

Department of Defense
Department of the Air Force
CONSOLIDATED BALANCE SHEET
As of March 31, 2005 and 2004

| | 2005 Consolidated | 2004 Consolidated |
|--|-------------------------------------|-------------------------------------|
| 1. ASSETS (Note 2) | | |
| A. Intragovernmental: | | |
| 1. Fund Balance with Treasury (Note 3) | | |
| a. Entity | \$ 116,208,310,084.02 | \$ 122,062,266,107.45 |
| b. Non-Entity Seized Iraqi Cash | 0.00 | 0.00 |
| c. Non-Entity-Other | 136,034,520.60 | 432,403,195.33 |
| 2. Investments (Note 4) | 710,061.34 | 711,897.34 |
| 3. Accounts Receivable (Note 5) | 628,575,094.40 | 437,346,152.22 |
| 4. Other Assets (Note 6) | 366,014,579.90 | 288,895,556.18 |
| 5. Total Intragovernmental Assets | <u>\$ 117,339,644,340.26</u> | <u>\$ 123,221,622,908.52</u> |
| B. Cash and Other Monetary Assets (Note 7) | \$ 147,468,121.99 | \$ 148,187,139.07 |
| C. Accounts Receivable (Note 5) | 969,919,225.46 | 938,217,451.04 |
| D. Loans Receivable (Note 8) | 0.00 | 0.00 |
| E. Inventory and Related Property (Note 9) | 48,643,476,455.88 | 52,202,386,284.22 |
| F. General Property, Plant and Equipment (Note 10) | 119,949,046,605.98 | 113,904,299,620.71 |
| G. Investments (Note 4) | 0.00 | 0.00 |
| H. Other Assets (Note 6) | 11,535,139,870.02 | 10,492,083,249.08 |
| 2. TOTAL ASSETS | <u><u>\$ 298,584,694,619.59</u></u> | <u><u>\$ 300,906,796,652.64</u></u> |
| 3. LIABILITIES (Note 11) | | |
| A. Intragovernmental: | | |
| 1. Accounts Payable (Note 12) | \$ 1,692,869,764.70 | \$ 1,669,557,861.90 |
| 2. Debt (Note 13) | 0.00 | 0.00 |
| 3. Other Liabilities (Note 15 & Note 16) | 1,732,526,825.79 | 2,225,954,096.62 |
| 4. Total Intragovernmental Liabilities | <u>\$ 3,425,396,590.49</u> | <u>\$ 3,895,511,958.52</u> |
| B. Accounts Payable (Note 12) | \$ 6,703,865,262.24 | \$ 5,851,267,290.10 |
| C. Military Retirement Benefits and Other Employment-Related Actuarial Liabilities (Note 17) | 1,163,442,240.00 | 1,262,267,550.00 |
| D. Environmental Liabilities (Note 14) | 7,099,189,747.85 | 7,169,710,790.75 |
| E. Loan Guarantee Liability (Note 8) | 0.00 | 0.00 |
| F. Other Liabilities (Note 15 & Note 16) | 3,642,387,544.25 | 5,024,342,845.64 |
| 4. TOTAL LIABILITIES | <u>\$ 22,034,281,384.83</u> | <u>\$ 23,203,100,435.01</u> |
| 5. NET POSITION | | |
| A. Unexpended Appropriations | \$ 107,410,309,551.75 | \$ 113,225,824,331.40 |
| B. Cumulative Results of Operations | 169,140,103,683.01 | 164,477,871,886.23 |
| 6. TOTAL NET POSITION | <u>\$ 276,550,413,234.76</u> | <u>\$ 277,703,696,217.63</u> |
| 7. TOTAL LIABILITIES AND NET POSITION | <u><u>\$ 298,584,694,619.59</u></u> | <u><u>\$ 300,906,796,652.64</u></u> |

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CONSOLIDATED STATEMENT OF NET COST

For the periods ended March 31, 2005 and 2004

| | 2005 Consolidated | 2004 Consolidated |
|---|----------------------|----------------------|
| 1. Program Costs | | |
| A. Intragovernmental Gross Costs | \$ 14,370,171,537.75 | \$ 13,993,273,886.92 |
| B. (Less: Intragovernmental Earned Revenue) | (1,864,889,198.71) | (1,408,566,529.05) |
| C. Intragovernmental Net Costs | \$ 12,505,282,339.04 | \$ 12,584,707,357.87 |
| D. Gross Costs With the Public | 50,759,094,344.71 | 47,681,785,706.87 |
| E. (Less: Earned Revenue From the Public) | (1,850,834,321.36) | (681,222,482.58) |
| F. Net Costs With the Public | \$ 48,908,260,023.35 | \$ 47,000,563,224.29 |
| G. Total Net Cost | \$ 61,413,542,362.39 | \$ 59,585,270,582.16 |
| 2. Cost Not Assigned to Programs | 0.00 | 0.00 |
| 3. (Less: Earned Revenue Not Attributable to Programs) | 0.00 | 0.00 |
| 4. Net Cost of Operations | \$ 61,413,542,362.39 | \$ 59,585,270,582.16 |

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CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION

For the periods ended March 31, 2005 and 2004

| | 2005 Consolidated | 2004 Consolidated |
|---|-----------------------|-----------------------|
| CUMULATIVE RESULTS OF OPERATIONS | | |
| 1. Beginning Balances | \$ 168,982,134,685.46 | \$ 161,327,683,610.64 |
| 2. Prior period adjustments (+/-) | | |
| 2.A. Prior Period Adjustments - Restated (+/-) | 0.00 | 0.00 |
| 2.B. Beginning Balance, Restated | 168,982,134,685.46 | 161,327,683,610.64 |
| 2.C. Prior Period Adjustments - Not Restated (+/-) | 0.00 | 0.00 |
| 3. Beginning Balances, as adjusted | 168,982,134,685.46 | 161,327,683,610.64 |
| 4. Budgetary Financing Sources: | | |
| 4.A. Appropriations received | 0.00 | 0.00 |
| 4.B. Appropriations transferred-in/out (+/-) | 0.00 | 0.00 |
| 4.C. Other adjustments (rescissions, etc) (+/-) | 0.00 | 0.00 |
| 4.D. Appropriations used | 61,240,201,644.34 | 61,826,662,736.19 |
| 4.E. Nonexchange revenue | (2,317,125.02) | 50,203,735.45 |
| 4.F. Donations and forfeitures of cash and cash equivalents | 1,132,886.55 | 1,642,093.78 |
| 4.G. Transfers-in/out without reimbursement (+/-) | 0.00 | 0.00 |
| 4.H. Other budgetary financing sources (+/-) | 0.00 | 0.00 |
| 5. Other Financing Sources: | | |
| 5.A. Donations and forfeitures of property | 0.00 | 0.00 |
| 5.B. Transfers-in/out without reimbursement (+/-) | (31,923,880.00) | 527,853,585.03 |
| 5.C. Imputed financing from costs absorbed by others | 364,417,834.07 | 329,096,707.30 |
| 5.D. Other (+/-) | 0.00 | 0.00 |
| 6. Total Financing Sources | 61,571,511,359.94 | 62,735,458,857.75 |
| 7. Net Cost of Operations (+/-) | 61,413,542,362.39 | 59,585,270,582.16 |
| 8. Ending Balances | \$ 169,140,103,683.01 | \$ 164,477,871,886.23 |

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CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION

For the periods ended March 31, 2005 and 2004

| | 2005 Consolidated | 2004 Consolidated |
|---|-----------------------|-----------------------|
| UNEXPENDED APPROPRIATIONS | | |
| 1. Beginning Balances | \$ 49,660,670,196.09 | \$ 50,742,316,104.12 |
| 2. Prior period adjustments (+/-) | | |
| 2.A. Prior Period Adjustments - Restated (+/-) | 0.00 | 0.00 |
| 2.B. Beginning Balance, Restated | 49,660,670,196.09 | 50,742,316,104.12 |
| 2.C. Prior Period Adjustments - Not Restated (+/-) | 0.00 | 0.00 |
| 3. Beginning Balances, as adjusted | 49,660,670,196.09 | 50,742,316,104.12 |
| 4. Budgetary Financing Sources: | | |
| 4.A. Appropriations received | 118,485,621,000.00 | 124,835,282,566.22 |
| 4.B. Appropriations transferred-in/out (+/-) | 1,214,409,000.00 | 98,174,000.00 |
| 4.C. Other adjustments (rescissions, etc) (+/-) | (710,189,000.00) | (623,285,602.75) |
| 4.D. Appropriations used | (61,240,201,644.34) | (61,826,662,736.19) |
| 4.E. Nonexchange revenue | 0.00 | 0.00 |
| 4.F. Donations and forfeitures of cash and cash equivalents | 0.00 | 0.00 |
| 4.G. Transfers-in/out without reimbursement (+/-) | 0.00 | 0.00 |
| 4.H. Other budgetary financing sources (+/-) | 0.00 | 0.00 |
| 5. Other Financing Sources: | | |
| 5.A. Donations and forfeitures of property | 0.00 | 0.00 |
| 5.B. Transfers-in/out without reimbursement (+/-) | 0.00 | 0.00 |
| 5.C. Imputed financing from costs absorbed by others | 0.00 | 0.00 |
| 5.D. Other (+/-) | 0.00 | 0.00 |
| 6. Total Financing Sources | 57,749,639,355.66 | 62,483,508,227.28 |
| 7. Net Cost of Operations (+/-) | | |
| 8. Ending Balances | \$ 107,410,309,551.75 | \$ 113,225,824,331.40 |

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

| | 2005 Combined | 2004 Combined |
|--|-------------------------------------|-------------------------------------|
| BUDGETARY FINANCING ACCOUNTS | | |
| BUDGETARY RESOURCES | | |
| 1. Budget Authority: | | |
| 1a. Appropriations received | \$ 118,487,128,264.83 | \$ 124,836,924,660.00 |
| 1b. Borrowing authority | 0.00 | 0.00 |
| 1c. Contract authority | 0.00 | 0.00 |
| 1d. Net transfers (+/-) | 145,073,000.00 | 138,873,000.00 |
| 1e. Other | 337,481.10 | 332,433.78 |
| 2. Unobligated balance: | | |
| 2a. Beginning of period | 9,048,570,951.49 | 9,189,944,640.03 |
| 2b. Net transfers, actual (+/-) | 1,069,336,000.00 | 410,301,000.00 |
| 2c. Anticipated Transfers balances | 0.00 | 0.00 |
| 3. Spending authority from offsetting collections: | | |
| 3a. Earned | 0.00 | 0.00 |
| 1. Collected | 4,078,968,908.87 | 3,440,021,482.87 |
| 2. Receivable from Federal sources | (13,042,526.83) | (100,444,016.26) |
| 3b. Change in unfilled customer orders | 0.00 | 0.00 |
| 1. Advance received | 377,466,159.26 | 556,480,722.90 |
| 2. Without advance from Federal sources | 2,091,377,272.82 | 1,442,358,779.13 |
| 3c. Anticipated for the rest of year, without advances | 1,698,586,890.77 | 2,419,824,802.52 |
| 3d. Previously unavailable | 0.00 | 0.00 |
| 3e. Transfers from trust funds | 0.00 | 0.00 |
| 3f. Subtotal | <u>8,233,356,704.89</u> | <u>7,758,241,771.16</u> |
| 4. Recoveries of prior year obligations | 519,358,235.05 | 4,044,334,668.68 |
| 5. Temporarily not available pursuant to Public Law | 0.00 | 0.00 |
| 6. Permanently not available | (710,189,000.00) | (640,068,000.00) |
| 7. Total Budgetary Resources | <u><u>\$ 136,792,971,637.36</u></u> | <u><u>\$ 145,738,884,173.65</u></u> |

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

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

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

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

Department of Defense

Department of the Air Force

COMBINED STATEMENT OF FINANCING

For the periods ended March 31, 2005 and 2004

| | 2005 Combined | 2004 Combined |
|---|----------------------------|----------------------------|
| Resources Used to Finance Activities: | | |
| Budgetary Resources Obligated | | |
| 1. Obligations incurred | \$ 72,843,838,558.13 | \$ 74,256,098,574.92 |
| 2. Less: Spending authority from offsetting collections and recoveries (-) | (7,054,128,049.17) | (9,382,751,637.32) |
| 3. Obligations net of offsetting collections and recoveries | 65,789,710,508.96 | 64,873,346,937.60 |
| 4. Less: Offsetting receipts (-) | (54,298,673.62) | (92,123,350.52) |
| 5. Net obligations | 65,735,411,835.34 | 64,781,223,587.08 |
| Other Resources | | |
| 6. Donations and forfeitures of property | 0.00 | 0.00 |
| 7. Transfers in/out without reimbursement (+/-) | (31,923,880.00) | 527,853,585.03 |
| 8. Imputed financing from costs absorbed by others | 364,417,834.07 | 329,096,707.30 |
| 9. Other (+/-) | 0.00 | 0.00 |
| 10. Net other resources used to finance activities | 332,493,954.07 | 856,950,292.33 |
| 11. Total resources used to finance activities | 66,067,905,789.41 | 65,638,173,879.41 |
| Resources Used to Finance Items not Part of the Net Cost of Operations | | |
| 12. Change in budgetary resources obligated for goods, services and benefits ordered but not yet provided | | |
| 12a. Undelivered Orders (-) | (7,018,847,522.58) | (5,037,331,325.36) |
| 12b. Unfilled Customer Orders | 2,468,843,432.08 | 1,998,839,502.03 |
| 13. Resources that fund expenses recognized in prior periods | (939,711,396.16) | (1,072,837,377.70) |
| 14. Budgetary offsetting collections and receipts that do not affect net cost of operations | 54,298,673.62 | 1,642,093.78 |
| 15. Resources that finance the acquisition of assets | (7,270,974,986.66) | (10,384,101,494.03) |
| 16. Other resources or adjustments to net obligated resources that do not affect net cost of operations | | |
| 16a. Less: Trust or Special Fund Receipts Related to | 0.00 | 0.00 |
| 16b. Other (+/-) | 31,923,880.00 | (527,853,585.03) |
| 17. Total resources used to finance items not part of the net cost of operations | (12,674,467,919.70) | (15,021,642,186.31) |
| 18. Total resources used to finance the net cost of operations | 53,393,437,869.71 | 50,616,531,693.10 |

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COMBINED STATEMENT OF FINANCING

For the periods ended March 31, 2005 and 2004

| | 2005 Combined | 2004 Combined |
|---|---------------------------------|---------------------------------|
| 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: | | |
| 19. Increase in annual leave liability | 111,715,365.28 | 0.00 |
| 20. Increase in environmental and disposal liability | 0.00 | 0.00 |
| 21. Upward/Downward reestimates of credit subsidy expense (+/-) | 0.00 | 0.00 |
| 22. Increase in exchange revenue receivable from the public (-) | 0.00 | 0.00 |
| 23. Other (+/-) | 10,273,341.61 | 338,678,060.42 |
| 24. Total components of Net Cost of Operations that will require or generate resources in future periods | <u>121,988,706.89</u> | <u>338,678,060.42</u> |
| Components not Requiring or Generating Resources: | | |
| 25. Depreciation and amortization | 4,398,698,092.67 | 7,266,960,556.28 |
| 26. Revaluation of assets or liabilities (+/-) | (978,170,113.59) | (541,589,105.37) |
| 27. Other (+/-) | | |
| 27a. Trust Fund Exchange Revenue | 0.00 | 0.00 |
| 27b. Cost of Goods Sold | 0.00 | 0.00 |
| 27c. Operating Material & Supplies Used | 676,888,133.45 | 1,516,105,161.75 |
| 27d. Other | 3,800,699,673.26 | 388,584,215.98 |
| 28. Total components of Net Cost of Operations that will not require or generate resources | <u>7,898,115,785.79</u> | <u>8,630,060,828.64</u> |
| 29. Total components of net cost of operations that will not require or generate resources in the current period | <u>8,020,104,492.68</u> | <u>8,968,738,889.06</u> |
| 30. Net Cost of Operations | <u><u>61,413,542,362.39</u></u> | <u><u>59,585,270,582.16</u></u> |

Note 1. Significant Accounting Policies**1.A. Basis of Presentation**

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

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

In addition, the Air Force needs to improve documentation, user access, separation of duty, and oversight controls over the travel pay process. Also, the Air Force continues to enter a material number of unsupported accounting entries because financial and nonfinancial feeder systems continue to lack sufficient customer identification information to accurately process eliminations. This issue was disclosed in the DoD Agency-wide Note 1 and is addressed in the Air Force’s plan to obtain a favorable opinion by FY 2007.

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

1.B. Mission of the Reporting Entity

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

The Air Force incorporates internal controls, reconciliations, management by exception reports, and other management control information into its accounting systems. When possible, the financial statements are presented on the accrual basis of accounting, as required by federal accounting standards.

The accounts used to prepare the financial statements are categorized as either entity or nonentity. Entity accounts consist of resources that are available for use in the operations of the entity. The Air Force is authorized to decide how to use resources in entity accounts or may be legally obligated to use these resources to meet entity obligations. Nonentity accounts, on the other hand, consist of assets that are held by an entity but that are not available for use in the operations of the entity.

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

| <u>Air Force Account Number</u> | <u>Title</u> |
|---------------------------------|---|
| 57 * 0704 | Military Family Housing (O&M and Construction), Air Force |
| 57 * 0740 | Military Family Housing (Construction), Air Force |
| 57 * 0745 | Military Family Housing (O&M), Air Force |
| 57 * 0810 | Environmental Restoration, Air Force |
| 57 * 1999 | Unclassified Receipts and Expenditures, Air Force |
| 57 * 3010 | Aircraft Procurement, Air Force |
| 57 * 3011 | Procurement of Ammunition, Air Force |
| 57 * 3020 | Missile Procurement, Air Force |
| 57 * 3080 | Other Procurement, Air Force |
| 57 * 3300 | Military Construction, Air Force |
| 57 * 3400 | Operation and Maintenance (O&M), Air Force |
| 57 * 3500 | Military Personnel, Air Force |
| 57 * 3600 | Research, Development, Testing, and Evaluation (RDT&E), AF |
| 57 * 3700 | Personnel, Air Force Reserve |
| 57 * 3730 | Military Construction, Air Force Reserve |
| 57 * 3740 | Operation and Maintenance (O&M), Air Force Reserve |
| 57 * 3830 | Military Construction, Air National Guard |
| 57 * 3840 | Operation and Maintenance (O&M), Air National Guard |
| 57 * 3850 | Personnel, Air National Guard |
| 57 X 5095 | Wildlife Conservation, etc., Military Reservations, Air Force |
| 57 X 8418 | Air Force Cadet Fund |
| 57 X 8928 | Air Force General Gift Fund |
| 57 * 3XXX | Budget Clearing Accounts |

1.C. Appropriations and Funds

The Air Force's appropriations and funds are used to fund and to report how resources have been used in the course of executing the Air Force's missions. The Air Force's appropriations and funds are divided into the following categories:

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

1.D. Basis of Accounting

The Air Force generally records transactions on a budgetary basis and not an accrual accounting basis as is required by Federal GAAP. For FY 2005, the Air Force's financial management systems are unable to meet all of the requirements for full accrual accounting. Many of the Air Force's financial and nonfinancial feeder systems and processes were designed and implemented prior to the issuance of Federal GAAP for federal agencies and, therefore, were not designed to collect and record financial information on the full accrual accounting basis as required by Federal GAAP.

The Air Force has undertaken efforts to determine the actions required to bring its financial and nonfinancial feeder systems and processes into compliance with all elements of Federal GAAP. One such action is the current revision of the Air Force's accounting systems to record transactions based on the United States Government Standard General Ledger (USSGL).

Until all of the Air Force's financial and nonfinancial feeder systems and processes are updated to collect and report financial information as required by Federal GAAP, some of Air Force's financial data will be based on budgetary transactions (obligations, disbursements, and collections) and nonfinancial feeder systems and then be adjusted for

known accruals of major items such as payroll expenses, accounts payable, and environmental liabilities. For example, much of the data on the Statement of Net Cost (SoNC) is based on obligations and disbursements and may not represent all accrued costs. However, when possible, the Air Force's financial statements are presented on the accrual basis of accounting as required by Federal GAAP.

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

1.E. Revenues and Other Financing Sources

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

The Air Force does not include nonmonetary support provided by U.S. Allies for common defense and mutual security in its list of other financing sources that appears in the Statement of Financing. Agreements between the U.S. and some foreign countries include both direct and indirect sharing of the costs that each country incurs in support of the same general purpose. Examples of such countries include those that have a mutual or reciprocal defense agreement with the U.S. and those where U.S. troops are stationed or the U.S. fleet is serviced. The DoD is reviewing this type of financing and cost reduction in order to establish accounting policies and procedures to identify which, if any, of these costs are appropriate for disclosure in the DoD and Air Force financial statements in accordance with Federal GAAP. Recognition of support provided by host nations would affect both financing sources and recognition of expenses

1.F. Recognition of Expenses

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

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

Operating expenses were adjusted as a result of the elimination of balances between DoD Components. See Note 18, Intragovernmental Expenses and Revenue, for disclosure of adjustment amounts.

1.G. Accounting for Intragovernmental Activities

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

The Air Force's proportionate share of public debt and related expenses of the federal government are not included in the financial statements. Debt issued by the federal government and the related costs are not apportioned to federal agencies. The Air Force's financial statements do not report any portion of the public debt or interest thereon, nor do the statements report the source of public financing, whether from issuance of debt or tax revenues.

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

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

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

adjusted to recognize unrecorded costs and accounts payable. Intra-Air Force balances were then eliminated.

The Department of the Treasury Financial Management Service (FMS) is responsible for eliminating transactions between the DoD and other federal agencies. In September 2004, the FMS issued the “Federal Intragovernmental Transactions Accounting Policies Guide.” The DoD was not able to fully implement the policies and procedures in this guide related to reconciling intragovernmental assets, liabilities, revenues, and expenses for nonfiduciary transactions. The Air Force, however, was able to implement the policies and procedures contained in the “Intragovernmental Fiduciary Transactions Accounting Guide,” as updated by the “Federal Intragovernmental Transactions Accounting Policies Guide” (September 2004) for reconciling intragovernmental transactions. These transactions include or pertain 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 OPM.

1.H. Transactions with Foreign Governments and International Organizations

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

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

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

In addition, the DFAS sites and USACE Finance Center submit reports to the Department of the Treasury, providing information at the appropriation level on interagency transfers, collections received, and disbursements issued. The Department of the Treasury then records this information to the applicable Fund Balance with Treasury (FBWT) account maintained in the Treasury’s system. Differences between the Air Force’s recorded balance in the FBWT accounts and Treasury’s FBWT accounts sometimes result and are subsequently reconciled. Material disclosures are provided at Note 3. Also disclosed at Note 3 are differences between accounting offices’ detail level records and Treasury’s FBWT accounts, specifically, differences caused by intransit disbursements and unmatched disbursements (where the specific

disbursement has not been recorded in the appropriate accounting offices' detail level records).

1.J. Foreign Currency

The Air Force conducts a significant portion of its operations overseas. The Congress established a special account to handle gains and losses from foreign currency transactions for the following five general fund appropriations: O&M, Military Personnel, Military Construction, Family Housing Operation and Maintenance, and Family Housing Construction. Gains and losses are computed as the variance between the exchange rate current at the date of payment and a budget rate established at the beginning of each fiscal year. Foreign currency fluctuations related to other appropriations require adjustment to the original obligation amount at the time of payment. These currency fluctuations are not identified separately. See Note 7 for material disclosures.

1.K. Accounts Receivable

As presented in the balance sheet statement, accounts receivable include accounts, claims, and refunds receivable from other federal entities or from the public. Allowances for uncollectible accounts due from the public are based upon analysis of collection experience by fund type. The DoD does not recognize an allowance for estimated uncollectible amounts from other federal agencies. Claims against other federal agencies are to be resolved between the agencies. See Note 5 for material disclosures.

1.L. Loans Receivable

Not applicable

1.M. Inventories and Related Property

The related property portion of the amount reported on the Inventory and Related Property line includes Operating Materials and Supplies (OM&S). The OM&S are reported at approximate historical cost using Standard Price (SP). The Air Force uses the SP method because its OM&S systems were designed for material management rather than for accounting. The systems provide accountability and visibility over inventory items. They do not maintain the historical cost data necessary to comply with Statement of Federal Financial Accounting Standards (SFFAS) No. 3, "Accounting for Inventory and Related Property." Neither can they directly produce financial transactions using the U.S. Standard General Ledger (USSGL), as required by the Federal Financial Management Improvement Act of 1996 (P.L. 104-208). The DoD is transitioning to a

Moving Average Cost methodology for valuing inventory that, when fully implemented, will allow the Air Force to comply with SFFAS No. 3.

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

Related property includes OM&S and stockpile materials. The OM&S, including munitions not held for use, are valued at SP. Ammunition and munitions are treated as OM&S. In general, the Air Force uses the consumption method of accounting for OM&S, expensing material when it is issued to the end user.

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

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

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

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

The Air Force invests in both marketable and nonmarketable securities. Marketable securities are investments trading on a public market. The two types of nonmarketable securities are par value and market-based intragovernmental securities. The Bureau of Public Debt issues nonmarketable, par value intragovernmental securities. Nonmarketable, market-based intragovernmental securities mimic marketable securities but are not traded publicly. See Note 4 for material disclosures.

1.O. General Property, Plant and Equipment

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

When it is in the best interest of the government, the Air Force provides contractors with government property necessary to complete contract work. The Air Force owns or leases this property, or the contractor purchases the property directly for the government under the terms of the contract. When the value of contractor procured General PP&E exceeds the DoD capitalization threshold, such PP&E must be included in the value of General PP&E reported on the Air Force's balance sheet. The DoD is developing new policies and a contractor reporting process that will provide appropriate General PP&E information for future financial statement purposes. Accordingly, the Air Force currently reports only government property in the possession of contractors maintained in the Air Force real property systems.

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

See Note 10 for material disclosures.

1.P. Advances and Prepayments

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

1.Q. Leases

Generally, lease payments are for the rental of equipment vehicles and operating facilities and are classified as either capital or operating leases. When a lease essentially is equivalent to an installment purchase of property (a capital lease), the Air Force records the applicable asset and liability if the value equals or exceeds the current DoD capitalization threshold. The Air Force records the amounts as the lesser of the following two values: (1) the present value of the rental and other lease payments during the lease

term (excluding portions representing executory costs paid to the lessor); or (2) the asset's fair value. The Air Force deems the use of estimates for these costs as adequate and appropriate due to the relatively low dollar value of capital leases. Imputed interest is necessary to reduce net minimum lease payments to present value calculated at the incremental borrowing rate at the inception of the leases. Leases that do not transfer substantially all of the benefits or risks of ownership are classified as operating leases and are expensed over the period of the lease.

1.R. Other Assets

The Air Force conducts business with commercial contractors under two primary types of contracts: fixed price and cost reimbursable. To alleviate the potential financial burden on the contractor that long-term contracts can cause, the Air Force provides financing payments. One type of financing payment for real property is based on the percentage of completion. In accordance with the SFFAS No. 1, "Accounting for Selected Assets and Liabilities," such payments are treated as construction-in-progress and reported on the General PP&E line and in Note 10, General PP&E, Net. In addition, based on the Federal Acquisition Regulation, the Air Force makes financing payments under fixed price contracts not based on percentage of completion. The Air Force reports these financing payments as advances or prepayments in the Other Assets line item. The Air Force treats these payments as advances or prepayments because the Air Force becomes liable only after the contractor delivers the goods. If the contractor does not deliver a satisfactory product, the Air Force is not obligated to reimburse the contractor, and the contractor is liable to repay the Air Force for the full amount of the advance.

The DoD has completed a review of the applicable federal accounting standards; public laws on contract financing; Federal Acquisition Regulation Parts 32, 49, and 52; and the OMB guidance in 5 Code of Federal Regulations Part 1315, "Prompt Payment." The DoD has concluded that SFFAS No. 1 does not fully address progress payment accounting and is considering what action is appropriate.

1.S. Contingencies and Other Liabilities

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

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

1.T. Accrued Leave

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

1.U. Net Position

Net Position consists of unexpended appropriations and cumulative results of operations. Unexpended appropriations represent (1) amounts of authority that are not obligated and that have not been rescinded or withdrawn, and (2) amounts that are obligated but for which legal liabilities for payments have not been incurred.

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

1.V. Treaties for Use of Foreign Bases

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

1.W. Comparative Data

The Financial Statements and accompanying Notes to the Financial Statements report the financial position and results of operations for the 2nd Quarter of FY 2005. Financial statement fluctuations greater than 2 percent of total assets on the Balance Sheet and/or greater than 10 percent between FY 2004 and FY 2005 are explained within the Notes to the Financial Statements.

1.X. Unexpended Obligations

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

1.Y. Undistributed Disbursements and Collections

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

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

| | |
|----------------|-------------------------|
| Note 2. | Nonentity Assets |
|----------------|-------------------------|

| As of March 31 | 2005 | 2004 |
|------------------------------------|-----------------------|-----------------------|
| 1. Intragovernmental Assets | | |
| A. Fund Balance with Treasury | \$ 136,034,520.60 | \$ 432,403,195.33 |
| B. Investments | 0.00 | 0.00 |
| C. Accounts Receivable | 2,266,222.93 | (9,187,530.59) |
| D. Other Assets | 0.00 | 0.00 |
| E. Total Intragovernmental Assets | \$ 138,300,743.53 | \$ 423,215,664.74 |
| 2. Nonfederal Assets | | |
| A. Cash and Other Monetary Assets | \$ 147,468,121.99 | \$ 148,187,139.07 |
| B. Accounts Receivable | 542,463,078.34 | 376,338,118.24 |
| C. Loans Receivable | 0.00 | 0.00 |
| D. Inventory & Related Property | 0.00 | 0.00 |
| E. General PP&E | 0.00 | 0.00 |
| F. Investments | 0.00 | 0.00 |
| G. Other Assets | 156,981,725.35 | 147,996,342.53 |
| H. Total Nonfederal Assets | \$ 846,912,925.68 | \$ 672,521,599.84 |
| 3. Total Nonentity Assets | \$ 985,213,669.21 | \$ 1,095,737,264.58 |
| 4. Total Entity Assets | \$ 297,599,480,950.38 | \$ 299,811,059,388.06 |
| 5. Total Assets | \$ 298,584,694,619.59 | \$ 300,906,796,652.64 |

Relevant Information for Comprehension

Nonentity Assets are assets that are held by an entity but that are not available for use in the operations of the entity. Non-Federal Other Assets classes are advances to contractors and outstanding travel advances. The Nonentity Fund Balance with Treasury asset class represents amounts in Air Force deposit and suspense accounts that are not available for Air Force use. Nonentity Accounts Receivables, both when collected, go to the Department of the Treasury as miscellaneous receipts. The Nonentity Non-Federal Accounts Receivable amount also includes interest receivables on aged debt. Nonentity Cash and Other Monetary Assets represent disbursing officers' cash and undeposited collections as reported on the Statement of Accountability. These assets are held by the Air Force disbursing officers as agents of the Treasury.

Fluctuations

The fluctuation in Non-Entity Fund Balance with Treasury on line 1.A is primarily attributed to revised guidance that clarifies what accounts should be reported as Non Entity Fund Balance with Treasury. This line now includes balances in deposit fund

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accounts, receipt accounts, and all budget clearing accounts with the exception of Civilian Thrift Saving Plan (TSP) and Military TSP. A balance of \$342,533 thousand in account 3875 was included at March 2004 as Non Entity and accounts for most of the fluctuation.

During the 2nd Quarter FY 04, intragovernmental accounts receivables represented an erroneous abnormal balance of \$9,188 thousand as a result of the implementation of a new accounting system (GAFS-R) and the incorrect beginning balances being interfaced. During FY 05, the Air Force reconciled nonfederal accounts receivables based on field level reported data and accurately recorded non-entity receivables to reflect field level activity.

The increase in nonfederal accounts receivable in the amount \$166,124 thousand is a result of increase debt reported on the Monthly Debt Management Report (MDMR). During FY 05 a debt in the amount of \$150,249 thousand for GE Company was recorded under the Air Force Procurement program.

| | |
|----------------|-----------------------------------|
| Note 3. | Fund Balance with Treasury |
|----------------|-----------------------------------|

| As of March 31 | 2005 | 2004 |
|--|------------------------------|------------------------------|
| 1. Fund Balances | | |
| A. Appropriated Funds | \$ 116,227,882,516.72 | \$ 122,420,099,565.78 |
| B. Revolving Funds | 0.00 | 0.00 |
| C. Trust Funds | 4,789,445.68 | 5,273,664.84 |
| D. Special Funds | 654,953.99 | 0.00 |
| E. Other Fund Types | 111,017,688.23 | 69,296,072.16 |
| F. Total Fund Balances | <u>\$ 116,344,344,604.62</u> | <u>\$ 122,494,669,302.78</u> |
| 2. Fund Balances Per Treasury Versus Agency | | |
| A. Fund Balance per Treasury | \$ 116,360,591,498.93 | \$ 122,494,846,375.08 |
| B. Fund Balance per | <u>116,344,344,604.62</u> | <u>122,494,669,302.78</u> |
| 3. Reconciling Amount | <u>\$ 16,246,894.31</u> | <u>\$ 177,072.30</u> |

Reconciling Amount

Parent Child Allocations that are not included in Air Force balances totals \$25,383 thousand. Included in these are allocations from Foreign Military Sales Military Assistance Program and the Department of Agriculture. Included in Air Force balance and not in Treasury balance is \$9,136 thousand for funds allocated to the Department of Transportation. This balance is reported on the 6654 for Treasury Index 69.

Fluctuations

The amount shown in Trust Funds for FY 2004 is incorrect. The amount in Appropriation 5095, Fish and Wildlife, \$541 thousand, was erroneously included in Trust Funds instead of being properly reported as Special Funds. The correct figure should have been \$4,733 thousand. The true fluctuation is an increase and is attributable to fewer expenditures being made in the Air Force Gift Fund.

The increase in Special Funds is due to the proper display of appropriation 5095, Fish and Wildlife, as a Special Fund. During FY 2004, these funds were included on line 1.C., Trust Funds. Other Fund Types include balances in deposit funds, and receipt accounts.

The fluctuation in Non-Entity – Other on line 1.A.1.C on the Balance Sheet is primarily attributed to revised guidance that clarifies what accounts should be reported as Non Entity Fund Balance with Treasury. This line now includes balances in deposit fund accounts and receipt accounts. The budget clearing accounts, with the exception of Civilian TSP and Military TSP, which were previously reported as Non-Entity, are now reported as Entity. A balance of \$342,533 thousand in

Budget Clearing Account Suspense, 3875, was included at March 2004 as Non Entity and accounts for most of the fluctuation.

Air Force Cadet Fund

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

Check Issue Discrepancy

DFAS is in the process of collecting information for all check-issue data that are unsupported because (1) records have been lost during deactivation of disbursing offices, (2) transactions past the one year period in which Treasury provides research assistance, or (3) corrections were processed for transactions that Treasury removed from the check-comparison report. Transactions that have no supporting documentation due to one of the preceding situations shall be provided to the Department of the Treasury with a request to remove them from the Treasury Check Comparison Report. The vast majority of the remaining check issue discrepancies result from timing differences between the Air Force and the Department of the Treasury for processing checks. The DoD does not require that Treasury remove any amounts from the check-issue comparison report since the check-issue report balance was \$0. Further, no empirical evidence has been presented that demonstrates that check issue discrepancies adversely affect the FBWT.

Note Reference

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

Status of Fund Balance with Treasury

| As of March 31 | 2005 | 2004 |
|---|-----------------------|-----------------------|
| 1. Unobligated Balance | | |
| A. Available | \$ 59,717,245,943.86 | \$ 66,610,002,117.18 |
| B. Unavailable | 2,533,762,763.50 | 2,457,898,898.06 |
| 2. Obligated Balance not yet Disbursed | \$ 53,957,613,893.74 | \$ 53,497,383,231.50 |
| 3. Total | \$ 116,208,622,601.10 | \$ 122,565,284,246.74 |

Fluctuations

Unobligated Balance, Available decreased due to less funding being received this fiscal year, specifically in the Air Force Operations & Maintenance appropriation.

The difference between the total amount of Status of Fund Balance with Treasury reflected here and fund balance with Treasury in part one of Note 3 is due to Nonentity assets and Entity assets recorded for budget clearing accounts, deposit funds and receipt accounts. Status of funds budgetary data is not recorded for these accounts. Only proprietary FBWT is updated for these balances.

Relevant Information for Comprehension

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

Disclosures Related to Suspense/Budget Clearing Accounts

| As of March 31 | 2003 | 2004 | 2005 | (Decrease)/ Increase from FY 2004 - 2005 |
|----------------|--------------------------|--------------------------|--------------------------|--|
| Account | | | | |
| F3875 | \$ 396,939,914.98 | \$ 342,533,903.38 | \$ 299,053,538.26 | (43,480,365.12) |
| F3880 | 1,331,053.48 | 1,313,563.90 | 887,583.39 | (425,980.51) |
| F3882 | 14,292,626.89 | 18,976,482.81 | 25,016,832.37 | 6,040,349.56 |
| F3885 | (12,812,756.56) | (14,450,667.38) | (31,578,097.90) | (17,127,430.52) |
| F3886 | 0.00 | 0.00 | 0.00 | 0.00 |
| Total | \$ 399,750,838.79 | \$ 348,373,282.71 | \$ 293,379,856.12 | (54,993,426.59) |

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

Suspense account F3882 is utilized to accommodate the Military Thrift Savings Plan (TSP). The National Finance Center posts amounts into each member's account, and they are consolidated and posted to the Treasury before the Air Force can post the amounts in the military accounting system in the following month. The \$6,040 thousand increase is the result of increased participation in the TSP.

The increase (in absolute value) in account F3885 is due to IPAC transactions received during the last business day of the month. The funds are placed in a suspense account until they can be researched and assigned a valid appropriation, which will fluctuate from one reporting period to another depending upon the amount processed to the Treasury at that time.

Disclosures Related to Problem Disbursements and In-Transit Disbursements

| As of March 31 | 2003 | 2004 | 2005 | (Decrease)/ Increase from FY 2004 - 2005 |
|---|---------------------|---------------------|---------------------|--|
| 1. Total Problem Disbursements, Absolute Value | | | | |
| A. Unmatched Disbursements (UMDS) | \$ 17,726,663.81 | \$ 130,838,906.28 | \$ 1,368,166,356.48 | \$ 1,237,327,450.20 |
| B. Negative Unliquidated Obligations (NULO) | 11,178,255.59 | 13,589,932.18 | 23,261,916.11 | 9,671,983.93 |
| 2. Total In-transit Disbursements, Net | \$ 1,985,225,990.09 | \$ 1,162,774,105.29 | \$ 622,396,365.44 | \$ (540,377,739.85) |

Problem disbursements represent disbursements of Air Force funds reported by a disbursing station to the Department of the Treasury but have not yet been precisely matched against the specific source obligation. The problem disbursement arises when the various contracting, disbursing, and accounting systems fail to match the data necessary to properly account for the transaction in all the applicable accounting systems.

The Air Force had a \$1,246,999 thousand increase in problem disbursements and a \$540,378 thousand decrease in In-transit disbursements. The Defense Finance and Accounting Service has efforts underway to improve the systems; to resolve all previous problem disbursements, and to process all In-transit disbursements in a timely manner. The amount of unmatched disbursements (UMDs) over 180 days is \$931,262.26, for Negative Unliquidated Disbursements (NULOs) is \$0.00 and for In-transits is \$8,489,292.30. The amount of UMDs over 120 days old is \$4,646,373.69, for NULOs is \$0.00, and for In-transits is \$28,353,115.10. The current absolute value of In-transit disbursements is \$870,909,629.01.

The increase in UMDs can be attributed to database mergers (San Bernardino to Dayton in July 2004 and San Antonio to Limestone in October 2004) and difficulties encountered with the merger of the Contract Procurement Accounting System (CPAS) and the General Accounting and Finance System (GAFS). Also, a substantial amount of problems were encountered when we implemented new business processes for handling Mechanization of Contract and Administrative Services (MOCAS) disbursements. The old procedure was to receive transactions through a process called Contract Payment Notice (CPN) and post to CPAS/GAFS. The new procedure takes these payments through the Departmental Cash Management System For Others/By Others (DCMS DFB). We experienced numerous posting problems when we made this change due to incorrect posting logic within GAFS/DCMS DFB. All corrections are expected to be accomplished by July 2005.

The increase in NULOs is the result of resources being utilized to analyze and process backlogged UMDs. Resources have now been (re)directed to the NULO effort and a substantial decrease is anticipated in May 2005.

| | |
|----------------|---|
| Note 4. | Investments and Related Interest |
|----------------|---|

| As of March 31 | 2005 | | | | 2004 | |
|--|----------------|-----------------------------|---------------------------------------|---------------------|----------------------------|---------------------|
| | Par Value/Cost | Amorti- zation Method | Unamortized (Premium/ Discount) | Investments, Net | Market Value Disclosure | Investments, Net |
| 1. Intragovernmental Securities | | | | | | |
| A. Non-Marketable, Market-Based | \$ 710,000.00 | | \$ 61.34 | \$ 710,061.34 | \$ 707,671.25 | \$ 711,897.34 |
| B. Accrued Interest | 0.00 | | | 0.00 | 0.00 | 0.00 |
| C. Total Intragovernmental Securities | \$ 710,000.00 | | \$ 61.34 | \$ 710,061.34 | \$ 707,671.25 | \$ 711,897.34 |
| 2. Other Investments | \$ 0.00 | | 0.00 | \$ 0.00 | N/A | \$ 0.00 |

Fluctuations

Relevant Information for Comprehension

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

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

Note Reference

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

| | |
|----------------|----------------------------|
| Note 5. | Accounts Receivable |
|----------------|----------------------------|

| As of March 31 | 2005 | | | 2004 |
|--|---------------------|---|-----------------------------|-----------------------------|
| | Gross Amount Due | Allowance For Estimated Uncollectibles | Accounts Receivable, Net | Accounts Receivable, Net |
| 1. Intragovernmental Receivables | \$ 628,575,094.40 | N/A | \$ 628,575,094.40 | \$ 437,346,152.22 |
| 2. Nonfederal Receivables (From the Public) | \$ 1,072,771,629.46 | \$ (102,852,404.00) | \$ 969,919,225.46 | \$ 938,217,451.04 |
| 3. Total Accounts Receivable | \$ 1,701,346,723.86 | \$ (102,852,404.00) | \$ 1,598,494,319.86 | \$ 1,375,563,603.26 |

The total allowance method is determined at the Air Force departmental level. These department-level amounts are derived as follows: For closed-years receivables and deferred debts in litigation, an allowance rate of 50 percent results in an estimated allowance of \$37,355 thousand. Interest allowance of \$430 thousand is calculated using an average percent of write-offs to outstanding public accounts receivable over a five-year period starting with FY 2000 data. For Air Force entity receivables, the allowance is computed each year based on the average percent of write-offs to outstanding public accounts receivable for the last five years resulting in an estimated allowance of \$65,067 thousand.

Relevant Information for Comprehension

As presented on the Consolidated Balance Sheet, accounts receivable include reimbursements receivable and refunds receivable such as out-of-service debts (amounts owed by former service members), contractor debt, and unused travel tickets. It also includes net interest receivables per Department of Defense (DoD) Financial Management Regulation (FMR) Vol. 6B guidance. Canceled accounts receivable is reported as nonentity receivables because these amounts are deposited into a Treasury Department miscellaneous receipt account when collected. Reconciliation between Report on Receivables Due from the Public and the balance sheet was accomplished. The differences between the balance sheet (line 1C) and Treasury Report on Receivables (TROR) Due from the Public (line 7) include the allowance for estimated receivables that will be uncollected of \$102,852 thousand, unsupported disbursements in transit in the amount of \$8 thousand, and undistributed collections of \$49,944 thousand. Undistributed collections are prorated between public and intragovernmental receivables on the balance sheet based on the percentages of distributed receivables. This reconciliation is performed to ensure that the financial statements are in agreement with the public receivables reported to the Department of the Treasury.

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

Allocation of Undistributed Collections

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

Fluctuations

Intragovernmental Accounts Receivable before eliminations increased by \$628,575 thousand. The increase on the financial statements of \$191,229 thousand is after intragovernmental Air Force eliminations.

| | MAR 2005 | MAR 2004 | \$Change |
|------------------------------------|-----------------|-----------------|-----------------|
| A/R Government before Eliminations | \$1,329,168 | \$ 541,071 | \$ 788,097 |
| Less Intra-AF Eliminations | <u>700,594</u> | <u>103,725</u> | <u>596,869</u> |
| Total | \$ 628,575 | \$ 437,346 | \$ 191,229 |

(Both Columns reflect data in thousands)

Toward the end of FY 04, the Air Force clarified methods for recording work chargeable to outside organizations to better reflect the total amount of goods and services provided. This change in methodology results in higher reimbursable transactions which currently increased accounts receivable.

Note Reference

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

| | |
|----------------|---------------------|
| Note 6. | Other Assets |
|----------------|---------------------|

| As of March 31 | 2005 | 2004 |
|--|-----------------------------|-----------------------------|
| 1. Intragovernmental Other Assets | | |
| A. Advances and Prepayments | \$ 366,014,579.90 | \$ 288,895,556.18 |
| B. Total Intragovernmental Other Assets | \$ 366,014,579.90 | \$ 288,895,556.18 |
| 2. Nonfederal Other Assets | | |
| A. Outstanding Contract Financing Payments | \$ 11,269,645,012.46 | \$ 10,161,038,453.57 |
| B. Other Assets (With the Public) | 265,494,857.56 | 331,044,795.51 |
| C. Total Nonfederal Other Assets | \$ 11,535,139,870.02 | \$ 10,492,083,249.08 |
| 3. Total Other Assets | <u>\$ 11,901,154,449.92</u> | <u>\$ 10,780,978,805.26</u> |

Fluctuations

Advances and Prepayments, line 1.A., increased \$75,429 thousand. As reflected in the table below, accruals to match seller data shows the largest increase. This is the recording of government advances from either seller side actuals or an estimation technique for level 1 trading partners. The increase is due to the inclusion of level 1 government advances, which were not required to be recorded 2nd Quarter, FY 2004. Additionally, advances increased due to a change in procedure in which unidentified trading partners are no longer allocated to other government agencies but instead are identified as solely Air Force, pending further research. This also caused intra-Air Force eliminations to substantially increase.

Government advances before accruals in FY 2004 was a negative figure due to the General Accounting and Finance System-Rehost (GAFS-R) incorrectly posting refunds receivable as an advance instead of accounts receivable during 2nd Quarter, FY 2004. This resulted in federal advances being understated by \$7,768 thousand. The posting logic was corrected and advances are now properly reflected on the statements.

The comparison of 2nd Quarter, FY 2005 to FY 2004 for the components of Advances and Prepayments (in thousands) is detailed below:

| | FY 2005 | FY 2004 |
|-------------------------------------|----------------|----------------|
| Government advances before accruals | \$ 34 | \$ (7,611) |
| Accruals to match seller data | <u>949,322</u> | <u>307,082</u> |
| | \$ 949,356 | \$ 299,471 |
| Less intra-Air Force eliminations | <u>585,032</u> | <u>10,575</u> |
| Reported advances and prepayments | \$ 364,324 | \$ 288,896 |

Outstanding Contract Financing Payments, line 2.A., increased \$1,108,607 due to additional progress payments made for the F-22 as it experiences increased production and an increase in the allowable percentage of progress payments for new fixed price contracts.

Other Assets with the Public, line 2.B., decreased \$65,550 thousand due primarily to the General Accounting and Finance System-Rehost (GAFS-R) incorrectly posting refunds receivable as an advance instead of accounts receivable during 2nd Quarter, FY 2004. This resulted in nonfederal advances being overstated by \$91,048 thousand. The posting logic was corrected and advances are now properly reflected on the statements.

Relevant Information for Comprehension

Other Assets

The amount of \$265,495 thousand on line 2.B., Other Assets with the Public, is composed of \$102,216 thousand in travel advances, \$6,599 thousand in other advances to contractors, and \$156,680 thousand in advances to contractors as reported on the SF 1219, Statement of Accountability.

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

Outstanding Contract Financing Payments

The Air Force reports as advances and prepayment all outstanding financing payments for fixed-price contracts that are not based on percentage or stage of completion. Under the contract terms, the Air Force becomes liable only after the contractor delivers the goods in conformance with the contract terms. If the contractor does not deliver a satisfactory product, the Air Force is not obligated to reimburse the contractor for its cost, and the contractor is liable to repay the Air Force for the full amount of the outstanding contract finance payments.

Note Reference

See Note Disclosure 1.R., Significant Accounting Policies, for additional discussion on financial reporting requirements and Department of Defense policies governing other assets.

| | |
|----------------|---------------------------------------|
| Note 7. | Cash and Other Monetary Assets |
|----------------|---------------------------------------|

| As of March 31 | 2005 | 2004 |
|---|-------------------|-------------------|
| 1. Cash | \$ 139,008,075.91 | \$ 139,637,582.75 |
| 2. Foreign Currency (non-purchased) | 8,460,046.08 | 8,549,556.32 |
| 3. Total Cash, Foreign Currency, & Other Monetary Assets | \$ 147,468,121.99 | \$ 148,187,139.07 |

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

Relevant Information for Comprehension

The amounts reported for the Cash and Foreign Currency asset classes consist primarily of cash held by disbursing officers to carry out their paying, collecting, and foreign-currency accommodation exchange mission. The primary source of the amounts reported is the Standard Form 1219, Statement of Accountability, reported by the Department of Defense (DoD) disbursing officers.

The amount reported for the Foreign Currency asset class is valued using the Department of Treasury Prevailing Rate of Exchange, the most favorable rate available to the U.S. Government when acquiring foreign currency to make official disbursements and to provide currency for exchange of U.S. dollars for troops.

Note Reference

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

| | |
|----------------|---|
| Note 8. | Direct Loan and/or Loan Guarantee Programs |
|----------------|---|

As of March 31

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

Military Housing Privatization Initiative

Armament Retooling & Manufacturing Support Initiative

Direct Loans Obligated After FY 1991

As of March 31

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

Total Amount of Direct Loans Disbursed

As of March 31

| | 2005 | 2004 |
|---|----------------|----------------|
| Direct Loan Programs | | |
| Military Housing Privatization Initiative | \$ 0.00 | \$ 0.00 |
| Total | \$ 0.00 | \$ 0.00 |

Subsidy Expense for Post-1991 Direct Loans

As of March 31

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

Subsidy Rate for Direct Loans

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

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

As of March 31

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

Defaulted Guaranteed Loans from Post-1991 Guarantees

As of March 31

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

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

Liability for Post-1991 Loan Guarantees, Present Value

As of March 31

| | 2005 | 2004 |
|--|----------------|----------------|
| Loan Guarantee Program | | |
| 1. Military Housing Privatization Initiative | \$ 0.00 | \$ 0.00 |
| 2. Armament Retooling & Manufacturing Support Initiative | 0.00 | 0.00 |
| 3. Total | \$ 0.00 | \$ 0.00 |

Subsidy Expense for Post-1991 Loan Guarantees

As of March 31

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

Subsidy Rate for Loan Guarantees

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

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

As of March 31

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

Administrative Expense

As of March 31

| | 2005 | 2004 |
|---|---------|---------|
| 1. Direct Loans | | |
| Military Housing Privatization Initiative | \$ 0.00 | \$ 0.00 |
| Total | \$ 0.00 | \$ 0.00 |
| 2. Loan Guarantees | | |
| Military Housing Privatization Initiative | \$ 0.00 | \$ 0.00 |
| Armament Retooling & Manufacturing Support Initiative | 0.00 | 0.00 |
| Total | \$ 0.00 | \$ 0.00 |

| | |
|----------------|---------------------------------------|
| Note 9. | Inventory and Related Property |
|----------------|---------------------------------------|

| As of March 31 | 2005 | 2004 |
|---|-----------------------------|-----------------------------|
| 1. Inventory, Net | \$ 0.00 | \$ 0.00 |
| 2. Operating Materials & Supplies, Net | 48,643,476,455.88 | 52,202,386,284.22 |
| 3. Stockpile Materials, Net | 0.00 | 0.00 |
| 4. Total | <u>\$ 48,643,476,455.88</u> | <u>\$ 52,202,386,284.22</u> |

Inventory, Net

As of March 31

| | 2005 | | | 2004 | | Valu- ation Metho |
|---|---------------------------|--------------------------|----------------|----------------|------|-------------------------|
| | Inventory, Gross Value | Revaluation Allowance | Inventory, Net | Inventory, Net | | |
| 1. Inventory Categories | | | | | | |
| A. Available and Purchased for Resale | \$ 0.00 | \$ 0.00 | 0.00 | \$ 0.00 | 0.00 | |
| B. Held for Repair | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | |
| C. Excess, Obsolete, and Unserviceable | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | |
| D. Raw Materials | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | |
| E. Work in Process | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | |
| F. Total | \$ 0.00 | \$ 0.00 | 0.00 | \$ 0.00 | 0.00 | |

Legend for Valuation Methods:Adjusted LAC = Latest Acquisition Cost, adjusted for holding gains
holding gains and losses

SP = Standard Price

AC = Actual Cost

NRV = Net Realizable Value

O = Other

Operating Materials and Supplies, Net

As of March 31

| | 2005 | | | 2004 | | Valuation Method |
|--|----------------------|-----------------------|----------------------|----------------------|--|------------------|
| | OM&S Gross Value | Revaluation Allowance | OM&S, Net | OM&S, Net | | |
| 1. OM&S Categories | | | | | | |
| A. Held for Use | \$ 37,629,913,436.64 | \$ 0.00 | \$ 37,629,913,436.64 | \$ 39,498,154,299.33 | | |
| B. Held for Repair | 11,013,563,019.24 | 0.00 | 11,013,563,019.24 | 12,704,231,984.89 | | |
| C. Excess, Obsolete, and Unserviceable | 1,082,180,807.15 | (1,082,180,807.15) | 0.00 | 0.00 | | |
| D. Total | \$ 49,725,657,263.03 | \$ (1,082,180,807.15) | \$ 48,643,476,455.88 | \$ 52,202,386,284.22 | | |

Legend for Valuation Methods:

Adjusted LAC = Latest Acquisition Cost adjusted for holding gains and losses

SP= Standard Price

AC= Actual Cost

NRV = Net Realizable Value

O = Other

Fluctuations

The \$1,690,669 thousand decrease in 'Held for Repair' is the result of a policy change which resulted in Aircraft Electronics POD being reclassified from OM&S to General PP&E. Additionally, in FY 2004, SBSS was reported manually and not broken out into the three categories. With the change from manual to direct interface, the SBSS now reports by category. Also, the decrease can be attributed to repairs completed in the Munitions category.

Information related to OM&S

General Composition of OM&S

OM&S include spare and repair parts, ammunition, tactical missiles, spare centrally managed aircraft engines, and uninstalled cruise missile motors.

Balances

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

Decision Criteria for Identifying the Category to Which OM&S Items Are Assigned

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

The category Held for Use includes all issuable materials and is coded within each supply or inventory system as condition codes A-D.

The category Excess, Obsolete, and Unserviceable includes all material assigned condition codes H, P, S, or V.

The Category Held for Repair relates to impaired assets and includes all other condition codes as defined by the Military Standard Transaction Reporting and Accounting Procedures Manual (DoD 4000.25-2-M).

Changes in the Criteria for Identifying the Category to Which OM&S Items Are Assigned

As stated above, the category Held for Use includes all issuable material, and the category Held for Repair includes all economically repairable material. Before FY 2002, the Department of Defense (DoD) categorized potentially redistributable material, regardless of condition, as Excess, Obsolete, and Unserviceable.

To date, the Air Force has partially implemented three systems to report “moving average cost,” the DoD-approved methodology for reporting historical cost within any of the supply or inventory accounting systems for OM&S. (In only one system was the beginning balance validated). Most OM&S assets are in systems not yet converted to moving average cost so are still valued at standard price, with an allowance for Excess, Obsolete, and Unserviceable. Under current DoD policy, no allowance is made for serviceable ready-to-issue items (category Held for Use). An allowance equal to 100 percent of standard price, however, is made for the category Excess, Obsolete, and Unserviceable. This allowance results in a net book value of zero, which is considered appropriate because the items are coded condemned and, therefore, have no intrinsic value to the Air Force. The category Held for Repair represents suspended, unserviceable (but repairable) items which have a value to the Air Force but whose value is less than that of the Held for Use items and greater than that of the Excess, Obsolete and Unserviceable items. To date, the Office of the Secretary of Defense has not provided sufficient guidance to the Air Force on the methodology for computing an allowance for the Held for Repair category; therefore, Held for Repair is reported at full standard price.

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

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

Operating Materials and Supplies (OM&S) Value

The OM&S data reported on the financial statements are derived from logistics systems designed for material management purposes. Some of these systems do not maintain the historical cost data

necessary to comply with the valuation requirements of the Statement of Federal Financial Accounting Standards (SFFAS) No. 3, “Accounting for Inventory and Related Property.”

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

In general, the Air Force is using the consumption method of accounting for OM&S, since OM&S is defined in the SFFAS No. 3 as material that has not yet been issued to the end user. Once issued, the material is expensed. According to federal accounting standards, the consumption method of accounting should be used to account for OM&S unless (1) the amount of OM&S is not significant, (2) OM&S are in the hands of the end-user for use in normal operations, or (3) it is cost-beneficial to expense OM&S when purchased (purchase method).

Note Reference

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

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

Other Air Force Disclosures

In the past, the Air Force provided only minimal OM&S accounting data that could be used to prepare the financial statements but has made considerable strides in improving the systems to provide actual transactions for completing the financial statements. However in some cases, the data provided still consists of only beginning and ending balances for each of the asset accounts Held for Use; Excess, Obsolete, Unserviceable; and Held for Repair. Without the required additional data (acquisitions, transfers in, amounts consumed, transfers out, trading partner data, etc), the Defense Finance and Accounting Service (DFAS) could only report the net change between prior-period ending balances and the values reported as current-period ending balances.

Although the Air Force OM&S systems, in most cases, capture some trading partner data at the transaction level, no electronic interfaces exist between the Air Force OM&S feeder systems, the DFAS accounting systems, other DoD services, and other federal agencies for reporting the data for all items transferred in and out. Consequently, intragovernmental transactions (trading partner data) could not always be reconciled. The Air Force and DFAS are currently developing processes, methodologies and standard electronic interfaces that will allow intragovernmental transactions to be reported monthly to the General Accounting and Finance System – Rehost.

Stockpile Materials, Net

As of March 31

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

Legend for Valuation Methods:

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

NRV = Net Realizable Value
 O = Other

| | |
|-----------------|------------------------------|
| Note 10. | General PP&E, Net |
|-----------------|------------------------------|

| As of March 31 | 2005 | | | | | 2004 |
|--|---|-----------------|------------------------------|--|------------------------------|------------------------------|
| | Depreciation/ Amortization Method | Service Life | Acquisition Value | (Accumulated Depreciation/ Amortization) | Net Book Value | Prior FY Net Book Value |
| 1. Major Asset Classes | | | | | | |
| A. Land | N/A | N/A | \$ 431,702,002.17 | N/A | \$ 431,702,002.17 | \$ 415,762,941.20 |
| B. Buildings, Structures, and Facilities | S/L | 20 Or 40 | 42,179,283,804.03 | \$ (24,656,099,796.23) | 17,523,184,007.80 | 17,392,651,938.01 |
| C. Leasehold Improvements | S/L | lease term | 0.00 | 0.00 | 0.00 | 0.00 |
| D. Software | S/L | 2-5 Or 10 | 23,806,209.00 | (24,096.00) | 23,782,113.00 | 23,782,113.00 |
| E. General Equipment | S/L | 5 or 10 | 35,709,167,240.47 | (27,862,104,100.26) | 7,847,063,140.21 | 5,019,706,801.09 |
| F. Military Equipment | S/L | Various | 305,860,000,000.00 | (215,620,000,000.00) | 90,240,000,000.00 | 88,460,000,000.00 |
| G. Assets Under Capital Lease | S/L | lease term | 459,265,000.60 | (295,504,253.02) | 163,760,747.58 | 188,025,052.45 |
| H. Construction-in-Progress | N/A | N/A | 3,719,301,008.22 | N/A | 3,719,301,008.22 | 2,402,814,792.67 |
| I. Other | | | 253,587.00 | 0.00 | 253,587.00 | 1,555,982.29 |
| 2. Total General PP&E | | | \$ 388,382,778,851.49 | \$ (268,433,732,245.51) | \$ 119,949,046,605.98 | \$ 113,904,299,620.71 |

¹ Note 15 for additional information on Capital Leases

Legend for Valuation Methods:

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

Fluctuations

The overall increase in General Equipment of \$2,827,356 thousand is the result of a policy change which resulted in \$740,624 thousand Aircraft Electronics POD being reclassified from OM&S to General PP&E. Additionally, the Air Force has determined that all equipment reported by the Air Force Equipment Management System (AFEMS) is now considered to be General PP&E which was previously considered to be part of Military Equipment. This resulted in an additional increase of \$2,559,376 thousand. These increases were offset by a reduction of \$472,644 to correct an accounting error that was reflected on the 2nd Quarter FY 2004 statements that was subsequently corrected.

The Construction-in-Progress on line 1.H. increased \$1,316,486 thousand due to an increase in construction projects started and not completed.

The Other asset class on line 1.I. decreased by \$1,302 thousand. The Other category represents the timing factor inherent in timber harvesting. The timber markets, driven by supply and demand, are volatile and fluctuate. Timber sale contracts are awarded at irregular intervals, with some contracts held back until the market improves. Similarly, when buyers pay for just the timber they cut, they may hold off when markets are bad and cut more when markets are good. Weather conditions also influence the flow of timber and revenue.

Relevant Information for Comprehension

The Federal Accounting Standards Advisory Board issued Statement of Federal Financial Accounting Standards No. 23, "Eliminating the Category National Defense Property, Plant and Equipment," in May 2003. This standard, which became effective for accounting periods after September 30, 2002, establishes Generally Accepted Accounting Principles (GAAP) for valuing and reporting military equipment (e.g., aircraft, satellites, and intercontinental ballistic missiles) in federal financial statements. The standard requires the capitalization and depreciation of the cost of military equipment, including the cost of modifications and upgrades. The Department of Defense has determined that it is not practicable at this time to accumulate sufficient information from internal records to value military equipment in accordance with GAAP. The Department is currently working to revise its accounting processes and systems to support the informational needs of management and compliance with GAAP. In the interim, the Department will base the value of military equipment for financial statement presentation purposes on data provided by the Bureau of Economic Analysis (BEA) at the Department of Commerce.

The value of the Bureau of Economic Analysis (BEA) data provided by the DoD to the Air Force for inclusion in the financial statements for the 2nd Quarter, 2005 amounted to approximately \$305,860,000 thousand less accumulated depreciation of \$215,620,000 thousand for a net realized book value of \$90,240,000 thousand.

The data provided by the BEA consists of investment and net book value data for 84 groups of equipment such as aircraft, ships, and combat vehicles. The Department adjusts BEA data to eliminate equipment items (such as spares, munitions, and inventory items) that are not accounted for as military equipment. Such items are accounted for and reported as Inventory and Related Property.

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

Other Air Force Disclosures

For the 2nd Quarter, FY 2005 reports, the Air Force used some FY 2002 ending data for (ST/STE) but did use actual data for the B2 aircraft. The FY 2002 values were still being used for all other (ST/STE) because the two systems previously used to report ST/STE have been turned off and are scheduled to be replaced by Air Force Equipment Management System (AFEMS) in FY 2005.

Earned Revenue from the Public increased \$1,169,612 thousand on the Statement of Net Cost primarily due to other gains reported by the Air Force Equipment Management System (AFEMS) for Air National Guard equipment found on base that have not been reported previously. Physical inventories of systems, such as for Special Tools and Test Equipment, identified assets that were previously not recorded in property records.

The value of the Air Force internal use software reported for 2nd Quarter FY 2005 is the same dollar value that was reported in previous financial statements. On prior reporting cycles, the Air Force used a rudimentary manual process to collect these values, however this process is no longer considered reliable. The Air Force is working this issue and estimates that a systematic process will be established to both capture and report internal used software in FY 2005. The value of the Air Force's General PP&E real property in the possession of contractors is included in the values reported above for the Major Asset Classes of Land and Buildings, Structures, and Facilities. The value of General PP&E personal property (Major Asset Classes of Software and Equipment) does not include all of the General PP&E above the DoD capitalization threshold in the possession of contractors. The net book amount of

AF GF

such property is immaterial in relation to the total General PP&E net book value. In accordance with a strategy approved by the OMB, the General Accounting Office, and the Inspector General, DoD, the Department is developing new policies and a contractor-reporting process to capture General PP&E information for future reporting purposes in compliance with GAAP.

Note Reference

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

| Assets Under Capital Lease | | | | |
|--|------|------------------|------|------------------|
| As of March 31 | 2005 | | 2004 | |
| 1. Entity as Lessee, Assets Under Capital Lease | | | | |
| A. Land and Buildings | \$ | 459,265,000.60 | \$ | 408,539,654.46 |
| B. Equipment | | 0.00 | | 958,167.69 |
| C. Other | | 0.00 | | 0.00 |
| D. Accumulated Amortization | | (295,504,253.02) | | (221,472,769.70) |
| E. Total Capital Leases | \$ | 163,760,747.58 | \$ | 188,025,052.45 |

The Air Force is the lessee in eleven capital leases. These leases are for military family housing acquired through Section 801 Family Housing Program. The leased items are capitalized and reported as an asset when the costs of the items exceed the capitalization threshold. Leased items not meeting the capitalization threshold are expensed. All leases originating prior to FY 1992 are funded on a fiscal-year basis. Six of the current military family housing leases originated before FY 1992.

Fluctuations

The increase of \$50,726 thousand in Land and Building and \$43,754 increase in Accumulated Amortization in Capital Leases is the result of a change in methodology for the use of interest rates that applies to the individual leases. The Air Force previously used the interest rate provided with each of the eleven capital leases. This interest rate did not accurately provide the cost of money to compute fair market value. The current interest rate used reflects the appropriate government rate which best reflects the governments cost of borrowing, using the historical rates from the Federal Reserve. The new change was coordinated between the Air Force and OSD.

| | |
|-----------------|---|
| Note 11. | Liabilities Not Covered by Budgetary Resources |
|-----------------|---|

| As of March 31 | 2005 | 2004 |
|--|-----------------------------|-----------------------------|
| 1. Intragovernmental Liabilities | | |
| A. Accounts Payable | \$ 0.00 | \$ 0.00 |
| B. Debt | 0.00 | 0.00 |
| C. Other | 874,923,147.69 | 533,073,541.49 |
| D. Total Intragovernmental Liabilities | \$ 874,923,147.69 | \$ 533,073,541.49 |
| 2. Nonfederal Liabilities | | |
| A. Accounts Payable | \$ 145,192,078.71 | \$ 3,211,028.00 |
| B. Military Retirement Benefits and Other Employment-Related Actuarial Liabilities | 1,163,442,240.00 | 1,262,267,550.00 |
| C. Environmental Liabilities | 6,520,072,090.37 | 6,550,342,413.53 |
| D. Loan Guarantee Liability | 0.00 | 0.00 |
| E. Other Liabilities | 2,686,315,757.84 | 3,244,553,077.77 |
| F. Total Nonfederal Liabilities | \$ 10,515,022,166.92 | \$ 11,060,374,069.30 |
| 3. Total Liabilities Not Covered by Budgetary Resources | \$ 11,389,945,314.61 | \$ 11,593,447,610.79 |
| 4. Total Liabilities Covered by Budgetary Resources | \$ 10,644,336,070.22 | \$ 11,609,652,824.22 |
| 5. Total Liabilities | \$ 22,034,281,384.83 | \$ 23,203,100,435.01 |

Definitions

Liabilities Not Covered and Covered by Budgetary Resources – These are liabilities that are not considered covered by realized budgetary resources as of the balance sheet date. Budgetary resources include the following:

- New budget authority
- Spending authority from offsetting collections (credited to an appropriation or fund account)
- Recoveries of unexpired budget authority through downward adjustments of prior-year obligations
- Unobligated balances of budgetary resources at the beginning of the year or net transfers of prior-year balances during the year
- Borrowing authority or permanent indefinite appropriations that have been enacted and signed into law as of the balance sheet date, provided that the Office of Management and Budget (OMB) can apportion the resources without first meeting a contingency or without additional action by the Congress.

Liabilities Covered by Budgetary Resources – These are resources the reporting entity incurred that are covered by realized budget resources as of the balance sheet date. Budgetary resources encompass not only new budget authority but also other resources available to cover liabilities for specified purposes in a given year. Available budgetary resources include the following:

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

Fluctuations and Abnormalities

The increase in Accounts Payable – Cancelled Appropriations is due to a change in the USSGL crosswalk. USSGL 2960, Accounts Payable from Cancelled Appropriations, is now reported on the Accounts Payable lines of the Balance Sheet instead of Other Liabilities. The FY 2004 balance of \$3,211 thousand was processed to the wrong USSGL and has since been corrected.

Information Related to Liabilities Not Covered by Budgetary Resources

Other Liability Disclosures

Other Intragovernmental Liabilities Not Covered by Budgetary Resources consists of \$234,173 thousand in Federal Employees' Compensation Act (FECA) reimbursement to the Department of Labor, \$31,186 thousand in unemployment compensation, and \$609,564 thousand in custodial liabilities.

Other Nonfederal Liabilities Not Covered by Budgetary Resources consists of \$42,180 thousand in capital lease liabilities, \$301,506 thousand in contingent liabilities, \$2,337,036 thousand in accrued annual leave liabilities for military and civilians, and \$934 thousand in accrued interest liability.

Note Reference

For Additional Line Item discussion, see:

- Note 12, Accounts Payable
- Note 13, Debt
- Note 14, Environmental Liabilities and Disposal Liabilities
- Note 15, Other Liabilities
- Note 16, Commitments and Contingencies
- Note 17, Military Retirement Benefits and Other Employment Related Actuarial Liabilities

| | |
|-----------------|-------------------------|
| Note 12. | Accounts Payable |
|-----------------|-------------------------|

| As of March 31 | 2005 | | | 2004 |
|--|----------------------------|--|----------------------------|----------------------------|
| | Accounts Payable | Interest, Penalties, and Administrative Fees | Total | Total |
| 1. Intragovernmental Payables | \$ 1,692,869,764.70 | \$ N/A | \$ 1,692,869,764.70 | \$ 1,669,557,861.90 |
| 2. Non-Federal Payables (to the Public) | 6,703,865,262.24 | 0.00 | 6,703,865,262.24 | 5,851,267,290.10 |
| 3. Total | <u>\$ 8,396,735,026.94</u> | <u>\$ 0.00</u> | <u>\$ 8,396,735,026.94</u> | <u>\$ 7,520,825,152.00</u> |

The Intragovernmental Payables category consists of amounts owed to other federal agencies for goods or services ordered and received but not yet paid for. Interest, penalties, and administrative fees are not applicable to intragovernmental payables. As a result of guidance from Treasury, Judgment Fund Liabilities are now included in Intragovernmental Payables. The Nonfederal Payables (to the Public) category consists of payments to nonfederal governmental entities

Fluctuations

Accounts Payable – Public increased by \$ 852,598 thousand. This can be attributed to a \$1,788,714 thousand increase in Aircraft Procurement - Air Force Materiel Command resulting from production increases for the F-22, C-130J, Predator and final delivery of the Joint STARS aircraft. The remaining \$ 936,116 thousand fluctuation is the result of a \$1,037,434 thousand decrease in classified Other Procurement – Air Force Special Programs.

Accounts Payable – Intragovernmental increased \$23,312 thousand. The fluctuation associated with Intragovernmental accounts payable is the direct result of the elimination process which requires the accrual of accounts payable to agree with Air Force trading partner seller data. The increase is primarily attributable to recording level 1 accounts payable based on actual seller side data provided by the agency or using an estimation technique for those agencies that did not provide actuals.

Judgment Fund liabilities for the 2nd Quarter FY 2005 in the amount of \$105,013 thousand decreased by \$97,305 thousand. This was a result of contractor claims under the Contract Disputes Act on Air Force contracts that have been adjudicated by a court or a board in favor of the contractor. Initially, Treasury pays the monetary awards to the contractor. The Air Force must subsequently reimburse the Treasury's Judgment Fund for the amount that was paid to the contractors. The amount reported as the total Judgment Fund liability is the amount owed as of March 31, 2005. This amount includes approximately \$1,136 thousand owed for Judgment Fund liabilities that resulted because of the Notification and Federal Employee Antidiscrimination and Retaliatory Act of 2002. This amount can change daily and can fluctuate substantially due to new billings by the Treasury and payments made to the Treasury by DFAS and the U.S. Army Corps of Engineers on behalf of the Air Force.

Intragovernmental Eliminations

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

Comparison prior to eliminations:

| | Mar 2005 | Mar 2004 | \$ Change |
|--|-----------------|-----------------|------------------|
| Intragovernmental accounts payable before eliminations | \$2,221,534 | \$1,773,283 | \$ 448,251 |
| Less Intra-Air Force eliminations | <u>528,664</u> | <u>103,725</u> | <u>(424,939)</u> |
| Total | \$1,692,870 | \$1,669,558 | \$ 23,312 |

(All data in thousands)

Allocation of Undistributed Disbursements

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

Note Reference

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

| | |
|-----------------|-------------|
| Note 13. | Debt |
|-----------------|-------------|

| As of March 31 | 2005 | | | 2004 |
|---------------------------------------|-------------------|----------------|----------------|----------------|
| | Beginning Balance | Net Borrowings | Ending Balance | Ending Balance |
| 1. Agency Debt | | | | |
| A. Debt to the Treasury | \$ 0.00 | \$ 0.00 | \$ 0.00 | \$ 0.00 |
| B. Debt to the Federal Financing Bank | 0.00 | 0.00 | 0.00 | 0.00 |
| C. Total Agency Debt | \$ 0.00 | \$ 0.00 | \$ 0.00 | \$ 0.00 |
| 2. Total Debt | \$ 0.00 | \$ 0.00 | \$ 0.00 | \$ 0.00 |

Note Reference

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

| | |
|-----------------|---|
| Note 14. | Environmental Liabilities and Disposal Liabilities |
|-----------------|---|

| As of March 31 | 2005 | | | 2004 |
|--|--------------------------|----------------------------|----------------------------|----------------------------|
| | Current Liability | Noncurrent Liability | Total | Total |
| 1. Environmental Liabilities – Non Federal | | | | |
| A. Accrued Environmental Restoration (DERP funded) Costs: | | | | |
| 1. Active Installations-- Environmental Restoration (ER) | \$ 382,368,000.00 | \$ 3,657,579,807.58 | \$ 4,039,947,807.58 | \$ 4,056,865,000.00 |
| 2. Active Installations--ER for Closed Ranges | 15,000,000.00 | 1,329,856,000.00 | 1,344,856,000.00 | 838,172,100.00 |
| 3. Formerly Used Defense Sites (FUDS) -- ER | 0.00 | 0.00 | 0.00 | 0.00 |
| 4. FUDS--ER for Transferred Ranges | 0.00 | 0.00 | 0.00 | 0.00 |
| B. Other Accrued Environmental Costs (Non-DERP funds) | | | | |
| 1. Active Installations-- Environmental Corrective Action | 0.00 | 175,968,896.17 | 175,968,896.17 | 198,730,146.31 |
| 2. Active Installations-- Environmental Closure Requirements | 6,177,000.00 | 106,106,000.00 | 112,283,000.00 | 66,454,200.00 |
| 3. Active Installations-- Environ.Response at Active Ranges | 0.00 | 0.00 | 0.00 | 0.00 |
| 4. Other | 0.00 | 0.00 | 0.00 | 0.00 |
| C. Base Realignment and Closure (BRAC) | | | | |
| 1. BRAC Installations-- Environmental Restoration (ER) | 0.00 | 1,292,367,000.73 | 1,292,367,000.73 | 1,825,092,522.44 |
| 2. BRAC Installations--ER for Transferring Ranges | 0.00 | 0.00 | 0.00 | 0.00 |
| 3. BRAC Installations-- Environmental Corrective Action | 7,538,606.94 | 126,228,436.43 | 133,767,043.37 | 133,804,496.00 |
| 4. Other | 0.00 | 0.00 | 0.00 | 0.00 |
| D. Environmental Disposal for Weapons Systems Programs | | | | |
| 1. Nuclear Powered Aircraft Carriers | 0.00 | 0.00 | 0.00 | 0.00 |
| 2. Nuclear Powered Submarines | 0.00 | 0.00 | 0.00 | 0.00 |
| 3. Other Nuclear Powered Ships | 0.00 | 0.00 | 0.00 | 0.00 |
| 4. Other National Defense Weapons Systems | 0.00 | 0.00 | 0.00 | 50,592,326.00 |
| 5. Chemical Weapons Disposal Program | 0.00 | 0.00 | 0.00 | 0.00 |
| 6. Other | 0.00 | 0.00 | 0.00 | 0.00 |
| 2. Total Environmental Liabilities: | \$ 411,083,606.94 | \$ 6,688,106,140.91 | \$ 7,099,189,747.85 | \$ 7,169,710,790.75 |

Fluctuations

New cost estimates for all environmental liabilities are only submitted at year-end. Quarterly changes to the liability figure are a result of current-year expenditures.

Accrued Environmental Restoration Costs (DERP-funded) Active Installations – Environmental Restoration for Closed Ranges increased \$506,684 thousand. The total number of all sites at September 30, 2003 was 260. The

comparable number of sites for September 30, 2004 was 292, which indicates the increase expected. However, this total number of sites includes sites that are closed, as well as active sites. The operation closed 52 sites during FY 2004, which leaves active sites at 240 as of September 30, 2004. The number of active sites at September 30, 2003 was 210. Because of the relatively new nature of the munitions response reporting for closed ranges and expected growth in sites, the Air Force believes this liability will continue to grow significantly for several years.

Other Accrued Environmental Costs (Non-DERP funds) Active Installations - Environmental Corrective Action decreased \$22,761 thousand. Resource Conservation and Recovery Act (RCRA) corrective action sites are defined by the Environmental Protection Agency as Solid Waste Management Units (SWMU). SWMUs are not determined in a scientific manner and may arise from any indication of potential pollution. Therefore, there are a high number of SWMUs. Superficial investigation generally leads to the conclusion that there is no significant pollution at the SWMU. The amount of the liability fluctuates greatly from year-to-year as further investigation results in significant changes in cost estimates. These changes result from the additional information gained in each step of the cleanup process and the relatively few sites that actually require significant cleanup costs.

Other Accrued Environmental Costs (Non-DERP funds) Active Installations - Environmental Closure Requirements increased \$45,829 thousand due to a change in the amortization computation for Underground Storage Tanks (USTs) and Landfills. Amortization of USTs is now based on the year the facility is placed in service instead of the planned year for closure. Additionally, the inventory of Landfills and USTs has expanded as reporting continues to improve. Likewise, units reported have moved to the use of the Remedial Action Cost Engineering and Requirements System (RACER) as the estimating tool, which changes the cost estimates from previous periods. The Air Force expects continued increase in the liability for closures as the inventory of facilities with a liability continues to increase and cost estimates are changed to the verified, validated, and approved cost methodology of RACER. During FY 2005, the liability for Treatment, Storage, and Disposal Facilities (TSDFs) is expected to increase significantly as the amortization computation is changed to the year the facility was placed in service instead of the planned closure year.

Base Realignment and Closure (BRAC) Installations – Environmental Restoration decreased \$532,726 thousand due to a new cost estimating and reporting policy being used by the active Air Force. In the past, site cost estimates were run until the duration of the remediation, for example, FY 2300. This policy was changed to 25 years of Remediation Action Operation (RA-O) with a 5 year Long Term Monitoring (LTM) cost estimate that means the site cost estimate would be cut-off by FY 2034.

Optimization of existing systems contributed to the decrease. This is a systematic approach for evaluating and improving site remediation processes by reducing risk and enhancing system performance, minimizing both short and long term costs, assessing decision logic to reach site cleanup goals, and accelerating site closure. Also, a portion of the cost reduction is due to privatization, in which the government cleanup function has been converted to the private sector. Additionally, the 1st Quarter, FY 2004 ending liability balance for Environmental Restoration was in error. Environmental Corrective Action requirements were added to the Environmental Restoration line as well as being reported on the Environmental Corrective Action line. This amount totaled \$139,956 thousand. The new ending Environmental Restoration balance includes the correction, contributing to the reported decrease.

Environmental Disposal for Weapons Systems Programs - Other National Defense Weapons Systems decreased \$50,592 thousand due to a policy change that transferred accounting responsibility for all disposal costs to the Department of the Army for inclusion in their financial statements. The Air Force no longer reports this activity.

General Disclosures

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

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

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

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

Included in the environmental restoration liability for active installations are 27 sites that represent building demolition and debris removal costs of approximately \$56,500 thousand at September 30, 2004. Building demolition and debris removal costs represent a mixture of environmental and nonenvironmental costs that are not separated due to their joint nature.

Accrued Environmental Restoration Costs (DERP funded) Active Installations - Environmental Restorations for Closed Ranges:

The environmental cleanup of military ranges is governed by the Military Munitions Rule in 40 CFR 266.201. Environmental cleanup liabilities on ranges refer only to munitions related activities. Other actions are captured under the DERP, BRAC, and non-DERP, non-BRAC environmental cleanup categories. Additionally, environmental cleanup liabilities are reported only for closed ranges. As of September 30, 2002, the Air Force had 509 ranges, of

which 268 were considered operational ranges. The environmental cleanup liability is reported only for closed ranges that numbered 260 as of September 30, 2003 (236 closed, 18 transferred, and 6 transferring).

Environmental cleanup areas within a closed range are referred to as Munitions Response Areas (MRAs). As studies are done to find munitions-related contamination on closed ranges, the number of sites is expected to rise. As of September 30, 2003, there were 210 active areas on closed ranges resulting in an estimated environmental cleanup liability of \$838,172 thousand, increasing to 240 active areas with an estimated cost of \$1,344,856 thousand by September 30, 2004. As investigations progress, the number of sites will increase to reflect specific areas of pollution. The Air Force expects the number of sites reported to increase as pollution is discovered and sites are defined in areas less than the total boundary of the closed range. For example, one closed range of 100 acres may become three sites: one of five acres with pollution A, one of 15 acres with pollution B, and the remaining 80 acres with no pollution found. Thus, one closed range can become three sites, each with its own cost-to-complete cleanup estimate. The sum of the sites' costs-to-complete cleanup becomes the environmental cleanup liability for closed ranges. The environmental cleanup for closed ranges is in its infancy, and the total liability is expected to increase significantly over the coming years as investigations progress. Current policy is to investigate all closed ranges by the end of 2007.

Although there are no stated standards for the environmental cleanup of closed ranges, the Air Force has implemented studies to determine the extent of pollution from munitions. It is expected that there will be significant changes in range cleanup standards that eventually will be applied on a case-by-case basis for munitions-response requirements.

As investigations progress, it is expected the environmental cleanup liability for closed ranges will increase materially. The liability for environmental cleanup will reflect direct costs. Also, the lack of expense history for range environmental cleanup makes it impossible to estimate current liabilities reliably for some time. The current liability reflects the amount contained in the President's Budget that shows the expected activity for the next fiscal year.

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

Environmental closure liabilities are incurred under RCRA with the cost-to-complete closure reported for RCRA facilities. Cost estimates are prepared under assumptions of a clean close, as defined in the RCRA law and estimated using RACER in the absence of a specific contract cost or bid. The specific facilities reported cover landfills, Underground Storage Tanks (USTs), and Treatment, Storage and Disposal Facilities (TSDFs).

Disposal liabilities are presented as an accrued amount for the life of the RCRA facilities, and the total liability is presented in the year-end narrative. The accounting standard requires full cost be recognized for closure liability. Closure liabilities recognized by the Air Force cover only direct costs. No cost accounting exists to determine indirect closure costs. This is not considered material in the cost estimates because indirect costs incurred would not happen for at least 20 years and, in many cases, far beyond 20 years. The present value of such costs would be negligible in recognition of closure liabilities.

There are no material changes in environmental closure liabilities on less than an annual basis because revaluation and addition of new sites occurs in the last quarter of the year in preparation for the budget process. Because environmental closure liabilities are estimated in the last quarter of the year, new closure sites recognized in the last quarter of the year and no accounting process to capture environmental closure expenses, there is no material change in environmental closure liabilities on less than an annual basis. The total amortized annual portion of the liability estimate is recognized in the fiscal yearend liability, therefore, there is no change in the amortized liability amount on a quarterly basis. There is no value to the amortization of the estimated liability more frequently than annually because there is no cash impact for such recognition and there is no funding requirement in connection with the liability amortization. Because the function does not generate any revenues it is not essential to match costs against revenues to establish net income.

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

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

UST closure liabilities are based on an assumed life of 20 years and two years of monitoring with closure costs estimated for a clean close. (*Clean close* is defined in the federal regulations.) TSDF closure liabilities are based on an assumed life of 30 years. Disposal costs include two years of monitoring with closure costs estimated for a clean close.

The unamortized and amortized liability amount is disclosed below. The amortized liability is the amount recognized on the financial statements.

| | FY 2004 (amts in thousands) | |
|---|--------------------------------|-----------|
| | Unamortized | Amortized |
| Treatment, Storage, and Disposal Facilities (TSDFs) | \$18,193 | \$5,361 |
| Landfills | \$204,590 | \$64,822 |
| Underground Storage Tanks (USTs) | \$59,229 | \$42,100 |
| Total | \$282,012 | \$112,283 |

Base Realignment and Closure (BRAC) Installations - Environmental Restoration and Environmental Corrective Action:

The Air Force Real Property Agency (AFRPA) estimates their total environment liability only at year-end. Quarterly changes to the liability figure are a result of current-year expenditures. This amount includes all cleanup requirements to meet applicable laws and regulatory requirements and to transfer property. However, this amount does not include Land Use Control/Institutional Control costs beyond system operations associated with property transfer. Cost estimates are assigned to current operating periods using RACER.

Reporting of Estimates

Our financial statements are prepared in accordance with Federal Generally Accepted Accounting Principles. These accounting principles require us to make certain estimates, judgments, and assumptions that we believe are reasonable based upon information available to us at the time. These estimates, judgments, and assumptions can affect the reported amounts of environmental liabilities as of the date of the financial statements.

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

Note Reference

For regulatory discussion on environmental liabilities, see DoD FMR, Volume 6B, Chapter 10, Paragraph 1016 and Volume 4, Chapters 13 and 14.

Note 15. Other Liabilities

| As of March 31 | 2005 | | | 2004 |
|---|----------------------------|--------------------------|----------------------------|----------------------------|
| | Current Liability | Noncurrent Liability | Total | Total |
| 1. Intragovernmental | | | | |
| A. Advances from Others | \$ 494,492,503.90 | \$ 0.00 | \$ 494,492,503.90 | \$ 999,103,865.83 |
| B. Deposit Funds and Suspense Account Liabilities | 11,894,994.96 | 0.00 | 11,894,994.96 | (128,543,253.44) |
| C. Disbursing Officer Cash | 304,148,121.99 | 0.00 | 304,148,121.99 | 220,682,512.64 |
| D. Judgment Fund Liabilities | 0.00 | 0.00 | 0.00 | 201,182,196.79 |
| E. FECA Reimbursement to the Department of Labor | 129,228,861.78 | 104,944,841.24 | 234,173,703.02 | 239,622,048.74 |
| F. Other Liabilities | 686,703,739.92 | 1,113,762.00 | 687,817,501.92 | 693,906,726.06 |
| G. Total Intragovernmental Other Liabilities | \$ 1,626,468,222.55 | \$ 106,058,603.24 | \$ 1,732,526,825.79 | \$ 2,225,954,096.62 |
| 2. Nonfederal | | | | |
| A. Accrued Funded Payroll and Benefits | \$ 630,936,651.46 | \$ 0.00 | \$ 630,936,651.46 | \$ 1,432,080,559.11 |
| B. Advances from Others | 79,445,936.32 | 0.00 | 79,445,936.32 | 53,692,968.75 |
| C. Deferred Credits | 0.00 | 0.00 | 0.00 | 0.00 |
| D. Deposit Funds and Suspense Accounts | 75,236,480.95 | 0.00 | 75,236,480.95 | 63,353,199.88 |
| E. Temporary Early Retirement Authority | 508,530.53 | 263,000.00 | 771,530.53 | 1,758,330.33 |
| F. Nonenvironmental Disposal Liabilities | | | | |
| (1) National Defense PP&E (Nonnuclear) | 0.00 | 0.00 | 0.00 | 0.00 |
| (2) Excess/Obsolete Structures | 0.00 | 0.00 | 0.00 | 389,472,500.00 |
| (3) Conventional Munitions Disposal | 0.00 | 0.00 | 0.00 | 5,879,598.00 |
| (4) Other | 0.00 | 0.00 | 0.00 | 0.00 |
| G. Accrued Unfunded Annual Leave | 2,337,035,488.49 | 0.00 | 2,337,035,488.49 | 2,121,294,210.97 |
| H. Capital Lease Liability | 34,924,059.44 | 181,597,313.41 | 216,521,372.85 | 263,801,403.68 |
| I. Other Liabilities | 934,267.77 | 301,505,815.88 | 302,440,083.65 | 693,010,074.92 |
| J. Total Nonfederal Other Liabilities | \$ 3,159,021,414.96 | \$ 483,366,129.29 | \$ 3,642,387,544.25 | \$ 5,024,342,845.64 |
| 3. Total Other Liabilities | \$ 4,785,489,637.51 | \$ 589,424,732.53 | \$ 5,374,914,370.04 | \$ 7,250,296,942.26 |

Intragovernmental Fluctuations

The \$504,611 thousand decrease in Advances from Others on Line 1.A. is due to the timing of the receipt and execution of orders mainly in the Research, Development, Test and Evaluation (RDT&E) classified program, causing variations.

The increase in Deposit Funds and Suspense Accounts is due to an erroneous posting of suspense account data to nonfederal during 2nd Quarter FY 2004. DDRS-B, which was first used during 1st Quarter FY 2004 to import the data into DDRS-AFS, contained the wrong crosswalk information. The data should have been reported as intragovernmental. The true fluctuation is an increase mainly attributable to suspense account 57 F 3875 that includes federal income tax withholdings and withheld FICA.

During FY 04, Disbursing Officer Cash was \$295,767 thousand. However, \$75,084 thousand was not identified on the trial balance under the attribute of Disbursing Officers Cash. Because of this, that portion was included in the amount on Line 1.A. Therefore the true variance between periods is only an increase of 3 percents.

The decrease in Judgment Fund Liabilities is a result of guidance received from Treasury requiring information to be included in Accounts Payable, Footnote 12.

Other Liabilities

The amount of \$687,818 thousand represents \$44,760 thousand in government contributions for employee benefits, \$31,186 thousand in unfunded unemployment compensation liabilities, \$1,113.8 thousand in funded unemployment compensation liabilities, \$609,562 thousand in custodial liabilities, and \$1,195 thousand in DoD education benefit liabilities.

Non-Federal Fluctuations

The decrease in Accrued Funded Payroll and Benefits is directly related to the accrual of the military payroll during FY 04. During FY 05, a review of the process was performed and it was determined that due to the military pay period ending on the last day of the month, there were no accrual needed.

The \$25,753 thousand increase in Advances from Others on Line 2.B. is due to the timing of the receipt and execution of orders primarily from nonfederal sources.

The \$11,883 thousand increase in Deposit Funds and Suspense Accounts is due to an erroneous posting of suspense account data to nonfederal during 1st Quarter FY 2004. DDRS-B, which was first used during 1st Quarter FY 2004 to import the data into DDRS-AFS, contained the wrong crosswalk information. The data should have been reported as intragovernmental. The true fluctuation is mainly attributable to changes in the budget clearing accounts.

The Temporary Early Retirement Authority (TERA) liabilities decrease of \$986.8 thousand is due to the expiration of the authority in FY 2001. The liability will continue to decrease as expenditures are made because the program was terminated resulting in no new liabilities.

Nonenvironmental Disposal Liabilities – Excess/Obsolete Structures decreased \$389,473 thousand due to the completion of Defense Reform Initiative Directive (DRID) 36. The liability was originally established to meet reporting requirements for DRID 36 which provided facility demolition goals for the Air Force beginning in FY 1998. DRID 36 directed that increased funding be used to eliminate these structures by FY 2003. Currently, there are no established facility demolition goals for the Air Force.

Nonenvironmental Disposal Liabilities – Conventional Munitions Disposal decreased \$5,880 thousand due to a policy change that transferred accounting responsibility for all disposal costs to the Department of the Army for inclusion in their financial statements. The Air Force no longer reports this activity.

Other Liabilities decreased \$390,570 thousand due to the reclassification of cancelled accounts payable in the amount of \$331,517 thousand from Other Liabilities to Accounts Payable. During FY 05, cancelled accounts payable is reported in Note 12, Accounts Payable.

The increase in Accrued Unfunded Annual Leave is due to fluctuations in civilian leave balances.

The decrease in Capital Lease Liability of \$47,280 thousand is due to the concerted effort by the Air Force to properly account for their eleven leases. Analysis of prior reporting revealed the calculation of the liability

Other Liabilities

The amount of \$302,440 thousand represents legal contingencies of \$301,505 thousand and accrued interest liability of \$934 thousand.

The recorded estimated probable liability amount of \$13,550 thousand has been included in the accompanying financial statements for open contractor claims greater than \$100,000 and neither under appeal nor in litigation. In addition to the contractor claims under appeal and the open contractor claims for an amount greater than \$100,000, the Air Force was party to numerous other contractor claims in amounts less than \$100,000 per claim. These claims are a routine part of the contracting business and are typically resolved through mutual agreement between the contracting officer and the contractor. Because of the routine nature of these claims, no requirement exists for a consolidated tracking mechanism to record the amount of each claim, the number of open claims, or the probability of the claim being settled in favor of the claimant. The potential liability arising from these claims in aggregate would not materially affect the operations or financial condition of the Air Force. A reasonably possible liability is estimated at \$5,669 thousand and is not included in the reported amount.

The total estimated probable liability for claims and litigation against the Air Force handled by the Civil Law and Litigation Directorate, as of March 31, 2005, was valued at \$275,189 thousand and has been included in the accompanying financial statements. As of March 31, 2005, the Air Force was party to 6,224 claims and litigation actions. This liability dollar amount recorded in the financial statements is an estimate based on the weighted average payout rate for the previous three years. A reasonably possible liability is estimated at \$99,311 thousand and is not included in the reported amount. Neither past payments nor the current contingent liability estimate provides a basis for accurately projecting the results of any individual lawsuit or claim. It is uncertain that claims will ever accrue to the Air Force. In addition, many claims and lawsuits, even if successful, will not be paid out of Air Force Funds.

As of March 31, 2005, the Air Force was party to 61 contract appeals before the Armed Services Board of Contract Appeals (ASBCA). The probable amount of loss from contractor claims of \$12,766 thousand has been included in the financial statements. The contractor claims involve unique circumstances, which are considered by the ASBCA in formulating decisions on the cases. Such claims are funded primarily from Air Force appropriations. A reasonably possible liability is estimated at \$74,487 thousand and is not included in the reported amount.

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Other Disclosures

Intragovernmental Reconciliation for Fiduciary Transactions with the Department of Labor (DoL) and the Office of Personnel Management (OPM):

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

Capital Lease Liability

As of March 31

| | 2005 | | | | 2004 |
|--|--------------------|-----------|---------|-------------------|-------------------|
| | Asset Category | | | | Total |
| | Land and Buildings | Equipment | Other | Total | |
| 1. Future Payments Due | | | | | |
| A. 2005 | \$ 45,127,536.20 | \$ 0.00 | \$ 0.00 | \$ 45,127,536.20 | \$ 45,600,286.05 |
| B. 2006 | 42,032,230.80 | 0.00 | 0.00 | 42,032,230.80 | 45,474,767.22 |
| C. 2007 | 38,953,523.76 | 0.00 | 0.00 | 38,953,523.76 | 45,151,536.20 |
| D. 2008 | 38,477,782.80 | 0.00 | 0.00 | 38,477,782.80 | 42,056,230.80 |
| E. 2009 | 38,477,782.80 | 0.00 | 0.00 | 38,477,782.80 | 38,977,523.80 |
| F. After 5 Years | 76,711,794.81 | 0.00 | 0.00 | 76,711,794.81 | 165,137,592.31 |
| G. Total Future Lease Payments Due | \$ 279,780,651.17 | \$ 0.00 | \$ 0.00 | \$ 279,780,651.17 | \$ 382,397,936.38 |
| H. Less: Imputed Interest Executory Costs | 63,259,278.33 | 0.00 | 0.00 | 63,259,278.33 | 118,596,532.70 |
| I. Net Capital Lease Liability | \$ 216,521,372.84 | \$ 0.00 | \$ 0.00 | \$ 216,521,372.84 | \$ 263,801,403.68 |
| 2. Capital Lease Liabilities Covered by Budgetary Resources | | | | \$ 169,681,187.15 | \$ 299,509,641.84 |
| 3. Capital Lease Liabilities Not Covered by Budgetary Resources | | | | \$ 46,840,185.70 | \$ 82,679,096.47 |

The Air Force is the lessee in eleven capital leases all for family housing. Six of the military housing leases were awarded prior to FY 1992 and are funded on a FY basis.

Fluctuations

The decrease in Capital Lease Liability in the amount of \$47,280 thousand is the result of a change in methodology for the use of interest rates that applies to the individual leases. The Air Force previously used the interest rate provided with each of the eleven capital leases. This interest rate did not accurately provide the cost of money to compute fair market value. The current interest rate used reflects the appropriate government rate which best reflects the governments cost of borrowing, using the historical rates from the Federal Reserve. The new change was coordinated between the Air Force and OSD.

| | |
|-----------------|--------------------------------------|
| Note 16. | Commitments and Contingencies |
|-----------------|--------------------------------------|

Relevant Information for Comprehension

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

Contractual Actions:

| | |
|--|---------------------------|
| Contractor Claims | \$ 5,669 Thousand |
| Appeals before Armed Services Board of Contract Appeals (ASBCA) | \$ <u>74,487</u> Thousand |
| | \$ 80,156 Thousand |
| Claims and Litigation from Civil Law | \$ <u>99,311</u> Thousand |
| Total | 179,467 Thousand |

Note Reference

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

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

| As of March 31 | 2005 | | | | 2004 |
|--|--|--------------------------|--|------------------------------|------------------------------|
| | Actuarial Present Value of Projected Plan Benefits | Assume Interest Rate (%) | (Less: Assets Available to Pay Benefits) | Unfunded Actuarial Liability | Unfunded Actuarial Liability |
| 1. Pension and Health Benefits | | | | | |
| A. Military Retirement Pensions | \$ 0.00 | | \$ 0.00 | \$ 0.00 | \$ 0.00 |
| B. Military Retirement Health Benefits | 0.00 | | 0.00 | 0.00 | 0.00 |
| C. Medicare-Eligible Retiree Benefits | 0.00 | | 0.00 | 0.00 | 0.00 |
| D. Total Pension and Health Benefits | \$ 0.00 | | \$ 0.00 | \$ 0.00 | \$ 0.00 |
| 2. Other | | | | | |
| A. FECA | \$ 1,163,442,240.00 | | \$ 0.00 | \$ 1,163,442,240.00 | \$ 1,262,267,550.00 |
| B. Voluntary Separation Incentive Programs | 0.00 | | 0.00 | 0.00 | 0.00 |
| C. DoD Education Benefits Fund | 0.00 | | 0.00 | 0.00 | 0.00 |
| D. <u>{Enter Program Name}</u> | 0.00 | | 0.00 | 0.00 | 0.00 |
| E. Total Other | \$ 1,163,442,240.00 | | \$ 0.00 | \$ 1,163,442,240.00 | \$ 1,262,267,550.00 |
| 3. Total Military Retirement Benefits and Other Employment Related Actuarial Liabilities: | \$ 1,163,442,240.00 | | \$ 0.00 | \$ 1,163,442,240.00 | \$ 1,262,267,550.00 |

Actuarial Cost Method Used:

Assumptions:

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

Military Retirement Pensions

Assumptions:

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

Military Retirement Health Benefits

Assumptions:

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

Federal Employees’ Compensation Act (FECA)

Assumptions and Actuarial Cost Method Used:

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

2004

4.883% in Year 1

5.235% in Year 2 and thereafter

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

The compensation COLAs and CPIMs used in the projections for various charge-back years (CBYs) are as follows:

| <u>CBY</u> | <u>COLA</u> | <u>CPIM</u> |
|------------|-------------|-------------|
| 2005 | 2.03% | 4.14% |
| 2006 | 2.73% | 3.96% |
| 2007 | 2.40% | 3.98% |
| 2008 | 2.40% | 3.99% |
| 2009+ | 2.40% | 4.02% |

The model’s resulting projections were analyzed to insure that the estimates were reliable. The analysis was based on two tests: (1) a comparison of the percentage change in the liability amount by agency to the percentage change in the actual payments, and (2) a comparison of the ratio of the estimated liability to the actual payment of the beginning year calculated for the current projection to the liability-payment ratio calculated for the prior projection.

Note Reference

For regulatory discussion on “Military Retirement Benefits and Other Employment Related Actuarial Liabilities,” see DoD Financial Management Regulation, Volume 6B, Chapter 10, paragraph 1019.

| | |
|-----------------|---|
| Note 18. | Disclosures Related to the Statement of Net Cost |
|-----------------|---|

Gross Cost and Earned Revenue by Budget Functional Classification

As of March 31

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

Statement of Net Cost fluctuations

Intragovernmental Earned Revenue increased \$456,323 thousand primarily due to greater reimbursable authority in the Research, Development, Test & Evaluation (RDT&E) appropriation, which allowed the Air Force to change how it pays for centrally managed service contracts as well as permitting larger orders. The centrally managed service contract is the Federally Funded Research and Development (FFRDC) contract. Previously, each program office would individually procure services off this contract. This year, the program offices are sending their funds to a central point of contact, the funds are converted to a reimbursable fund cite, and this fund cite is obligated and billed. This change in funds management amounts to an increase in additional orders and collections. Now, instead of direct citing the funds, those funds are accepted through reimbursement which increases orders and collections overall.

In addition, towards the end of FY 2004, the Air Force clarified methods for recording work chargeable to outside organizations. This change in methodology results in higher reimbursable transactions resulting in increased intragovernmental revenue.

AF GF

Earned Revenue from the Public increased \$1,169,612 thousand primarily due to other gains reported by the Air Force Equipment Management System (AFEMS) for Air National Guard equipment found on base that they have not reported previously. Physical inventories of systems, such as for Special Tools and Test Equipment, identified assets that were previously not recorded in property records.

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

As of March 31

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

Benefit Program Expenses

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

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

Stewardship Assets

Suborganization Program Costs

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

| As of March 31 | 2005 | | 2004 | |
|--|----------------------------------|---------------------------|----------------------------------|---------------------------|
| | Cumulative Results of Operations | Unexpended Appropriations | Cumulative Results of Operations | Unexpended Appropriations |
| 1. Prior Period Adjustments Increases (Decreases) to Net Position | | | | |
| A. Changes in Accounting Standards | \$ 0.00 | \$ 0.00 | \$ 0.00 | \$ 0.00 |
| B. Errors and Omissions in Prior Year Accounting Reports | 0.00 | 0.00 | 0.00 | 0.00 |
| C. Other Prior Period Adjustments | 0.00 | 0.00 | 0.00 | 0.00 |
| D. Total Prior Period Adjustments | \$ 0.00 | \$ 0.00 | \$ 0.00 | \$ 0.00 |
| 2. Imputed Financing | | | | |
| A. Civilian CSRS/FERS Retirement | \$ 110,128,396.57 | \$ 0.00 | \$ 122,591,471.43 | \$ 0.00 |
| B. Civilian Health | 210,976,220.00 | 0.00 | 193,465,449.50 | 0.00 |
| C. Civilian Life Insurance | 633,508.68 | 0.00 | 640,421.54 | 0.00 |
| D. Judgment Fund | 42,679,708.82 | 0.00 | 12,399,364.83 | 0.00 |
| E. Total Imputed Financing | \$ 364,417,834.07 | \$ 0.00 | \$ 329,096,707.30 | \$ 0.00 |

Relevant Information for Comprehension

Imputed Financing

The amounts remitted to the Office of Personnel Management (OPM) by and for employees covered by the Civil Service Retirement System (CSRS), the Federal Employees' Retirement System (FERS), the Federal Employees Health Benefits Program (FEHB), and the Federal Employees Group Life Insurance Program (FEGLI) do not fully cover the U.S. Government's cost to provide these benefits. An imputed cost is recognized as the difference between the Government's cost of providing these benefits to the employees and contributions made by and for them. The OPM provides the cost factors to Defense Finance and Accounting Service (DFAS) for computation of imputed financing cost. DFAS provides the costs to the Office of the Under Secretary of Defense (Personnel and Readiness) (OUSD [P&R]) for validation. Approved imputed costs are provided to the reporting components for inclusion in their financial statements.

AF GF

The total Civilian Retirement imputed financing of \$110,128 thousand is comprised of \$97,163 thousand for the CSRS and \$12,965 thousand for the FERS.

The imputed revenue is equal to the imputed expense recognized in the Statement of Net Cost.

Note Reference

For regulatory disclosure related to the Statement of Changes in Net Position, see Department of Defense Financial Management Regulation, Volume 6B, Chapter 10, paragraph 1022.

| | |
|-----------------|--|
| Note 20. | Disclosures Related to the Statement of Budgetary Resources |
|-----------------|--|

| As of March 31 | 2005 | 2004 |
|--|----------------------|----------------------|
| 1. Net Amount of Budgetary Resources Obligated for Undelivered Orders at the End of the Period | \$ 49,924,568,967.27 | \$ 48,143,845,299.51 |
| 2. Available Borrowing and Contract Authority at the End of the Period | 0.00 | 0.00 |

Other Information Related to the Statement of Budgetary Resources

The amount of direct obligations incurred and apportioned under category A is \$33,778,222 thousand, category B is \$30,876,149 thousand, and exempt is \$616 thousand. For reimbursable obligations incurred and apportioned, category A is \$5,958,252 thousand, category B is \$2,230,599 thousand, and exempt is \$0.

Unexpended Obligations presented in the SBR includes Unexpended Obligations for both direct and reimbursable funds. The Department of Defense has not fully implemented the U.S. Standard General Ledger (USSGL) in all operational accounting systems. The statement does not include any amounts for which the Department of Treasury is willing to accept corrections to canceled appropriation amounts, in accordance with the Statement of Federal Financial Accounting Standards No.1.

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

Due to accounting system deficiencies, the proper amount of intra-agency eliminations for this statement cannot be determined. Accounting systems currently do not provide or capture data needed for obligations incurred and recoveries of prior year obligations in accordance with the Office of Management and Budget Circular A-11, "Instructions on Budget Execution," requirements. Although the Defense Finance and Accounting Service-Denver (DFAS-DE) developed an alternative methodology to calculate these items, the auditors and DFAS-DE concur that this methodology also distorts the obligation figures. As a result, the amount of distortion cannot be reliably determined and may or may not be material.

| | |
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| Note 21. | Disclosures Related to the Statement of Financing |
|-----------------|--|

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

Note 1A and Note 1F provide additional detail.

Other Information Related to the Statement of Financing

Components Requiring or Generating Resources in Future Period, Other consists of \$10,273 thousand in closed-year liabilities. Components Not Requiring or Generating Resources, Other consists of \$124,048 thousand in bad debt expense, \$4,566,454 thousand in Other Expenses not Requiring Budgetary Resources, and \$(889,802) thousand in Cost Capitalization Offset.

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

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

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| Note 22. | Disclosures Related to the Statement of Custodial Activity |
|-----------------|---|

Not applicable

| | |
|-----------------|--------------------------|
| Note 23. | Other Disclosures |
|-----------------|--------------------------|

| As of March 31 | 2005 | | | | 2004 |
|---------------------------------|-------------------|------------------|-------------------|---------------------|-------------------|
| 1. ENTITY AS LESSEE- | | | | | |
| Operating Leases | | | | | |
| Future Payments Due | <u>Land and</u> | | | | |
| <u>Fiscal Year</u> | <u>Buildings</u> | <u>Equipment</u> | <u>Other</u> | <u>Total</u> | <u>Total</u> |
| 2006 | \$ 82,161,800.00 | \$ 0.00 | \$ 145,790,125.00 | \$ 227,951,925.00 | \$ 93,718,211.00 |
| 2007 | 86,230,300.00 | 0.00 | 148,705,928.00 | 234,936,228.00 | 96,306,176.60 |
| 2008 | 87,684,600.00 | 0.00 | 151,680,046.00 | 239,364,646.00 | 98,723,418.00 |
| 2009 | 85,382,000.00 | 0.00 | 154,713,647.00 | 240,095,647.00 | 101,684,588.00 |
| 2010 | 87,915,100.00 | 0.00 | 157,807,920.00 | 245,723,020.00 | N/A |
| After 5 Years | 90,534,400.00 | 0.00 | 160,964,079.00 | 251,498,479.00 | 0.00 |
| Total Future Lease Payments Due | \$ 519,908,200.00 | \$ 0.00 | \$ 919,661,745.00 | \$ 1,439,569,945.00 | \$ 390,432,393.60 |

Fluctuations and Abnormalities:

There was a significant increase in commercial lease costs for FY05Q2 of approximately \$30M to support various contingency operations. Over the past three quarters HQ Air Combat Command (ACC) LGTV has reported commercial vehicle lease data as prepared and forwarded by the using units in Southwest Asia (SWA). ACC's recent investigation has shown that certain units have experienced problems reporting correct commercial lease data due to lack of continuity and actual user/ownership of the leased assets. Due to the fluid nature of combat operations and the high rate of forces rotating in and out of SWA, fleet managers and contracting specialists have mistakenly reported monthly lease data in lieu of the required quarterly data. This disconnect was discovered after the FY05Q1. Due to the reasons listed above, we anticipate an increase in the total number of vehicles and lease costs being reported for the foreseeable future. We are taking every possible step to standardize the gathering and reporting of this data to include having a summary statement provided by each reporting unit when there are significant increases or decreases in lease data being reported from the previous quarter. Additionally, USCENTAF-A4/LGT will include training for leased vehicle procurement, accountability and data reporting for Vehicle Maintenance Managers prior to their deployment to the theater.