Department of Defense
Agency Wide
CONSOLIDATED BALANCE SHEET
As of March 31, 2007 and 2006

	2007 Consolidated	2006 Consolidated
1. ASSETS (Note 2)		
A. Intragovernmental:		
1. Fund Balance with Treasury (Note 3)		
a. Entity	$ 563,105,621,181.79	$ 511,767,035,132.05
b. Non-Entity Seized Iraqi Cash	29,066,113.41	42,738,977.61
c. Non-Entity-Other	10,672,102,870.93	1,547,419,991.93
2. Investments (Note 4)	341,847,088,184.81	306,994,237,916.01
3. Accounts Receivable (Note 5)	2,026,322,179.72	3,644,104,587.13
4. Other Assets (Note 6)	1,024,654,018.80	1,120,609,534.19
5. Total Intragovernmental Assets	$ 918,704,854,549.46	$ 825,116,146,138.92
B. Cash and Other Monetary Assets (Note 7)	$ 1,963,257,709.29	$ 1,854,869,552.08
C. Accounts Receivable,Net (Note 5)	7,835,397,901.07	8,236,645,297.72
D. Loans Receivable (Note 8)	3,565,235,325.01	4,093,154,813.34
E. Inventory and Related Property,Net (Note 9)	227,218,944,846.76	227,643,515,704.78
F. General Property, Plant and Equipment,Net (Note 10)	471,915,998,026.93	469,349,995,899.64
G. Investments (Note 4)	1,332,955,130.00	866,329,130.00
H. Other Assets (Note 6)	26,205,921,596.74	24,083,884,637.49
2. TOTAL ASSETS	$ 1,658,742,565,085.26	$ 1,561,244,541,173.97
3. LIABILITIES (Note 11)		
A. Intragovernmental:		
1. Accounts Payable (Note 12)	$ 2,149,601,594.37	$ 2,532,992,055.47
2. Debt (Note 13)	3,492,015,939.32	4,146,373,211.83
3. Other Liabilities (Note 15 & 16)	12,665,430,482.43	11,608,253,520.45
4. Total Intragovernmental Liabilities	$ 18,307,048,016.12	$ 18,287,618,787.75
B. Accounts Payable (Note 12)	$ 25,995,837,542.42	$ 29,333,570,787.58
C. Military Retirement and Other Federal Employment Benefits (Note 17)	1,816,442,732,416.50	1,736,057,866,413.76
D. Environmental and Disposal Liabilities (Note 14)	69,881,505,052.20	63,594,914,682.40
E. Loan Guarantee Liability (Note 8)	37,633,875.69	30,541,723.78
F. Other Liabilities (Note 15 & Note 16)	36,325,529,743.84	29,994,451,687.78
4. TOTAL LIABILITIES	$ 1,966,990,286,646.77	$ 1,877,298,964,083.05
5. NET POSITION		
A. Unexpended Appropriations - Earmarked Funds (Note 23)	$ 10,322,450.51	$ 16,467,363.60
B. Unexpended Appropriations - Other Funds	555,419,462,004.53	498,743,618,550.69
C. Cumulative Results of Operations - Earmarked Funds	(1,225,899,243,053.07)	(1,185,129,124,355.74)
D. Cumulative Results of Operations - Other Funds	362,221,737,036.52	370,314,615,532.37
6. TOTAL NET POSITION	$ (308,247,721,561.51)	$ (316,054,422,909.08)
7. TOTAL LIABILITIES AND NET POSITION	$ 1,658,742,565,085.26	$ 1,561,244,541,173.97

Department of Defense

Agency Wide

CONSOLIDATED STATEMENT OF NET COST

For the periods ended March 31, 2007 and 2006

	2007 Consolidated	2006 Consolidated
1. Program Costs		
A. Gross Costs	$ 296,567,060,898.19	$ 269,473,659,868.89
B. (Less: Earned Revenue)	(18,883,138,964.84)	(23,371,429,399.57)
C. Net Program Costs	$ 277,683,921,933.35	$ 246,102,230,469.32
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	$ 277,683,921,933.35	$ 246,102,230,469.32

Department of Defense

Agency Wide

CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION

For the periods ended March 31, 2007 and 2006

	2007 Earmarked Funds	2007 All Other Funds
CUMULATIVE RESULTS OF OPERATIONS		
1. Beginning Balances	$ (1,206,769,332,749.45)	$ 302,900,988,741.72
2. Prior Period Adjustments:		
2.A. Changes in accounting principles (+/-)	0.00	0.00
2.B. Corrections of errors (+/-)	0.00	0.00
3. Beginning balances, as adjusted	(1,206,769,332,749.45)	302,900,988,741.72
4. Budgetary Financing Sources:		
4.A. Other adjustments (rescissions, etc.)	0.00	0.00
4.B. Appropriations used	1,108,420.83	311,604,046,934.25
4.C. Nonexchange revenue	1,286,197,278.66	7,063,223,223.25
4.D. Donations and forfeitures of cash	13,916,331.98	125,896.84
and cash equivalents	0.00	0.00
4.E. Transfers-in/out without reimbursement	196,126,055.60	(119,389,161.83)
4.F. Other budgetary financing sources	0.00	0.00
5. Other Financing Sources:		
5.A. Donations and forfeitures of property	0.00	2,959,337.54
5.B. Transfers-in/out without reimbursement (+/-)	9,525,908.75	282,683,488.98
5.C. Imputed financing from costs absorbed by others	24.32	7,250,630,889.75
5.D. Other (+/-)	(11,254,851.04)	(4,542,243,942.50)
6. Total Financing Sources	1,495,619,169.10	321,542,036,666.28
7. Net Cost of Operations (+/-)	(41,059,798,611.40)	323,906,616,455.60
8. Net Change	42,555,417,780.50	(2,364,579,789.32)
9. Cumulative Results of Operations	(1,164,213,914,968.95)	300,536,408,952.40
UNEXPENDED APPROPRIATIONS		
10. Beginning Balances	$ 11,430,871.34	$ 313,301,864,412.90
11. Prior Period Adjustments:		
11.A. Changes in accounting principles	0.00	0.00
11.B. Corrections of errors	0.00	0.00
12. Beginning balances, as adjusted	11,430,871.34	313,301,864,412.90
13. Budgetary Financing Sources:		
13.A. Appropriations received	0.00	555,997,769,225.28
13.B. Appropriations transferred-in/out	0.00	22,018,731.00
13.C. Other adjustments (rescissions, etc)	0.00	(2,298,143,430.40)
13.D. Appropriations used	(1,108,420.83)	(311,604,046,934.25)
14. Total Budgetary Financing Sources	(1,108,420.83)	242,117,597,591.63
15. Unexpended Appropriations	10,322,450.51	555,419,462,004.53
16. Net Position	(1,164,203,592,518.44)	855,955,870,956.93

Department of Defense
Agency Wide
CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION
For the periods ended March 31, 2007 and 2006

	2007 Eliminations	2007 Consolidated
CUMULATIVE RESULTS OF OPERATIONS		
1. Beginning Balances	$ 0.00	$ (903,868,344,007.73)
2. Prior Period Adjustments:		
2.A. Changes in accounting principles (+/-)	0.00	0.00
2.B. Corrections of errors (+/-)	0.00	0.00
3. Beginning balances, as adjusted	0.00	(903,868,344,007.73)
4. Budgetary Financing Sources:		
4.A. Other adjustments (rescissions, etc.)	0.00	0.00
4.B. Appropriations used	0.00	311,605,155,355.08
4.C. Nonexchange revenue	0.00	8,349,420,501.91
4.D. Donations and forfeitures of cash	0.00	14,042,228.82
and cash equivalents	0.00	0.00
4.E. Transfers-in/out without reimbursement	0.00	76,736,893.77
4.F. Other budgetary financing sources	0.00	0.00
5. Other Financing Sources:		
5.A. Donations and forfeitures of property	0.00	2,959,337.54
5.B. Transfers-in/out without reimbursement (+/-)	0.00	292,209,397.73
5.C. Imputed financing from costs absorbed by others	5,162,895,910.85	2,087,735,003.22
5.D. Other (+/-)	0.00	(4,553,498,793.54)
6. Total Financing Sources	5,162,895,910.85	317,874,759,924.53
7. Net Cost of Operations (+/-)	5,162,895,910.85	277,683,921,933.35
8. Net Change	0.00	40,190,837,991.18
9. Cumulative Results of Operations	0.00	(863,677,506,016.55)
UNEXPENDED APPROPRIATIONS		
10. Beginning Balances	$ 0.00	$ 313,313,295,284.24
11. Prior Period Adjustments:		
11.A. Changes in accounting principles	0.00	0.00
11.B. Corrections of errors	0.00	0.00
12. Beginning balances, as adjusted	0.00	313,313,295,284.24
13. Budgetary Financing Sources:		
13.A. Appropriations received	0.00	555,997,769,225.28
13.B. Appropriations transferred-in/out	0.00	22,018,731.00
13.C. Other adjustments (rescissions, etc)	0.00	(2,298,143,430.40)
13.D. Appropriations used	0.00	(311,605,155,355.08)
14. Total Budgetary Financing Sources	0.00	242,116,489,170.80
15. Unexpended Appropriations	0.00	555,429,784,455.04
16. Net Position	0.00	(308,247,721,561.51)

Department of Defense
Agency Wide
CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION
For the periods ended March 31, 2007 and 2006

	2006 Earmarked Funds	2006 All Other Funds
CUMULATIVE RESULTS OF OPERATIONS		
1. Beginning Balances	$ (1,170,876,050,321.23)	$ 300,201,835,674.18
2. Prior Period Adjustments:		
2.A. Changes in accounting principles (+/-)	0.00	0.00
2.B. Corrections of errors (+/-)	0.00	(1,207,720.24)
3. Beginning balances, as adjusted	(1,170,876,050,321.23)	300,200,627,953.94
4. Budgetary Financing Sources:		
4.A. Other adjustments (rescissions, etc.)	0.00	0.00
4.B. Appropriations used	427,359.64	296,314,139,905.79
4.C. Nonexchange revenue	1,179,439,530.21	31,769,578.18
4.D. Donations and forfeitures of cash	12,441,791.86	0.00
and cash equivalents	0.00	0.00
4.E. Transfers-in/out without reimbursement	6,797,943.96	599,540,338.36
4.F. Other budgetary financing sources	605,484.10	(247,899,728.47)
5. Other Financing Sources:		
5.A. Donations and forfeitures of property	0.00	6,134,327.03
5.B. Transfers-in/out without reimbursement (+/-)	(129,973,844.51)	130,180,531.17
5.C. Imputed financing from costs absorbed by others	20,973.49	2,169,261,774.79
5.D. Other (+/-)	(225,413,351.10)	2,121,523,392.52
6. Total Financing Sources	844,345,887.65	301,124,650,119.37
7. Net Cost of Operations (+/-)	(43,739,170,942.15)	289,847,253,405.25
8. Net Change	44,583,516,829.80	11,277,396,714.12
9. Cumulative Results of Operations	(1,126,292,533,491.43)	311,478,024,668.06
UNEXPENDED APPROPRIATIONS		
10. Beginning Balances	$ 13,394,723.24	$ 273,446,877,320.22
11. Prior Period Adjustments:		
11.A. Changes in accounting principles	0.00	0.00
11.B. Corrections of errors	0.00	(527,457.36)
12. Beginning balances, as adjusted	13,394,723.24	273,446,349,862.86
13. Budgetary Financing Sources:		
13.A. Appropriations received	100,000.00	528,251,446,632.00
13.B. Appropriations transferred-in/out	3,400,000.00	(134,095,630.00)
13.C. Other adjustments (rescissions, etc)	0.00	(6,505,942,408.38)
13.D. Appropriations used	(427,359.64)	(296,314,139,905.79)
14. Total Budgetary Financing Sources	3,072,640.36	225,297,268,687.83
15. Unexpended Appropriations	16,467,363.60	498,743,618,550.69
16. Net Position	(1,126,276,066,127.83)	810,221,643,218.75

Department of Defense
Agency Wide
CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION
For the periods ended March 31, 2007 and 2006

	2006 Eliminations	2006 Consolidated
CUMULATIVE RESULTS OF OPERATIONS		
1. Beginning Balances	$ 0.00	$ (870,674,214,647.05)
2. Prior Period Adjustments:		
2.A. Changes in accounting principles (+/-)	0.00	0.00
2.B. Corrections of errors (+/-)	0.00	(1,207,720.24)
3. Beginning balances, as adjusted	0.00	(870,675,422,367.29)
4. Budgetary Financing Sources:		
4.A. Other adjustments (rescissions, etc.)	0.00	0.00
4.B. Appropriations used	0.00	296,314,567,265.43
4.C. Nonexchange revenue	0.00	1,211,209,108.39
4.D. Donations and forfeitures of cash	0.00	12,441,791.86
and cash equivalents	0.00	0.00
4.E. Transfers-in/out without reimbursement	0.00	606,338,282.32
4.F. Other budgetary financing sources	0.00	(247,294,244.37)
5. Other Financing Sources:		
5.A. Donations and forfeitures of property	0.00	6,134,327.03
5.B. Transfers-in/out without reimbursement (+/-)	0.00	206,686.66
5.C. Imputed financing from costs absorbed by others	5,851,993.78	2,163,430,754.50
5.D. Other (+/-)	0.00	1,896,110,041.42
6. Total Financing Sources	5,851,993.78	301,963,144,013.24
7. Net Cost of Operations (+/-)	5,851,993.78	246,102,230,469.32
8. Net Change	0.00	55,860,913,543.92
9. Cumulative Results of Operations	0.00	(814,814,508,823.37)
UNEXPENDED APPROPRIATIONS		
10. Beginning Balances	$ 0.00	$ 273,460,272,043.46
11. Prior Period Adjustments:		
11.A. Changes in accounting principles	0.00	0.00
11.B. Corrections of errors	0.00	(527,457.36)
12. Beginning balances, as adjusted	0.00	273,459,744,586.10
13. Budgetary Financing Sources:		
13.A. Appropriations received	0.00	528,251,546,632.00
13.B. Appropriations transferred-in/out	0.00	(130,695,630.00)
13.C. Other adjustments (rescissions, etc)	0.00	(6,505,942,408.38)
13.D. Appropriations used	0.00	(296,314,567,265.43)
14. Total Budgetary Financing Sources	0.00	225,300,341,328.19
15. Unexpended Appropriations	0.00	498,760,085,914.29
16. Net Position	0.00	(316,054,422,909.08)

Department of Defense

Agency Wide

COMBINED STATEMENT OF BUDGETARY RESOURCES

For the periods ended March 31, 2007 and 2006

	2007 Combined	2006 Combined
BUDGETARY FINANCING ACCOUNTS		
BUDGETARY RESOURCES:		
1. Unobligated balance, brought forward, October 1	$ 111,707,911,035.96	$ 68,608,624,657.41
2. Recoveries of prior year unpaid obligations	20,083,891,374.17	17,598,408,777.79
3. Budget authority		
3.A. Appropriation	641,328,840,618.24	609,431,156,639.54
3.B. Borrowing authority	0.00	0.00
3.C. Contract authority	62,148,538,795.52	62,321,030,746.88
3.D. Spending authority from offsetting collections		
3.D.1 Earned		
3.D.1.a. Collected	76,591,602,429.28	75,943,404,404.51
3.D.1.b. Change in receivables from Federal sources	(2,343,100,829.20)	883,323,622.76
3.D.2 Change in unfilled customer orders		
3.D.2.a. Advance received	132,182,925.46	667,748,418.37
3.D.2.b. Without advance from Federal sources	23,269,959,977.24	17,012,742,128.93
3.D.3. Anticipated for rest of year, without advances	32,933,702,158.66	35,785,808,589.85
3.D.4. Previously unavailable	0.00	0.00
3.D.5. Expenditure transfers from trust funds	0.00	0.00
3.E. Subtotal	834,061,726,075.20	802,045,214,550.84
4. Nonexpenditure transfers, net, anticipated and actual	101,109,731.73	(168,707,475.82)
5. Temporarily not available pursuant to Public Law	(54,538,465,849.79)	(55,186,786,833.41)
6. Permanently not available	(43,592,031,486.57)	(37,840,887,625.47)
7. Total Budgetary Resources	$ 867,824,140,880.70	$ 795,055,866,051.34

Department of Defense

Agency Wide

COMBINED STATEMENT OF BUDGETARY RESOURCES

For the periods ended March 31, 2007 and 2006

	2007 Combined	2006 Combined
Status of Budgetary Resources:		
8. Obligations incurred:		
8.A. Direct	$ 410,923,649,933.08	$ 369,971,481,371.85
8.B. Reimbursable	92,015,627,746.74	81,787,283,282.41
8.C. Subtotal	502,939,277,679.82	451,758,764,654.26
9. Unobligated balance:		
9.A. Apportioned	336,236,317,606.12	315,381,456,912.89
9.B. Exempt from apportionment	4,251,775,509.27	4,487,934,665.79
9.C. Subtotal	340,488,093,115.39	319,869,391,578.68
10. Unobligated balance not available	24,396,770,085.49	23,427,709,818.40
11. Total status of budgetary resources	$ 867,824,140,880.70	$ 795,055,866,051.34
Change in Obligated Balance:		
12. Obligated balance, net		
12.A. Unpaid obligations, brought forward, October 1	323,859,640,769.61	302,426,881,241.17
12.B. Less: Uncollected customer payments from Federal sources, brought forward, October 1	$ (55,414,809,002.65)	$ (54,586,765,275.73)
12.C. Total unpaid obligated balance	268,444,831,766.96	247,840,115,965.44
13. Obligations incurred net (+/-)	$ 502,939,277,679.82	$ 451,758,764,654.26
14. Less: Gross outlays	(426,741,811,723.75)	(402,505,381,210.94)
15. Obligated balance transferred, net		
15.A. Actual transfers, unpaid obligations (+/-)	0.00	(526,121.95)
15.B. Actual transfers, uncollected customer payments from Federal sources (+/-)	0.00	(32,537.97)
15.C. Total Unpaid obligated balance transferred, net	0.00	(558,659.92)
16. Less: Recoveries of prior year unpaid obligations, actual	(20,083,891,374.17)	(17,598,408,777.79)
17. Change in uncollected customer payments from Federal sources (+/-)	(20,926,859,148.04)	(17,896,065,751.69)
18. Obligated balance, net, end of period		
18.A. Unpaid obligations	379,973,215,351.51	334,081,329,784.75
18.B. Less: Uncollected customer payments (+/-) from Federal sources (-)	(76,341,668,150.69)	(72,482,863,565.39)
18.C. Total, unpaid obligated balance, net, end of period	303,631,547,200.82	261,598,466,219.36
Net Outlays		
19. Net Outlays:		
19.A. Gross outlays	426,741,811,723.75	402,505,381,210.94
19.B. Less: Offsetting collections	(76,723,785,354.74)	(76,611,152,822.88)
19.C. Less: Distributed Offsetting receipts	(61,616,853,216.65)	(56,834,218,538.98)
19.D. Net Outlays	$ 288,401,173,152.36	$ 269,060,009,849.08

Department of Defense

Agency Wide

COMBINED STATEMENT OF BUDGETARY RESOURCES

For the periods ended March 31, 2007 and 2006

		2007 Combined	2006 Combined
NONBUDGETARY FINANCING ACCOUNTS			
BUDGETARY RESOURCES			
1.	Unobligated balance, brought forward, October 1	$ 46,834,726.25	$ 82,987,971.16
2.	Recoveries of prior year unpaid obligations	0.00	0.00
3.	Budget authority		
	3.A. Appropriation	0.00	0.00
	3.B. Borrowing authority	124,858,180.52	44,451,372.00
	3.C. Contract authority	0.00	0.00
	3.D. Spending authority from offsetting collections		
	3.D.1 Earned		
	3.D.1.a. Collected	611,257,279.40	486,512,530.88
	3.D.1.b. Change in receivables from Federal sources	162,508.50	0.00
	3.D.2 Change in unfilled customer orders		
	3.D.2.a. Advance received	0.00	0.00
	3.D.2.b. Without advance from Federal sources	8,083,542.00	(24,796,454.00)
	3.D.3 Anticipated for rest of year, without advances	128,295,242.19	197,543,278.05
	3.D.4 Previously unavailable	0.00	0.00
	3.D.5 Expenditure transfers from trust funds	0.00	0.00
	3.E. Subtotal	872,656,752.61	703,710,726.93
4.	Nonexpenditure transfers, net, anticipated and actual	0.00	0.00
5.	Temporarily not available pursuant to Public Law	0.00	0.00
6.	Permanently not available	(812,864,260.47)	(616,101,697.72)
7.	**Total Budgetary Resources**	$ 106,627,218.39	$ 170,597,000.37

Department of Defense
Agency Wide
COMBINED STATEMENT OF BUDGETARY RESOURCES
For the periods ended March 31, 2007 and 2006

	2007 Combined	2006 Combined
Status of Budgetary Resources:		
8. Obligations incurred:		
8.A. Direct	$ 148,934,452.54	$ 40,461,315.73
8.B. Reimbursable	0.00	0.00
8.C. Subtotal	148,934,452.54	40,461,315.73
9. Unobligated balance:		
9.A. Apportioned	160,734,343.98	5,451,137.10
9.B. Exempt from apportionment	0.00	0.00
9.C. Subtotal	160,734,343.98	5,451,137.10
10. Unobligated balance not available	(203,041,578.13)	124,684,547.54
11. Total Status of Budgetary Resources	$ 106,627,218.39	$ 170,597,000.37
Change in Obligated Balance:		
12. Obligated balance, net		
12.A. Unpaid obligations, brought forward, October 1	3,417,765,197.00	3,863,849,780.81
12.B. Less: Uncollected customer payments from Federal sources, brought forward, October 1	$ (76,910,703.00)	$ (123,710,109.00)
12.C. Total unpaid obligated balance	3,340,854,494.00	3,740,139,671.81
13. Obligations incurred net (+/-)	$ 148,934,452.54	$ 40,461,315.73
14. Less: Gross outlays	(256,913,136.86)	(254,584,156.54)
15. Obligated balance transferred, net		
15.A. Actual transfers, unpaid obligations (+/-)	0.00	0.00
15.B. Actual transfers, uncollected customer payments from Federal sources (+/-)	0.00	0.00
15.C. Total Unpaid obligated balance transferred, net	0.00	0.00
16. Less: Recoveries of prior year unpaid obligations, actual	0.00	0.00
17. Change in uncollected customer payments from Federal sources (+/-)	(8,246,050.50)	24,796,454.00
18. Obligated balance, net, end of period		
18.A. Unpaid obligations	3,309,786,512.68	3,649,726,940.00
18.B. Less: Uncollected customer payments (+/-) from Federal sources (-)	(85,156,753.50)	(98,913,655.00)
18.C. Total, unpaid obligated balance, net, end of period	3,224,629,759.18	3,550,813,285.00
Net Outlays		
19. Net Outlays:		
19.A. Gross outlays	256,913,136.86	254,584,156.54
19.B. Less: Offsetting collections	(611,257,279.40)	(486,512,530.88)
19.C. Less: Distributed Offsetting receipts	0.00	0.00
19.D. Net Outlays	$ (354,344,142.54)	$ (231,928,374.34)

Department of Defense

Agency Wide

CONSOLIDATED STATEMENT OF FINANCING

For the periods ended March 31, 2007 and 2006

	2007 Consolidated	2006 Consolidated
Resources Used to Finance Activities:		
Budgetary Resources Obligated		
1. Obligations incurred	$ 503,088,212,132.36	$ 451,799,225,969.99
2. Less: Spending authority from offsetting collections and recoveries (-)	(118,354,039,206.85)	(112,567,343,429.24)
3. Obligations net of offsetting collections and recoveries	384,734,172,925.51	339,231,882,540.75
4. Less: Offsetting receipts (-)	(61,616,853,216.65)	(56,834,218,538.98)
5. Net obligations	323,117,319,708.86	282,397,664,001.77
Other Resources		
6. Donations and forfeitures of property	2,959,337.54	6,134,327.03
7. Transfers in/out without reimbursement (+/-)	292,209,397.73	206,686.66
8. Imputed financing from costs absorbed by others	2,087,735,003.22	2,163,430,754.50
9. Other (+/-)	(4,553,498,793.54)	1,896,110,041.42
10. Net other resources used to finance activities	(2,170,595,055.05)	4,065,881,809.61
11. Total resources used to finance activities	$ 320,946,724,653.81	$ 286,463,545,811.38
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 (-)	(59,401,895,256.52)	(30,713,069,118.95)
12b. Unfilled Customer Orders	23,410,226,444.70	17,655,694,093.30
13. Resources that fund expenses recognized in prior periods	(6,573,693,573.27)	(3,663,623,808.08)
14. Budgetary offsetting collections and receipts that do not affect net cost of operations	1,698,572,382.43	1,918,911,416.23
15. Resources that finance the acquisition of assets	(48,286,228,640.85)	(60,626,229,275.09)
16. Other resources or adjustments to net obligated resources that do not affect net cost of operations		
16a. Less: Trust or Special Fund Receipts Related to exchange in the Entity's Budget (-)	(10,000,000.00)	(10,000,000.00)
16b. Other (+/-)	4,262,958,820.21	(1,902,023,515.99)
17. Total resources used to finance items not part of the net cost of operations	$ (84,900,059,823.30)	$ (77,340,340,208.58)
18. Total resources used to finance the net cost of operations	$ 236,046,664,830.51	$ 209,123,205,602.80

Department of Defense
Agency Wide
CONSOLIDATED STATEMENT OF FINANCING
For the periods ended March 31, 2007 and 2006

	2007 Consolidated	2006 Consolidated
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	1,630,928,220.95	463,557,077.38
20. Increase in environmental and disposal liability	1,517,594,996.31	235,721,419.29
21. Upward/Downward reestimates of credit subsidy expense (+/-)	8,991,359.65	0.00
22. Increase in exchange revenue receivable from the public (-)	(38,939,316.83)	(17,152,860.65)
23. Other (+/-)	3,734,961,394.65	353,527,614.10
24. Total components of Net Cost of Operations that will require or generate resources in future periods	6,853,536,654.73	1,035,653,250.12
Components not Requiring or Generating Resources:		
25. Depreciation and amortization	16,515,509,620.69	24,648,874,826.58
26. Revaluation of assets or liabilities (+/-)	3,314,015,387.66	3,283,837,676.53
27. Other (+/-)		
27a. Trust Fund Exchange Revenue	(7,128,760,700.25)	(12,572,834,716.33)
27b. Cost of Goods Sold	26,376,565,679.53	23,456,427,752.12
27c. Operating Material & Supplies Used	12,101,831,420.84	3,151,038,124.66
27d. Other	(16,395,440,960.36)	(6,023,972,047.16)
28. Total components of Net Cost of Operations that will not require or generate resources	34,783,720,448.11	35,943,371,616.40
29. Total components of net cost of operations that will not require or generate resources in the current period	$ 41,637,257,102.84	$ 36,979,024,866.52
30. Net Cost of Operations	$ 277,683,921,933.35	$ 246,102,230,469.32

Department of Defense

Agency Wide

COMBINED STATEMENT OF CUSTODIAL ACTIVITY

For the periods ended March 31, 2007 and 2006

		2007 Combined		2006 Combined
1.SOURCE OF COLLECTIONS				
A. Deposits by Foreign Governments	$	8,653,565,698.32	$	5,901,309,254.65
B. Seized Iraqi Cash		0.00		0.00
C. Other Collections		0.00		0.00
D. Total Cash Collections	$	8,653,565,698.32	$	5,901,309,254.65
E. Accrual Adjustments (+/-)	$	0.00	$	0.00
F. Total Custodial Collections	$	8,653,565,698.32	$	5,901,309,254.65
2.DISPOSITION OF COLLECTIONS				
A. Disbursed on Behalf of Foreign Governments and International Organizations	$	6,695,935,523.35	$	5,722,961,166.08
B. Seized Assets Disbursed on behalf of Iraqi People		1,149,460.98		18,630,867.78
C. Increase (Decrease) in Amounts to be Transferred		1,957,630,174.97		178,348,088.57
D. Collections Used for Refunds and Other Payments		0.00		0.00
E. Retained by The Reporting Entity		0.00		0.00
F. Seized Assets Retained for Support of the Iraqi People		(1,149,460.98)		(18,630,867.78)
G. Total Disposition of Collections	$	8,653,565,698.32	$	5,901,309,254.65
3. NET CUSTODIAL COLLECTION ACTIVITY	$	0.00	$	0.00

Note 1. Significant Accounting Policies

1.A. Basis of Presentation

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

The Department is unable to fully implement all elements of GAAP and OMB Circular No. A-136 due to limitations of its financial management processes and systems, and nonfinancial systems and processes that feed into the financial statements. The Department derives its reported values and information for major asset and liability categories largely from nonfinancial systems, such as inventory systems and logistics systems. These systems were designed to support reporting requirements for maintaining accountability over assets and reporting the status of federal appropriations rather than preparing financial statements in accordance with GAAP. The Department continues to implement process and system improvements addressing these limitations. The Department currently has 12 previously identified auditor material weaknesses: (1) Financial Management Systems, (2) Intragovernmental Eliminations, (3) Unsupported Accounting Entries, (4) Fund Balance with Treasury, (5) Environmental Liabilities, (6) General Property, Plant and Equipment, (7) Government Property and Material in Possession of Contractors, (8) Inventory, (9) Operating Materials and Supplies (OM&S), (10) Statement of Net Cost, (11) Statement of Financing, and (12) Accounts Payable.

1.B. Mission of the Reporting Entity

The National Security Act of 1947 established the Department of Defense. The Department's mission is to organize, train, and equip armed forces to deter aggression and, if necessary, defeat aggressors against the United States and its allies. Fiscal year (FY) 2007 is the twelfth year that the Department has prepared its audited financial statements as required by the Chief Financial Officers Act and Government Management Reform Act (GMRA). Beginning in FY 2006, the Department no longer publishes consolidating and/or combining statements. Auditors are required to audit the financial statements of the following stand-alone Department reporting activities: (1) Army General Fund, (2) Army Working Capital Fund, (3) Navy General Fund, (4) Navy Working Capital Fund, (5) Air Force General Fund, (6) Air Force Working Capital Fund, (7) Military Retirement Fund, (8) DoD Medicare-Eligible Retiree Health Care Fund, and (9) U.S. Army Corps of Engineers (Civil Works).

The Department requires the Marine Corps General and Working Capital Funds and the following Defense Agencies to prepare internal stand-alone auditable financial statements: (1) Defense Logistics Agency, (2) Defense Finance and Accounting Service, (3) Defense Information Systems Agency, (4) Defense Contract Audit Agency, (5) Defense Commissary Agency, (6) Defense Security Service, (7) Defense Threat Reduction Agency, (8) Defense Advanced Research Projects Agency, (9) Chemical and Biological Defense Program, (10) Missile Defense Agency, (11) Services Medical Activity, (12) TRICARE Management Activity, and (13) U.S. Special Operations Command.

1.C. Appropriations and Funds

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

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

Working capital funds (WCF) receive their initial funding through an appropriation or a transfer of resources from existing appropriations or funds and use those capital resources to finance the initial startup. The WCF entities provide goods and services on a reimbursable basis. Reimbursable receipts fund ongoing operations.

Trust funds contain receipts and expenditures of funds held in trust by the government for use in carrying out specific purposes or programs in accordance with the terms of the donor, trust agreement, or statute.

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

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

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

The Department is a party to allocation transfers with other federal agencies as both a transferring (parent) entity and a receiving (child) entity. Allocation transfers are legal delegations by one department of its authority to obligate budget authority and outlay funds to another department. Generally, all financial activity related to these allocation transfers (e.g., budget authority, obligations, outlays) is reported in the financial statements of the parent entity. Exceptions to this general rule will apply to specific funds for which the Office of Management and Budget (OMB) has directed that all activity will be reported in the financial statements of the child to the transfer. Exceptions include all Treasury-Managed Trust Funds, Executive Office of the President, and all other funds specifically designated by OMB.

The Department is a party to allocation transfers as the child for the following funds meeting the OMB exception, and all related activity is thus included in the Department's financial statements: South Dakota Terrestrial Wildlife Habitat Restoration, Inland Waterways and Harbor Maintenance, and the Executive Office of the President. In addition to these funds, the Department allocates funds, as the parent, to the Departments of Agriculture and Transportation. The Department receives allocation transfers, as the child, from the Departments of Agriculture, Interior, Energy, and Transportation; the Appalachian Regional Commission; Foreign Military Financing Program; International Military Education and Training Program; and Federal Highway Administration.

1.D. Basis of Accounting

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

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

In addition, the Department identifies program costs based upon the major appropriation groups provided by the Congress. Current processes and systems do not capture and report accumulated costs for major programs based upon the performance measures as required by the Government Performance and Results Act (GPRA). The Department is in the process of reviewing available data and attempting to develop a cost reporting methodology that balances the need for cost information required by GPRA and the Statement of Federal Financial Accounting Standard (SFFAS) No. 4, "Managerial Cost Accounting Concepts and Standards for the Federal Government."

1.E. Revenues and Other Financing Sources

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

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

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

1.F. Recognition of Expenses

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

1.G. Accounting for Intragovernmental Activities

Preparation of reliable financial statements requires the elimination of transactions occurring among entities within the Department or between two or more federal agencies. However, the Department cannot accurately identify most of its intragovernmental transactions by customer because the Department's systems do not track buyer and seller data needed to match related transactions. Seller entities within the Department provide summary seller-side balances for revenue, accounts receivable, and unearned revenue to the buyer-side internal Department accounting offices. In most cases, intraDoD buyer-side records are adjusted to agree with the seller-side balances. The Department's intragovernmental balances are then eliminated. The Department is developing 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 an after-the-fact reconciliation is not practical.

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

The Department's proportionate share of public debt and related expenses of the Federal Government is not included. The Federal Government does not apportion debt and its related costs to federal agencies. The Department's financial statements, therefore, do not report any portion of public debt or interest thereon, nor do the statements report the source of public financing whether from issuance of debt or tax revenues. Financing for the construction of the Department's facilities is obtained through appropriations. To the extent this financing ultimately may have been obtained through the issuance of public debt, interest costs have not been capitalized since the U.S. Treasury does not allocate such interest costs to the benefiting agencies.

1.H. Transactions with Foreign Governments and International Organizations

Each year, the Department sells defense articles and services to foreign governments and international organizations under the provisions of the "Arms Export Control Act of 1976." Under the provisions of the Act, the Department has authority to sell defense articles and services to foreign countries and international organizations generally at no profit or loss to the U.S. Government. Payment is required in advance and a liability recorded until delivery of the item(s).

Beginning in 1st Quarter, FY 2007, the Department began reporting in its basic financial statements all programs executed on behalf of the Executive Office of the President, including those authorized by the "Arms Export Control Act of 1976." Funds managed by the Department for the Executive Office of the President were previously reported in the Department's financial statements as "Other Accompanying Information."

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

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

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

1.J. Foreign Currency

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

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

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

1.K. Accounts Receivable

As presented in the Balance Sheet, accounts receivable includes accounts, claims, and refunds receivable from other federal entities or from the public. Allowances for uncollectible accounts due from the public are based upon analysis of collection experience by fund type. By law, the DoD is to collect all costs incurred for reimbursable work with other federal agencies, therefore, the DoD does not recognize an allowance for estimated uncollectible amounts from other federal agencies. The Department does not recognize an allowance for estimated uncollectible amounts from other federal agencies. Claims against other federal agencies are to be resolved between the agencies in accordance with dispute resolution procedures defined in the “Intragovernmental Business Rules” published in the Treasury Financial Manual at http://www.fms.treas.gov/tfm/vol1/07-03.pdf.

1.L. Direct Loans and Loan Guarantees

The Department operates three direct loan and loan guarantee programs: The Military Housing Privatization Initiative (MHPI), Foreign Military Financing (FMF), and the Armament Retooling and Manufacturing Support Initiative (ARMS). The MHPI Program is authorized by the National Defense Authorization Act (NDAA) for FY 1996, Public Law (P.L.) 104-106, Statute 186, Section 2801, as amended by NDAA FY 2005 P.L. 108-375, section 2805. The NDAA FY 2005, P.L. 108-375, Section 2805, provided permanent authorities to the MHPI. This Act, as amended, includes a series of authorities that allow the Department to work with the private sector to renovate military housing. The Department’s goals are to obtain private capital to leverage government dollars, make efficient use of limited resources, and use a variety of private sector approaches to build and renovate military housing faster and at a lower cost to American taxpayers.

The Act also provides the Department with a variety of authorities to obtain private sector financing and expertise to improve military housing. The Department uses these authorities individually or in combination. They include guarantees (both loan and rental); conveyance/leasing of existing property and facilities; differential lease payments; investments (both limited partnerships and stock/bond ownership); and direct loans. In addition, the “Federal Credit Reform Act of 1990” governs all amended direct loan obligations and loan guarantee commitments made after FY 1991 resulting in direct loans or loan guarantees.

The Department administers the Foreign Military Financing program on behalf of the Executive Office of the President. Sections 23 and 24 of the Arms Export Control Act (P.L. 90-629), as amended, and sections 503(a) and 541 of the Foreign Assistance Act authorize this program. The Foreign Military Financing program provides loans to help countries purchase U.S. produced weapons, defense equipment, services, or military training.

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

Beginning in 1st Quarter, FY 2007, the Department began reporting all programs it executes on behalf of the Executive Office of the President, including the ones authorized by the "Arms Export Control Act of 1976," in its basic financial statements. Funds managed by the Department for the Executive Office of the President had been previously reported in the Department's financial statements as "Other Accompanying Information."

1.M. Inventories and Related Property

The Department values approximately 58% of its resale inventory using the moving average cost method. An additional 5% (fuel inventory) is reported using the first-in-first-out method. The Department reports the remaining 37% of resale inventories at an approximation of historical cost using latest acquisition cost adjusted for holding gains and losses. The latest acquisition cost method is used because legacy inventory systems were designed for materiel management rather than compliance with accounting standards. Although these systems provide visibility and accountability over inventory items, they do not maintain historical cost data necessary to comply with SFFAS No. 3, "Accounting for Inventory and Related Property." Additionally, these systems cannot produce financial transactions using the USSGL, as required by the Federal Financial Management Improvement Act of 1996 (P.L. 104-208). By utilizing new systems development processes, the Department's components are continuing to transition the balance of their inventories to the moving average cost method. However, since the on-hand balances that were transitioned were not, for the most part, baselined to auditable historical cost, the reported values remain noncompliant with SFFAS No. 3 and GAAP.

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

Related property includes Operation Material and Supplies (OM&S) and stockpile materials. The OM&S, including munitions not held for sale, are valued at standard purchase price. The Department uses both the consumption method and the purchase method of accounting for OM&S. Items that are centrally managed and stored, such as ammunition and engines, are generally recorded using the consumption method and reported on the Balance Sheet as OM&S. When current systems cannot fully support the consumption method, the Department uses the purchase method. Under this method, materials and supplies are expensed when purchased. During FY 2007, the Department expensed significant amounts using the purchase method because the systems could not support the consumption method or management deemed that the item was in the hands of the end user.

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

The Department recognizes condemned materiel as "Excess, Obsolete, and Unserviceable." The cost of disposal is greater than the potential scrap value; therefore, the net value of condemned materiel is zero. Potentially redistributed materiel, presented in previous years as "Excess, Obsolete, and Unserviceable," is included in "Held for Use" or "Held for Repair" categories according to its condition.

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

1.N. Investments

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

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

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

Other investments represent limited partnerships, entered into on behalf of the U.S. Government in support of the Military Housing Privatization Initiative authorized by Public Law 104-106, Section 2801. These investments do not require market value disclosure.

1.O. General Property, Plant and Equipment

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

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

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

In FY 2006, the capitalization threshold was revised from $100,000 to $20,000 for real property. The capitalization threshold remains unchanged at $100,000 for the remaining General PP&E categories.

General PP&E assets are capitalized at historical acquisition cost plus capitalized improvements when an asset has a useful life of 2 or more years, and when the acquisition cost equals or exceeds the Department's capitalization threshold of $100,000, except for the USACE and WCF as discussed below. The Department also requires capitalization of improvement costs that exceed the Department's capitalization threshold of $100,000 for General PP&E. The Department depreciates all General PP&E on a straight-line basis, with the exception of land, which is not depreciated.

Prior to FY 1996, General PP&E was capitalized if it had an acquisition cost of $15,000, $25,000, and $50,000 for FYs 1993, 1994, and 1995, respectively, and an estimated useful life of two or more years. General PP&E previously capitalized at amounts below $100,000 were written off General Fund financial statements in FY 1998. No adjustment was made for WCF assets. These assets remain capitalized and reported on WCF financial statements.

The USACE Civil Works General PP&E is capitalized at historical acquisition cost plus capitalized improvements when an asset has a useful life of two or more years, and when the acquisition cost exceeds $25,000. One USACE exception is that all buildings and structures related to hydropower projects are capitalized regardless of cost. Prior to FY 2004, the Corps capitalized all buildings and structures regardless of cost. In FY 2003, the Corps increased the threshold (effective FY 2004) for buildings and structures to $25,000 for all Civil Works appropriations with the exception of Revolving Fund and Power Marketing Agency assets, and expensed all previously acquired assets not meeting the new $25,000 threshold.

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

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

1.P. Advances and Prepayments

It is the Department's policy to record payments in advance of the receipt of goods and services as advances or prepayments and report the advances as an asset on the Balance Sheet, and to recognize the expense and/or proper asset classification when it receives the related goods and services.

1.Q. Leases

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

Office space and leases entered into by the Department in support of contingency operations are the largest cost elements of operating leases. These costs were gathered from existing leases, General Services Administration (GSA) bills, and Inter-service Support Agreements. Future year projections use the Consumer Price Index (CPI), rather than the Department inflation factor. The CPI impacts increases to the leases, especially those at commercial lease sites. Equipment leases have a variety of lease terms which are not expected to be renewed upon expiration. Other operating leases are generally one-year leases. The Department expects to continue to reduce the level of owned assets while increasing the number of leased assets. The Department will strive to displace commercial leases with more economical GSA leases.

1.R. Other Assets

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

Contract financing payments are defined in the Federal Acquisition Regulation (FAR), Part 32, as authorized disbursements of monies to a contractor prior to acceptance of supplies or services by the Government. These payments are designed to alleviate the potential financial burden on contractors performing certain long-term contracts and facilitate competition for defense contracts. Contract financing payments clauses are incorporated in the contract terms and conditions and may include advance payments, performance-based payments, commercial advance and interim payments, progress payments based on cost, and interim payments under certain cost-reimbursement contracts.

Contract financing payments do not include invoice payments, payments for partial deliveries, lease and rental payments, or progress payments based on a percentage or stage of completion, which the Defense Federal Acquisition Regulation Supplement (DFARS) authorizes only for construction of real property, shipbuilding and ship conversion and alteration or repair. Progress payments for real property and ships are reported as Construction in Progress in Note 10.

1.S. Contingencies and Other Liabilities

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

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

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

1.T. Accrued Leave

The Department reports earned military and civilian leave, except sick leave, as accrued liabilities; however, it is not reported as of the Balance Sheet date, but rather reported as the amount of leave recorded as of the last payroll report. Sick leave is expensed when taken. The liability reported at the end of the accounting period reflects the current pay rates.

1.U. Net Position

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

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

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

1.V. Treaties for Use of Foreign Bases

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

1.W. Comparative Data

Financial statement fluctuations greater than 2% of total assets on the Balance Sheet or 10% from the prior period presented, but no less than $100 thousand, are generally explained within the notes to the financial statements.

1.X. Unexpended Obligations

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

1.Y. Undistributed Disbursements and Collection

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

The Department's 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.

Note 2. Nonentity Assets

As of March 31	2007	2006
1. Intragovernmental Assets		
A. Fund Balance with Treasury	$ 10,701,168,984.34	$ 1,590,158,969.54
B. Accounts Receivable	244,465.55	754,924.52
C. Total Intragovernmental Assets	$ 10,701,413,449.89	$ 1,590,913,894.06
2. Nonfederal Assets		
A. Cash and Other Monetary Assets	$ 1,806,186,744.47	$ 1,747,964,116.34
B. Accounts Receivable	5,508,445,451.32	5,213,589,455.57
C. Other Assets	196,825,000.00	204,877,633.56
D. Total Nonfederal Assets	$ 7,511,457,195.79	$ 7,166,431,205.47
3. Total Nonentity Assets	$ 18,212,870,645.68	$ 8,757,345,099.53
4. Total Entity Assets	$ 1,640,529,694,439.58	$ 1,552,487,196,074.44
5. Total Assets	$ 1,658,742,565,085.30	$ 1,561,244,541,174.00

Fluctuations

Total Nonentity Assets increased $9.5 billion (108%) primarily due to the change in reporting requirements effective 1st Quarter, FY 2007. The Office of Management and Budget (OMB) Circular A-136, "Financial Reporting Requirements," requires the Department to include programs that are executed on behalf of the Executive Office of the President. Previously, this information was reported in the Other Accompanying Information section of the financial statements. In addition, the Department changed the method for reporting the assets. In previous years, only current year-to-date activity was reported.

Other Disclosures

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

Intragovernmental Fund Balance with Treasury consists of deposit funds, seized Iraqi cash, Development Fund for Iraq, and Foreign Military Sales Trust Funds (FMSTF) advance deposits. Deposit funds are generally used to record amounts held temporarily until paid to the appropriate government or public entity. The FMSTF was established to facilitate the purchases of U.S. Defense articles and services by foreign countries and receives funds in advance for foreign customers based on future requirement forecasts.

Nonfederal Cash and Other Monetary Assets consist of cash held by disbursing officers to carry out their paying, collecting, and foreign currency accommodation exchange missions. These assets are held by disbursing officers as agents of the U.S. Treasury.

Nonfederal Accounts Receivable consists of receivables due for cancelled year appropriations, interest receivable on aged debt, and fines and penalties due to delinquency on a debt. Proceeds must be returned to the U.S. Treasury.

Nonfederal Other Assets consists of advances with the Massachusetts Institute of Technology to finance research and development projects.

Note 3. Fund Balance with Treasury

As of March 31	2007	2006
1. Fund Balances		
A. Appropriated Funds	$ 550,696,518,363.99	$ 500,865,358,630.44
B. Revolving Funds	9,613,048,400.78	8,608,268,245.65
C. Trust Funds	10,018,443,735.45	1,119,872,061.39
D. Special Funds	322,109,800.08	341,617,842.85
E. Other Fund Types	3,156,669,865.83	2,422,077,321.26
F. Total Fund Balances	$ 573,806,790,166.13	$ 513,357,194,101.59
2. Fund Balances Per Treasury Versus Agency		
A. Fund Balance per Treasury	$ 570,990,698,303.11	$ 510,881,745,552.57
B. Fund Balance per Agency	573,806,790,166.13	513,357,194,101.59
3. Reconciling Amount	$ (2,816,091,863.02)	$ (2,475,448,549.02)

Fluctuations

Fund Balance with Treasury (FBWT) increased $60.4 billion (12%) primarily due to an increase of $49.8 billion this fiscal year in appropriated funds in support of the Global War on Terror (GWOT).

Trust Funds increased $8.9 billion primarily due to a change in reporting requirements for the Foreign Military Sales Trust Fund effective 1st Quarter, FY 2007. The Office of Management and Budget (OMB) Circular A-136, “Financial Reporting Requirements,” requires the Department to include programs that are executed on behalf of the Executive Office of the President. This information was previously reported in Other Accompanying Information of the financial statements. In addition, the Department changed the method for reporting foreign government assets from current fiscal year activity to end of period balances.

Other Disclosures

The Department shows a reconciling net difference of $2.8 billion with the U.S Treasury as of 2nd Quarter, FY 2007, which is primarily comprised of $3.0 billion in funds recognized under Continuing Resolution Authority related to the funding for the annual Energy and Water Development Appropriations Act recorded by the Department, but not reported by the U.S. Treasury.

Status of Fund Balance with Treasury

As of March 31	2007		2006	
1. Unobligated Balance				
A. Available	$	302,168,037,458.70	$	283,779,902,055.91
B. Unavailable		359,377,495,092.04		321,718,561,348.24
2. Obligated Balance not yet Disbursed	$	383,283,001,864.19	$	337,731,024,186.78
3. Nonbudgetary FBWT	$	11,520,055,725.14	$	7,360,162,248.89
4. NonFBWT Budgetary Accounts	$	(482,152,413,864.40)	$	(434,793,513,634.14)
5. Total	$	574,196,176,275.67	$	515,796,136,205.68

Fluctuations

Total Status of FBWT increased $58.4 billion (11%) primarily due to the receipt of appropriation warrants of $49.8 billion this fiscal year.

Other Disclosures

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

Unobligated Balance represents the cumulative amount of budgetary authority that has not been set aside to cover outstanding obligations. Unobligated Balance is classified as available or unavailable and is associated with appropriations expiring at fiscal year end that remain available only for obligation adjustments until the account is closed.

Obligated balance not yet disbursed represents funds that have been obligated for goods that have not been received, services that have not been performed, and goods and services that have been delivered/received but not yet paid.

Nonbudgetary FBWT includes entity and nonentity FBWT accounts which do not have budgetary authority, such as unavailable receipt accounts or clearing accounts. Nonbudgetary FBWT consists of balances of deposit funds, seized Iraqi cash, Development Fund for Iraq, and Foreign Military Sales Trust Funds (FMSTF) advance deposits.

NonFBWT Budgetary Accounts include budgetary accounts that do not affect FBWT, such as contract authority, borrowing authority and investment accounts, accounts receivable, as well as the unfilled orders without advance from customers. This category reduces the Status of Fund Balance with Treasury. NonFBWT Budgetary Accounts consists of Trust Fund investments in U.S. Treasury securities, unfilled customer orders without advance, contract and borrowing authority, and reimbursements receivable.

The Status of FBWT disagrees with the FBWT by $389.4 million. The Department has recognized the difference is a result of an internal weakness of creating proprietary accounting reports from budgetary information for Security Assistance. Effective in 1st Quarter, FY 2007, the Department began reporting these balances in the financial statements. Security Assistance programs are reported by the Department, as a result of the change in reporting requirements for allocation transfers. The OMB Circular A-136, “Financial Reporting Requirements,” generally requires financial activity related to these allocation transfers (e.g., budget authority, obligations, outlays) to be reported in the financial statements of the parent entity. Exceptions to this general rule affecting the Department include Security Assistance programs executed on behalf of the Executive Office of the President.

Certain unobligated balances are restricted for future use and are not apportioned for current use. Unobligated balances for trust fund accounts are restricted by the Public Law that established the funds. The Department is the lead agency for reporting the financial data for certain trust funds such as the Inland Waterways, Harbor Maintenance, and South Dakota Terrestrial Wildlife Habitat Restoration. The U. S. Treasury, Bureau of Public Debt (BPD) maintains the investments and the investment accounting records for these funds and invests the trust fund receipts. The BPD transfers funds to the individual trust funds as funds are needed.

Disclosures Related to Suspense/Budget Clearing Accounts

As of March 31	2005	2006	2007	(Decrease)/ Increase from FY 2006 - 2007
Account				
F3845 – Personal Property Proceeds	$ 984,803.82	$ 1,248,646.87	$ 723,559.94	$ (525,086.93)
F3875 – Disbursing Officer Suspense	172,634,269.92	889,611,572.91	967,105,836.91	77,494,264.00
F3880 – Lost or Cancelled Treasury Checks	23,453,202.81	12,630,901.58	20,627,366.68	7,996,465.10
F3882 – Uniformed Services Thrift Savings Plan Suspense	62,132,593.37	107,793,376.51	155,718,983.01	47,925,606.50
F3885 – Interfund/IPAC Suspense	(592,425,915.58)	(126,979,606.96)	(178,984,217.14)	(52,004,610.18)
F3886 – Thrift Savings Plan Suspense	(5,112,257.78)	(6,192,984.92)	(7,762,847.10)	(1,569,862.18)
Total	$ (338,333,303.44)	$ 878,111,905.99	$ 957,428,682.30	$ 79,316,776.31

Abnormal Balances

The $7.8 million credit balance for F3886, Thrift Savings Plan Suspense (TSP), represents negative adjustments, lost earnings, forfeitures, and loan repayments.

Other Disclosures

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

The F3875 suspense clearing represents the Disbursing Officer's suspense. Account F3885, represents the Interfund and Intragovernmental Payment and Collection suspense. Account F3886 represents payroll deductions for the (TSP) suspense. These three suspense accounts temporarily hold collections or disbursements until they can be assigned or identified to a valid appropriation.

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

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

The total amounts reported above for FY 2005 and FY 2006 does not agree with balances reported last year-end due to the inclusion of the Personal Property Proceeds account in the current year schedule. The note schedule did not include this account for 2nd Quarter, FY 2006. In addition, the amounts reported in FY 2005 have been changed to reflect correct balances reported in the prior year. Due to timing issues in receipt of expenditure information in prior years, the Department corrected prior year balances to better reflect year-end reporting.

Disclosures Related to Problem Disbursements

As of March 31	2005	2006	2007	(Decrease)/ Increase from FY 2006 to 2007
1. Total Problem Disbursements, Absolute Value				
A. Unmatched Disbursements (UMDs)	$ 6,610,926,402.00	$ 1,961,130,233.00	$ 1,752,679,322.57	$ (208,450,910.43)
B. Negative Unliquidated Obligations (NULO)	195,989,356.00	197,474,454.00	128,106,142.15	(69,368,311.85)
C. In-Transit Disbursements	8,236,781,127.00	7,292,010,667.00	7,599,519,269.33	307,508,602.33
Total	$ 15,043,696,885.00	$ 9,450,615,354.00	$ 9,480,304,734.05	$ 29,689,380.05

Fluctuations

The Department reported a $208.4 million decrease (11%) in UMDs. This consists of $126 million decrease due to upgrades made to the Automatic Reject Control System (ARCS) during FY 2006, which led to quicker isolation of problems, implementation of corrective actions, and an increase of the automatic posting rate of Mechanization of Contract Administration Services disbursements. In addition, process improvements made by the Department resulted in an additional decrease of $82.4 million.

The Department reported a $69.4 million decrease (35%) in NULOs. This consists of a $52.9 million decrease due to upgrades made to ARCS during FY 2006, which led to quicker isolation of problems, implementation of corrective actions, and an increase of the automatic posting rate. Furthermore, beginning in 4th Quarter, FY 2006 the Department obligated the Miscellaneous Obligating Documents originating from Operation Iraqi Freedom at the end of each month which led to the additional decrease in NULOs in the 2nd Quarter, FY 2007 compared to 2nd Quarter, FY 2006.

Other Disclosures

Problem Disbursements are reported as an absolute value amount. Absolute value is the sum of the positive values of debit and credit transactions without regard to the plus or minus signs.

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

A NULO occurs when a payment is made against a valid obligation, but the payment is greater than the amount of the obligation recorded in the official accounting system. These payments have been made using available funds and are based on valid receiving reports for goods and services delivered under valid contracts.

The In-transits represent the absolute value of disbursements and collections made by a Department disbursing activity on behalf of an accountable activity and have not been posted to the accounting system. Starting 2nd Quarter FY, 2007, In-transit disbursements are reported as absolute value as opposed to net amounts disclosed in prior years. This reporting change applies to amounts in the note schedule for both the current and comparative years.

The amounts reported in FY 2005 and FY 2006 have been changed to reflect correct balances reported in the prior year problem disbursements. Due to timing issues in receipt of expenditure information in prior years, the Department corrected prior year balances to better reflect year-end reporting.

Note 4. Investments and Related Interest

As of March 31	2007							
		Cost	Amortization Method		Amortized (Premium) / Discount		Investments, Net		Market Value Disclosure
1. Intragovernmental Securities									
A. Nonmarketable, Market-Based									
1. Military Retirement Fund	$	229,080,522,852.62	See Below	$	(5,783,086,220.05)	$	223,297,436,632.57	$	218,770,332,753.23
2. Medicare Eligible Retiree Health Care Fund		110,381,420,943.19	See Below		(1,465,907,292.87)		108,915,513,650.32		106,191,211,709.19
3. US Army Corps of Engineers		3,831,049,228.12	See Below		(38,040,893.31)		3,793,008,334.81		3,780,141,087.43
4. Other Funds		1,983,887,697.38	See Below		(8,044,847.63)		1,975,842,849.75		1,981,394,676.68
5. Total Nonmarketable, Market-Based		345,276,880,721.31			(7,295,079,253.86)		337,981,801,467.45		330,723,080,226.53
B. Accrued Interest		3,865,286,717.36					3,865,286,717.36		3,865,286,717.36
C. Total Intragovernmental Securities	$	349,142,167,438.67		$	(7,295,079,253.86)	$	341,847,088,184.81	$	334,588,366,943.89
2. Other Investments									
A. Total Other Investments	$	1,332,955,130.00		$	0.00	$	1,332,955,130.00		N/A

As of March 31	2006								
		Cost	Amortization Method		Amortized (Premium) / Discount		Investments, Net		Market Value Disclosure
3. Intragovernmental Securities									
A. Nonmarketable, Market-Based									
1. Military Retirement Fund	$	225,952,891,547.57	See Below	$	(13,938,100,575.37)	$	212,014,790,972.20	$	207,266,310,704.56
2. Medicare Eligible Retiree Health Care Fund		86,150,309,734.83	See Below		(759,413,410.81)		85,390,896,324.02		82,440,852,530.11
3. US Army Corps of Engineers		3,434,057,013.80	See Below		(65,008,110.63)		3,369,048,903.17		3,306,256,464.07
4. Other Funds		1,922,170,542.68	See Below		(16,437,611.82)		1,905,732,930.86		1,906,623,305.57
5. Total Nonmarketable, Market-Based		317,459,428,838.88			(14,778,959,708.63)		302,680,469,130.25		294,920,043,004.31
B. Accrued Interest		4,313,768,785.76					4,313,768,785.76		4,313,768,785.76
C. Total Intragovernmental Securities	$	321,773,197,624.64		$	(14,778,959,708.63)	$	306,994,237,916.01	$	299,233,811,790.07
4. Other Investments									
A. Total Other Investments	$	866,329,130.00		$	0.00	$	866,329,130.00		N/A

Amortization Method Used: Effective Interest

Fluctuations

Intragovernmental Securities

Total Intragovernmental Securities, Net Investments increased $34.9 billion (11%), primarily due to increases of $23.9 billion from Medicare-Eligible Retiree Health Care Fund and $10.4 billion from Military Retirement Fund. These increases are attributable to investing the amount of the annual payment for unfunded liabilities, the contributions (in excess of beneficiary payments) from the U.S Treasury, Military Services and other Uniformed Services (U.S. Coast Guard, U.S. Public Health Service, and the National Oceanic Atmospheric Administration), accrued interest, and the reinvesting of matured securities.

Other Investments

Other Investments (with the Public) increased $466.7 million (54%) from new investments in limited partnerships in support of military housing.

Other Disclosures

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

Note 5. Accounts Receivable

As of March 31	2007			2006
	Gross Amount Due	Allowance For Estimated Uncollectibles	Accounts Receivable, Net	Accounts Receivable, Net
1. Intragovernmental Receivables	$ 2,026,322,179.72	N/A	$ 2,026,322,179.72	$ 3,644,104,587.13
2. Nonfederal Receivables (From the Public)	$ 8,065,660,716.58	$ (230,262,815.51)	$ 7,835,397,901.07	$ 8,236,645,297.72
3. Total Accounts Receivable	$ 10,091,982,896.30	$ (230,262,815.51)	$ 9,861,720,080.79	$ 11,880,749,884.85

Fluctuations

Intragovernmental accounts receivables decreased by $1.6 billon (44%), primarily due to payments of outstanding receivables by the Federal Emergency Management Agency (FEMA) for hurricane relief efforts in the Gulf Coast.

Aged Accounts Receivable

As of March 31	2007		4th Quarter 2006	
	Intragovernmental	Nonfederal	Intragovernmental	Nonfederal
CATEGORY				
Nondelinquent				
Current	$ 7,313,002,754.42	$ 1,730,521,471.61	$ 7,735,555,767.05	$ 1,840,827,242.84
Noncurrent	234,574,682.78	1,750,831,854.90	232,111,648.02	1,740,931,578.87
Delinquent				
1 to 30 days	$ 320,272,890.85	$ 217,063,605.87	$ 321,052,807.18	$ 159,895,550.01
31 to 60 days	117,668,022.48	59,952,827.65	345,741,938.72	53,397,232.71
61 to 90 days	109,721,970.54	69,906,635.75	57,232,435.27	117,793,085.90
91 to 180 days	263,523,424.93	194,164,686.19	716,488,077.02	129,963,454.25
181 days to 1 year	161,642,491.03	175,504,105.28	908,685,417.83	207,191,843.01
Greater than 1 year and less than or equal to 2 years	81,512,767.52	206,273,579.46	44,433,524.59	192,239,173.34
Greater than 2 years and less than or equal to 6 years	68,395,240.69	903,892,692.42	55,010,045.48	896,217,539.17
Greater than 6 years and less than or equal to 10 years	2,500,641.08	576,559,477.60	1,178,125.70	676,041,764.31
Greater than 10 years	18,979.97	2,667,505,549.77	17,933.35	2,640,490,814.55
Subtotal	$ 8,672,833,866.29	$ 8,552,176,486.50	$ 10,417,507,720.21	$ 8,654,989,278.96
Less Supported Undistributed Collections	(435,523,911.73)	(373,202,870.06)	(492,669,910.54)	(478,889,512.10)
Less Eliminations	(6,008,921,321.63)	0.00	(6,986,274,309.01)	0.00
Less Other	(202,066,453.21)	(113,312,900.55)	(11,109,327.79)	38,516,930.32
Total	$ 2,026,322,179.72	$ 8,065,660,715.89	$ 2,927,454,172.87	$ 8,214,616,697.18

The accounts receivable aging schedule prior year column represents 4th Quarter, FY 2006 ending balances, rather than the ending balances as of 2nd Quarter, FY 2006. Therefore, the prior year accounts receivable balance on the aging schedule will not agree with the prior year balance on the Balance Sheet or the prior year balance in the first schedule in this note.

Other Information

Nondelinquent noncurrent accounts receivable total $1.9 billion for 2nd Quarter, FY 2007 and represents those amounts that are due beyond the next 12 months. These accounts are not considered delinquent since the associated repayment schedules allow for repayment after a 30-day period and the payments are not yet due under the contract or billing documents pertaining to the receivable.

The Intragovernmental Other line consists of $202.1 million of Interfund clearing accounts, pending customer returns, and purchase card payments.

The Nonfederal Other line consists of $113.3 million of adjustments to collections and offsets in receivables.

The Department utilizes several different systems and programs (U. S. Treasury Offset Program, Vendor Pay Offset Program, Central Debt System, Intragovernmental Payment and Collection, Defense Cash Accountability System, Defense Debt Management System, Salary Offset Program), and private collection services to pursue collection action on delinquent and nondelinquent accounts receivable in accordance with Office of Management and Budget Circular A-129, “Policies for Federal Credit Programs and Non-Tax Receivables.” In certain instances, the status of litigation impacts the Department’s ability to pursue collection actions.

Note 6. Other Assets

As of March 31		2007		2006
1. Intragovernmental Other Assets				
A. Advances and Prepayments	$	899,729,018.80	$	1,120,609,534.19
B. Other Assets		124,925,000.00		0.00
C. Total Intragovernmental Other Assets	$	1,024,654,018.80	$	1,120,609,534.19
2. Nonfederal Other Assets				
A. Outstanding Contract Financing Payments	$	24,443,091,828.30	$	21,996,644,615.98
B. Other Assets (With the Public)		1,762,829,768.44		2,087,240,021.51
C. Total Nonfederal Other Assets	$	26,205,921,596.74	$	24,083,884,637.49
3. Total Other Assets	$	27,230,575,615.54	$	25,204,494,171.68

Intragovernmental Other Assets

Intragovernmental Other Assets consists of the Department's right to approximately 6 million barrels of crude oil held by the Department of Energy (DOE). The Department provided funds to DOE in FY 1993 to acquire the reserve, but incorrectly expensed the purchase. In 4th Quarter, FY 2006 the Department recorded a prior period adjustment and increased the value of Other Assets by $124.9 million to recognize the right to the oil. Due to system deficiencies, the prior period adjustment did not restate intervening comparative quarters, and thus the 2nd and 3rd Quarters, FY 2006, comparative balances will not reflect the correction.

Non Federal Other Assets

Outstanding Contract Financing Payment is comprised of $22.8 billion in contract financing payments and an additional $1.6 billion in estimated future payments to the contractor contingent upon delivery and Government acceptance of a satisfactory product. (See additional discussion in Note 15, Other Liabilities).

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

Other Assets (With the Public) are primarily comprised of $1.4 billion in advances for military and travel pay.

Note 7. Cash and Other Monetary Assets

As of March 31	2007	2006
1. Cash	$ 1,172,662,433.47	$ 1,365,641,224.21
2. Foreign Currency	790,595,275.82	489,228,327.87
3. Other Monetary Assets	0.00	0.00
4. Total Cash, Foreign Currency, & Other Monetary Assets	$ 1,963,257,709.29	$ 1,854,869,552.08

Other Disclosures

Approximately $1.0 billion in cash and $790.6 million in foreign currency are classified as nonentity and their use is restricted.

Note 8. Direct Loan and/or Loan Guarantee Programs

As of March 31

Direct Loan and/or Loan Guarantee Programs

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

- Military Housing Privatization Initiative
- Armament Retooling and Manufacturing Support Initiative
- Foreign Military Financing

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

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

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

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

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

Military Housing Privatization Initiative

The Military Housing Privatization Initiative (MHPI) includes both Direct Loan and Loan Guarantee Programs. The Department obtains private sector capital to leverage government dollars. The Department provides protection against specific risks, such as base closure or member deployment, for the private sector partner. The Loan Guarantee Program is authorized by the National Defense Authorization Act for FY 1996, Public Law (P.L.) 104-106, Statute 186, Section 2801.

Armament Retooling and Manufacturing Support Initiative

The Armament Retooling and Manufacturing Support Initiative (ARMS), Title 10 United States Code (USC) 4551-4555, is a Loan Guarantee Program designed to encourage commercial use of the Army's Inactive Ammunition Plants through many incentives for businesses willing to locate to a government ammunition production facility. The production capacity of these facilities is greater than current military requirements; however, this capacity may be needed by the military in the future. The revenues from the property rental are used to pay for the operation, maintenance and environmental cleanup at the facilities. The resulting savings in overhead costs lower the production cost of the goods manufactured and fund environmental cleanup at no cost to the government.

Foreign Military Financing

The Foreign Military Financing Account (FMFA) is a military assistance program and is comprised of the Foreign Military Loan Liquidating Account, the Foreign Military Financing Account and the Military Debt Reduction Financing Account. The FMFA is under the purview of the Department of State (DOS) and is included in its International Affairs Budget request to the Office of Management and Budget (OMB). The FMFA, appropriated by the U.S. Congress, is provided to the Department of Defense by the DOS to execute the authorities of the Foreign Assistance Act, sections 503(a) and 541 and the Arms Export Control Act, section 23. The Defense Security Cooperation Act (DSCA), under the auspices of the Executive Office of the President, administers the FMFA.

Beginning in the 1st Quarter, FY 2007, the Department implemented a new requirement from the Office of Management and Budget Circular A-136, "Financial Reporting Requirements", which states that the Department will include programs executed on behalf of the Executive Office of the President as part of the basic financial statements, rather than in the Other Accompanying Information section of the financial statements.

Summary of Direct Loans and Loan Guarantees

As of March 31	2007	2006
Direct Loan Programs		
1. Foreign Military Loan Liquidating Account	$ 2,744,483,120.26	$ 3,144,300,420.91
2. Military Housing Privatization Initiative	196,800,657.43	138,421,514.60
3. Foreign Military Financing Account	384,070,498.72	586,757,257.41
4. Military Debt Reduction Financing Account	224,570,984.05	223,675,620.42
5. Defaulted Guaranteed Loans Receivable:		
A. Foreign Military Financing Account	0.00	0.00
B. Military Housing Privatization Initiative	0.00	0.00
C. Armament Retooling & Manufacturing Support Initiative	15,310,064.55	0.00
6. Total Loans Receivable	$ 3,565,235,325.01	$ 4,093,154,813.34

As of March 31	2007	2006
Loan Guarantee Programs		
1. Foreign Military Liquidating Account	$ 0.00	$ 0.00
2. Military Housing Privatization Initiative	24,983,924.08	29,584,103.06
3. Armament Retooling & Manufacturing Support Initiative	12,649,951.61	957,620.72
4. Total Loan Guarantee Liability	$ 37,633,875.69	$ 30,541,723.78

Direct Loans Obligated

As of March 31		2007		2006
Direct Loans Obligated Prior to FY 1992 (Allowance for Loss Method):				
1. Foreign Military Loan Liquidating Account				
A. Loans Receivable Gross	$	2,410,267,426.37	$	2,808,930,571.20
B. Interest Receivable		334,215,693.89		335,369,849.71
C. Foreclosed Property		0.00		0.00
D. Allowance for Loan Losses		0.00		0.00
E. Value of Assets Related to Direct Loans, Net	$	2,744,483,120.26	$	3,144,300,420.91
Direct Loans Obligated After FY 1991 (Present Value Method):				
2. Military Housing Privatization Initiative				
A. Loans Receivable Gross	$	308,125,490.91	$	224,312,585.58
B. Interest Receivable		3,673,048.96		4,763,403.52
C. Foreclosed Property		0.00		0.00
D. Allowance for Subsidy Cost (Present Value)		(114,997,882.44)		(90,654,474.50)
E. Value of Assets Related to Direct Loans	$	196,800,657.43	$	138,421,514.60
3. Foreign Military Financing Account				
A. Loans Receivable Gross	$	21,870,000.00	$	262,691,290.00
B. Interest Receivable		862,816.44		1,750,616.76
C. Foreclosed Property		0.00		0.00
D. Allowance for Subsidy Cost (Present Value)		361,337,682.28		322,315,350.65
E. Value of Assets Related to Direct Loans	$	384,070,498.72	$	586,757,257.41
4. Military Debt Reduction Financing Account				
A. Loans Receivable Gross	$	515,878,185.28	$	506,555,929.64
B. Interest Receivable		19,135,690.10		11,293,402.26
C. Foreclosed Property		0.00		0.00
D. Allowance for Subsidy Cost (Present Value)		(310,442,891.33)		(294,173,711.48)
E. Value of Assets Related to Direct Loans, Net	$	224,570,984.05	$	223,675,620.42
5. Total Direct Loans Receivable	$	3,549,925,260.46	$	4,093,154,813.34

Fluctuations

The Total Direct Loans Receivable decreased $543.2 million (13%) primarily due to a $399.8 million decrease in the Foreign Military Loan Liquidating Account (FMLLA) related to $204 million prepayment of loans and quarterly payments by foreign countries. The FMLLA is a Pre-1992 Loan program, and does not have any new loans.

Abnormal Balances

The abnormal balance for Allowance for Subsidy Cost in the Foreign Military Financing Account is believed to be in error. The Department will work to identify and resolve any errors before 3rd Quarter, FY 2007.

Other Disclosures

Subsidy costs are recognized when direct loans are disbursed to borrowers and are reestimated each year as of the date of the financial statements. The allowance for subsidy cost is the difference between the outstanding principal of the loans and the present value of their net cash flows.

The Department's loans receivable are not the same as the proceeds that it would expect to receive from selling the loans.

<u>MHPI Program</u>

Gross direct loan values for the MHPI program through March 31, 2007, consist of the following:

Direct Loans		**2007 (in millions)**
Elmendorf Air Force Base, Alaska	*	$ 134.4
Kirtland Air Force Base, New Mexico	*	58.6
Camp Pendleton Marine Corps Base, California		29.4
Dyess Air Force Base, Texas		28.9
Robins Air Force Base, Georgia		22.3
Wright Patterson AFB, Ohio		21.9
Lackland Air Force Base, Texas		10.2
Kingsville Air Force Base, Texas		2.5
Total		**$ 308.2**

*Loan disbursement during the 2nd Quarter, FY 2007.

<u>Foreign Military Financing</u>

Effective 1st Quarter, FY 2007, the OMB Circular A-136, "Financial Reporting Requirements," requires the Department to include programs that are executed on behalf of the Executive Office of the President as part of the basic financial statements. This information was previously reported in Other Accompanying Information.

The Foreign Military Debt Reduction Financing Account wrote off $32.0 million in loans to impoverished countries.

Total Amount of Direct Loans Disbursed

As of March 31	2007	2006
Direct Loan Programs		
1. Military Housing Privatization Initiative	$ 11,900,000.00	$ 82,950,000.00
2. Foreign Military Financing Account	0.00	0.00
3. Military Debt Reduction Financing Account	0.00	0.00
4. Total	$ 11,900,000.00	$ 82,950,000.00

Direct loans disbursed decreased $71.1 million (86%) from the 2nd Quarter, FY 2006 to FY 2007. There were three new MHPI direct loans issued in FY 2006 compared to the one loan disbursed in FY 2007.

Subsidy Expense for Post FY 1991 Direct Loan

As of March 31

2007	Interest Differential	Defaults	Fees	Other	Total
1. New Direct Loans Disbursed:					
Military Housing Privatization Initiative	$ 2,126,653.00	$ 1,303,433.00	$ 0.00	$ 0.00	$ 3,430,086.00
Foreign Military Financing Account	0.00	0.00	0.00	0.00	0.00
Military Debt Reduction Financing Account	0.00	0.00	0.00	0.00	0.00
Total	$ 2,126,653.00	$ 1,303,433.00	$ 0.00	$ 0.00	$ 3,430,086.00

2006	Interest Differential	Defaults	Fees	Other	Total
2. New Direct Loans Disbursed:					
Military Housing Privatization Initiative	$ 12,992,616.00	$ 11,803,838.00	$ 0.00	$ 0.00	$ 24,796,454.00
Foreign Military Financing Account	0.00	0.00	0.00	0.00	0.00
Military Debt Reduction Financing Account	0.00	0.00	0.00	0.00	0.00
Total	$ 12,992,616.00	$ 11,803,838.00	$ 0.00	$ 0.00	$ 24,796,454.00

2007	Modifications	Interest Rate Reestimates	Technical Reestimates	Total Reestimates	Total
3. Direct Loan Modifications and Reestimates:					
Military Housing Privatization Initiative	$ 0.00	$ 234,866.00	$ 6,742,155.00	$ 6,977,021.00	$ 6,977,021.00
Foreign Military Financing Account	0.00	0.00	0.00	0.00	0.00
Military Debt Reduction Financing Account	0.00	0.00	0.00	0.00	0.00
Total	$ 0.00	$ 234,866.00	$ 6,742,155.00	$ 6,977,021.00	$ 6,977,021.00

2006	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
Foreign Military Financing Account	0.00	0.00	0.00	0.00	0.00
Military Debt Reduction Financing Account	0.00	0.00	0.00	0.00	0.00
Total	$ 0.00	$ 0.00	$ 0.00	$ 0.00	$ 0.00

	2007	2006
5. Total Direct Loan Subsidy Expense:		
Military Housing Privatization Initiative	$ 10,407,107.00	$ 24,796,454.00
Foreign Military Financing Account	0.00	0.00
Military Debt Reduction Financing Account	0.00	0.00
Total	$ 10,407,107.00	$ 24,796,454.00

Fluctuations

The total decrease of $14.5 million (58%) is due to the correction of the subsidy expense for direct loans issued to the developers at Kirtland AFB, NM, and Elmendorf AFB, AK, in 4th Quarter, FY 2006. The downward reestimate of the subsidy occurred in 1st and 2nd Quarters, FY 2007.

Subsidy Rate for Direct Loans by Program

As of March 31	Interest Differential	Defaults	Fees and other Collections	Other	Total
Budget Subsidy Rates for Direct Loans:					
1. Military Housing Privatization Initiative	19.45%	8.95%	0.00%	0.00%	28.40%
2. Foreign Military Financing Account	0.00%	0.00%	0.00%	0.00%	0.00%
3. Military Debt Reduction Financing Account	0.00%	0.00%	0.00%	0.00%	0.00%

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

During the current year there have been no new loans contracted for the Foreign Military and Military Debt Reduction Financing Accounts.

Schedule for Reconciling Subsidy Cost Allowance Balances for Post FY1991 Direct Loans

As of March 31	2007	2006
Beginning Balances, Changes and Ending Balance:		
1. Beginning Balance of the Subsidy Cost Allowance	$ 49,691,650.37	$ 74,898,302.61
2. Add: Subsidy Expense for Direct Loans Disbursed during the Reporting Years by Component		
A. Interest Rate Differential Costs	$ 2,126,653.00	$ 12,992,616.00
B. Default Costs (Net of Recoveries)	1,303,433.00	11,803,838.00
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	$ 3,430,086.00	$ 24,796,454.00
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	4,004,334.12	(37,181,921.28)
F. Other	0.00	0.00
G. Total of the above Adjustment Components	$ 4,004,334.12	$ (37,181,921.28)
4. Ending Balance of the Subsidy Cost Allowance before Re-estimates	$ 57,126,070.49	$ 62,512,835.33
5. Add or Subtract Subsidy Re-estimates by Component		
A. Interest Rate Re-estimate	$ 234,866.00	$ 0.00
B. Technical/Default Reestimate	6,742,155.00	0.00
C. Total of the above Reestimate Components	$ 6,977,021.00	$ 0.00
6. Ending Balance of the Subsidy Cost Allowance	$ 64,103,091.49	$ 62,512,835.33

Other Disclosures

Beginning in the 1st Quarter, FY 2007, the Department implemented a new requirement from the Office of Management and Budget Circular A-136, "Financial Reporting Requirements," which states that the Department will include programs executed on behalf of the Executive Office of the President as part of the basic financial statements, rather than in the Other Accompanying Information section of the financial statements. Beginning balances reflect the impact of these changes for A-136.

Defaulted Guaranteed Loans

As of March 31	2007	2006
Defaulted Guaranteed Loans from Pre-FY 1992 Guarantees (Allowance for Loss Method):		
1. Foreign Military Liquidating Account		
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 Loan Losses	0.00	0.00
E. Value of Assets Related to Defaulted Guaranteed Loans Receivable, Net	$ 0.00	$ 0.00
Defaulted Guaranteed Loans from Post-FY 1991 Guarantees (Present Value Method):		
2. 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, Net	$ 0.00	$ 0.00
3. Armament Retooling & Manufacturing Support Initiative		
A. Defaulted Guaranteed Loans Receivable, Gross	$ 14,407,200.02	$ 0.00
B. Interest Receivable	902,864.53	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, Net	$ 15,310,064.55	$ 0.00
4. Total Value of Assets Related to Defaulted Guaranteed Loans Receivable	$ 15,310,064.55	$ 0.00

Fluctuations

The Total Value of Assets Related to Defaulted Guaranteed Loans Receivable increased $15.3 million due to two defaulted loans in the ARMS Initiative Program. Payments to third party lenders were made on the loss claims for these defaults during 2nd Quarter, FY 2006, and 1st Quarter, FY 2007.

Guaranteed Loans Outstanding

As of March 31	Outstanding Principal of Guaranteed Loans, Face Value	Amount of Outstanding Principal Guaranteed
Guaranteed Loans Outstanding		
1. Military Housing Privatization Initiative	$ 549,412,228.00	$ 549,412,228.00
2. Armament Retooling & Manufacturing Support Initiative	4,303,551.80	3,658,019.03
3. Foreign Military Liquidating Account	0.00	0.00
4. Total	$ 553,715,779.80	$ 553,070,247.03
2007		
New Guaranteed Loans Disbursed		
1. Military Housing Privatization Initiative	$ 0.00	$ 0.00
2. Armament Retooling & Manufacturing Support Initiative	0.00	0.00
3. Foreign Military Liquidating Account	0.00	0.00
4. Total	$ 0.00	$ 0.00
2006		
New Guaranteed Loans Disbursed		
1. Military Housing Privatization Initiative	$ 0.00	$ 0.00
2. Armament Retooling & Manufacturing Support Initiative	739,852.83	628,874.91
3. Foreign Military Liquidating Account	0.00	0.00
4. Total	$ 739,852.83	$ 628,874.91

Other Disclosures

The Guaranteed Loans Outstanding for the MHPI program as of the 2nd Quarter, FY 2007, consist of the following:

Guarantees	**FY 2007 (in millions)**	**Default Rate**
Fort Polk, Louisiana	$165.0	6%
Fort Carson, Colorado	142.4	3%
Kirtland AFB, New Mexico	74.0	5%
Wright Patterson AFB, Ohio	65.0	6%
Elmendorf AFB, Alaska	48.0	6%
Lackland AFB, Texas	29.4	6%
Robins AFB, Georgia	25.6	6%
Total	**$549.4**	

Liabilities for Post FY 1991 Loan Guarantees, Present Value

As of March 31	2007	2006
Liabilities for Loan Guarantee Programs from Pre-FY 1992 (Allowance for Loss):		
1. Foreign Military Liquidating Account	$ 0.00	$ 0.00
2. Total Loan Guarantee Liability (Pre-FY 1992)	$ 0.00	$ 0.00
Liabilities for Loan Guarantee Programs Post-FY 1991 (Present Value):		
3. Military Housing Privatization Initiative	$ 24,983,924.08	$ 29,584,103.06
4. Armament Retooling & Manufacturing Support Initiative	12,649,951.61	957,620.72
5. Total Loan Guarantee Liability (Post-FY 1991)	$ 37,633,875.69	$ 30,541,723.78
6. Total Loan Guarantee Liability	$ 37,633,875.69	$ 30,541,723.78

For additional information, see the Schedule for Reconciling Loan Guarantee Liability Balances for Post-FY 1991 Loan Guarantees.

Subsidy Expense for Loan Guarantees by Program

As of March 31

2007	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

2006	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

2007	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

2006	Modifications	Interest Rate Reestimates	Technical Reestimates	Total Reestimates	Total
4. Modifications and Reestimates:					
Military Housing Privatization Initiative	$ 906,670.74	$ 0.00	$ 0.00	$ 0.00	$ 906,670.74
Armament Retooling & Manufacturing Support Initiative	0.00	0.00	0.00	0.00	0.00
Total	$ 906,670.74	$ 0.00	$ 0.00	$ 0.00	$ 906,670.74

	2007	2006
5. Total Loan Guarantee:		
Military Housing Privatization Initiative	$ 0.00	$ 906,670.74
Armament Retooling & Manufacturing Support Initiative	0.00	0.00
Total	$ 0.00	$ 906,670.74

Subsidy Rates for Loan Guarantees by Program

As of March 31	Interest Supplements	Defaults	Fees and other Collections	Other	Total
Budget Subsidy Rates for Loan Guarantees:					
1. Military Housing Privatization Initiative	0.00%	9.65%	0.00%	0.00%	9.65%
2. Armament Retooling & Manufacturing Support Initiative	0.00%	20.00%	0.00%	0.00%	20.00%

The subsidy rates disclosed pertain only to loan agreements made during the current fiscal year. These rates cannot be applied to the guarantees of loans disbursed during the current reporting year to yield the subsidy expense. The subsidy expense for new loans reported in the current year result from disbursements of loans from both current year loan agreements and prior year(s) loan agreements. The subsidy expense reported in the current year also includes modifications and reestimates.

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

As of March 31		2007		2006
Beginning Balance, Changes, and Ending Balance:				
1. Beginning Balance of the Loan Guarantee Liability	$	36,737,916.80	$	41,071,277.64
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)		15,310,064.55		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	$	15,310,064.55	$	0.00
3. Adjustments				
A. Loan Guarantee Modifications	$	0.00	$	0.00
B. Fees Received		0.00		0.00
C. Interest Supplements Paid		(902,864.53)		0.00
D. Foreclosed Property and Loans Acquired		0.00		0.00
E. Claim Payments to Lenders		(14,407,200.02)		(11,436,224.60)
F. Interest Accumulation on the Liability Balance		1,110,906.24		906,670.74
G. Other		(214,947.35)		0.00
H. Total of the above Adjustments	$	(14,414,105.66)	$	(10,529,553.86)
4. Ending Balance of the Loan Guarantee Liability before Reestimates	$	37,633,875.69	$	30,541,723.78
5. Add or Subtract Subsidy Reestimates by Component				
A. Interest Rate Reestimate		0.00		0.00
B. Technical/default Reestimate		0.00		0.00
C. Total of the above Reestimate Components	$	0.00	$	0.00
6. Ending Balance of the Loan Guarantee Liability	$	37,633,875.69	$	30,541,723.78

Fluctuations

The Loan Guarantee Liability balance reflects the business activity conducted during the fiscal year. The Loan Guarantee Liability increased $7.1 million (23%) primarily due to the reestimates completed in the 4th Quarter, FY 2006, and the accrued interest accumulation on uninvested balances for the Military Housing Privatization Initiative (MHPI) Program and the Armanent Retooling and Manufacturing Support (ARMS) Program.

The Department had two defaulted loan guarantees in the ARMS Program. The first loan defaulted in August 1999 and was previously in litigation to determine the actual amount of debt owed. This $11.4 million claim was paid in 2nd Quarter, FY 2006. The second loan defaulted in September 2006. The payment on the loss claim of $15.3 million was paid to the bank in 1st Quarter, FY 2007.

Administrative Expenses

Administrative Expense is limited to separately identified expenses administered for pre FY 1992 and post FY 1991 direct and loan guarantees. The Department does not maintain a separate program to capture the expenses related to direct and guaranteed loans for the MHPI Program and the Foreign Military Financing Program. Administrative Expense for the ARMS Initiative Program is a fee paid to the U.S. Department of Agriculture, Rural Business Cooperative Service for administering the loan guarantees under ARMS. There were no administrative expenses in FY 2007.

Note 9. Inventory and Related Property

As of March 31	2007	2006
1. Inventory, Net	$ 83,615,969,971.39	$ 80,766,122,685.93
2. Operating Materials & Supplies, Net	142,621,643,284.05	145,717,308,852.95
3. Stockpile Materials, Net	981,331,591.32	1,160,084,165.90
4. Total	$ 227,218,944,846.76	$ 227,643,515,704.78

Inventory, Net

As of March 31	2007			2006	
	Inventory, Gross Value	Revaluation Allowance	Inventory, Net	Inventory, Net	Valuation Method
1. Inventory Categories					
A. Available and Purchased for Resale	$ 87,019,088,200.69	$ (29,613,471,402.13)	57,405,616,798.56	$ 55,409,197,690.58	LAC,MAC
B. Held for Repair	30,950,811,436.18	(5,382,598,663.77)	25,568,212,772.41	24,554,139,578.69	LAC,MAC
C. Excess, Obsolete, and Unserviceable	8,586,493,152.18	(8,586,493,152.18)	0.00	0.00	NRV
D. Raw Materials	74,108,911.87	0.00	74,108,911.87	39,683,137.22	MAC,SP,LAC
E. Work in Process	568,031,488.55	0.00	568,031,488.55	763,102,279.44	AC
F. Total	$ 127,198,533,189.47	$ (43,582,563,218.08)	83,615,969,971.39	$ 80,766,122,685.93	

Legend for Valuation Methods:

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

Restrictions

There are no restrictions on disposition of inventory as related to environmental liabilities or issues. Restrictions on disposition related to other liabilities include material pending litigation or negotiation with contractors or common carriers. This material is restricted from disposition until litigation or negotiation is completed. The balance of this restricted inventory as of March 31, 2007, was $62.6 million.

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

- Distributions without reimbursement are made when authorized by Department directives.
- War reserve material includes fuels and subsistence items that are considered restricted.
- Inventory, with the exception of safety stocks, may be sold to foreign, state and local governments, private parties, and contractors in accordance with the current policies and guidance or at the direction of the President.

General Composition of Inventory

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

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

The relevant cost associated with maintaining the available inventory and the time required to replenish the inventory are the criteria used in determining the assigned category.

Operating Materials and Supplies, Net

As of March 31	2007			2006	
	OM&S Gross Value	Revaluation Allowance	OM&S, Net	OM&S, Net	Valuation Method
1. OM&S Categories					
A. Held for Use	$ 126,162,065,298.94	$ (14,863.04)	$ 126,162,050,435.90	$ 129,938,725,169.54	SP, LAC, MAC
B. Held for Repair	17,569,499,541.13	(1,109,906,692.98)	16,459,592,848.15	15,778,583,683.41	SP, LAC, MAC
C. Excess, Obsolete, and Unserviceable	2,885,947,569.16	(2,885,947,569.16)	0.00	0.00	NRV
D. Total	$ 146,617,512,409.23	$ (3,995,869,125.18)	$ 142,621,643,284.05	$ 145,717,308,852.95	

Legend for Valuation Methods:

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

Restrictions

Some munitions included in Operating Material and Supplies (OM&S) are restricted for use. Restricted munitions are items that cannot be expected to meet performance requirements under all conditions. The restricted munitions are only used in emergency combat situations in which no other suitable munitions are immediately available.

General Composition of Operating Materials and Supplies

The OM&S includes spare and repair parts, ammunition, tactical missiles, aircraft configuration pods, and centrally managed aircraft engines held for consumption. The Held for Use category includes a total of $55.0 million held for future use.

The relevant cost associated with maintaining the available operating materials and supplies, as well as the time required to replenish the operating materials and supplies, are the criteria used in determining the assigned category.

Stockpile Materials, Net

As of March 31	2007			2006	
	Stockpile Materials Amount	Allowance for Gains (Losses)	Stockpile Materials, Net	Stockpile Materials, Net	Valuation Method
1. Stockpile Materials Categories					
A. Held for Sale	$ 887,251,144.52	$ 0.00	$ 887,251,144.52	$ 1,066,002,777.12	AC, LCM
B. Held in Reserve for Future Sale	94,080,446.80	0.00	94,080,446.80	94,081,388.78	AC, LCM
C. Total	$ 981,331,591.32	$ 0.00	$ 981,331,591.32	$ 1,160,084,165.90	

Legend for Valuation Methods:

LAC = Latest Acquisition Cost	NRV = Net Realizable Value
SP = Standard Price	LCM = Lower of Cost or Market
AC = Actual Cost	O = Other

Restrictions

There are legal restrictions on the use of stockpile materials. All materials held by the National Defense Stockpile (NDS) are classified as Material Held in Reserve until congressional action declares the materials are no longer required to be stockpiled, and are available for sale on the open market. Disposals cannot be made from the stockpile except under the following situations: (1) necessary upgrading, refining, or processing, (2) necessary rotation to prevent deterioration, (3) determination as excess with potential financial loss if retained, and (4) as authorized by law.

Mercury sales were voluntarily suspended by the NDS in 1994. The suspension was in response to concerns raised by the U.S. Environmental Protection Agency regarding the accumulation of mercury in the global environment. An Environmental Impact Statement was issued and storage consolidation at Hawthorne, Nevada, was the selected alternative.

Additional restrictions on the use of material are being proposed in the Requirements Report to Congress for beryllium metal, mica block, and quartz.

General Composition of Stockpile Materials

Stockpile materials are strategic and critical materials held due to statutory requirements for use in national defense, conservation, or national emergencies.

The Annual Materials Plan lists the maximum quantity of each commodity that may be sold by the Department in a given fiscal year. Before any materials may be sold, Congress must enact specific enabling legislation (e.g., the National Defense Authorization Act). When NDS receives authorization to offer materials for sale, NDS removes the materials from Material Held in Reserve and reclassifies them as Materials Held for Sale. The estimated market price of the stockpile materials held for sale is $1.5 billion.

Note 10. General PP&E, Net

As of March 31	2007					2006
	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	$ 10,500,053,778.91	N/A	$ 10,500,053,778.91	$ 10,501,884,546.15
B. Buildings, Structures, and Facilities	S/L	20 Or 40	169,755,738,760.45	$ (99,664,511,675.92)	70,091,227,084.53	68,451,693,297.48
C. Leasehold Improvements	S/L	lease term	482,436,819.24	(297,982,143.24)	184,454,676.00	169,102,544.57
D. Software	S/L	2-5 Or 10	8,958,694,096.83	(5,411,326,073.71)	3,547,368,023.12	3,704,028,520.30
E. General Equipment	S/L	5 or 10	60,754,186,060.57	(44,328,077,777.71)	16,426,108,282.86	18,225,246,489.01
F. Military Equipment	S/L	Various	656,429,022,922.25	(305,586,477,878.43)	350,842,545,043.82	346,990,000,000.00
G. Assets Under Capital Lease	S/L	lease term	836,944,419.67	(564,703,872.12)	272,240,547.55	163,647,939.31
H. Construction-in-Progress	N/A	N/A	19,986,048,129.86	N/A	19,986,048,129.86	21,079,262,037.39
I. Other			67,165,801.63	(1,213,341.35)	65,952,460.28	65,130,525.43
J. Total General PP&E			$ 927,770,290,789.41	$ (455,854,292,762.48)	$ 471,915,998,026.93	$ 469,349,995,899.64

[1] Note 15 for additional information on Capital Leases

Legend for Valuation Methods:

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

Military Equipment

The Department changed its method of valuing military equipment in 3rd Quarter, FY 2006. The FY 2007 values for military equipment above are based on internal records. Previously, military equipment was valued based upon estimates using Bureau of Economic Analysis data. The Department recorded a prior period adjustment in 3rd Quarter, FY 2006, restating comparative asset values. Due to system deficiencies, the prior period adjustment did not restate intervening comparative quarters, and thus the 2nd Quarter, FY 2006, comparative balances above do not reflect the correction. The net values of Military Equipment and Total General Property, Plant and Equipment (PP&E) above are each overstated by approximately $8 billion.

Heritage Assets and Stewardship Land

The Federal Accounting Standards Advisory Board, Statement of Federal Financial Accounting Standards 29, "Heritage Assets and Stewardship Land," requires note disclosures for heritage assets and stewardship land. The Department is committed to preserving and accounting for its heritage assets' historical, cultural, educational, or artistic importance. Additionally, the Department possesses and maintains land not acquired in connection with General PP&E, land donated to the Federal Government, and land previously recorded as public domain.

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

Other Disclosures

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

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

Assets Under Capital Lease

As of March 31	2007	2006
1. Entity as Lessee, Assets Under Capital Lease		
A. Land and Buildings	$ 605,352,373.89	$ 619,551,791.97
B. Equipment	231,592,045.78	11,024,208.16
C. Accumulated Amortization	(564,703,872.12)	(466,928,060.82)
D. Total Capital Leases	$ 272,240,547.55	$ 163,647,939.31

Note 11. Liabilities Not Covered by Budgetary Resources

As of March 31		2007		2006
1. Intragovernmental Liabilities				
A. Accounts Payable	$	1,628,109.00	$	1,121,856.73
B. Debt		1,816,773,566.71		2,009,597,857.82
C. Other		7,633,814,059.62		7,129,972,277.67
D. Total Intragovernmental Liabilities	$	9,452,215,735.33	$	9,140,691,992.22
2. Nonfederal Liabilities				
A. Accounts Payable	$	470,335,851.29	$	441,736,055.52
B. Military Retirement and Other Federal Employment Benefits		1,466,636,166,982.52		1,428,373,446,300.67
C. Environmental Liabilities		65,595,026,232.83		59,944,112,206.31
D. Other Liabilities		15,392,529,941.81		13,681,802,808.79
E. Total Nonfederal Liabilities	$	1,548,094,059,008.50	$	1,502,441,097,371.30
3. Total Liabilities Not Covered by Budgetary Resources	$	1,557,546,274,743.80	$	1,511,581,789,363.50
4. Total Liabilities Covered by Budgetary Resources	$	409,444,011,902.99	$	365,717,174,719.54
5. Total Liabilities	$	1,966,990,286,646.80	$	1,877,298,964,083.00

Liabilities Not Covered by Budgetary Resources are those liabilities which are not legally obligated with realized budgetary resources as of the Balance Sheet date.

Other Disclosures

Military Retirement and Other Federal Employment Benefits not covered by budgetary resources are comprised of various employee actuarial liabilities. Refer to Note 17, Military Retirement and Other Federal Employment Benefits, for additional details and disclosures.

Intragovernmental Liabilities Other are comprised of $6.5 billion in custodial liabilities and $1.1 billion in unfunded Employment Compensation Act liabilities.

Military Retirement and Other Federal Employment Benefits are primarily comprised of $732.4 billion in pension liabilities and $725.3 billion in health benefit liabilities.

Nonfederal Other Liabilities are primarily comprised of $8.4 billion in unfunded annual leave liabilities, $2.6 billion in contingent liabilities, $2.0 billion in custodial liabilities and $1.4 billion in estimated contingent legal liabilities.

Note 12. Accounts Payable

As of March 31	2007			2006
	Accounts Payable	Interest, Penalties, and Administrative Fees	Total	Total
1. Intragovernmental Payables	$ 2,149,601,594.37	$ N/A	$ 2,149,601,594.37	$ 2,532,992,055.47
2. Nonfederal Payables (to the Public)	25,993,800,729.18	2,036,813.24	25,995,837,542.42	29,333,570,787.58
3. Total	$ 28,143,402,323.55	$ 2,036,813.24	$ 28,145,439,136.79	$ 31,866,562,843.05

Fluctuations

Intragovernmental accounts payable decreased $383.6 million (15%), primarily due to a decrease of $208.4 million in accounts payable to the Department of State and the U.S. Postal Service. In addition, 2nd Quarter, FY 2006, accounts payable to the Department of Homeland Security were overstated by $99.0 million due to an error made in FY 2005. The error was corrected in the 3rd Quarter, FY 2006.

Nonfederal payables decreased $3.3 billion (11%) primarily due to improved business practices on the part of the Marine Corps. The deployment and use of Wide Area Work Flow for receipt processing assisted in reducing Marine Corps nonfederal payables by $1.9 billion. In addition, the Air Force General Fund reported a $1.1 billion decrease for the purchase of military aircraft because of the return to normal aircraft production levels.

Note 13. Debt

As of March 31	2007			2006	
	Beginning Balance	Net Borrowing	Ending Balance	Net Borrowing	Ending Balance
1. Agency Debt (Intragovernmental)					
A. Debt to the Treasury	$ 581,560,522.03	$ 21,047,186.87	$ 602,607,708.90	$ 76,168,556.36	$ 740,778,591.77
B. Debt to the Federal Financing Bank	2,917,707,192.08	(28,298,961.66)	2,889,408,230.42	(120,224,190.88)	3,405,594,620.06
C. Total Agency Debt	$ 3,499,267,714.11	$ (7,251,774.79)	$ 3,492,015,939.32	$ (44,055,634.52)	$ 4,146,373,211.83
2. Total Debt	$ 3,499,267,714.11	$ (7,251,774.79)	$ 3,492,015,939.32	$ (44,055,634.52)	$ 4,146,373,211.83

Fluctuations

The total agency debt decreased $654.4 million (16%) primarily due to $399.8 million in payments to reduce debt to the Federal Financing Bank for pre-1992 loans for Foreign Military Sales during the 2nd Quarter, FY 2007 and $152.5 million in principal payments to the U.S. Treasury for post-1991 direct loans between 2nd Quarter, FY 2006 and FY 2007.

Other Information Related to Debt

The outstanding debt consists of interest and principal payments due to the U.S. Treasury and the Federal Financing Bank. The Department borrows funds for Foreign Military Sales, Navy - Ship Leasing and the Military Housing Privatization Initiative (MHPI).

Other Disclosures

Beginning in the 1st Quarter, FY 2007, the Department implemented a new requirement from the Office of Management and Budget Circular A-136, "Financial Reporting Requirements," which states that the Department will include programs that are executed on behalf of the Executive Office of the President as part of the basic financial statements, rather than in the Other Accompanying Information section of the financial statements.

Note 14. Environmental Liabilities and Disposal Liabilities

As of March 31	2007			2006
	Current Liability	Noncurrent Liability	Total	Total
1. Environmental Liabilities-- Nonfederal				
A. Accrued Environmental Restoration Liabilities				
1. Active Installations—Installation Restoration Program (IRP) and Building Demolition and Debris Removal (BD/DR)	$ 1,177,462,908.99	$ 7,525,849,520.89	$ 8,703,312,429.88	$ 9,401,791,610.94
2. Active Installations—Military Munitions Response Program (MMRP)	105,410,845.00	5,260,435,359.49	5,365,846,204.49	7,034,629,000.00
3. Formerly Used Defense Sites—IRP and BD/DR	142,830,000.00	3,952,339,000.00	4,095,169,000.00	4,165,485,000.00
4. Formerly Used Defense Sites--MMRP	87,948,000.00	14,665,871,000.00	14,753,819,000.00	14,566,691,000.00
B. Other Accrued Environmental Liabilities—Active Installations				
1. Environmental Corrective Action	59,342,529.35	686,484,768.85	745,827,298.20	653,377,632.85
2. Environmental Closure Requirements	7,588,000.00	988,900,120.00	996,488,120.00	358,678,594.00
3. Environmental Response at Operational Ranges	37,277,000.00	230,863,417.00	268,140,417.00	316,085,000.00
4. Other	88,517,821.55	726,068,941.40	814,586,762.95	683,856,883.74
C. Base Realignment and Closure (BRAC)				
1. Installation Restoration Program	245,674,683.33	3,164,567,485.96	3,410,242,169.29	2,738,458,639.36
2. Military Munitions Response Program	19,781,119.00	887,954,929.00	907,736,048.00	731,533,000.00
3. Environmental Corrective Action / Closure Requirements	31,920,988.00	129,980,024.37	161,901,012.37	271,082,344.59
4. Other	144,557,000.00	0.00	144,557,000.00	358,495,584.41
D. Environmental Disposal for Weapons Systems Programs				
1. Nuclear Powered Aircraft Carriers	0.00	5,668,309,534.27	5,668,309,534.27	5,600,200,000.00
2. Nuclear Powered Submarines	484,006,242.85	3,202,361,597.94	3,686,367,840.79	5,966,000,000.00
3. Other Nuclear Powered Ships	226,908,489.60	66,535,508.00	293,443,997.60	332,300,000.00
4. Other National Defense Weapons Systems	777,625.80	208,732,486.56	209,510,112.36	435,941,541.25
5. Chemical Weapons Disposal Program	1,497,558,000.00	14,921,284,000.00	16,418,842,000.00	9,925,048,000.00
6. Other	0.00	3,237,406,105.00	3,237,406,105.00	55,260,851.26
2. Total Environmental Liabilities	$ 4,357,561,253.47	$ 65,523,943,798.73	$ 69,881,505,052.20	$ 63,594,914,682.40

Service Component – Environmental Restoration (Cleanup) Liabilities and Environmental Disposal Liabilities (Amounts in millions)	Army	Navy	Air Force	ODO	Total
1. Environmental Liabilities-Nonfederal					
A. Accrued Environmental Restoration Liabilities:					
1. Active Installations--Installation Restoration Program (IRP) and Building Demolition and Debris Removal (BD/DR)	$ 2,743.8	$ 2,273.2	$ 3,464.5	$ 221.8	$ 8,703.3
2. Active Installations--Military Munitions Response Program (MMRP)	3,304.4	667.7	1,393.7	0.0	5,365.8
3. Formerly Used Defense Sites--IRP and BD/DR	4,095.1	0.0	0.0	0.0	4,095.1
4. Formerly Used Defense Sites--MMRP	14,753.8	0.0	0.0	0.0	14,753.8
B. Other Accrued Environmental Liabilities--Active Installations					
1. Environmental Corrective Action	404.7	46.7	132.2	162.2	745.8
2. Environmental Closure Requirements	96.9	773.3	99.5	26.8	996.5
3. Environmental Response at Operational Ranges	226.0	41.3	0.0	0.9	268.2
4. Other	720.3	2.6	0.0	91.7	814.6
C. Base Realignment and Closure (BRAC)					
1. Installation Restoration Program	523.7	1,697.0	1,153.6	36.0	3,410.3
2. Military Munitions Response Program	800.3	107.5	0.0	0.0	907.8
3. Environmental Corrective Action/Closure Requirements	32.3	51.7	77.9	0.0	161.9
4. Other	144.6	0.0	0.0	0.0	144.6
D. Environmental Disposal for Weapons Systems Programs					
1. Nuclear Powered Aircraft Carriers	0.0	5,668.2	0.0	0.0	5,668.2
2. Nuclear Powered Submarines	0.0	3,686.4	0.0	0.0	3,686.4
3. Other Nuclear Powered Ships	0.0	293.4	0.0	0.0	293.4
4. Other National Defense Weapons Systems	0.0	209.5	0.0	0.0	209.5
5. Chemical Weapons Disposal Program	16,418.9	0.0	0.0	0.0	16,418.9
6. Other	0.0	3,237.4	0.0	0.0	3,237.4
2. Total Nonfederal Environmental Liabilities:	**$ 44,264.8**	**$ 18,755.9**	**$ 6,321.4**	**$ 539.4**	**$ 69,881.5**

Fluctuations

Environmental liabilities increased by $6.3 billion (10%). This is attributable to an improved cost estimate for the destruction of chemical weapons based on actual historical data from seven chemical demilitarization sites. The previous estimate was based on selected historical information primarily from two sites.

Others Category Disclosure Comparative Table

Types (Amounts in millions)	March 31, 2007	March 31, 2006
Other Accrued Environmental Liabilities-Active Installations-Other		
U.S. Army Corps of Engineers Pollution Control & Abatement related to the Formerly Utilized Sites Remedial Action Program (FUSRAP)	$653.3	$618.0
U.S. Army Corps of Engineers Pollution Control & Abatement not related to FUSRAP	6.2	0.0
Army Low Level Radioactive Waste Program	60.8	35.7
National Defense Stockpile Transaction	50.5	0.0
Defense Commissary Agency – Asbestos and/or Lead Based Paint	29.9	30.2
TRICARE Management Activity Uniformed Services University of Health Sciences	11.3	0.0
Navy estimate for disposal of Polychlorinated Biphenyls transformers.	2.6	0.0
Total	**$814.6**	**$683.9**
Base Realignment and Closure (BRAC)-Other		
Army unliquidated obligations associated with clean-up contracts at BRAC installations	$144.6	$140.4
Manpower services at BRAC installations and headquarters offices	0.0	218.1
Total	**$144.6**	**$358.5**
Environmental Disposal for Weapons Systems Programs-Other		
Navy Spent Nuclear Fuel	$3,237.4	$0.0
National Defense Stockpile -Other Defense Organizations (ODO)	0.0	51.0
ASA (FM&C) Emergency Response Fund - ODO	0.0	0.2
Under Secretary of Defense - Operation and Maintenance - ODO	0.0	4.1
Total	**$3,237.4**	**$55.3**

Environmental Disclosures

As of March 31	2007	2006
A. Amount of operating and capital expenditures used to remediate legacy waste. Legacy wastes are the remediation efforts covered by IRP, MMRP, and BD/DR regardless of funding source.	371,400,911.91	606,142,645.74
B. The unrecognized portion of the estimated total cleanup costs associated with general property, plant, and equipment.	1,563,833,359.90	1,373,134,941.00
C. The estimated cleanup costs associated with general property, plant, and equipment placed into service during each fiscal year.	54,239,865.77	97,000.00
D. Changes in total cleanup costs due to changes in laws, regulations, and/or technology.	0.00	0.00
E. Portion of the changes in estimated costs due to changes in laws and technology that is related to prior periods.	0.00	0.00

Environmental Disclosures – Line A represents the amount of operating and capital expenditures used to remediate legacy waste. The amount on Line A is attributable to DERP activity which was established to clean up or control hazardous waste and Base Realignment and Closure (BRAC) activity which leads to environmental corrective actions and environmental restoration cleanup. The Department is implementing procedures to more accurately disclose the amount of operating and capital resources disbursed to remediate legacy waste.

Environmental Disclosures – Line B represents the unrecognized costs associated with General Property, Plant, and Equipment (PP&E). The unrecognized portion of the estimated total cleanup costs is associated with Non-DERP, such as nuclear-powered carriers and submarines, conventional ships, spent nuclear fuel, and landfills. The Department is implementing procedures to more accurately disclose the unrecognized portion of the estimated cleanup costs associated with General PP&E.

Environmental Disclosures – Line C represents the estimated cleanup costs associated with General PP&E placed into service during each fiscal year and is associated with environmental disposal of weapons systems programs.

Environmental Disclosures – Line D represents the amount of changes in total cleanup costs due to changes in laws, regulations, and/or technology. The Department is unable to report this cost due to system and internal control weaknesses. The Department is implementing procedures in FY 2007 to more accurately disclose changes in total cleanup costs due to changes in laws, regulations, and/or technology.

Environmental Disclosures – Line E represents the portion of changes in estimated costs due to changes in laws and technology that is related to prior periods. The Department is unable to report this amount due to system and internal control weaknesses. The Department is implementing procedures in FY 2007 to more accurately disclose the amount of change in estimates for cost due to changes in laws and technology relating to prior periods.

Other Disclosures

Applicable Laws and Regulations for Cleanup Requirements

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

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

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

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

Methods for Assigning Total Cleanup Costs to Current Operating Periods

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

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

For General PP&E placed into service after September 30, 1997, the Department expenses the associated environmental costs systematically over the life of the asset. The Department expenses the full cost to clean up contamination for Stewardship PP&E at the time the asset is placed into service.

The Department uses two methods for systematic recognition: physical capacity for operating landfills, and life expectancy in years for all other assets.

Types of Environmental Liabilities and Disposal Liabilities Identified

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

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

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

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

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

The Department is uncertain regarding the extent of the liabilities at installations that are realigning or closing as a result of BRAC requirements. The Department is in the process of determining the extent of environmental liabilities at BRAC installations, in particular those liabilities associated with unexploded ordnance on training ranges.

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

The Army has a liability to take environmental restoration/corrective action for buried chemical munitions, and agents. The Army is unable to provide a reasonable estimate at this time, because the extent of the buried chemical munitions and agents is not known.

The USACE is unable to provide a complete estimate for FUSRAP. The USACE has studies on-going and will update its liabilities as it identifies additional liabilities.

Note 15. Other Liabilities

As of March 31	2007			2006
	Current Liability	Noncurrent Liability	Total	Total
1. Intragovernmental				
A. Advances from Others	$ 319,254,547.66	$ 0.00	$ 319,254,547.66	$ 328,761,484.62
B. Deposit Funds and Suspense Account Liabilities	1,787,557,910.31	0.00	1,787,557,910.31	1,382,896,818.64
C. Disbursing Officer Cash	1,994,065,435.69	0.00	1,994,065,435.69	1,938,065,746.42
D. Judgment Fund Liabilities	165,484,728.16	0.00	165,484,728.16	161,835,240.45
E. FECA Reimbursement to the Department of Labor	798,843,873.57	566,927,966.13	1,365,771,839.70	1,272,190,388.88
F. Other Liabilities	5,426,118,937.70	1,607,177,083.21	7,033,296,020.91	6,524,503,841.44
G. Total Intragovernmental Other Liabilities	$ 10,491,325,433.09	$ 2,174,105,049.34	$ 12,665,430,482.43	$ 11,608,253,520.45
2. Nonfederal				
A. Accrued Funded Payroll and Benefits	$ 4,112,223,398.50	$ 0.00	$ 4,112,223,398.50	$ 7,674,686,067.17
B. Advances from Others	8,603,273,300.07	0.00	8,603,273,300.07	1,964,041,305.78
C. Deferred Credits	0.00	0.00	0.00	11,800,000.00
D. Deposit Funds and Suspense Accounts	216,600,425.65	0.00	216,600,425.65	204,942,296.72
E. Temporary Early Retirement Authority	0.00	0.00	0.00	159,620.76
F. Nonenvironmental Disposal Liabilities				
(1) Military Equipment (Nonnuclear)	10,763,503.29	244,999,739.95	255,763,243.24	685,040,622.10
(2) Excess/Obsolete Structures	59,412,000.00	626,206,000.00	685,618,000.00	235,897,000.00
(3) Conventional Munitions Disposal	0.00	1,406,060,320.00	1,406,060,320.00	1,184,317,440.31
G. Accrued Unfunded Annual Leave	8,488,508,040.34	0.00	8,488,508,040.34	8,372,695,266.77
H. Capital Lease Liability	26,965,765.76	178,906,435.26	205,872,201.02	245,246,234.61
I. Other Liabilities	8,897,534,806.06	3,454,076,008.96	12,351,610,815.02	9,415,625,833.56
J. Total Nonfederal Other Liabilities	$ 30,415,281,239.67	$ 5,910,248,504.17	$ 36,325,529,743.84	$ 29,994,451,687.78
3. Total Other Liabilities	$ 40,906,606,672.76	$ 8,084,353,553.51	$ 48,990,960,226.27	$ 41,602,705,208.23

Fluctuations

Total Nonfederal Other Liabilities increased $6.3 billion (21%) primarily due to a $6.6 billion increase in advances from others. This increase represents advances received from foreign governments in the Foreign Military Sales Trust Fund and is due to the change in Office of Management and Budget (OMB) Circular A-136, "Financial Reporting Requirements." Effective 1st Quarter, FY 2007, OMB directed the Department to include programs that are executed on behalf of the Executive Office of the President. Previous reporting of this information was included in the Other Accompanying Information (OAI) section of the financial statements. In addition, the Department changed the method for reporting these advances. In previous years, only the year-to-date amount of the advance was reported in OAI.

Other Disclosures

Intragovernmental Other Liabilities are comprised of approximately $6.0 billion in custodial liabilities from accounts receivable for cancelled appropriations and interest, penalties, fines, and administrative fees from the public. The amounts collected cannot be used by the Department and must be distributed to the U.S. Treasury.

Nonfederal Other Liabilities consist of approximately $4.7 billion in contingencies, $3.5 billion in accrued liabilities for contractual services, and $2.0 billion in custodial liabilities.

Contingent Liabilities includes $1.6 billion in estimated future contract financing payments that will be paid to the contractor upon delivery and Government acceptance of a satisfactory product. In accordance with contract terms, specific rights to the contractor's work vests with the Government when a specific type of contract financing payment is made. This action protects taxpayer funds in the event of contract nonperformance. These rights should not be misconstrued as the rights of ownership. The Department is under no obligation to pay the contractor for amounts greater than the amounts authorized in the contract until delivery and Government acceptance of a satisfactory product. Because it is probable that the contractor will complete its efforts and deliver a satisfactory product to the Department and the amount of potential future payments are estimable, the Department has recognized a contingent liability for estimated future payments, which are conditional pending delivery and Government acceptance of a satisfactory product.

Agency Wide

Capital Lease Liability

As of March 31	2007				2006
	Asset Category				
	Land and Buildings	Equipment	Other	Total	Total
1. Future Payments Due					
A. 2007	$ 28,109,458.45	$ 2,671,132.93	$ 0.00	$ 30,780,591.38	$ 32,022,003.72
B. 2008	47,123,104.55	155,951.00	0.00	47,279,055.55	59,036,839.78
C. 2009	43,853,305.76	93,058.00	0.00	43,946,363.76	51,158,055.55
D. 2010	43,853,305.76	0.00	0.00	43,853,305.76	43,946,363.76
E. 2011	41,295,407.67	0.00	0.00	41,295,407.67	43,853,305.76
F. 2012	13,087,621.97	0.00	0.00	13,087,621.97	0.00
G. After 5 Years	31,011,160.44	0.00	0.00	31,011,160.44	37,389,143.94
H. Total Future Lease Payments Due	$ 248,333,364.60	$ 2,920,141.93	$ 0.00	$ 251,253,506.53	$ 267,405,712.51
I. Less: Imputed Interest Executory Costs	45,304,263.29	77,042.21	0.00	45,381,305.50	63,454,885.59
J. Net Capital Lease Liability	$ 203,029,101.31	$ 2,843,099.72	$ 0.00	$ 205,872,201.03	$ 203,950,826.92
2. Capital Lease Liabilities Covered by Budgetary Resources				$ 168,493,883.32	$ 172,597,428.36
3. Capital Lease Liabilities Not Covered by Budgetary Resources				$ 37,378,317.70	$ 72,648,806.25

All leases entered into prior to FY 1992 are funded on an annual basis and subject to the availability of funds. Noncurrent amounts for these leases are shown as not covered by budgetary resources.

Note 16. Commitments and Contingencies

Legal Contingencies

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

The OGC reassesses legal cases annually at fiscal year (FY) end. In FY 2006, the Department reported 65 legal actions with individual claims greater than the Department-wide materiality threshold for reporting litigation, claims, or assessments of $107.6 million. Management determined that claims totaling approximately $484.2 billion had a remote probability of an adverse decision against the Department. The Department also had a number of potential claims that individually did not meet the $107.6 million threshold materiality at the DoD-wide level, but did meet individual DoD Component thresholds. These claims should be disclosed in the Components' financial statements.

The materiality threshold for FY 2007 has been determined to be $110.5 million per individual case. The Department is currently assessing cases meeting that threshold for FY 2007 year end reporting.

Other Commitments and Contingencies

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

Note 17. Military Retirement and Other Federal Employment Benefits

As of March 31	2007				2006
	Present Value of Benefits	Assumed Interest Rate (%)	(Less: Assets Available to Pay Benefits)	Unfunded Liability	Present Value of Benefits
1. Pension and Health Actuarial Benefits					
A. Military Retirement Pensions	$ 963,696,276,612.06	6.0	$ (231,291,397,383.62)	$ 732,404,879,228.44	$ 892,111,600,551.72
B. Military Retirement Health Benefits	299,203,802,000.00	6.25	0.00	299,203,802,000.00	296,473,202,000.00
C. Military Medicare-Eligible Retiree Benefits	538,032,547,000.00	6.25	(111,867,461,969.41)	426,165,085,030.59	537,397,092,000.00
D. Total Pension and Health Actuarial Benefits	$ 1,800,932,625,612.10		$ (343,158,859,353.03)	$ 1,457,773,766,259.00	$ 1,725,981,894,551.70
2. Other Actuarial Benefits					
A. FECA	$ 6,855,989,000.01	5.17	$ 0.00	$ 6,855,989,000.01	$ 6,918,865,000.04
B. Voluntary Separation Incentive Programs	1,391,124,000.00	4.0	(707,366,619.77)	683,757,380.23	1,495,755,463.00
C. DoD Education Benefits Fund	1,785,339,161.00	5.2	(462,684,817.75)	1,322,654,343.25	1,661,351,399.00
D. Total Other Actuarial Benefits	$ 10,032,452,161.01		$ (1,170,051,437.52)	$ 8,862,400,723.49	$ 10,075,971,862.04
3. Other Federal Employment Benefits	$ 5,477,654,643.43		$ (4,110,807,890.91)	$ 1,366,846,752.52	$ 0.00
4. Total Military Retirement and Other Federal Employment Benefits:	$ 1,816,442,732,416.50		$ (348,439,718,681.46)	$ 1,468,003,013,735.00	$ 1,736,057,866,413.70

Actuarial Cost Method Used: Aggregate entry-age method
Assumptions: See below
Market Value of Investments in Market-based and Marketable Securities: $326.9 billion

Fluctuations

The present value of Military Retirement and Other Federal Employment Benefits increased $80.4 billion (5%) and is primarily attributable to an increase of $71.6 billion (8%) in the actuarial liability for Military Retirement Pensions. Other Federal Employment Benefits due and payable contributed another $5.5 billion to the increase. In prior years, these liabilities were reported in Note 15, Other Liabilities.

Military Retirement Pensions

The $71.6 billion increase in the actuarial liability for Military Pensions primarily results from a decrease in the assumed interest rate on invested balances, and thus a decrease in the associated assumed earning that reflects a $32.8 billion increase in the actuarial liability. The majority of the remaining change is due to expected liability increases.

The Military Retirement Fund is a single-employer, defined benefit plan authorized by Public Law 98-94. Administrative costs of the Fund are not ascertainable. Projected revenues into the Fund come from three sources: interest earnings on Fund assets, monthly Department contributions, and annual contributions from the U. S. Treasury. The monthly Department contributions are determined as a percentage of basic pay as approved by the Department's Retirement Board of Actuaries. The annual contribution from U. S. Treasury is paid into the Fund at the beginning of each fiscal year, and represents the amortization of the unfunded liability for service performed prior to October 1, 1984, as well as the amortization of actuarial gains and losses that have since arisen. Effective FY 2005, the U. S. Treasury began making an annual contribution to the Fund that represents the normal cost amount for the concurrent receipt provisions of the FY 2004 National Defense

Authorization Act. The Board of Actuaries determine the U. S. Treasury's contribution, and the Secretary of Defense directs the Secretary of Treasury to make the payment.

The long-term economic assumptions for each valuation are set by the Department's Retirement Board of Actuaries. The long-term assumptions for the FY 2005 valuation were 6.25% interest, 3.0% Consumer Price Index, and 3.75% salary increase. The long-term economic assumption for interest was lowered to 6.00% by the Board at its August 2006 meeting. Other assumptions used to calculate the actuarial liabilities, such as mortality and retirement rates, were based on actual experience. Because of reporting deadlines, the current year actuarial present value of projected plan benefits is rolled forward, using accepted actuarial methods, from the prior year valuation results as reported in the Department's Office of Actuary Valuation of the Military Retirement System. For purposes of the Fund's financial reporting, this process is applied annually. In calculating the FY 2006 roll-forward amount, the following assumptions were used:

	Inflation	Salary	Interest
Fiscal Year 2006	4.1% (actual)	3.1% (actual)	6.0%
Fiscal Year 2007	3.0% (estimated)	2.7% (estimated)	6.0%
Long-Term	3.0%	3.75%	6.0%

Change in MRF Actuarial Liability	(Amounts in billions)
Actuarial Liability as of 9/30/05	$892.1
Expected Normal Cost for FY 2006	15.5
Plan Amendment Liability	0.1
Assumption Change Liability	35.4
Expected Benefit Payments for FY 2006	(40.5)
Interest Cost for FY 2006	55.0
Actuarial (gains)/losses due to changes in trend assumptions	6.1
Actuarial Liability as of 09/30/06	$963.7
Change in Actuarial Liability	$71.6

Actuarial Cost Method Used: Aggregate entry-age normal method.
Market Value of Investments in Market-Based and Marketable Securities: $221.5 billion
Assumed Interest Rate: 6%

Military Retirement Health Benefits (MRHB)

The MRHB are post-retirement benefits the Department provides to non-Medicare-eligible military retirees and other eligible beneficiaries who are not Medicare-eligible, through private sector health care providers and Department Medical Treatment Facilities.

Change in MRHB Actuarial Liability	(Amounts in billions)
Actuarial Liability as of 09/30/05 (Department preMedicare + all uniformed services Medicare cost-basis effect)	$296.5
Expected Normal Cost for FY 2006	10.0
Expected Benefit Payments for FY 2006	(9.3)
Interest Cost for FY 2006	18.9
Actuarial (gains)/losses due to other factors	39.4
Actuarial (gains)/losses due to changes in trend assumptions	(56.3)
Actuarial Liability as of 09/30/06 (Department preMedicare + all uniformed services Medicare cost-basis effect)	$299.2
Change in Actuarial Liability	$ 2.7

Actuarial Cost Method Used: Aggregate Entry-Age Normal Method
Assumed Interest Rate: 6.25%

Medical Trend	FY 2005 – FY 2006	Ultimate Rate - 2030
Medicare Inpatient:	5.62%	6.25%
Medicare Outpatient:	7.83%	6.25%
Medicare Prescriptions (Direct Care):	8.13%	6.25%
Medicare Prescriptions (Purchased Care)	11.22%	6.25%
Non-Medicare Inpatient (Direct Care):	7.50%	6.25%
Non-Medicare Outpatient (Direct Care):	4.00%	6.25%
Non-Medicare Prescriptions (Direct Care):	7.00%	6.25%
Non-Medicare Inpatient (Purchased Care):	10.40%	6.25%
Non-Medicare Outpatient (Purchased Care):	7.40%	6.25%
Non-Medicare Prescriptions (Purchased Care):	12.11%	6.25%

Other Information

The MRHB liability represents the Department's preMedicare liabilities for direct care and purchase care benefits, plus the direct-care cost-basis effect for Medicare liabilities for all Uniformed Services. The cost-basis effect is approximately $28 billion as of September 30, 2006, and arises because liabilities for direct care in the total retiree health liability are valued at a higher cost basis than they are in the Medicare Eligible Retiree Health Care Fund (MERHCF) liability. The $299.2 billion liability includes $298.5 billion for the Department, $600.0 million for the Coast Guard, $69.8 million for the Public Health Service and $4.6 million for the National Oceanic and Atmospheric Administration (NOAA). For purposes of the Fund's financial reporting, the liability is calculated annually.

The actuarial liability reported above does not include $1.4 billion in incurred but not reported liabilities as of March 31, 2007. These liabilities are reflected in Other Federal Employment Benefits in the table above.

Military Medicare-Eligible Retiree Benefits

Public Law 106-398 authorized the establishment of MERHCF for the purpose of accumulating funds to finance the health care program liabilities of Medicare-eligible retirees for all the Uniformed Services and specific Medicare-eligible beneficiaries beginning operations October 1, 2002. Projected revenues into MERHCF, authorized by Chapter 56 of Title 10, United States Code, come from three sources: interest earnings on Fund assets, annual Uniformed Services "normal cost" contributions, and annual contributions from the U. S. Treasury. Prior to October 1, 2005, the normal cost contributions by the Services were paid monthly at per capita amount times actual end strength as approved by the Department's Board of Actuaries. Beginning in FY 2006, the normal cost is paid annually at the beginning of the fiscal year by the U. S. Treasury, from amounts appropriated to the Military Services, and is calculated at the approved rate times the budgeted force strengths. The contribution from U. S. Treasury is also paid into the Fund at the beginning of each fiscal year and represents the amortization of the unfunded liability for services performed prior to October 1, 2002, as well as the amortization of actuarial gains and losses that have since arisen. The Department's Board of Actuaries determines U. S. Treasury's contribution, and the Secretary of Defense directs the Secretary of Treasury to make the payment.

Assumptions used to calculate the actuarial liabilities, such as mortality and retirement rates, were based on actual experience. Claim cost assumptions for direct care were based on actual experience. Assumptions for purchased care were developed from industry-based cost estimates adjusted to approximate the military retired population. Because of reporting deadlines, the current year actuarial present value of projected plan benefits is rolled forward, using accepted actuarial methods, from the prior year's results. For purposes of the Fund's financial reporting, this process is applied annually. In calculating the FY 2006 roll-forward amount, the following medical trend assumptions were used:

Medical Trend	FY 2005 - FY 2006	Ultimate Rate - 2030
Medicare Inpatient:	5.62%	6.25%
Medicare Outpatient:	7.83%	6.25%
Medicare Prescriptions (Direct Care):	8.13%	6.25%
Medicare Prescriptions (Purchased Care):	11.22%	6.25%

Changes in MERHCF Actuarial Liability

	(Amounts in billions)
Actuarial Liability as of 09/30/05 (all uniformed services Medicare)	$537.4
Expected Normal Cost for FY 2006	11.0
Expected Benefit Payments for FY 2006	(7.5)
Interest Cost for FY 2006	34.1
Actuarial (gains)/losses due to other factors	42.1
Actuarial (gains)/losses due to changes in trend assumptions	(79.1)
Actuarial Liability as of 09/30/06 (all uniformed services Medicare)	$538.0
Change in Actuarial Liability	$0.6

Actuarial Cost Method Used for MERHCF Liability: Aggregate Entry-Age Normal
Market Value of Investments in Market-Based and Marketable Securities: $107.3 billion
Assumed Interest Rate: 6.25%

The MERHCF liability includes Medicare liabilities for all Uniformed Services. The $538.0 billion liability includes $526.3 billion for the Department, $10.5 billion for the Coast Guard, $1.1 billion for the Public Health Service and $100.0 million for NOAA. The FY 2006 contributions from each of the services were: $10.8 billion by the Department, $300.0 million by the Coast Guard, $34.5 million by the Public Health Service, and $1.6 million by NOAA.

The actuarial liability reported above does not include $587.8 million in incurred but not reported liabilities as of March 31, 2007. These liabilities are reflected in Other Federal Employment Benefits in the table above.

Federal Employees Compensation Act (FECA)

Assumptions

The liability for future workers' compensation benefits includes the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases, plus a component for incurred but not reported claims. The liability is determined annually using a method that utilizes historical benefit payment patterns related to a specific incurred period to predict the ultimate payments related to that period. Consistent with past practice, these projected annual benefit payments have been discounted to present value using the Office of Management and Budget's economic assumptions for 10-year U. S. Treasury notes and bonds. A 5.17% interest rate was assumed in year one and 5.31% were assumed in year two and thereafter.

To provide more specifically for the effects of inflation on the liability for future workers' compensation benefits, wage inflation factors (cost of living adjustments or COLAs) and medical inflation factors (consumer price index medical or CPIMs) were applied to the calculation of projected future benefits. The actual rates for these factors for charge back year (CBY) 2006 were also used to adjust the methodology's historical payments to current year constant dollars.

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

CBY	COLA	CPIM
2006	3.50%	4.00%
2007	3.13%	4.01%
2008	2.40%	4.01%
2009	2.40%	4.01%
2010	2.43%	4.09%

The model's resulting projections were analyzed to ensure that the estimates were reliable. The analysis was based on four tests: (1) a sensitivity analysis of the model of economic assumptions, (2) a comparison of the percentage change in the liability amount by agency to the percentage change in the actual payments, (3) a comparison of the incremental paid losses (the medical component in particular) in CBY 2006 (by injury cohort) to the average pattern observed during the prior three charge back years, and (4) 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.

Voluntary Separation Incentive Programs (VSI)

Assumptions

The VSI program was established by Public Law 102-190. The intent of this program is to reduce the number of military personnel on active duty. This plan was offered to personnel with a minimum of six years of service who did not qualify for retirement. The incentive payments are spread over a period equivalent to twice the years of active service. The annual payment is based on 2.5% of the person's annual basic pay at the time they departed service multiplied by the number of years of service. The September 30, 2006, VSI Actuarial Present Value of Projected Plan Benefits (Actuarial Liability) was calculated at an assumed annual interest rate of 4%. Since VSI program is no longer offered, each year the Actuarial Liability is expected to decrease with benefit outlays, and increase with interest cost. The present value of plan benefits actuarial liability for the VSI fund is $1.4 billion as of September 30, 2006. The liability is calculated annually at the present value of all remaining payments as of September 30, 2006.

Market Value of Investments in Market-based and Marketable Securities: $645.8 million

DoD Education Benefits Fund (EBF)

Assumptions

The EBF was established by Public Law 98-525. The program is designed to accumulate funds for the Educational Assistance program, to promote the recruitment and retention of members for the All-Volunteer Forces program and the Total Force Concept of the Armed Forces, and aid in the readjustment of members of the Armed Forces to civilian life after separation from military service. The actuarial liability is calculated annually and has a present value of $1.8 billion as of September 30, 2006.

Market Value of Investments in Market-based and Marketable Securities: $1.3 billion

Other Federal Employment Benefits

The format of this note was changed in FY 2006 to include Other Federal Employment Benefits, such as pension and other post-employment benefits due and payable, which were previously included in Note 15.

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

Intragovernmental Costs and Exchange Revenue As of March 31		2007		2006
1. Intragovernmental Costs	$	15,428,416,073.46	$	12,669,449,700.96
2. Public Costs		281,138,644,824.73		256,804,210,167.93
3. Total Costs	$	296,567,060,898.19	$	269,473,659,868.89
4. Intragovernmental Earned Revenue	$	(7,202,841,476.61)	$	(12,413,976,764.62)
5. Public Earned Revenue		(11,680,297,488.23)		(10,957,452,634.95)
6. Total Earned Revenue	$	(18,883,138,964.84)	$	(23,371,429,399.57)
7. Net Cost of Operations	$	277,683,921,933.35	$	246,102,230,469.32

Fluctuations

Total Costs increased $27.1 billion (10%) primarily due to the following increases: (1) a change of accounting procedures for Foreign Military Sales Trust Fund, which now includes all costs incurred rather than only the administrative costs necessary to execute the program, (2) increased expenses in support of the Global War of Terror, and (3) increases in environmental expenses and expenses related to contingencies.

Total Earned Revenue decreased $4.5 billion (19%) primarily due to a $3.1 billion decrease in interest on U.S. Treasury Inflation Protected Securities (TIPS), which provide protection against inflation. In 2nd Quarter, FY 2007, interest on TIPS reflects a decrease due to deflation. In addition, there was $1.7 billion less in revenue with the Federal Emergency Management Agency for hurricane relief efforts.

Other Disclosures

The Statement of Net Cost (SNC) is unique because its principles are driven on understanding the net cost of programs and/or organizations that the Federal Government supports through appropriations or other means. This statement provides gross and net cost information that can be related to the amount of output or outcome for a given program and/or organization administered by a responsible reporting entity. Intragovernmental costs and revenue are related to transactions made between two reporting entities within the Federal Government. Public costs and revenues are exchange transactions made between the reporting entity and a nonfederal entity.

For General Funds, the amounts presented in SNC are based on obligations and disbursements and therefore may not, in all cases, accrue actual costs. While the Department's Working Capital Funds generally record transactions on an accrual basis, the systems do not always capture actual costs in a timely manner. As such, information presented in SNC is based on budgetary obligations, disbursements, and collection transactions, as well as nonfinancial feeder systems and are adjusted to record known accruals for major items such as payroll expenses, accounts payable and environmental liabilities.

The majority of the Department's accounting systems do not capture information relative to Heritage Assets separately and distinctly from normal operations. Where it was able to separately identify the cost of acquiring, constructing, improving, reconstructing or renovating heritage assets, the Department has identified $970.6 thousand for the fiscal year.

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

As of March 31	2007		2006	
	Cumulative Results of Operations	Unexpended Appropriations	Cumulative Results of Operations	Unexpended Appropriations
1. Prior Period Adjustments Increases (Decreases) to Net Position Beginning Balance				
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	(1,207,720.24)	(527,457.36)
C. Total Prior Period Adjustments	$ 0.00	$ 0.00	$ (1,207,720.24)	$ (527,457.36)
2. Imputed Financing				
A. Civilian CSRS/FERS Retirement	$ 696,188,727.55	$ 0.00	$ 756,072,763.19	$ 0.00
B. Civilian Health	1,334,439,819.18	0.00	1,286,562,382.00	0.00
C. Civilian Life Insurance	3,873,734.98	0.00	12,280,148.65	0.00
D. Judgment Fund	53,232,721.51	0.00	108,515,460.66	0.00
E. IntraEntity	0.00	0.00	0.00	0.00
F. Total Imputed Financing	$ 2,087,735,003.22	$ 0.00	$ 2,163,430,754.50	$ 0.00

Fluctuations

Budgetary Financing Sources, Appropriations Received increased $27.7 billion (5%) largely due to increased funding for the Global War on Terror. The Department of the Army received the majority of the increase in funds.

Nonexchange Revenue increased $7.1 billion (589%). The increase is primarily in Security Assistance due to the change in reporting requirements effective 1st Quarter, FY 2007. The Office of Management and Budget Circular A-136, "Financial Reporting Requirements," requires the Department to include programs that are executed on behalf of the Executive Office of the President. This information was previously reported in Other Accompanying Information on the financial statements.

Other Financing Sources, Other, which is used primarily to record adjustments to reconcile budgetary and proprietary trial balances, decreased by $6.4 billion (340%). Due to system deficiencies, the Department is unable to fully reconcile budgetary and proprietary trial balances and must make adjustments to compensate for the system limitations.

Other Disclosures

In FY 2006, prior period adjustments (PPAs) totaling $8.1 billion were recorded in the 3rd and 4th Quarters. These restated the cumulative results of operations for the revaluation of military equipment, and the recognition of a strategic petroleum reserve established in FY 1993. The FY 2006 PPAs are included in the beginning net position for FY 2007, but are not presented in the 2nd Quarter, FY 2006 comparative column in the table above. Due to system shortcomings, comparable quarterly data prior to the quarter in which PPAs are originally made are not restated.

The amounts the Department of Defense remits to the Office of Personnel Management (OPM) by and for employees covered by the Civil Service Retirement System, the Federal Employees' Retirement System, the Federal Employees' Health Benefits program, and the Federal

Employees' Group Life Insurance program do not fully cover the government's cost to provide these benefits. An imputed cost is recognized as the difference between the government's cost of providing these benefits to employees and the Department’s contributions. The OPM provides cost factors for the computation of imputed financing costs, and these estimates are included in the Department’s financial statements.

Statement of Federal Financial Accounting Standards Number 27, “Identifying and Reporting Earmarked Funds,” effective for reporting years after FY 2005, required that the Department modify the Statement of Changes in Net Position (SCNP). To meet the requirement, additional columns were added to separately display gross amounts for earmarked funds, and all other (nonearmarked) funds. In SCNP, all offsetting balances (i.e. transfers in and transfers out, revenues and expenses) for activity within the department between earmarked and other (nonearmarked) funds are reported on the same lines. This results in an eliminations column, which appears to contain no balances, except for intra entity imputed financing costs. In reality, the column contains all appropriate elimination entries, but all net to zero within each respective line.

There is an $85.3 billion difference between Appropriations Received that are reported on SCNP ($556.0 billion) and Appropriations Received in the Statement of Budgetary Resources ($641.3 billion). This difference is primarily due to appropriations transferred to the trust and special funds which are duplicated in the Statement of Budgetary Resources. In addition, a small portion of the differences relates to interest collected by the trust funds. See Note 20, “Disclosures Related to the Statement of Budgetary Resources,” for additional information and fluctuation explanations.

Note 20. Disclosures Related to the Statement of Budgetary Resources

As of March 31	2007	2006
1. Net Amount of Budgetary Resources Obligated for Undelivered Orders at the End of the Period	$ 359,808,894,112.91	$ 307,920,791,021.99
2. Available Borrowing and Contract Authority at the End of the Period	68,037,951,177.03	62,540,482,998.97

Fluctuations

Obligations incurred increased $51.3 billion (11%) primarily due to increased obligations during 1st Quarter, following receipt of FY 2007 Title IX funding for the Global War on Terror (GWOT).

Gross Outlays increased $24.2 billion due primarily to increased expenditures for military personnel, operation and maintenance, and procurement in support of the GWOT.

Reconciliation Differences

There is a difference of $5.9 billion between the Borrowing and Contract Authority reported in the table above ($68.0 billion) and the amount reported for Available Borrowing and Contract Authority on the Statement of Budgetary Resources (SBR) ($62.1 billion). The table above reports current-year activity as well as carry-forward amounts for both categories of authority. The SBR only reports current-year activity for these categories.

Appropriations Received on the SBR exceed Appropriations Received on the Statement of Changes in Net Position by $85.3 billion. Appropriations received by the Military Departments and Defense Agencies that are subsequently recognized a second time on the SBR as appropriations transferred into trust and special funds comprise $62.8 billion. Actual and anticipated earnings in trust and special funds comprise the balance of the difference.

Permanent Indefinite Appropriations

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

- Department of the Army General Gift Fund (10 USC 2601(b)(1))
- Department of the Navy General Gift Fund (10 USC 2601(b)(2))
- Department of the Air Force General Gift Fund (10 USC 2601 (b)(3))
- Foreign National Employees Separation Pay Account, Defense (10 USC 1581)
- United States Naval Academy Gift and Museum Fund (10 USC 6973-4)
- Ship Stores Profits, Navy (10 USC 7220, 31 USC 1321)
- Midshipmen's Store (10 USC 6971B)
- Burdensharing Contributions Account (10 USC 2350(j))
- Forest Program (10 USC 2665)
- Department of Defense Base Closure Account (10 USC 2687)
- Medicare Eligible Retiree Health Care Fund (MERHCF) (10 USC 1111)
- Military Retirement Fund (MRF) (10 USC 1461)
- Education Benefits Fund (10 USC 2006)
- Reserve Mobilization Income Insurance Fund (10 USC 12528)
- Host Nation Support for U.S. Relocation Activities (10 USC 2350(k))
- National Defense Sealift Fund (10 USC 2218)
- Environmental Restoration, Navy (10 USC 2702)

- Hydraulic Mining Debris Reservoir (33 USC 683)
- Maintenance and Operation of Dams and Other Improvements of Navigable Waters (16 USC 810(a))
- Payments to States (33 USC 701c-3)
- Wildlife Conservation (16 USC 670-670(f))
- Ainsworth Bequest (31 USC 1321)
- Department of Defense Family Housing Improvement Fund (10 USC 2883 (a))
- Department of Defense Military Unaccompanied Housing Improvement Fund (10 USC 2883 (a))

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

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

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

Apportionment Categories for Obligations

The Department reported the following amounts of direct obligations: $296.6 billion in category A; $86.3 billion in category B; and $28.1 billion in exempt from apportionment. The Department reported the following amounts of reimbursable obligations: $43.2 billion in category A; $32.0 billion in category B; and $16.8 billion in exempt from apportionment. Category A relates to appropriations for a specific period of time (e.g., Military Personnel appropriation), and category B relates to appropriations for a specific project (e.g., Military Construction appropriation).

Other Disclosures

The Department received Continuing Resolution Authority for Civil Works, Military Construction, Family Housing, and Energy and Water Development in the amount of $2.8 billion during the 2nd Quarter, FY 2007, in order to continue operations until the FY 2007 appropriation and authorization bills are passed by Congress.

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

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

There are no legal arrangements affecting the use of unobligated balances of budget authority.

The Department received a capital infusion during 2nd Quarter, FY 2007, of $70.0 billion in Title IX funds for the Global War on Terror.

The Department reported a change in unobligated balances brought forward. OMB Circular A-136 generally requires financial activity related to these allocation transfers (e.g. budget authority, obligations, outlays) to be reported in the financial statements of the parent entity. Exceptions to this general rule affecting the Department include Security Assistance programs executed on behalf of the Executive Office of the President. Effective in 1st Quarter, FY 2007, the Department began reporting these balances in the basic financial statements. The change resulted in a $24.9 billion increase in the unobligated balances brought forward from FY 2006.

Note 21. Disclosures Related to the Statement of Financing

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

Resources That Finance the Acquisition of Assets	$ 16.7 billion
Other - Other Components Not Requiring or Generating Resources	$ 7.4 million

The following Statement of Financing lines are presented as combined instead of consolidated due to intraagency budgetary transactions not being eliminated:

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

Fluctuations

Resources Used to Finance Activities

Obligations incurred increased $51.3 billion (11%) primarily due to increased obligations during 1st Quarter, following receipt of FY 2007 Title IX funding for the Global War on Terror.

Resources Used to Finance Items not Part of the Net Cost of Operations

Undelivered orders increased $28.7 billion (93%) due largely to the increase in the obligations described above.

Resources that finance the acquisition of assets increased $12.3 billion (20%) primarily due to the $16.7 billion adjustment disclosed above that was made to bring the Statement of Financing into balance with the Statement of Net Cost.

Other Disclosures

Liabilities not covered by budgetary resources on the Balance Sheet total $1.6 trillion and the amount reported as components requiring or generating resources in future periods on the Statement of Financing totals $6.9 billion. The difference is primarily due to the differing perspectives between the two statements. Liabilities not covered by budgetary resources report the cumulative balance for Balance Sheet liabilities not yet funded whereas components requiring or generating resources in future periods reflect only the current period changes for all unfunded liabilities.

Note 22. Disclosures Related to the Statement of Custodial Activity

The Statement of Custodial Activity displays current year collections and disbursements for three custodial accounts: (1) Foreign Military Sales, (2) Development Fund for Iraq, and (3) Seized Assets. Funds held in a custodial activity are only used for the stated purposes and are not available for the Department's use.

Foreign Military Sales (FMS)

Under authority of the Arms Export and Control Act, the Foreign Military Sales Trust Fund (FMSTF) receives collections from foreign governments that are dedicated specifically to FMS purchases. Funds collected into the FMSTF are in advance of the performance of services or sale of articles.

Current year Deposits by Foreign Governments into FMSTF are $8.7 billion. Disbursements on Behalf of Foreign Governments and International Organizations total $6.7 billion.

The FMSTF neither recognizes nor reports revenue, except for cost clearing accounts, which are reflected in all other principal financial statements. Since various Department Components actually perform the services and sell the articles, recognition of revenue and expense occurs in the financial statements of the applicable Department Components.

Development Fund for Iraq (DFI)

The DFI is for urgent humanitarian assistance, reconstruction, and other projects carried out for the benefit of the Iraqi people. During FY 2007, there were $5.9 million in disbursements by the Multi-National Force Iraq with no additional deposits. As of March 31, 2007, $12.9 million remains to be disbursed.

(Amounts in Millions)	During FY 2007	Cumulative from Inception
Source of Collections		
Deposits By Foreign Governments	$ 0.0	$ 136.0
Disposition of Collections		
Security and Law Enforcement	$ 0.0	$ 1.0
Electric Sector	1.1	46.3
Oil Infrastructure	0.0	.4
Water Resources and Sanitation	1.1	17.7
Transportation and Telecommunications	0.3	5.6
Roads, Bridges and Construction	0.0	5.0
Health Care	0.0	2.9
Private Sector Development	0.0	7.2
Education, Refugees, Human Rights, and Governance	3.4	37.0
Total Disbursed on Behalf of Foreign Governments	5.9	123.1
Retained for Future Support of Foreign Governments *****	(5.9)	12.9
Total Disposition of Collections	$ 0.0	$ 136.0
Net Custodial Collection Activity	$ 0.0	$ 0.0

*Note - Reported on the Statement of Custodial Activity under Disposition of Collections, Increase (Decrease) in Amounts to be Transferred.

Seized Assets

During Operation Iraqi Freedom, the U.S. Government seized assets from the Iraqi Government that are used in support of the Iraqi people. In FY 2007, $1.1 million was disbursed with no additional seized assets. As of March 31, 2007, $29.1 million of seized monetary assets remain to be disbursed in support of the Iraqi people as shown in the table below.

(Amounts in Millions)	During FY 2007	Cumulative From Inception
Source of Collections		
Seized Iraqi Cash	$ 0.0	$ 927.2
Disposition of Collections		
Iraqi Salaries	$ 0.0	$ 30.8
Repair/Reconstruction/Humanitarian Assistance	1.1	527.3
Iraqi Ministry Operations (Ministry of Finance, Defense, etc.)	0.0	264.7
Fuel/Supplies	0.0	75.3
Total Disbursed on Behalf of Iraqi People	1.1	898.1
Retained for Future Support of the Iraqi People	(1.1)	29.1
Total Disposition of Collections	$ 0.0	$ 927.2
Net Custodial Collection Activity	$ 0.0	$ 0.0

Note 23. Earmarked Funds

BALANCE SHEET As of March 31, 2007	Military Retirement Fund	Medicare Eligible Retiree Health Care Fund	Other Earmarked Funds	Eliminations	Total
ASSETS					
Fund balance with Treasury	$ 26,081,898.35	$ 5,000,000.00	$ 1,915,614,045.27	$ 0.00	$ 1,946,695,943.62
Investments	226,022,200,137.71	110,022,510,053.38	5,802,347,505.47	0.00	341,847,057,696.56
Accounts and Interest Receivable	23,332,148.30	11,740,294.44	832,416,412.39	(1,462,295.06)	866,026,560.07
Other Assets	0.00	0.00	1,851,816,811.05	0.00	1,851,816,811.05
Total Assets	$ 226,071,614,184.36	$ 110,039,250,347.82	$ 10,402,194,774.18	$ (1,462,295.06)	$ 346,511,597,011.30
LIABILITIES and NET POSITION					
Military Retirement Benefits and Other Federal Employment Benefits	$ 967,218,575,125.50	$ 538,620,353,000.00	$ 3,176,463,161.00	$ 0.00	$ 1,509,015,391,286.50
Other Liabilities	924,062.51	338,383,707.55	1,361,952,768.24	(76,145,819.87)	1,625,114,718.43
Total Liabilities	$ 967,219,499,188.01	$ 538,958,736,707.55	$ 4,538,415,929.24	$ (76,145,819.87)	$ 1,510,640,506,004.90
Unexpended Appropriations	0.00	0.00	10,322,450.51	0.00	10,322,450.51
Cumulative Results of Operations	(741,147,885,003.65)	(428,919,486,359.73)	5,853,456,394.43	(61,685,328,084.12)	(1,225,899,243,053.10)
Total Liabilities and Net Position	$ 226,071,614,184.36	$ 110,039,250,347.82	$ 10,402,194,774.18	$ (61,761,473,903.99)	$ 284,751,585,402.31

STATEMENT OF NET COST For the period ended March 31, 2007	Military Retirement Fund	Medicare Eligible Retiree Health Care Fund	Other Earmarked Funds	Eliminations	Total
Program Costs	$ 21,557,988,415.37	$ 3,827,601,791.23	$ 1,370,997,500.12	$ (1,319,472,883.67)	$ 25,437,114,823.05
Less Earned Revenue	(39,071,419,080.42)	(28,190,056,395.94)	(554,910,841.76)	62,814,158,147.86	(5,002,228,170.26)
Net Program Costs	$ (17,513,430,665.05)	$ (24,362,454,604.71)	$ 816,086,658.36	$ 61,494,685,264.19	$ 20,434,886,652.79
Less Earned Revenues Not Attributable to Programs	0.00	0.00	0.00	0.00	0.00
Net Cost of Operations	$ (17,513,430,665.05)	$ (24,362,454,604.71)	$ 816,086,658.36	$ 61,494,685,264.19	$ 20,434,886,652.79

Agency Wide

STATEMENT OF CHANGES IN NET POSITION For the period ended March 31, 2007	Military Retirement Fund	Medicare Eligible Retiree Health Care Fund	Other Earmarked Funds	Eliminations	Total
Net Position Beginning of the Period	$ (758,661,315,668.70)	$ (453,467,940,964.44)	$ 5,371,354,755.03	$ 0.00	$ (1,206,757,901,878.10)
Net Cost of Operations	(17,513,430,665.05)	(24,362,454,604.71)	816,086,658.36	61,494,685,264.19	20,434,886,652.79
Budgetary Financing Sources	0.00	186,000,000.00	1,310,239,666.24	(192,366,144.79)	1,303,873,521.45
Other Financing Sources	0.00	0.00	(1,728,917.97)	1,723,324.86	(5,593.11)
Change in Net Position	$ 17,513,430,665.05	$ 24,548,454,604.71	$ 492,424,089.91	$ (61,685,328,084.12)	$ (19,131,018,724.45)
Net Position End of Period	$ (741,147,885,003.65)	$ (428,919,486,359.73)	$ 5,863,778,844.94	$ (61,685,328,084.12)	$ (1,225,888,920,602.60)

Other Disclosures

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

The Total column is shown as consolidated and relates only to Earmarked Funds. The Elimination column includes only eliminations associated with Earmarked Funds and excludes the offsetting eliminations from All Other Funds. This exclusion causes assets to not equal liabilities and net position in the note. However, the amounts in the Total column equal the amounts reported for Earmarked Funds on the Balance Sheet.

The SFFAS, effective for reporting years after fiscal year (FY) 2005, required the Department modify the Statement of Changes in Net Position. To meet the requirement, additional columns were added to separately display gross amounts from Earmarked Funds and All Other (nonearmarked) Funds. Cumulative Results of Operations ending balances for Earmarked Funds on the Statement of Changes in Net Position do not agree with the Cumulative Results of Operations for Earmarked Funds reported on the Balance Sheet because the Cumulative Results of Operations on the Balance Sheet are presented net of eliminations. The summation for Military Retirement Fund (MRF), Medicare-Eligible Retiree Health Care Fund (MERHCF), and Other Earmarked Funds is equivalent to the gross amount presented on the Statement of Changes in Net Position.

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

Medicare-Eligible Retiree Health Care Fund, 10 USC 1111. The MERHCF accumulates funds to finance, on an actuarially sound basis, liabilities of the Department and the uniformed services health care programs for specific Medicare-eligible beneficiaries. The MERHCF was authorized by Public Law 106-398. Financing sources for MERHCF are provided primarily through an annual actuarial liability payment from U.S. Treasury, annual contribution(s) from the Military Services and other Uniformed Services (U.S. Coast Guard, the National Oceanic and Atmospheric Administration, and the U.S. Public Health Service), and interest earned from the Fund's investments.

Other Earmarked Funds

Special Recreation Use Fees, 16 USC 4061-6a note. The United States Army Corps of Engineers (USACE) is granted the authority to charge and collect fair and equitable Special Recreation Use Fees at campgrounds located at lakes or reservoirs that are under the jurisdiction of the USACE. Types of allowable fees include, but are not limited to, daily use fees, admission fees, recreational fees, annual pass fees, and other permit type fees. The receipts are used for the operation and maintenance of the recreational sites.

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

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

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

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

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

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

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

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

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

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

Defense Commissary Agency Surcharge Trust Fund, 10 USC 2685. This fund was established as the repository for the surcharge on sales of commissary goods paid for by authorized patrons to finance certain operating expenses and capital purchases of the Commissary System, which are precluded by law from being paid with appropriated funds. Most Surcharge public revenue is generated by the 5% surcharge applied to each sale. These funds may be used to pay for the commissary store-related information technology investments, to purchase commissary equipment, to finance advance design modifications to prior year projects, for both minor and major construction projects, and to maintain and repair commissary facilities and equipment. The surcharge account also allows for obligations based on anticipated proceeds without regard to fiscal year limitations, if needed to carry out the purposes of the Fund.

Note 24. Other Disclosures

As of March 31	2007 Asset Category			
	Land and Buildings	Equipment	Other	Total
1. ENTITY AS LESSEE- Operating Leases				
Future Payments Due				
Fiscal Year				
2007	$ 161,558,538.79	$ 2,234,542.48	$ 129,665,879.00	$ 293,458,960.27
2008	245,484,301.33	1,581,475.28	134,852,515.00	381,918,291.61
2009	239,418,171.35	1,105,894.28	140,246,615.00	380,770,680.63
2010	232,308,497.39	1,121,630.66	145,856,480.00	379,286,608.05
2011	222,183,594.73	866,397.36	151,690,739.00	374,740,731.09
2012	176,884,162.48	880,790.22	157,758,369.00	335,523,321.70
After 5 Years	238,444,263.92	897,522.25	164,068,703.00	403,410,489.17
Total Future Lease Payments Due	$ 1,516,281,529.99	$ 8,688,252.53	$ 1,024,139,300.00	$ 2,549,109,082.52

Note 25.	Restatements

The Department did not record any restatements during FY 2007.