying notes are an integral part of the financial statements. See notes 1 and 20.*

# Combined Statement of Budgetary Resources—Working Capital Fund

For the years ended September 30, 2003 and 2002 ($ in thousands)

| | 2003 Combined | 2002 Combined |
|---|---|---|
| **BUDGETARY FINANCING ACCOUNTS** | | |
| **BUDGETARY RESOURCES** | | |
| 1. Budget Authority: | | |
| 1a. Appropriations received | $ 23,956 | $ 32,886 |
| 1b. Borrowing authority | 0 | 0 |
| 1c. Contract authority | -35,575 | 362,674 |
| 1d. Net transfers (+/-) | 0 | 0 |
| 1e. Other | 0 | 0 |
| 2. Unobligated balance: | | |
| 2a. Beginning of period | 305,847 | 191,172 |
| 2b. Net transfers, actual (+/-) | -125,000 | 78,000 |
| 2c. Anticipated Transfers balances | 0 | 0 |
| 3. Spending authority from offsetting collections: | | |
| 3a. Earned | 0 | 0 |
| 1. Collected | 17,643,264 | 15,835,543 |
| 2. Receivable from Federal sources | 83,803 | 102,158 |
| 3b. Change in unfilled customer orders | 0 | 0 |
| 1. Advance received | -371,890 | -262,178 |
| 2. Without advance from Federal sources | 200,583 | 591,243 |
| 3c. Anticipated for the rest of year, without advances | 0 | 0 |
| 3d. Transfers from trust funds | 0 | 0 |
| 3e. Subtotal | 17,555,760 | 16,266,766 |
| 4. Recoveries of prior year obligations | 2,027 | 0 |
| 5. Temporarily not available pursuant to Public Law | 0 | 0 |
| 6. Permanently not available | -119,535 | -140,972 |
| **7. Total Budgetary Resources** | $ 17,607,480 | $ 16,790,526 |
| **STATUS OF BUDGETARY RESOURCES** | | |
| 8. Obligations incurred: | | |
| 8a. Direct | $ 23,956 | $ 32,886 |
| 8b. Reimbursable | 16,976,393 | 16,451,794 |
| 8c. Subtotal | 17,000,349 | 16,484,680 |
| 9. Unobligated balance: | | |
| 9a. Apportioned | 607,132 | 305,848 |
| 9b. Exempt from apportionment | 0 | 0 |
| 9c. Other available | -1 | -2 |
| 10. Unobligated Balances Not Available | 0 | 0 |
| **11. Total, Status of Budgetary Resources** | $ 17,607,480 | $ 16,790,526 |
| **RELATIONSHIP OF OBLIGATIONS TO OUTLAYS:** | | |
| 12. Obligated Balance, Net - beginning of period | $ 3,504,176 | $ 3,490,438 |
| 13. Obligated Balance transferred, net (+/-) | 0 | 0 |
| 14. Obligated Balance, Net - end of period: | | |
| 14a. Accounts receivable | -1,145,183 | -1,061,380 |
| 14b. Unfilled customer order from Federal sources | -3,999,386 | -3,798,802 |
| 14c. Undelivered orders | 6,166,726 | 5,698,622 |
| 14d. Accounts payable | 2,295,155 | 2,665,736 |
| 15. Outlays: | | |
| 15a. Disbursements | 16,900,798 | 15,777,541 |
| 15b. Collections | -17,271,374 | -15,573,364 |
| 15c. Subtotal | -370,576 | 204,177 |
| 16. Less: Offsetting receipts | 0 | 0 |
| **17. Net Outlays** | $ -370,576 | $ 204,177 |

*The accompanying notes are an integral part of the financial statements. See notes 1 and 21.*

# Combined Statement of Financing—Working Capital Fund

For the years ended September 30, 2003 and 2002 ($ in thousands)

| | 2003 Combined | 2002 Combined |
|---|---|---|
| **Resources Used to Finance Activities:** | | |
| Budgetary Resources Obligated | | |
| 1. Obligations incurred | $ 17,000,349 | $ 16,484,680 |
| 2. Less: Spending authority from offsetting collections and recoveries (-) | -17,557,786 | -16,266,764 |
| 3. Obligations net of offsetting collections and recoveries | -557,437 | 217,916 |
| 4. Less: Offsetting receipts (-) | 0 | 0 |
| 5. Net obligations | -557,437 | 217,916 |
| Other Resources | | |
| 6. Donations and forfeitures of property | 0 | 0 |
| 7. Transfers in/out without reimbursement (+/-) | -209,350 | 0 |
| 8. Imputed financing from costs absorbed by others | 145,206 | 127,203 |
| 9. Other (+/-) | 0 | -3 |
| 10. Net other resources used to finance activities | -64,144 | 127,200 |
| **11. Total resources used to finance activities** | -621,581 | 345,116 |
| **Resources Used to Finance Items not Part of the Net Cost of Operations** | | |
| 12. Change in budgetary resources obligated for goods, services and benefits ordered but not yet provided | | |
| 12a. Undelivered Orders (-) | -468,106 | -385,929 |
| 12b. Unfilled Customer Orders | -171,307 | 329,064 |
| 13. Resources that fund expenses recognized in prior periods | 0 | 0 |
| 14. Budgetary offsetting collections and receipts that do not affect net cost of operations | 0 | 0 |
| 15. Resources that finance the acquisition of assets | 1,006,802 | -1,402,468 |
| 16. Other resources or adjustments to net obligated resources that do not affect net cost of operations | | |
| 16a. Less: Trust or Special Fund Receipts Related to Exchange in the | 0 | 0 |
| 16b. Other (+/-) | 0 | 0 |
| **17. Total resources used to finance items not part of the net cost of operations** | 367,389 | -1,459,333 |
| **18. Total resources used to finance the net cost of operations** | -254,192 | -1,114,217 |
| **Components of the Net Cost of Operations that will not Require or Generate Resources in the Current Period:** | | |
| Components Requiring or Generating Resources in Future Periods: | | |
| 19. Increase in annual leave liability | 0 | 0 |
| 20. Increase in environmental and disposal liability | 0 | 0 |
| 21. Upward/Downward reestimates of credit subsidy expense (+/-) | 0 | 0 |
| 22. Increase in exchange revenue receivable from the the public (-) | 0 | 0 |
| 23. Other (+/-) | 27,382 | 5,613 |
| 24. Total components of Net Cost of Operations that will require or generate resources in future periods | 27,382 | 5,613 |
| Components not Requiring or Generating Resources: | | |
| 25. Depreciation and amortization | 185,805 | 124,590 |
| 26. Revaluation of assets or liabilities (+/-) | 2,466 | 0 |
| 27. Other (+/-) | 0 | 0 |
| 28. Total components of Net Cost of Operations that will not require or generate resources | 188,271 | 124,590 |
| **29. Total components of net cost of operations that will not require or generate resources in the current period** | 215,653 | 130,203 |
| **30. Net Cost of Operations** | -38,539 | -984,014 |

*The accompanying notes are an integral part of the financial statements. See notes 1 and 22.*

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# Footnotes to the Principal Statements

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# Note 1. Significant Accounting Policies

## 1.A. Basis of Presentation

These financial statements have been prepared to report the financial position and results of operations of the United States Air Force Working Capital Fund (AFWCF), as required by the "Chief Financial Officers (CFO) Act of 1990," expanded by the "Government Management Reform Act (GMRA) of 1994," and other appropriate legislation. The financial statements have been prepared from the books and records of the Air Force WCF in accordance with "Department of Defense Financial Management Regulation (DoDFMR)," the Office of Management and Budget (OMB) Bulletin No. 01-09, "Form and Content of Agency Financial Statements" and to the extent possible Federal Generally Accepted Accounting Principles (GAAP). The accompanying financial statements account for all resources for which the AFWCF is responsible except that information relative to classified assets, programs, and operations. This information has been excluded from the statements or otherwise aggregated and reported in such a manner that is no longer considered classified. The AFWCF's financial statements are in addition to the financial reports that are prepared by the United States Air Force pursuant to OMB directives to monitor and control the Air Force's use of budgetary resources.

The AFWCF is unable to implement all elements of Federal GAAP and the OMB Bulletin No. 01-09, due to limitations of its financial management processes and systems, including non-financial feeder systems and processes. Reported values and information for the AFWCF's major asset and liability categories are derived largely from non-financial feeder systems, such as inventory systems and logistic systems. These systems were designed to support reporting requirements focusing on maintaining accountability over assets and reporting the status of federal appropriations, rather than preparing financial statements in accordance with Federal GAAP. The AFWCF continues to implement process and system improvements addressing the limitations of its financial and non-financial feeder systems. A more detailed explanation of these financial statement elements is provided in the applicable footnote.

The AFWCF continues to enter material amounts of unsupported accounting entries. Financial and non-financial feeder systems continue to lack sufficient customer identification necessary to accurately process eliminations. The issue has been addressed as part of the Air Force plan for gaining a favorable opinion by FY 2007. This was also disclosed in the DoD Agency wide Note 1.

## 1.B. Mission of the 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 Department of Defense (DoD) and made the Air Force a department within DoD. The overall mission of the DoD is to organize, train and equip armed forces to deter aggression and if necessary, defeat aggressors of the United States and its allies. The overall mission of the Air Force is to defend the United States through control and exploitation of air and space.

The stock and industrial revolving fund accounts were created by the National Security Act of 1947, as amended in 1949 and codified in Title 10, U.S.C., Section 2208. The revolving funds were established as a means to more effectively control the cost of work performed by DoD. The DoD began operating under the revolving fund concept as early as July 1, 1951.

## 1.C. Appropriations and Funds

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

Working Capital Funds receive their initial working capital through an appropriation or a transfer of resources from existing appropriations or funds, and use those capital resources to finance the initial cost of products and services.

Financial resources to replenish the initial working capital and to permit continuing operations are generated by the acceptance of customer orders. The Defense Working Capital Fund (DCWF) operates with financial principles that provide improved cost visibility and accountability to enhance business management and improve the decision making process. The activities provide goods and services on a reimbursable basis. Receipts derived from operations generally are available in their entirety for use without further congressional action.

Air Force systems are not transaction driven for budgetary accounts. Therefore, in some cases proprietary and statistical accounts are used to develop the Report on Budget Execution (SF133) and Statement of Budgetary Resources for reporting budgetary data.

## Supply Management

The Air Force Stock Funds were established within the DoD under 10 U.S.C. 2208, as described in DoD Financial Management Regulation 7000.14-R, to finance inventories of supplies. Most inventories of supplies are financed by use of a stock fund. Exceptions include an item financed with a procurement appropriation or when financing by other means has been deemed to be more economical and efficient. A stock fund operates as a revolving fund acquiring inventories with funds received from prior sales to customers.

There are four active business activities in the Supply Management Activity Group (SMAG). They are Materiel Support Division (MSD), General Support Division (GSD), Medical-Dental Division and Academy Division. In FY 2001 the Fuels Division was taken over by the Defense Energy Support Center, therefore all activity within the Fuels Division is residual. Troop Support is also a residual activity.

## Depot Maintenance

The Air Force Depot Maintenance Activity Group (DMAG) performs manufacturing, development and test work as well as aviation maintenance. Primarily supporting Air Force organizations, DMAG also supports other DoD components, government agencies, and foreign governments. The DMAG environment is rapidly changing. Weapons systems embodying new material and technologies require new maintenance processes, while improvements in reliability reduce the frequency of maintenance for many items. The net result requires flexibility in addressing both wartime and peacetime workload changes. The DMAG achieves this flexibility by employing the unique strengths of organic (in-house) and contractor repair resources.

## Transportation

The unique transportation responsibilities of the Air Mobility Command (AMC) include the executive travel mission and operation of other operational support aircraft, the air weather service, AMC training, AMC base operations, tanker operations, and other miscellaneous AMC functions. The Air Force Transportation Defense Business Operations Fund (DBOF) was established during FY 1993 and discontinued in FY 1995 in accordance with the DWCF improvement plan. Only residual accounting remains.

## Information Services

### Air Force Central Design Activities

The Air Force Central Design Activities (CDAs) provide software design, development, maintenance and technical support services. As of October 1, 1995, the Air Force CDA business area was transferred to DBOF. This transfer expanded the Information Services Business Area in compliance with Program Budgeting Decision (PBD) 433. Transfer procedures were set forth in a DFAS-Arlington memo dated May 3, 1995. The Central Design Activities include the Standard Systems Group and the Materiel Systems Group. Prior to this transfer the CDAs were funded by Air Force Operations and Maintenance funds.

## United States Transportation Command (USTC)

For AFS purposes only, USTC is not included with the Air Force Working Capital Funds. The Office of the Under Secretary Defense, Chief Financial Officer, directed FY 1999, that USTC will be reported with the Other Defense Organizations Working Capital Fund Consolidated statements, submitted by DFAS-Indianapolis. However, USTC remains part of the Air Force budget operations for all other financial reporting.

## Air Force Working Capital Fund Component

The purpose of the Air Force Component Activity is to provide an activity within the AFWCF to record transactions that cannot be identified to a specific business area. The January 21, 1997 memorandum "Policy and Procedures for Cash Management Working Capital Funds (DWCF)" established the "Component Level Adjustment" column. Additional DFAS-Arlington memorandums provided specific and detailed instructions and procedures to maintain accountability for fund balances with Treasury.

Operations of the activities within the AFWCF are based on policies and procedures that include:

**(1) Funding Authority.** Prior to FY 1992, industrial fund activities were not issued funding documents. Activities now receive obligation authority for customer orders from the Air Force Deputy Assistant Secretary, Budget (SAF/FMB). The total costs that can be incurred are a function of the cost goals applied to the actual customer funded workload.

**(2) Minor Construction Funding.** Minor construction projects that cost $100,000 or more, but less than $300,000, are funded through a separate section of the capital budget, and depreciated over a 20 year period.

**(3) Software Development Costs.** Policy and procedures have been changed to move the development costs of new software that meets capitalization requirements to the capital budget. Software is to be amortized after release.

**(4) Capital Budgeting.** Activity group budgets are segregated into operating and capital budgets. Any investment in equipment, software, minor construction and other management improvements that meet capitalization requirements are funded through the capital budget and the cost is depreciated or amortized over the relevant life cycle.

**(5) Asset Capitalization and Depreciation.** The assets of the industrial and stock funds were transferred to the DBOF and subsequently to the AFWCF. Capital assets, excluding land, which exceed a unit cost of $100,000 or more are subject to depreciation. In addition, capital assets previously capitalized using the established thresholds for prior years will continue to be depreciated if depreciation was being recorded prior to the increase to the $100,000 threshold.

**(6) Rates and Prices.** All Air Force activity groups within the WCF are expected to set their rates and prices based upon full cost recovery, ensuring that cost reductions made by an activity will be passed on to the customers. Rates and prices normally will not change during the year of execution, but occasionally change based on certain world situations. If there is a need for a price change in Depot Maintenance, the authority is requested from HQ Air Force Material Command.

The FY 2003 AFWCF operations encompass three activity groups: Supply Management, Depot Maintenance and Information Services. These activity groups use their resources to finance the initial cost of products or services for activities of the United States Government, primarily those of the DoD. Work is generated by the acceptance of customer orders from ordering activities.

## 1.D. Basis of Accounting

The AFWCF generally records transactions on an accrual accounting basis as is required by Federal GAAP. However, some of the Air Force's financial and non-financial feeder systems and processes are not designed to collect and record financial information on the full accrual accounting basis. The AFWCF has undertaken efforts to determine the

actions required to bring all of its financial and non-financial feeder systems and processes in compliance with all elements of Federal GAAP. One such action is the current revision of its accounting systems to record transactions based on the United States Government Standard General Ledger (USSGL). Until such time that all of the processes are updated to collect and report financial information as required by Federal GAAP, some of the AFWCF's financial data will be based on budgetary transactions (obligations, disbursements, and collections) and non-financial feeder systems. For example, most of information presented on the Statement of Net Cost is based on accrued costs. However, some of this information is based on obligations and disbursements.

Under the accrual method revenues are recognized when earned and expenses are recognized when incurred, without regard to receipt or payment of cash. Budgetary accounting is accomplished through unique general ledger accounts to facilitate compliance with legal and internal control requirements associated with the use of federal funds. However, the cash basis of accounting may be followed if the reported activity and amounts are not materially significant. In addition to the accrual basis of accounting, Depot Maintenance also uses the full absorption accounting principal. During FY 1996, DFAS-DE, SAF/FMB, and OSD/FM jointly agreed on the use of this principal by Depot Maintenance. This principal requires that overhead costs such as depreciation and bad debt expenses are included in the cost of services sold. The effect of known intra-fund transactions is eliminated.

The Air Force uses several service unique general ledger structures plus data converted from the Defense Business Management System (DBMS). The financial statements depicted are derived from supply, maintenance and accounting records, utilizing the Air Force service and DBMS unique general ledger structures. The activity groups' general ledger accounts are "cross-walked" to the USSGL chart of accounts to produce the financial statements.

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

The asset accounts used to prepare the statements are categorized as either entity or nonentity. Entity assets consist of resources that the agency has the authority to use, or where management is legally obligated to use funds to meet entity obligations. Nonentity assets are assets that are held by an entity that are not available for use in the operations of the entity.

Material disclosures are provided at Note 10.

## 1.E. Revenues and Other Financing Sources

The Under Secretary of Defense (Comptroller) directed, per memorandum dated January 1992, all of the services to use the percentage of completion accounting method to recognize revenue and expenses. The DoD 7000.14-R, Financial Management Regulation, Chapter 11B, January 1995, also prescribes this method of accounting.

Each working capital activity group recognizes revenue in the following manner:

### Supply Management

Air Force Supply Management revenue is recognized at the time of sale under constructive delivery terms (normally when an item is released from inventory or delivered to the customer). Foreign Military Sales transactions also require proof of shipment before revenue is recognized. Generally, Supply Management's revenue consists of sales at standard prices less sales returns. Sales of Materiel Support Division items are at exchange price. The Medical-Dental division and the Air Force Academy Store add surcharges to their billings rather than include a surcharge in the standard price. Intra-division Supply Management sales have been eliminated. Cash discounts and interfund retail stock loss allowances are reported as additional revenue.

### Depot Maintenance

Revenue recognition for Organic DMAG is the percentage of completion method now that the Depot Maintenance Accounting and Production System (DMAPS) is fully operational at all three ALCs.

Revenue recognition for the Contract DMAG is based on the number of units produced times the Unit Sales Price (USP) and does not recognize IRR at this time. Contract DMAG is scheduled to close at the end of FY 2004.

### Information Services.

The Information Services Activity Group (ISAG), as a service type organization, recognizes revenue in one of two ways based on the service level agreement between the customer and the provider. ISAG uses the either the completed contract method or the percentage of completion method.

## 1.F. Recognition of Expenses

For financial reporting purposes the DoD policy requires the recognition of operating expenses in the period incurred. However, because the Air Force's financial and non-financial feeder systems were not designed to collect and record financial information on the full accrual accounting basis, accrual adjustments are made for major items such as payroll expenses, accounts payable, and environmental liabilities. Expenditures for capital and other long-term assets are not recognized as expenses in the AFWCF's operations until depreciated in the case of property, plant and equipment (PP&E) or consumed in the case of operating materials and supplies (OM&S). Certain expenses, such as annual and military leave earned but not taken, are financed in the period in which payment is made. Operating expenses were adjusted as a result of the elimination of balances between the DoD Components. Net increases or decreases in unexpended appropriations are recognized as a change in net position. See Note 19.I Intragovernmental expenses and revenue for disclosure of adjustment amounts.

## 1.G. 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 was 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 costs are not apportioned to the 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 the DoD facilities is obtained through budget appropriations. To the extent this financing ultimately may have been obtained through the issuance of public debt, interest costs have not been capitalized since the Department of the Treasury does not allocate such interest costs to the benefiting agencies.

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

To prepare reliable financial statements, transactions occurring between components or activities within the DoD or between two or more federal agencies must be eliminated. However, the Air Force, as well as the rest of the federal

government, cannot accurately identify all intragovernmental transactions by customer. The Defense Finance and Accounting Service (DFAS) is responsible for eliminating transactions between the components or activities of the AFWCF. For FY 1999 and beyond, seller entities within the Department provided summary seller-side balances for revenue, accounts receivable, and unearned revenue to the buyer-side internal DoD accounting offices. In most cases, the buyer-side records have been adjusted to recognize unrecorded costs and accounts payable. Intra DoD intragovernmental balances were then eliminated.

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

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

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

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

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

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

Fund Balances with Treasury are maintained at the AFWCF corporate business area today. In 1992, when the Defense Business Operating Fund was established, the FBWT was moved from the Air Force level to the Department of Defense level. In 1996, the DWCF was established and the FBWT was moved back to the Air Force level. However, allocations of FBWT were at a lower level than the level transferred out. The cash balance had been maintained at 10 days worth of cash, but what was allocated back was 3 days worth of cash. The days are based on the average of cash needed to pay vendors. The fund has been "under funded" since that time.

Material disclosures are provided at Note 3. Differences are caused by in-transit disbursements and unmatched disbursements, which are not recorded in the accounting offices' detail-level records.

## 1.J. Foreign Currency

Not applicable.

## 1.K. Accounts Receivable

As presented on the Balance Sheet, accounts receivable includes accounts receivables, claims receivables, and refunds receivable from other Federal entities or from non-federal entities. Allowances for loss on accounts receivable due from non-federal entities are based upon analysis of collection experience by fund type. The AFWCF does not recognize an allowance for loss on accounts receivable amounts from another Federal agency. Claims against another federal agency are to be resolved between the agencies. If the claim cannot be resolved by the agencies involved, it should be referred to the General Accounting Office. Only Supply Management allows for allowance for loss accounts receivable based upon analysis of historical data from prior year accounts receivable balances, write-offs, and collection policy.

Material disclosures are provided at Note 5.

## 1.L. Loans Receivable. As Applicable.

Not applicable.

## 1.M. Inventories and Related Property

Inventory data is maintained in logistics systems designed for material management purposes. Inventories are reported at approximate historical cost based on Latest Acquisition Cost (LAC), adjusted for holding gains and losses. The AFWCF uses the LAC method because its inventory systems were designed for material management rather than financial reporting. These systems provide accountability and visibility over inventory items. They do not maintain the historical cost data necessary to comply with the SSFAS No. 3, "Accounting for Inventory and Related Property." Nor can they directly produce financial transactions using the United States Government Standard General Ledger (USSGL), as required by the Federal Management Improvement Act of 1996 (P.L. 104-208). These logistics systems support the categorization of inventory as: held for sale, held in reserve for future sale, or excess, obsolete, and unserviceable, yet the business practices in the supply community do not use these categories. The categories were identified based on guidance in the DoDFMR Volume 11B. Additionally, past audit results have led to uncertainties about the completeness and existence of the inventory quantities used to derive the balances reported in the financial statements.

Approximately 60% of the General Support Division is managed in the Standard Base Supply System using a Moving Average Cost for the value of the inventory. This change was effective October 2000. The remaining 40% of the GSD inventory is managed in the Stock Control and Distribution System using the LAC method for valuation. Within the Materiel Support Division, inventory is valued at either LAC or carcass. Carcass value is calculated within the pricing system.

Only the Supply Management Activity Group maintains inventories. Gains and losses resulting from valuation changes for inventory items are recognized and reported in the Statement of Net Cost and included in the calculation of cost of goods sold. To calculate the allowances for gain or loss on inventories, an inventory worksheet is prepared monthly for each fund code within the Supply Management Activity Group.

SFFAS No. 3 distinguishes between "Inventory held for sale" and "Inventory held in reserve for future sale." There is no management or valuation difference between the two USSGL accounts. Further, the DoD manages only military or government specific material under normal conditions. Items commonly used in and available from the commercial sector are not managed in the DoD material management activities. Operational cycles are irregular, and the military risks associated with stock-out positions have no commercial parallel. The AFWCF holds material based on military need and support for contingencies. Therefore, the AFWCF does not attempt to account separately for items held for "current" or "future" sale.

Related property includes operating materials and supplies (OM&S) and stockpile materials. The OM&S including munitions not held for sale are valued at standard purchase price. The department uses the consumption method of accounting for OM&S for the most part, expensing material when it is issued to the end user. Where current systems cannot fully support the consumption method, the AFWCF uses the purchase method, expensed when purchased. For FY 2003, the AFWCF reported significant amounts using the purchase method either because the systems could not support the consumption method or because management deems that the item is in the hands of the end user.

The AFWCF implemented a new policy in FY 2002 to account for condemned material (only) as "Excess, Obsolete, and Unserviceable." The net value of the condemned material is zero, because the costs of disposal are greater than the potential scrap value. Potentially re-distributable material, presented in previous years as "Excess, Obsolete, and Unserviceable," is now included in "Held for Use" or "Held for Repair" categories according to its condition.

Material disclosures related to inventory and related property are provided at Note 9.

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

Not applicable.

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

General property, plant, and equipment (PP&E) assets are capitalized at historical acquisition cost plus capitalized improvements, when an asset has a useful life of two or more years, and when the acquisition cost equals or exceeds the DoD capitalization threshold of $100,000. Also, improvement costs over the DoD capitalization threshold of $100,000 for General PP&E are required to be capitalized. All General PP&E, other than land, is depreciated using the straight-line method. Land is not depreciated.

Prior to FY 1996, General PP&E with an acquisition cost of $15,000, $25,000, and $50,000 for FYs 1993, 1994, and 1995 respectively, and an estimated useful life of 2 or more years was capitalized. These assets remain capitalized and are reported on WCF financial statements. General PP&E previously capitalized at amounts below $100,000 were written off General Fund financial statements in FY 1998.

When it is in the best interest of the government, the Air Force provides government property necessary to complete contract work to contractors. Such property is either owned or leased by the Air Force, or purchased directly by the contractor for the government based on contract terms. When the value of contractor procured General PP&E exceeds the DoD capitalization threshold, the items should be included in the value of General PP&E reported on the Air Force's Balance Sheet. The AFWCF recently completed a study that indicates that the value of General PP&E that meets the capitalization requirement and is in the possession of contractors is not material to the Department's financial statements. Regardless, the AFWCF is developing new policies and a contractor reporting process that will provide appropriate General PP&E information for future financial statement reporting purposes. Accordingly, the Air Force currently reports only the government property in the possession of contractors that is maintained in the Air Force's property systems.

For entities operating as business type activities (WCFs), all PP&E used in the performance of their mission is categorized as General PP&E, whether or not it meets the definition of any other PP&E categories. National Defense PP&E, Heritage Assets and Stewardship Land owned or maintained on a WCF installation are reported in the Supplemental Stewardship Report of the applicable military department.

Material disclosures are provided at Note 10.

## 1.P. Advances and Prepayments

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

## 1.Q. Leases

Not applicable.

## 1.R. Other Assets

The AFWCF conducts business with commercial contractors under two primary types of contracts: fixed price and cost reimbursable. To alleviate the potential financial burden on the contractor that these long-term contracts can cause, the AFWCF provides financing payments. One type of financing payment that the AFWCF makes is for real property, and is based upon a percentage of completion. In accordance with SFFAS No 1., "Accounting for Selected Assets and Liabilities," such payments are treated as construction in process and are reported on the General PP&E line and in Note 10, General PP&E, Net. In addition, based on the provision of the Federal Acquisition Regulations, the AFWCF makes financing payments under fixed price contracts that are not based on a percentage of completion. The AFWCF reports these financing payments as advances or prepayments in the " Other Assets" line item. The AFWCF treats these payments as advances or prepayments because the AFWCF becomes liable only after the contractor delivers the goods in conformance with the contract terms. If the contractor does not deliver a satisfactory product, the AFWCF is not obligated to reimburse the contractor for its costs, and the contractor is liable to repay the AFWCF for the full amount of the advance. The AFWCF has completed a review of all applicable federal accounting standards, applicable public laws on contract financing, Federal Acquisition Regulation Parts 32, 49, and 52 and the OMB guidance in Code 5 of Federal Regulations Part 1315, "Prompt Payment." The AFWCF has concluded that SFFAS No. 1 does not fully or adequately address the subject of progress payment accounting and is considering what further action is appropriate.

## 1.S. Contingencies and Other Liabilities

The SFFAS No. 5, "Accounting for Liabilities of the Federal Government," defines a contingency as an existing condition, situation, or set of circumstances that involves an uncertainty as to possible gain or loss to the AFWCF. The uncertainty will be resolved when one or more future events occur or fail to occur. A contingency is recognized as a liability when a past event or exchange transaction has occurred, a future loss is probable and the amount of loss can be reasonably estimated. Financial statement reporting is limited to disclosure when conditions for liability recognition do not exist, but there is at least a reasonable possibility that a loss or an additional loss will be incurred. Examples of loss contingencies include the collectibility of receivables, pending or threatened litigation, possible claims and assessments. The AFWCF's loss contingencies arising are events such as aircraft, ship and vehicle accidents, medical malpractice, property or environmental damages, and contractual disputes.

## 1.T. Accrued Leave

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

## 1.U. Net Position

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

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

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

The DoD Components have the use of land, buildings and other facilities that are located overseas and have been obtained through various international treaties and agreements negotiated by the Department of State. The DoD capital assets located overseas are purchased with appropriated funds, however the host country retains the title to the land and any improvements. Generally, treaty terms allow the DoD Components continued use of these properties until the treaties expire. These fixed assets are subject to loss in the event treaties are not renewed or the AFWCF does not reach agreements that allow for the continued use. Therefore, in the event treaties or other agreements are terminated and the use of foreign bases is not allowed the losses will be recorded for the value of any nonretrievable capital assets. Negotiations between the United States and the host country determine the amount to be paid the United States for such capital investments.

## 1.W. Comparative Data

Beginning in FY 2001, the AFWCF has presented the current and previous year's financial data for comparative purposes. This data is presented in the financial statements, as well as in the notes to the principal statements.

## 1.X. Unexpended Obligations

The AFWCF records obligations for goods and services that have been ordered but not yet received. No liability for payment has been established in the financial statements because goods/services have yet to be delivered.

# Note 2. Nonentity and Entity Assets

| ` | 2003 | | | 2002 |
|---|---|---|---|---|
| As of September 30, | Nonentity | Entity | Total | |
| (Amounts in thousands) | | | | |
| **1. Intra-governmental Assets:** | | | | |
| A. Fund Balance with Treasury | $ 0 | $ 732,842 | $ 732,842 | $ 0 |
| B. Investments | 0 | 0 | 0 | 0 |
| C. Accounts Receivable | 0 | 605,077 | 605,077 | 0 |
| D. Other Assets | 0 | 3 | 3 | 0 |
| E. Total Intra-governmental Assets | $ 0 | $ 1,337,922 | $ 1,337,922 | $ 0 |
| **2. Non-Federal Assets:** | | | | |
| A. Cash and Other Monetary Assets | $ 0 | $ 0 | $ 0 | $ 0 |
| B. Accounts Receivable | 0 | 167,764 | 167,764 | 0 |
| C. Loans Receivable | 0 | 0 | 0 | 0 |
| D. Inventory & Related Property | 0 | 11,154,540 | 11,154,540 | 0 |
| E. General Property, Plant and Equipment | 0 | 1,329,629 | 1,329,629 | 0 |
| F. Other Assets | 0 | 380,362 | 380,362 | 0 |
| G. Total Non-Federal Assets | $ 0 | $ 13,032,295 | $ 13,032,295 | $ 0 |
| **3. Total Assets:** | $ 0 | $ 14,370,217 | $ 14,370,217 | $ 0 |

Asset accounts are categorized either as entity or nonentity. Entity accounts consist of resources that the agency has the authority to use, or when management is legally obligated to use funds to meet entity obligations. Nonentity accounts are assets that are held by an entity, but are not available for use in the operations of the entity.

## Note Reference

For additional line item discussion, see Note 3, Fund Balance with Treasury; Note 4, Investments; Note 5, Accounts Receivable; Note 6, Other Assets; Note 7, Cash and Other Monetary Assets; Note 8, Direct Loans and Loan Guarantees Assets; Note 9, Inventory and Related Property; Note 10, General PP&E, Net; and Note 23, Disclosures Related to the Statement of Custodial Activity.

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

# Note 3. Fund Balance with Treasury

| As of September 30, | 2003 | 2002 |
|---|---|---|
| (Amounts in thousands) | | |
| **1. Fund Balances:** | | |
| A. Appropriated Funds | $ 0 | $ 0 |
| B. Revolving Funds | 732,842 | 463,312 |
| C. Trust Funds | 0 | 0 |
| D. Other Fund Types | 0 | 0 |
| E. Total Fund Balances | $ 732,842 | $ 463,312 |
| **2. Fund Balances Per Treasury Versus Agency:** | | |
| A. Fund Balance per Treasury | $ 2,475,046 | $ 1,323,257 |
| B. Fund Balance per AFWCF | 732,842 | 463,312 |
| C. Reconciling Amount | $ 1,742,204 | $ 859,945 |

## Explanation of Reconciliation Amount

The reconciling amount on line 2C above represents $1,742,203.1 thousand for the United States Transportation Command (USTC) which is reported by Treasury as part of the Air Force Working Capital Fund. For AFS purposes, the amount for USTC is included in the Other Defense Organizations (ODO) Fund Balance.

## Other Information Related to Fund Balance with Treasury:

### Fluctuations and Abnormalities

The Supply Management (SMAG) and Depot Maintenance (DMAG) Activity Groups account for the $269,532.0 thousand increase in fund balance with treasury (FBwT).

SMAG—FBwT increased $234,526.1 thousand which can be attributed to a direct reimbursement for the cost of the war effort and the implementation of a 10 percent surcharge for the Material Support Division.

DMAG—FBwT increased $43,128.6 thousand which can be attributed to the Defense Industrial Fund Management System (DIFMS) implementation, in which revenue is recognized and billings are processed more timely.

### Note Reference

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

# Note 4. Investments

Not applicable.

# Note 5. Accounts Receivable

| As of September 30, | 2003 | | | 2002 |
|---|---|---|---|---|
| | Gross Amount Due | Allowance For Estimated Uncollectibles | Accounts Receivable, Net | Accounts Receivable, Net |
| (Amounts in thousands) | | | | |
| **1. Intra-governmental Receivables:** | $ 605,077 | N/A | $ 605,077 | $ 628,025 |
| **2. Non-Federal Receivables (From the Public):** | $ 167,842 | $ (78) | $ 167,764 | $ 15,847 |
| **3. Total Accounts Receivable:** | $ 772,919 | $ (78) | $ 772,841 | $ 643,872 |

## Other Information

### Fluctuations

Non-federal receivables increased $151,916.6 thousand, or 958.65 percent. The increase is due to a change in classification of receivables due from foreign governments in the Supply Management Activity Group (SMAG). Prior to FY

2003, the receivables were treated as other assets, until a determination could be made on the actual amount that would be collected. In FY 2003, an additional $116,271.0 thousand was classified as public receivables. Remaining increases can be attributed to normal business operations and are within expected fluctuation ranges.

## Information Related to Accounts Receivables

### Allowance Method

SMAG uses an allowance method for non-federal receivables which is based on historical data. Depot Maintenance and Information Services generally use the direct write-off method for uncollectible accounts.

### Allocation of Undistributed Collections

The Department of Defense policy is to allocate supported undistributed collections between federal and non-federal categories based on the percentage of federal and nonfederal accounts receivable. Unsupported undistributed collections are recorded in United States Standard General Ledger (USSGL) account 2400, liability for deposit funds, clearing accounts, and undeposited collections. The AFWCF followed this allocation procedure, applying $17,631.7 thousand in undistributed collections to accounts receivable.

### Elimination Adjustments

Accounts receivable within the AFWCF have been eliminated for statement presentation purposes. The total value of the receivables that were eliminated on these financial statements is $436,312.1 thousand.

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

### Receivables over 180 Days

The Air Force has $11,819.3 thousand government receivables over 180 days, and $13,783.1 thousand public receivables. Processes have been implemented to closely monitor the delinquent receivables, and to refer them to the appropriate entity for resolution.

### Note Reference

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

# Note 6. Other Assets

| As of September 30, | 2003 | 2002 |
|---|---|---|
| (Amounts in thousands) | | |
| **1. Intra-governmental Other Assets:** | | |
| A. Advances and Prepayments | $ 3 | $ 0 |
| B. Other Assets | 0 | 0 |
| C. Total Intra-governmental Other Assets | $ 3 | $ 0 |
| **2. Non-Federal Other Assets:** | | |
| A. Outstanding Contract Financing Payments | $ 0 | $ 0 |
| B. Other Assets (With the Public) | 380,362 | 530,335 |
| C. Total Non-Federal Other Assets | $ 380,362 | $ 530,335 |
| **3. Total Other Assets:** | $ 380,365 | $ 530,335 |

## Other Information Related to Other Assets:

### Fluctuations and Abnormalities

Intragovernmental advances and prepayments increased $2.6 thousand. Accruals were processed to agree with unearned revenue reported by trading partners.

Total non-federal other assets decreased $149,973.8 thousand. This decrease was mainly caused by a reclassification of other assets to accounts receivable involving receivables due from foreign governments in the Supply Management Activity Group (SMAG). The total amount reclassified represents a $98,390.0 thousand decrease from FY 2002. In addition, there was a decrease of $44,643.0 thousand in assets returns to vendors. The decrease is attributable to improvements in processing these items in a more timely manner. The remaining decrease is supported by acceptable decreases in advances and prepayments to contractors.

## Non-Federal Other Assets (Line 2)

**Non-Federal Other Assets (in Thousands)**

| Types of Asset | 2003 | 2002 |
|---|---|---|
| SMAG - Advances and Prepayments to Contractors | 128,304 | $122,516 |
| DMAG - Advances and Prepayments to Contractors | $38,899 | $53,099 |
| SMAG - Other assets accounts receivable - deliveries suspense | | $98,524 |
| SMAG - Air Force assets - other DoD foreign military sales (depot) | | ($134) |
| SMAG - Other assets returns to vendors pending credit | $211,688 | $256,330 |
| SMAG - Uncollected overhead | | |
| DMAG - Unallocated labor and materials | $1,471 | |
| **Total Non-Federal Other Assets** | **$380,362** | **$530,335** |

### Note Reference

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

# Note 7. Cash and Other Monetary Assets

| As of September 30, | 2003 | 2002 |
|---|---|---|
| (Amounts in thousands) | | |
| 1. Cash | $ 0 | $ 4 |
| 2. Foreign Currency (non-purchased) | 0 | 0 |
| 3. Other Monetary Assets | 0 | 0 |
| 4. Total Cash, Foreign Currency, and Other Monetary Assets | $ 0 | $ 4 |

## Other Information Pertaining to Entity Cash and Other Monetary Assets

### Definitions

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

**Foreign Currency**—consists the total U.S dollar equivalent of non-purchased foreign currencies held in foreign currency fund accounts. Non-purchased foreign currency is limited to the Treasury Index 97X7000 fund account (formerly called FT accounts).

**Other Monetary Assets**—included gold, special drawing rights, and U.S Reserve in the International Monetary Fund. This category is principally for use by the Department of Treasury.

### Fluctuations

The amount shown for FY 2002 represents undeposited collections in the ISAG area. Amounts can vary each period but total value is immaterial.

### Note Reference

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

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

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

Not applicable.

# Note 9. Inventory and Related Property

| As of September 30, | 2003 | 2002 |
|---|---|---|
| (Amounts in thousands) | | |
| 1. Inventory, Net (Note 9.A.) | $ 10,499,179 | $ 12,846,841 |
| 2. Operating Materials & Supplies, Net (Note 9.B.) | 655,361 | 1,145,118 |
| 3. Stockpile Materials, Net (Note 9.C.) | 0 | 0 |
| 4. Total | $ 11,154,540 | $ 13,991,959 |

# Note 9.A. Inventory, Net

| As of September 30, | 2003 | | | 2002 | |
|---|---|---|---|---|---|
| | Inventory, Gross Value | Revaluation Allowance | Inventory, Net | Inventory, Net | Valuation Method |
| (Amounts in thousands) | | | | | |
| **1. Inventory Categories:** | | | | | |
| A. Available and Purchased for Resale | $ 23,956,088 | $ (17,357,254) | 6,598,834 | $ 8,455,169 | LAC/O |
| B. Held for Repair | 11,374,820 | (8,168,120) | 3,206,700 | 3,104,822 | LAC/O |
| C. Excess, Obsolete, and Unserviceable | 0 | 0 | 0 | 0 | |
| D. Raw Materials | 0 | 0 | 0 | 0 | |
| E. Work in Process | 693,645 | 0 | 693,645 | 1,286,850 | AC |
| F. Total | $ 36,024,553 | $ (25,525,374) | 10,499,179 | $ 12,846,841 | |

Legend for Valuation Methods:

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

## Restrictions of Inventory Use, Sale, or Disposition

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

(1) Distributions without reimbursement are made when authorized by DoD directives;

(2) War Reserve Material includes fuels and subsistence items that are considered restricted; and

(3) Inventory, with the exception of safety stocks, may be sold to foreign, state and local governments, private parties, and contractors in accordance with current policies and guidance or at the direction of the President.

## Other Information

### Fluctuations

Inventory Available and Purchased for Resale decreased $1,856,335.0 thousand due to an increase in the revaluation allowance in the Supply Management Activity Group. The allowance is a computation which is based on costs associated with inventory. Since more inventory was sold in FY 2003 to support the war effort, more costs were incurred, which resulted in an increase in the allowance ratio of overall costs to ending inventory value.

Work in process (WIP) decreased $593,205.0 thousand. WIP for contract DMAG decreased 445,989.5 thousand, due to the phase out of contract DMAG operations. The remaining $147,215.5 thousand decrease is due to the implementation of DIFMS and the change in revenue recognition to the percentage of completion method, and the increased activity and completion of jobs in support of the war effort.

### General Composition of Inventory

Inventory includes spare and repair parts, clothing and textiles, fuels, and ammunition. Inventory is tangible personal property that is

(1) Held for sale, or held for repair for eventual sale;

(2) In the process of production for sale; or

(3) To be consumed in the production of goods for sale or in the provision of services for a fee.

"Inventory held for repair" is damaged material that requires repair to make it usable. "Excess inventory" is condemned material that must be retained for management purposes. The category "held for sale" includes all issuable material. The category "held for repair" includes all economically reparable material. "Work in process" includes depot maintenance work with its associated labor, applied overhead, and supplies used in the delivery of maintenance

services. The USSGL does not include a separate work in process account unrelated to sales. Inventory is assigned to categories based on guidance in the DoDFRM Volume 11B.

## Note Reference

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

# Note 9.B. Operating Materials and Supplies, Net

| As of September 30, | 2003 | | | 2002 | |
|---|---|---|---|---|---|
| | OM&S, Gross Value | Revaluation Allowance | OM&S, Net | OM&S, Net | Valuation Method |
| (Amounts in thousands) | | | | | |
| **1. OM&S Categories:** | | | | | |
| A. Held for Use | $ 655,361 | $ 0 | $ 655,361 | $ 1,145,118 | O |
| B. Held for Repair | 0 | 0 | 0 | 0 | |
| C. Excess, Obsolete, and Unserviceable | 0 | 0 | 0 | 0 | |
| D. Total | $ 655,361 | $ 0 | $ 655,361 | $ 1,145,118 | |

| Legend for Valuation Methods: | |
|---|---|
| Adjusted LAC = Latest Acquisition Cost, adjusted for holding gains and losses | NRV = Net Realizable |
| SP = Standard Price | O = Other |
| AC = Actual Cost | |

## Other Information

### Fluctuations

SMAG reclassified $314M from OM&S to inventory due to a cross-walk error from the prior years.

The remaining decline in the balance of the OM&S is attributable to DMAG. DMAG is currently phasing out contracts causing inventory to be liquidated at a greater rate than replenishment. This trend should continue as more contracts are closed.

### General Composition of Operating Materials and Supplies

Operating materials and supplies includes spare and repair parts. The Operating Materials & Supplies (OM&S) data reported on the financial statements are derived from logistics systems designed for material management purposes, i.e. accountability and visibility. The reported balances from these systems are not recorded at historical cost, in conformance with the valuation requirements in the Statement of Federal Financial Accounting Standard (SFFAS) No. 3, "Accounting for Inventory and Related Property." Instead the Air Force uses standard price to value its operating materials and supplies without computing unrealized holding gains or losses. Furthermore, past audit results have led to uncertainties pertaining to the completeness and existence of the OM&S quantities used to derive the balances reported in the financial statements.

For the most part, DMAG is using the consumption method of accounting for OM&S, since OM&S is defined in the SFFAS No. 3 as material which has not yet been issued to the end user. Once issued, the material is expensed. As stated above, current financial and logistics systems cannot fully support the consumption method. According to federal accounting standards, the consumption method of accounting should be used to account for OM&S unless: (1) the amount of OM&S is not significant, (2) OM&S are in the hands of the end user for use in normal operations, or (3) it is cost-beneficial to expense OM&S when purchased (purchase method). The DoD, in consultation with its auditors, is: (1) developing specific criteria for determining when OM&S amounts are not significant for the purpose of using the consumption method, (2) developing functional requirements for feeder systems to support the consumption method, and (3) identifying feeder systems that are used to manage OM&S items, and (4) developing plans to revise those systems to support the consumption method. For FY 2003, the department reported significant amounts

using the purchase method either because the systems could not support the consumption method or because management deems that the item is in the hands of the end user.

### Note Reference

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

## Note 9.C. Stockpile Materials, Net

Not applicable.

## Note 10. General PP&E, Net

| As of September 30, | 2003 | | | | | 2002 |
|---|---|---|---|---|---|---|
| | Depreciation/ Amortization Method | Service Life | Acquisition Value | (Accumulated Depreciation/ Amortization) | Net Book Value | Prior FY Net Book Value |
| (Amounts in thousands) | | | | | | |
| **1. Major Asset Classes:** | | | | | | |
| A. Land | N/A | N/A | $ 0 | N/A | $ 0 | $ 0 |
| B. Buildings, Structures, and Facilities | S/L | 20 or 40 | 791,355 | $ (555,551) | 235,804 | 259,557 |
| C. Leasehold Improvements | S/L | lease term | 0 | 0 | 0 | 0 |
| D. Software | S/L | 2-5 or 10 | 942,877 | (133,025) | 809,852 | 299,852 |
| E. Equipment | S/L | 5 or 10 | 1,971,847 | (1,744,530) | 227,317 | 540,743 |
| F. Assets Under Capital Lease [1] | S/L | lease term | 0 | 0 | 0 | 0 |
| G. Construction-in-Progress | N/A | N/A | 27,884 | N/A | 27,884 | 220,657 |
| H. Other | | | 28,772 | 0 | 28,772 | 0 |
| I. Total General PP&E | | | $ 3,762,735 | $ (2,433,106) | $ 1,329,629 | $ 1,320,809 |

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

Legend for Valuation Methods:

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

## Other Information

### Fluctuations and Abnormalities

Software increased $509,999.8 thousand due to a reclassification of equipment and construction in progress in the Supply Management Activity Group. Software costs had been erroneously coded to other asset classifications prior to FY 2003. Offsetting decreases of $313,425.2 thousand and $192,772.7 are reflected in the equipment and construction in progress categories.

Other PP&E increased in FY 2003 based on a transfer of automated data processing (ADP) equipment from the Ogden Air Logistics Center (ALC) to the Oklahoma City and Warner Robbins ALCs.

## Information Related to General PP&E, Net

In Fiscal Year 2003, real property reported by the Automated Civil Engineering System (ACES), and personal property reported by the Air Force Equipment Management System (AFEMS) and the Information Processing Management System (IPMS) has not been validated and reconciled to reported figures received from the field activities by DFAS. However, the Depot Maintenance ALCs and Aerospace Maintenance and Regeneration Center (AMARC) use the Automated Civil Engineer System (ACES) to capture the costs of real property based on preponderance of use for each building. They use the straight-line method for recording depreciation maintained on spreadsheets vice the ACES schedule. The accounting entries are recorded directly into the field level trial balances.

Any WCF Special Tools and Special Test equipment in the possession and control of the Air Force are reported in the Air Force General Funds financial statements.

The value of Air Force General PP&E real property in the possession of contractors is included in the value reported above for the Major Asset Classes of Land and Buildings, Structures, and Facilities. The value of General PP&E personal property (Major Asset Classes of Software and Equipment) does not include all of the General PP&E above the

DoD capitalization threshold in the possession of contractors. The net book amount of such property is immaterial in relation to the total General PP&E net book value. In accordance with an approved strategy with the Office of Management and Budget, the General Accounting Office and the Inspector General, DOD, is developing new policies and a contractor reporting process to capture General PP&E information for future reporting purposes for compliance with federal-wide accounting standards.

Past audit results have identified uncertainties as to whether all General PP&E assets in the possession or control (existence) of the Department's are properly and accurately recorded in the system (completeness).

### Note Reference

See Note Disclosure 1. N., Significant Accounting Policies, for additional discussion on financial reporting requirements and DoD policies governing General Property, Plant and Equipment (PP&E).

## Note 10.A. Assets Under Capital Lease

Not applicable.

## Note 11. Liabilities Not Covered and Covered by Budgetary Resources

| As of September 30, (Amounts in thousands) | 2003 Covered by Budgetary Resources | 2003 Not Covered by Budgetary Resources | 2003 Total | 2002 |
|---|---|---|---|---|
| **1. Intra-governmental Liabilities:** | | | | |
| A. Accounts Payable | $ 231,725 | $ 0 | $ 231,725 | $ 0 |
| B. Debt | 0 | 0 | 0 | 0 |
| C. Environmental Liabilities | 0 | 0 | 0 | 0 |
| D. Other | 345,437 | 0 | 345,437 | 0 |
| E. Total Intra-governmental Liabilities | $ 577,162 | $ 0 | $ 577,162 | $ 0 |
| **2. Non-Federal Liabilities:** | | | | |
| A. Accounts Payable | $ 88,984 | $ 0 | $ 88,984 | $ 0 |
| B. Military Retirement Benefits and Other Employment-Related Actuarial Liabilities | 0 | 275,132 | 275,132 | 247,750 |
| C. Environmental Liabilities | 0 | 0 | 0 | 0 |
| D. Loan Guarantee Liability | 0 | 0 | 0 | 0 |
| E. Other Liabilities | 1,891,851 | 0 | 1,891,851 | 0 |
| F. Total Non-Federal Liabilities | $ 1,980,835 | $ 275,132 | $ 2,255,967 | $ 247,750 |
| **3. Total Liabilities:** | $ 2,557,997 | $ 275,132 | $ 2,833,129 | $ 247,750 |

## Other Information

### Fluctuations and Abnormalities

The amounts recorded on Line 2B represent the Federal Employees Compensation Act (FECA) actuarial liabilities provided by the Department of Labor. The increase is due to rising cost factors used in the actuarial computation.

### Definitions

#### Liabilities Not Covered and Covered by Budgetary Resources

Liabilities that are not considered covered by realized budgetary resources as of the Balance Sheet date. Budgetary resources encompass the following:

- New budget authority.
- Spending authority from offsetting collections (credited to an appropriation or fund account).
- Recoveries of unexpired budget authority through downward adjustments of prior-year obligations.

- Unobligated balances of budgetary resources at the beginning of the year or net transfers of prior-year balances during the year.
- Borrowing authority or permanent indefinite appropriations, which have been enacted and signed into law as of the Balance Sheet date, provided that the resources may be apportioned by the OMB without further action by the Congress or without a contingency first having to be met.

### Liabilities Covered by Budgetary Resources

Resources incurred by the reporting entity which are covered by realized budget resources as of the Balance Sheet date. Budgetary resources encompass not only new budget authority, but also other resources available to cover liabilities for specified purposes in a given year. Available budgetary resources include the following:

- New budget authority.
- Spending authority from offsetting collections (credited to an appropriation or fund account).
- Recoveries of unexpired budget authority through downward adjustments of prior-year obligations.
- Unobligated balances of budgetary resources at the beginning of the year or net transfers of prior-year balances during the year.
- Borrowing authority or permanent indefinite appropriations, which have been enacted and signed into law as of the balance sheet date, provided that the resources may be apportioned by the OMB without further action by the Congress or without a contingency first having to be met.

## Note Reference

For Additional Line Item discussion, see:

- Note 8, Direct Loans and/or Loan Guarantee Programs
- Note 12, Accounts Payable
- Note 13, Liabilities Not Covered and Covered by Budgetary Resources
- Note 14, Environmental Restoration Liabilities and Environmental Disposal Liabilities
- Note 15, Other Liabilities
- Note 16, Commitments and Contingencies
- Note 17, Military Retirement Benefits and Other Employment Related

# Note 12. Accounts Payable

| As of September 30, (Amounts in thousands) | 2003 | | | 2002 |
|---|---|---|---|---|
| | Accounts Payable | Interest, Penalties, and Administrative Fees | Total | Total |
| **1. Intra-governmental Payables:** | $ 231,725 | N/A | $ 231,725 | $ 154,696 |
| **2. Non-Federal Payables (to the Public):** | $ 88,984 | $ 0 | $ 88,984 | $ 1,791,467 |
| **3. Total** | $ 320,709 | $ 0 | $ 320,709 | $ 1,946,163 |

## Other Information

### Definition

Intra-governmental accounts payable consists of amounts owed to other federal agencies for goods of services ordered and received but not yet paid. Interest, penalties and administrative fees are not applicable to intragovernmental payables. Non-federal payables (to the public) are payments to nonfederal entities.

### Fluctuations and Abnormalities

Intragovernmental payables increased $77,032 thousand from FY2002, a 50 percent increase. This increase can be attributed to the Depot Maintenance Activity Group with the war effort.

Non-federal payables decreased $1,702,484 thousand from FY2002, which is a 95 percent decrease. A change in elimination procedures was the cause of the decrease. In prior years, non-federal payables needed to be accrued as an offset to federal expenses to match seller reported revenue data from Defense Logistic Agency (DLA) at the fund code level. By processing the elimination adjustments at the consolidated activity group level, the large accrual was not necessary.

Total payables on the 1307 report decreased by $71,824 thousand. The Depot Maintenance Activity Group (DMAG) payables increased by $171,770 thousand, which was attributed to increased expenses supporting the war effort. Supply Management Activity Group (SMAG) had an offsetting decrease of $243,594 thousand which is primarily due to credits processed in MSD for erroneous prior year expenses.

The fuels division of SMAG had an abnormal payable balance which is the result of undistributed disbursements that exceed accounts payables. Once the undistributed amounts are resolved, the abnormal will be corrected. The abnormal balances were offset by payable balances at the consolidated business activity level, therefore no accrual was necessary.

### Undistributed Disbursements

Undistributed disbursements are the difference between disbursements/collections recorded at the transaction level to a specific obligation, payable, or receivable in the activity field records as opposed to those reported by the U.S. Treasury via the reconciled DD1329 and DD1400. The total undistributed disbursement amounts displayed in this note should agree with the undistributed amounts reported on accounting reports (SF 133/(M) 1002/(M) 1307). Intransit payments are payments that have been made for other agencies or entities that have not been recorded in their accounting records. These payments are applied to each entity's outstanding accounts payable balance at year-end. Accounts payable were adjusted downward in the amount of $580,943 thousand for these payments.

### Allocation of Undistributed Disbursements

The Department of Defense (DoD) policy is to allocate supported undistributed disbursements between federal and non-federal categories based on the percentage of federal and non-federal accounts payable. Unsupported undistributed disbursements should be netted against unsupported undistributed collections and recorded in United States Standard General Ledger (USSGL) account 2120, disbursements in transit. The Air Force Working Capital Fund (AFWCF) followed this allocation policy.

### Intragovernmental Eliminations

For the majority of intra-agency sales, the AFWCF accounting systems do not capture trading partner data at the transaction level in a manner that facilitates trading partner aggregations. Therefore, the AFWCF was unable to reconcile intragovernmental accounts payable to the related intragovernmental accounts receivable that generated the payable. For the 4th Quarter, elimination adjustments were made at the consolidated business activity level instead of at the fund code level, which resulted in less distortion of the actual payable amounts.

The DoD intends to develop long-term systems improvements that will include sufficient up-front edits and controls to eliminate the need for after-the-fact reconciliations. The volume of intragovernmental transactions is so large that after-the-fact reconciliations cannot be accomplished with the existing or foreseeable resources.

### Note Reference

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

## Note 13. Debt

Not applicable.

## Note 14. Environmental Liabilities and Disposal Liabilities

Not applicable.

## Note 15.A. Other Liabilities

| As of September 30, | 2003 | | | 2002 |
|---|---|---|---|---|
| (Amounts in thousands) | Current Liability | Noncurrent Liability | Total | Total |
| **Intra-governmental:** | | | | |
| Advances from Others | $ 339,303 | $ 0 | $ 339,303 | $ 1,755 |
| Other Liabilities | 6,134 | 0 | 6,134 | 9,629 |
| Total Intra-governmental Other Liabilities | $ 345,437 | $ 0 | $ 345,437 | $ 11,384 |

| As of September 30, | 2003 | | | 2002 |
|---|---|---|---|---|
| (Amount in Thousands) | Current Liability | Noncurrent Liability | Total | Total |
| **Non-Federal:** | | | | |
| Accrued Funded Payroll and Benefits | $ 161,111 | $ 0 | $ 161,111 | $ 147,659 |
| Advances from Others | 5,542 | 0 | 5,542 | 1,070 |
| Deposit Funds and Deposit Funds and Suspense Accounts | -22 | | -22 | 0 |
| Other Liabilities | 1,725,220 | 0 | 1,725,220 | 3,002,398 |
| Total Non-Federal Other Liabilities | $ 1,891,851 | $ 0 | $ 1,891,851 | $ 3,151,127 |
| **Total Other Liabilities:** | $ 2,237,288 | $ 0 | $ 2,237,288 | $ 3,162,511 |

### Other Information Pertaining to Other Liabilities

### Fluctuations and Abnormalities

Intra-governmental advances from others increased $337,547.0 thousand. With the implementation of DIFMS in FY 2003, DMAG changed its procedures on revenue recognition from the incremental revenue recognition (IRR) to the percentage of completion method, resulting in advances being recorded versus progress billings. The explanation of Line 2.M has further information of the variance.

Other intra-governmental liabilities decreased $3,406.0 thousand. These liabilities represent employee benefits that are payable to the Office of Personnel Management. Liabilities fluctuate based on staffing levels and participation in benefit programs by employees.

Non-federal advances from others increased $4,472.8 thousand. As with advances from others, the DMAG change in revenue recognition is the source of the increase.

The fluctuation represents unsupported undistributed collections, for which guidance was issued to reclassify to deposit funds and suspense accounts. The amount is abnormal as there is more support for the undistributed collections than the amount of undistributed recorded in the general ledger.

Non-federal other liabilities decreased $1,277,180.4 thousand. This decrease is attributable to the following factors:

- Progress billings of $915,608.0 thousand are no longer recorded due to the change in revenue recognition by DMAG. The new method, advances, are lower than the FY 2002 progress billings due to a $386,000.0 thousand decrease attributable to Contract DMAG being removed from the Air Force Working Capital Fund, and $209,771.8 thousand in eliminations with SMAG.
- Work in process for DMAG decreased $342,265.0 thousand which is attributable to Contract DMAG being removed from the Air Force Working Capital Fund. The reduction in contracts has resulted in a decline in material, labor and overhead costs and accruals.
- Future Purchases from Foreign Military Sales in SMAG has decreased $19,076.0 thousand.

## Information Related to Other Liabilities

| | FY 2003 | FY 2002 |
|---|---|---|
| DMAG- Progress Billings | 0 | $915,608 |
| DMAG - WIP Accrued Expenses | 1,616,599 | 1,958,864 |
| SMAG - Contract Holdbacks | 0 | 272 |
| SMAG - Future Purchase - Foreign Military Sales | 73,151 | $92,227 |
| ISAG - Misc liabilities | 1 | 0 |
| Component - Reclass of Abnormal Public Accounts Receivable | 35,469 | 35,427 |
| **Total** | **$1,725,220** | **$3,002,398** |

The SMAG Other Liabilities related to Foreign Military Sales arrive from money that various countries have deposited with the SMAG as a buy-in on future purchases they plan to make under the foreign military sales program. These funds are considered a liability as the funds are returned if the countries do not make future purchases. Revenue is not recognized on these transactions until the purchase takes place.

The Component Other Liabilities is related to an abnormal Non-Federal Accounts Receivable amount. The amount was abnormal because of Undistributed Collections. FACTS I will not accept an abnormal balance in Non-Federal Accounts Receivable, therefore the amount was reclassified as a Non-Federal Other Liability.

### Note Reference

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

## Note 15.B. Capital Lease Liability

Not applicable.

## Note 16. Commitments and Contingencies

Not applicable.

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

| As of September 30, | 2003 | | | | 2002 |
|---|---|---|---|---|---|
| | Actuarial Present Value of Projected Plan Benefits | Assumed Interest Rate (%) | (Less: Assets Available to Pay Benefits) | Unfunded Actuarial Liability | Unfunded Actuarial Liability |
| (Amounts in Thousands) | | | | | |
| FECA | $ 275,132 | | $ 0 | $ 275,132 | $ 247,750 |
| Total Other | $ 275,132 | | $ 0 | $ 275,132 | $ 247,750 |
| **Total Military Retirement Benefits and Other Employment Related Actuarial Liabilities:** | $ 275,132 | | $ 0 | $ 275,132 | $ 247,750 |

## Other Information Pertaining to Military Retirement Benefits and Other Employment-Related Actuarial Liabilities

### Fluctuations and Abnormalities

The increase is due to rising cost factors used in the actuarial computation.

### Federal Employee's Compensation Act (FECA)

The Air Force Working Capital Fund's actuarial liability for workers' compensation benefits is developed by the Department of Labor and provided to the Air Force at the end of each fiscal year. The liability includes the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases. The liability is determined using a method that utilizes historical benefit payment patterns related to predict the ultimate payments. The projected annual benefit payments are then discounted to the present value using the OMB' economic assumptions for 10-year Treasury notes and bonds. Cost-of-living adjustments and medical inflation factors are also applied to the calculation of projected future benefits.

Interest rate assumptions utilized for discounting are as follows:

| 2001 | 2002 | 2003 |
|---|---|---|
| 5.21% in year 1 | 5.20% in year 1 | 3.84% in year 1 |
| 5.21% in year 2 | 5.20% in year 2 | 4.35% in year 2 |
| and thereafter | and thereafter | and thereafter |

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

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

| CBY | COLA | CPIM |
|---|---|---|
| 2004 | 2.3% | 3.21% |
| 2005 | 2.00% | 3.54% |
| 2006 | 1.83 | 3.64% |
| 2007 | 1.97% | 3.80% |
| 2008+ | 2.17% | 3.92% |

The model's resulting projections were analyzed to insure that the estimates were reliable. The analysis was based on two tests: (1) a comparison of the percentage change in the liability amount by agency to the percentage change in

actual payments, and (2) a comparison of the ratio of the estimated liability to the actual payment of the beginning year calculated for the current projection to the liability-payment ration calculated for the prior projection.

### Note Reference

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

## Note 18. Unexpended Appropriations

Not applicable.

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

### Fluctuations and Abnormalities

### Intragovernmental Gross Costs

Intragovernmental gross costs increased by $584,207.4 thousand, or 12.01 percent. Of the $584,207 thousand increase, $248,989 thousand is attributed to the Depot Maintenance Activity Group (DMAG) and the accelerated cost recognition implemented by the Defense Industrial Financial Management System (DIFMS) in FY 2003. DMAG moved from a revenue/cost recognition methodology based upon units completed (FY 2002) to a percentage of completion methodology (2003). Supply Management Activity Group (SMAG) increased by $278,741 thousand. The largest portion of the SMAG increase is in the Material Support Division (MSD) supporting the war effort and an increase in the repair budget accounts. Information Services Activity Group (ISAG) increased by $56,477 thousand, which is solely due to adjustments made to balance to their intragovernmental seller side trading partners elimination transactions.

The 1307 costs increased by $998,007.0 thousand or 11.82 percent. There is a difference of ($413,800) thousand between the increases in the financial statement and 1307 which is attributed to ($206,296.0) thousand in intraentity transactions eliminated within the AFWCF, and ($207,504.0) thousand in AFS adjustments reversing prior year elimination accruals necessary to match data reported by trading partners.

### Intragovernmental Earned Revenue

Intragovernmental earned revenue increased by $2,410,387.4 thousand, or 22.10 percent. DMAG increased $778,662.6 thousand which is attributed to a sales rate increase of 26 percent. The overall revenue increase is only 21 percent as in FY 2002 DMAG received a surcharge reimbursement. In addition, the implementation of DIFMS also resulted in faster revenue recognition under the percentage of completion method. SMAG's increase of $1,611,183.9 thousand is attributed to increased revenues in support of the war effort. ISAG increased $20,540.8 thousand, which is an acceptable variance at 5 percent. Eliminations within the AFWCF total $5,422,205.9 thousand.

### Gross Costs With the Public

Public costs increased by $2,857,519.0 thousand, or 53.24 percent. 1307 costs increased by $5,221,774.0 thousand, which is 85.89 percent. The difference between the increases is attributed to $2,253,998.0 thousand in AFS adjustments to include elimination entries that were necessary to match data reported by trading partners in the two periods reported and reclassification of prior period adjustments. The cost of war effort was also a driver for the increases.

### Earned Revenue from the Public

Earned revenue from the public increased $85,865.2 thousand, or 27.88%. DMAG increased $71,548.6 thousand, due to the war effort. SMAG increased $35,021.2 thousand due to increased activity to support the war effort. ISAG decreased $19,884.5 thousand which is attributed to FY 2002 revenues reclassed to match to waived entities. Transportation decreased $820.1 thousand which was a FY2002 prior period adjustment reclassified to revenue.

## Information Related to the Statement of Net Cost

### Statement of Net Cost

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

### Working Capital Funds

While the Air Force Working Capital Funds (WCFs) generally record transactions on an accrual basis as is required by generally accepted accounting principles, the systems do not always capture actual costs. Information presented on the Statement of Net Cost (SoNC) is primarily based on budgetary obligation, disbursements, or collection transactions, as well as information from non-financial feeder systems.

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

Not applicable.

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

### Relevant Information for Comprehension

The Department's accounting systems do not capture cost data in a manner that enables the Department to determine if the cost was incurred to generate intragovernmental revenue. Therefore, the Department was unable to complete this note. The Department is in the process of upgrading its financial and feeder systems and will be addressing this issue. Additionally, the identification of intragovernmental revenue and expenses is a government-wide problem. The OMB and the Department of the Treasury have efforts underway to develop government-wide guidance to enable accurate reporting of intragovernmental transactions. OMB and the Department of the Treasury have efforts underway to develop government-wide guidance to enable accurate reporting of intragovernmental transactions.

## Note 19.D. Imputed Expenses

| As of September 30, | 2003 | 2002 |
|---|---|---|
| (Amount in thousands) | | |
| 1. Civilian (e.g.,CSRS/FERS) Retirement | $ 64,298 | $ 48,268 |
| 2. Civilian Health | 80,667 | 78,711 |
| 3. Civilian Life Insurance | 241 | 224 |
| 4. Military Retirement Pension | 0 | 0 |
| 5. Military Retirement Health | 0 | 0 |
| 6. Judgment Fund | 0 | 0 |
| 7. Total Imputed Expenses | $ 145,206 | $ 127,203 |

### Other Information

### Fluctuations and Abnormalities

The increase in imputed expenses can be attributed to rising cost of employee benefit programs.

## Note 19.E. Benefit Program Expenses

Not applicable.

## Note 19.F. Exchange Revenue

### Definition

Exchange Revenue—arises when a Government entity provides goods and services to the public or to another Government entity for a price—"earned revenue." Exchange revenue included most user charges other than taxes, i.e., regulatory user charges.

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

Not applicable.

## Note 19.H. Stewardship Assets

Not applicable.

## Note 19.I. Intra-governmental Revenue and Expense

### Information Related to Intragovernmental Revenue and Expense

### Intragovernmental Revenue

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

### Intragovernmental Operating Expenses

The AFWCF's operating expenses were adjusted based on a comparison between the AFWCF's accounts payable and the DoD summary level seller accounts receivables. An adjustment was posted to accounts payable and operating expenses to reflect unrecognized accounts payable and operating expenses. The operating expenses of the AFWCF were adjusted upward in the amount of $207,504.0 thousand.

## Note 19.J. Suborganization Program Costs

Not applicable.

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

| As of September 30, | Cumulative Results of Operations 2003 | Unexpended Appropriations 2003 | Cumulative Results of Operations 2003 | Unexpended Appropriations 2002 |
|---|---|---|---|---|
| (Amounts in thousands) | | | | |
| **Prior Period Adjustments Increases (Decreases) to Net Position** | | | | |
| **Beginning Balance:** | | | | |
| Errors and Omissions in Prior Year Accounting Reports | $ -55,128 | $ 0 | $ 0 | $ 0 |
| Other Prior Period Adjustments | 0 | 0 | 1,628,844 | 0 |
| Total Prior Period Adjustments | $ -55,128 | $ 0 | $ 1,628,844 | $ 0 |
| **Imputed Financing:** | | | | |
| Civilian CSRS/FERS Retirement | $ 64,298 | $ 0 | $ 48,268 | $ 0 |
| Civilian Health | 80,667 | 0 | 78,711 | 0 |
| Civilian Life Insurance | 241 | 0 | 224 | 0 |
| Total Imputed Financing | $ 145,206 | $ 0 | $ 127,203 | $ 0 |

## Other Information

### Information Related to the Statement of Changes in Net Position

**Prior Period Adjustments.** The Defense Industrial Fund Management System, a CFO-compliant, transaction-driven system, was implemented in FY 2003 at the Warner-Robins and Oklahoma City Air Logistic Centers. During implementation, a review of the balance in the legacy system, which was a non-transaction driven, noncompliant system, revealed that corrections were required to the legacy balances to reflect accurate balances as supported by DIFMS. The adjustments were processed as a prior period adjustment, and the following statement lines were impacted:

| | |
|---|---|
| Intragovernmental Accounts Receivable - Decrease | (90,236) |
| Public Accounts Receivable - Decrease | (1,446) |
| Inventory and Related Property - Increase | 437,709 |
| General Property, Plant and Equipment - Decrease | (11,507) |
| Other Assets - Decrease | (11,451) |
| Intragovernmental Accounts Payable - Increase | (65,522) |
| Intragovernmental Other Liabilities - Increase | (312,934) |
| Public Accounts Payable - Decrease | 656 |
| Public Other Liabilities - Increase | (6,496) |
| Intragovernmental Earned Revenue - Increase | (43,329) |
| Intragovernmental Gross Costs - Increase | 5,425 |
| Gross Costs with the Public - Decrease | 44,003 |
| **Prior Period Adjustment Total** | **(55,128)** |

### Imputed Financing

The amounts remitted to Office of Personnel Management (OPM) by and for employees covered by the Civil Service Retirement System (CSRS), Federal Employee Retirement System (FERS), Federal Employees Health Benefits Program (FEHB) and the Federal Employee Group Life Insurance Program (FEGLI) do not fully cover the Government's cost to provide these benefits. An imputed cost is recognized as the difference between the Government's cost of providing these benefits to the employees and contributions made by and for them. The OPM provides the cost factors to DFAS for computation of imputed financing cost. The DFAS provides the costs to the Office of the Under Secretary of Defense (Personnel and Readiness) (OUSD(P&R)) for validation. Approved imputed costs are provided to the reporting components for inclusion in their financial statements.

## Note 21.A. Disclosures Related to the Statement of Budgetary Resources

| As of September 30, | 2003 | 2002 |
|---|---|---|
| (Amounts in thousands) | | |
| 1. Net Amount of Budgetary Resources Obligated for Undelivered Orders at the End of the Period | $ 6,166,726 | $ 5,698,622 |
| 2. Available Borrowing and Contract Authority at the End of the Period | 3,191,601 | 1,807,646 |

### Other Information

### Information Related to the Statement of Budgetary Resources

**Intra-entity Transactions.** The Statement of Budgetary Resources (SBR) does not include intra-entity transactions because the statements are presented as combined and combining.

**Apportionment Categories.** OMB Bulletin No. 01-09, section 9.27, specifically requires disclosure of the amount of direct and reimbursable obligations incurred against amounts apportioned under categories A, B and exempt from apportionment. This disclosure should agree with the aggregate of the related information as included in each reporting entity's SF 133 and lines 8A and 8B in the SBR.

**Undelivered Orders.** Undelivered orders presented in the SBR includes undelivered orders-unpaid for both direct and reimbursable funds.

**Spending Authority from Offsetting Collections.** Adjustments in funds that are temporarily not available pursuant to Public Law, and those that are permanently not available (included in the "Adjustments" line on the SBR), are not included in the "Spending Authority from Offsetting Collections and Adjustments" line on the SBR or the "Spending Authority for Offsetting Collections and Adjustments" line on the Statement of Financing.

**Other Information.** The prior year (FY 2002) total for line 2, Available Borrowing and Contract Authority at the End of Period, has increased by $362,674 thousand since the FY 2002 published statements and footnotes. This increase is due to a mapping change for this line within DDRS to include general ledger account 4131, Current Year Contract Authority Realized.

## Note 21.B. Disclosures Related to Problem Disbursements, In-transit Disbursements and Suspense/Budget Clearing Accounts

| As of September 30, | Sep 2001 | Sep 2002 | Sep 2003 | (Decrease)/ Increase from 2002 to 2003 |
|---|---|---|---|---|
| (Amounts in thousands) | | | | |
| 1. Total Problem Disbursements | | | | |
| A. Absolute Unmatched Disbursements | $ 4,115 | $ 2,548 | $ 2,813 | $ 265 |
| B. Negative Unliquidated Obligations | 16,153 | 11,616 | 6,498 | (5,118) |
| 2. Total In-transit Disbursements, Net | $ 606,436 | $ 537,627 | $ 464,049 | $ (73,578) |

For 4th Quarter, FY 2003, the Air Force Working Capital Fund (AFWCF) has $2,813 thousand in unmatched disbursements UMDs) which is an increase of $265 thousand since 4th Quarter, FY 2002. A UMD occurs when a payment is not matched to a corresponding obligation in the accounting system. Absolute value is the sum of the positive values of debit and credit transactions without regard to the sign.

The AFWCF reported $6,498 thousand in negative unliquidated obligations (NULOs), which is a decrease of $5,118 thousand since 4th Quarter, FY2002. A NULO occurs when a payment is made against a valid obligation, but the payment is greater than the amount of the obligation recorded in the official accounting system. These problem disbursements represent the absolute value of the AFWCF funds that have been reported by a disbursing station to the Department of Treasury, but have not yet been precisely matched against the specific source obligation that gave rise

to the disbursements. These payments have been made using available funds and based on valid receiving reports for goods and services delivered under valid contracts.

For 4th Quarter, FY 2003, the AFWCF reported $464,049 in aged in-transit disbursements, which is a decrease of $73,579 thousand since 4th Quarter, FY 2002. The in-transits represent the net value of disbursements and collections made by a DoD disbursing activity on behalf of an accountable activity and have not been posted to the accounting system.

# Note 22. Disclosures Related to the Statement of Financing

## Other Disclosures

The objective of the Statement of Financing is to reconcile the difference between budgetary obligations and the net cost of operations reported. It is presented as combined or combining statements rather than consolidated statements due to intragovernmental transactions not being eliminated. Due to the AFWCF's financial system limitations, budgetary data is not in agreement with proprietary expenses and assets capitalized. Differences between budgetary and proprietary data are a previously identified deficiency.

Note 1A and Note 1F provide additional detail.

## Other Information Related to the Statement of Financing

**Statement of Financing Adjustments.** Budgetary data is not in agreement with Proprietary Expenses and Assets Capitalized. This causes a difference in Net Cost between the Statement of Net Cost and the Statement of Financing. On the Statement of Financing Line 15, Resources that finance the acquisition of assets is adjusted in order to align the amount of net cost on the Statement of Financing with the amount reported on the Statement of Net Cost. Line 15 was adjusted by $1,061,929.7 thousand to balance the report.

# Note 23. Disclosures Related to the Statement of Custodial Activity

Not applicable.

# Note 24.A. Other Disclosures

## Undistributed Collections and Disbursements

Timing differences often occur between Treasury recording cash transactions and the field recording transactions in the general ledger. The differences are accounted for in the undistributed collection and disbursements accounts, which offset accounts receivable and accounts payable in the accounting records. Undistributed amounts are reconciled monthly to ensure that they are fully supported. With the exception of the Materiel Support Division, all of the undistributed transactions are 100% supported.

Various categories make up the total undistributed. Intransit items and uncleared interfund transactions represent the majority of the undistributed. The intransit category consists of transactions that are paid/collected by one entity on behalf of another entity. The transaction is recorded at Treasury in the month of occurrence, however it generally takes 30-60 days to be distributed to the accountable entity. Interfund transactions are intragovernmental no check drawn transactions that are generated by the billing activity at end of month. They are then transmitted to a central location to be distributed to the accountable entity. Since this is an end of month process, the accountable entity does not receive the data until the next month. Recons and suspense are also a category of undistributed. Recons are created when the cumulative disbursements and collections reported by the field entities on monthly reports do not equal cumulative amounts generated from current month transactions. When differences occur between the field-level weekly and monthly reports, the amount is suspensed until out of balances can be researched and corrected in subsequent months. The suspense category may also contain amounts that are not supported by voucher data, but

have been reported to Treasury. Once again, this is researched and corrected. Other miscellaneous posting errors can contribute to undistributed balances, which are identified monthly and corrected at the appropriate location.

The Materiel Support Division currently has an unsupported balance of $34,800 thousand. The unsupported balance has been stabilized for the most part. The accountability for this appropriation was previously shared between Denver and Columbus. Denver took over accountability for the entire appropriation in March FY 2003. This will bring all of the supporting information into Denver systems and will allow complete reconciliation once the transition is complete. Information Services Activity Group currently has an unsupported balance of $218 thousand, which is also stabilized. Performance measurements are in place to ensure timely processing of Air Force Working Capital Funds transactions.

# Consolidating and Combining Statements

# Consolidating Balance Sheet—Working Capital Fund

As of September 30, 2003 and 2002 ($ in thousands)

| | Depot Maintenance | Supply Management | Information Services |
|---|---|---|---|
| **ASSETS (Note 2)** | | | |
| Intragovernmental: | | | |
| Fund Balance with Treasury (Note 3) | | | |
| Entity | $ 352,628 | $ 326,850 | $ 50,410 |
| Non-Entity Seized Iraqi Cash | 0 | 0 | 0 |
| Non-Entity-Other | 0 | 0 | 0 |
| Investments (Note 4) | 0 | 0 | 0 |
| Accounts Receivable (Note 5) | 595,133 | 389,651 | 54,066 |
| Other Assets (Note 6) | 0 | 209,775 | 0 |
| Total Intragovernmental Assets | $ 947,761 | $ 926,276 | $ 104,476 |
| Cash and Other Monetary Assets (Note 7) | $ 0 | $ 0 | $ 0 |
| Accounts Receivable (Note 5) | 36,522 | 130,617 | 8 |
| Loans Receivable (Note 8) | 0 | 0 | 0 |
| Inventory and Related Property (Note 9) | 1,349,006 | 9,805,534 | 0 |
| General Property, Plant and Equipment (Note 10) | 1,099,329 | 197,308 | 32,985 |
| Investments (Note 4) | 0 | 0 | 0 |
| Other Assets (Note 6) | 40,370 | 339,992 | 0 |
| **TOTAL ASSETS** | $ 3,472,988 | $ 11,399,727 | $ 137,469 |
| **LIABILITIES (Note 11)** | | | |
| Intragovernmental: | | | |
| Accounts Payable (Note 12) | $ 294,323 | $ 369,217 | $ 1,959 |
| Debt (Note 13) | 0 | 0 | 0 |
| Environmental Liabilities (Note 14) | 0 | 0 | 0 |
| Other Liabilities (Note 15 & Note 16) | 554,365 | 525 | 319 |
| Total Intragovernmental Liabilities | $ 848,688 | $ 369,742 | $ 2,278 |
| Accounts Payable (Note 12) | $ 20,605 | $ 46,559 | $ 153,196 |
| Military Retirement Benefits and Other Employment-Related Actuarial Liabilities (Note 17) | 239,080 | 24,173 | 11,879 |
| Environmental Liabilities (Note 14) | 0 | 0 | 0 |
| Loan Guarantee Liability (Note 8) | 0 | 0 | 0 |
| Other Liabilities (Note 15 and Note 16) | 1,755,146 | 91,249 | 9,987 |
| Debt Held by Public | 0 | 0 | 0 |
| **TOTAL LIABILITIES** | $ 2,863,519 | $ 531,723 | $ 177,340 |
| **NET POSITION** | | | |
| Unexpended Appropriations (Note 18) | $ 0 | $ 0 | $ 0 |
| Cumulative Results of Operations | 609,469 | 10,868,004 | -39,871 |
| **TOTAL NET POSITION** | $ 609,469 | $ 10,868,004 | $ -39,871 |
| **TOTAL LIABILITIES AND NET POSITION** | $ 3,472,988 | $ 11,399,727 | $ 137,469 |

*The accompanying notes are an integral part of the financial statements. See notes 1 and 21.*

| Transportation | Component Level | Combined Total | Eliminations | 2003 Consolidated | 2002 Consolidated |
|---|---|---|---|---|---|
| $ 9,929 | $ -6,975 | $ 732,842 | $ 0 | $ 732,842 | $ 463,312 |
| 0 | 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 | 0 |
| 0 | -1 | 1,038,849 | 433,772 | 605,077 | 628,025 |
| 0 | 0 | 209,775 | 209,772 | 3 | 0 |
| $ 9,929 | $ -6,976 | $ 1,981,466 | $ 643,544 | $ 1,337,922 | $ 1,091,337 |
| $ 0 | $ 0 | $ 0 | $ 0 | $ 0 | $ 4 |
| 617 | 0 | 167,764 | 0 | 167,764 | 15,847 |
| 0 | 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 11,154,540 | 0 | 11,154,540 | 13,991,959 |
| 7 | 0 | 1,329,629 | 0 | 1,329,629 | 1,320,809 |
| 0 | 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 380,362 | 0 | 380,362 | 530,335 |
| $ 10,553 | $ -6,976 | $ 15,013,761 | $ 643,544 | $ 14,370,217 | $ 16,950,291 |
| | | | | | |
| $ -1 | $ -1 | $ 665,497 | $ 433,772 | $ 231,725 | $ 154,696 |
| 0 | 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 555,209 | 209,772 | 345,437 | 11,384 |
| $ -1 | $ -1 | $ 1,220,706 | $ 643,544 | $ 577,162 | $ 166,080 |
| $ 1,982 | $ -133,358 | $ 88,984 | $ 0 | $ 88,984 | $ 1,791,467 |
| 0 | 0 | 275,132 | 0 | 275,132 | 247,750 |
| | | | | | |
| 0 | 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 | 0 |
| 0 | 35,469 | 1,891,851 | 0 | 1,891,851 | 3,151,129 |
| 0 | 0 | 0 | 0 | 0 | 0 |
| $ 1,981 | $ -97,890 | $ 3,476,673 | $ 643,544 | $ 2,833,129 | $ 5,356,426 |
| | | | | | |
| $ 0 | $ 0 | $ 0 | $ 0 | $ 0 | $ 0 |
| 8,572 | 90,914 | 11,537,088 | 0 | 11,537,088 | 11,593,865 |
| $ 8,572 | $ 90,914 | $ 11,537,088 | $ 0 | $ 11,537,088 | $ 11,593,865 |
| $ 10,553 | $ -6,976 | $ 15,013,761 | $ 643,544 | $ 14,370,217 | $ 16,950,291 |

*The accompanying notes are an integral part of the financial statements. See notes 1 and 21.*

# Consolidating Statement of Net Cost—Working Capital Fund

For the years ended September 30, 2003 and 2002 ($ in thousands)

| | Combined Total | Eliminations | 2003 Consolidated | 2002 Consolidated |
|---|---|---|---|---|
| **Program Costs** | | | | |
| **B. Component Level** | | | | |
| Intragovernmental Gross Costs | $ 0 | $ 0 | $ 0 | $ 0 |
| (Less: Intragovernmental Earned Revenue) | 0 | 0 | 0 | 0 |
| Intragovernmental Net Costs | $ 0 | $ 0 | $ 0 | $ 0 |
| Gross Costs With the Public | 0 | 0 | 0 | -2,474 |
| (Less: Earned Revenue From the Public) | 0 | 0 | 0 | 0 |
| Net Costs With the Public | $ 0 | $ 0 | $ 0 | $ -2,474 |
| Total Net Cost | $ 0 | $ 0 | $ 0 | $ -2,474 |
| **C. Depot Maintenance** | 0 | | | |
| Intragovernmental Gross Costs | $ 3,565,894 | $ 2,366,965 | $ 1,198,929 | $ 949,940 |
| (Less: Intragovernmental Earned Revenue) | -7,543,191 | -2,889,488 | -4,653,703 | -3,875,040 |
| Intragovernmental Net Costs | $ -3,977,297 | $ -522,523 | $ -3,454,774 | $ -2,925,100 |
| Gross Costs With the Public | 4,291,719 | 0 | 4,291,719 | 2,989,168 |
| (Less: Earned Revenue From the Public) | -199,659 | 0 | -199,659 | -128,110 |
| Net Costs With the Public | $ 4,092,060 | $ 0 | $ 4,092,060 | $ 2,861,058 |
| Total Net Cost | $ 114,763 | $ -522,523 | $ 637,286 | $ -64,042 |
| **D. Information Services** | | | | |
| Intragovernmental Gross Costs | $ 83,905 | $ 94 | $ 83,811 | $ 27,334 |
| (Less: Intragovernmental Earned Revenue) | -646,329 | -170,792 | -475,537 | -454,996 |
| Intragovernmental Net Costs | $ -562,424 | $ -170,698 | $ -391,726 | $ -427,662 |
| Gross Costs With the Public | 589,886 | 0 | 589,886 | 609,888 |
| (Less: Earned Revenue From the Public) | 0 | 0 | 0 | -19,885 |
| Net Costs With the Public | $ 589,886 | $ 0 | $ 589,886 | $ 590,003 |
| Total Net Cost | $ 27,462 | $ -170,698 | $ 198,160 | $ 162,341 |
| **E. Supply Management** | | | | |
| Intragovernmental Gross Costs | $ 7,190,323 | $ 3,024,753 | $ 4,165,570 | $ 3,886,829 |
| (Less: Intragovernmental Earned Revenue) | -10,520,079 | -2,331,531 | -8,188,548 | -6,577,365 |
| Intragovernmental Net Costs | $ -3,329,756 | $ 693,222 | $ -4,022,978 | $ -2,690,536 |
| Gross Costs With the Public | 3,343,049 | 0 | 3,343,049 | 1,770,726 |
| (Less: Earned Revenue From the Public) | -194,230 | 0 | -194,230 | -159,209 |
| Net Costs With the Public | $ 3,148,819 | $ 0 | $ 3,148,819 | $ 1,611,517 |
| Total Net Cost | $ -180,937 | $ 693,222 | $ -874,159 | $ -1,079,019 |
| **F. Transportation** | | | | |
| Intragovernmental Gross Costs | $ 0 | $ 0 | $ 0 | $ 0 |
| (Less: Intragovernmental Earned Revenue) | 0 | 0 | 0 | 0 |
| Intragovernmental Net Costs | $ 0 | $ 0 | $ 0 | $ 0 |
| Gross Costs With the Public | 174 | 0 | 174 | 0 |
| (Less: Earned Revenue From the Public) | 0 | 0 | 0 | -820 |
| Net Costs With the Public | $ 174 | $ 0 | $ 174 | $ -820 |
| Total Net Cost | $ 174 | $ 0 | $ 174 | $ -820 |
| **G. Total Program Costs** | | | | |
| Intragovernmental Gross Costs | $ 10,840,122 | $ 5,391,812 | $ 5,448,310 | $ 4,864,103 |
| (Less: Intragovernmental Earned Revenue) | -18,709,599 | -5,391,811 | -13,317,788 | -10,907,401 |
| Intragovernmental Net Costs | $ -7,869,477 | $ 1 | $ -7,869,478 | $ -6,043,298 |
| Gross Costs With the Public | 8,224,828 | 0 | 8,224,828 | 5,367,308 |
| (Less: Earned Revenue From the Public) | -393,889 | 0 | -393,889 | -308,024 |
| Net Costs With the Public | $ 7,830,939 | $ 0 | $ 7,830,939 | $ 5,059,284 |
| Total Net Cost | $ -38,538 | $ 1 | $ -38,539 | $ -984,014 |
| **Cost Not Assigned to Programs** | 0 | 0 | 0 | 0 |
| **(Less:Earned Revenue Not Attributable to Programs)** | 0 | 0 | 0 | 0 |
| **Net Cost of Operations** | $ -38,538 | $ 1 | $ -38,539 | $ -984,014 |



*The accompanying notes are an integral part of the financial statements. See notes 1 and 19.*

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# Consolidating Statement of Changes in Net Position—Working Capital Fund

For the years ended September 30, 2003 and 2002 ($ in thousands)

| | Depot Maintenance | Supply Management | Information Services |
|---|---|---|---|
| **CUMULATIVE RESULTS OF OPERATIONS** | | | |
| **Beginning Balances** | $ 656,546 | $ 10,858,068 | $ -20,611 |
| **Prior period adjustments (+/-)** | -55,128 | 0 | 0 |
| **Beginning Balances, as adjusted** | 601,418 | 10,858,068 | -20,611 |
| **Budgetary Financing Sources:** | | | |
| Appropriations received | 0 | 0 | 0 |
| Appropriations transferred-in/out (+/-) | 0 | 0 | 0 |
| Other adjustments (rescissions, etc) (+/-) | 0 | 0 | 0 |
| Appropriations used | 0 | 23,956 | 0 |
| Nonexchange revenue | 0 | 0 | 0 |
| Donations and forfeitures of cash and cash equivalents | 0 | 0 | 0 |
| Transfers-in/out without reimbursement (+/-) | 0 | 0 | 0 |
| Other budgetary financing sources (+/-) | 0 | 0 | 0 |
| **Other Financing Sources:** | | | |
| Donations and forfeitures of property | 0 | 0 | 0 |
| Transfers-in/out without reimbursement (+/-) | 151 | -209,299 | 0 |
| Imputed financing from costs absorbed by others | 122,662 | 14,341 | 8,203 |
| Other (+/-) | 0 | 0 | 0 |
| **Total Financing Sources** | 122,813 | -171,002 | 8,203 |
| **Net Cost of Operations (+/-)** | 114,763 | -180,937 | 27,462 |
| **Ending Balances** | $ 609,468 | $ 10,868,003 | $ -39,870 |
| **UNEXPENDED APPROPRIATIONS** | | | |
| **Beginning Balances** | $ 0 | $ 0 | $ 0 |
| **Prior period adjustments (+/-)** | 0 | 0 | 0 |
| **Beginning Balances, as adjusted** | 0 | 0 | 0 |
| **Budgetary Financing Sources:** | | | |
| Appropriations received | 0 | 23,956 | 0 |
| Appropriations transferred-in/out (+/-) | 0 | 0 | 0 |
| Other adjustments (rescissions, etc) (+/-) | 0 | 0 | 0 |
| Appropriations used | 0 | -23,956 | 0 |
| Nonexchange revenue | 0 | 0 | 0 |
| Donations and forfeitures of cash and cash equivalents | 0 | 0 | 0 |
| Transfers-in/out without reimbursement (+/-) | 0 | 0 | 0 |
| Other budgetary financing sources (+/-) | 0 | 0 | 0 |
| **Other Financing Sources:** | | | |
| Donations and forfeitures of property | 0 | 0 | 0 |
| Transfers-in/out without reimbursement (+/-) | 0 | 0 | 0 |
| Imputed financing from costs absorbed by others | 0 | 0 | 0 |
| Other (+/-) | 0 | 0 | 0 |
| **Total Financing Sources** | 0 | 0 | 0 |
| **Net Cost of Operations (+/-)** | 0 | 0 | 0 |
| **Ending Balances** | $ 0 | $ 0 | $ 0 |



*The accompanying notes are an integral part of the financial statements. See notes 1 and 20.*

| Transportation | Component Level | Combined Total | Eliminations | 2003 Consolidated | 2002 Consolidated |
|---|---|---|---|---|---|
| $ 8,948 | $ 90,914 | $ 11,593,865 | $ 0 | $ 11,593,865 | $ 8,784,032 |
| 0 | 0 | -55,128 | 0 | -55,128 | 1,628,844 |
| 8,948 | 90,914 | 11,538,737 | 0 | 11,538,737 | 10,412,876 |
| 0 | 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 23,956 | 0 | 23,956 | 32,886 |
| 0 | 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 | 0 |
| -202 | 0 | -209,350 | 0 | -209,350 | 36,886 |
| 0 | 0 | 145,206 | 0 | 145,206 | 127,203 |
| 0 | 0 | 0 | 0 | 0 | 0 |
| -202 | 0 | -40,188 | 0 | -40,188 | 196,975 |
| 174 | 0 | -38,538 | 1 | -38,539 | -984,014 |
| $ 8,572 | $ 90,914 | $ 11,537,087 | $ -1 | $ 11,537,088 | $ 11,593,865 |
| $ 0 | $ 0 | $ 0 | $ 0 | $ 0 | $ 0 |
| 0 | 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 23,956 | 0 | 23,956 | 32,886 |
| 0 | 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | -23,956 | 0 | -23,956 | -32,886 |
| 0 | 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 | 0 | 0 |
| $ 0 | $ 0 | $ 0 | $ 0 | $ 0 | $ 0 |

*The accompanying notes are an integral part of the financial statements. See notes 1 and 20.*

# Combining Statement of Budgetary Resources—Working Capital Fund

For the years ended September 30, 2003 and 2002 ($ in thousands)

| | Depot Maintenance | Supply Management | Information Services |
|---|---|---|---|
| **BUDGETARY FINANCING ACCOUNTS** | | | |
| **BUDGETARY RESOURCES** | | | |
| Budget Authority: | | | |
| Appropriations received | $ 0 | $ 23,956 | $ 0 |
| Borrowing authority | 0 | 0 | 0 |
| Contract authority | 0 | -35,575 | 0 |
| Net transfers (+/-) | 0 | 0 | 0 |
| Other | 0 | 0 | 0 |
| Unobligated balance: | | | |
| Beginning of period | 174,357 | 29,286 | 6,238 |
| Net transfers, actual (+/-) | 0 | -125,000 | 0 |
| Anticipated Transfers Balances | 0 | 0 | 0 |
| Spending authority from offsetting collections: | | | |
| Earned | 0 | 0 | 0 |
| Collected | 7,020,961 | 9,963,296 | 658,964 |
| Receivable from Federal sources | 41,836 | 44,236 | -2,226 |
| Change in unfilled customer orders | 0 | 0 | 0 |
| Advance received | -371,890 | 0 | 0 |
| Without advance from Federal sources | 154,056 | -38,787 | 85,314 |
| Anticipated for the rest of year, without advances | 0 | 0 | 0 |
| Transfers from trust funds | 0 | 0 | 0 |
| Subtotal | 6,844,963 | 9,968,745 | 742,052 |
| Recoveries of prior year obligations | 0 | 0 | 0 |
| Temporarily not available pursuant to Public Law | 0 | 0 | 0 |
| Permanently not available | -26,754 | -89,737 | -1,930 |
| **Total Budgetary Resources** | $ 6,992,566 | $ 9,771,675 | $ 746,360 |
| **STATUS OF BUDGETARY RESOURCES** | | | |
| Obligations incurred: | | | |
| Direct | $ 0 | $ 23,956 | $ 0 |
| Reimbursable | 6,508,703 | 9,738,727 | 728,963 |
| Subtotal | 6,508,703 | 9,762,683 | 728,963 |
| Unobligated balance: | | | |
| Apportioned | 483,863 | 8,992 | 17,397 |
| Exempt from apportionment | 0 | 0 | 0 |
| Other available | 0 | 0 | 0 |
| Unobligated Balances Not Available | 0 | 0 | 0 |
| **Total, Status of Budgetary Resources** | $ 6,992,566 | $ 9,771,675 | $ 746,360 |
| **Relationship of Obligations to Outlays:** | | | |
| Obligated Balance, Net - beginning of period | $ 289,032 | $ 3,248,388 | $ 47,534 |
| Obligated Balance transferred, net (+/-) | 0 | 0 | 0 |
| Obligated Balance, Net - end of period: | | | |
| Accounts receivable | -631,481 | -493,518 | -55,036 |
| Unfilled customer order from Federal sources | -2,596,113 | -1,112,046 | -291,227 |
| Undelivered orders | 1,180,365 | 4,766,480 | 217,283 |
| Accounts payable | 2,043,128 | 216,980 | 166,423 |
| Outlays: | | | |
| Disbursements | 6,605,942 | 9,627,726 | 655,967 |
| Collections | -6,649,071 | -9,963,296 | -658,964 |
| Subtotal | -43,129 | -335,570 | -2,997 |
| Less: Offsetting receipts | 0 | 0 | 0 |
| **Net Outlays** | $ -43,129 | $ -335,570 | $ -2,997 |



*The accompanying notes are an integral part of the financial statements. See notes 1 and 21.*

| Transportation | Component Level | 2003 Combined | 2002 Combined |
|---|---|---|---|
| $ 0 | $ 0 | $ 23,956 | $ 32,886 |
| 0 | 0 | 0 | 0 |
| 0 | 0 | -35,575 | 362,674 |
| 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 |
| 5,053 | 90,913 | 305,847 | 191,172 |
| 0 | 0 | -125,000 | 78,000 |
| 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 |
| 0 | 43 | 17,643,264 | 15,835,543 |
| 0 | -43 | 83,803 | 102,158 |
| 0 | 0 | 0 | 0 |
| 0 | 0 | -371,890 | -262,178 |
| 0 | 0 | 200,583 | 591,243 |
| 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 |
| 0 | 0 | 17,555,760 | 16,266,766 |
| 2,027 | 0 | 2,027 | 0 |
| 0 | 0 | 0 | 0 |
| -1,114 | 0 | -119,535 | -140,972 |
| $ 5,966 | $ 90,913 | $ 17,607,480 | $ 16,790,526 |

| | | | |
|---|---|---|---|
| $ 0 | $ 0 | $ 23,956 | $ 32,886 |
| 0 | 0 | 16,976,393 | 16,451,794 |
| 0 | 0 | 17,000,349 | 16,484,680 |
| 5,966 | 90,914 | 607,132 | 305,848 |
| 0 | 0 | 0 | 0 |
| 0 | -1 | -1 | -2 |
| 0 | 0 | 0 | 0 |
| $ 5,966 | $ 90,913 | $ 17,607,480 | $ 16,790,526 |
| $ 6,163 | $ -86,941 | $ 3,504,176 | $ 3,490,438 |
| 0 | 0 | 0 | 0 |
| -617 | 35,469 | -1,145,183 | -1,061,380 |
| 0 | 0 | -3,999,386 | -3,798,802 |
| 2,598 | 0 | 6,166,726 | 5,698,622 |
| 1,982 | -133,358 | 2,295,155 | 2,665,736 |
| 173 | 10,990 | 16,900,798 | 15,777,541 |
| 0 | -43 | -17,271,374 | -15,573,364 |
| 173 | 10,947 | -370,576 | 204,177 |
| 0 | 0 | 0 | 0 |
| $ 173 | $ 10,947 | $ -370,576 | $ 204,177 |

*The accompanying notes are an integral part of the financial statements. See notes 1 and 21.*

# Combining Statement of Financing—Working Capital Fund

For the years ended September 30, 2003 and 2002 ($ in thousands)

| | Depot Maintenance | Supply Management | Information Services |
|---|---|---|---|
| **Resources Used to Finance Activities:** | | | |
| Budgetary Resources Obligated | | | |
| Obligations incurred | $ 6,508,703 | $ 9,762,683 | $ 728,963 |
| Less: Spending authority from offsetting collections and recoveries (-) | -6,844,963 | -9,968,744 | -742,052 |
| Obligations net of offsetting collections and recoveries | -336,260 | -206,061 | -13,089 |
| Less: Offsetting receipts (-) | 0 | 0 | 0 |
| Net obligations | -336,260 | -206,061 | -13,089 |
| Other Resources | | | |
| Donations and forfeitures of property | 0 | 0 | 0 |
| Transfers in/out without reimbursement (+/-) | 151 | -209,299 | 0 |
| Imputed financing from costs absorbed by others | 122,662 | 14,341 | 8,203 |
| Other (+/-) | 0 | 0 | 0 |
| Net other resources used to finance activities | 122,813 | -194,958 | 8,203 |
| **Total resources used to finance activities** | -213,447 | -401,019 | -4,886 |
| | | | |
| **Resources Used to Finance Items not Part of the Net Cost of Operations** | | | |
| Change in budgetary resources obligated for goods, services and benefits ordered but not yet provided | | | |
| Undelivered Orders (-) | -31,073 | -385,843 | -53,398 |
| Unfilled Customer Orders | -217,834 | -38,787 | 85,314 |
| Resources that fund expenses recognized in prior periods | 0 | 0 | 0 |
| Budgetary offsetting collections and receipts that do not affect net cost of operations | 0 | 0 | 0 |
| Resources that finance the acquisition of assets | 456,690 | 557,994 | -8,077 |
| Other resources or adjustments to net obligated resources that do not affect net cost of operations | | | |
| Less: Trust or Special Fund Receipts Related to Exchange in the | 0 | 0 | 0 |
| Other (+/-) | 0 | 0 | 0 |
| **Total resources used to finance items not part of the net cost of operations** | 207,783 | 133,364 | 23,839 |
| **Total resources used to finance the net cost of operations** | -5,664 | -267,655 | 18,953 |
| | | | |
| **Components of the Net Cost of Operations that will not Require or Generate Resources in the Current Period:** | | | |
| Components Requiring or Generating Resources in Future Periods: | | | |
| Increase in annual leave liability | 0 | 0 | 0 |
| Increase in environmental and disposal liability | 0 | 0 | 0 |
| Upward/Downward reestimates of credit subsidy expense (+/-) | 0 | 0 | 0 |
| Increase in exchange revenue receivable from the the public (-) | 0 | 0 | 0 |
| Other (+/-) | 24,751 | 1,749 | 882 |
| Total components of Net Cost of Operations that will require or generate resources in future periods | 24,751 | 1,749 | 882 |
| Components not Requiring or Generating Resources: | | | |
| Depreciation and amortization | 93,210 | 84,967 | 7,628 |
| Revaluation of assets or liabilities (+/-) | 2,466 | 0 | 0 |
| Other (+/-) | 0 | 0 | 0 |
| Total components of Net Cost of Operations that will not require or generate resources | 95,676 | 84,967 | 7,628 |
| **Total components of net cost of operations that will not require or generate resources in the current period** | 120,427 | 86,716 | 8,510 |
| **Net Cost of Operations** | 114,763 | -180,939 | 27,463 |



*The accompanying notes are an integral part of the financial statements. See notes 1 and 22.*

| Transportation | Component Level | 2003 Combined | 2002 Combined |
|---|---|---|---|
| $ 0 | $ 0 | $ 17,000,349 | $ 16,484,680 |
| -2,027 | 0 | -17,557,786 | -16,266,764 |
| -2,027 | 0 | -557,437 | 217,916 |
| 0 | 0 | 0 | 0 |
| -2,027 | 0 | -557,437 | 217,916 |
| 0 | 0 | 0 | 0 |
| -202 | 0 | -209,350 | 0 |
| 0 | 0 | 145,206 | 127,203 |
| 0 | 0 | 0 | -3 |
| -202 | 0 | -64,144 | 127,200 |
| -2,229 | 0 | -621,581 | 345,116 |
| 2,208 | 0 | -468,106 | -385,929 |
| 0 | 0 | -171,307 | 329,064 |
| 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 |
| 195 | 0 | 1,006,802 | -1,402,468 |
| 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 |
| 2,403 | 0 | 367,389 | -1,459,333 |
| 174 | 0 | -254,192 | -1,114,217 |
| 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 |
| 0 | 0 | 0 | 0 |
| 0 | 0 | 27,382 | 5,613 |
| 0 | 0 | 27,382 | 5,613 |
| 0 | 0 | 185,805 | 124,590 |
| 0 | 0 | 2,466 | 0 |
| 0 | 0 | 0 | 0 |
| 0 | 0 | 188,271 | 124,590 |
| 0 | 0 | 215,653 | 130,203 |
| 174 | 0 | -38,539 | -984,014 |

*The accompanying notes are an integral part of the financial statements. See notes 1 and 22.*

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# Required Supplementary Information

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| Schedule, Part A<br>DoD Intra-governmental Asset Balances<br>($ in thousands) | Treasury Index | Fund Balance with Treasury | Accounts Receivable | Loans Receivable | Investments | Other |
|---|---|---|---|---|---|---|
| Executive Office of the President | 11 | | $22 | | | |
| Department of Agriculture | 12 | | $4 | | | |
| Department of Commerce | 13 | | $2 | | | |
| Department of the Interior | 14 | | $0 | | | |
| Department of Justice | 15 | | $315 | | | |
| Navy General Fund | 17 | | $10,240 | | | |
| Department of State | 19 | | $19 | | | |
| Department of the Treasury | 20 | $732,843 | $410 | | | |
| Army General Fund | 21 | | $2,317 | | | |
| General Service Administration | 47 | | $432 | | | |
| National Science Foundation | 49 | | $9 | | | |
| Air Force General Fund | 57 | | $527,751 | | | |
| Department of Transportation | 69 | | $500 | | | |
| National Aeronautics and Space Administration | 80 | | $1,210 | | | |
| US Army Corps of Engineers | 96 | | $5 | | | |
| Other Defense Organizations General Funds | 97 | | $33,667 | | | |
| Other Defense Organizations Working Capital Funds | 97-4930 | | $14,200 | | | |
| Army Working Capital Fund | 97-4930.001 | | $412 | | | $3 |
| Navy Working Capital Fund | 97-4930.002 | | $12,118 | | | |
| Homeland Security | | | $1,447 | | | |
| ***Totals might not match reports*** | **TOTAL** | **$732,843** | **$605,080** | **$0** | **$0** | **$3** |

| Schedule, Part B<br>DoD Intra-governmental Entity Liabilities<br>($ in thousands) | Treasury Index | Accounts Payable | Debts/ Borrowings from Other Agencies | Other |
|---|---|---|---|---|
| Department of Justice | 15 | | | $0 |
| Navy General Fund | 17 | $4,974 | | $7,422 |
| Department of State | 19 | | | $1 |
| Department of the Treasury | 20 | | | $9 |
| Army General Fund | 21 | $1,484 | | $47 |
| Office of Personnel Management | 24 | | | $6,134 |
| Air Force General Fund | 57 | $74,731 | | $319,796 |
| National Aeronautics and Space Administration | 80 | | | $171 |
| Other Defense Organizations General Funds | 97 | $2,356 | | $103 |
| Other Defense Organizations Working Capital Funds | 97-4930 | $131,204 | | $665 |
| Army Working Capital Fund | 97-4930.001 | $12,655 | | $299 |
| Navy Working Capital Fund | 97-4930.002 | $4,323 | | $9,458 |
| Homeland Security | | | | $1,331 |
| ***Totals might not match reports*** | **TOTAL** | **$231,727** | **$0** | **$345,436** |

| Schedule, Part C<br>DoD Intra-governmental Revenue and Related Costs<br>($ in thousands) | Treasury Index | Earned Revenue |
|---|---|---|
| Executive Office of the President | 11 | $232 |
| Department of Agriculture | 12 | $3 |
| Department of the Interior | 14 | $18 |
| Department of Justice | 15 | $3,165 |
| Navy General Fund | 17 | $143,724 |
| Department of State | 19 | $181 |
| Department of the Treasury | 20 | $358 |
| Army General Fund | 21 | $26,647 |
| General Service Administration | 47 | $241 |
| National Science Foundation | 49 | $35 |
| Air Force General Fund | 57 | $11,231,839 |
| Department of Transportation | 69 | $2,072 |
| Small Business Administration | 73 | $1 |
| National Aeronautics and Space Administration | 80 | $5,162 |
| Department of Energy | 89 | $3 |
| US Army Corps of Engineers | 96 | $10 |
| Other Defense Organizations General Funds | 97 | $1,154,307 |
| Other Defense Organizations Working Capital Funds | 97-4930 | $411,066 |
| Army Working Capital Fund | 97-4930.001 | $18,338 |
| Navy Working Capital Fund | 97-4930.002 | $302,046 |
| Homeland Security | | $18,339 |
| ***Totals might not match reports*** | **TOTAL** | **$13,317,787** |

| Schedule, Part E<br>DoD Intra-governmental non-exchange revenues<br>($ in thousands) | Treasury Index | Transfers In | Transfers Out |
|---|---|---|---|
| Air Force General Fund | 57 | $748 | $85,097 |
| Other Defense Organizations Working Capital Funds | 97-4930 | | $125,000 |
| ***Totals might not match reports*** | **TOTAL** | **$748** | **$210,097** |

# Audit Opinion

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

December 4, 2003

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

SUBJECT: Independent Auditor's Report on the Air Force Working Capital Fund Fiscal Year 2003 Principal Financial Statements (Report No. D-2004-027)

The Chief Financial Officers Act of 1990, as amended, requires the Inspector General of the Department of Defense to audit the accompanying Consolidated Balance Sheet of the Air Force Working Capital Fund as of September 30, 2003 and 2002, the related Consolidated Statements of Net Cost and Changes in Net Position, and the Combined Statements of Financing[1] and Budgetary Resources for the fiscal years then ended. These financial statements are the responsibility of Air Force management. Air Force is also responsible for implementing effective internal control and for complying with laws and regulations. We are including the required reports on internal control and compliance with laws and regulations.

## Disclaimer of Opinion on the Financial Statements

The Assistant Secretary of the Air Force (Financial Management and Comptroller) acknowledged that the Air Force previously identified material weaknesses in internal control and instances of noncompliance with laws and regulations that continue to affect the current period. As a result of those conditions, management acknowledged that the financial data reported in the financial statements were unreliable. Therefore, we did not perform auditing procedures to support material amounts on the financial statements. In addition, other auditing procedures were not performed because Section 1008(d) of the FY 2002 National Defense Authorization Act requires the Inspector General of the Department of Defense to perform only the audit procedures required by generally accepted government auditing standards that are consistent with the representations made by management. These material deficiencies also affect the reliability of certain information contained in the accompanying Management's Discussion and Analysis and certain other information—much of which is taken from the same data sources

[1] The Office of Management and Budget requires a Consolidated Statement of Financing, instead of the Combined Statement of Financing prepared by the Air Force.

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

as the principal financial statements.[2] These deficiencies would have precluded an audit opinion. As described above, we are unable to express, and we do not express, an opinion on the referenced financial statements and other information.

## Summary of Internal Control

In planning and performing our audit, we considered the Air Force internal control over financial reporting and compliance. We did this to determine our procedures for auditing the financial statements and to comply with Office of Management and Budget guidance, but not to express an opinion on internal control. Accordingly, we do not express an opinion on internal control over financial reporting and compliance because previously identified reportable conditions,[3] all of which are material, continue to exist in the following areas.

- financial management systems
- policies and practices
- Fund Balance with Treasury
- Inventory
- Operating Material and Supplies
- Government furnished material and contractor acquired material
- accounting entries
- Intragovernmental Eliminations
- Statement of Net Cost
- Statement of Financing

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

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[2] Other information includes the Supporting Consolidating and Combining Financial Statements, Required Supplementary Stewardship Information, Required Supplementary Information, and Other Accompanying Information.

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

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

## Summary of Compliance with Laws and Regulations

Our work to determine compliance with selected provisions of the applicable laws and regulations was limited because management acknowledged instances of noncompliance, and previously reported instances of noncompliance continue to exist in the following areas:

- Federal financial management systems requirements,
- generally accepted accounting principles, and
- United States Government Standard General Ledger.

Therefore, we did not determine whether Air Force was in compliance with all applicable laws and regulations related to financial reporting. See the Attachment for additional details on compliance with laws and regulations.

In order for DoD to comply with statutory reporting requirements and applicable financial systems requirements, the Under Secretary of Defense (Comptroller)/Chief Financial Officer is developing the DoD-wide Business Enterprise Architecture. Until the architecture is fully developed and implemented, the Air Force will be unable to fully comply with the statutory reporting requirements.

We caution that other noncompliance may have occurred and not been detected. Further, the results of our limited procedures may not be sufficient for other purposes. Our objective was not to express an opinion on compliance with applicable laws and regulations.

## Management Responsibility

Management is responsible for:

- preparing the financial statements in conformity with generally accepted accounting principles,
- establishing, maintaining, and assessing internal control to provide reasonable assurance that the broad control objectives of the Federal Managers' Financial Integrity Act (FMFIA) of 1982 are met.

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

- ensuring that Air Force financial management systems substantially comply with Federal Financial Management Improvement Act (FFMIA) of 1996 requirements, and
- complying with applicable laws and regulations.

Paul J. Granetto, CPA
Director
Defense Financial Auditing
Service

Attachment
as stated

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

4

# Reports on Internal Control and Compliance with Laws and Regulations

## Internal Control

Management is responsible for implementing effective internal control and for providing reasonable assurance that accounting data is accumulated, recorded, and reported properly; and that assets are safeguarded. We did not perform tests of internal control over financial reporting for the Air Force, and we did not obtain sufficient evidence to support or express an opinion on internal control. We limited our audit tests because previously identified reportable conditions, all of which are material, continue to exist in the following areas. These material internal control weaknesses significantly impair the ability of Air Force to detect and prevent fraud or theft of assets. A high risk of material misstatements will continue to exist until the internal control deficiencies are corrected.

**Air Force Financial Management Systems**

- The Air Force financial management systems do not substantially comply with Federal financial management systems requirements. For details, see Notes 1.A. of the financial statements.
- The Air Force has not fully implemented the USSGL at the transaction level. For details, see Note 1.D. of the financial statements.
- The Air Force is unable to implement fully all elements of GAAP and Office of Management and Budget (OMB) Bulletin 01-09 due to limitations in financial management processes and systems, including non-financial feeder systems and processes. For details, see Note 1.A. of the financial statements.
- The Air Force generally records transactions on a cash (budgetary) basis, not on an accrual basis as required by GAAP. The amounts presented in the Consolidated Statement of Net Cost are based on budgetary obligations and disbursements and collection transactions, and are adjusted to record known accruals for major items and known imputed expenses. For details, see Note 19.A. of the financial statements.
- Air Force systems are not transaction driven for budgetary accounts. Therefore, in some cases proprietary and statistical accounts are used to develop the Report on Budget Execution and Budgetary Resources (SF-133) and Statement of Budgetary Resources for reporting budgetary data. For details, see Note 1.C. of the financial statements.

**Policies and Practices**

- Air Force resource managers do not always maintain adequate documentation or use transaction subsidiary ledgers and special journals to support recorded trial balance accounts.

- Air Force and Defense Finance and Accounting Service personnel do not perform reconciliation and system validations to verify the accuracy of accounts receivable from foreign military sales, progress payments to contractors, and accounts payable from the material support division.

**Fund Balance with Treasury**

The Air Force Working Capital Fund (WCF) continues to experience problem disbursements. As discussed in Note 21.B. to the financial statements, unmatched disbursements increased slightly to $2,813,000 at the end of FY 2003 from $2,548,000 at the end of FY 2002. Negative unliquidated obligations decreased significantly to $6,498,000 at the end of FY 2003 compared to $11,616,000 at the end of FY 2002.

In addition, Note 5 to the financial statements showed that the accounts receivable line item balance was reduced by $17,631,700 to close the undistributed collections general ledger account. Similarly, Note 12 to the financial statements showed that the accounts payable line item was reduced by $580,943,000 to close the undistributed disbursements general ledger account.

**Balance Sheet**

- Property, Plant, and Equipment values cannot be verified in accordance with Statement of Federal Financial Accounting Standards (SFFAS) No. 6, "Accounting for Property, Plant, and Equipment." Further, Property, Plant, and Equipment has not been properly recorded. For details, see Note 10 of the financial statements.

- Air Force supply management systems do not provide sufficient audit trails to confirm and value the in-transit inventory reported as part of inventory held-for-sale on the Consolidated Balance Sheet.

**Operating Materials and Supplies**

Cost of Goods Sold and Work In Progress are not recorded in accordance with SFFAS No. 3, "Accounting for Inventory and Related Property." Instead of using historical costs, the Air Force WCF values operating material and supplies based on standard price. Further uncertainties exist regarding the existence and completeness of quantities used to derive the balances reported in the Balance Sheet for operating material and supplies. For details, see Note 1.M. of the financial statements.

**Inventory**

Cost of Goods Sold and Work In Progress are not entirely recorded in accordance with SFFAS No. 3, "Accounting for Inventory and Related Property." Instead of using historical cost, the Air Force WCF values most inventory at latest acquisition cost. Further uncertainties exist regarding the existence and completeness of quantities used to derive the balances reported in the Balance Sheet for inventory. For details, see Note 1.M. of the financial statements.

**Government Furnished Material**

The General Property, Plant, and Equipment line item on the Balance Sheet does not include all Government furnished equipment in the hands of contractors whose value exceeds the capitalization threshold. The Air Force is developing policies and a contractor reporting system so that the Air Force WCF will report appropriate values. For details, see Note 1.O. of the financial statements.

**Accounting Entries**

The Air Force had not implemented adequate procedures to support and document all journal vouchers in the Air Force WCF. For details, see Note 1.A. of the financial statements.

**Intragovernmental Transactions**

- The Air Force cannot accurately identify all intragovernmental transactions by customer; and cannot be assured that transactions occurring between entities within DoD, or two or more Federal agencies, are eliminated. For details, see Note 1.G. of the financial statements.

- The Air Force cannot reconcile intragovernmental accounts receivable or accounts payable balances, or reconcile intragovernmental revenue balances with its trading partners. For details, see Note 1.G. of the financial statements.

**Statement of Net Cost**

- The Air Force does not accumulate cost information as required by GAAP. The Air Force identifies costs in the Consolidated Statement of Net Cost based on the major appropriation groups funded by Congress instead of being based on major programs and activities as set forth in SFFAS No. 4, "Managerial Cost Accounting Concepts and Standards for the Federal Government." For details, see Note 1.D. of the financial statements.

- The Air Force WCF has not fully implemented the percentage-of-completion revenue accounting method for revenue and costs as required by SFFAS No. 7, "Accounting for Revenue and Other Financing." For details, see Note 1.E. of the financial statements.

- The Air Force does not recognize an allowance for loss on accounts receivable amounts with other Federal agencies. For details, see Note 1.K. of the financial statements.

**Statement of Financing**

The Air Force cannot reconcile budgetary data with proprietary expenses and assets capitalized without making unsupported adjustments to resolve differences. For FY 2003, this adjustment was $1.1 billion compared to a negative $1.4 billion adjustment in FY 2002. Additionally, the Air Force prepared the Statement of Financing on a combined basis, instead of the consolidated basis required by OMB Bulletin No. 01-09, "Form and Content of Agency Financial Statements." For details, see Note 22 of the financial statements.

## Compliance with Laws and Regulations

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

The Air Force is required to comply with the following financial management systems reporting requirements.

The Federal Financial Management Improvement Act of 1996 requires Air Force to establish and maintain financial management systems that comply substantially with the Federal financial management systems requirements, applicable generally accepted accounting principles, and the United States Government Standard General Ledger at the transaction level. In addition, the Federal Managers' Financial Integrity Act of 1982 requires Air Force to evaluate the systems and to annually report whether those systems are in compliance with applicable requirements. The Chief Financial Officers Act of 1990 requires DoD to prepare a 5-year Financial Management Plan describing activities that DoD will conduct during the next 5 years to improve financial management.

The Air Force acknowledged that many of its critical financial management and feeder systems do not comply substantially with the Federal financial management systems requirements, Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level. In an attempt to comply with statutory reporting requirements and applicable financial systems requirements, DoD is developing a DoD-wide Business Enterprise Architecture. The architecture is intended to provide a "blueprint" of the Department's financial management systems and processes to initiate a comprehensive financial management reform effort. Until the architecture is fully developed and implemented, Air Force will be unable to fully comply with the statutory reporting requirements. Therefore, we did not perform tests of compliance for these requirements.

## Audit Disclosures

Based on audit procedures performed, we obtained a limited understanding of internal control. However, we were unable to obtain sufficient understanding of internal control in order to plan the audit and to determine the nature, timing, and extent of tests to be performed.

The Assistant Secretary of the Air Force (Financial Management and Comptroller) acknowledged to us on June 20, 2003, that the Air Force financial management systems do not comply substantially with Federal financial management system requirements, GAAP, the USSGL at the transaction level. These deficiencies in Air Force critical financial feeder systems limited its ability to present information accurately and in conformance with GAAP. As a result, we were unable to obtain adequate evidential matter to form or express an opinion on the financial statements, internal control, and compliance with laws and regulations. Furthermore,

we were unable to design the audit to provide reasonable assurance of detecting material misstatements resulting from violations of provisions of contracts or grant agreements that have a direct and material effect on the determination of financial statement amounts or other financial data significant to the audit objectives.

In addition, we were unable to conduct sufficient audit follow-up work related to the deficiencies identified in the FY 2002 Air Force financial statement audit. Finally, we did not perform audit tests of Air Force compliance with certain provisions of the Antideficiency Act, Debt Collection Improvement Act, Federal Credit Reform Act, Pay and Allowance System for Civilian Employees, and the Prompt Payment Act.

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

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# United States Air Force

## Annual Financial Statement

The U.S. Air Force Annual Financial Statement is available for viewing on the Internet at www.saffm.hq.af.mil/FMP/cfo.html.