Principal Financial Statements And Notes

The principal financial statements included in this report have been prepared in accordance with the requirements of the Chief Financial Officers Act of 1990, the Government Management Reform Act of 1994, and the Office of Management and Budget's Circular A-136, "Financial Reporting Requirements." The responsibility for the integrity of the financial information included in these statements rests with the management of DoD. The Department's fiscal years 2007 and 2006 principal financial statements were audited by the Office of Inspector General. The auditor's report accompanies the principal statements.

The Department's principal financial statements for fiscal years 2007 and 2006 consisted of the following:

The Balance Sheet

The Balance Sheet, which presents as of September 30, 2007 and 2006 those resources owned or managed by the Department which are available to provide future economic benefits (assets); amounts owed by the Department that will require payments from those resources or future resources (liabilities); and residual amounts retained by the Department, comprising the difference (net position).

The Statement of Net Cost

The Statement of Net Cost, which presents the net cost of the Department's operations for the years ended September 30, 2007 and 2006. The Department's net cost of operations includes the gross costs incurred by the Department less any exchange revenue earned from Department activities.

The Statement of Changes in Net Position

The Statement of Changes in Net Position, which presents the change in the Department's net position resulting from the net cost of the Department's operations, budgetary financing sources other than exchange revenues, and other financing sources for the years ended September 30, 2007 and 2006.

The Statement of Budgetary Resources

The Statement of Budgetary Resources, which presents the budgetary resources available to the Department during FY 2007 and 2006, the status of these resources at September 30, 2007 and 2006, and the outlay of budgetary resources for the years ended September 30, 2007 and 2006.

CONSOLIDATED BALANCE SHEET

Department of Defense

As of September 30, 2007 and 2006

($ in millions)

	2007	2006 Restated
Assets (Note 2)		
Intragovernmental		
Fund Balance with Treasury (Note 3)	$ 407,167.0	$ 329,045.1
Investments and Related Interest (Note 4)	333,711.0	299,261.2
Accounts Receivable, Net (Note 5)	1,412.9	2,941.8
Other Assets (Note 6)	1,212.5	1,189.6
Total Intragovernmental Assets	743,503.4	632,437.7
Cash and Other Monetary Assets (Note 7)	15,028.0	2,199.8
Accounts Receivable, Net (Note 5)	7,469.4	7,864.1
Loans Receivable (Note 8)	3,207.1	3,855.1
Inventory and Related Property, Net (Note 9)	224,948.7	231,823.2
General Property, Plant and Equipment, Net (Note 10)	474,530.5	465,439.5
Investments and Related Interest (Note 4)	1,412.3	1,089.8
Other Assets (Note 6)	36,246.1	27,928.7
Total Assets	**$ 1,506,345.5**	**$ 1,372,637.9**
Liabilities (Note 11)		
Intragovernmental		
Accounts Payable (Note 12)	$ 1,911.5	$ 1,549.8
Debt (Note 13)	3,242.3	3,697.8
Other Liabilities (Notes 15 and 16)	11,501.0	13,199.7
Total Intragovernmental Liabilities	16,654.8	18,447.3
Accounts Payable (Note 12)	29,674.0	27,388.4
Military Retirement and Other Federal Employment Benefits (Note 17)	1,874,679.5	1,815,769.5
Environmental and Disposal Liabilities (Note 14)	72,489.9	69,985.1
Loan Guarantee Liability (Note 8)	25.0	36.8
Other Liabilities (Notes 15 and 16)	57,203.7	31,566.1
Total Liabilities	**2,050,726.9**	**1,963,193.2**
Net Position		
Unexpended Appropriations - Earmarked Funds (Note 23)	8.1	11.4
Unexpended Appropriations - Other Funds	380,510.0	309,521.1
Cumulative Results of Operations - Earmarked Funds	(1,280,107.2)	(1,271,684.5)
Cumulative Results of Operations - Other Funds	355,207.7	371,596.7
Total Net Position	(544,381.4)	(590,555.3)
Total Liabilities and Net Position	**$ 1,506,345.5**	**$ 1,372,637.9**

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

CONSOLIDATED STATEMENT OF NET COST

Department of Defense

For the years ended September 30, 2007 and 2006

($ in millions)

	2007	2006 Restated
Program Costs		
Gross Costs	$ 668,138.4	$ 634,544.0
Less: Earned Revenue	(45,686.4)	(48,495.7)
Net Program Costs	$ 622,452.0	$ 586,048.3
Cost Not Assigned to Programs	-	-
Less: Earned Revenue Not Attributable to Programs	-	-
Net Cost of Operations	**$ 622,452.0**	**$ 586,048.3**

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

CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION

Department of Defense

As of September 30, 2007 and 2006

($ in millions)

	FY 2007		
	Earmarked Funds	All Other Funds	Eliminations
Cumulative Results of Operations			
Beginning Balances	$ (1,206,769.4)	$ 306,681.6	$ -
Prior Period Adjustments:			
Changes in Accounting Principles	-	(4,230.9)	-
Correction of Errors	-	-	-
Beginning Balances, as adjusted	(1,206,769.4)	302,450.7	-
Budgetary Financing Sources			
Appropriations used	3.3	585,691.3	-
Nonexchange revenue	3,076.9	16,665.2	-
Donations and forfeitures of cash and cash equivalents	63.8	-	-
Transfers in(out) without reimbursement	200.2	(78.4)	-
Other budgetary financing sources	-	-	-
Other Financing Sources (Non-Exchange)			
Donations and forfeitures of property	-	13.8	-
Transfers in(out) without reimbursement	243.3	(330.2)	-
Imputed financing from costs absorbed by others	-	14,813.4	10,392.1
Other	(21.8)	(8,077.5)	-
Total Financing Sources	3,565.7	608,697.6	10,392.1
Net Cost of Operations	8,617.5	624,226.6	10,392.1
Net Change	(5,051.8)	(15,529.0)	-
Cumulative Results of Operations	$ (1,211,821.2)	$ 286,921.7	$ -
Unexpended Appropriations			
Beginning Balances	$ 11.4	$ 309,521.1	$ -
Prior Period Adjustments:			
Changes in accounting principles	-	3,745.5	-
Corrections of errors	-	-	-
Beginning balances, as adjusted	11.4	313,266.6	-
Budgetary Financing Sources			
Appropriations received	-	658,617.9	-
Appropriations transferred in(out)	-	(197.4)	-
Other adjustments (rescissions, etc)	-	(5,485.8)	-
Appropriations used	(3.3)	(585,691.3)	-
Total Budgetary Financing Sources	(3.3)	67,243.4	-
Total Unexpended Appropriations	**8.1**	380,510.0	-
Net Position	**$ (1,211,813.1)**	**$ 667,431.7**	**$ -**

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

CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION

Department of Defense

As of September 30, 2007 and 2006

($ in millions)

	2007 Consolidated Total	2006 Consolidated Total Restated
Cumulative Results of Operations		
Beginning Balances	$ (900,087.8)	$ (870,674.3)
Prior Period Adjustments:		
Changes in Accounting Principles	(4,230.9)	-
Correction of Errors	-	(8,034.3)
Beginning Balances, as adjusted	(904,318.7)	(878,708.6)
Budgetary Financing Sources		
Appropriations used	585,694.6	552,838.4
Nonexchange revenue	19,742.1	3,057.1
Donations and forfeitures of cash and cash equivalents	63.8	25.4
Transfers in(out) without reimbursement	121.8	958.5
Other budgetary financing sources	-	0.6
Other Financing Sources (Non-Exchange)		
Donations and forfeitures of property	13.8	47.3
Transfers in(out) without reimbursement	(86.9)	(83.7)
Imputed financing from costs absorbed by others	4,421.3	4,409.6
Other	(8,099.3)	3,415.9
Total Financing Sources	601,871.2	564,669.1
Net Cost of Operations	622,452.0	586,048.3
Net Change	(20,580.8)	(21,379.2)
Cumulative Results of Operations	**$ (924,899.5)**	**$ (900,087.8)**
Unexpended Appropriations		
Beginning Balances	$ 309,532.5	$ 273,460.3
Prior Period Adjustments:		
Changes in accounting principles	3,745.5	-
Corrections of errors	-	(0.5)
Beginning balances, as adjusted	313,278.0	273,459.8
Budgetary Financing Sources		
Appropriations received	658,617.9	559,255.2
Appropriations transferred in(out)	(197.4)	(120.7)
Other adjustments (rescissions, etc)	(5,485.8)	(10,223.4)
Appropriations used	(585,694.6)	(552,838.4)
Total Budgetary Financing Sources	67,240.1	36,072.7
Total Unexpended Appropriations	**380,518.1**	**309,532.5**
Net Position	**$ (544,381.4)**	**$ (590,555.3)**

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

COMBINED STATEMENT OF BUDGETARY RESOURCES

Department of Defense

For the Years Ended September 30, 2007 and 2006

($ in millions)

	2007	
	Budgetary Financing Accounts	**Non-Budgetary Credit Reform Financing Accounts**
Budgetary Resources		
Unobligated balance, brought forward, October 1	$ 85,793.1	$ 46.8
Recoveries of prior year unpaid obligations	44,879.2	-
Budget Authority:		
Appropriations received	762,641.4	13.1
Borrowing authority	-	381.8
Contract authority	116,690.2	-
Spending authority from offsetting collections:		
Earned:		
Collected	164,627.8	867.5
Receivable from federal sources	(1,277.6)	-
Change in unfilled customer orders:		
Advanced received	448.9	-
Without advance from federal sources	5,994.0	53.5
Subtotal	1,049,124.7	1,315.9
Nonexpenditure transfers, net, anticipated and actual	(118.4)	-
Temporarily not available pursuant to Public Law	(33,819.5)	-
Permanently not available	(90,598.2)	(791.1)
Total Budgetary Resources	**$ 1,055,260.9**	**$ 571.6**
Status of Budgetary Resources		
Obligations Incurred:		
Direct	$ 772,419.6	$ 512.4
Reimbursable	170,850.3	-
Subtotal	943,269.9	512.4
Unobligated balance:		
Apportioned	98,585.7	23.2
Exempt from apportionment	1,050.5	-
Subtotal	99,636.2	23.2
Unobligated balances not available	12,354.8	36.0
Total Status of Budgetary Resources	**$ 1,055,260.9**	**$ 571.6**

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

COMBINED STATEMENT OF BUDGETARY RESOURCES

Department of Defense

For the Years Ended September 30, 2007 and 2006

($ in millions)

	2007	
	Budgetary Financing Accounts	**Non-Budgetary Credit Reform Financing Accounts**
Change in Obligated Balance		
Obligated balance, net		
Unpaid obligations, brought forward, October 1	$ 349,774.5	$ 3,417.8
Less: Uncollected customer payments from Federal sources, brought forward, October 1	(55,414.9)	(76.9)
Total unpaid obligated balance	294,359.6	3,340.9
Obligations incurred net	943,269.9	512.4
Less: Gross outlays	(814,588.1)	(421.8)
Obligated balance transferred, net:		
Actual transfers, unpaid obligations	-	-
Actual transfers, uncollected customer payments from federal sources	-	-
Total unpaid obligated balance transferred, net	-	-
Less: Recoveries of prior year unpaid obligations, actual	(44,879.2)	-
Change in uncollected customer payments from federal sources	(4,716.4)	(53.5)
Obligated balance, net, end of period:		
Unpaid obligations	433,577.1	3,508.4
Less: Uncollected customer payments from federal sources	(60,131.3)	(130.4)
Total, unpaid obligated balance, net, end of period	**$ 373,445.8**	**$ 3,378.0**
Net Outlays		
Net Outlays:		
Gross outlays	$ 814,588.1	$ 421.8
Less: Offsetting collections	(165,077.2)	(867.7)
Less: Distributed offsetting receipts	(64,105.0)	-
Net Outlays	**$ 585,405.9**	**$ (445.9)**

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

COMBINED STATEMENT OF BUDGETARY RESOURCES

Department of Defense

For the Years Ended September 30, 2007 and 2006

($ in millions)

	2006	
	Budgetary Financing Accounts (Restated)	Non-Budgetary Credit Reform Financing Accounts
Budgetary Resources		
Unobligated balance, brought forward, October 1	$ 68,608.6	$ 83.0
Recoveries of prior year unpaid obligations	30,252.3	-
Budget Authority:		
Appropriations received	686,284.4	16.0
Borrowing authority	-	119.4
Contract authority	59,451.7	-
Spending authority from offsetting collections:		
Earned:		
Collected	164,718.1	1,169.6
Receivable from federal sources	649.0	-
Change in unfilled customer orders:		
Advanced received	313.9	-
Without advance from federal sources	179.1	(46.8)
Subtotal	911,596.2	1,258.2
Nonexpenditure transfers, net, anticipated and actual	(156.2)	-
Temporarily not available pursuant to Public Law	(35,746.3)	-
Permanently not available	(71,908.9)	(1,083.2)
Total Budgetary Resources	**$ 902,645.7**	**$ 258.0**
Status of Budgetary Resources		
Obligations Incurred:		
Direct	$ 651,019.8	$ 211.3
Reimbursable	165,521.3	-
Subtotal	816,541.1	211.3
Unobligated balance:		
Apportioned	74,623.8	1.2
Exempt from apportionment	1,220.4	-
Subtotal	75,844.2	1.2
Unobligated balances not available	10,260.4	45.5
Total Status of Budgetary Resources	**$ 902,645.7**	**$ 258.0**

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

COMBINED STATEMENT OF BUDGETARY RESOURCES

Department of Defense

For the Years Ended September 30, 2007 and 2006

($ in millions)

	2006	
	Budgetary Financing Accounts (Restated)	**Non-Budgetary Credit Reform Financing Accounts**
Change in Obligated Balance		
Obligated balance, net		
Unpaid obligations, brought forward, October 1	$ 302,427.0	$ 3,863.8
Less: Uncollected customer payments from Federal sources, brought forward, October 1	(54,586.9)	(123.7)
Total unpaid obligated balance	247,840.1	3,740.1
Obligations incurred net	816,541.1	211.3
Less: Gross outlays	(768,310.0)	(657.3)
Obligated balance transferred, net:		
Actual transfers, unpaid obligations	-	-
Actual transfers, uncollected customer payments from federal sources	-	-
Total unpaid obligated balance transferred, net	-	-
Less: Recoveries of prior year unpaid obligations, actual	(30,252.3)	-
Change in uncollected customer payments from federal sources	(827.8)	46.8
Obligated balance, net, end of period:		
Unpaid obligations	320,405.8	3,417.8
Less: Uncollected customer payments from federal sources	(55,414.7)	(76.9)
Total, unpaid obligated balance, net, end of period	**$ 264,991.1**	**$ 3,340.9**
Net Outlays		
Net Outlays:		
Gross outlays	$ 768,310.0	$ 657.3
Less: Offsetting collections	(165,031.7)	(1,169.4)
Less: Distributed Offsetting receipts	(48,222.1)	-
Net Outlays	**$ 555,056.2**	**$ (512.1)**

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

Note 1. Significant Accounting Policies

1.A. Basis of Presentation

These financial statements have been prepared to report the financial position and results of operations of the Department of Defense (DoD), as required by the Chief Financial Officers Act of 1990, expanded by the Government Management Reform Act of 1994, and other appropriate legislation. The financial statements have been prepared from the books and records of the Department in accordance with the "DoD Financial Management Regulation," the Office of Management and Budget (OMB) Circular No. A-136, "Financial Reporting Requirements," and to the extent possible, generally accepted accounting principles (GAAP). Effective 4th Quarter, fiscal year (FY) 2006, the Department no longer publishes consolidating/combining financial statements. The accompanying financial statements account for all resources for which the Department is responsible unless otherwise noted. Information relative to classified assets, programs, and operations is excluded from the statements or otherwise aggregated and reported in such a manner that it is not discernable.

The Department is unable to fully implement all elements of GAAP and OMB Circular No. A-136 due to limitations of its financial and nonfinancial management processes and systems that support the financial statements. The Department derives its reported values and information for major asset and liability categories largely from nonfinancial systems, such as inventory and logistics systems. These systems were designed to support reporting requirements for maintaining accountability over assets and reporting the status of federal appropriations rather than preparing financial statements in accordance with GAAP. The Department continues to implement process and system improvements addressing these limitations.

Auditors are required to audit the financial statements of the following Department reporting activities: Army General Fund, Army Working Capital Fund, Navy General Fund, Navy Working Capital Fund, Air Force General Fund, Air Force Working Capital Fund, Military Retirement Fund, Medicare-Eligible Retiree Health Care Fund, and U.S. Army Corps of Engineers (Civil Works).

In addition, the Department requires the Marine Corps General and Working Capital Funds and the following Defense Agencies to prepare internal stand-alone auditable financial statements: Defense Logistics Agency, Defense Finance and Accounting Service, Defense Information Systems Agency, Defense Contract Audit Agency, Defense Commissary Agency, Defense Security Service, Defense Threat Reduction Agency, Defense Advanced Research Projects Agency, Chemical and Biological Defense Program, Missile Defense Agency, Services Medical Activity, TRICARE Management Activity, U.S. Special Operations Command, and Defense Security Cooperative Agency.

The Department currently has 13 auditor-identified material weaknesses: (1) Accounts Payable, (2) Accounting Entries, (3) Environmental Liabilities, (4) Government Property and Materiel in Possession of Contractors, (5) Intragovernmental Eliminations, (6) Operating Materiels and Supplies, (7) Reconciliation of Net Cost of Operations to Budget (formerly Statement of Financing), (8) Statement of Net Cost, (9) Financial Management Systems, (10) Fund Balance with Treasury, (11) General Property, Plant and Equipment, (12) Inventory, and (13) Accounts Receivable.

1.B. Mission of the Reporting Entity

The Department of Defense was established by the National Security Act of 1947. The Department provides the military forces needed to deter war and protect the security of our country. Since the creation of America's first army in 1775, the Department and its predecessor organizations have evolved into a global presence with a worldwide infrastructure dedicated to defending the United States by deterring and defeating aggression and coercion in critical regions.

The Department of Defense includes the Military Departments, the Defense Agencies and the Department Field Activities. The Military Departments consist of the Army, Navy (of which the Marine Corps is a component), and the Air Force. The Defense Agencies and the Department Field Activities provide support services commonly used throughout the Department.

1.C. Appropriations of Funds

The Department receives its appropriations and funds as general, working capital (revolving), trust, special, and deposit funds. The Department uses these appropriations and funds to execute its missions and subsequently report on resource usage.

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

Working capital funds (WCF) received funding to establish an initial corpus through an appropriation or a transfer of resources from existing appropriations or funds. The corpus finances operations and transactions that flow through the fund. The WCF resources the goods and services sold to customers on a reimbursable basis and maintains the corpus. Reimbursable receipts fund future operations and generally are available in their entirety for use without further congressional action. At various times, the Congress provides additional appropriations to supplement the WCF as an infusion of cash when revenues are inadequate to cover costs within the corpus.

Trust funds contain receipts and expenditures of funds held in trust by the government for use in carrying out specific purposes or programs in accordance with the terms of the donor, trust agreement, or statute. Certain trust and special funds may be designated as earmarked funds. Earmarked funds are financed by specifically identified revenues, required by statute to be used for designated activities, benefits or purposes, and remain available over time. The Department is required to separately account for and report on the receipt, use and retention of revenues and other financing sources for earmarked funds.

Special fund accounts are used to record government receipts reserved for a specific purpose.

Deposit funds are used to record amounts held temporarily until paid to the appropriate government or public entity. The Department is acting as an agent or custodian for funds awaiting distribution.

The Department is a party to allocation transfers with other federal agencies as a transferring (parent) or receiving (child) entity. Allocation transfers are an agency's legal delegation of its authority to obligate budget authority and outlay funds to another agency. Generally, all financial activity related to these allocation transfers (e.g., budget authority, obligations, outlays) is reported in the financial statements of the parent entity. Exceptions to this general rule apply to specific funds for which OMB has directed that all activity be reported in the financial statements of the child entity. These exceptions include U.S. Treasury-Managed Trust Funds, Executive Office of the President (EOP), and all other funds specifically designated by OMB.

The Department is a receiving (child) party to allocation transfers for the following agencies: Departments of Agriculture, Interior, Energy, and Transportation; the Appalachian Regional Commission; and the Federal Highway Administration.

Additionally, the Department is a party to other allocation transfers as the child for certain funds meeting the OMB exception and all related activity is thus included in the Department's financial statements. The exceptions reported by the Department include South Dakota Terrestrial Wildlife Habitat Restoration, Inland Waterways and Harbor Maintenance, and the EOP.

As the parent, the Department allocates funds to the Departments of Transportation and Agriculture and reports related activity in its financial statements.

1.D. Basis of Accounting

For FY 2007, the Department's financial management systems are unable to meet all of the requirements for full accrual accounting. Many of the Department's financial and nonfinancial feeder systems and processes were designed and implemented prior to the issuance of GAAP for federal agencies. These systems were not designed to collect and record financial information on the full accrual accounting basis as required by GAAP. Most of the Department's financial and nonfinancial legacy systems were designed to record information on a budgetary basis.

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

In addition, the Department identifies program costs based upon the major appropriation groups provided by the Congress. Current processes and systems do not capture and report accumulated costs for major programs based upon the performance measures as required by the Government Performance and Results Act. The Department is working toward a cost reporting methodology that will satisfy the requirement for cost information as mandated in the Statement of Federal Financial Accounting Standards (SFFAS) No. 4, "Managerial Cost Accounting Concepts and Standards for the Federal Government."

1.E. Revenues and Other Financing Sources

The Department receives congressional appropriations as financing sources for general funds that expire annually, on a multiyear basis, or do not expire. When authorized by legislation, these appropriations are supplemented by revenues generated by sales of goods or services. The Department recognizes revenue as a result of costs incurred for goods and services provided to other federal agencies and the public. Full-cost pricing is the Department's standard policy for services provided as required by OMB Circular A-25, "User Charges." The Department recognizes revenue when earned within the constraints of current system capabilities. In some instances, revenue is recognized when bills are issued.

Depot Maintenance and Ordnance WCF activities recognize revenue according to the percentage of completion method. Supply Management WCF activities recognize revenue from the sale of inventory items.

The Department does not include nonmonetary support provided by U.S. allies for common defense and mutual security in amounts reported in the Statement of Net Cost and Note 21, "Reconciliation of Net Cost of Operations to Budget." The U.S. has cost sharing agreements with other countries. Examples include countries where there is a mutual or reciprocal defense agreement, where U.S. troops are stationed, or where the U.S. Fleet is in a port.

1.F. Recognition of Expenses

For financial reporting purposes, the Department's policy requires the recognition of operating expenses in the period incurred. However, because the Department's financial and nonfinancial feeder systems were not designed to collect and record financial information on the full accrual accounting basis, estimates are made for major items such as payroll expenses, accounts payable, and environmental liabilities. In addition, expenditures for capital and other long-term assets are recognized as operating expenses. Expenses for operating materials and supplies are currently recognized when the items are purchased.

1.G. Accounting for Intragovernmental Transactions

Preparation of reliable financial statements requires the elimination of transactions occurring among entities within the Department or between two or more federal agencies. However, the Department cannot accurately eliminate intragovernmental transactions by customer because the Department's systems do not track buyer and seller data at the transaction level. Generally, seller entities within the Department provide summary seller-side balances for revenue, accounts receivable, and unearned revenue to the buyer-side internal Department accounting offices. In most cases, the buyer-side records are adjusted to agree with the Department's seller-side balances. Intra-Department governmental balances are then eliminated. The volume of intragovernmental transactions is so large that after-the-fact reconciliations cannot be accomplished effectively. The Department is developing long-term system improvements to ensure accurate intragovernmental information, to include sufficient up-front edits and controls, eliminating the need for after-the-fact reconciliations.

The U.S. Treasury Financial Management Service is responsible for eliminating transactions between the Department and other federal agencies. The U.S. Treasury's "Federal Intragovernmental Transactions Accounting Policies Guide" and Treasury Financial Manual Part 2 – Chapter 4700, "Agency Reporting Requirements for the Financial Report of the United States Government," provide guidance for reporting and reconciling intragovernmental balances. While the Department is unable to fully reconcile intragovernmental transactions with all federal partners, the Department is able to reconcile balances pertaining to investments in federal securities, borrowings from the U.S. Treasury and the Federal Financing Bank, Federal Employees' Compensation Act transactions with the Department of Labor, and benefit program transactions with the Office of Personnel Management.

The Department's proportionate share of public debt and related expenses of the Federal Government is not included. The Federal Government does not apportion debt and its related costs to federal agencies. The Department'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. Generally, financing for the construction of the Department's facilities is obtained through appropriations. To the extent this financing ultimately may have been obtained through the issuance of public debt, interest costs have not been capitalized since the U.S. Treasury does not allocate such costs to the Department.

1.H. Transactions with Foreign Governments and International Organizations

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

The Department additionally reports foreign military sales transactions on behalf of the Executive Office of the President.

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

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

In addition, DFAS sites and USACE Finance Center submit reports to the U.S. Treasury by appropriation on interagency transfers, collections received, and disbursements issued. The U.S. Treasury records these transactions to the applicable Fund Balance with Treasury (FBWT) account. The Department's recorded balance in FBWT accounts and U.S. Treasury's FBWT accounts must balance monthly.

1.J. Foreign Currency

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

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

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

1.K. Accounts Receivable

The Balance Sheet reports accounts receivable in three categories: accounts receivable, claims receivable, and refunds receivable from other federal entities or from the public. Allowances for uncollectible accounts due from the public are based upon an analysis of collection experience by fund type. The Department does not recognize an allowance for estimated uncollectible amounts from other federal agencies. Claims against other federal agencies are to be resolved between the agencies in accordance with dispute resolution procedures defined in the Intragovernmental Business Rules published in the Treasury Financial Manual at http://www.fms.treas.gov/tfm/vol1/07-03.pdf.

1.L. Direct Loans and Loan Guarantees

The Department operates a direct loan and loan guarantee program authorized by the National Defense Authorization Act for FY 1996, P.L. 104-106, Section 2801. The Act includes a series of authorities that allow the Department to work with the private sector to renovate military housing. The Department's goals are to obtain private capital to leverage government dollars, make efficient use of limited resources, and use a variety of private sector approaches to build and renovate military housing faster and at a lower cost to the American taxpayers.

The Act also provides the Department with a variety of authorities to obtain private sector financing and expertise to improve military housing. The Department uses these authorities individually or in combination. They include guarantees (both loan and rental), conveyance/leasing of existing property and facilities, differential lease payments, investments (both limited partnerships and stock/bond ownership), and direct loans.

The National Defense Authorization Act for FY 2005, P.L. 108-375, Section 2805 provided permanent authorities to the Military Housing Privatization Initiative (MHPI).

The Department operates a loan guarantee program designed to encourage commercial use of inactive government facilities. The revenue generated from property rental offsets the cost of maintaining these facilities.

The Department administers the Foreign Military Financing program on behalf of EOP. This program is authorized by sections 23 and 24 of the Arms Export Control Act of 1976, as amended, P.L. 90-629, as amended, and section 503(a). This program provides loans to help countries purchase U.S.-produced weapons, defense equipment, services, or military training. The direct loans and loan guarantees related to Foreign Military Sales are included in the basic financial statements.

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

1.M. Inventories and Related Property

The Department values approximately 63% of its resale inventory using the moving average cost method. An additional 9% (fuel inventory) is reported using the first-in-first-out method. The Department reports the remaining 28% of resale inventories at an approximation of historical cost using latest acquisition cost adjusted for holding gains and losses. The latest acquisition cost method is used because legacy inventory systems were designed for materiel management rather than accounting. Although these systems provide visibility and accountability over inventory items, they do not maintain historical cost data necessary to comply with SFFAS No. 3, "Accounting for Inventory and Related Property." Additionally, these systems cannot produce financial transactions using the USSGL, as required by the Federal Financial Management Improvement Act of 1996, P.L. 104-208. The Department is continuing to transition the balance of the inventories to the moving average cost method through the use of new inventory systems. However, since the on-hand balances which were transitioned were not, for the most part, baselined to auditable historical cost, the reported values remain noncompliant with SFFAS No. 3 and GAAP.

The Department manages only military or government-specific materiel under normal conditions. Materiel is a unique term that relates to military force management, and includes items such as ships, tanks, self-propelled weapons, aircraft, etc., and related spares, repair parts, and support equipment. Real property, installations, and utilities that are necessary to equip, operate, maintain, and support military activities without distinction as to application for administrative or combat purposes are excluded. Items commonly used in and available from the commercial sector are not managed in the Department's materiel management activities. Operational cycles are irregular and the military risks associated with stock-out positions have no commercial parallel. The Department holds materiel based on military need and support for contingencies. The Department does not attempt to account separately for "inventory held for sale" and "inventory held in reserve for future sale" based on SFFAS No. 3 definitions, unless otherwise noted.

Related property includes OM&S and stockpile materiels. The OM&S, including munitions not held for sale, are valued at standard purchase price. The Department uses both the consumption method and the purchase method of accounting for OM&S. Items that are centrally managed and stored, such as ammunition and engines, are generally recorded using the consumption method and are reported on the Balance Sheet as OM&S. When current systems cannot fully support the consumption method, the Department uses the purchase method. Under this method, materiels and supplies are expensed when purchased. During FY 2007, the Department expensed significant amounts using the purchase method because the systems could not support the consumption method or management deemed that the item was in the hands of the end user. This is a material weakness for the Department and long-term system corrections are in process. Once the proper systems are in place, these items will be accounted for under the consumption method of accounting.

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

The Department recognizes condemned materiel as "excess, obsolete, and unserviceable." The cost of disposal is greater than the potential scrap value; therefore, the net value of condemned materiel is zero. Potentially redistributed materiel, classified in previous years as "excess, obsolete, and unserviceable," is included in the "held for use" or "held for repair" categories according to its condition.

Inventory available and purchased for resale includes consumable spare and repair parts and repairable items owned and managed by the Department. This inventory is retained to support military or national contingencies. Inventory held for repair is damaged inventory that requires repair to make suitable for sale. Often, it is more economical to repair these items rather than to procure them. The Department often relies on weapon systems and machinery no longer in production. As a result, the Department supports a process that encourages the repair and rebuilding of certain items. This repair cycle is essential to maintaining a ready, mobile, and armed military force. Work in process balances include costs related to the production or servicing of items, including direct material, direct labor, applied overhead, and other direct costs. Work in process also includes the value of finished products or completed services that are yet to be placed in service and transferred to an asset account. Work in process includes munitions in production and depot maintenance work with its associated labor, applied overhead, and supplies used in the delivery of maintenance services.

1.N. Investments

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

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

The Department's net investments are held by various trust and special funds. These funds include the Military Retirement Trust Fund; Medicare-Eligible Retiree Health Care Fund; Other Defense Organizations General Fund trust and special funds; donations (Gift Funds); and the USACE South Dakota Terrestrial Habitat Restoration, Inland Waterways, and Harbor Maintenance Trust Fund accounts.

Other investments represent limited partnerships entered into on behalf of the U.S. Government in support of the MHPI authorized by P.L. 104-106, Section 2801. These investments do not require market value disclosure.

1.O. General Property, Plant and Equipment

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

Effective 3rd Quarter, FY 2006, the Department replaced the BEA estimation methodology with one based on departmental internal records for military equipment. The Department identified the universe of military equipment by accumulating information relating to program funding and associated military equipment, equipment useful life, program acquisitions, and disposals to create a baseline. The military equipment baseline is updated using expenditure information and information related to acquisitions and disposals.

In FY 2006, the Department revised the real property capitalization threshold from $100 thousand to $20 thousand. The current $100 thousand capitalization threshold remains unchanged for the remaining General Property, Plant and Equipment (PP&E) categories. Not all Military Departments have implemented this revised policy due to system and process limitations. General PP&E assets are capitalized at historical acquisition cost plus capitalized improvements when an asset has a useful life of two or more years and the acquisition cost equals or exceeds the Department's capitalization threshold. The Department also requires capitalization of improvement costs over the Department's capitalization threshold. The Department depreciates all General PP&E, other than land, on a straight-line basis.

Prior to FY 1996, General PP&E was capitalized if it had an acquisition cost of $15 thousand, $25 thousand, and $50 thousand for FYs 1993, 1994, and 1995 respectively, and an estimated useful life of two or more years. General PP&E previously capitalized at amounts below $100 thousand was written off General Fund financial statements in FY 1998. No adjustment was made for WCF assets that remain capitalized and reported on WCF financial statements.

The USACE Civil Works General PP&E is capitalized at historical acquisition cost plus capitalized improvements when an asset has a useful life of two or more years and the acquisition cost exceeds $25 thousand. One exception is that all buildings and structures related to hydropower projects are capitalized regardless of cost. Prior to FY 2004, the USACE capitalized all buildings and structures regardless of cost. In FY 2003, the USACE increased the threshold (effective FY 2004) for buildings and structures to $25 thousand for all Civil Works appropriations with the exception of Revolving Fund and Power Marketing Agency assets and expensed all previously acquired assets that did not meet the new $25 thousand threshold.

When it is in the best interest of the government, the Department provides government property to contractors to complete contract work. The Department either owns or leases such property, or it is purchased directly by the contractor for the government based on contract terms. When the value of contractor-procured General PP&E exceeds the Department's capitalization threshold, federal accounting standards require that it be reported on the Department's Balance Sheet.

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

1.P. Advances and Prepayments

The Department's policy is to record advances and prepayments in accordance with GAAP. As such, payments made in advance of the receipt of goods and services are reported as assets on the Balance Sheet. The Department's policy is to expense or capitalize assets when the related goods and services are received. Not all Department entities have implemented this policy primarily due to system limitations.

1.Q. Leases

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

Office space and leases entered into by the Department are the largest component of operating leases. These costs were gathered from existing leases, General Services Administration (GSA) bills, and interservice support agreements. Future year projections use the consumer price index (CPI) rather than the Department's inflation factor.

1.R. Other Assets

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

The Department conducts business with commercial contractors under two primary types of contracts: fixed price and cost reimbursable. To alleviate the potential financial burden on the contractor that long-term contracts can cause, the Department may provide financing payments. Contract financing payments are defined in the Federal Acquisition Regulation, Part 32, as authorized disbursements of monies to a contractor prior to acceptance of supplies or services by the Government. Contract financing payment clauses are incorporated in the contract terms and conditions and may include advance payments, performance-based payments, commercial advances and interim payments, progress payments based on cost, and interim payments under certain cost-reimbursement contracts.

Contract financing payments do not include invoice payments, payments for partial deliveries, lease and rental payments, or progress payments based on a percentage or stage of completion. The Defense Federal Acquisition Regulation Supplement authorizes progress payments based on a percentage or stage of completion only for construction of real property, shipbuilding and ship conversion, alteration, or repair. Progress payments for real property and ships are reported as construction in progress. It is the Department's policy to record certain contract financing payments as other asset.

1.S. Contingencies and Other Liabilities

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

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

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

1.T. Accrued Leave

The Department reports liabilities for military leave and accrued annual leave for DoD civilians. Sick leave for DoD civilians is expensed when taken. The liability reported at the end of the accounting period reflects the current pay rates.

1.U. Net Position

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

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

Cumulative results of operations represents the net difference between expenses and losses, and financing sources (including appropriations, revenue, and gains), since inception. Beginning with FY 1998, cumulative results of operations also includes donations and transfers in and out of assets that were not reimbursed.

1.V. Treaties for Use of Foreign Bases

The Department has the use of land, buildings, and other overseas facilities that are obtained through various international treaties and agreements negotiated by the Department of State. The Department purchases capital assets overseas with appropriated funds; however, the host country retains title to the land and capital improvements. Generally, treaty terms allow the Department continued use of these properties until the treaties expire. In the event treaties or other agreements are terminated, whereby use of the foreign bases is prohibited, losses are recorded for the value of any nonretrievable capital assets. The settlement due to the U.S. or host nation is negotiated and takes into account the value of capital investments and may be offset by the cost of environmental cleanup.

1.W. Comparative Data

The Department's financial statements and notes are presented on a comparative basis.

1.X. Unexpended Obligations

The Department obligates funds to provide goods and services for outstanding orders not yet delivered. Unless title has passed, the financial statements do not reflect a liability for payment for goods and services not yet delivered. Unexpended obligations includes both obligations for which goods and services have been delivered (title passed) and a liability recognized, and obligations for which no delivery has occurred and no liability recognized. The balance of unexpended obligations appears immediately before net outlays in the Statement of Budgetary Resources, and is referred to as "Total, unpaid obligated balances, net, end of period."

1.Y. Undistributed Disbursements and Collection

Undistributed disbursements and collections represent the difference between disbursements and collections matched at the transaction level to a specific obligation, payable, or receivable in the activity field records as opposed to those reported by the U.S. Treasury. These amounts should agree with the undistributed amounts reported on the departmental accounting reports. In-transit payments are those payments that have been made, but have not been recorded in the fund holder's accounting records. These payments are applied to the outstanding accounts payable balance. In-transit collections are those collections from other agencies or entities that have not been recorded in the accounting records. These collections are applied to the accounts receivable balance.

The Department's policy is to allocate supported undistributed disbursements and collections between federal and nonfederal categories based on the percentage of distributed federal and nonfederal accounts payable and accounts receivable. Unsupported undistributed disbursements are recorded in accounts payable. Unsupported undistributed collections are recorded in other liabilities.

1.Z. Significant Events

In FY 2007 the Department made several modifications to its financial reports and notes that had significant and pervasive effects. These changes are summarized below:

In response to updated reporting requirements from OMB, the Department began reporting in its basic financial statements all activity for the programs it administers on behalf of the Executive Office of the President including the Foreign Military Sales Program (FMS). Previously, the Department reported these programs as "Other Accompanying Information" in its Performance and Accountability Report.

Prior to FY 2007, the Department had reported the current year changes only in undelivered orders, contract authority, collections, and disbursements for FMS. Based on changes to accounting and reporting methodologies, the Department now correctly reflects undelivered orders, contract authority, and Fund Balance with Treasury (FBWT) for FMS in its financial statements and notes with cumulative-from-inception balances.

In addition, the Department no longer reports FMS undelivered orders and FBWT in the Statement of Custodial Activity (SCA). The Department's remaining custodial activity is immaterial and incidental to its primary mission. Therefore, the Department is no longer producing a SCA. Note 22 has been renamed and revised to report "Incidental Custodial Collections."

In accordance with updated reporting requirements in OMB Circular A-136, the Department eliminated the Statement of Financing and began presenting the information formerly contained in the Statement in Note 21 "Reconciliation of Net Cost of Operations to Budget."

Note 2. Nonentity Assets

As of September 30	2007	2006 Restated
(amounts in millions)		
Intragovernmental Assets		
Fund Balance with Treasury	$ 9,926.3	$ 2,896.6
Accounts Receivable	0.9	11.6
Total Intragovernmental Assets	9,927.2	2,908.2
Nonfederal Assets		
Cash and Other Monetary Assets	14,879.6	2,085.2
Accounts Receivable	5,162.9	5,486.7
Other Assets	9,386.9	196.8
Total Nonfederal Assets	29,429.4	7,768.7
Total Nonentity Assets	39,356.6	10,676.9
Total Entity Assets	1,466,988.9	1,361,961.0
Total Assets	$ 1,506,345.5	$ 1,372,637.9

Nonentity assets are assets for which the Department maintains stewardship accountability and responsibility to report, but are not available for the Department's operations.

Nonentity Fund Balance with Treasury is comprised of deposit funds, seized Iraqi cash, the Development Fund for Iraq (DFI), and advances from foreign governments for Foreign Military Sales Trust Funds (FMSTF) for the purchase of defense articles and services. Deposit funds are generally used to record amounts held temporarily until paid to the appropriate party. Seized Iraqi cash is former Iraqi regime monies confiscated by coalition forces and restricted for support of the Iraqi people. The DFI consists of proceeds from Iraqi oil sales, repatriated assets from the United States and other nations, and deposits from unencumbered oil-for-food proceeds. The DFI funds are restricted for Iraqi infrastructure and other Iraqi support needs.

Intragovernmental Accounts Receivable consists of amounts due from cancelled appropriations.

Nonfederal Cash and Other Monetary Assets consists of cash received from foreign governments deposited in the Federal Reserve Bank, U.S. commercial banks and foreign banks; and cash held by Disbursing Officers to carry out payment, collection, and foreign currency accommodation exchange missions.

Nonfederal Accounts Receivable consists of amounts due for cancelled year appropriations; and interest, fines and penalties due on debt. The Department generally cannot use the collections and must distribute them to the U.S. Treasury. The Department has specific statutory authority to retain collections from certain cancelled year accounts receivable as entity assets.

Nonfederal Other Assets primarily consists of advances paid to contractors for undelivered defense articles and services owed to foreign governments.

The Department is reporting nonentity balances of Fund Balance with Treasury of $8.5 billion, Cash and Other Monetary Assets of $12.4 billion, and Other Assets of $9.2 billion on behalf of the Executive Office of the President. The Department holds these amounts as stewards on the behalf of others and are therefore, not available for use by the Department.

Note 3. Fund Balance with Treasury

As of September 30	2007	2006 Restated
(amounts in millions)		
Fund Balances		
Appropriated Funds	$ 383,074.3	$ 313,962.4
Revolving Funds	11,021.1	9,619.6
Trust Funds	9,703.5	2,212.2
Special Funds	396.5	328.1
Other Fund Types	2,971.6	2,922.8
Total Fund Balances	407,167.0	329,045.1
Fund Balances Per Treasury Versus Agency		
Fund Balance per Treasury	399,862.9	329,921.4
Fund Balance per Agency	407,167.0	329,045.1
Reconciling Amount	$ (7,304.1)	$ 876.3

Fund Balance with Treasury includes immaterial nonentity balances the Department holds on behalf of others, and entity balances which represent funds with Treasury for which the Department is authorized to make expenditures and pay liabilities. It reflects the balance of all fund types held by the Department.

Other Fund Types primarily consists of deposit funds, receipt accounts, clearing accounts, seized Iraqi cash, Development Fund for Iraq, and Foreign Military Sales Trust Funds (FMSTF) advance deposits.

The Department shows a reconciling net difference of ($7.3) billion with the U.S. Treasury. This includes ($11.9) billion differences due to the U.S. Treasury treatment of allocation transfers, offset by $3.2 billion in cancelled appropriations and $1.4 billion in unavailable receipt accounts.

The balance in Fund Balance with Treasury includes $11.9 billion ($3.4 billion entity and $8.5 billion nonentity) that the Department is executing on behalf of the Executive Office of the President. The Department holds these amounts as stewards on the behalf of others and are therefore, not available for use by the Department.

Status of Fund Balance with Treasury		
As of September 30	2007	2006 Restated
(amounts in millions)		
Unobligated Balance		
Available	$ 99,188.4	$ 75,403.0
Unavailable	338,343.1	302,061.5
Obligated Balance not yet Disbursed	437,085.6	323,823.5
Nonbudgetary FBWT	4,755.7	7,640.4
NonFBWT Budgetary Accounts	(472,205.8)	(379,883.3)
Total	$ 407,167.0	$ 329,045.1

The Status of Fund Balance with Treasury is the reconciliation between budgetary and proprietary accounts at Treasury. It consists of unobligated and obligated balances. The balances reflect the budgetary authority remaining for disbursement against current or future obligations.

Unobligated Balance is classified as available or unavailable and represents the cumulative amount of budgetary authority that has not been set aside to cover outstanding obligations. The unavailable balance consists primarily of funds invested in U.S. Treasury securities that are temporarily precluded from obligation by law.

Obligated Balance not yet Disbursed represents funds that have been obligated for goods and services not received, and those received but not paid.

Nonbudgetary FBWT includes accounts that do not have budgetary authority, such as deposit funds, receipt accounts, clearing accounts, and nonentity FBWT.

NonFBWT Budgetary Accounts reduces the Status of FBWT and consists of investments in U.S. Treasury securities, contract and borrowing authority, unfilled customer orders without advance, and receivables.

Certain unobligated balances are restricted for future use and are not apportioned for current use. Unobligated balances for trust fund accounts are restricted for use by the Public Law that established the funds.

Disclosures Related to Suspense/Budget Clearing Accounts				
As of September 30	2005	2006	2007	(Decrease)/ Increase FY 2006-2007
(amounts in millions)				
Account				
F3845 – Personal Property Proceeds	$ 0.9	$ 0.7	$ 0.8	$ 0.1
F3875 – Budget Clearing Account Suspense	263.5	903.9	20.0	(883.9)
F3880 – Lost or Cancelled Treasury Checks	11.9	26.4	5.8	(20.6)
F3882 – Uniformed Services Thrift Savings Plan Suspense	83.5	108.5	115.8	7.3
F3885 – Interfund/IPAC Suspense	(211.6)	(114.9)	(100.2)	14.7
F3886 – Thrift Savings Plan Suspense	(4.9)	(6.4)	(10.1)	(3.7)
Total	$ 143.3	$ 918.2	$ 32.1	$ (886.1)

Abnormal Balances

The ($10.1) million balance for F3886 suspense account reflects the timing differences due to the additional processing time for negative adjustments, lost earnings, forfeitures, and loan repayments.

Other Disclosures

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

The F3875 and F3885 suspense accounts temporarily hold collections or disbursements until identified and applied to a valid appropriation.

The F3880 suspense account represents the balance of U.S. Treasury checks that: (1) have either been lost by the payee and need to be reissued, (2) have never been cashed by the payee, or (3) have been cancelled by the U.S. Treasury and need to be transferred to the original appropriation.

The F3882 and F3886 suspense accounts represent the difference between retirement funds withheld from members of the uniformed services and civilians employed by the Department and amounts transferred to the Federal Retirement Thrift Investment Board, who administers the Thrift Savings Plan.

Disclosures Related to Problem Disbursements and In-Transit Disbursements				
As of September 30	2005	2006 Restated	2007	(Decrease)/ Increase from FY 2006 – 2007
(amounts in millions)				
Total Problem Disbursements, Absolute Value				
Unmatched Disbursements (UMDs)	$ 2,225.3	$ 1,353.4	$ 1,414.1	$ 60.7
Negative Unliquidated Obligations (NULO)	95.5	78.6	107.9	29.3
In-Transit Disbursements	6,869.4	6,994.3	7,534.3	540.0
Total	$ 9,190.2	$ 8,426.3	$ 9,056.3	$ 630.0

The Department reports Problem Disbursements as an absolute value, which is the sum of the debit and credit transactions without regard to the sign.

An Unmatched Disbursement occurs when a payment does not match an obligation in the accounting system.

A Negative Unliquidated Obligation occurs when a payment matches, but exceeds a valid obligation in the accounting system.

In-Transit Disbursements represents disbursements and collections made by a disbursing activity on behalf of an accountable activity and not posted to the accounting system.

The amounts reported in FY 2005 and FY 2006 were changed to correct balances and to change reporting methodology from net to absolute for In-Transit Disbursements.

Note 4. Investments and Related Interest

As of September 30	2007				
(amounts in millions)	Cost	Amortization Method	Amortized (Premium)/ Discount	Investments, Net	Market Value Disclosure
Intragovernmental Securities					
Nonmarketable, Market- Based					
Military Retirement Fund	$ 222,030.5	See Below	$ (6,666.2)	$ 215,364.3	$ 212,242.6
Medicare Eligible Retiree Health Care Fund	110,206.3	See Below	(1,762.9)	108,443.4	106,692.8
US Army Corps of Engineers	4,058.5	See Below	(44.1)	4,014.4	4,043.1
Other Funds	2,039.0	See Below	(11.5)	2,027.5	2,040.2
Total Nonmarketable, Market-Based	338,334.3		(8,484.7)	329,849.6	325,018.7
Accrued Interest	3,861.4			3,861.4	3,861.4
Total Intragovernmental Securities	342,195.7		(8,484.7)	333,711.0	328,880.1
Other Investments					
Total Other Investments	$ 1,412.3		$ 0.0	$ 1,412.3	$ N/A

As of September 30	2006				
(amounts in millions)	Cost	Amortization Method	Amortized (Premium)/ Discount	Investments, Net	Market Value Disclosure
Intragovernmental Securities					
Nonmarketable, Market-Based					
Military Retirement Fund	$ 213,248.6	See Below	$ (7,889.9)	$ 205,358.7	$ 202,876.7
Medicare Eligible Retiree Health Care Fund	85,730.6	See Below	(1,123.3)	84,607.3	82,962.7
US Army Corps of Engineers	3,632.9	See Below	(81.3)	3,551.6	3,519.5
Other Funds	1,911.1	See Below	(11.1)	1,900.0	1,900.6
Total Nonmarketable, Market-Based	304,523.2		(9,105.6)	295,417.6	291,259.5
Accrued Interest	3,843.6			3,843.6	3,843.6
Total Intragovernmental Securities	308,366.8		(9,105.6)	299,261.2	295,103.1
Other Investments					
Total Other Investments	$ 1,089.8		$ 0.0	$ 1,089.8	$ N/A

Amortization Method Used: Effective Interest

The market value of the non-marketable securities held by the Department fluctuates in tandem with the current selling price of the equivalent marketable security on the open bond market. It is the intent of the Department to hold the investments to maturity to prevent losses on the securities.

The Federal Government does not set aside assets to pay future benefits and expenditures associated with earmarked funds. The cash generated from earmarked funds is deposited in the U.S. Treasury, which uses the cash for general Government purposes. The U.S. Treasury securities are issued to the earmarked funds as evidence of its receipts. The U.S. Treasury securities are an asset to the Department and a liability to the U.S. Treasury. Because the Department and the U.S. Treasury are both parts of the Government, these assets and liabilities offset each other from the standpoint of the Government as a whole. For this reason, they do not represent an asset or a liability in the U.S. Governmentwide financial statements.

The U.S. Treasury securities provide the Department with authority to draw upon the U.S. Treasury to make future benefit payments or other expenditures. When the Department requires redemption of these securities, the Government finances the securities out of accumulated cash balances, by raising taxes or other receipts, by borrowing from the public or repaying less debt, or by curtailing other expenditures. This is the same way the Government finances all other expenditures.

Other Funds are primarily comprised of DoD Education Benefits Fund and Voluntary Separation Incentive investments.

Note 5. Accounts Receivable

As of September 30	2007			2006 Restated
(amounts in millions)	Gross Amount Due	Allowance For Estimated Uncollectibles	Accounts Receivable, Net	Accounts Receivable, Net
Intragovernmental Receivables	$ 1,412.9	$ N/A	$ 1,412.9	$ 2,941.8
Nonfederal Receivables (From the Public)	7,702.1	(232.7)	7,469.4	7,864.1
Total Accounts Receivable	$ 9,115.0	$ (232.7)	$ 8,882.3	$ 10,805.9

Aged Accounts Receivable				
As of September 30	2007		2006	
	Intragovernmental	Nonfederal	Intragovernmental	Nonfederal
(amounts in millions)				
Category				
Nondelinquent				
Current	$ 8,299.6	$ 1,771.0	$ 7,735.6	$ 1,840.8
Noncurrent	233.9	1,607.4	232.1	1,740.9
Delinquent				
1 to 30 days	132.3	167.4	321.1	159.9
31 to 60 days	50.0	136.7	345.7	53.4
61 to 90 days	54.3	98.0	57.2	117.8
91 to 180 days	68.1	184.5	716.5	130.0
181 days to 1 year	49.8	201.9	908.7	207.2
Greater than 1 year and less than or equal to 2 years	65.4	205.4	44.4	192.2
Greater than 2 years and less than or equal to 6 years	25.1	169.2	55.0	896.2
Greater than 6 years and less than or equal to 10 years	0.7	588.9	1.2	676.0
Greater than 10 years	0.0	2,714.4	0.0	2,640.5
Subtotal	8,979.2	7,844.8	10,417.5	8,654.9
Less Supported Undistributed Collections	(76.8)	(162.1)	(492.7)	(478.9)
Less Eliminations	(7,166.8)	0.0	(6,986.3)	0.0
Less Other	(322.7)	19.4	(11.1)	38.5
Total	$ 1,412.9	$ 7,702.1	$ 2,927.4	$ 8,214.5

The prior year Intragovernmental accounts receivable on the aging schedule does not agree with the accounts receivable reported on the Balance Sheet. The FY 2006 aging schedule does not include $14.4 million for the Foreign Military Account Program.

Nondelinquent noncurrent accounts receivable consists of nonfederal receivables of $1.6 billion on repayment schedules primarily for long term water storage contracts with state and local municipalities. The balance represents intragovernmental accounts receivable collected but not posted to accounting systems.

The Intragovernmental Other consists of pending customer returns.

The Nonfederal Other reflects reconciling differences between the general and subsidiary ledgers.

The Department generates debt letters and pursues all debts over 30 days delinquent. For debts over 180 days delinquent, the Department utilizes various offset programs and collection agencies to pursue collections. In certain instances, the status of litigation affects the Department's ability to pursue collection actions.

Note 6. Other Assets

As of September 30	2007	2006
(amounts in millions)		
Intragovernmental Other Assets		
Advances and Prepayments	$ 1,087.6	$ 1,064.7
Other Assets	124.9	124.9
Total Intragovernmental Other Assets	1,212.5	1,189.6
Nonfederal Other Assets		
Outstanding Contract Financing Payments	25,030.3	25,630.4
Advances and Prepayments From Foreign Governments	8,015.3	0.0
Advances and Prepayments From the Public	1,549.6	1,176.2
Other Assets (With the Public)	1,650.9	1,122.1
Total Nonfederal Other Assets	36,246.1	27,928.7
Total Other Assets	$ 37,458.6	$ 29,118.3

Intragovernmental Other Assets consists of the Department's right to approximately six million barrels of crude oil held by the Department of Energy.

Advances and Prepayments From Foreign Governments is comprised of advances paid to contractors for undelivered defense articles and services owed to foreign governments under the Foreign Military Sales Program.

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

Outstanding Contract Financing Payments balance of $25.0 billion is comprised of $23.4 billion in contract financing payments and an additional $1.7 billion in estimated future payments to the contractor upon delivery and Government acceptance of a satisfactory product. (See additional discussion in Note 15, Other Liabilities.)

Nonfederal Other Assets consists primarily of undelivered assets.

The balance in Other Assets includes $9.4 billion that the Department is executing on behalf of the Executive Office of the President. The Department holds these amounts as stewards on the behalf of others and the assets are therefore, not available for use by the Department.

Note 7. Cash and Other Monetary Assets

As of September 30	2007	2006
(amounts in millions)		
Cash	$ 13,907.0	$ 1,389.0
Foreign Currency	1,121.0	810.8
Total Cash, Foreign Currency, & Other Monetary Assets	$ 15,028.0	$ 2,199.8

The Department began reporting the accrued assets, liabilities, and expenses of the Foreign Military Sales Trust Fund during FY 2007, resulting in the recognition of an additional $12.4 billion in cash. Nonentity assets of $15.0 billion, consisting of $13.7 billion in cash and $1.1 billion in foreign currency which are restricted and unavailable for use in the Department's mission.

The balance in Cash includes $12.4 billion that the Department is executing on behalf of the Executive Office of the President. The Department holds these amounts as stewards on the behalf of others and are therefore, not available for use by the Department.

Note 8. Direct Loan and/or Loan Guarantee Programs

Direct Loan and/or Loan Guarantee Programs

The Department operates the following direct loan and loan guarantee programs:

- Foreign Military Account Program (FMA)
- Military Housing Privatization Initiative (MHPI)
- Armament Retooling and Manufacturing Support Initiative (ARMS)

The Federal Credit Reform Act of 1990 governs all amended direct loan obligations and loan guarantee commitments made after FY 1991 and the resulting direct loans or loan guarantees. The OMB Circular A-11, section 185, "Federal Credit" and OMB Circular A-129 provide additional guidance for direct loan and loan guarantee programs.

Direct loans are reported at the net present value of the following projected cash flows:

- Loan disbursements;
- Repayments of principal; and
- Payments of interest and other payments over the life of the loan after adjusting for estimated defaults, prepayments, fees, penalties and other recoveries.

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

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

Foreign Military Account Program

The FMA is a military assistance program that includes both direct loan and loan guarantee programs. The Department is authorized by the U.S. Congress to execute the authorities of the Foreign Assistance Act of 1961, as amended, section 503(a) and the Arms Export Control Act of 1976, as amended, section 23. The Defense Security Cooperation Agency, under the auspices of the Executive Office of the President (EOP), administers the FMA program. The FMA program is comprised of: (1) the pre 1992 Foreign Military Loan Liquidating Account, (2) the post 1991 Foreign Military Financing Account, and (3) the post 1991 Military Debt Reduction Financing Account.

Military Housing Privatization Initiative

The MHPI includes both direct loan and loan guarantee programs. The loan guarantee program is authorized by the National Defense Authorization Act for FY 1996, Public Law 104-106, Statute 186, Section 2801, and includes a series of authorities that allow the Department to work with the private sector to renovate and build military family housing. The MHPI accelerates the construction of new housing, builds to market standards, and leverages private sector capital with government dollars. The Department provides protection to the private sector partner against specific risks, such as base closure or member deployment.

Armament Retooling and Manufacturing Support Initiative

The ARMS Initiative, authorized by Title 10 United States Code 4551-4555, is a loan guarantee program designed to incentivize commercial use of the Army's inactive ammunition plants for businesses willing to locate to a government ammunition production facility. The production capacity of these facilities is greater than current military requirements; however, this capacity may be needed in the future. Revenues from property rental are used to help offset the overhead costs for the operation, maintenance and environmental cleanup at the facilities.

In an effort to preclude additional loan liability, the Army instituted an ARMS loan guarantee moratorium in FY 2004. The Army continues to operate under the moratorium and does not anticipate new loans.

Summary of Direct Loans and Loan Guarantees		
As of September 30	2007	2006 Restated
(amounts in millions)		
Loans Receivable		
Direct Loans		
Foreign Military Loan Liquidating Account	$ 2,683.2	$ 2,865.6
Military Housing Privatization Initiative	212.1	191.7
Foreign Military Financing Account	92.7	573.5
Military Debt Reduction Financing Account	219.0	224.3
Total Direct Loans	3,207.0	3,855.1
Defaulted Loan Guarantees		
Armament Retooling & Manufacturing Support Initiative	0.1	0.0
Total Default Loan Guarantees	0.1	0.0
Total Loans Receivable	3,207.1	3,855.1
Loan Guarantee Liability		
Military Housing Privatization Initiative	24.7	23.8
Armament Retooling & Manufacturing Support Initiative	0.3	13.0
Total Loan Guarantee Liability	$ 25.0	$ 36.8

Loans receivable, net, or value of assets related to loans, is not the same as the proceeds the Department would expect to receive from selling the loans.

Direct Loans Obligated		
As of September 30	2007	2006 Restated
(amounts in millions)		
Direct Loans Obligated Prior to FY 1992		
(Allowance for Loss Method):		
Foreign Military Loan Liquidating Account		
Loans Receivable Gross	$ 1,364.2	$ 1,629.3
Interest Receivable	1,319.0	1,236.3
Value of Assets Related to Direct Loans, Net	2,683.2	2,865.6
Direct Loans Obligated After FY 1991		
(Present Value Method):		
Military Housing Privatization Initiative		
Loans Receivable Gross	308.0	296.3
Allowance for Subsidy Cost (Present Value)	(95.9)	(104.6)
Value of Assets Related to Direct Loans	212.1	191.7
Foreign Military Financing Account		
Loans Receivable Gross	0.0	214.4
Interest Receivable	0.0	3.1
Allowance for Subsidy Cost (Present Value)	92.7	356.0
Value of Assets Related to Direct Loans	92.7	573.5
Military Debt Reduction Financing Account		
Loans Receivable Gross	512.1	511.3
Interest Receivable	25.3	14.1
Allowance for Subsidy Cost (Present Value)	(318.4)	(301.1)
Value of Assets Related to Direct Loans	219.0	224.3
Total Direct Loans Receivable	$ 3,207.0	$ 3,855.1

Abnormal Balances

The abnormal balance in the Allowance for Subsidy Cost for the Foreign Military Financing Account reflects loans prepaid in FY 2006 and FY 2007. The allowance for subsidy cost was adjusted to reflect the balance due to the U.S. Treasury.

Total Amount of Direct Loans Disbursed		
As of September 30	2007	2006 Restated
(amounts in millions)		
Direct Loan Programs		
Military Housing Privatization Initiative	$ 11.9	$ 155.0
Foreign Military Financing Account	299.0	274.9
Total	$ 310.9	$ 429.9

Subsidy Expense for Post FY 1991 Direct Loan					
As of September 30					
(amounts in millions)					
2007	Interest Differential	Defaults	Fees	Other	Total
New Direct Loans Disbursed:					
Military Housing Privatization Initiative	$ 2.1	$ 1.3	$ 0.0	$ 0.0	$ 3.4
2006	Interest Differential	Defaults	Fees	Other	Total
New Direct Loans Disbursed:					
Military Housing Privatization Initiative	$ 27.9	$ 20.7	$ 0.0	$ 0.0	$ 48.6
2007	Modifications	Interest Rate Reestimates	Technical Reestimates	Total Reestimates	Total
Direct Loan Modifications and Reestimates:					
Military Housing Privatization Initiative	$ 0.0	$ (7.3)	$ (8.2)	$ (15.5)	$ (15.5)
Foreign Military Financing Account	0.0	62.6	0.0	62.6	62.6
Total	$ 0.0	$ 55.3	$ (8.2)	$ 47.1	$ 47.1
2006 Restated	Modifications	Interest Rate Reestimates	Technical Reestimates	Total Reestimates	Total
Direct Loan Modifications and Reestimates:					
Military Housing Privatization Initiative	$ 0.0	$ (0.3)	$ (7.8)	$ (8.1)	$ (8.1)
Foreign Military Financing Account	0.0	0.0	(17.7)	(17.7)	(17.7)
Total	$ 0.0	$ (0.3)	$ (25.5)	$ (25.8)	$ (25.8)

	2007	2006 Restated
Total Direct Loan Subsidy Expense:		
Military Housing Privatization Initiative	$ (12.1)	$ 40.5
Foreign Military Financing Account	62.6	(17.7)
Total	$ 50.5	$ 22.8

Subsidy Rate for Direct Loans by Program					
As of September 30	Interest Differential	Defaults	Fees and Other Collections	Other	Total
Budget Subsidy for Direct Loans:					
Military Housing Privatization Initiative	16.07%	10.31%	0.00%	0.00%	26.38%

Subsidy rates pertain to the loan agreements contracted during the current fiscal year. These rates cannot be applied to the direct loans disbursed during the current reporting year to yield the subsidy expense. The subsidy expense for new loans disbursed in the current year could result from disbursement of loans from both current and prior year loan agreements. The subsidy expense reported in the current year also includes reestimates.

Schedule for Reconciling Subsidy Cost Allowance Balances for Post 1991 Direct Loans		
As of September 30	2007	2006 Restated
(amounts in millions)		
Beginning Balance of the Subsidy Cost Allowance	$ 49.7	$ 63.1
Add: Subsidy Expense for Direct Loans Disbursed during the Reporting Years by Component		
Interest Rate Differential Costs	2.1	27.9
Default Costs (Net of Recoveries)	1.3	20.7
Total of the above Subsidy Expense Components	3.4	48.6
Adjustments		
Loans Written Off	(5.0)	(24.2)
Subsidy Allowance Amortization	219.4	(12.0)
Other	7.0	0.0
Total of the above Adjustment Components	221.4	(36.2)
Ending Balance of the Subsidy Cost Allowance before Reestimates	274.5	75.5
Add or Subtract Reestimates by Component		
Interest Rate Reestimate	55.3	(0.3)
Technical/Default Reestimate	(8.2)	(25.5)
Total of the above Reestimate Components	47.1	(25.8)
Ending Balance of the Subsidy Cost Allowance	$ 321.6	$ 49.7

Three Foreign Military Financing Account loans were prepaid in FY 2006 and FY 2007. The allowance for subsidy cost was adjusted to reflect the balance due to the U.S. Treasury.

Defaulted Guaranteed Loans		
As of September 30	2007	2006
(amounts in millions)		
Defaulted Guaranteed Loans from Post-FY 1991 Guarantees		
(Present Value Method):		
Armament Retooling & Manufacturing Support Initiative		
Defaulted Guaranteed Loans Receivable, Gross	$ 14.4	$ 0.0
Allowance for Subsidy Cost (Present Value)	(14.3)	0.0
Total Value of Assets Related to Defaulted Guaranteed Loans Receivable	$ 0.1	$ 0.0

The value of assets related to defaulted guaranteed loans totaling $0.1 million represents the net recovery from a defaulted loan.

Guaranteed Loans Outstanding		
As of September 30	Outstanding Principal of Guaranteed Loans, Face Value	Amount of Outstanding Principal Guaranteed
(amounts in millions)		
Guaranteed Loans Outstanding		
Military Housing Privatization Initiative	$ 499.1	$ 499.1
Armament Retooling & Manufacturing Support Initiative	4.1	3.5
Total	503.2	502.6
2007 New Guaranteed Loans Disbursed	0.0	0.0
2006 New Guaranteed Loans Disbursed		
Armament Retooling & Manufacturing Support Initiative	2.7	2.3
Total	$ 2.7	$ 2.3

In FY 2006, an incremental disbursement of $2.7 million was made on a loan guaranteed previous to the 2004 moratorium on new ARMS Initiative loans.

Liabilities for Post FY 1991 Loan Guarantees, Present Value		
As of September 30	2007	2006
(amounts in millions)		
Military Housing Privatization Initiative	$ 24.7	$ 23.8
Armament Retooling & Manufacturing Support Initiative	0.3	13.0
Total Loan Guarantee Liability	$ 25.0	$ 36.8

Pre-1992 loan guarantee liabilities are to be calculated based on the allowance method. Currently no allowances are reported.

Subsidy Expense for Loan Guarantees by Program					
As of September 30					
(amounts in millions)					
	Interest Differential	Defaults	Fees	Other	Total
2007 New Loan Guarantees Disbursed:					
Military Housing Privatization Initiative	$ 0.0	$ 0.0	$ 0.0	$ 0.0	$ 0.0
Armament Retooling & Manufacturing Support Initiative	0.0	0.0	0.0	0.0	0.0
2006 New Loan Guarantees Disbursed:					
Military Housing Privatization Initiative	0.0	0.0	0.0	0.0	0.0
Armament Retooling & Manufacturing Support Initiative	0.0	0.0	0.0	0.0	0.0
	Modifications	Interest Rate Reestimates	Technical Reestimates	Total Reestimates	Total
2007 Modifications and Reestimates:					
Military Housing Privatization Initiative	0.0	0.0	(0.2)	(0.2)	(0.2)
Armament Retooling & Manufacturing Support Initiative	0.0	2.1	(1.1)	1.0	1.0
Total	$ 0.0	$ 2.1	$ (1.3)	$ 0.8	$ 0.8

	Modifications	Interest Rate Reestimates	Technical Reestimates	Total Reestimates	Total
2006 Modifications and Reestimates:					
Military Housing Privatization Initiative	$ 0.0	$ 0.0	$ (6.4)	$ (6.4)	$ (6.4)
Armament Retooling & Manufacturing Support Initiative	0.0	0.2	11.6	11.8	11.8
Total	$ 0.0	$ 0.2	$ 5.2	$ 5.4	$ 5.4

	2007	2006
Total Loan Guarantee:		
Military Housing Privatization Initiative	$ (0.2)	$ (6.4)
Armament Retooling & Manufacturing Support Initiative	1.0	11.8
Total	$ 0.8	$ 5.4

Subsidy Rates for Loan Guarantees

There are no subsidy rates to report because the Department did not have any new loan guarantees in FY 2007.

Schedule for Reconciling Loan Guarantee Liability Balances for Post FY 1991 Loan Guarantees		
As of September 30	2007	2006
(amounts in millions)		
Beginning Balance of the Loan Guarantee Liability	$ 36.8	$ 41.1
Add: Subsidy Expense for Guaranteed Loans Disbursed during the Reporting Years	0.0	0.0
Adjustments		
Foreclosed Property and Loans Acquired	2.3	0.0
Claim Payments to Lenders	(15.3)	(11.4)
Interest Accumulation on the Liability Balance	0.6	1.7
Other	(0.2)	0.0
Total of the above Adjustments	(12.6)	(9.7)
Ending Balance of the Loan Guarantee Liability before Reestimates	24.2	31.4
Add or Subtract Subsidy Reestimates by Component		
Interest Rate Reestimate	2.1	0.2
Technical/default Reestimate	(1.3)	5.2
Total of the above Reestimate Components	0.8	5.4
Ending Balance of the Loan Guarantee Liability	$ 25.0	$ 36.8

Administrative Expenses

Administrative Expenses are limited to separately identified expenses for administrating direct loans and loan guarantee programs. The Department does not maintain a separate program to capture the expenses related to direct loans and loan guarantees for MHPI and the FMA. Administrative expenses for ARMS represent a fee paid to U.S. Department of Agriculture, Rural Business Cooperative.

Note 9. Inventory and Related Property

As of September 30	2007	2006
(amounts in millions)		
Inventory, Net	$ 84,191.0	$ 83,861.1
Operating Materials & Supplies, Net	139,871.2	146,883.3
Stockpile Materials, Net	886.5	1,078.8
Total	$ 224,948.7	$ 231,823.2

Inventory, Net					
As of September 30	2007			2006	
(amounts in millions)	Inventory, Gross Value	Revaluation Allowance	Inventory, Net	Inventory, Net	Valuation Method
Inventory Categories					
Available and Purchased for Resale	$ 86,546.5	$ (25,465.8)	$ 61,080.7	$ 56,674.9	LAC,MAC
Held for Repair	31,477.7	(9,003.8)	22,473.9	26,349.0	LAC,MAC
Excess, Obsolete, and Unserviceable	7,324.0	(7,324.0)	0.0	0.0	NRV
Raw Materials	100.1	0.0	100.1	43.1	LAC,SP,MAC
Work in Process	536.3	0.0	536.3	794.1	AC
Total	$ 125,984.6	$ (41,793.6)	$ 84,191.0	$ 83,861.1	

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
MAC = Moving Average Cost

Restrictions

Generally, there are no restrictions on the use, sale, or disposition of inventory. However, some restrictions currently do exist, and they include the following:

- War reserve materiel valued at $2.1 billion;
- Commissary items valued at $341.9 million for purchase by authorized patrons;
- Dispositions pending litigation or negotiation valued at $1.5 million; or
- Identified safety stocks restricted from sale outside the federal government.

There are no known restrictions on inventory disposition as related to environmental or other liabilities.

General Composition of Inventory

Inventory includes spare and repair parts, clothing and textiles, and fuels held for sale by the Defense Working Capital Funds. Inventory is tangible personal property that is:

- Held for sale, or held for repair and eventual sale;
- In the process of production for sale; or
- To be consumed in the production of goods for sale or in the provision of service for a fee.

The Department assigns inventory items to a category based upon the type and condition of the asset.

Operating Materials and Supplies, Net					
As of September 30	2007			2006	
(amounts in millions)	OM&S Gross Value	Revaluation Allowance	OM&S, Net	OM&S, Net	Valuation Method
OM&S Categories					
Held for Use	$ 123,958.8	$ (0.8)	$ 123,958.0	$ 130,617.2	SP, LAC,MAC
Held for Repair	17,021.7	(1,108.5)	15,913.2	16,266.1	SP, LAC,MAC
Excess, Obsolete, and Unserviceable	2,387.3	(2,387.3)	0	0	NRV
Total	$ 143,367.8	$ (3,496.6)	$ 139,871.2	$ 146,883.3	
Legend for Valuation Methods: Adjusted LAC = Latest Acquisition Cost, adjusted for holding gains and losses SP = Standard Price NRV = Net Realizable Value MAC = Moving Average Cost					

Restrictions

Some munitions included in Operating Materiels and Supplies (OM&S) are restricted due to condition. Restricted munitions are considered obsolete or unserviceable when they cannot be expected to meet performance requirements. Obsolete and unserviceable OM&S may be used in emergency combat situations in which no other suitable munitions are immediately available.

General Composition of Operating Materials and Supplies

The OM&S includes spare and repair parts, ammunition, tactical missiles, aircraft configuration pods, and centrally managed aircraft engines held for consumption.

The Department assigns OM&S items to a category based upon the type and condition of the asset.

Stockpile Materials, Net					
As of September 30	2007			2006	
(amounts in millions)	Stockpile Materials Amount	Allowance for Gains (Losses)	Stockpile Materials, Net	Stockpile Materials, Net	Valuation Method
Stockpile Materials Categories					
Held for Sale	$ 857.2	$ 0.0	$ 857.2	$ 984.7	AC, LCM
Held in Reserve for Future Sale	29.3	0.0	29.3	94.1	AC, LCM
Total	$ 886.5	$ 0.0	$ 886.5	$ 1,078.8	
Legend for Valuation Methods: AC = Actual Cost LCM = Lower of Cost or Market					

Restrictions

Stockpile materiels held by the National Defense Stockpile (NDS) are restricted until relieved by congressional action and made available for sale on the open market. Stockpile materiels may not be disposed except for: (1) necessary upgrading, refining, or processing, (2) necessary rotation to prevent deterioration, (3) determination as excess with potential financial loss if retained, or (4) as authorized by law.

In 1994, the NDS voluntarily suspended mercury sales. The suspension was in response to concerns raised by the U.S. Environmental Protection Agency regarding the accumulation of mercury in the global environment.

The Requirements Report to Congress proposes additional restrictions on the use of beryllium metal, mica block, and quartz.

General Composition of Stockpile Materiels

The Department holds strategic and critical stockpile materiels due to statutory requirements for use in national defense, conservation, or national emergencies.

Before any materiels are sold, Congress must enact specific enabling legislation (e.g., the National Defense Authorization Act). When authorized to offer materiels for sale, NDS removes the materiels from Materiel Held in Reserve and reclassifies them as Materiels Held for Sale. The estimated market price of the stockpile materiels held for sale is $1.2 billion.

Note 10. General PP&E, Net

As of September 30	2007					2006
(amounts in millions)	Depreciation/ Amortization Method	Service Life	Acquisition Value	(Accumulated Depreciation/ Amortization)	Net Book Value	Prior FY Net Book Value
Land	N/A	N/A	$ 10,509.6	$ N/A	$ 10,509.6	$ 10,533.4
Buildings, Structure, and Facilities	S/L	20 or 40	173,311.1	(101,467.1)	71,844.0	69,455.2
Leasehold Improvements	S/L	Lease term	569.2	(340.8)	228.4	167.2
Software	S/L	2-5 or 10	9,313.8	(5,801.5)	3,512.3	3,391.0
General Equipment	S/L	5 or 10	71,015.8	(48,921.5)	22,094.3	16,718.1
Military Equipment	S/L	Various	657,100.3	(310,779.1)	346,321.2	344,945.0
Assets Under Capital Lease[1]	S/L	lease term	982.7	(501.4)	481.3	149.7
Construction-in-Progress	N/A	N/A	19,480.5	N/A	19,480.5	20,019.5
Other			60.3	(1.4)	58.9	60.4
Total General PP&E			$ 942,343.3	$ (467,812.8)	$ 474,530.5	$ 465,439.5
[1]Note 15 for additional information on Capital Leases						
Legend for Valuation Methods: S/L = Straight Line N/A = Not Applicable						

Military Equipment

In accordance with the Statement of Federal Financial Accounting Standards (SFFAS) No. 23, "Eliminating the Category National Defense Property, Plant, and Equipment," beginning in FY 2003, the Department capitalized military equipment into General Property, Plant, and Equipment (PP&E) at estimated historical cost using information obtained from the Bureau of Economic Analysis (BEA). During FY 2006, the Department replaced the BEA estimates with one based on departmental internal records for military equipment.

Heritage Assets and Stewardship Land

The Federal Accounting Standards Advisory Board, SFFAS No. 29, “Heritage Assets and Stewardship Land,” requires note disclosures for these types of assets. The Department’s policy is to preserve and account for its heritage assets’ historical, cultural, educational, or artistic importance. Additionally, the Department possesses and maintains land not acquired in connection with General PP&E, land donated to the Federal Government, and land previously recorded as public domain.

Heritage Assets within the Department consist of buildings and structures, archeological sites, museums, and monuments and memorials. Stewardship Land consists mainly of mission essential (donated, public domain, executive order) land. The Department, with minor exceptions, uses most of the buildings and structures as part of its everyday activities and includes them on the Balance Sheet as multi-use heritage assets (capitalized and depreciated).

Other Disclosures

The Department has the use of land, buildings, and other overseas facilities that are obtained through international treaties and agreements negotiated by the Department of State. The Department is restricted by treaty covenants regarding the use and disposal of real property (land and buildings) located outside the continental United States.

The Department does not have the acquisition value for all General PP&E and uses several cost methodologies to provide General PP&E values for financial statement reporting purposes.

Other primarily consists of assets awaiting disposal and the projected value of forest product sales.

Assets Under Capital Lease		
As of September 30	2007	2006
(amounts in millions)		
Entity as Lessee, Assets Under Capital Lease		
Land and Buildings	$ 719.5	$ 619.6
Equipment	263.2	8.2
Accumulated Amortization	(501.4)	(478.1)
Total Capital Leases	$ 481.3	$ 149.7

Note 11. Liabilities Not Covered by Budgetary Resources

As of September 30	2007	2006 Restated
(amounts in millions)		
Intragovernmental Liabilities		
Accounts Payable	$ 3.3	$ 1.0
Debt	1,850.0	1,842.3
Other	6,986.1	7,780.8
Total Intragovernmental Liabilities	8,839.4	9,624.1
Nonfederal Liabilities		
Accounts Payable	461.8	371.9
Military Retirement and Other Federal Employment Benefits	1,547,796.2	1,524,140.2
Environmental Liabilities	68,718.8	65,343.7
Other Liabilities	13,904.4	14,664.4
Total Nonfederal Liabilities	1,630,881.2	1,604,520.2
Total Liabilities Not Covered by Budgetary Resources	1,639,720.6	1,614,144.3
Total Liabilities Covered by Budgetary Resources	411,006.3	349,048.9
Total Liabilities	$ 2,050,726.9	$ 1,963,193.2

Liabilities Not Covered by Budgetary Resources represents liabilities for which congressional action is generally needed to provide resources. The Department expects to receive the necessary budgetary resources to cover these liabilities in future budget years.

Intragovernmental Accounts Payable and Nonfederal Accounts Payable represent liabilities in cancelled appropriations that, if paid, will be disbursed using funds current in the year of disbursement.

Debt consists primarily of borrowing from the U.S. Treasury for loans made to foreign governments.

Intragovernmental Liabilities Other is comprised of custodial liabilities for non-entity assets. The amounts collected cannot be used by the Department and must be returned to the U.S. Treasury. Intragovernmental Liabilities Other also includes unfunded Federal Employees Compensation Act liabilities that were not due during FY 2007.

Military Retirement and Other Federal Employment Benefits is comprised of employee actuarial liabilities not due and payable during the current fiscal year. These liabilities are primarily comprised of $813.5 billion in pension liabilities and $726.3 billion in health benefit liabilities. (Refer to Note 17, Military Retirement and Other Federal Employment Benefits, for additional details and disclosures.)

Nonfederal Liabilities Other is comprised of unfunded annual leave, contingent liabilities, and expected expenditures for disposal of conventional munitions.

Note 12. Accounts Payable

As of September 30	2007			2006 Restated
(amounts in millions)	Accounts Payable	Interest, Penalties, and Administrative Fees	Total	Total
Intragovernmental Payables	$ 1,911.5	$ N/A	$ 1,911.5	$ 1,549.8
Nonfederal Payables (to the Public)	29,671.7	2.3	29,674.0	27,388.4
Total	$ 31,583.2	$ 2.3	$ 31,585.5	$ 28,938.2

Accounts payable are amounts owed to federal and nonfederal entities for goods and services received by the Department that have not been paid. The Department's systems do not track intragovernmental transactions by customer at the transaction level. Therefore, buyer-side balances are adjusted to agree with seller-side balances for revenue, accounts receivable, and unearned revenue. Accounts payable were adjusted by reclassifying amounts between federal and nonfederal accounts payable.

Note 13. Debt

As of September 30	2007			2006 Restated	
(amounts in millions)	Beginning Balance	Net Borrowing	Ending Balance	Net Borrowing	Ending Balance
Agency Debt (Intragovernmental)					
Debt to the Treasury	$ 659.0	$ (170.5)	$ 488.5	$ 123.3	$ 659.0
Debt to the Federal Financing Bank	3,038.8	(285.0)	2,753.8	(208.3)	3,038.8
Total Agency Debt	3,697.8	(455.5)	3,242.3	(85.0)	3,697.8
Total Debt	$ 3,697.8	$ (455.5)	$ 3,242.3	$ (85.0)	$ 3,697.8

The Department's debt consists of interest and principal payments due to the U.S. Treasury and the Federal Financing Bank. The Department borrows funds for the Foreign Military Financing Program, the Washington Aqueduct Project, the U.S. Navy Afloat Prepositioning Force Program, the Military Housing Privatization Initiative, and the Armanment Retooling and Manufacturing Support.

The majority of the debt represents direct and guaranteed loans to foreign governments. Before 1992, funds were borrowed from the Federal Financing Bank to either directly loan the funds to foreign governments or to reimburse defaulted guaranteed loans. Beginning in 1992, the Department began borrowing funds for the Foreign Military Account Program from the U.S. Treasury, in accordance with the Federal Credit Reform Act of 1990, which governs all direct loan obligations and loan guarantee commitments made after FY 1991.

The Department must pay the debt on direct loans if borrowers (e.g. foreign governments, county or city governments, ship owners, or housing builders) default. For loan guarantees, the Department must pay the amount of outstanding principal guaranteed.

Note 14. Environmental and Disposal Liabilities

As of September 30	2007			2006
(amounts in millions)	Current Liability	Noncurrent Liability	Total	Total
Environmental Liabilities—Nonfederal				
Accrued Environmental Restoration Liabilities				
Active Installations—Installation Restoration Program (IRP) and Building Demolition and Debris Removal (BD/DR)	$ 1,179.5	$ 7,958.3	$ 9,137.8	$ 9,084.8
Active Installations—Military Munitions Response Program (MMRP)	130.2	5,274.5	5,404.7	5,396.5
Formerly Used Defense Sites—IRP and BD/DR	151.5	3,662.5	3,814.0	4,169.5
Formerly Used Defense Sites–MMRP	89.2	14,607.6	14,696.8	14,797.3
Other Accrued Environmental Liabilities—Active Installations				
Environmental Corrective Action	50.3	868.1	918.4	727.4
Environmental Closure Requirements	7.1	1,017.7	1,024.8	409.4
Environmental Response at Operational Ranges	35.1	174.5	209.6	305.0
Other	149.2	593.7	742.9	781.4
Base Realignment and Closure (BRAC)				
Installation Restoration Program	673.0	3,279.2	3,952.2	2,882.5
Military Munitions Response Program	35.6	993.1	1,028.7	913.2
Environmental Corrective Action / Closure Requirements	38.0	125.3	163.3	181.2
Other	0.0	0.0	0.0	149.2
Environmental Disposal for Weapons Systems Programs				
Nuclear Powered Aircraft Carriers	0.0	5,665.8	5,665.8	5,604.3
Nuclear Powered Submarines	484.0	3,202.4	3,686.4	3,377.7
Other Nuclear Powered Ships	226.9	66.5	293.4	277.2
Other National Defense Weapons Systems	0.8	204.3	205.1	233.8
Chemical Weapons Disposal Program	1,458.4	16,850.2	18,308.6	17,457.3
Other	0.0	3,237.4	3,237.4	3,237.4
Total Environmental Liabilities	$ 4,708.8	$ 67,781.1	$ 72,489.9	$ 69,985.1

Others Category Disclosure Comparative Table		
As of September 30	2007	2006
(amounts in millions)		
Other Accrued Environmental Liabilities—Active Installations—Other		
U.S. Army Corps of Engineers (USACE) remediation of the Formerly Utilized Sites Remedial Action Program (FUSRAP)	$ 622.4	$ 653.4
USACE environmental liabilities not related to FUSRAP	4.4	0.0
Army Low Level Radioactive Waste Program	46.4	35.8
National Defense Stockpile (NDS) Transaction Fund	27.8	52.2
Defense Commissary Agency—asbestos and/or lead-based paint	40.7	29.0
TRICARE Management Activity Uniformed Services University of Health Sciences—disposal liability for research laboratories	0.0	11.0
Under Secretary of Defense—Operations and Maintenance—Other Defense Organizations	0.2	0.0
Navy estimate for disposal of polychlorinated biphenyls transformers	1.0	0.0
Total	742.9	781.4
Base Realignment and Closure (BRAC)—Other		
Army unliquidated obligations associated with cleanup contracts at BRAC installations	0.0	149.2
Total	0.0	149.2
Environmental Disposal for Weapons Systems Program—Other		
Navy Spent Nuclear Fuel	3,237.4	3,237.4
Total	$ 3,237.4	$ 3,237.4

Other Accrued Environmental Liabilities, Active Installations, Other primarily consists of remediation related to FUSRAP. The USACE is responsible for FUSRAP, which remediates radiological contamination from the Department of Energy's U.S. Atomic Energy and Weapons Program.

Environmental Disposal for Weapons Systems Programs, Other represents spent nuclear fuel, which is used fuel removed from the nuclear reactors of nuclear-powered ships and submarines. The estimate includes shipping, processing, and storing spent nuclear fuel.

Environmental Disclosures		
As of September 30	2007	2006
(amounts in millions)		
A. The unrecognized portion of the estimated total cleanup costs associated with General Property, Plant, and Equipment.	$ 1,589.1	$ 1,527.4
B. Changes in total cleanup costs due to changes in laws, regulations, and/or technology.	(12.7)	(44.9)
C. Portion of the changes in estimated costs due to changes in laws and technology that is related to prior periods.	$ (4.4)	$ 0.0

Environmental Disclosures – Line A represents the unrecognized costs associated with General Property, Plant, and Equipment (PP&E). The unrecognized portion of the estimated total cleanup costs is primarily associated with Non-Defense Environmental Restoration Program (DERP), such as nuclear-powered carriers and submarines, conventional ships, spent nuclear fuel, and landfills. Not all components of the Department disclose the unrecognized portion of the estimated cleanup costs associated with General PP&E. The Department is implementing procedures to address this deficiency.

Environmental Disclosures – Line B represents the amount of changes in total cleanup costs due to changes in laws, regulations, and/or technology. Not all components of the Department disclose changes in total cleanup costs due to changes in laws, regulations, and/or technology. The Department is implementing procedures to address this deficiency.

Environmental Disclosures – Line C represents the portion of changes in estimated costs due to changes in laws and technology that is related to prior periods. Not all components of the Department disclose the amount of change in estimates for costs due to changes in laws and technology relating to prior periods. The Department is implementing procedures to address this deficiency.

Other Disclosures

Types of Environmental Liabilities and Disposal Liabilities Identified

The Department has cleanup requirements for DERP sites at active installations, BRAC installations, Formerly Used Defense Sites, sites at active installations that are not covered by DERP, weapons systems programs, and chemical weapons disposal programs. The weapons systems programs consists of chemical weapons disposal, nuclear powered aircraft carriers, nuclear powered submarines, and other nuclear ships. All cleanup is done in coordination with regulatory agencies, other responsible parties, and current property owners.

Applicable Laws and Regulations for Cleanup Requirements

The Department is required to clean up contamination resulting from past waste disposal practices, leaks, spills, and other past activity that created a public health or environmental risk. The Department accomplishes this effort in coordination with regulatory agencies and, if applicable, other responsible parties and current property owners. The Department is also required to recognize closure and post-closure costs for its General PP&E and environmental corrective action costs for current operations. Each of the Department's major reporting entities is responsible for tracking and reporting all required environmental information related to environmental restoration costs, other accrued environmental costs, disposal costs of weapons systems, and environmental costs related to BRAC actions that have taken place.

The Department follows the Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA) and the Superfund Amendment and Reauthorization Act to clean up DERP-eligible contamination. Contamination clean up that is not eligible for DERP is performed in accordance with the Resource Conservation and Recovery Act (RCRA) or other applicable federal or state laws. The CERCLA and RCRA require the Department to clean up contamination in coordination with regulatory agencies, current owners of property damaged by the Department, and third parties that have a partial responsibility for the environmental restoration. Failure to comply with agreements and legal mandates will put the Department at risk of incurring fines and penalties.

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

The Chemical Weapons Disposal Program is based on FY 1986 National Defense Authorization Act (PL 99-145, as amended by subsequent acts) that directed the Department to destroy the unitary chemical stockpile by April 29, 2004. The current guidelines for destruction are based on the Chemical Weapons Convention Treaty. The United States ratified the Treaty in April 1997, requiring the stockpile of chemical weapons to be destroyed by April 2007, according to the terms outlined. The Army, as Executive Agent within the Department, provides policy, direction, and oversight for both the Chemical Stockpile Program and the Nonstockpile Chemical Materiel Project. As such, the Army is responsible for the safe and economical disposal of the U.S. stockpile of lethal and incapacitating chemical warfare agents and munitions.

Methods for Assigning Total Cleanup Costs to Current Operating Periods

The Department uses engineering estimates and independently validates models to estimate environmental costs. The models are contained within the Remedial Action Cost Engineering Requirements and the Normalization of Data System. The Department validates the models in accordance with DoD Instruction 5000.61 and primarily uses the models to estimate the liabilities based on data received during a preliminary assessment and initial site investigation. The Department primarily uses engineering estimates after obtaining extensive data during the remedial investigation/feasibility phase of the environmental project.

Once the environmental cost estimates are complete, the Department complies with accounting standards to assign costs to current operating periods. The Department has already expensed the costs for cleanup associated with General PP&E placed into service prior to October 1, 1997, unless the costs are intended to be recovered through user charges. If the costs are recovered through user charges, then the Department expensed cleanup costs associated with that portion of the asset life that had passed since the General PP&E was placed into service, and is systematically recognizing the remaining cost over the remaining life of the asset.

For General PP&E placed into service after September 30, 1997, the Department expenses associated environmental costs systematically over the life of the asset using two methods: physical capacity for operating landfills, and life expectancy in years for all other assets. The Department expenses the full cost to clean up contamination for Stewardship PP&E at the time the asset is placed into service.

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

The Department had changes in estimates resulting from overlooked or previously unknown contaminants, reestimation based on different assumptions, and lessons learned. Environmental liabilities may change in the future due to changes in laws and regulation, changes in agreements with regulatory agencies, and advances in technology.

Uncertainty Regarding the Accounting Estimates Used to Calculate the Reported Environmental Liabilities

The environmental liabilities for the Department are based on accounting estimates, which require certain judgments and assumptions that are reasonable, based upon available information at the time the estimates are calculated. The actual results may materially vary from the accounting estimates if agreements with regulatory agencies require remediation to a different degree than anticipated when calculating the estimates. The liabilities can be further impacted if investigation of the environmental sites reveals contamination levels that differ from the estimate parameters.

The Army has a liability to take environmental restoration/corrective action for buried chemical munitions and agents, which they are unable to estimate at this time because the extent of the buried chemical munitions and agents is not known. The USACE is also unable to provide a complete estimate for the FUSRAP. The USACE has ongoing studies and will update its estimate as additional liabilities are identified. In addition, not all components of the Department recognize environmental liabilities associated with General PP&E due to process and system limitations.

The Department is in the process of determining the extent of the liabilities at installations that are realigning or closing as a result of recent BRAC requirements, in particular those liabilities associated with unexploded ordnance on training ranges. In addition, the Department has the potential to incur costs for restoration initiatives in conjunction with returning overseas Defense facilities to host nations. The Department is unable to provide a reasonable estimate at this time because the extent of required restoration is not known.

Note 15. Other Liabilities

As of September 30	2007			2006 Restated
(amounts in millions)	Current Liability	Noncurrent Liability	Total	Total
Intragovernmental				
Advances from Others	$ 308.9	$ 0.0	$ 308.9	$ 448.8
Deposit Funds and Suspense Account Liabilities	1,181.6	0.0	1,181.6	2,009.3
Disbursing Officer Cash	2,620.0	0.0	2,620.0	2,273.2
Judgment Fund Liabilities	167.5	0.0	167.5	164.2
FECA Reimbursement to the Department of Labor	601.8	785.8	1,387.6	1,404.7
Custodial Liabilities	3,718.2	1,518.3	5,236.5	5,960.0
Employer Contribution & Payroll Taxes Payable	281.8	0.0	281.8	290.5
Other Liabilities	317.1	0.0	317.1	649.0
Total Intragovernmental Other Liabilities	9,196.9	2,304.1	11,501.0	13,199.7
Nonfederal				
Accrued Funded Payroll and Benefits	6,197.3	0.0	6,197.3	4,497.8
Advances from Others	31,423.4	0.0	31,423.4	2,074.3
Deposit Funds and Suspense Accounts	59.9	0.0	59.9	205.6
Temporary Early Retirement Authority	0.0	0.0	0.0	0.1
Nonenvironmental Disposal Liabilities				
Military Equipment (Nonnuclear)	8.2	263.0	271.2	285.2
Excess/Obsolete Structures	76.0	587.0	663.0	685.6
Conventional Munitions Disposal	0.0	1,284.1	1,284.1	1,217.8
Accrued Unfunded Annual Leave	8,708.2	0.0	8,708.2	9,403.9
Capital Lease Liability	17.8	165.7	183.5	226.1
Contract Holdbacks	827.6	0.0	827.6	747.0
Employer Contribution & Payroll Taxes Payable	1,565.9	0.0	1,565.9	1,226.8
Contingent Liabilities	2,984.2	2,250.1	5,234.3	5,204.1
Other Liabilities	781.3	4.0	785.3	5,791.8
Total Nonfederal Other Liabilities	52,649.8	4,553.9	57,203.7	31,566.1
Total Other Liabilities	$ 61,846.7	$ 6,858.0	$ 68,704.7	$ 44,765.8

Intragovernmental Custodial Liabilities is primarily comprised of accounts receivable for cancelled appropriations and interest, penalties, fines, and administrative fees from the public. The Department generally cannot use the collections and must distribute them to the U.S. Treasury. The Department has specific statutory authority to retain collections from certain cancelled year accounts receivable as entity assets.

Intragovernmental Other Liabilities is primarily comprised of other unfunded employment related liabilities.

Contingent Liabilities includes $1.7 billion in estimated future contract financing payments. In accordance with contract terms, specific rights to the contractors' work vests with the Government when a specific type of contract financing payment is made. This action protects taxpayer funds in the event of contract nonperformance. These rights should not be misconstrued as rights of ownership. The Department is under no obligation to pay contractors for amounts greater than the amounts authorized in contracts until delivery and Government acceptance. Due to the probability the contractors will complete their efforts and deliver satisfactory products, and because the amount of potential future payments are estimable, the Department has recognized a contingent liability for estimated future payments which are conditional pending deliver and Government acceptance.

Nonfederal Other Liabilities consists primarily of estimated accruals for work in process by contractors in support of depot maintenance activities.

The balance in Nonfederal Other Liabilities includes $29.2 billion that the Department is executing on behalf of the Executive Office of the President. These amounts do not represent liabilities of the Department.

Capital Lease Liability					
As of September 30	2007 Asset Category				2006
(amounts in millions)	Land and Buildings	Equipment	Other	Total	Total
Future Payments Due					
2007	$ 0.0	$ 0.0	$ 0.0	$ 0.0	$ 63.0
2008	47.1	3.8	0.0	50.9	47.3
2009	43.9	1.5	0.0	45.4	43.9
2010	43.9	0.0	0.0	43.9	43.9
2011	41.3	0.0	0.0	41.3	36.8
2012	15.5	0.0	0.0	15.5	0.0
After 5 Years	28.6	0.0	0.0	28.6	52.1
Total Future Lease Payments Due	220.3	5.3	0.0	225.6	287.0
Less: Inputed Interest Executory Costs	42.0	0.1	0.0	42.1	60.9
Net Capital Lease Liability	$ 178.3	$ 5.2	$ 0.0	$ 183.5	$ 226.1
Capital Lease Liabilities Covered by Budgetary Resources				150.8	181.2
Capital Lease Liabilities Not Covered by Budgetary Resources				$ 32.7	$ 44.9

Note 16. Commitments and Contingencies

Legal Contingencies

The Department is a party in various administrative proceedings and legal actions related to claims for environmental damage, equal opportunity matters, and contractual bid protests. The Department has accrued contingent liabilities for legal actions where the Office of General Counsel (OGC) considers an adverse decision probable and the amount of loss measurable. In the event of an adverse judgment against the Government, some of the liabilities may be payable from the U.S. Treasury Judgment Fund. The Department records Judgment Fund liabilities in Note 12, "Accounts Payable," and Note 15, "Other Liabilities."

The OGC reported 63 legal actions with individual claims greater than the Department's FY 2007 materiality threshold of $110.5 million. The total of these 63 actions is approximately $1.6 trillion. Of this amount, the OGC determined that claims totaling approximately $15.4 billion are reasonably possible, $12.9 billion are remote, and $1.57 trillion unable to determine the probability of loss. The Department also had a number of potential claims that individually did not meet the Department's materiality threshold, but did meet the individual Components' thresholds. These claims are disclosed in the Components' financial statements.

Other Commitments and Contingencies

Undelivered orders for open (unfilled or unreconciled) contracts citing cancelled appropriations, for which the Department may incur a contractual commitment for payment, total $1.2 billion.

The Department is a party in numerous individual contracts that contain clauses, such as price escalation, award fee payments, or dispute resolution, that may result in a future outflow of funds if contract terms are satisfied. Currently, the Department has limited automated system processes by which it captures or assesses these potential contingent liabilities.

Note 17. Military Retirement and Other Federal Employment Benefits

As of September 30	2007				2006
(amounts in millions)	Present Value of Benefits	Assumed Interest Rate (%)	(Less: Assets Available to Pay Benefits)	Unfunded Liability	Present Value of Benefits
Pension and Health Actuarial Benefits					
Military Retirement Pensions	$ 1,025,320.6	6.0	$ (211,854.6)	$ 813,466.0	$ 963,696.1
Military Retirement Health Benefits	317,332.8	6.0	0.0	317,332.8	299,203.8
Military Medicare-Eligible Retiree Benefits	516,479.2	6.0	(107,454.2)	409,025.0	538,032.5
Total Pension and Health Actuarial Benefits	1,859,132.6		(319,308.8)	1,539,823.8	1,800,932.4
Other Actuarial Benefits					
FECA	6,830.1	5.2	0.0	6,830.1	6,856.0
Voluntary Separation Incentive Programs	1,250.5	4.0	(548.6)	701.9	1,391.2
Department Education Benefits Fund	1,858.2	5.0	(1,417.8)	440.4	1,785.3
Total Other Actuarial Benefits	9,938.8		(1,966.4)	7,972.4	10,032.5
Other Federal Employment Benefits	5,608.1		(5,608.1)	0.0	4,804.6
Total Military Retirement and Other Federal Employment Benefits	$ 1,874,679.5		$ (326,883.3)	$ 1,547,796.2	$ 1,815,769.5

Actuarial Cost Method Used: Aggregate entry-age normal method
Assumptions: See below
Market Value of Investments in Market-based and Marketable Securities: $324.8 billion

Military Retirement Pensions

The Military Retirement Fund (MRF) is a defined benefit plan authorized by Public Law (P.L.) 98-94 to provide funds used to pay annuities and pensions to retired military personnel and their survivors. The Board approves the long-term economic assumptions for inflation, salary, and interest. The actuaries calculate the actuarial liabilities annually using economic assumptions and actual experience (e.g., mortality and retirement rates). Due to reporting deadlines, the current year actuarial present value of projected plan benefits rolls forward from the prior year's valuation results. The Department used the following assumptions in calculating the FY 2007 roll-forward amount.

	Inflation	Salary	Interest
Fiscal Year 2007	3.3% (actual)	2.2% (actual)	6.0%
Fiscal Year 2008	2.3% (estimated)	3.5% (estimated)	6.0%
Long-Term	3.0%	3.75%	6.0%

Historically, the initial unfunded liability of the program was being amortized over a 50-year period. Effective FY 2008, the initial unfunded liability will be paid over a 42-year period to ensure the annual payments cover the interest on the unfunded actuarial liablity, with the last payment expected to be made October 1, 2025. All subsequent gains and losses experienced by the system are amortized over a 30-year period.

Change in MRF Actuarial Liability	(Amounts in billions)
Actuarial Liability as of 9/30/06	$963.7
Expected Normal Cost for FY 2007	17.7
Plan Amendment Liability	1.5
Assumption Change Liability	26.5
Expected Benefit Payments for FY 2007	(43.5)
Interest Cost for FY 2007	57.1
Actuarial (gains)/losses due to changes in trend assumptions	2.2
Actuarial Liability as of 09/30/07	$1,025.3
Change in Actuarial Liability	**$61.6**

Actuarial Cost Method Used: Aggregate entry-age normal method.
Market Value of Investments in Market-Based and Marketable Securities: $215.0 billion
Assumed Interest Rate: 6.0%

Military Retirement Health Benefits (MRHB)

The MRHB are post-retirement benefits the Department provides to non-Medicare-eligible military retirees and other eligible beneficiaries, through private sector health care providers and Department Medical Treatment Facilities. The Department used the following assumptions in calculating the FY 2007 actuarial liability.

Medical Trend	FY 2006 – FY 2007	Ultimate Rate FY 2031
Medicare Inpatient	6.74%	6.25%
Medicare Outpatient	6.54%	6.25%
Medicare Prescriptions (Direct Care)	6.25%	6.25%
Medicare Prescriptions (Purchased Care)	6.25%	6.25%
Non-Medicare Inpatient (Direct Care)	6.25%	6.25%
Non-Medicare Outpatient (Direct Care)	6.25%	6.25%
Non-Medicare Prescriptions (Direct Care)	6.25%	6.25%
Non-Medicare Inpatient (Purchased Care)	6.25%	6.25%
Non-Medicare Outpatient (Purchased Care)	9.48%	6.25%
Non-Medicare Prescriptions (Purchased Care)	9.84%	6.25%

Change in MRHB Actuarial Liability	(Amounts in billions)
Actuarial Liability as of 09/30/06 (Department preMedicare + all Uniformed services Medicare cost-basis effect)	$299.2
Expected Normal Cost for FY 2007	$10.0
Expected Benefit Payments for FY 2007	($10.4)
Interest Cost for FY 2007	$19.0
Actuarial (gains)/losses due to other factors	($11.9)
Actuarial (gains)/losses due to changes in trend assumptions	$11.9
Actuarial Liability as of 09/30/07 (Department preMedicare + all Uniformed Services Medicare cost-basis effect)	$317.3
Change in Actuarial Liability	**$18.1**

Actuarial Cost Method Used: Aggregate Entry-Age Normal Method
Assumed Interest Rate: 6.0%

Medicare-Eligible Retiree Health Care Fund (MERHCF) Benefits

In accordance with P.L. 106-398, the MERHCF accumulates funds to finance the health care program liabilities of Medicare-eligible retirees for all the Uniformed Services and specific Medicare-eligible beneficiaries. The Board approves the long-term assumptions for medical trends and interest. The actuaries calculate the actuarial liabilities annually using actual experience (e.g., mortality and retirement rates, direct care costs, purchased care). Due to reporting deadlines, the current year actuarial present value of projected plan benefits rolls forward from the prior year's results. The Department used the following assumptions in calculating the FY 2007 roll-forward amount.

Medical Trend	FY 2006 – FY 2007	Ultimate Rate FY 2031
Medicare Inpatient	6.74%	6.25%
Medicare Outpatient	6.54%	6.25%
Medicare Prescriptions (Direct Care)	6.25%	6.25%
Medicare Prescriptions (Purchased Care)	10.95%	6.25%

Changes in MERHCF Actuarial Liability	(Amounts in billions)
Actuarial Liability as of 09/30/06 (all Uniformed Services Medicare)	$538.0
Expected Normal Cost for FY 2007	10.8
Expected Benefit Payments for FY 2007	(8.5)
Interest Cost for FY 2007	34.0
Actuarial (gains)/losses due to other factors	(4.8)
Actuarial (gains)/losses due to changes in trend assumptions	(53.1)
Actuarial Liability as of 09/30/07 (all Uniformed Services Medicare)	$516.5
Change in Actuarial Liability	**($21.5)**

Actuarial Cost Method Used for MERHCF Liability: Aggregate Entry-Age Normal
Market Value of Investments in Market-Based and Marketable Securities: $107.8 billion
Assumed Interest Rate: 6.0%

The MERHCF liability includes Medicare liabilities for all Uniformed Services. The $516.5 billion liability includes $505.1 billion for the Department, $10.2 billion for the Coast Guard, $1.1 billion for the Public Health Service and $72.8 million for National Oceanic and Atmospheric Association (NOAA). The FY 2007 contributions from each of the services were: $11.2 billion by the Department, $278.7 million by the Coast Guard, $36.3 million by the Public Health Service, and $1.8 million by NOAA.

Federal Employees Compensation Act (FECA)

The Department of Labor (DOL) determines the liability for future workers' compensation benefits, which includes the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases, plus a component for incurred but not reported claims. The liability is determined annually using historical benefit payment patterns related to a specific incurred period to predict the final payment related to that period. Consistent with past practice, these projected annual benefit payments have been discounted to present value using the Office of Management and Budget's economic assumptions for 10-year U.S. Treasury notes and bonds. A 4.93% interest rate was assumed for year one and 5.08% was assumed for year two and thereafter.

The DOL calculates this liability using wage inflation factors (cost of living adjustments or COLA) and medical inflation factors (consumer price index medical or CPIM). The actual rates for these factors for charge back year (CBY) 2007 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 were as follows.

CBY	COLA	CPIM
2007	2.63%	3.74%
2008	2.90%	4.04%
2009	2.47%	4.00%
2010	2.37%	3.94%
2011+	2.30%	3.94%

The model's resulting projections were analyzed to ensure the estimates were reliable. The analysis was based on four tests: (1) a sensitivity analysis of the model of economic assumptions, (2) a comparison of the percentage change in the liability amount by agency to the percentage change in the actual incremental payments, (3) a comparison of the incremental paid losses (the medical component in particular) in CBY 2007 (by injury cohort) to the average pattern observed during the prior three charge back years, and (4) a comparison of the estimated liability per case in the 2007 projection to the average pattern for the projections for the most recent three years.

Voluntary Separation Incentive (VSI) Program

The P.L. 102-190 established the VSI program to reduce the number of military personnel on active duty. The VSI Board of Actuaries approved the assumed annual interest rate of 4.5% used to calculate the actuarial liability. Since the VSI program is no longer offered, the actuarial liability is expected to continue to decrease with benefit outlays and increase with interest cost. The liability is calculated annually at the present value of all remaining payments.

Market Value of Investments in Market-based and Marketable Securities: $573.1 million

DoD Education Benefits Fund (EBF)

The P.L. 98-525 established the EBF program to recruit and retain military members and aid in the readjustment of military members to civilian life. The EBF Board of Actuaries approved the assumed interest rate of 5% used to calculate the actuarial liability.

Market Value of Investments in Market-based and Marketable Securities: $1.4 billion

Other Federal Employment Benefits

Other Federal Employment Benefits primarily consists of accrued pensions and annuities and an estimated liability for Incurred But Not Reported medical claims not processed prior to fiscal year end.

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

Intragovernmental Costs and Exchange Revenue		
As of September 30	2007	2006 Restated
(amounts in millions)		
Intragovernmental Costs	$ 27,266.6	$ 31,990.6
Public Costs	640,871.8	602,553.4
Total Costs	668,138.4	634,544.0
Intragovernmental Earned Revenue	(20,465.9)	(24,327.1)
Public Earned Revenue	(25,220.5)	(24,168.6)
Total Earned Revenue	(45,686.4)	(48,495.7)
Net Cost of Operations	$ 622,452.0	$ 586,048.3

The Statement of Net Cost (SNC) represents the net cost of programs and organizations of the Federal Government supported by appropriations or other means. The intent of the SNC is to provide gross and net cost information related to the amount of output or outcome for a given program or organization administered by a responsible reporting entity. The Department's current processes and systems do not capture and report accumulated costs for major programs based upon the performance measures as required by the Government Performance and Results Act. The Department is in the process of reviewing available data and developing a cost reporting methodology as required by the Statement of Federal Financial Accounting Standard No. 4, "Managerial Cost Accounting Concepts and Standards for the Federal Government."

Intragovernmental costs and revenues represent transactions made between two reporting entities within the Federal Government. Public costs and revenues are exchange transactions made between the reporting entity and a nonfederal entity.

The Department's systems do not track intragovernmental transactions by customer at the transaction level. Buyer-side expenses are adjusted to agree with internal seller-side revenues. Expenses are generally adjusted by reclassifying amounts between federal and nonfederal expenses.

The SNC presents information based on budgetary obligation, disbursement, and collection transactions. Amounts are adjusted for accruals based on data from nonfinancial feeder systems for major items such as payroll expenses, accounts payable, and environmental liabilities. The General Fund data is generally derived from budgetary transactions (obligations, disbursements, and collections) from nonfinancial systems, and accruals made for major items. While Working Capital Funds generally record transactions on an accrual basis, the systems do not always capture actual costs in a timely manner.

The majority of the Department's accounting systems do not capture information relative to heritage assets separately and distinctly from normal operations. Where it was able to identify the cost of acquiring, constructing, improving, reconstructing or renovating heritage assets, the Department has identified $2.0 million for the fiscal year.

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

As of September 30	2007		2006 Restated	
(amounts in millions)	Cumulative Results of Operations	Unexpended Appropriations	Cumulative Results of Operations	Unexpended Appropriations
Prior Period Adjustments Increases (Decreases) to Net Position Beginning Balance				
Changes in Accounting Standards	$ (4,230.9)	$ 3,745.5	$ 0.0	$ 0.0
Errors and Omissions in Prior Year Accounting Reports	0.0	0.0	(8,034.3)	(0.5)
Total Prior Period Adjustments	(4,230.9)	3,745.5	(8,034.3)	(0.5)
Imputed Financing				
Civilian CSRS/FERS Retirement	1,429.4	0.0	1,553.8	0.0
Civilian Health	2,784.7	0.0	2,646.5	0.0
Civilian Life Insurance	8.4	0.0	26.1	0.0
Judgment Fund	198.8	0.0	183.2	0.0
Total Imputed Financing	$ 4,421.3	$ 0.0	$ 4,409.6	$ 0.0

The Department recognized a net prior period adjustment of ($485.4) million in FY 2007 and restated cumulative results of operations by ($4.2) billion and unexpended appropriations by $3.7 billion. The adjustment relates to a change in reporting parent/child allocation transfers, and is presented as a change in accounting principle. The change affects the Balance Sheet and the Statement of Changes in Net Position. Parent/child reporting is intended to consolidate the complete financial reporting of delegated activities and funds within the parent's financial statements for overall performance reporting. In accordance with Office of Management and Budget (OMB) Circular A-136, "Financial Reporting Requirements," the Department, as the parent agency, reports the financial activity carried out by the child agencies who received transfer appropriations from the Department. When the Department performs as the child, it does not report any information relating to transfer appropriations received from other agencies except for Treasury-Managed Trust funds and funds for which the Executive Office of the President (EOP) is the parent. The OMB Circular A-136 makes exceptions for these transfer appropriations. The Department includes transfer appropriations received from the EOP whereby the EOP is the parent. The EOP delegates authority to the Department for foreign military sales, and the Department reports the related activity in its financial statements on behalf of the EOP.

Contributions to the Office of Personnel Management (OPM) do not fully cover the Government's cost to provide benefits for employees covered by the Civil Service Retirement System, the Federal Employees' Retirement System, the Federal Employees' Health Benefits program, and the Federal Employees' Group Life Insurance program. An imputed cost is recognized as the difference between the Government's cost of providing these benefits to employees and the Department's contributions. The OPM provides cost factors for the computation of imputed financing costs, and these estimates are included in the Department's financial statements.

Other Financing Sources, Other consists primarily of adjustments to reconcile budgetary and proprietary trial balances. Due to financial system limitations, the Department adjusts for these unreconciled differences.

Unexpended Appropriations, Budgetary Financing Sources, Other Adjustments is comprised of rescissions, capital transfers, and canceling appropriations.

In the Statement of Changes in Net Position (SCNP), offsetting balances for intraDepartmental activity between Earmarked Funds and All Other Funds is reported on the same lines. The Eliminations column contains all appropriate elimination entries, which net to zero within each respective line, except for intraentity imputed financing costs.

Earmarked Cumulative Results of Operations ending balance on the SCNP does not agree with the Earmarked Cumulative Results reported on the Balance Sheet because the cumulative results on the Balance Sheet are presented net of eliminations.

Appropriations on the Statement of Budgetary Resources (SBR) exceed Appropriations Received on the SCNP by $104.1 billion. The SCNP recognizes appropriations received by the Military Departments and Defense Agencies totaling $70.4 billion which are additionally recognized on the SBR as appropriated receipts in trust and special funds. Investments in trust and special funds accumulate interest earnings; the interest earnings comprise most of the remaining difference of $33.7 billion, which is recognized only on the SBR.

Note 20. Disclosures Related to the Statement of Budgetary Resources

As of September 30	2007	2006 Restated
(amounts in millions)		
Net Amount Budgetary Resources Obligated for Undelivered Orders at the End of the Period	$ 350,761.4	$ 297,272.1
Available Borrowing and Contract Authority at the End of the Period	$ 0.0	$ 29,488.9

Reconciliation Differences

The Department modified this note to more accurately report the remaining available balance of borrowing and contract authority. Previously, the Department reported the amount of borrowing and contract authority used, but not the amount replaced by reimbursement or appropriation.

Appropriations Received on the Statement of Budgetary Resources (SBR) exceed Appropriations Received on the Statement of Changes in Net Position by $104.1 billion. In accordance with Office of Management and Budget (OMB) guidance, appropriations received by the Military Departments and Defense Agencies totaling $70.4 billion are subsequently recognized a second time on the SBR as appropriations transferred into trust and special funds. Actual and anticipated earnings in trust and special funds comprise the balance of the difference.

Permanent Indefinite Appropriations

The Department of Defense (DoD) received the following permanent indefinite appropriations:

- Department of the Army General Gift Fund (10 USC 2601(b)(1))
- Department of the Navy General Gift Fund (10 USC 2601(b)(2))
- Department of the Air Force General Gift Fund (10 USC 2601(b)(3))

- Foreign National Employees Separation Pay Account, Defense (10 USC 1581)
- United States Naval Academy Gift and Museum Fund (10 USC 6973-4)
- Ship Stores Profits, Navy (10 USC 7220, 31 USC 1321)
- Midshipmen's Store (10 USC 6971B)
- Burdensharing Contributions Account (10 USC 2350(j))
- Forest Program (10 USC 2665)
- Department of Defense Base Closure Account (10 USC 2687)
- Medicare Eligible Retiree Health Care Fund (MERHCF) (10 USC 1111)
- Military Retirement Fund (MRF) (10 USC 1461)
- Education Benefits Fund (10 USC 2006)
- Reserve Mobilization Income Insurance Fund (10 USC 12528)
- Host Nation Support for U.S. Relocation Activities (10 USC 2350(k))
- National Defense Sealift Fund (10 USC 2218)
- Environmental Restoration, Navy (10 USC 2702)
- Hydraulic Mining Debris Reservoir (33 USC 683)
- Maintenance and Operation of Dams and Other Improvements of Navigable Waters (16 USC 810(a))
- Payments to States (33 USC 701c-3)
- Wildlife Conservation (16 USC 670-670(f))
- Ainsworth Bequest (31 USC 1321)
- Department of Defense Family Housing Improvement Fund (10 USC 2883 (a))
- Department of Defense Military Unaccompanied Housing Improvement Fund (10 USC 2883 (a))

The above permanent indefinite appropriations cover a wide variety of purposes to help the Department accomplish its missions. These purposes include: (1) military retirees health care benefits, retirement and survivor pay, and education benefits for veterans; (2) environmental, coastal, and wildlife habitat restoration, and water resources maintenance; (3) costs associated with the closure or realignment of military installations; (4) relocation of armed forces to a host nation; (5) separation payments for foreign nationals; (6) the construction, purchase, alteration, and conversion of sealift vessels; and (7) upkeep of libraries and museums. (See Note 23 for additional information on earmarked funds.)

In addition to the above, the Executive Office of the President has given the Department authority to execute the funds listed below on its behalf:

- Special Defense Acquisition Fund (22 USC 2795)
- Foreign Military Loans Liquidating Account (22 USC 2764)
- Foreign Military Financing, Direct Loan Financing Account (2 USC 661 (d))
- Military Debt Reduction Financing Account (2 USC 661 (d))
- Advances, Foreign Military Sales (22 USC 2761-2762)

Apportionment Categories for Obligations

The Department reported the following amounts of direct obligations: (1) $516.3 billion in category A; (2) $159.9 billion in category B; and (3) $96.7 billion in exempt from apportionment. The Department reported the following amounts of reimbursable obligations: (1) $93.0 billion in category A; (2) $77.9 billion in category B; and (3) $14.0 million in exempt from apportionment. Category A relates to appropriations for a specific period of time (e.g., Military Personnel appropriation), and category B relates to appropriations for a specific project (e.g., Military Construction appropriation).

Other Disclosures

The President's budget for FY 2009 has not yet been published. The budget is expected to be published on February 4, 2008, and will be available at: http://www.defenselink.mil/comptroller/defbudget.

The SBR includes intraentity transactions because the statements are presented as combined.

The Department utilizes borrowing authority for the Military Housing Privatization Initiative, the Armament Retooling and Manufacturing Support Initiative, and the Foreign Military Account Program. Borrowing authority is used in accordance with OMB Circular A-129, "Managing Federal Credit Programs."

The Department operates within the constraints of fiscal law and has no additional legal arrangements affecting the use of unobligated balances.

The Department received additional funding of $70.0 billion to replenish expenses incurred outside of normal operating expenses. The Department also received an additional $99.4 billion primarily for U.S. Troop Readiness, Veterans Care, and Hurricane Katrina recovery.

The Department reported a change in obligated balances brought forward of $29.2 billion, and unobligated balances brought forward of $1.0 billion, due to stipulations of OMB Circular A-136, "Financial Reporting Requirements." (See Note 1, "Significant Accounting Policies", and Note 25, "Restatements" for details.)

The Department is executing balances of Contract Authority of $48.0 billion, Permanently not Available of ($16.6) billion, and Distributed Offsetting Receipts of $15.8 billion, on behalf of the Executive Office of the President. These amounts do not represent budgetary resources or obligations of the Department.

Note 21. Reconciliation of Net Cost of Operations to Budget

As of September 30	2007	2006 Restated
(amounts in millions)		
Resources Used to Finance Activities:		
Budgetary Resources Obligated:		
Obligations Incurred	$ 943,782.3	$ 816,752.4
Less: Spending Authority from Offsetting Collections and Recoveries (-)	(215,593.3)	(197,235.2)
Obligations Net of Offsetting Collections and Recoveries	728,189.0	619,517.2
Less: Offsetting Receipts (-)	(64,105.0)	(48,222.1)
Net Obligations	664,084.0	571,295.1
Other Resources:		
Donations and Forfeitures of Property	13.8	47.3
Transfers in/out Without Reimbursement (+/-)	(86.9)	(83.7)
Inputed Financing from Costs Absorbed by Others	4,421.3	4,409.6
Other (+/-)	(8,099.3)	3,415.9
Net Other Resources Used to Finance Activities	(3,751.1)	7,789.1
Total Resources Used to Finance Activities	660,332.9	579,084.2
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 (-)	(82,882.9)	(19,138.7)
Unfilled Customer Orders	6,496.4	446.2
Resources that Fund Expenses Recognized in Prior Periods (-)	(34,595.5)	(6,392.3)
Budgetary Offsetting Collections and Receipts that do not Affect Net Cost of Operations	18,663.2	6,202.7
Resources that Finance the Acquisition of Assets (-)	(92,704.7)	(132,348.5)
Other Resources or Adjustments to Net Obligated Resources that do not Affect Net Cost Of Operations:		
Less: Trust or Special Fund Receipts Related to Exchange in the Entity's Budget (-)	(10.0)	(10.0)
Other (+/-)	$ 8,172.3	$ (3,379.2)

Total resources used to finance items not part of the Net Cost of Operations	$ (176,861.2)	$ (154,619.8)
Total resources used to finance the Net Cost of Operations	483,471.7	424,464.4
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 Period:		
Increase in Annual Leave Liability	1,866.1	7,401.2
Increase in Environmental and Disposal Liability	2,615.0	5,632.5
Upward/Downward Reestimates of Credit Subsidy Expense (+/-)	(103.6)	(35.6)
Increase in Exchange Revenue Receivable from the Public (-)	(23.3)	(47.7)
Other (+/-)	91,873.1	73,776.0
Total Components of Net Cost of Operations that Will Require or Generate Resources in Future Periods	96,227.3	86,726.4
Components not Requiring or Generating Resources:		
Depreciation and Amortization	27,287.0	65,116.2
Revaluation of Assets or Liabilities (+/-)	6,073.3	5,174.4
Other (+/-)		
Trust Fund Exchange Revenue	(39,246.6)	(40,583.4)
Cost of Goods Sold	56,125.0	47,718.4
Operating Material and Supplies Used	30,590.5	10,062.5
Other	(38,076.2)	(12,630.6)
Total Components of Net Cost of Operations that will not Require or Generate Resources	42,753.0	74,857.5
Total Components of Net Cost of Operations that will not Require or Generate Resources in the current period	138,980.3	161,583.9
Net Cost of Operations	$ 622,452.0	$ 586,048.3

Beginning 4th Quarter, FY 2007, the Department began presenting the Statement of Financing (SOF) as a note in accordance with OMB Circular A-136. The SOF is no longer considered a basic statement and is now referred to as Reconciliation of Net Cost of Operations to Budget. The reconciliation of the former SOF is now incorporated into Note 21.

Due to the Department's financial system limitations, budgetary data is not in agreement with proprietary expenses and capitalized assets. The difference between budgetary and proprietary data is a previously identified deficiency. The following adjustments (absolute value) were made to balance the Reconciliation of Net Cost of Operations to the Statement of Net Cost (amounts in millions):

Resources That Finance the Acquisition of Assets	$1,862.0
Other - Other Components Not Requiring or Generating Resources	55.5
Revaluation of Assets or Liabilities	14.3
Total Amount	$1,931.8

The following Reconciliation of Net Cost of Operations to Budget lines are presented as combined instead of consolidated due to intra-agency budgetary transactions not being eliminated:

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

Other Resources – Other and Other Resources or Adjustments to Net Obligated Resources that Do Not Affect Net Cost of Operations – Other primarily consists of nonexchange gains and losses necessary to reconcile the proprietary and budgetary accounts.

Components Requiring or Generating Resources in Future Period - Other primarily consists of future funded expenses for the current year change in actuarial liabilities.

Components not Requiring or Generating Resources - Other primarily consists of other expenses not requiring budgetary resources, cost capitalization offsets, and applied overhead.

Liabilities not covered by budgetary resources on the Balance Sheet total $1.6 trillion. The amount reported as Components Requiring or Generating Resources in Future Periods in Note 21, the Reconciliation of Net Cost of Operations to Budget, totals $96.2 billion. The difference of $1.5 trillion is primarily due to the differing perspectives between the two reports. Liabilities not covered by budgetary resources report the cumulative balance for Balance Sheet liabilities not yet funded whereas as Components Requiring or Generating Resources in Future Periods in Note 21 reflects only the current period changes for all unfunded liabilities.

Note 22. Disclosures Related to Incidental Custodial Collections

Incidental custodial collections represent miscellaneous receipts, such as collections of fines and penalties, which are deposited directly into the General Fund of the U.S. Treasury. These funds are not available for use by the Department. At the end of each fiscal year the accounts are closed and the balances absorbed by the U.S. Treasury. The Department collected and distributed to the U.S. Treasury $92.4 million of incidental custodial revenues generated primarily from the collection of fines and penalties.

Note 23. Earmarked Funds

BALANCE SHEET As of September 30, 2007 (amounts in millions)	Military Retirement Fund	Medicare Eligible Retiree Health Care Fund	Other Earmarked Funds	Eliminations	Total
ASSETS					
Fund balance with Treasury	$ 20.4	$ 5.0	$ 1,961.4	$ 0.0	$ 1,986.8
Investments	218,085.0	109,549.1	6,075.9	0.0	333,710.0
Accounts and Interest Receivable	143.1	10.3	515.2	(151.8)	516.8
Other Assets	0.0	0.0	2,215.7	0.0	2,215.7
Total Assets	$ 218,248.5	$ 109,564.4	$ 10,768.2	$ (151.8)	$ 338,429.3
LIABILITIES and NET POSITION					
Military Retirement Benefits and Other Federal Employment Benefits	$ 1,028,850.7	$ 517,104.6	$ 3,108.7	$ 0.0	$ 1,549,064.0
Other Liabilities	1.0	256.6	1,072.6	(133.8)	1,196.4
Total Liabilities	1,028,851.7	517,361.2	4,181.3	(133.8)	1,550,260.4
Unexpended Appropriations	0.0	0.0	8.1	0.0	8.1
Cumulative Results of Operations	(810,603.2)	(407,796.8)	6,578.8	(68,286.0)	(1,280,107.2)
Total Liabilities and Net Position	$ 218,248.5	$ 109,564.4	$ 10,768.2	$ (68,419.8)	$ 270,161.3

BALANCE SHEET As of September 30, 2007 (amounts in millions)	Military Retirement Fund	Medicare Eligible Retiree Health Care Fund	Other Earmarked Funds	Eliminations	Total
STATEMENT OF NET COST For the Year Ended September 30, 2007					
Program Costs	$ 105,253.0	$ (13,945.8)	$ 3,242.8	$ (2,542.8)	$ 92,007.2
Less Earned Revenue	(53,311.2)	(31,539.3)	(1,082.0)	70,427.7	(15,504.8)
Net Program Costs	51,941.8	(45,485.1)	2,160.8	67,884.9	76,502.4
Net Cost of Operations	$ 51,941.8	$ (45,485.1)	$ 2,160.8	$ 67,884.9	$ 76,502.4
STATEMENT OF CHANGES IN NET POSITION For the period ended September 30, 2007					
Net Position Beginning of the Period	$ (758,661.4)	$ (453,467.9)	$ 5,371.4	$ 0.0	$ (1,206,757.9)
Net Cost of Operations	51,941.8	(45,485.1)	2,160.8	67,884.9	76,502.4
Budgetary Financing Sources	0.0	186.0	3,154.8	(414.2)	2,926.6
Other Financing Sources	0.0	0.0	221.5	13.1	234.6
Change in Net Position	(51,941.8)	45,671.1	1,215.5	(68,286.0)	(73,341.2)
Net Position End of Period	$ (810,603.2)	$ (407,796.8)	$ 6,586.9	$ (68,286.0)	$ (1,280,099.1)

Other Disclosures

The Statement of Federal Financial Accounting Standards (SFFAS) No. 27, "Identifying and Reporting Earmarked Funds," requires the disclosure of Earmarked Funds separately from All Other Funds on the Statement of Changes in Net Position and Balance Sheet. Funds must meet three criteria to be classified as earmarked: (1) a statute committing use of specifically identified revenues for designated purposes, (2) explicit authority to retain the revenues, and (3) a requirement to account and report on the revenues. The Department's earmarked funds are either special or trust funds and use both receipt and expenditure accounts to report activity to the U.S. Treasury. There have been no changes in legislation during or subsequent to this reporting period that significantly changed the purposes of any of the following funds.

The Total column is shown as consolidated and relates only to Earmarked Funds. The Eliminations column includes eliminations associated with Earmarked Funds and excludes the offsetting eliminations from All Other Funds. This exclusion causes assets to not equal liabilities and net position in the note. However, the amounts in the Total column equal the amounts reported for Earmarked Funds on the Balance Sheet. The SFFAS No. 27 requires the presentation of gross amounts of Earmarked Funds separate from All Other (nonearmarked) Funds. Cumulative Results of Operations ending balances for Earmarked Funds on the Statement of Changes in Net Position do not agree with the Cumulative Results of Operations for Earmarked Funds reported on the Balance Sheet because the Cumulative Results of Operations on the Balance Sheet are presented net of eliminations. The summation for Military Retirement Fund (MRF), Medicare-Eligible Retiree Health Care Fund (MERHCF), and Other Earmarked Funds is equivalent to the gross amount presented on the Statement of Changes in Net Position.

Military Retirement Fund, 10 United States Code (USC) 1461. The MRF accumulates funds in order to finance, on an actuarially sound basis, the liabilities of the Department's military retirement and survivor benefit programs. Financing sources for the MRF are interest earnings on Fund assets, monthly Department contributions, and annual contributions from the U.S. Treasury. The monthly Department contributions are calculated as a percentage of basic pay. The contribution from the U.S. Treasury represents the amortization of the unfunded liability for service performed prior to October 1, 1984, plus the amortization of actuarial gains and losses that have arisen since then. The U.S. Treasury annual contribution also includes the normal cost amount for the concurrent receipt provisions of the FY 2004 National Defense Authorization Act.

Medicare-Eligible Retiree Health Care Fund, 10 USC 1111. The MERHCF accumulates funds to finance, on an actuarially sound basis, liabilities of the Department and the uniformed services health care programs for qualified Medicare-eligible beneficiaries. Financing sources for MERHCF are provided primarily through an annual actuarial liability payment from the U.S. Treasury, annual contributions from the Military Services and other Uniformed Services (the U.S. Coast Guard, the

National Oceanic and Atmospheric Administration, and the U.S. Public Health Service), and interest earned from the Fund's investments.

Other Earmarked Funds

Special Recreation Use Fees, 16 USC 4061-6a note. The United States Army Corps of Engineers (USACE) is granted the authority to charge and collect fair and equitable Special Recreation Use Fees at campgrounds located at lakes or reservoirs that are under the jurisdiction of the USACE. Types of allowable fees include daily use fees, admission fees, recreational fees, annual pass fees, and other permit type fees. The receipts are used for the operation and maintenance of the recreational sites.

Hydraulic Mining in California, Debris, 33 USC 683. Operators of hydraulic mines through which debris flows in part or in whole to a body restrained by a dam or other work erected by the California Debris Commission are required to pay an annual tax as determined by the Commission. Taxes imposed under this code are collected and then expended under the supervision of the USACE and the direction of the Department of the Army. The funds are used for repayment of funds advanced by the federal government or other agency for construction, restraining works, settling reservoirs, and maintenance.

Payments to States, Flood Control Act of 1954, 33 USC 701c-3. Seventy-five percent of all funds received and deposited from the leasing of lands acquired by the United States for flood control, navigation, and allied purposes (including the development of hydroelectric power) are returned to the state in which the property is located. The USACE collects lease receipts into a receipt account. Funds are appropriated for the amount of receipts the following fiscal year. The funds may be expended by the states for the benefit of public schools and public roads of the counties in which such property is situated, or for defraying any of the expenses of county government.

Maintenance and Operation of Dams and Other Improvements of Navigable Waters, 16 USC 803(f) and 810. The USC states, "All proceeds from any Indian reservation shall be placed to the credit of the Indians of such reservation." However, the USC also states, "…all other charges arising from licenses…" except those charges established by the Federal Power Commission, now known as the Federal Energy Regulatory Commission, for purpose of administrative reimbursement shall be paid to the U.S. Treasury from which specific allocations will be made. From the specific allocations, 50% of charges from "all other licenses" is reserved and appropriated as a special fund in the U.S. Treasury to be expended under the direction of the Secretary of the Army in the maintenance, operation, and improvement of dams and other navigation structures that are owned by the United States or in construction, maintenance, or operation of headwater or other improvements of navigable waters of the United States.

Fund for Non-Federal Use of Disposal Facilities (for dredged material), 33 USC 2326. Any dredged material disposal facility under the jurisdiction of, or managed by, the Secretary of the Army (Secretary) may be used by a nonfederal interest if the Secretary determines that such use will not reduce the availability of the facility for project purposes. Fees may be imposed to recover capital, operation, and maintenance costs associated with such use. Any monies received through collection of fees under this law shall be available to, and used by, the Secretary for the operation and maintenance of the disposal facility from which the fees were collected.

South Dakota Terrestrial Wildlife Habitat Restoration Trust Fund, Public Law 106-53 Sec. 603. Yearly transfers are made from the General Fund of the U.S. Treasury to the Trust Fund for investment purposes. Investment activity is managed by the Bureau of the Public Debt (BPD). The BPD purchases and redeems nonmarketable market-based securities. Investments include one-day certificates, bonds, and notes. When the fund reaches the aggregate amount of $108 million, withdrawals may be made by the USACE for payment to the State of South Dakota. The state uses the payments to fund the annually scheduled work for wildlife habitat restoration.

Coastal Wetlands Restoration Trust Fund and Coastal Wetlands Planning, Protection and Restoration Act, 16 USC 3951-3956. The USACE, (along with the Environmental Protection Agency, and the Fish and Wildlife Service) is granted the authority to work with the State of Louisiana to develop, review, evaluate, and approve a plan to achieve a goal of "no net loss of wetlands" in coastal Louisiana. The USACE is also responsible for allocating funds among the named task force members. Federal contributions are established at 75% of project costs or 85% if the State has an approved Coastal Wetlands Conservation Plan.

Rivers and Harbors Contributed and Advance Funds, 33 USC 701h, 702f, and 703. Whenever any state or political subdivision offers to advance funds for a flood control project duly adopted and authorized by law the Secretary of the Army may, in his discretion, receive such funds and expend them in the immediate prosecution of such work. The funding may be used to construct, improve, and maintain levees, water outlets, flood control, debris removal, rectification, and enlargement of river channels, etc. in the course of flood control and river/harbor maintenance.

Inland Waterways Trust Fund, 26 USC 9506. This law made the Inland Waterways Trust Fund available for USACE expenditures for navigation, construction, and rehabilitation projects on inland waterways. Collections for excise taxes from the public are made into the Trust Fund. The collections are invested and investment activity is managed by the BPD. The BPD purchases and redeems nonmarketable market-based securities. Investments include one-day certificates, bonds, and notes.

Harbor Maintenance Trust Fund, 26 USC 9505. The USACE Civil Works mission is funded by the Energy and Water Developments Appropriations Act. The Water Resources Development Act of 1986 was implemented to cover a portion of USACE operations and maintenance costs for deep draft navigation. The Harbor Maintenance Trust Fund is available for making expenditures to carry out the functions specified in the act and for the payment of all expenses of administration incurred by the U.S. Treasury, USACE, and the Department of Commerce. Collections are made into the Trust Fund from taxes collected from imports, domestics, passengers, and foreign trade. The collections are invested and investment activity is managed by the BPD.

Foreign National Employees Separation Pay Account Trust Fund, 10 USC 1581. This fund makes payments from amounts obligated by the Secretary of Defense that remain unexpended for separation pay for foreign national employees of the Department. The foreign national employees' separation pay funded by Foreign Military Sales administrative funds is maintained as a separate fund.

Defense Commissary Agency Surcharge Trust Fund, 10 USC 2685. This fund was established as the repository for the surcharge on sales of commissary goods paid for by authorized patrons to finance certain operating expenses and capital purchases of the Commissary System, which are precluded by law from being paid with appropriated funds. Most Surcharge revenue is generated by the 5% surcharge applied to each sale. These funds may be used to pay for commissary store-related information technology investments, to purchase commissary equipment, to finance advance design modifications to prior year projects, for both minor and major construction projects, and to maintain and repair commissary facilities and equipment.

Education Benefit Fund, 10 USC 2006. This fund was established to finance, on an actuarially sound basis, the liabilities of the Department's education benefit programs for current and former active duty, guard, and reserve members of the armed forces, and members of the Coast Guard. Financing sources for the Education Benefit Fund are interest earnings on Fund assets and monthly Department contributions.

Voluntary Separation Incentive Fund, 10 USC 1175. This fund was established to finance, on an actuarially sound basis, the liabilities of the Department's incentive program for early separation from military service. Financing sources for the Voluntary Separation Incentive Fund are interest earnings on Fund assets and annual Department contributions.

Military Housing Privatization Initiative, Public Law 104-106, Statute 186, Section 2801. The Military Housing Privatization Initiative (MHPI) includes both direct loan and loan guarantee programs, is authorized by the National Defense Authorization Act for FY 1996, and includes a series of authorities that allow the Department to work with the private sector to renovate and build military family housing. The MHPI accelerates the construction of new housing, builds to market standards, and leverages private sector capital with government dollars. The Department provides protection to the private sector partner against specific risks, such as base closure or member deployment.

Armament Retooling and Manufacturing Support Initiative, 10 USC 4551-4555. The Armament Retooling and Manufacturing Support Initiative is a loan guarantee program designed to incentivize commercial use of the Army's inactive ammunition plants for businesses willing to locate to a government ammunition production facility. The production capacity of these facilities is greater than current military requirements, however, this capacity may be needed in the future. Revenues from property rental are used to pay for the operation, maintenance and environmental cleanup at the facilities.

Note 24. Other Disclosures

As of September 30	2007 Asset Category							
(amounts in millions)	Land and Buildings		Equipment		Other		Total	
Entity as Lessee—Operating Leases								
Future Payments Due								
Fiscal Year								
FY 2008	$	384.1	$	15.7	$	113.2	$	513.0
FY 2009		366.2		15.1		117.7		499.0
FY 2010		317.7		15.1		122.4		455.2
FY 2011		299.1		15.2		127.3		441.6
FY 2012		279.5		15.2		132.4		427.1
After 5 years		530.2		1.2		137.7		669.1
Total Future Lease Payments Due	$	2,176.8	$	77.5	$	750.7	$	3,005.0

Note 25. Restatements

During the reporting period, material errors were identified or accounting principle changes deemed necessary. As a result, prior year changes have been made retrospectively in accordance with generally accepted accounting principles (GAAP).

Correction Due to Change in Allocation Transfer Reporting

Effective FY 2007, the Office of Management and Budget (OMB) Circular A-136 “Financial Reporting Requirements” changed the reporting of allocation transfers. Due to this change, the Department reports in its basic financial statements the programs it administers on behalf of the Executive Office of the President (EOP) including the Foreign Military Sales (FMS) Program. Previously, the Department recorded the majority of FMS programs as “Other Accompanying Information,” rather than as part of the basic financial statements. The FMS Trust Fund was not part of this change, as it was formerly included in the Department’s financial statements.

Per OMB Circular A-136 Section I.14.2, the cumulative effect of the change on prior periods should be reported as a change in accounting principle, consistent with Statement of Federal Financial Accounting Standards No. 21, “Reporting Corrections of Errors and Changes in Accounting Principles.” Although this is not considered an error, due to the material and pervasive impact, the Department, in coordination with OMB and the U.S. Treasury, restated prior year comparative columns as outlined below:

FY 2006 Balance Sheet
(amounts in billions)

Fund Balance with Treasury	$1.9
Loans Receivable	3.7
Total Assets	$5.6
Debt	$3.3
Other Liabilities	0.4
Total Liabilities	$3.7
Net Position	$1.9

FY 2006 Statement of Net Cost
(amounts in billions)

Gross Costs	$4.8
Less: Earned Revenue	(0.2)
Net Cost of Operations	$4.6

Statement of Budgetary Resources
(amounts in billions)

Beginning Balance Change for FY 2007:	
Unobligated Balance, Brought Forward	($1.0)
Obligated Balance, Brought Forward	$29.2
Comparative Year Effect for FY 2006:	
Appropriation	$4.7
Spending Authority from Offsetting Collections	
Earned	
Collected	1.1
Permanently Not Available	(1.1)
Total Budgetary Resources	$4.7
Obligations	$4.7
Total Status of Budgetary Resources	$4.7
Gross Outlays	$5.2
Less: Offsetting Collections	(1.1)
Distributed Offsetting Receipts	13.8
Net Outlays	$17.9

Beginning balances were changed to accommodate the proper reporting of the EOP balances in the Department's Statement of Budgetary Resources. The Unobligated Balance, Brought Forward decrease of $1.0 billion was the result of a decrease of $1.4 billion for FMS offset by an increase of $385.2 million in the Army General Fund Iraqi Reconstruction Fund. The Obligated Balance, Brought Forward increase of $29.2 billion included an increase from FMS of $25.9 billion and an increase of $3.5 billion in the Iraqi Reconstruction Fund. The amounts reported as Comparative Year Effect were restatements of prior years.

Correction of Error

Following the current reporting period, the Department discovered an error in the computation of the Distributed Offsetting Receipts reported on the Statement of Budgetary Resources. The Department previously included all of the annual contribution from Treasury for the Military Retirement Fund and should have excluded the concurrent receipts of the normal cost contribution as Distributed Offsetting Receipts. The Department had also included the Military Departments' contributions, the non-DoD employing agency contributions, and the interest receivable for the DoD Medicare-Eligible Retiree Health Care Fund as Distributed Offsetting Receipts. The Department confirmed with OMB and the U.S. Treasury that only specific receipt accounts, and no accrued interest, should be reported as Distributed Offsetting Receipts. Due to the size of the misstatement in FY 2006, the Department restated lines on the Statement of Budgetary Resources and Note 21, "Reconciliation of Net Cost of Operations to Budget," formerly the Statement of Financing. The restatement has no impact on the Department's overall net position. The Department restated the prior year comparative column decreasing Distributed Offsetting Receipts by $13.8 billion in the Statement of Budgetary Resources. The Reconciliation of Net Cost of Operations to Budget was adjusted by like amount in the Distributed Offsetting Receipts and Trust Fund Exchange Revenue lines, resulting in no change in Net Cost of Operations.