



GLOBAL STRENGTH IN AN UNCERTAIN WORLD





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2016

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GLOBAL STRENGTH IN AN UNCERTAIN WORLD

*The Army protects our national interests and stands ready
whenever called upon to win our nation's wars.*



GLOBAL STRENGTH IN AN UNCERTAIN WORLD



Our Army continues to serve at the forefront of our nation's commitment to global security. The Army protects our national interests and stands ready whenever called upon to win our nation's wars. Through forward presence and international partnerships, our ready forces reassure our allies, deter potential aggression, and confront terrorism around the world. The 2016 Annual Financial Report (AFR) provides insights into the resources and outcomes that those resources yield for an Army that continues to be globally engaged in a complex and ever-changing world.

To sustain the best Army in the world, we must make the most of resources entrusted to us while balancing competing requirements for readiness, end strength, and modernization—to ensure America's Army remains ready to fight and win, both today and in the future. Funding reductions over the past several years, coupled with the uncertainty of future funding, provide significant challenges; however, we have focused our resource priorities on

producing readiness, sustaining key modernization programs, and ensuring Soldier and family quality of life. Budget instability complicates the formulation of any long-term plan, but we remain committed to providing our Soldiers the best training, equipment and leadership to navigate through the high demands while under such fiscal pressure.

The operational Army has proven to be adaptive and agile while the institutional Army implements meaningful acquisition reform, encourages collaboration and innovation, and reengineers processes to create savings that can be reinvested in support of the Warfighter.

The Army's AFR, in an alternative format to the *Performance and Accountability Report*, highlights our financial commitment to Army priorities and demonstrates our progress toward producing reliable and complete financial data in our quest to meet congressionally-mandated audit readiness requirements by September 30, 2017. The AFR discusses the material weaknesses in our Internal Controls over Financial Reporting (ICOFR), which are currently being addressed within corrective action plans. Such plans are generated from insights gained from independent public audits of Army's Schedule of Budgetary Activity (SBA), which began in FY 2015, as well as reviews of specific balance sheet items and the current FY 2016 SBA audit.

Presently, our role is to develop the capabilities required, obtain meaningful acquisition reform and meet the Army's requirement of being auditable by 2018. The Army's new "Rapid Capabilities Office" seeks to assess the threats that our adversaries are posing, and in turn, acquire new or counter capabilities in areas such as cyber or electronic warfare as quickly as possible. Attaining meaningful acquisition reform ensures that when we ask our Soldiers and Civilians to perform, they have the equipment and technology readily available to do so. Audit readiness implies that we in turn take our stewardship role responsibly, as we evaluate the success of our various programs in the midst of current budget instability and a fiscally constrained environment.

We remain dedicated to providing the proper stewardship over the necessary resources needed to sustain the nation's over one million Soldiers, including the 180,000 either serving or supporting the United States in more than 140 countries, all of whom are enabled by over 240,000 civilians – meeting America's national security demands.

A handwritten signature in black ink that reads "Eric K. Fanning".

ERIC K. FANNING
Secretary of the Army

The Army has continued to improve the performance and functionality of our financial systems.

GLOBAL STRENGTH IN AN UNCERTAIN WORLD



Our mission is to win the nation's wars. To do so, Congress must appropriate the dollars to provide the capabilities and sustain the readiness our Army needs. This can best be done when we can build realistic and defensible budgets supported by timely, accurate, and reliable financial information.

To this end, audit readiness remains an Army top priority and we remain engaged and committed in our goal of asserting full financial statement audit readiness by September 30, 2017. The Army Financial Report demonstrates our commitment to meeting this objective, as we strive to optimize Army financial management resources.

The Army financial improvement plan reflects the objectives of the overall Department of Defense audit readiness plan. Independent Public Accounting audits conducted in fiscal year (FY) 2016 on the Army General Fund Schedule of Budgetary Activity (SBA) and specific elements of the General Fund balance

sheet highlighted specific financial improvements and more robust reporting system requirements necessary to meet the auditable financial statements goal.

From our recent audits, we have developed corrective action plans to address the deficiencies and internal control weaknesses noted in the FY 2015 General Fund SBA audit, FY 2016 Department of Defense Inspector General (DoD IG) Financial Statement audit report, and reports on Internal Controls over Financial Reporting. The DoD IG also issued opinions this year related to documentation supporting Army General Fund adjustments, suspense account balances, and Working Capital Fund inventory valuations. These reports, together with reviews of acquisition management and contractor assessments, have highlighted areas for improvement. Revised approaches are in development for valuing assets and liabilities such as real property, equipment, operating materiel and supplies, and environmental liabilities. Our Army leaders meet regularly to evaluate the success of efforts undertaken by these corrective action plans to remediate these deficiencies as we drive audit readiness goals.

Meanwhile, the Army has continued to improve the performance and functionality of our financial systems, to include our core accounting system, the General Fund Enterprise Business System (GFEBS), as well as the working capital accounting system that is integrated within the Logistics Modernization Program (LMP) system. Additionally, these primary systems and the integrity of the information for decision making is federated with the Global Combat Support System -Army (GCSS-A); enabling greater visibility of resources, as well as providing Commanders and Soldiers with the equipment availability, quantity, location, and status.

Complementing the process of learning through the audit experience, we implemented a plan to integrate financial management functionality and synchronize priorities of work across a workforce stressed by downsizing and increasing budget uncertainty. Our priorities are centered on standardizing business processes across the Army, building systems capacity for storing and retrieving financial information, developing our professional workforce, and building leaders with intellectual capacity to meet demands of our dynamic, complex environment.

Army leaders remain fully committed to ensuring compliance with congressionally-mandated auditability requirements; while resourcing against Army priorities of building readiness, building the future force and taking care of our people – Soldiers, Civilians and Families.

ROBERT M. SPEER

Assistant Secretary of the Army, Financial Management and Comptroller

GLOBAL STRENGTH

IN AN UNCERTAIN WORLD



Supporting a heavy equipment drop. (U.S. Army
photo by Spc. Emily Houdershielt)



Infantrymen move through a trench during a company-level combined arms live-fire exercise. (U.S. Army photo by Spc. Craig Philbrick)

OVERVIEW

Our Army's fundamental purpose—to fight and win our Nation's wars—remains the same. Here at home, Soldiers are helping our friends and neighbors recover from natural disasters. In Europe and Asia, the Army reassures allies while deterring the chance of miscalculation and war, as powerful adversaries practice aggression and militarized competition. The Army is working with allies and partners to train, advise, and assist Iraqi and Afghan forces as they fight ruthless enemies within their borders. These efforts include engaging our partners in Africa and throughout the Americas. At home, the Army partners with civil authorities to provide aid, protect our citizens, and defend our Nation. In every circumstance and region of the world today, our Army stands ready to deter, to fight, and to win.

While more than 187,000 Soldiers are serving in over 140 countries around the world, the Army has gained new insight into the character of future conflict. Future warfare will involve transporting, fighting, and sustaining geographically dispersed Army, joint, and multinational forces over long and contested distances, likely into an opposed environment and against a technologically sophisticated and numerically superior enemy. All domains will be vigorously contested, and both air and maritime superiority—which have been unquestioned American advantages for more than 75 years—will no longer be a given.

The character of war changes due to unique geopolitical factors. To prepare for these changes, the Army must solve four operational problems. First, as part of the Joint Force, the Army must develop credible military capabilities to deter, and if necessary defeat, a peer military power. Second, the Army must retain the competencies, capabilities, and capacity built for the counterterrorism and counterinsurgency fights of the past 15 years. Third, the Army must establish a common recognition among allies and partners of the collective problems the Army faces and the best way ahead. Finally, as the Army works through these implications, the Army must reexamine internal operational and institutional models.

Meeting our current demands for forces while preparing for future warfare is expensive. With today's budget uncertainty and fiscally constrained environment, it means focusing resources on immediate readiness priorities to meet current worldwide missions. This often results in readiness being consumed as fast as it is built, while increasing pressure and causing higher risk in long-term readiness and modernization. Therefore, the financial management community must best distribute scarce resources toward strategic plans and Army priorities, and provide commanders with improved financial information and processes to enable timely decisions regarding readiness and current mission requirements. Only through predictable funding can the Army build readiness now and prepare for the future.

MISSION AND ORGANIZATION OF THE ARMY

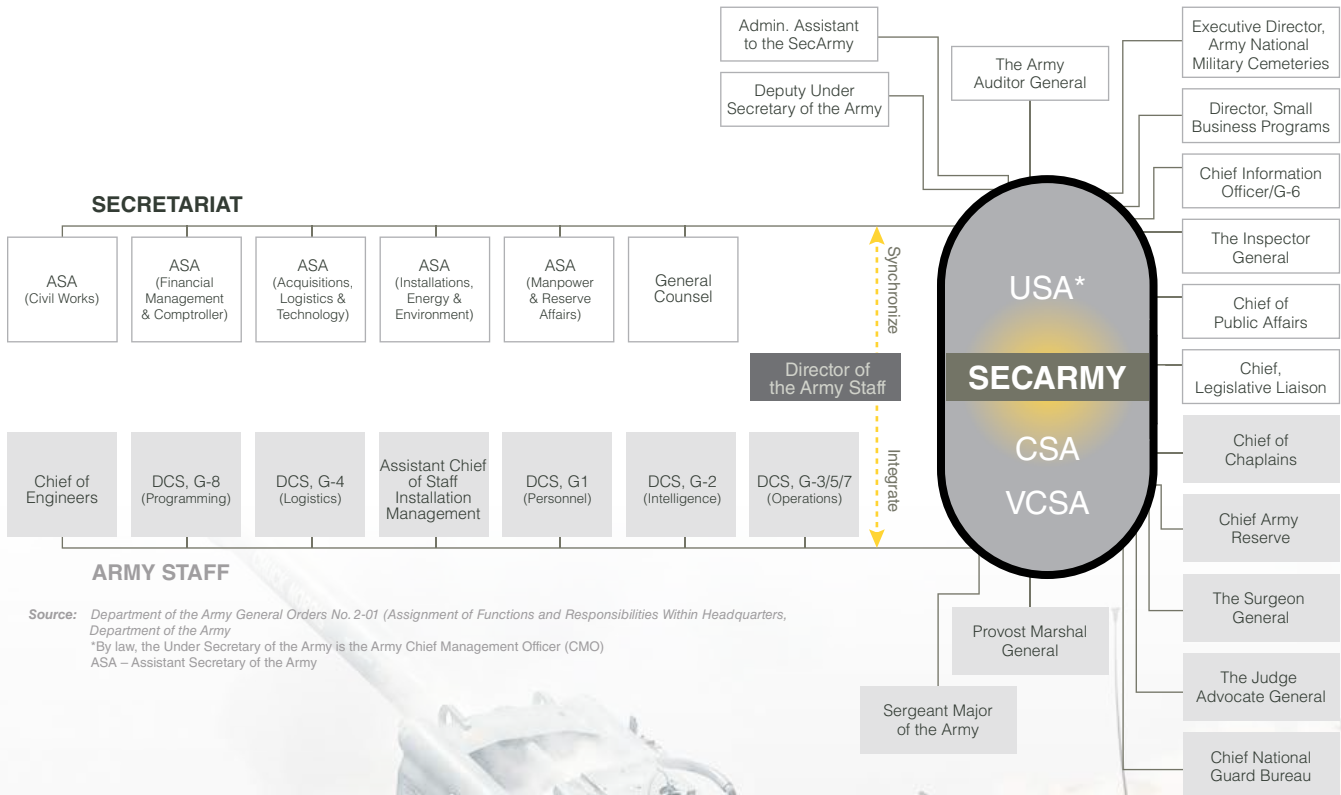
The mission of the United States Army is to fight and win the Nation's wars through prompt and sustained land combat as the foundation of the Joint Force. The Army organizes, equips, and trains Soldiers for rapid, sustained combat operations on land; integrates Army capabilities with those of the other armed services; accomplishes all missions assigned by the President, Secretary of Defense, and combatant commanders; and remains ready while preparing for the future.

The Army is organized to support and sustain the mobilization, training, and deployment of its Soldiers anywhere in the world. Headquarters, Department of

the Army (HQDA) (Figure 1), under the direction of the Secretary of the Army, leads and manages the entire Army. The HQDA Staff is composed of the Secretariat and the Army Staff (ARSTAF). The HQDA Staff:

- Develops policies, plans, and programs.
- Establishes and prioritizes requirements.
- Provides resources to organize, man, train, and equip Soldiers to meet the combatant commands' current and future operational requirements and other needs as defined by the President and the Secretary of Defense.

FIGURE 1. Headquarters, Department of the Army (HQDA)

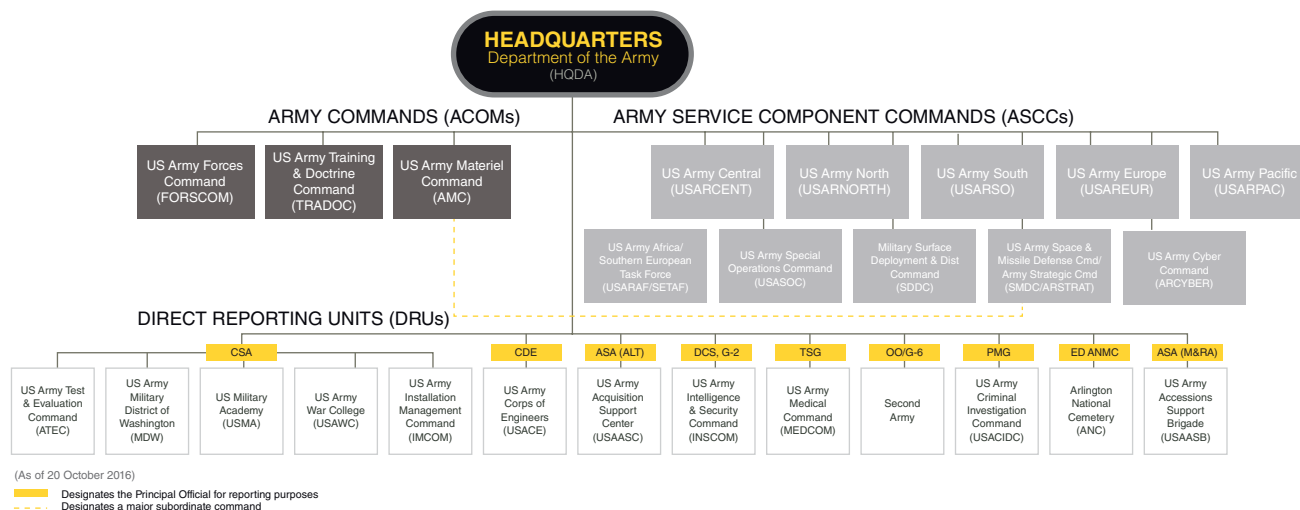


Source: Department of the Army General Orders No. 2-01 (Assignment of Functions and Responsibilities Within Headquarters, Department of the Army)

*By law, the Under Secretary of the Army is the Army Chief Management Officer (CMO)
 ASA – Assistant Secretary of the Army

Organizations reporting to HQDA as part of the Army's command structure (Figure 2) include Army Commands (ACOMs), Army Service Component Commands (ASCCs), and Direct Reporting Units (DRUs). The operational Army consists of numbered armies, corps, divisions, brigades, and battalions that conduct the full range of military operations. The institutional Army supports the operational Army by providing the infrastructure necessary to man, train, equip, deploy, and ensure the readiness of all Army forces.

FIGURE 2. Army Command Structure



PERFORMANCE GOALS, OBJECTIVES, AND RESULTS

Maintaining credible strategic land-power requires the Army to assess and refine continually how it operates, manages its human capital, and increases its capabilities. The Army will build globally responsive, regionally engaged strategic land forces with a versatile mix of capabilities, formations, and equipment that are mission tailored, scalable, and cost effective. Going beyond materiel and equipment solutions, the Army's modernization strategy is a comprehensive effort that includes doctrine, organizations, training, leadership and education, personnel, facilities, and policy. The Army will develop, field, and sustain equipment that provides Soldiers and units the capabilities they need to be successful.

SUSTAIN

The Army must maintain the quality and viability of the all-volunteer force, as well as the many capabilities it provides the Nation, to sustain Soldiers, their Families, and Army Civilians in an era of persistent conflict. Sustainment ensures that Soldiers and their Families have the quality of life they deserve which leads to improved retention rates.

MANNING THE FORCE—RECRUITING AND RETAINING SOLDIERS

While the recruiting environment is challenging, the Army remains committed to bringing only the very best into its ranks. The Army's goal is to achieve no less than a 90 percent rate of new recruits with Tier 1 educational credentials, i.e., high school diploma or above. The Army achieved approximately 96 percent Tier 1 recruits in Fiscal Year (FY) 2016. The overall attrition rate remained virtually unchanged over the last three years. The unvarying attrition rate and overall quality of recruits are positive signs that the Army is recruiting, training, and retaining a highly qualified force.

TABLE 1. Quality Percent Tier 1 Educational Credential Holders (Active Component)

| | FY 2012 | FY 2013 | FY 2014 | FY 2015 | FY 2016 |
|---------------|---------|---------|---------|---------|---------|
| Tier 1 Goal | 90% | 90% | 90% | 90% | 90% |
| Tier 1 Actual | 96% | 99% | 95% | 98% | 96% |

While the recruiting environment remained tough, the Army met all recruiting requirements in the Active Component, U.S. Army Reserve (USAR), and Army National Guard (ARNG) in FY 2016.

TABLE 2. Enlisted Recruiting

| | FY 2012 Actual | FY 2013 Actual | FY 2014 Actual | FY 2015 Actual | FY 2016 Goal | FY 2016 Actual |
|---------------------|-------------------|-------------------|-------------------|-------------------|-----------------|-------------------|
| Active Component | 60,489 | 69,154 | 57,101 | 59,177 | 62,500 | 62,681 |
| Army National Guard | 43,297 | 44,734 | 43,280 | 38,430 | 33,000 | 33,135 |
| U.S. Army Reserve | 15,729 | 15,568 | 14,595 | 14,971 | 15,400 | 15,865 |

TABLE 3. Active Component End Strength

| | FY 2012 | FY 2013 | FY 2014 | FY 2015 | FY 2016 |
|---------------|---------|---------|---------|---------|---------|
| Goal | 562,000 | 552,100 | 520,000 | 490,000 | 475,000 |
| Actual | 550,763 | 532,506 | 508,324 | 491,439 | 475,487 |
| Percent Delta | -2.0% | -3.5% | -2.3% | +0.3% | +0.1% |

Performance Measure: The number of Soldiers on active duty at the end of the fiscal year; data as of September 30, 2016; includes Soldiers on Active Duty for Operational Support (over 1,095 days). Under presidential-declared states of national emergency, end-strength limits may be waived. Goals and minimums based upon Sections 401 and 402 of appropriate fiscal year's National Defense Authorization Act (NDAA).

TABLE 4. Reserve (ARNG and USAR) End Strength

| | FY 2012 Actual | FY 2013 Actual | FY 2014 Actual | FY 2015 Actual | FY 2016 Goal | FY 2016 Actual |
|---------------------|-------------------|-------------------|-------------------|-------------------|-----------------|-------------------|
| Army National Guard | 358,078 | 357,735 | 354,072 | 350,023 | 342,000 | 341,590 |
| U.S. Army Reserve | 201,166 | 198,209 | 195,438 | 198,552 | 198,000 | 198,395 |

Performance Measure: The number of Soldiers in ARNG and USAR at the end of the fiscal year; data as of September 30, 2016.

TABLE 5. Active and Reserve Component Retention

| | FY 2011 Actual | FY 2012 Actual | FY 2013 Actual | FY 2014 Actual | FY 2015 Actual | FY 2016 Goal | FY 2016 Actual |
|---------------------|-------------------|-------------------|-------------------|-------------------|-------------------|-----------------|-------------------|
| Active Component | 43,626 | 64,012 | 58,739 | 51,628 | 50,083 | 53,000 | 55,181 |
| Army National Guard | 39,750 | 49,272 | 51,145 | 43,817 | 35,713 | 34,288 | 31,319 |
| U.S. Army Reserve | 10,330 | 14,377 | 15,731 | 15,230 | 16,102 | 12,249 | 15,886 |

Performance Measure: The number of Soldiers reenlisted during a given FY against published goals.



A Soldier walks across a rope bridge.
(U.S. Army photo by Pfc. Jada Owens)

The retention program continued to support Army readiness by retaining Soldiers serving in high demand special skills. In FY 2016, the Army offered a Critical Skills Retention and Selective Retention Bonus to attract and retain personnel in specific skill areas, including Special Forces, Cyber, and Language proficiencies. These bonuses, which are vital tools in retaining Soldiers who possess valuable combat experience, helped the Army to exceed its FY 2016 retention goal. Careful and deliberate adjustments to bonuses, including designation of targeted critical skills, ensured the correct mixture of skilled Soldiers. Recruiting and retaining Soldiers—confident, adaptive, competent, and able to handle the complexity of 21st century warfare in a combined, joint, expeditionary environment—is a highly-competitive endeavor. The Army will continue to develop and implement programs to address them.

STRENGTHENING SOLDIER AND FAMILY READINESS

Family readiness means being prepared to navigate effectively the challenges of daily living experienced in the unique context of military service. Prepared Soldiers and their Families understand the challenges they may face, are aware of supportive resources, have the skills needed to function in the face of challenges, and use those skills and resources to manage challenges.

Total Army Strong succeeds the Army Family Covenant as the Army's commitment and responsibility to our Total Army Family—Soldiers, their Families, and Civilian employees. Through Total Army Strong, the Army remains steadfast in its commitment to maintain trust; foster an environment of adaptability and self-reliance; promote physical, emotional, social, family, and spiritual strengths; and honor the service and sacrifices of those who serve our Nation.

Soldiers, their Families, and Civilians have primary responsibility for their well-being, but through Total Army Strong, the Army remains committed to a system of programs and services to mitigate the unique demands of military life, foster life skills, strengthen resilience, and promote a strong and ready Army.



A military working dog handler laughs at her dog during K9 hoist evacuation training. (U.S. Army photo by Staff Sgt. Siuta B. Ika)

As the Nation and Army prepare for the future, the Army must anticipate the evolving needs of Soldiers and their Families and increase flexibility to ensure programs and services are available where and when they are needed by our most precious resources—Soldiers, their Families, and Civilians.

WARRIOR CARE AND TRANSITION

With the sunset of wars across Theaters, the Army has seen a steady decrease in the number of wounded, ill, and injured entering into the Army's Warrior Care and Transition Program (WCTP). As a result of a significantly reduced population, the Army has reduced its footprint of Warrior Transition Units (WTUs) as well as reduced the organization providing oversight of the WCTP in the interest of increased efficiency in the new norm of a downsized Army, while maintaining the quality of care for our wounded, ill, and injured population. Reconstructed oversight of the WCTP has resulted in the transition of Warrior Care and Transition (WCT), previously known as Warrior Transition Command (WTC), to a Deputy

The funding-supported pillars of the Warrior Care and Transition Program include such activities as:

- **ADAPTIVE RECONDITIONING** (*physical and mental stamina activities*). Includes programs geared toward the holistic healing and mental and physical fitness of wounded, ill, and injured Soldiers.
- **WARRIOR GAMES.** Offers the opportunity to highlight the incredible strength of our Soldiers. The Warrior Transition Command, in partnerships with Department of Defense (DoD) agencies and coalition forces, prepares our Soldiers to compete in Warrior Games and in events, such as *The Invictus Games*.
- **COMPREHENSIVE SOLDIER AND FAMILY FITNESS.** Provides performance enhancement and resilience training.
- **CAREER, EDUCATION, AND READINESS PROGRAM.** Provides a disciplined and deliberate approach to prepare Warrior Transition Unit Soldiers properly for success before, during, and after their transition.
- **COMPREHENSIVE TRANSITION PLAN.** As described in the discussion to the right.

Chief of Staff (DCS) element under U.S. Army Medical Command (MEDCOM) Headquarters. Though it is no longer a Command, the mission remains the same - to provide the Army's wounded, ill, and injured Soldiers, Veterans, and their Families with the care, medical management, and transition support they need and deserve. The MEDCOM DCS WCT ensures focused and effective management across all aspects of the WCTP. In FY 2016, the Department of Defense dedicated \$183.5 million to the Army to resource the Warrior Care and Transition Program with support staff, training, information technology, and adaptive reconditioning/rehabilitative programs and events.

As the Army's proponent for WCT, the DCS WCT, provides centralized oversight, guidance, and advocacy empowering wounded, ill, or injured Soldiers, Veterans, and their Families using integrated medical and nonmedical plans for successful reintegration into the force or the community with dignity, respect, and self-determination. Currently, there are approximately 2,127 Soldiers receiving care and transition services at 15 WTUs and Community Care Units on Army installations throughout the continental United States, Germany, Alaska, Hawaii, and Puerto Rico. In support at each of these locations are the Army's Soldier Family Assistance Centers and other installation provided support activities. The Army's Wounded Warrior Program, under the direction of the DCS WCT, supports over 21,500 Soldiers and Veterans with the holistic assistance of over 200 advocates, acting as recovery care coordinators, located at major military treatment facilities, Army installations, Department of Veterans Affairs medical centers, and in local communities throughout the continental United States, Germany, Alaska, Hawaii, and Puerto Rico. These advocates function as integrated, collaborative members of multidisciplinary healthcare and benefit teams within the Warrior Care and Transition Program to assist the most severely wounded, ill, and injured Soldiers, Veterans, their Family members and caregivers.

To empower each WCTP Soldier to either return to the Force or transition to veteran status, the Army developed a systematic framework known as the Comprehensive Transition Plan (CTP). The CTP is a dynamic living plan of action that focuses on the Soldier's future and encompasses the six domains of career, physical, emotional, social, family, and spiritual. The individual plan is created by the Soldier with the assistance of a dedicated Triad of Care and Interdisciplinary Teams. Using a standardized framework and specifically developed software, the process enables wounded, ill, and injured Soldiers to customize their recovery plans to set and reach their personal and professional goals. In total, through FY 2016, resourcing allowed approximately 43 percent of the wounded warrior population to Return to the Force, while enabling another 55 percent through internships, civilian education and training,

to transition to civilian life confidently and, when possible, successfully enter the workforce. The program's success can be attributed, in part, to an aggressive clinical and non-clinical rehabilitative approach and career and education assistance. The Army will remain dedicated to the mission of holistic healing for our Soldiers through the work of the WCTP as Behavior Health and Post Traumatic Stress Disorder continues to impact our force.

READY AND RESILIENT CAMPAIGN

The Ready and Resilient Campaign (R2C) is a comprehensive plan to address the immediate and enduring needs of the Total Army, including USAR, and ARNG Soldiers, their Families, and Army Civilians. The R2C guides the Army's efforts to build and maintain resilience across the Total Army to improve unit readiness and further reinforce the Army profession. The Army supports R2C through various programs and services delivered on the garrison, such as, but not limited to, Sponsorship, the Army Substance Abuse Program, Suicide Prevention, Comprehensive Soldier and Family Fitness Program,

Soldier Family Assistance Centers, Army Communities of Excellence, internships, and Transition programs.

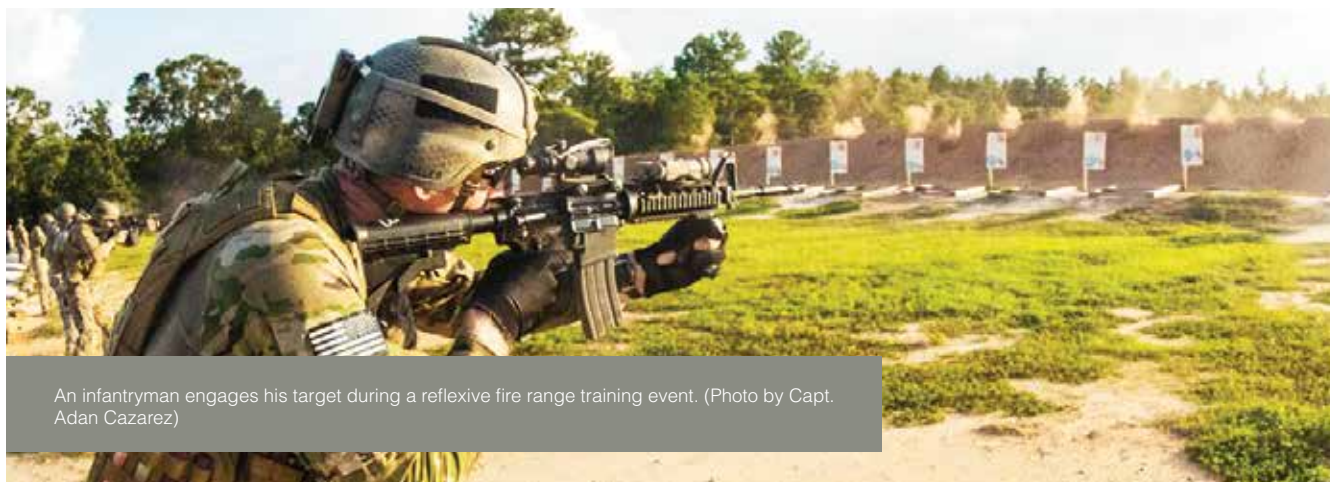
IMPROVING SOLDIER AND FAMILY HOUSING

The Army has pledged to provide for Soldiers and their Families a quality of life commensurate with their service. The Army continues to receive congressional support for housing programs in order to improve both family and unaccompanied housing and to enable the Army to fulfill its pledge. The Army continues to eliminate inadequate family housing at enduring locations through privatization, replacement and improvement projects and divestiture of excess or substandard inventory.

The Army maintains about 10,300 Army-owned family housing units and seeks to improve or replace inadequate family residences to achieve a 90 percent 1st quarter and 2nd quarter quality standard. The privatization of housing at 44 installations was completed on schedule in FY 2010. These 44 installations have an end-state inventory of 86,077 family homes. In addition to privatized family housing, the Army executed five unaccompanied



Family and friends send off Soldiers for federal active duty in the Middle East. (Photo by Marc Heaton, 29th Infantry Division, Public Affairs)



An infantryman engages his target during a reflexive fire range training event. (Photo by Capt. Adan Cazarez)

housing (UH) privatization projects. Four UH privatization projects were for Staff Sergeants and above at Forts Irwin, Drum, Bragg, and Stewart; and the fifth project was for Sergeants and those ranked below at Fort Meade. Together, these privatized UH facilities will provide 2,408 bedrooms at five installations for unaccompanied personnel.

The Army's inventory of inadequate lodging is being eliminated at enduring United States locations through the Privatization of Army Lodging (PAL) program, and divestiture of excess or substandard facilities. PAL buildings are located at 41 installations, and are in the development phase, which is scheduled to be completed by FY 2022 with a projected end-state of 12,492 guest rooms.

As of the end of FY 2016, the Army maintains an inventory of approximately 182,600 permanent party (PP) barracks spaces, only 139,105 spaces of which are required. Unfortunately, while the Army's inventory of approximately 154,300 adequate barracks spaces exceeds its requirement, some installations still possess either a quantity deficit or quality deficit of PP barracks spaces. The Army is conducting a comprehensive inventory of its barracks spaces during FY 2016 and FY 2017 in order to enable it to better formulate a strategy for rightsizing its inventory. It is also examining the resource and readiness implications of revising its current construction standard from 1+1E for permanent party to a 2+0 standard in order to potentially allow units to house junior enlisted Soldiers together, thereby increasing readiness by reducing isolationism.

The Army's Training Barracks Modernization Program constructs, restores, and modernizes initial entry and institutional training barracks to eliminate existing deficits and improve facility quality for Soldiers attending basic training, one-station unit training, and advanced individual training. As of the end of FY 2016, the Army has 89,329 spaces in the training barracks inventory. The buyback program for Training Barracks is expected to be complete in FY 2025.

PREPARE

To prepare Soldiers, units, and equipment, the Army must maintain a high level of readiness for success in current operations, especially in Afghanistan and Iraq, while maintaining a deterrent force that can transition rapidly to decisive action if deterrence fails. The Army is continually adapting training and materiel to maintain an edge against adversaries that are increasingly becoming more capable. The Army remains committed to deploying Soldiers with modern equipment to maintain a technological advantage over any adversary the Army may face.

PROVIDING READY FORCES

The Army's greatest risk, given its high operational tempo, is being ill-prepared to respond to emerging threats and major contingencies with ready and available units. For this reason, readiness is the Army's number one priority.

The Army sustains readiness by leaders optimizing resources and synchronizing activities to train the force in a way that maximizes our readiness against

the operational demand, both current known demand as well as potential war plan contingencies. These key resources and activities include manning, equipping, sustaining, installation support, leading, and training. The Army's new method of force generation, Sustainable Readiness, enables the Army to understand what a ready Army looks like and more importantly, how ready an Army can be generated. It is a philosophy, concept, and process with an underlying model that drives our Army to maximize the overall readiness posture and minimize the risk to war plan contingencies. Sustainable Readiness provides the Army with the much-needed flexibility to respond to the broad array of security challenges in the contemporary operating environment.

Sustainable Readiness builds and preserves the highest possible unit and overall Army strategic readiness, while minimizing risk to meeting operational demands within existing resources. It will posture the Army to manage risk effectively and maximize the Army's ability to fight and win when called. As such, it allows the Army to assess readiness requirements to assure the support of both existing and contingency

war plan demands. Ultimately, the objective of Sustainable Readiness is to sustain an optimized level of readiness throughout the Total Army to be prepared for the requirements of an operational force, to include early-deployers for war plans, as well as the operational and strategic depth of follow-on forces.

TRAINING SOLDIERS

The Army's institutional training and education system for Soldiers includes Initial Military Training (IMT), Professional Military Education, and Special Skills / Functional Training. In IMT, the Army builds the foundation for Soldiers to be experts in critical combat skills and cultivate self-confidence, adaptability, physical strength, resilience, and mental agility. A primary part of a Soldier's IMT instruction includes basic skills called warrior tasks and battle drills. Warrior tasks and battle drills are reviewed about every two years to ensure their relevancy to current combat operations and doctrine. The IMT is the Army's top priority within the institutional training base. Throughout their career, Soldiers acquire knowledge and skills through resident courses, mobile training teams, and distributed learning.

TABLE 6. Individual Training

| Initial Military Training | Basic Combat Training | One-Station Unit Training | Advanced Individual Training | Basic Officer Leader Course | Officer Candidate School | Warrant Officer Candidate School | Initial Entry Rotary Wing |
|---------------------------|-----------------------|---------------------------|------------------------------|-----------------------------|--------------------------|----------------------------------|---------------------------|
| FY 2013 Trained (Actual) | 75,860 | 30,364 | 88,550 | 14,588 | 1,139 | 1,888 | 1,127 |
| FY 2014 Trained (Actual) | 67,865 | 26,738 | 88,245 | 12,873 | 866 | 1,730 | 910 |
| FY 2015 Trained (Actual) | 65,983 | 26,033 | 82,717 | 12,246 | 756 | 1,580 | 910 |
| FY 2016 Trained (Interim) | 47,116 | 16,879 | 65,152 | 9,082 | 555 | 1,543 | 425 |

Data reflects only Army students.

FY 2013- 2014 data is from the FY 2015 report, which included Army and other Service schools that Army Soldiers attended.

FY 2015-2016 data is from the FY 2016 report as of September 19, 2016, which included only Army schools.

FY 2015 and FY 2016 data include follow-on courses, while FY 2013-2014 data does not include all follow-on courses.

FY 2016 interim data is based on report data as of September 19, 2016, i.e., not a complete reporting year.

TRAINING UNITS

In the 1st Quarter FY 2016, training by Army units was constrained by the Continuing Resolution Authority and budget controls, even though there were modest increases in ground home station training and the flying hour program resources. The Army focused training resources on maintaining the decisive action readiness of Brigade Combat Teams (BCTs) through demanding training and live fire exercise at home station and Combat Training Centers (CTC). The

official results for training miles and hours executed in FY 2016 were not yet available at the time of this publication.

The Army's CTC Program remains the cornerstone of an integrated Training strategy that builds trained and proficient, combat-ready units and leaders to conduct operations as part of the Joint Force – ready to win in a complex world.

The purpose of the CTCs is to provide a crucible experience for units and leaders training in a complex and highly realistic Decisive Action environment designed to replicate combat by stressing every Warfighting Function with operations against tough, free-thinking, realistic hybrid threats under the most difficult conditions possible. The CTCs will accelerate a return to a decisive action focus from a counter-insurgency focus by challenging units and leaders to adapt to battlefield conditions, and by enhancing lethality and our ability to operate with our Unified Action Partners and Special Operations Forces across the range of military operations. The desired end state of a CTC rotation is units and leaders who are prepared to deploy worldwide, fight with confidence, and win, at any time, against any adversary, under any conditions.

In FY 2016 the Army conducted 19 rotations at maneuver CTCs: 16 Decisive Action/Unified Land Operations (DA/ULO) rotations for Active BCTs, two DA/ULO rotations for ARNG BCTs, and one enabler rotation (Defense Chemical Biological Radiological Nuclear Response Force Exercise). The Mission Command Training Program conducted

command post exercises for 55 HQs (4 Army Service Component Command, 1 Corps, 7 Division, 6 BCT, 1 Expeditionary Sustainment Command, 7 Sustainment Brigade, and 29 Functional or Multifunctional Brigade).

TRAINING SUPPORT SYSTEMS

The Army's Training Support System (TSS) enables training at home stations, CTCs, and other institutions by creating realistic conditions that reflect the operational environment. The TSS also enables Soldier self-development by modernizing the Army's distributed learning point of delivery infrastructure. The TSS provides training support products, services, and facilities in the form of critical training enablers, such as ranges and targets; live-virtual-constructive and gaming Training Aids, Devices, Simulators, and Simulations (TADSS); instrumentation systems; training facilities; maintenance of fielded TADSS; and training support operations and management. The FY 2016 funding levels provided base capability to enable training readiness. The TSS will continue to utilize the Strategic Portfolio Analysis and Review, which provides strategic guidance to prioritize and sequence the products within the TSS portfolio.



Developing leaders today is the key to preparing the Army for the future. The increasingly uncertain, complex, and interconnected global environment demands an investment in leader development; the life-long synthesis of training, education, and experience acquired through opportunities in the operational, institutional, and self-development training domains, enabled by the training support system.

The CTC Modernization Program (CTC Mod) continued to field the Range Communications System, which provides an updated voice and data communications system that enables the CTC Instrumentation System (CTC IS) to include a third maneuver battalion and to provide a realistic operational environment necessary to stimulate and track rotational units, Opposing Force, and role player activities. It also tracks operational ground-truth, combat engagements, and unit performance necessary to provide the rotational unit's fully analyzed feedback in the form of After Action Reviews. The Army continues to address challenges of implementing system performance and testing; however anticipates performance of the Government Acceptance Test beginning April 2017.

The Mission Command Training Support Program modernizes Mission Training Complexes (MTCs) and training simulations to upgrade individual and collective training to include battle-staff training for mission-rehearsal capabilities for units. The MTCs provide units the ability to train and sustain critical individual/operator and collective battle-staff skills on Mission Command Information Systems. The MTCs network with other installations and simulation capabilities to support Army, Joint, and Coalition training events. New TSS capabilities were fielded to support requirements driven by the Army Campaign Plan. A persistent Live, Virtual, Constructive-Integrating Architecture (LVC-IA) has been implemented at selected home stations. The LVC-IA links Home Station Instrumentation Training Systems in live training areas to MTCs, which house constructive, virtual, and gaming TADSS. The MTC serves as the nexus for the installation's LVC-IA, which has completed fielding to 12 installations.

Sustainable Range Program (SRP) and Integrated Training Area Management (ITAM) maximize the capability, availability, and accessibility of ranges and training lands to support doctrinal requirements, mobilization, and deployments under normal and surge conditions. The SRP provides modernization of the Army's range complexes using training systems fielded on ranges. The SRP also provides range operations and maintenance to support individual

and crew-serviced weapons qualification at over 100 Continental United States (CONUS) and outside the Continental United States (OCONUS) locations, and collective live fire capability on the largest 25 installations. The capabilities provided at each of these locations were reduced to levels appropriate with the reduction of the force. Ranges continue to be modernized to integrate digital systems that enable squads and platoons to train as they fight, as well as to provide commanders and leaders with objective data to assess their units' performance and training levels. The ITAM provides Army range officers with the capabilities to manage and maintain training lands and support mission readiness. By implementing a uniform land management program, ITAM integrates the mission requirements derived from the SRP, with environmental requirements and environmental management practices. It also establishes the policies and procedures to achieve optimal, sustainable use of training and testing lands.

Soldier Training Support Program (STSP) reduced programmed acquisition and fielding for systems, such as the Homestation Instrumentation System, Engagement Skills Trainer (EST), Call for Fire Trainer (CFFT), and Medical Simulation Training Centers (MSTC), which are critical components of the Live, Virtual, Constructive – Integrated Training Environment (LVC-ITE). However, Instrumentable Multiple Integrated Laser Engagement System (IMILES) buyout continued an accelerated fielding to achieve “pure fleet” distribution. Additionally, the lack of funding for planned upgrades and improvements to support concurrency, relevance, and usefulness of fielded devices, such as the EST, CFFT, and the Improvised Explosive Device Effects Simulator, has had a negative impact on modernization of devices fielded at home station and institutional locations for nearly a decade. The STSP continued to provide Common Levels of Support manpower and services, however directed TSS manpower Table of Distribution and Allowances authorization reductions have significantly challenged execution commands in delivering specified services to mission commanders. New requirements, driven by the fielding of approved systems, e.g., flight simulators, MSTCs, and the

LVC-ITE, increased manpower requirements in an era of significant reductions. The result will be a reduction of baseline services to all customers at most installations. Because Reserve Component units must habitually train on evenings and weekends, there will be an even greater reduction in available services to the Reserve Component customer base at installations with regional training support service delivery responsibility. Reductions in authorized Training Support Center manpower have resulted in systemic maintenance challenges and operational ready rates for complex TADSS, e.g., IMILES, as diagnostics and troubleshooting are conducted by inexperienced users, rather than by trained contact teams, resulting in significant increases in repair costs, repair turnaround times, and decreases in training benefit to Soldiers and commanders.

Army Training Information System (ATIS) will provide an enterprise capability to enable the training environment for scheduling, development, learning management, training management, and resource management for individual and collective training and education. The Army Acquisition Executive (AAE) approved the Materiel Development Decision, which authorized proceeding to the Materiel Solution Analysis phase of the Acquisition process. In addition, the AAE signed the Acquisition Decision Memorandum on October 7, 2014, which authorized the performance of the Analysis of Alternatives. The ATIS Team is seeking a Milestone A Decision from AAE in 1st Quarter FY 2016. Army TSS, including manpower and operations support required to maintain and operate TADSS, must continue to keep pace with equipment modernization and Army transformation. This will ensure that training supports current operations, addresses Sustainable Readiness Model training and readiness requirements, and enables training Army forces for prompt and sustained land combat operations.

ADAPTIVE ARMY LEADERS FOR A COMPLEX WORLD

Unit training and leader development are the Army's life-blood. Developing leaders is a competitive advantage the Army possesses that cannot be replaced by technology or substituted with advanced weaponry and platforms. Developing leaders today is the key to preparing the Army for 2020 and beyond. The increasingly uncertain, complex, and interconnected global environment demands that an Army of preparation invests in leader development: the life-long synthesis of training, education, and experience acquired through opportunities in the operational, institutional, and self-development domains. The Army is focused on developing our Military and Civilian leaders to meet the challenges of the 21st century and holding commanders responsible for developing and executing progressive, challenging, and realistic training guided by the doctrine of mission command. These efforts will result in more adaptive forces capable of achieving regional alignment or mission tailoring as required. Guided by the Army Leader Development Strategy, the Army is undertaking efforts to foster continued commitment to the Army profession, preserve the all-volunteer force, and build leaders for our Nation.

The Army must balance its commitment to the training, education, and experience components of leader development. Due to the high operational demand over the past 15 years, many Army leaders did not attend professional military education (PME) at the optimal time in their careers. To reduce PME backlog, the Army leveraged the One Army School System, implemented Structured Self-Development, increased the use of Distributed Learning to conduct PME, and implemented Select-Train-Educate-Promote (STEP) policy requiring enlisted Soldiers to graduate from the appropriate formal Noncommissioned Officer Education System course before attaining eligibility for promotion. STEP policy sets conditions to better prepare Noncommissioned Officers before assuming the duties and responsibilities of the next higher grade.

TABLE 7. Professional Development (Active Component Schools Only)¹

| | 2016 Professional Development (Active Component Schools Only) | | | | | | | | |
|--|---|------------------------|----------------------|---|--|--|--|--|---|
| | NonCommissioned Officer Education System (NCOES) Graduates | | | | Officer Education System (OES) Graduates | | Warrant Officer Education System (WOES) Graduates | | |
| | Basic Leader Course | Advanced Leader Course | Senior Leader Course | Sergeants Major Course Resident/Ph 2 Non-resident | Intermediate Level Education Resident/ Common Core | Senior Service College (SSC) Resident/ Distance Learning | Warrant Officer Advance Course Resident/Non-resident | Warrant Officer Staff Course Resident/Non-resident | Warrant Officer Senior Staff Course Resident/Non-resident |
| FY 2012 Trained (Actual) | 27,756 | 18,259 | 10,449 | 592/671 | 1,076/952 | 911/699 | 2,688/430 | 1,034/1,014 | 316/348 |
| FY 2013 Trained (Actual) | 23,254 | 17,670 | 9,600 | 450/520 | 1,132/946 | 901/756 | 2,485/295 | 1,087/900 | 981/345 |
| FY 2014 Trained (Actual) | 19,489 | 16,066 | 8,827 | 404/564 | 1,118/943 | 930/662 | 2,347/338 | 969/929 | 387/387 |
| FY 2015 Trained (Actual) ² | 18,726 | 11,816 | 7,599 | 423/495 | 1,019/941 | 879/660 | 2,461/507 | 1,182/1,087 | 358/367 |
| FY 2016 Trained (Interim) ² | 15,984 | 15,379 | 7,878 | 0/355 | 0/608 | 671/0 | 2,219/323 | 1,071/785 | 356/371 |

Note 1: This data represents Active Component, ARNG, and USAR students graduating from Active Component schools. All data is based on start date, i.e., if a class starts in FY 2015 and graduates in FY 2016, it is counted as FY 2015 data.

Note 2: Actual FY 2015 trained data and interim FY 2016 trained data are as of September 30, 2016.

ARMY CIVILIAN TRAINING AND LEADER DEVELOPMENT

The Army is keenly aware of the valuable contributions made by its Civilian corps in supporting the National Military Strategy. Here, too, it must provide training, education, and operational experiences that develop and improve the leadership competencies, which collectively enhance this cadre's ability to support Soldiers, the Army, and the Nation. To advance this goal, the Army maintains the Civilian Education System leader development program. Courses are sequential and progressively targeted at specific civilian grade levels to be taken throughout the civilian's career. Specifically, the Civilian Education System (CES) meets the Secretary of the Army's mandate that the leaders of tomorrow be adaptable and multi-skilled. This mandate demands a centralized education, training, and development program in which to "grow" Civilian leaders who—in both operational and institutional capacities and in evolving environments—can meet and succeed in their missions.

TABLE 8. Civilian Professional Development

| Program | Students |
|--|----------|
| Senior Service College (Army War College/ Dwight D. Eisenhower) | 22 |
| Leader Development Programs | 66 |
| Army Civilian Education System Leader Development Courses-Resident | 3,996 |
| Army Civilian Education System Leader Development Courses-Online | 21,744 |
| Supervisor Development Courses-online | 12,587 |
| Management Development Courses-online | 5,161 |
| Career Field Functional Training Courses | 10,751 |

Section 1113 of the NDAA for FY 2010, and the Federal Supervisory Training Act of FY 2010, outline specific requirements for the development of a mandatory supervisor training course for all DoD supervisors, both Civilian and Military. Specifically, supervisor training must include the use of new NDAA authorities, instruction on prohibited personnel practices, and mentoring of new supervisors. First-time supervisors who are in their jobs for less than two years are required to complete training no later than one year from the date on which they are appointed to a supervisory position. Supervisors are also required to take refresher training every three years.

The Army revised its Supervisor Development Course to meet the NDAA requirements. Training for all

supervisors of Civilian employees promotes the development of world-class leaders and provides opportunities for new managers and supervisors to interact, share experiences, and learn from each other. This training ensures continuity of the leadership and supervisory pipeline, and promotes the Army's vision for competency-based development across the leadership continuum. The Army is committed to improving employee engagement by investing in efforts that make the Army an employer of choice in the Federal Government.

In direct support of the Secretary of the Army's initiative to transform the Army Civilian workforce, the Civilian Training and Student Account (CTSA), was established for Army-funded Civilians attending an Army Senior Service College (SSC), i.e., the Army War College and the Dwight D. Eisenhower School for National Security and Resource Strategy. The account mirrors the Military Trainees, Transients, Holdees, and Students account by reassigning SSC participants to an HQDA-centralized operational Table of Distribution and Allowances. By assigning SSC participants to the CTSA, the command providing the individual for SSC attendance can immediately backfill against the position and mitigate any disruption to the organizational mission.

Based on its prior successes, the Army continues to use the CTSA, and will subsequently place graduates in enterprise positions most needed by the Army. Recently the Army renamed the CTSA to Civilian Personnel Training Account (CPTA). Other initiatives will be developed and implemented to ensure a robust, accessible training program for all Army Civilians. These initiatives include, but are not limited to, the following:

- An Army-wide Civilian training management system.
- Fellowships and experience-broadening interagency and multinational assignments.
- Increased outreach and communication to the Army Civilian Corps with the goal of increasing training and leader development participation.

The Army will continue to refine, improve, and update

the CES programs to meet emerging initiatives and requirements and enhance employee performance.

RESET

In FY 2016, Congress appropriated \$3.12 billion to resource operational (Operation and Maintenance, Army) and procurement programs (Other Procurement, Army) for Overseas Contingency Operations Reset. The Army obligated its full Reset operational and sustainment funding. Six brigades completed Field Level Reset in FY 2016. Three brigades are in the Reset process. Army Materiel Command (AMC) reported the completion of 30,130 items of the FY 2016 Annual Sustainment Level Reset requirement. The FY 2016 requirements were adjusted periodically to reflect real-world changes in demand, due to the dynamic operating environment that existed overseas. Equipment deemed beyond economical repair accounted for fluctuations in both carry-in and FY 2016 requirements. The Army executed 100 percent of the \$712.7 million available from FY 2014 Procurement Funding, 93 percent of the \$995.3 million available from FY 2015 Procurement Funding, and executed 69 percent of the \$1,217.2 million available from FY 2016 Procurement Funding.

MODERNIZATION

The Army's funding for equipment modernization entered a critical time frame during FY 2016. This year's budget represents the Army's equipment modernization during a period where the operational and fiscal environments are straining Army efforts to balance modernization to meet current demands, while building the foundations of a force that can meet future challenges. Over the past several years the Army has absorbed significant reductions in Research, Development, and Acquisition (RDA) accounts.

The Army took three steps to minimize the effect of reduced RDA funding on equipment modernization. First, the Army successfully protected our Science and Technology (S&T) funding at President's Budget (PB) 2015 levels. Protecting S&T helps maintain the Army's future overmatch capabilities in the mid- to far-term. Next, the Army carefully reduced the number and pace of new systems in development to meet

budget parameters, while accepting the risk of reduced operational overmatch. Finally, the Army continues to develop and improve current equipment components, systems, and sub-systems to enhance capabilities, albeit at a slower modernization rate.

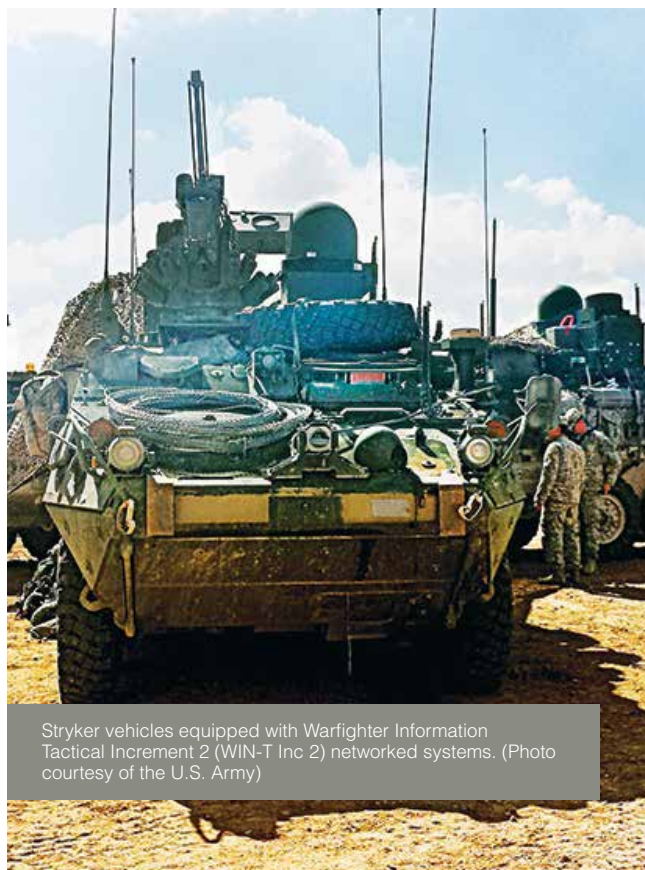
There are three main efforts this year that characterize equipment modernization. These efforts are:

Focused Technology Investment: The Army intent is to protect core capabilities aligned with the 30-year strategic equipment plans and foster innovation, maturation, and demonstration of technology enabling capabilities to prepare for the Army of the future. The Army met Defense Department guidance to fund S&T at PB 2015 levels. The key efforts are in combat vehicle prototyping, assured Position/Navigation/Timing and technology demonstrations for Joint Multi Role helicopter and High Energy Laser efforts. The Army is also able to continue some investments in technologies for degraded visual environments, long-range fires, cyber, high energy laser, materials, and quantum science technologies.

System Development: The Army has limited systems in development and has slowed the pace of development to meet budget parameters, while accepting risk of reduced overmatch for the remainder of this decade. Some systems that this budget continues to support and increase capabilities for the near- and mid-term are:

- Tactical Vehicles: Armored Multipurpose Vehicle and Joint Light Tactical Vehicle;
- Air and Missile Defense: Integrated Battle Command System; Indirect Fire Protection Capability; future radar;
- Aviation: Improved Turbine Engine Program;
- Intelligence and Electronic Warfare: Maintains Aerial Intelligence, Surveillance, and Reconnaissance 2020 Strategy; and
- Network: Small Airborne Network Radio.

System Upgrades and Procurement: By continuing



Stryker vehicles equipped with Warfighter Information Tactical Increment 2 (WIN-T Inc 2) networked systems. (Photo courtesy of the U.S. Army)

to develop and improve existing components, sub-systems, and systems the Army improves capabilities. Our priority focus is to enhance capabilities of the current force through low risk and cost-effective fleet modernization. Some examples are:

- Soldier Equipment: Maintains our priority focus on Soldiers; fields systems such as Soldier Protection Systems, Counter-Defilade Target Engagement systems, and Family of Weapon Sights;
- Vehicles: Double-V Hull for 4 of 9 Stryker Brigades; HERCULES recovery vehicles for 9 of 15 Armored Brigade Combat Teams (ABCT); Paladin upgrade for 7 ABCT; Abrams upgrades for 2 ABCT; Bradley upgrades for 4 ABCT;
- Aviation: CH-47F for 3 Chinook companies; AH-64E for 2 Apache battalions, UH-60M for 2 Assault battalions and 2 Medical Evacuation companies; Light Utility Helicopter for the training base;
- Integrated Fires and Air Defense: Procures insensitive munitions compliant Alternative

Warhead for 63 percent of the Guided Multiple Launch Rocket System inventory; service life extension for 10 percent of the Army Tactical Missile System inventory; upgrades to Patriot systems; improved Patriot missile for 17 percent of the missile inventory; and

- Network: Synchronizes network capabilities by procuring WIN-T Increment 2 for 3 brigades, 3 division headquarters and 6 battalions realigned to BCT. Procures and fields Handheld, Manpack, and Small Form Fit Rifleman Radio systems for 3 Operational Capability Set BCTs in FY 2016. Additionally, procures Joint Battle Command-Platform for approximately 30 BCTs and Brigade size formations, including replacement of Enhanced Position Location and Reporting System radios in BCTs.

Our equipment modernization efforts reflect the priorities of a relatively modern Army with constrained resources. Affordability and cost-effectiveness are prime factors in planning resources to modernize our equipment and close capability gaps in this fiscal environment.

BRIGADE COMBAT TEAM REORGANIZATION

In July 2015, the Army announced the Active Component would inactivate two BCTs by the end of 2017: 4/25 Infantry Division (ID) Airborne Infantry BCT (IBCT) from Joint Base Elmendorf-Richardson, Alaska, and 3/3 ID IBCT from Fort Benning, Georgia, bringing the number of active BCTs to 30. At the same time, two battalion task forces will be created at the locations of the inactivated brigades to retain combat power and provide the means to grow the Army in the future if necessary. These battalions will also be available to be employed for a variety of missions or to round out the OCONUS IBCTs, bringing them up to a three maneuver battalion BCT. This reduction is a part of a larger effort to comply with the 2011 Budget Control Act, reducing the Active Component from 490,000 to 450,000 Soldiers. Part of the reduction strategy is also to redesign the ABCT by reducing each brigade by two infantry companies. As a result, the ABCT will field two armor heavy combined arms battalions (two tank companies (COs) and one infantry CO) and one infantry heavy combined arms battalion.

To preserve the same number of armor COs, a tank CO will be added to the cavalry squadron. Four Active Component IBCTs outside the contiguous United States (Italy, Alaska, and two in Hawaii) remain resourced with two maneuver battalions.

The Army's employment of modular formations and their prepare phase following sustained combat operations helps manage the impact and mitigate the effects of high operational demand. As America's dominant and decisive force, the Army remains committed to securing United States' interests across the full range of operations—from aiding civil authorities and citizens at home, to combating insurgents abroad.

SCIENCE AND TECHNOLOGY PROGRAM

The Army's S&T investments support Army modernization goals to develop and field affordable equipment in a rapidly changing technological environment. The Army's S&T mission is to foster invention, innovation, and the use of new technologies to enable future force capabilities, while exploiting opportunities to apply new technology capabilities to the current force. The Army depends on its S&T program to research, mature, and demonstrate new science and technology options that maintain leading edge technology; enable a broad technology outlook; and go beyond the limits of static threat assessments to prevent tactical, operational, and strategic surprise.

The Army's S&T investments reflect a balanced approach to far-term, basic research for discovery and understanding of phenomena [Research, Development, Test, and Engineering (RDT&E) Budget Activity (BA) 1]; mid-term, applied research for laboratory concept demonstrations to develop and evaluate the feasibility and practicality of proposed solutions (RDT&E BA 2); and near-term, advanced technology demonstrations of subsystems and components in relevant environments (RDT&E BA 3). In addition, the Army S&T and Acquisition communities have partnered to invest a portion of the Army's RDT&E BA 4 funding (Advanced Component Development and Prototypes) to mature high potential technologies further, reduce transition risk to Army programs of record, more quickly provide mature technologies earlier in the acquisition life cycle, and

increase competitive prototyping. For FY 2016, the Army S&T funding level helped maintain the Army's future overmatch capabilities in the mid- to far-term. The Army has dedicated more than \$2 billion to its S&T Program in FY 2016, all of which is aligned with the Army's needs and priorities: \$425 million in RDT&E BA 1, \$880 million in RDT&E BA 2, and \$896 million in RDT&E BA 3.

The Army S&T program is organized into eight investment portfolios that have been scoped to provide Soldiers with the technology to win by enhancing the current force and enabling the future force:

- Soldier Portfolio: Executes innovative S&T programs that increase the effectiveness, health, and reliability of the human component of the total Army and develops and integrates the equipment that can unburden Soldiers/Squad during dismounted operations.
- Ground Portfolio: Provides overmatch of offensive, defensive, and mobility capabilities in weapons and military vehicles and includes the Combat Vehicle Prototyping Program. Sustainment S&T efforts are focused within the Soldier/Squad and Ground Portfolios.
- Air Portfolio: Aims to be the global leader in providing game-changing range, payloads, speed, survivability, and lethality to maintain technical superiority and combat overmatch for vertical lift systems.
- Lethality Portfolio: Includes Weapon Enablers, Fire Support, Directed Energy, Close Combat, and Air Defense to provide affordable weapon systems with improved performance and increased survivability.
- Command, Control, Communications, and Intelligence Portfolio: Provides Soldiers at the tactical edge with trusted and responsive sensors, communications, information, cyber, and electronic warfare adaptable in dynamic and austere environments to support battlefield operations and non-kinetic warfare.

- Medical Portfolio: Focuses on materiel and knowledge-based medical solutions to increase warfighter fitness, health, protection, and resilience; improves downrange health delivery; and enhances recovery, rehabilitation, or reintegration.
- Innovation Enablers Portfolio: Supports all of the Army's generating and operational forces with environmental quality and installations and high performance computing.
- Basic Research Portfolio: Underpins all of the Army S&T efforts to build an agile and adaptive foundation of technical understanding and knowledge so that the Army can respond to future threats and maintain technological overmatch.

Integrated within each of these programs is the Army's Technology Maturation Initiative and Manufacturing Technology (ManTech) program. The Technology Maturation Initiative invests in technology efforts that are closely partnered with planned or existing programs of record, seeking to mature and prototype technologies further before Milestone B. The ManTech program is a key aspect of the Army mission to provide Soldiers with a decisive advantage in any mission. It addresses required manufacturing maturation for critical S&T efforts, provides cost reduction in current manufacturing and repair processes, and enables above-the-shop-floor efforts related to digital product and production data.

The Army S&T Program continues to identify and harvest technologies suitable for transition to our current and future Force. A strategic approach to modernization is being executed to address emerging threats; current and future technology gaps; and leverage state-of-the-art commercial, academic, other government agency, and international partner research, and limited resources. The focus remains on the Soldier; Army S&T consistently seeks new avenues to increase the Soldier's capability and ensures their technological superiority today, tomorrow, and decades from now.

LANDWARNET OPERATIONAL CAPABILITIES AND FOCUS

In the complex world described in the Army Operating Concept, the network operating environment presents ever-evolving threats and opportunities. Even as network capabilities enable the Army to conduct successful business and warfighting functions, our adversaries have access to similar technologies with which to avoid our strengths and exploit our vulnerabilities. This and other challenges to the development and defense of an “always on, always available” capability require a robust combination of materiel, personnel, processes, and policy solutions. From a network perspective, changes in the Army’s operating environment are manifested in several major areas: the strategic conditions, fiscal boundaries, and technological evolution, which includes the cyberspace mission.

Recent and ongoing conflicts reinforce the need to balance the technological focus of Army modernization with recognition of the limits of technology and an emphasis on the human, cultural, and political aspects of armed conflict. The strategic environment is characterized by a constantly shifting geopolitical landscape facilitated by the proliferation of information and communications technologies that increase the momentum of human interaction. The Army cannot predict whom it will fight, where it will fight, and with what coalition it will fight, so the network must support a broad range of potential missions with a myriad of possible unified action partners. An Army that is globally engaged and regionally aligned requires access at the point of need, robust network capacity, and capability that is tailorable and scalable to support the full range of business and warfighting processes.

To achieve these capabilities, the Army is following an enterprise and regional approach. The investments made in FY 2016 continue to focus on optimizing the Signal force, enhancing cybersecurity capabilities, increasing network capacity, delivering IT services to the edge, and strengthening network operations. These efforts are consistent with the Joint Information Environment, covers 95 percent of the CONUS

population, and represents the most significant modernization of the CONUS network in DoD history.

DEVELOPING THE NETWORK OF 2025

To enable the Army of 2025 to meet the challenges of the 21st century, the Army is working to rebalance and unify the network to provide an end-to-end capability. The Army will synchronize the hardware, applications, and services that support both warfighting and business operations. Using assessments conducted as part of the Army Enterprise Network portfolio management process and the Army Warfighter Challenge process, the Army will continue to maintain and modernize the network. Efficiencies from ongoing network modernization efforts will be realized over the Future Years Defense Program (FYDP). The main goal of network modernization continues to be the transition to a managed services model, Army Enterprise Service Management, in alignment with DoD and Joint guidance.

EFFICIENCIES AND COST SAVINGS

LandWarNet investments in FY 2016 continued to adapt to the continuing uncertain financial environment during the Program Objective Memorandum years. The Army has taken disciplined steps to deliver standardized solutions, to improve network resilience and regionalize data centers continuously, and to enhance cyber security, by leveraging commodity buys, consolidation activities, and proactive contract management. As a result, the Army continues to reduce operating costs and create efficiencies to reinvest in LandWarNet modernization. Table 9 lists specific cost reduction/avoidance successes. Looking forward, these investments are the precursor to meeting the Secretary of the Army’s directive (Secretary of the Army’s memo September 9, 2011, subject: Information Technology (IT) Management Reform) to achieve \$1.5 billion in annual IT savings beginning in FY 2015. Table 10 displays the savings that these investments are expected to yield.

TABLE 9. Efficiencies and Cost Savings

| |
|--|
| Commodity Buys (Enabled Regionalization and Divestiture Strategy) |
| Utilized bulk-purchase for MPLS routers and end-user building switches |
| Army Data Center Consolidation |
| Data Center Closures: 429 |
| Personnel Efficiencies: 140 (Reductions) |
| Application Efficiencies: 1,299 applications (Kills in Closure Reports) |
| Server Efficiencies: 2,799 servers (Decommissioned) |
| Floor Space Efficiencies: 148,019 square feet (Relinquished or Repurposed) |
| Reported Cost Savings: \$54.3 million |
| Estimated Annual Energy Savings: \$1,546,157 |

TABLE 10. Expected Savings

| Initiative (Amounts in millions) | Total To-Date Realized Savings | Total Expected Savings thru FY 20 |
|--|--------------------------------|-----------------------------------|
| Enterprise Services | (350.2) | (626.0) |
| Enterprise License/Service Agreements | (107.0) | (354.6) |
| Enterprise E-mail | (188.0) | (139.9) |
| Elimination of Devices (Desktop/Laptop/ Tablets/Mobile Devices/Air Cards) | (55.2) | (29.4) |
| Unified Communications (Voice, Video & Chat) | 0.0 | (102.1) |
| Capacity | (55.8) | (310.9) |
| Army Data Center Consolidation Plan (ADCCP) | (55.8) | (76.6) |
| Bulk Buys for Switches - EAS, ACS & ADS | 0.0 | (234.3) |
| Security | | (341.6) |
| Network Modernization - Top Level Architecture (TLA) to JRSS (NIPR & SIPR) | 0.0 | (341.6) |
| Grand Total | (406.0) | (1,278.5) |

BUILDING FORCE PROJECTION READINESS

With recent and rapid changes to the strategic security environment, it is critical to be able to project expeditionary land power globally. The Army can get to the fight, but as a power projection force, it is paramount that the Army improves its ability to deploy forces rapidly into any Theater of Operations no matter its maturity level.

The Army is building readiness by expanding its Emergency Deployment Readiness Exercise (EDRE) program, exercises that test its ability to conduct rapid expeditionary deployments. This is especially important as the Army is becoming more CONUS-based and must develop the ability to project forces rapidly.

This year, the Army conducted four EDREs. For the first time in more than a decade, it included a Sealift Deployment Readiness Exercise, with the 3rd Brigade, 101st Airborne Division, shipping their equipment through the Port of Jacksonville, Florida, on their way to a training center rotation at Fort Polk, Louisiana.

The Army expanded the Army Prepositioned Stocks (APS) Program, its go-to-war assets positioned afloat and ashore around the world. Units



Soldiers attach a cling-load to the belly of a UH-60 Black Hawk. (Photo by Capt. Adan Cazarez)

used the stocks in regionally aligned force rotational exercises; and initiated plans to use them in support of the European Command's expanding mission requirements to deter Russian aggression.

Over the next few years APS will build several training activity sets for humanitarian and sustainment assistance in Southeast Asia, Africa, Central/South America, and in support of special operations in the Middle East.

IMPLEMENTING BASE REALIGNMENT AND CLOSURE/RESTITUTIONING FORCES

Base Realignment and Closure (BRAC) 2005 provided an unprecedented opportunity that improved Army training, deployment, and supply capabilities. The primary goal of BRAC 2005 was to transform the Army so it could properly support combatant commanders conducting two simultaneous conflicts and meet American security commitments around the world. BRAC 2005 was fully synchronized with other Army stationing initiatives, including global defense posture realignment, Grow the Army, and Army modular forces. In addition, BRAC 2005 is currently saving the Army more than \$1 billion of net recurring savings per year. It did so by closing low military value, single purpose installations, and leased facilities that were either no longer relevant or less effective in supporting a joint and expeditionary Army. In partnership with other Services, the Army used BRAC 2005 to transform Reserve Component infrastructure to create more operational opportunities for joint training and deployment. This transformation created efficiencies in core Army business processes.

The Army fully supports the Office of the Secretary of Defense (OSD)'s most recent request for an additional BRAC round in 2019. As the Army's end strength declines alongside available funding, millions of dollars will be wasted maintaining buildings at underutilized installations. The Army must immediately address excess infrastructure and reduce costs at its installations. The Army has taken action within current authorities to reduce our inventory of underutilized facilities, but installation-level footprint reduction efforts will have a limited impact on the overall excess capacity in the Army. The Army estimates those reductions will result in \$150 million

cost avoidance after units consolidate into the best facilities on the installation and facility disposals are completed over the next 5-8 years. Without an additional BRAC round, the Army will still be required to spend substantial amounts of scarce resources to maintain underutilized facilities.

On January 25, 2013, the Secretary of Defense directed a European Infrastructure Consolidation (EIC) analysis with a focus on reducing long-term expenses through footprint consolidation and eliminating excess capacity, while ensuring that the infrastructure properly supports our operational requirements and strategic commitments. The Army, other Services, and four Joint Working Groups, identified and analyzed opportunities for consolidation of functions, including common support functions, such as logistics, training, medical, and Command, Control, Communications, Computers, and Information Technology.

On November 13, 2014, the Secretary of Defense approved 26 EIC actions. The OSD assigned 20 to the Army for implementation, along with 13 "Quick Win" EIC actions that the Secretary of Defense approved and announced in May 2014. The Army spent approximately \$103 million in FY 2016 to implement the 33 EIC actions. The Army received approximately \$177 million in FY 2016 and FY 2017 from OSD to continue implementation. The Army completed 4 additional EIC actions in FY 2016, bringing the total completed to 14 of 33 actions. Collectively, the 33 EIC actions require one-time costs across FY 2016-21 of \$332 million and will yield \$172 million in annual savings beginning in FY 2021. The EIC effort will produce beneficial outcomes for the Army and the Joint Force. The net effect of the EIC effort will be to reduce cost significantly; eliminate excess infrastructure; and validate the remaining European infrastructure without degrading strategic or operational capabilities.

BUSINESS TRANSFORMATION INITIATIVES

Throughout FY 2016, the Army significantly improved the effectiveness of its business governance, while accelerating its business transformation. Army business transformation efforts continue to focus on linking business processes to defined strategies based on complete understanding and analysis of

requirements and cost drivers. From the strategy, the Army continues to improve the business processes and information technology that drives the Institutional Army. The Army's multi-faceted approach to business transformation enabled the Institutional Army to provide trained and ready forces in a smarter, faster, and cheaper way. Army business transformation seeks to:

- Enable strategic outcome based and cost-informed enterprise governance.
- Improve the efficiency and effectiveness of business operations.
- Provide better alignment between business operations and operational forces.
- Improve business process alignment between the Army and DoD.
- Achieve audit-readiness.

In 2016, the Army initiated more targeted business process reengineering "deep dives" to improve business processes and identify improvement opportunities. Deep dives included: streamlining ammunition management and accountability, prioritization of IT systems by Program Evaluation Group, Program Executive Office - Owned Assets to account for property using the Defense Property Accountability System and interface with the Army's Enterprise Resource Planning (ERP) systems for management and auditability, and determination for military pay disbursement for future ERP development. These deep dives removed unnecessary duplication and complexity from selected business processes and their supporting information technology systems. Efforts currently underway include: cost of Training Readiness, Single Army Logistics Enterprise, Transition to Sustainment Governance Group, Aviation Logistics Platform for an auditable maintenance management and recordkeeping for both Army Doctrine and Federal Aviation Administration requirements, and Information Management Data Integrity Project that will form the foundational methodology the Army uses to create enterprise cost models.

In response to persistent resource constraints and vital strategic shifts that force constant change on

our institutions, continuing process improvement (CPI) leadership is accelerating efforts to streamline and improve Army processes, infrastructure and organization. The desired end state is an Army generating force that: (1) strives to eliminate all process activity that does not directly lead to enabling operational capability and adaptability, (2) possesses a multi-disciplinary capability and institutionalizes various levels of this capability in Army training and schools, (3) employs technology as applicable to streamline the Army generating processes, and (4) continues to improve the adaptability of generating processes through organizational redesign, innovation, and integration. To that end, the Army is revitalizing its CPI strategy and approach to assure that the best methods and tools are applied to the complex challenges the Army faces by focusing on the effective integration of the CPI capabilities that exist in our Army without additional programs or resources.

In FY 2016 the Army completed over 1,000 projects with over \$1.3 billion in estimated financial benefits-conferred (savings and cost avoidance). Since 2006 when the CPI effort was initiated by the Secretary and Chief of Staff of the Army, it has averaged annual savings of \$1 billion. That is new saving on average every year. In FY 2016, CPI efforts produced \$16 million in savings by reducing equipment inventory days-of-supply; \$24 million in cost avoidance by comparing two courses of action for managing product lifecycle, and leveraging efficiencies of Value Engineering. In addition to the fiscal savings, these efforts improved logistics throughput, program management, better buying practices, headquarters restructuring, and other functions that enhanced the effectiveness and efficiency of Army operations. This capability introduces real efficiencies for our Soldiers, their Families, and our Civilians. Processes reduced in length, with lines cut short. These make a difference in people's lives every single day.

The Army is developing its innovation strategy that aligns innovation efforts, through a distributed community of practice, with its strategic direction. The strategy will serve as an embedding mechanism to advance a culture of innovation and entrepreneurship across the enterprise.

The Army recently piloted the Army Ideas for Innovation program. The program is designed to solicit ideas to streamline business processes resulting in cost-savings Army-wide. These innovative ideas are designed to contribute to safety and security, provide technological solutions to today's and tomorrow's problems, offer competitive advantage on the battlefield, improve morale and quality of life, improve effectiveness and efficiency of operations, and save money or time.

Business Process Reengineering (BPR) Center of Excellence (COE): This is an Office of Business Transformation (OBT) initiative with AMC's Communications and Electronics Command. Once the COE is established and staffed it will become a self-sustaining activity. The Army will see total cost saving by the capability provided and by eliminating other organizations from having to stand up their own BPR cells to meet statutory requirements. The first pilot project underway: Enterprise Governance, Risk, Compliance for automated access controls and permissions. Success on this project will eliminate a significant audit finding.

The OBT and Assistant Secretary of the Army (Financial Management and Comptroller) spearheaded the Every Dollar Counts initiative; an effort to foster an Army culture that practices good stewardship, values accountability of resources, and reflects a spirit of innovation. The Every Dollar Counts goal is to ensure every leader across the Army, from the lowest to the highest levels, understands the costs to achieve an outcome and uses that knowledge to assess risks, make resource-informed decisions, and develop innovative solutions to increase efficiency and effectiveness. Cultural change takes time. The first step of the initiative was the Secretary of the Army's *Directive 2016-16 (Changing Management Behavior: Every Dollar Counts)*, published on April 15, 2016. This directive presents the vision for what the Army needs to do to change its cost management culture.

The Army's portfolio management of Army business systems, its compliance orientation in support of DoD business system certification requirements, and its continued emphasis upon the ERP system federation generated many successes in FY 2016.

Based on the plan developed last year to reduce the number of businesses in its portfolio by more than one-third over the FYDP, the Army exceeded system reduction targets two-fold, and expanded oversight into business systems residing within the warfighter and Enterprise Information Mission areas. The Army closed numerous long standing audit findings with the publication of the Army Business Strategy (ABS) in June 2016, along with continued progress in development and use of the Army business enterprise architecture, structured annual business portfolio reviews, and business system certification processes. The goals and objectives of the ABS will focus business leaders on process improvement, performance assessment, training, education and IT portfolio management resulting in improved leadership and fact-based decision making that enables cost savings and alignment of resources with Army priorities. To complement the ABS, the Army developed an ERP strategy. The purpose of the strategy is to create a governance model and road map for an integrated ERP landscape that supports the ABS through effective management of Army ERP investments, improved data and information availability for decision making, better data management, and improved business process performance.

Finally, the Army continued to focus its efforts on the evolution of its four core ERP systems throughout FY 2016. This focus enabled the Army to reduce program risks associated with these complex ERPs and their associated business processes.

The Army formed an Overarching Integrated Project Team to review its ERPs and provide recommendations on achieving long-term affordability and sustainment of current and future Defense Business Systems. The effort was focused on requirements definition, ERP sustainment, and return on investment including the reinvestment of efficiencies.

Having compliant, auditable systems with integrated and automated controls is critical to sustaining Army business processes and mitigating financial risks. The Army, with the support of the OSD and agencies across DoD, underwent a robust schedule of audits

and tests of its business IT systems through FY 2013. These audits assessed financial transactions, the existence and completeness of assets, internal controls, and other critical functions required to meet audit readiness goals. The Army asserted readiness for the audit of the Schedule of Budgetary Activity for FY 2015, and the Army is on track to achieve audit-readiness by FY 2017.

The General Fund Enterprise Business System (GFEBS) is the Army's integrated financial management system for funds distribution, execution, and reporting, as well as real property management and maintenance. The GFEBS was implemented across the Army, i.e., the Active Army, ARNG and USAR, and, within the CONUS and with the deployed Army world-wide. Since the Army's full deployment in 2012, there have been 36,000 active end users in over 200 locations and 71 countries. The use of GFEBS enabled the Army to retire over 48 separate systems to date and has plans for an additional anticipated 64 systems by FY 2021.

While GFEBS involved implementing a new system, changes in business processes and the integration of data, it also improved standardization and common business processes across the Army. The GFEBS has achieved a total 97 percent compliance rate with Federal Financial Management Improvement Act of 1996 (FFMIA), Business Enterprise Architecture, Standard Financial Information Structure, Federal Information System Controls Audit Manual, and other statutory and regulatory requirements, standards, attributes, and business rules. In FY 2016, the Army:

- ❑ Obligated \$157 billion in GFEBS – an increase of \$22 billion over FY 2015.
- ❑ Processed payroll of over 236,000 Civilian employees bi-weekly.
- ❑ Processed over 70 million transactions.

Additionally, GFEBS operates collaboratively with the Global Combat Support System–Army (GCSS-Army), the Army's logistics related financial ERP system. While these are two separate ERP systems, they are fully integrated with GCSS-Army utilizing a financial execution module from GFEBS. Both GCSS-Army and GFEBS provide improved readiness,

accountability, and financial auditability by integrating key capabilities such as centralized funds distribution and retraction, consolidated status of funds and trial balance reporting, centralized reimbursable execution, and comprehensive managerial cost accounting and reporting.

The Army is continuing to build additional GFEBS capabilities by providing core ERP Central Component enhancements and Business Intelligence Architecture/Infrastructure upgrades. Also, GFEBS direct disbursing solution which the Department of Treasury continues to expand, supported a total of 68 percent of GFEBS-entitled CONUS invoices in August 2016. The disbursing solution enables the Army to maintain zero difference between GFEBS accounting and Fund Balance with Treasury, integrated payment offsets for unsettled debts, and accelerated vendor payments.

For the first time ever, the Army will have complete visibility of the total force in one Human Resource System—over 1.1 million Soldiers for Active, ARNG, and Reserves within the Integrated Personnel and Pay System – Army (IPPS-A). The IPPS-A will move from an Industrial Age personnel system to a 21st century talent management system, that provides an audit capability for pay and benefits to ensure the best use of Army dollars to employ human capital, while providing continuous reconciliation with GFEBS. The IPPS-A standardized business processes from over 157 to 34; eliminating over 30 Legacy systems, and over 100 interfaces that create errors, data inaccuracies, and inefficiencies.



National Guard Soldiers clear a road blocked by a fallen tree.
(Photo by Cotton Puryear, Virginia National Guard Public Affairs)

CONCLUSION

Continued investment in readiness allows the Army to meet current demands, respond to unforeseeable threats, and decisively defeat our enemies on land. To enforce our Nation's will and win in combat, the Army prepares leaders to take the best-

trained and equipped Soldiers to war. The cost of unpreparedness in war is the lives of our Soldiers. Predictable funding allows the Army to provide the means to equip and train the Army that wins while reducing the risk of loss of life.

MANAGEMENT ASSURANCES

Commanders and managers throughout the Department of the Army annually ensure the integrity of their reporting systems, programs, and operations. This section focuses on the Army's system of internal controls to comply with such laws as the FFMIA of 1996 and the Federal Financial Manager's Financial Integrity Act of 1982 (FMFIA). The requirements promote the production of reliable, timely, and accurate financial information through efficient and effective internal controls. By having effective internal controls, the Army is able to improve efficiency, operating effectiveness and enhance public confidence in Army stewardship of public resources.

CHIEF FINANCIAL OFFICER COMPLIANCE

The passage of the CFO Act of 1990 required major federal agencies to prepare audited financial statements for the first time. In 1994, the Government Management Reform Act (GMRA) extended the CFO Act to include agency-wide reports from all major executive branch agencies and their components. The Government Performance and Results Act (GPRA) of 1993 required agencies to systematically report on plans and performance. The FFMIA of 1996, along with the Clinger-Cohen Act of 1996 (also known as the Information Technology Management Reform Act), required that agencies install integrated systems that comply with federal accounting standards and produce auditable financial statements in accordance with Office of Management and Budget (OMB) Circular A-136, Financial Reporting Requirements. Additionally, agencies must follow generally accepted accounting principles formulated by the Federal Accounting Standards Advisory Board (FASAB).

INTERNAL CONTROLS

The Army operates a robust Manager's Internal Control Program in compliance with OMB Circular

A-123 to employ a comprehensive system of continuous evaluation of internal controls. The Army's program is fully integrated with functional program control assessments. In strict adherence to the Office of the Under Secretary of Defense (Comptroller) guidance, the Army reports a level of assurance over its internal controls in three distinct areas: Internal Controls over Non-Financial Operations (ICONO), Internal Controls over Financial Reporting (ICOFR), and Internal Controls over Financial Systems (ICOFS). See the complete Army Annual Statement of Assurance at <http://asafm.army.mil/offices/FO/IntControl.aspx?OfficeCode=1500>

ICOFR AND ICOFS

As stated in the Army's Annual Statement of Assurance dated September 1, 2016, the Army conducted its assessment of the effectiveness of internal controls over financial reporting in accordance with OMB Circular A-123, Appendix A, *Internal Control over Financial Reporting*. Based on the results of this assessment, the Army is able to provide a qualified statement of reasonable assurance that the internal controls over financial reporting as of June 30, 2016, were operating effectively, with the exception of 28 material weaknesses. The Fiscal Year 2015 Schedule of Budgetary Activity audit has identified eight new ICOFR material weaknesses. In order to address the findings associated with the weaknesses, the Army is implementing the necessary corrective actions across the organization. The Army continues to show progress in strengthening the internal control environment through leadership involvement and audit readiness training efforts.

In addition to the 28 ICOFR material weaknesses, there are two ICOFS material weaknesses for a total of 30 material weaknesses.

ANALYSIS OF FINANCIAL STATEMENTS

As discussed in the accompanying independent auditor's reports, long-standing financial management challenges prevent the Army from producing auditable financial statements for the Army General Fund and the Army Working Capital Fund. The Army, however, continues to work with the DoD to develop sustainable business practices and enhanced internal controls to improve financial management processes and produce quality financial management information. These processes must be supported by compliant business systems and an effective set of management controls.

ARMY GENERAL FUND FINANCIAL RESULTS AND BALANCE SHEET

The Army General Fund Balance Sheet includes total assets of \$290.9 billion. Two asset categories, Fund Balance with Treasury and General Property, Plant and Equipment (PP&E), comprise 88 percent of total assets, with values of \$106.1 billion and \$150.2 billion, respectively.

Liabilities primarily consist of \$26.2 billion in Environmental Liabilities, \$10.5 billion in Other Liabilities and \$2.9 billion in Accounts Payable.

FIGURE 3. Composition of Army General Fund Assets and Liabilities

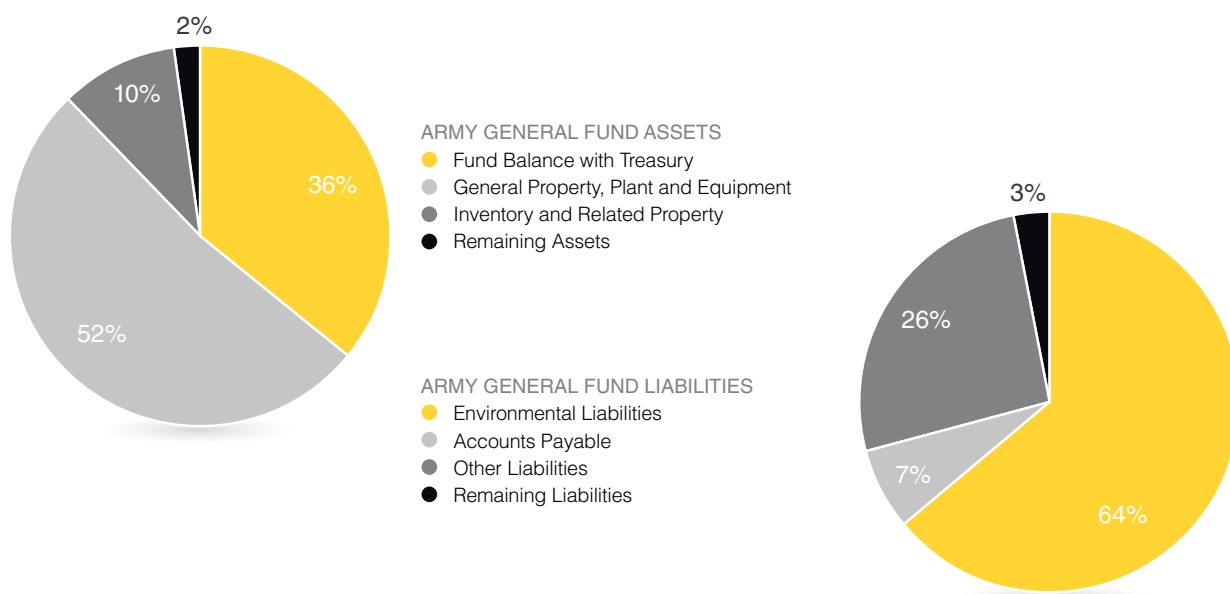


TABLE 11. Select Army General Fund Assets and Liabilities

(Amounts in billions)

| Asset Type | FY 2015 | FY 2016 | Change | Percentage of FY 2016 Assets |
|---------------------------------------|----------------|----------------|--------------|------------------------------|
| Fund Balance with Treasury | \$113.1 | \$106.1 | (\$7.0) | 36% |
| General Property, Plant and Equipment | 133.7 | 150.2 | 16.5 | 52% |
| Inventory and Related Property | 31.3 | 29.7 | (1.6) | 10% |
| Remaining Assets | 4.5 | 4.9 | 0.4 | 2% |
| Total Assets | \$282.6 | \$290.9 | \$8.3 | 100% |

| Liability Type | FY 2015 | FY 2016 | Change | Percentage of FY 2016 Liabilities |
|---------------------------|---------------|---------------|----------------|-----------------------------------|
| Environmental Liabilities | \$27.5 | \$26.2 | (\$1.3) | 64% |
| Accounts Payable | 2.3 | 2.9 | 0.6 | 7% |
| Other Liabilities | 11.7 | 10.5 | (1.2) | 26% |
| Remaining Liabilities | 1.2 | 1.2 | 0 | 3% |
| Total Liabilities | \$42.7 | \$40.8 | (\$1.9) | 100% |

ARMY WORKING CAPITAL FUND FINANCIAL RESULTS

The Army Working Capital Fund activities maintain the Army's combat readiness by providing supplies, equipment, and ordnance to prepare, sustain, and reset our forces in the most efficient and cost-effective manner possible. In performing this mission, Working Capital Fund activities are obligated to control and minimize costs. Financial performance is measured through cash management, net operating results (NOR), and accumulated operating results (AOR). Operational performance is measured by carryover, stock availability, and production.

CASH MANAGEMENT

The current balance of funds with the U.S. Treasury equals the beginning of the fiscal year amount plus the cumulative fiscal-year-to-date amounts of collections, appropriations and transfers-in, minus the cumulative fiscal year-to-date amounts of disbursements, withdrawals and transfers-out. The Army Working Capital Fund is required to maintain a positive cash balance to prevent an Anti-deficiency Act (ADA) violation under 31 USC, § 1517(a), Prohibited Obligations and Expenditures. Unlike appropriated funds, the Army Working Capital Fund cash balance is not equal to outstanding obligations; however, the cash-on-hand at Treasury must be sufficient to pay bills when due.

Sufficient cash levels should be maintained to support operational disbursements, plus adequate cash to meet six months of capital investment program disbursements, plus the amount of any positive accumulated operating results that is to be returned to customers. In concert with a newly developed process, the cash requirement is developed based on four primary elements: 1) the rate of disbursements, 2) the range of operations, 3) risk mitigation, and 4) cash reserves.

The cash balance is primarily affected by cash generated from operations; however, the balance is also affected by appropriations, transfers, and withdrawals. Maintaining a proper cash balance depends on setting rates to recover full costs—including prior year losses—accurately projecting workload and meeting established operational goals. The Army Working Capital Fund ended FY 2016 with a cash balance of \$1,321.2 million within the upper and lower operating range for the year.



Providing security at a training center. (U.S. Army photo by Pfc. Jasmine Ballard)

Table 12 shows an overall growth in cash primarily from operations and direct appropriations offset by transfers out. The Army Working Capital Fund received direct appropriations for war reserve materiel and arsenals initiative.

TABLE 12. Army Working Capital Fund Cash

| (Amounts in millions) | FY 2014 | FY 2015 | FY 2016 |
|-----------------------------------|------------------|------------------|------------------|
| Beginning Cash | \$1,399.9 | \$1,835.2 | \$1,810.4 |
| Collections | 8,542.1 | 8,132.0 | 13,417.8 |
| Disbursements | 8,185.7 | 7,840.9 | 13,214.4 |
| Net Disbursements and Collections | 356.4 | 291.1 | 203.4 |
| Appropriations Received | 219.9 | 238.7 | 195.4 |
| Transfers In | 0 | 0 | 0 |
| Transfers Out | 141.0 | 554.6 | 888.0 |
| Net Cash Transactions | 435.3 | (24.8) | (489.2) |
| Ending Cash Balance | \$1,835.2 | \$1,810.4 | \$1,321.2 |

NET OPERATING RESULTS AND ACCUMULATED OPERATING RESULTS

The NOR represents the difference between revenues and costs within a fiscal year. The AOR represents the aggregate of all recoverable and non-recoverable net earnings, including prior-year adjustments, since inception of the Army Working Capital Fund. The goal of the Army Working Capital Fund is to establish rates that will bring the AOR to zero in the budget year. An activity group's financial performance is measured by comparing actual results to the budget's NOR and AOR.

TABLE 13. Net and Accumulated Operating Results by Activity Group

| (Amounts in millions) | FY 2014 | FY 2015 | FY 2016 |
|----------------------------|---------|----------|---------|
| Industrial Operations NOR | \$100.4 | (\$47.5) | \$14.5 |
| Industrial Operations AOR* | 432.3 | 384.8 | 399.2 |
| Supply Management NOR* | (176.9) | (12.9) | (334.4) |
| Non-Recoverable AOR | 487.8 | 0 | 0 |
| Supply Management AOR* | 157.8 | 144.9 | (189.5) |

*Includes prior-period AOR and NOR adjustments.

CARRYOVER

Carryover is the dollar amount of orders accepted from customers that have not been completed by fiscal year-end. It is a normal part of doing business. These orders enable the industrial workforce to maintain continuity in production operations. The Army expects the carryover for FY 2016 to be less than the maximum allowable amount. The figures shown in Table 14 for FY 2016 are estimates.

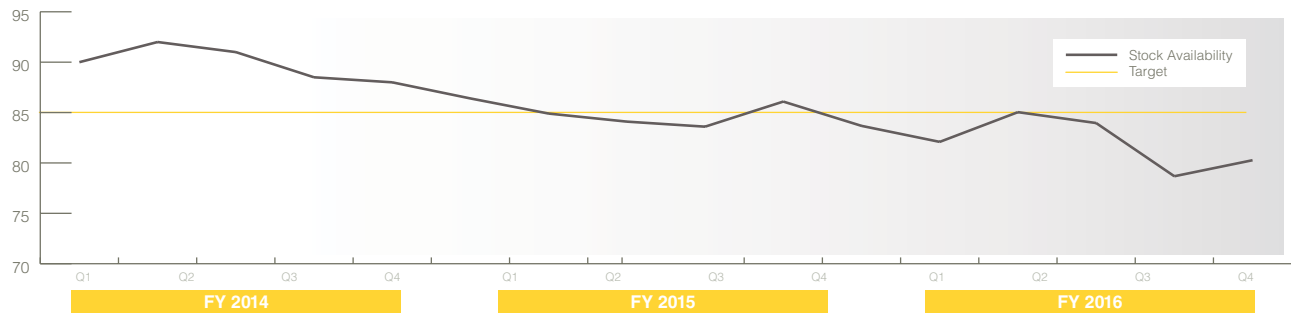
TABLE 14. Army Working Capital Fund Carryover

| (Amounts in millions) | FY 2014 | FY 2015 | FY 2016 |
|-----------------------|-----------|-----------|-----------|
| New Orders* | \$4,396.3 | \$4,473.8 | \$4,089.7 |
| Allowable Carryover | 3,379.3 | 3,084.3 | 2,454.1** |
| Calculated Carryover | 4,444.5 | 4,022.7 | 3,492.4** |

*Includes prior year adjustments **Preliminary

STOCK AVAILABILITY

Stock availability measures the percentage of requisitions filled within established timeframes. The DoD and Army have set a target average 85 percent first pass stock availability. For FY 2015, the average stock availability was below the 85 percent target at 84 percent. For FY 2016, the average stock availability was below the 85 percent target at 82 percent.

FIGURE 4. Stock Availability (percentage)

PRODUCTION

Although the Industrial Operations Activity Group is comprised of 13 Government Owned Government Operated activities, the preponderance of workload is performed at the five hard-iron maintenance depots. As a result of the higher operating tempo, rough desert environments, and limited depot maintenance available in theater, operational fleets age at a far greater pace than expected. To counter this, the Army established a reset program designed to reverse the effects of combat stress on equipment and to prepare equipment for future missions.

The Army's depots and their efforts to partner with industry are critical to the entire reset effort. These repair programs must continue through the end of the current conflict and for at least three additional years to reconstitute equipment completely. Due to Sequestration which caused a reduction in personnel and funding, the Industrial Operations Activity Group depot production was negatively impacted, as illustrated in Table 15.



Dragging a parachute toward a target during a training event.
(Photo by Sgt. Brady Pritchett)

The decrease in Bradleys and Helicopter Engines shown in the FY 2016 column of Table 15 is due to a decrease in requirements for the respective programs. The increase in Track Shoes is due to an increase in usage and subsequent repair requirements.

TABLE 15. Annual Production Throughput¹

| | Pre-War | FY 2014 | FY 2015 | FY 2016 |
|--------------------|---------|---------|---------|---------|
| Aircraft | 4 | 72 | 69 | 43 |
| Helicopter Engines | <200 | 631 | 534 | 329 |
| Bradleys | 144 | 306 | 102 | 40 |
| HMMWVs | <100 | 5,637 | 1,108 | 2,650 |
| Firefinder Radars | <1 | 4 | 18 | 4 |
| Track Shoes | 120,000 | 23,151 | 40,524 | 86,600 |

Note 1: Throughput is the number of weapon systems completed for any given year.

ARMY WORKING CAPITAL FUND BALANCE SHEET

The Army Working Capital Fund balance sheet shows assets of \$21.4 billion, primarily in Inventory, PP&E and Fund Balance with Treasury. Liabilities consist of Accounts Payable and Other Liabilities, which include payroll, benefits, accrued annual leave, and workers' compensation

FIGURE 5. Army Working Capital Fund Assets and Liabilities

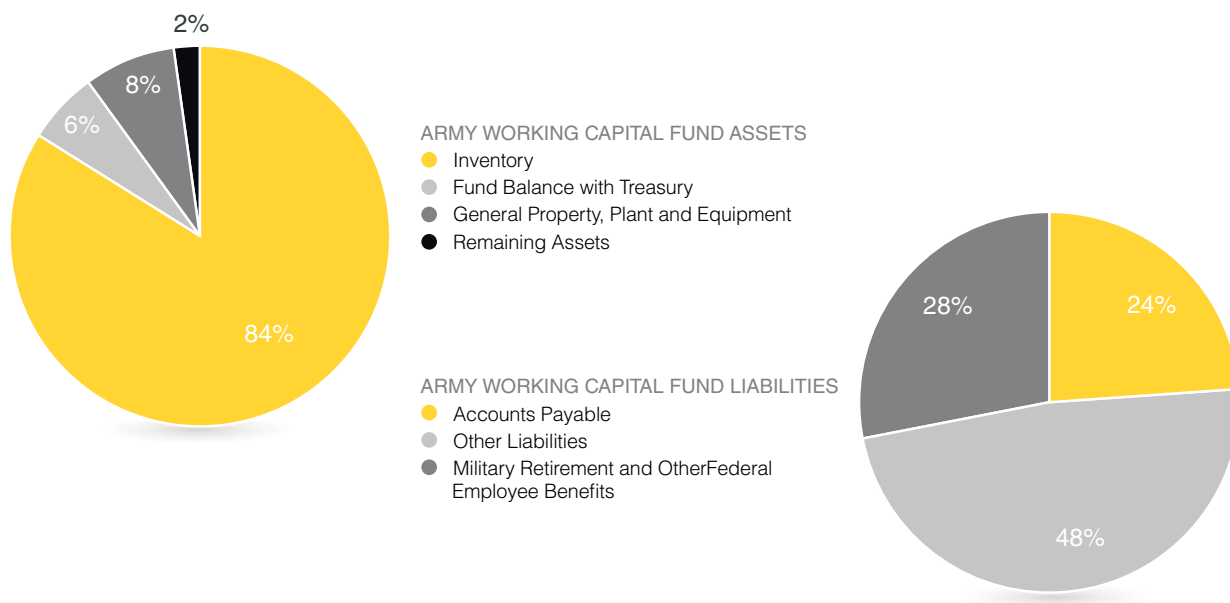


TABLE 16. Army Working Capital Fund Assets and Liabilities

(Amounts in millions)

| Asset Type | FY 2015 | FY 2016 | Change | Percentage of FY 2016 Assets |
|---------------------------------------|-------------------|-------------------|--------------------|------------------------------|
| Inventory | \$19,484.1 | \$17,948.4 | (\$1,535.7) | 84% |
| Fund Balance with Treasury | 1,810.4 | 1,321.2 | (489.2) | 6% |
| General Property, Plant and Equipment | 1,738.7 | 1,715.1 | (23.6) | 8% |
| Remaining Assets | 458.8 | 436.1 | (22.7) | 2% |
| Total Assets | \$23,492.0 | \$21,420.8 | (\$2,071.2) | 100% |

| Liability Type | FY 2015 | FY 2016 | Change | Percentage of FY 2016 Liabilities |
|---|------------------|----------------|------------------|-----------------------------------|
| Accounts Payable | \$277.3 | \$219.2 | (\$58.1) | 24% |
| Other Liabilities | 478.3 | 435.0 | (43.3) | 48% |
| Military Retirement and Other Federal Employee Benefits | 265.4 | 256.7 | (8.7) | 28% |
| Total Liabilities | \$1,021.0 | \$910.9 | (\$110.1) | 100% |

Amounts may not sum due to rounding.

REQUIRED SUPPLEMENTARY STEWARDSHIP INFORMATION AND REQUIRED SUPPLEMENTARY INFORMATION

Stewardship information relates to expenditures involving a substantial investment by the Army for the benefit of the nation. When made, these expenditures are treated as expenses in the financial statements. Since these expenses are intended to provide long-term benefits to the public, they are reported as supplemental information in the financial statements.¹ There are four reported areas for stewardship information: (1) nonfederal physical property; (2) investments in research and development (R&D); (3) deferred maintenance; and (4) heritage assets and stewardship land.

Investment in nonfederal physical property is an expense incurred by the Army for the purchase, construction, or major renovation of physical property owned by state and local governments. An example of this type of investment is funding provided to the ARNG for assistance in the construction of an ARNG facility on state land. Since the facility is constructed on state land, it is the property of the state; therefore, the Army cannot report it as an asset. However, since the funds were used to acquire a mission-related state facility, the outlay is tracked as an investment in nonfederal physical property.

Investments in R&D are based on R&D outlays (expenditures). Outlays are used because current Army accounting systems are unable to capture and summarize costs in accordance with federal accounting standards. The R&D programs are classified as basic research, applied research, and development.

Stewardship information is also comprised of real property and military equipment deferred maintenance. Real property deferred maintenance relates to maintenance needed on Army facilities that has not been funded. At the end of FY 2016, the Army reported approximately \$ 60.4 billion in deferred real property maintenance on facilities with a replacement value of approximately \$374.2 billion. Real property deferred maintenance totals approximately 16 percent of estimated replacement value of the facilities requiring maintenance. The 10 major categories of military equipment deferred maintenance totaled approximately \$917.8 million at the end of FY 2016. Automotive Equipment represented the largest identifiable category of deferred equipment maintenance at approximately \$344.2 million.

Heritage assets are comprised of PP&E of historical, natural, cultural, educational, or artistic significance. Stewardship land is land other than that acquired for, or in connection with, general PP&E. The Army's heritage assets are comprised of buildings and structures, archeological sites, museums, and museum collection items.

Detailed information concerning most stewardship information may be found in the Required Supplementary Stewardship Information (RSSI) and the Required Supplementary Information (RSI) sections of this report. Heritage assets and stewardship land are no longer reported in the RSI; they are now required to be reported in a note to the statements.² Additional information on heritage assets and stewardship land may be found in Note 10 of the Army General Fund statements.

¹ Federal Accounting Standards Advisory Board. Statement of Federal Financial Accounting Concepts and Standards (June 30, 2010). Statement of Federal Financial Accounting Standards 8: Supplementary Stewardship Reporting, page 762. See http://www.fasab.gov/pdf/files/codification_report2010.pdf.

² *ibid.* Statement of Federal Financial Accounting Standards 29: Heritage Assets and Stewardship Land, pages 9 and 13 and Technical Release 9: Implementation Guide for Statement of Federal Financial Accounting Standards 29: Heritage Assets and Stewardship Land, page 4. SFFAS 29 found at http://www.fasab.gov/pdf/files/sffas_29.pdf on October 23, 2011. Technical Release 9 can be found at http://www.fasab.gov/pdf/files/handbook_tr_9.pdf



LIMITATIONS OF THE FINANCIAL STATEMENTS

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

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

The statements should be read with the realization that they are for a component of the United States Government, a sovereign entity.

A large, faded background image of a soldier in silhouette, wearing a helmet and carrying a rifle, positioned in a desert environment. The soldier is looking towards the right, where a very bright light source creates a series of radiating lines across the sky and ground.

(Photo by Justin Connaher)

CONSOLIDATED BALANCE SHEET

As of September 30, 2016 and 2015

(Amounts in thousands)

| | 2016 Consolidated | 2015 Consolidated |
|---|-----------------------|-----------------------|
| ASSETS (Note 2) | | |
| Intragovernmental: | | |
| Fund Balance with Treasury (Note 3) | \$ 106,100,483 | \$ 113,051,240 |
| Investments (Note 4) | 2,257 | 2,177 |
| Accounts Receivable (Note 5) | 497,337 | 228,611 |
| Other Assets (Note 6) | 391,690 | 228,888 |
| Total Intragovernmental Assets | \$ 106,991,767 | \$ 113,510,916 |
| Cash and Other Monetary Assets (Note 7) | 908,582 | 862,976 |
| Accounts Receivable, Net (Note 5) | 484,464 | 467,944 |
| Inventory and Related Property, Net (Note 9) | 29,711,383 | 31,333,626 |
| General Property, Plant and Equipment, Net (Note 10) | 150,240,322 | 133,748,058 |
| Other Assets (Note 6) | 2,611,907 | 2,704,180 |
| TOTAL ASSETS | \$ 290,948,425 | \$ 282,627,700 |
| STEWARDSHIP PROPERTY, PLANT & EQUIPMENT (Note 10) | | |
| LIABILITIES (Note 11) | | |
| Intragovernmental: | | |
| Accounts Payable (Note 12) | \$ 1,619,144 | \$ 1,744,839 |
| Other Liabilities (Note 15 & 16) | 2,202,341 | 2,255,167 |
| Total Intragovernmental Liabilities | \$ 3,821,485 | \$ 4,000,006 |
| Accounts Payable (Note 12) | 1,309,432 | 516,915 |
| Military Retirement and Other Federal Employment Benefits (Note 17) | 1,238,941 | 1,239,177 |
| Environmental and Disposal Liabilities (Note 14) | 26,224,781 | 27,508,693 |
| Other Liabilities (Note 15 and Note 16) | 8,160,871 | 9,445,368 |
| TOTAL LIABILITIES | \$ 40,755,510 | \$ 42,710,159 |
| COMMITMENTS AND CONTINGENCIES (NOTE 16) | | |
| NET POSITION | | |
| Unexpended Appropriations - Other Funds | \$ 99,761,180 | \$ 105,905,462 |
| Cumulative Results of Operations - Dedicated | 67,093 | 55,780 |
| Cumulative Results of Operations - Other Funds | 150,364,642 | 133,956,299 |
| TOTAL NET POSITION | \$ 250,192,915 | \$ 239,917,541 |
| TOTAL LIABILITIES AND NET POSITION | \$ 290,948,425 | \$ 282,627,700 |

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

Department of Defense – Department of the Army

CONSOLIDATED STATEMENT OF NET COST

For the Years Ended September 30, 2016 and 2015

(Amounts in thousands)

| | 2016 Consolidated | 2015 Consolidated |
|--|-----------------------|-----------------------|
| Program Costs | | |
| Gross Costs | \$ 157,066,507 | \$ 158,314,042 |
| Military Personnel | 57,556,338 | 58,639,011 |
| Operations, Readiness & Support | 62,310,466 | 56,681,723 |
| Procurement | 17,474,069 | 15,261,999 |
| Research, Development, Test & Evaluation | 11,442,581 | 10,880,461 |
| Family Housing & Military Construction | 8,283,053 | 16,850,848 |
| (Less: Earned Revenue) | \$ (7,828,542) | \$ (6,845,700) |
| Net Cost before Losses/(Gains) from Actuarial Assumption Changes for Military Retirement Benefits | \$ 149,237,965 | \$ 151,468,342 |
| Net Program Costs Including Assumption Changes | \$ 149,237,965 | \$ 151,468,342 |
| Net Cost of Operations (Note 18) | <u>\$ 149,237,965</u> | <u>\$ 151,468,342</u> |

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

CONSOLIDATED CHANGES IN NET POSITION-DEDICATED COLLECTIONS

For the Years Ended September 30, 2016 and 2015

(Amounts in thousands)

| | 2016 Dedicated Collections | 2016 All Other Funds | 2016 Eliminations | 2016 Consolidated |
|--|----------------------------|----------------------|-------------------|-------------------|
| CUMULATIVE RESULTS OF OPERATIONS | | | | |
| Beginning Balances | \$ 55,779 | \$ 133,956,300 | \$ 0 | \$ 134,012,079 |
| Beginning balances, as adjusted | \$ 55,779 | \$ 133,956,300 | \$ 0 | \$ 134,012,079 |
| Budgetary Financing Sources: | | | | |
| Appropriations used | | 146,471,967 | 0 | 146,471,967 |
| Nonexchange revenue | 2,782 | (754) | 0 | 2,028 |
| Donations and forfeitures of cash and cash equivalents | 28,721 | 165,172 | 0 | 193,893 |
| Transfers-in/out without reimbursement | | 2,255,435 | 0 | 2,255,435 |
| Other budgetary financing sources | | (5,670,751) | 0 | (5,670,751) |
| Other Financing Sources: | | | | |
| Donations and forfeitures of property | | | 0 | |
| Transfers-in/out without reimbursement (+/-) | | 2,138,368 | 0 | 2,138,368 |
| Imputed financing from costs absorbed by others | | 940,948 | 0 | 940,948 |
| Other (+/-) | (10,023) | 19,335,755 | 0 | 19,325,732 |
| Total Financing Sources | \$ 21,480 | \$ 165,636,140 | \$ 0 | \$ 165,657,620 |
| Net Cost of Operations (+/-) | 10,166 | 149,227,799 | 0 | 149,237,965 |
| Net Change | \$ 11,314 | \$ 16,408,341 | \$ 0 | \$ 16,419,655 |
| Cumulative Results of Operations | \$ 67,093 | \$ 150,364,642 | \$ 0 | \$ 150,431,735 |
| UNEXPENDED APPROPRIATIONS | | | | |
| Beginning Balances | \$ 0 | \$ 105,905,462 | \$ 0 | \$ 105,905,462 |
| Budgetary Financing Sources: | | | | |
| Appropriations received | \$ 0 | \$ 147,860,194 | \$ 0 | \$ 147,860,194 |
| Appropriations transferred-in/out | 0 | 1,170,696 | 0 | 1,170,696 |
| Other adjustments (rescissions, etc) | 0 | (8,703,205) | 0 | (8,703,205) |
| Appropriations used | 0 | (146,471,967) | 0 | (146,471,967) |
| Total Budgetary Financing Sources | \$ 0 | \$ 6,144,282 | \$ 0 | \$ 6,144,282 |
| Total Unexpended Appropriations | 0 | 99,761,180 | 0 | 99,761,180 |
| Net Position | \$ 67,093 | \$ 250,125,822 | \$ 0 | \$ 250,192,915 |

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

Department of Defense – Department of the Army

CONSOLIDATED CHANGES IN NET POSITION-DEDICATED COLLECTIONS

For the Years Ended September 30, 2016 and 2015

(Amounts in thousands)

| | 2015 Dedicated Collections | 2015 All Other Funds | 2015 Eliminations | 2015 Consolidated |
|--|----------------------------|----------------------|-------------------|-------------------|
| CUMULATIVE RESULTS OF OPERATIONS | | | | |
| Beginning Balances | \$ 37,731 | \$ 136,371,919 | \$ 0 | \$ 136,409,650 |
| Beginning balances, as adjusted | \$ 37,731 | \$ 136,371,919 | \$ 0 | \$ 136,409,650 |
| Budgetary Financing Sources: | | | | |
| Appropriations used | 0 | 155,031,142 | 0 | 155,031,142 |
| Nonexchange revenue | 1,571 | 3,521 | 0 | 5,092 |
| Donations and forfeitures of cash and cash equivalents | 25,377 | 152,564 | 0 | 177,941 |
| Transfers-in/out without reimbursement | 0 | 828,344 | 0 | 828,344 |
| Other budgetary financing sources | 0 | (1,755,633) | 0 | (1,755,633) |
| Other Financing Sources: | | | | |
| Donations and forfeitures of property | 0 | 76 | 0 | 76 |
| Transfers-in/out without reimbursement (+/-) | 0 | 2,226,377 | 0 | 2,226,377 |
| Imputed financing from costs absorbed by others | 0 | 991,361 | 0 | 991,361 |
| Other (+/-) | 2,207 | (8,436,136) | 0 | (8,433,929) |
| Total Financing Sources | \$ 29,155 | \$ 149,041,616 | \$ 0 | \$ 149,070,771 |
| Net Cost of Operations (+/-) | 11,106 | 151,457,236 | 0 | 151,468,342 |
| Net Change | \$ 18,049 | \$ (2,415,620) | \$ 0 | \$ (2,397,571) |
| Cumulative Results of Operations | \$ 55,780 | \$ 133,956,299 | \$ 0 | \$ 134,012,079 |
| UNEXPENDED APPROPRIATIONS | | | | |
| Beginning Balances | \$ 0 | \$ 122,656,579 | \$ 0 | \$ 122,656,579 |
| Budgetary Financing Sources: | | | | |
| Appropriations received | \$ 0 | \$ 148,334,705 | \$ 0 | \$ 148,334,705 |
| Appropriations transferred-in/out | 0 | 478,422 | 0 | 478,422 |
| Other adjustments (rescissions, etc) | 0 | (10,533,102) | 0 | (10,533,102) |
| Appropriations used | 0 | (155,031,142) | 0 | (155,031,142) |
| Total Budgetary Financing Sources | \$ 0 | \$ (16,751,117) | \$ 0 | \$ (16,751,117) |
| Total Unexpended Appropriations | 0 | 105,905,462 | 0 | 105,905,462 |
| Net Position | \$ 55,780 | \$ 239,861,761 | \$ 0 | \$ 239,917,541 |

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

COMBINED STATEMENT OF BUDGETARY RESOURCES

For the Years Ended September 30, 2016 and 2015

(Amounts in thousands)

| | 2016 Combined | 2015 Combined |
|--|-----------------------|-----------------------|
| Budgetary Resources: | | |
| Unobligated balance brought forward, Oct 1 | \$ 35,230,814 | \$ 42,912,597 |
| Adjustment to unobligated balance, brought forward, Oct 1 (+ or -) | | |
| Unobligated balance brought forward, Oct 1, as adjusted, | \$ 35,230,814 | \$ 42,912,597 |
| Recoveries of prior year unpaid obligations | 19,531,882 | 19,843,020 |
| Other changes in unobligated balance (+ or -) | (4,822,374) | (8,014,898) |
| Unobligated balance from prior year budget authority, net | \$ 49,940,322 | \$ 54,740,719 |
| Appropriations (discretionary and mandatory) | 147,453,294 | 147,266,432 |
| Spending Authority from offsetting collections (discretionary and mandatory) | 21,342,475 | 17,448,318 |
| Total Budgetary Resources | \$ 218,736,091 | \$ 219,455,469 |
| Status of Budgetary Resources: | | |
| New obligations and upward adjustments (total) | \$ 185,011,939 | \$ 184,224,655 |
| Unobligated balance, end of year | | |
| Apportioned, unexpired accounts | 16,279,348 | 17,476,932 |
| Exempt from apportionment, unexpired accounts | 33,498 | 34,321 |
| Unapportioned, unexpired accounts | 159,103 | 351,578 |
| Unexpired unobligated balance, end of year | 16,471,949 | 17,862,831 |
| Expired unobligated balance, end of year | 17,252,203 | 17,367,983 |
| Total unobligated balance, end of year | \$ 33,724,152 | \$ 35,230,814 |
| Total Budgetary Resources | \$ 218,736,091 | \$ 219,455,469 |
| Change in Obligated Balance: | | |
| Unpaid obligations: | | |
| Unpaid obligations, brought forward, Oct 1 | \$ 99,818,300 | \$ 111,937,128 |
| New obligations and upward adjustments | 185,011,939 | 184,224,655 |
| Outlays (gross) (-) | (169,713,639) | (176,500,463) |
| Recoveries of prior year unpaid obligations (-) | (19,531,882) | (19,843,020) |
| Unpaid obligations, end of year | 95,584,718 | 99,818,300 |
| Uncollected payments: | | |
| Uncollected pymts, Fed sources, brought forward, Oct 1 (-) | (22,926,443) | (26,393,857) |
| Change in uncollected pymts, Fed sources (+ or -) | (1,435,218) | 3,467,414 |
| Uncollected pymts, Fed sources, end of year (-) | (24,361,661) | (22,926,443) |
| Memorandum Entries: | | |
| Obligated balance, start of year (+ or -) | \$ 76,891,857 | \$ 85,543,271 |
| Obligated balance, end of year (+ or -) | \$ 71,223,057 | \$ 76,891,857 |
| Budget Authority and Outlays, Net: | | |
| Budget authority, gross (discretionary and mandatory) | \$ 168,795,769 | \$ 164,714,750 |
| Actual offsetting collections (discretionary and mandatory) (-) | (19,933,236) | (21,029,321) |
| Change in uncollected customer payments from Federal | | |
| Sources (discretionary and mandatory) (+ or -) | (1,435,218) | 3,467,414 |
| Recoveries of prior year paid obligations (discretionary and mandatory) | 24,420 | 115,150 |
| Budget Authority, net (discretionary and mandatory) | \$ 147,451,735 | \$ 147,267,993 |
| Outlays, gross (discretionary and mandatory) | 169,713,639 | 176,500,463 |
| Actual offsetting collections (discretionary and mandatory) (-) | (19,933,236) | (21,029,321) |
| Outlays, net (discretionary and mandatory) | 149,780,403 | 155,471,142 |
| Distributed offsetting receipts (-) | (362,062) | (930,148) |
| Agency Outlays, net (discretionary and mandatory) | \$ 149,418,341 | \$ 154,540,994 |

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

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES

1.A. Basis of Presentation

These financial statements have been prepared to report the financial position and results of operations of the Army General Fund, as required by the *Chief Financial Officers Act of 1990*, expanded by the *Government Management Reform Act of 1994*, and other appropriate legislation. The financial statements have been prepared from the books and records of the Army General Fund in accordance with, and to the extent possible, U.S. generally accepted accounting principles (U.S. GAAP) promulgated by the Federal Accounting Standards Advisory Board; the Office of Management and Budget (OMB) Circular No. A-136, *Financial Reporting Requirements*; and the *Department of Defense (DoD) Financial Management Regulation*. The accompanying financial statements account for all resources for which the Army General Fund is responsible unless otherwise noted.

Information relative to classified assets, programs, and operations is excluded from the statements or otherwise aggregated and reported in such a manner that it is not discernible.

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

The Army General Fund has implemented process and system improvements addressing these limitations within its Enterprise Resource Planning (ERP) systems, which are improving financial performance, standardizing business processes, ensuring that capability exists to meet future financial management needs, and providing management with relevant, reliable, and timely financial information. The ERP systems allow the sharing of standardized and real-time financial, cost, and accounting data across the Army. The primary ERP systems, General Fund Enterprise Business System (GFEBS) and Global Combat Support System (GCSS) - Army, contain the following six major business process areas: funds management; financials; cost management; reimbursement management; spending chain; and property, plant, and equipment (PP&E).

The Army General Fund currently has 19 auditor-identified financial statement material weaknesses: (1) General Information Technology (IT) Systems Control; (2) Completeness; (3) Evidential Matter – Supporting Documentation; (4) Service Provider Oversight; (5) Accrual Estimation Methodology; (6) Financial Management Improvements; (7) Fund Balance with Treasury; (8) Inventory (Operating Materials and Supplies); (9) General Property, Plant and Equipment; (10) Environmental Liabilities; (11) Intragovernmental Eliminations; (12) Manual General Ledger Adjustments / Accounting Adjustments; (13) Statement of Net Cost; (14) Financial Reporting / Abnormal Account Balances; (15) Accounts Receivable; (16) Accounts Payable; (17) Statement of Budgetary Resources; (18) Reconciliation of Net Cost of Operations to Budget; and (19) Contingency Payment Audit Trails.

1.B. Mission of the Reporting Entity

The Army mission is to support the national security and defense strategies by providing well-trained, well-led, and well-equipped forces to the combatant commanders. This mission encompasses the intent of the Congress, as defined in *Title 10 of the U.S. Code*, to preserve the peace and security and provide for the defense of the U.S., its territories, commonwealths, possessions, and any areas occupied by the U.S.; support national policies; implement national objectives; and overcome any nations responsible for aggressive acts that imperil the peace and security of the U.S.

This mission has been unchanged for the 241-year life of the Army, but the environment and nature of conflict have undergone many changes over that time, especially with overseas contingency operations. These contingency operations have required that the Army simultaneously transform the way that it fights, trains, and equips its soldiers. This transformation is progressing rapidly, but it must be taken to its full conclusion if the Army is to continue to meet the nation's domestic and international security obligations today and into the future.

1.C. Appropriations and Funds

The Army General Fund receives appropriations and funds as general, trust, and special funds. The Army General Fund 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.

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. Certain trust and special funds may be designated as funds from dedicated collections. Funds from dedicated collections are financed by specifically identified revenues; required by statute to be used for designated activities, benefits or purposes; and remain available over time. The Army General Fund is required to account separately for and report on the receipt, use, and retention of revenues and other financing sources for funds from dedicated collections.

Deposit funds are used to record amounts held temporarily until paid to the appropriate government or public entity. They are not funds of the Army General Fund and, as such, are not available for the Army General Fund's operations. The Army General Fund is acting as an agent or a custodian for funds awaiting distribution.

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

The Army General Fund receives allocation transfers from the Federal Highway Administration and the U.S. Forestry Service. The Army General Fund receives allocation transfers for the Security Assistance programs that meet the OMB exception for EOP funds. The activities for these programs are reported separately from the DoD financial statements based on an agreement with OMB.

As a parent, the Army General Fund reports in these financial statements funds allocated to the Department

of Agriculture and the Department of Transportation for the active Army and Army National Guard.

In accordance with *Statement of Federal Financial Accounting Standards (SFFAS) 43: Funds from Dedicated Collections: Amending Statement of Federal Financial Accounting Standards 27, Identifying and Reporting Earmarked Funds*, the Department has elected to display a combined presentation of the non-exchange revenue and other financing sources, including appropriations, and net cost of operations for funds from dedicated collections with all other funds. See Note 19 for additional discussion regarding dedicated collections.

1.D. Basis of Accounting

The Army General Fund financial management systems are unable to meet all full accrual accounting requirements. This is primarily because many of the Army General Fund's financial and nonfinancial systems and processes were designed prior to the legislative mandate to produce financial statements in accordance with U.S. GAAP. The legacy systems were not designed to collect and record financial information on the full accrual accounting basis but were designed to record information on a budgetary basis.

The Army General Fund financial statements and supporting trial balances are compiled from the underlying financial data and trial balances of the Army General Fund sub-entities. The underlying data is largely derived from budgetary transactions (obligations, disbursements, and collections), from nonfinancial feeder systems, and accruals made for major items such as payroll expenses, accounts payable, and environmental liabilities. Some of the sub-entity level trial balances may reflect known abnormal balances resulting largely from business and system processes. At the consolidated Army General Fund level, these abnormal balances may not be evident. Disclosures of abnormal balances are made in the applicable footnotes, but only to the extent that the abnormal balances are evident at the consolidated level.

The DoD is continuing the actions required to bring its financial and nonfinancial feeder systems and processes into compliance with U.S. GAAP. The Army has implemented ERP systems, which contain a chart of accounts based on the United States Standard General Ledger (USSGL). The Army has also created additional subsidiary accounts within the ERP systems to track its General Fund financial activities at a detailed level. However, until all of the Army General Fund's financial and nonfinancial feeder systems and

processes are able to collect and report financial information as required by U.S. GAAP, there will be instances when the Army General Fund's financial data will be derived from budgetary transactions or data from nonfinancial feeder systems.

1.E. Revenues and Other Financing Sources

The Army General Fund receives congressional appropriations as financing sources for general funds, and on occasion, will also receive congressional appropriations for Working Capital Funds (WCF). These funds either expire annually, on a multi-year basis, or do not expire. When authorized by legislation, these appropriations are supplemented by revenues generated by sales of goods or services. The Army General Fund 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 Army General Fund's standard policy for services provided as required by OMB Circular A-25, *User Charges*.

The Army General Fund recognizes revenue when earned within the constraints of its current system capabilities. In some instances, revenue is recognized when bills are issued. The Army General Fund does not include nonmonetary support provided by U.S. allies for common defense and mutual security in amounts reported in the Statement of Net Cost and Note 21, *Reconciliation of Net Cost of Operations to Budget*. The U.S. has cost-sharing agreements with countries having a mutual or reciprocal defense agreement, where U.S. troops are stationed, or where the U.S. Fleet is in a port.

In accordance with SFFAS No. 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*, the Army General Fund records accrued interest from U.S. Treasury securities and user fees transferred from custodial activities in trust and special funds as nonexchange revenue.

1.F. Recognition of Expenses

For financial reporting purposes, DoD policy requires the recognition of operating expenses in the period incurred. Now that GFEBs has been deployed, it will be the source for the Army General Fund to derive a substantial portion of its reported data. Estimates are made for major items such as payroll expenses, accounts payable, environmental liabilities, and unbilled revenue. In the case of operating materiel 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. Under the consumption method, OM&S would be expensed when consumed. Due to system limitations, in some instances expenditures for capital and other long-term assets may be recognized as operating expense. The Army General Fund continues to implement process and system improvements to ERP systems to address these limitations. However, Army continues to rely partially on some current financial and nonfinancial feeder systems that were not designed to collect and record financial information on the full accrual accounting basis.

1.G. Accounting for Intragovernmental Activities

Accounting standards require an entity to eliminate intra-entity activity and balances from consolidated financial statements in order to prevent an overstatement for business with itself. However, the Army General Fund cannot accurately identify intragovernmental transactions by customer because the Army General Fund's systems do not track buyer and seller data at the transaction level. Generally, seller entities within the DoD provide summary seller-side balances for revenue, accounts receivable, and unearned revenue to the buyer-side internal accounting offices. In most cases, the buyer-side records are adjusted to agree with DoD seller-side balances and are then eliminated. The DoD is implementing replacement systems and a standard financial information structure that will incorporate the necessary elements to enable DoD to correctly report, reconcile, and eliminate intragovernmental balances.

The *Treasury Financial Manual, Part 2 – Chapter 4700, Agency Reporting Requirements for the Financial Report of the United States Government*, provides guidance for reporting and reconciling intragovernmental balances. While the Army General Fund is unable to fully reconcile intragovernmental transactions with all federal agencies, the Army General Fund is able to reconcile balances pertaining to investments in federal securities, *Federal Employees' Compensation Act* (FECA) transactions with the Department of Labor, and benefit program transactions with the Office of Personnel Management.

The DoD'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 DoD financial statements do not report any public debt, interest or source of public financing, whether from issuance of debt or tax revenues.

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

Imputed financing represents the cost paid on behalf of the Army General Fund by another Federal entity. The Army General Fund recognizes imputed costs for: (1) employee pension, post-retirement health, and life insurance benefits; (2) post-employment benefits for terminated and inactive employees to include unemployment and workers' compensation under the Federal Employees' Compensation Act; (3) losses in litigation proceedings; and (4) military payroll for service members assigned to the Army General Fund.

1.H. Transactions with Foreign Governments and International Organizations

Each year, the Army General Fund 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*, DoD has authority to sell defense articles and services to foreign countries and international organizations generally at no profit or loss to the federal government. Payment in U.S. dollars is required in advance.

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

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

In addition, DFAS and the USACE Finance Center submit reports to the U.S. Treasury by appropriation on interagency transfers, collections received, and disbursements issued. The U.S. Treasury records these transactions to the applicable Fund Balance with Treasury (FBWT) account. On a monthly basis, the Army General Fund FBWT is reviewed and adjusted, as required, to agree with the U.S. Treasury accounts.

1.J. Cash and Other Monetary Assets

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

The majority of cash and all foreign currency is classified as "nonentity" and is restricted. Amounts reported consist primarily of cash and foreign currency held by disbursing officers to carry out their paying, collecting, and foreign currency accommodation exchange missions.

The Army General Fund conducts a significant portion of operations overseas. The Congress established a special account to handle the gains and losses from foreign currency transactions for five general fund appropriations: (1) operation and maintenance; (2) military personnel; (3) military construction; (4) family housing operation and maintenance; and (5) family housing construction. The gains and losses are calculated as the variance between the exchange rate current at the date of payment and a budget rate established at the beginning of each fiscal year. Foreign currency fluctuations related to other appropriations require adjustments to the original obligation amount at the time of payment. The Army General Fund does not separately identify currency fluctuation transactions.

1.K. Accounts Receivable

Accounts receivable from other federal entities or the public include accounts receivable, claims receivable, and refunds receivable. Generally, allowances for uncollectible accounts due from the public are based upon analysis of collection experience by age category. The DoD does not recognize an allowance for estimated uncollectible amounts from other federal agencies, as receivables from other federal agencies are resolved between the agencies in accordance with the Intragovernmental Business Rules published in the *Treasury Financial Manual*.

1.L. Direct Loans and Loan Guarantees

The Army General Fund operates no direct loan or loan guarantee programs.

1.M. Inventories and Related Property

The Army General Fund manages only military or government-specific materiel under normal conditions.

Materiel is a unique term that relates to military force management and includes items such as ships, tanks, self-propelled weapons, aircraft and related spares, repair parts, and support equipment. Items commonly used in and available from the commercial sector are not managed in Army General Fund materiel management activities. Operational cycles are irregular and the military risks associated with stock-out positions have no commercial parallel. The Army General Fund holds materiel based on military need and support for contingencies.

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

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

The Army General Fund recognizes excess, obsolete, and unserviceable OM&S at a net realizable value of zero pending development of an effective means of valuing such materiel.

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

The Army General Fund reports investments in U.S. Treasury securities at cost, net of amortized premiums or discounts. Premiums or discounts are amortized over the term of the investments using the effective interest rate method or another method obtaining

similar results. The intent of the Army General Fund 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 Army General Fund invests in nonmarketable market-based U.S. Treasury securities, issued to federal agencies by the U.S. Treasury Bureau of Fiscal Service. These securities are not traded on any financial exchange but are priced consistently with publicly traded U.S. Treasury securities.

1.O. General Property, Plant and Equipment

In some instances, the Army General Fund uses the estimated historical cost for valuing equipment. To establish a baseline, the DoD accumulated information relating to program funding and associated equipment, equipment useful life, program acquisitions, and disposals. The equipment baseline is updated using expenditure, acquisition, and disposal information.

The Army's General PP&E capitalization threshold is \$250 thousand. The capitalization threshold applies to asset acquisitions and modifications/improvements placed into service after September 30, 2013. PP&E assets acquired prior to October 1, 2013 were capitalized at prior threshold levels (\$100 thousand for equipment and \$20 thousand for real property) and are carried at the remaining net book value.

General PP&E assets are capitalized at historical acquisition cost when an asset has a useful life of two or more years and when the acquisition cost equals or exceeds the DoD capitalization threshold. The DoD capitalizes improvements to existing General PP&E assets if the improvements equal or exceed the capitalization threshold and extend the useful life or increase the size, efficiency, or capacity of the asset. The DoD depreciates all General PP&E, other than land, on a straight-line basis.

When it is in the best interest of the government, the Army General Fund provides government property to contractors to complete contract work. The Army General Fund 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 meets or exceeds the DoD capitalization threshold, federal accounting standards require that it be reported on the Army General Fund Balance Sheet.

The DoD developed a policy and a reporting process for contractors with government-furnished equipment, which provide appropriate General PP&E information for financial statement reporting. The DoD requires Army General Fund to maintain, in its property systems, information on all property furnished to contractors. These actions are structured to capture and report the information necessary for compliance with federal accounting standards. The Army General Fund has not fully implemented this policy primarily due to system limitations.

1.P. Advances and Prepayments

When advances are permitted by law, legislative action, or presidential authorization, the DoD policy is to record advances and prepayments in accordance with U.S. GAAP. As such, payments made in advance of the receipt of goods and services should be reported as an asset on the Balance Sheet. The DoD policy is to expense and/or properly classify assets when the related goods and services are received. The Army General Fund has not fully implemented the policy for advances identified in contract feeder systems primarily due to system limitations.

1.Q. Leases

Lease payments for the rental of equipment and operating facilities are classified as either capital or operating leases. Capital leases are leases that transfer substantially all the benefits and risks of ownership to the Army General Fund. If, at its inception, a lease meets one or more of the following four criteria, the Army General Fund should classify that lease as a capital lease: (a) The lease transfers ownership of the property to the Army General Fund by the end of the lease term; (b) The lease contains an option to purchase the leased property at a bargain price; (c) The lease term is equal to or greater than 75 percent of the estimated economic life of the leased property or (d) The present value of rental and other minimum lease payments, excluding that portion of the payments representing executory cost, equals or exceeds 90 percent of the fair value of the leased property.

The last two criteria are not applicable when the beginning of the lease term falls within the last 25% of the total estimated economic life of the leased property. Multi-year service contracts and multi-year purchase contracts for expendable commodities are not capital leases. 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. If a lease does not meet at least one of the above criteria it should be classified as an operating lease. Payments for operating

leases are expensed over the lease term as they become payable.

Office space and leases entered into by the Army General Fund are the largest component of operating leases and are based on costs gathered from existing leases, General Services Administration bills, and interservice support agreements. Future-year projections use the Consumer Price Index.

1.R. Other Assets

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

The Army General Fund conducts business with commercial contractors under two primary types of contracts: fixed price and cost reimbursable. To alleviate the potential financial burden on the contractor that long-term contracts can cause, the Army General Fund may provide financing payments. Contract financing payments are defined in the *Federal Acquisition Regulations, Part 32 - Contract Financing*, as authorized disbursements to a contractor before acceptance of supplies or services by the government. Contract financing payments clauses are incorporated in the contract terms and conditions and may include advance payments, performance-based payments, commercial advances and interim payments, progress payments based on cost, and interim payments under certain cost-reimbursement contracts. It is DoD policy to record certain contract financing payments as other assets. The Army General Fund has not fully implemented this policy primarily due to system limitations.

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

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 Army General Fund recognizes contingent liabilities when past events or exchange transactions occur, a future loss is probable, and the loss amount can be reasonably estimated.

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

Other liabilities also arise as a result of anticipated disposal costs for Army General Fund assets. Consistent with SFFAS No. 6, *Accounting for Property, Plant and Equipment*, recognition of an anticipated environmental disposal liability begins when the asset is placed into service. Based on DoD policy, which is consistent with SFFAS No. 5, nonenvironmental disposal liabilities are recognized when management decides to dispose of an asset. In addition, DoD recognizes nonenvironmental disposal liabilities for nuclear-powered military equipment when placed into service. These amounts are not easily distinguishable and are developed in conjunction with environmental disposal costs.

1.T. *Accrued Leave*

The Army General Fund reports liabilities for military leave and accrued compensatory and annual leave for Civilians. Sick leave for Civilians is expensed as taken. The liabilities are based on current pay rates.

1.U. *Net Position*

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

Unexpended appropriations represent the amounts of budget 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 between expenses and losses and financing sources (including appropriations, revenue, and gains) since inception. The cumulative results of

operations also include donations and transfers in and out of assets that were not reimbursed.

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

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

1.W. *Undistributed Disbursements and Collections*

Undistributed disbursements and collections represent the difference between disbursements and collections matched at the transaction level to specific obligations, payables, or receivables in the source systems and those reported by the U.S. Treasury. Supported disbursements and collections have corroborating documentation for the summary level adjustments made to accounts payable and receivable. Unsupported disbursements and collections do not have supporting documentation for the transactions and most likely would not meet audit scrutiny. However, both supported and unsupported adjustments may have been made to the Army General Fund accounts payable and receivable trial balances before validating the underlying transactions.

Due to noted material weaknesses in current accounting and financial feeder systems, the DoD generally cannot determine whether undistributed disbursements and collections should be applied to federal or nonfederal accounts payable and accounts receivable at the time accounting reports are prepared. Accordingly, the DoD policy is to allocate supported undistributed disbursements and collections between federal and nonfederal categories based on the percentage of distributed federal and nonfederal accounts payable and accounts receivable. Unsupported undistributed disbursements and collections are also applied to reduce accounts payable and receivable accordingly.

1.X. Fiduciary Activities

Fiduciary cash and other assets are not assets of the Army General Fund and are not recognized on the balance sheet. Fiduciary activities are reported on the financial statement note schedules.

1.Y. Military Retirement and Other Federal Employment Benefits

The Army General Fund reported no gains and losses in retirement benefits during this fiscal year.

1.Z. Significant Events

The Army General Fund incurred no significant events during the fiscal year.

NOTE 2. NONENTITY ASSETS

As of September 30

(Amounts in thousands)

1. Intragovernmental Assets

| | | | | |
|-----------------------------------|----|---------|----|---------|
| A. Fund Balance with Treasury | \$ | 391,979 | \$ | 178,173 |
| B. Accounts Receivable | | 0 | | 0 |
| C. Other Assets | | 0 | | 0 |
| D. Total Intragovernmental Assets | \$ | 391,979 | \$ | 178,173 |

2. Nonfederal Assets

| | | | | |
|-----------------------------------|----|---------|----|---------|
| A. Cash and Other Monetary Assets | \$ | 908,582 | \$ | 844,324 |
| B. Accounts Receivable | | 12,025 | | 50,217 |
| C. Other Assets | | 0 | | 0 |
| D. Total Nonfederal Assets | \$ | 920,607 | \$ | 894,541 |

3. Total Nonentity Assets

| | | | |
|----|-----------|----|-----------|
| \$ | 1,312,586 | \$ | 1,072,714 |
|----|-----------|----|-----------|

4. Total Entity Assets

| | | | |
|----|-------------|----|-------------|
| \$ | 289,635,839 | \$ | 281,554,986 |
|----|-------------|----|-------------|

5. Total Assets

| | | | |
|----|-------------|----|-------------|
| \$ | 290,948,425 | \$ | 282,627,700 |
|----|-------------|----|-------------|

Information Related to Nonentity Assets

Nonentity assets are assets for which the Army General Fund maintains stewardship accountability and reporting responsibility. These assets are not available for the Army General Fund's normal operations.

Nonentity Fund Balance with Treasury consists of deposit funds for humanitarian relief and reconstruction, seized Iraqi cash, and Development Fund Iraq (DFI). Deposit funds are generally used to record amounts held temporarily until paid to the appropriate government or public entity. Humanitarian relief and reconstruction deposit funds are funds held for expenditures on behalf of the Iraqi people. Seized Iraqi cash are former Iraqi regime monies confiscated by coalition forces. The DFI consists of proceeds from Iraqi oil sales, repatriated assets from the United States and other nations, and deposits from unencumbered oil-for-food program funds. The deposit funds for seized Iraqi cash and DFI consist only of residual amounts.

Nonentity Cash and Other Monetary Assets consist of cash held by disbursing officers to carry out their paying and collecting missions. These amounts also include foreign currency accommodation exchange primarily consisting of the burden-sharing for the Republic of Korea. Foreign currency is valued using the U.S. Treasury prevailing rate of exchange.

Nonentity Nonfederal accounts receivable are primarily from canceled year appropriations and interest receivables. These receivables will be returned to the U.S. Treasury as miscellaneous receipts once collected.

NOTE 3. FUND BALANCE WITH TREASURY

| As of September 30 | 2016 | 2015 |
|--|-----------------------|-----------------------|
| <i>(Amounts in thousands)</i> | | |
| 1. Fund Balances | | |
| A. Appropriated Funds | \$ 105,646,030 | \$ 112,814,269 |
| B. Revolving Funds | 0 | 0 |
| C. Trust Funds | 35,307 | 30,470 |
| D. Special Funds | 27,167 | 28,328 |
| E. Other Fund Types | 391,979 | 178,173 |
| F. Total Fund Balances | <u>\$ 106,100,483</u> | <u>\$ 113,051,240</u> |
| 2. Fund Balances Per Treasury Versus Agency | | |
| A. Fund Balance per Treasury | \$ 106,133,745 | \$ 113,087,767 |
| B. Fund Balance per Army | 106,100,483 | 113,051,240 |
| 3. Reconciling Amount | <u>\$ 33,262</u> | <u>\$ 36,527</u> |

Information Related to Fund Balance with Treasury**Other Fund Types**

Other Fund Types consist of deposit funds, clearing accounts, unavailable receipt accounts and seized Iraqi cash. Deposit funds are generally used to record amounts held temporarily until paid to the appropriate government or public entity. Clearing accounts are used as a temporary suspense account until later paid by or refunded into another account or when the government acts as a banker or agent for others. Unavailable receipt accounts are credited with all collections not earmarked by law for a specific purpose. These collections include taxes, customs duties, and miscellaneous receipts. Seized Iraqi cash is former Iraqi regime monies confiscated by coalition forces.

Reconciling Amount:

The U.S. Treasury reported \$33.3 million more in Fund Balance with Treasury (FBWT) than reported by the Army General Fund. This difference includes (\$10.4) million in fiduciary activity and \$44.1 million in net differences because of the U.S. Treasury treatment of allocation transfers, offset by \$0.4 million in unappropriated receipts. The fiduciary activity (contributions less distributions to and on behalf of beneficiaries) amount is provided by the U.S. Treasury. The true balance should not be abnormal and research is underway to identify the necessary corrective action (see Note 24). The reconciling difference due to allocation transfers results from instances in which Army allocates to, or is allocated funds from, various governmental entities. In cases in which Army is allocated funds, the allocated amount is excluded from the Fund Balance per Army, but included in the Fund Balance per Treasury.

Status of Fund Balance with Treasury

| As of September 30 | 2016 | 2015 |
|---|------------------------|------------------------|
| <i>(Amounts in thousands)</i> | | |
| 1. Unobligated Balance | | |
| A. Available | \$ 16,312,845 | \$ 17,511,252 |
| B. Unavailable | 17,412,640 | 17,721,374 |
| 2. Obligated Balance not yet Disbursed | \$ 95,584,718 | \$ 99,818,300 |
| 3. Nonbudgetary FBWT | \$ 1,154,183 | \$ 928,929 |
| 4. NonFBWT Budgetary Accounts | <u>\$ (24,363,903)</u> | <u>\$ (22,928,615)</u> |
| 5. Total | <u>\$ 106,100,483</u> | <u>\$ 113,051,240</u> |

Status of Fund Balance with Treasury Definitions

The Status of FBWT reflects the budgetary resources to support the FBWT and is a reconciliation between budgetary and proprietary accounts. It primarily consists of unobligated and obligated balances. The balances reflect the budgetary authority remaining for disbursement against current and future obligations.

Unobligated Balance is classified as available or unavailable and represents the cumulative amount of budgetary authority that has not been set aside to cover outstanding obligations. The unavailable balance consists primarily of funds temporarily precluded from obligation by law which are invested in U.S. Treasury securities. Certain unobligated balances are restricted for future use and are not apportioned for current use. Unobligated balances for trust fund accounts are restricted for use by the public law that established the funds.

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

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

NonFBWT Budgetary Accounts reduce the Status of FBWT. Examples include borrowing authority, investment accounts, and accounts receivable as well as unfilled orders without advance from customers.

NOTE 4. INVESTMENTS AND RELATED INTEREST

As of September 30

(Amounts in thousands)

1. Intragovernmental Securities

A. Nonmarketable, Market-Based

| | | | | | | | | |
|---|----|-------|----|------|----|-------|----|-------|
| 1. Military Retirement Fund | \$ | 0 | \$ | 0 | \$ | 0 | \$ | 0 |
| 2. Medicare Eligible Retiree Health Care Fund | | 0 | | 0 | | 0 | | 0 |
| 3. US Army Corps of Engineers | | 0 | | 0 | | 0 | | 0 |
| 4. Other Funds | | 2,271 | | (20) | | 2,251 | | 2,241 |
| 5. Total Nonmarketable, Market-Based | | 2,271 | | (20) | | 2,251 | | 2,241 |
| B. Accrued Interest | | 6 | | | | 6 | | 6 |
| C. Total Intragovernmental Securities | \$ | 2,277 | \$ | (20) | \$ | 2,257 | \$ | 2,247 |

2. Other Investments

| | | | | | | | | |
|----------------------------|----|---|----|---|----|---|--|-----|
| A. Total Other Investments | \$ | 0 | \$ | 0 | \$ | 0 | | N/A |
|----------------------------|----|---|----|---|----|---|--|-----|

As of September 30

(Amounts in thousands)

1. Intragovernmental Securities

A. Nonmarketable, Market-Based

| | | | | | | | | |
|---|----|-------|----|-----|----|-------|----|-------|
| 1. Military Retirement Fund | \$ | 0 | \$ | 0 | \$ | 0 | \$ | 0 |
| 2. Medicare Eligible Retiree Health Care Fund | | 0 | | 0 | | 0 | | 0 |
| 3. US Army Corps of Engineers | | 0 | | 0 | | 0 | | 0 |
| 4. Other Funds | | 2,182 | | (8) | | 2,174 | | 2,171 |
| 5. Total Nonmarketable, Market-Based | | 2,182 | | (8) | | 2,174 | | 2,171 |
| B. Accrued Interest | | 3 | | | | 3 | | 3 |
| C. Total Intragovernmental Securities | \$ | 2,185 | \$ | (8) | \$ | 2,177 | \$ | 2,174 |

2. Other Investments

| | | | | | | | | |
|----------------------------|----|---|----|---|----|---|--|-----|
| A. Total Other Investments | \$ | 0 | \$ | 0 | \$ | 0 | | N/A |
|----------------------------|----|---|----|---|----|---|--|-----|

Information Related to Investments and Related Interest

Other Funds are comprised of the Army Gift Fund. The amortization method used is the effective interest rate. The Army Gift Fund was established to control and account for the disbursement and use of monies donated to the Army General Fund along with interest received from the investment of such donations. The related earnings are allocated to the appropriate Army General Fund activities to be used in accordance with the directions of the donor. These funds are recorded as Nonmarketable Market-Based U.S. Treasury Securities, which are not traded on any securities exchange, but mirror the prices of marketable securities with similar terms.

The U.S. Treasury securities are issued to the Army Gift Fund as evidence of its receipts and are an asset to the Army General Fund and a liability to the U.S. Treasury. The federal government does not set aside assets to pay future benefits or other expenditures associated with funds from dedicated collections. The cash generated from the Army Gift Fund is deposited in the U.S. Treasury, which uses the cash for general government purposes. Since the Army General Fund and the U.S. Treasury are both part of the Federal Government, these assets and liabilities offset each other from the standpoint of the Federal Government as a whole. For this reason, they do not represent an asset or a liability in the U.S. government wide financial statements.

The U.S. Treasury securities provide the Army General Fund with authority to draw upon the U.S. Treasury to make future benefit payments or other expenditures. When the Army General Fund requires redemption of these securities to make expenditures, the Federal Government will meet the requirement by using accumulated cash balances, raising taxes or other receipts, borrowing from the public, repaying less debt, or curtailing other expenditures. The Federal Government uses the same method to finance all other expenditures.

NOTE 5. ACCOUNTS RECEIVABLE

As of September 30

(Amounts in thousands)

| | 2016 | | |
|--|---------------------|--|--------------------------|
| | Gross Amount Due | Allowance For Estimated Uncollectibles | Accounts Receivable, Net |
| 1. Intragovernmental Receivables | \$ 497,337 | N/A | \$ 497,337 |
| 2. Nonfederal Receivables (From the Public) | \$ 656,876 | \$ (172,412) | \$ 484,464 |
| 3. Total Accounts Receivable | <u>\$ 1,154,213</u> | <u>\$ (172,412)</u> | <u>\$ 981,801</u> |

As of September 30

(Amounts in thousands)

| | 2015 | | |
|--|-------------------|--|--------------------------|
| | Gross Amount Due | Allowance For Estimated Uncollectibles | Accounts Receivable, Net |
| 1. Intragovernmental Receivables | \$ 228,611 | N/A | \$ 228,611 |
| 2. Nonfederal Receivables (From the Public) | \$ 697,438 | \$ (229,494) | \$ 467,944 |
| 3. Total Accounts Receivable | <u>\$ 926,049</u> | <u>\$ (229,494)</u> | <u>\$ 696,555</u> |

Information Related to Accounts Receivable

Accounts receivable represent the Army General Fund's claim for payment from other entities. The Army General Fund only recognizes an allowance for uncollectible amounts from the public. Claims with other federal agencies are resolved in accordance with the Intragovernmental Business Rules.

NOTE 6. OTHER ASSETS

| As of September 30 | 2016 | 2015 |
|--|---------------------|---------------------|
| <i>(Amounts in thousands)</i> | | |
| 1. Intragovernmental Other Assets | | |
| A. Advances and Prepayments | \$ 391,690 | \$ 228,888 |
| B. Other Assets | 0 | 0 |
| C. Total Intragovernmental Other Assets | \$ 391,690 | \$ 228,888 |
| 2. Nonfederal Other Assets | | |
| A. Outstanding Contract Financing Payments | \$ 1,579,955 | \$ 1,516,020 |
| B. Advances and Prepayments | 1,031,952 | 1,188,160 |
| C. Other Assets (With the Public) | 0 | 0 |
| D. Total Nonfederal Other Assets | \$ 2,611,907 | \$ 2,704,180 |
| 3. Total Other Assets | \$ 3,003,597 | \$ 2,933,068 |

Information Related to Other Assets

Contract terms and conditions for certain types of contract financing payments convey certain rights to the Army General Fund that protect the contract work from state or local taxation, liens or attachment by the contractors' 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 Army General Fund. The Army General Fund does not have the right to take the work, except as provided in contract clauses related to termination or acceptance, and the Army General Fund is not obligated to make payment to the contractor until delivery and acceptance.

In May 2015 the Office of the Under Secretary of Defense (OUSD) limited recognition of contract financing payments as defined under Federal Acquisition Regulation 32.4—*Advance Payments for Non-Commercial Items* to advances for non-commercial items. Other authorized disbursements made to contractors prior to acceptance are to be recorded as an asset or expense, as performance based payments, commercial advance or interim payments, or progress payments based on cost or percentage of completion.

Outstanding Contract Financing Payments

The balance of Outstanding Contract Financing Payments includes \$911.6 million in contract financing payments and an additional \$668.4 million in estimated future payments to contractors upon delivery and government acceptance of a satisfactory product. Refer to Note 15, *Other Liabilities*, for additional information.

NOTE 7. CASH AND OTHER MONETARY ASSETS

| As of September 30 | 2016 | 2015 |
|---|-------------------|-------------------|
| <i>(Amounts in thousands)</i> | | |
| 1. Cash | \$ 193,222 | \$ 154,022 |
| 2. Foreign Currency | 715,360 | 708,954 |
| 3. Total Cash, Foreign Currency, & Other Monetary Assets | \$ 908,582 | \$ 862,976 |

Information Related to Cash

Cash consists primarily of cash held by disbursing officers to carry out their paying and collecting mission. Foreign currency consists primarily of burden-sharing funds from the Republic of Korea.

Foreign currency is valued using the U.S. Treasury prevailing rate of exchange. This rate is the most favorable rate that would legally be available to the Federal Government for foreign currency exchange transactions. The Army General Fund cash and foreign currency are nonentity and are restricted.

NOTE 8. DIRECT LOAN AND LOAN GUARANTEES

The Army General Fund operates no direct loan or loan guarantee programs .

NOTE 9. INVENTORY AND RELATED PROPERTY

| As of September 30 (Amounts in thousands) | 2016 | 2015 |
|---|----------------------|----------------------|
| 1. Inventory, Net | \$ 0 | \$ 0 |
| 2. Operating Materiel & Supplies (OM&S), Net | 29,711,383 | 31,333,626 |
| 3. Stockpile Materiel, Net | 0 | 0 |
| 4. Total | <u>\$ 29,711,383</u> | <u>\$ 31,333,626</u> |

Inventory, Net

Not applicable

Operating Materiel and Supplies, Net

| As of September 30 (Amounts in thousands) | 2016 | | | | Valuation Method |
|--|----------------------|-----------------------|----------------------|--|------------------|
| | OM&S Gross Value | Revaluation Allowance | OM&S, Net | | |
| 1. OM&S Categories | | | | | |
| A. Held for Use | \$ 27,166,108 | \$ 0 | \$ 27,166,108 | | Standard Price |
| B. Held for Repair | 2,545,275 | 0 | 2,545,275 | | Standard Price |
| C. Excess, Obsolete, and Unserviceable | 1,021,412 | (1,021,412) | 0 | | Standard Price |
| D. Total | <u>\$ 30,732,795</u> | <u>\$ (1,021,412)</u> | <u>\$ 29,711,383</u> | | |

| As of September 30 (Amounts in thousands) | 2015 | | | | Valuation Method |
|--|----------------------|-----------------------|----------------------|--|------------------|
| | OM&S Gross Value | Revaluation Allowance | OM&S, Net | | |
| 1. OM&S Categories | | | | | |
| A. Held for Use | \$ 28,697,609 | \$ 0 | \$ 28,697,609 | | Standard Price |
| B. Held for Repair | 2,636,017 | 0 | 2,636,017 | | Standard Price |
| C. Excess, Obsolete, and Unserviceable | 420,888 | (420,888) | 0 | | Standard Price |
| D. Total | <u>\$ 31,754,514</u> | <u>\$ (420,888)</u> | <u>\$ 31,333,626</u> | | |

Information Related to OM&S, Net

OM&S include ammunition, tactical missiles, and their related spare and repair parts. The Held for Use category, which includes all materiel available to be issued, consists of \$25.0 billion in Operating Materiel and Supplies Held for Use and \$2.2 billion in Operating Materiel and Supplies Held in Reserve for Future Use.

Managers determine which items are more costly to repair than to replace. The value of these items is offset by an allowance for excess, obsolete, and unserviceable OM&S which results in a net value of zero. The Army General Fund established this allowance at 100 percent of the carrying account in accordance with DoD policy. These items, which include ammunition and missiles, are reported as Excess, Obsolete, and Unserviceable.

The values of the Army's government-furnished materiel and contractor-acquired materiel in the hands of the contractors are normally not included in the OM&S values reported above. The DoD is presently reviewing its process for reporting these amounts in an effort to determine the appropriate accounting treatment and the best method to collect and report required information annually without duplicating information in other existing logistics systems.

Currently, there are no restrictions on OM&S.

NOTE 10. GENERAL PROPERTY, PLANT & EQUIPMENT (PP&E), NET

As of September 30

(Amounts in thousands)

1. Major Asset Classes

| | Depreciation/ Amortization Method | Service Life | Acquisition Value | (Accumulated Depreciation/ Amortization) | Net Book Value |
|--|---|--------------|-----------------------|---|-----------------------|
| A. Land | N/A | N/A | \$ 558,560 | N/A | \$ 558,560 |
| B. Buildings, Structures, and Facilities | S/L | 20 or 40 | 94,367,014 | \$ (40,261,674) | 54,105,340 |
| C. Leasehold Improvements | S/L | lease term | 24,634 | (16,392) | 8,242 |
| D. Software | S/L | 2-5 or 10 | 501,718 | (206,237) | 295,481 |
| E. General Equipment | S/L | Various | 191,951,146 | (106,150,374) | 85,800,772 |
| F. Assets Under Capital Lease | S/L | lease term | 0 | 0 | 0 |
| G. Construction-in- Progress | N/A | N/A | 9,471,775 | N/A | 9,471,775 |
| H. Other | | | 152 | 0 | 152 |
| I. Total General PP&E | | | \$ 296,874,999 | \$ (146,634,677) | \$ 150,240,322 |

As of September 30

(Amounts in thousands)

1. Major Asset Classes

| | Depreciation/ Amortization Method | Service Life | Acquisition Value | (Accumulated Depreciation/ Amortization) | Net Book Value |
|--|---|--------------|-----------------------|---|-----------------------|
| A. Land | N/A | N/A | \$ 600,250 | N/A | \$ 600,250 |
| B. Buildings, Structures, and Facilities | S/L | 20 or 40 | 91,163,029 | \$ (36,415,884) | 54,747,145 |
| C. Leasehold Improvements | S/L | lease term | 24,634 | (16,383) | 8,251 |
| D. Software | S/L | 2-5 or 10 | 501,718 | (206,237) | 295,481 |
| E. General Equipment | S/L | Various | 150,235,830 | (79,961,681) | 70,274,149 |
| F. Assets Under Capital Lease | S/L | lease term | 0 | 0 | 0 |
| G. Construction-in- Progress | N/A | N/A | 7,822,667 | N/A | 7,822,667 |
| H. Other | | | 115 | 0 | 115 |
| I. Total General PP&E | | | \$ 250,348,243 | \$ (116,600,185) | \$ 133,748,058 |

Legend for Valuation Methods: S/L = Straight Line N/A = Not Applicable

Information Related to General PP&E

The Army General Fund is not aware of any restrictions on the use or convertibility of General PP&E.

Significant accounting adjustments have been made to the Army General Fund's mission critical assets as a result of the Army's ongoing audit readiness efforts. These accounting adjustments were recognized in current year gain or loss accounts when auditable data were not available to support restatement of prior-period financial statements.

Other includes General PP&E not otherwise classified above.

Heritage Assets and Stewardship Land Information

The mission of the Army is to provide the military forces needed to deter war and protect the security of the United States by organizing, training, supplying, equipping, and mobilizing forces for assignment in support of that mission. Executing this mission requires efficient and effective use of resources in a manner that ensures operational and environmental sustainability, while respecting the history and heritage that reflect and support the military mission. The Army has stewardship responsibilities for heritage assets that date not only from the military history of the land, but also from prior historic occupations. The Army relies upon heritage assets, such as historic buildings and stewardship land, for daily use in administering, housing, and training soldiers. Heritage assets not currently employed as multi-use, such as archeological collections or museum collections, are items that embody the multi-faceted history of the land, the military, the local communities, and the nation. In that mission, the Army General Fund, with minor exceptions, uses most of the buildings and stewardship land in its daily activities and includes the buildings on the Balance Sheet as multi-use heritage assets (capitalized and depreciated).

SFFAS No. 29, *Heritage Assets and Stewardship Land*, issued by the Federal Accounting Standards Advisory Board, requires note disclosures for these types of assets. The Army General Fund's policy is to preserve its heritage assets, which are items of historical, cultural, educational, or artistic importance.

The Army General Fund is unable to identify all quantities of heritage assets and stewardship land added through donation or devise in FY 2016 due to limitations of the Department of the Army's financial and nonfinancial management processes and systems.

Heritage assets within the Army General Fund consist of buildings and structures, archeological sites, and museum collections. The Army General Fund defines these assets as follows:

Buildings and Structures

Buildings and structures which are listed on, or eligible for listing on, the National Register of Historic Places, including multi-use heritage assets.

Archaeological Sites

Sites that have been identified, evaluated, and determined to be eligible for, or are listed on, the National Historical Places in accordance with Section 110, *National Historical Preservation Act*.

Museum Collection Items

Items which are unique for one or more of the following reasons: historical or natural significance; cultural, educational, or artistic importance; or significant technical or architectural characteristics. The heritage assets for the Army General Fund are listed below:

| Categories | Measure Quantity | Beginning Balance | Additions | Deletions | Ending Balance |
|---|-------------------------|--------------------------|------------------|------------------|-----------------------|
| Buildings and Structures | Each | 41,101 | 258 | 5,114 | 36,245 |
| Archeological Sites | Each | 9,947 | 626 | 327 | 10,246 |
| Museum Collection Items (Objects, Not Including Fine Art) | Each | 585,969 | 0 | 22,165 | 563,804 |
| Museum Collection Items (Objects, Fine Art) | Each | 0 | 36,999 | 0 | 36,999 |

Stewardship Land

Stewardship land is land and land rights owned by the Department of the Army, but not acquired as, or in connection with, items of General PP&E. All land provided to the Department from the public domain or at no cost, regardless of its use, is classified as Stewardship Land.

Stewardship land is presented in context of all categories of DoD lands and reported in acres based on the predominant use of the land. The three categories of Stewardship land held in public trust are as follows: State-Owned Land, Withdrawn Public Land, and Public Land. The Department of Army's stewardship land consists mainly of mission-essential land.

The following is a description of the methods of acquisition and withdrawal of stewardship land:

- ☐ Acquiring additional land through donation or withdrawals from public domain.
- ☐ Identifying missing land records.
- ☐ Disposing of Base Realignment and Closure (BRAC) sites or transferring land to another DoD agency.
- ☐ Identifying cemeteries and historical facilities.
- ☐ Disposing of BRAC property or excess installations.
- ☐ Privatizing residential community initiatives programs.

The Army General Fund holds the following acres of stewardship land:

(Acres in thousands)

| Facility Code | Facility Title | Beginning Balance | Additions | Deletions | Ending Balance |
|---------------------------------|-----------------------------|-------------------|-----------|-----------|----------------|
| 9110 | Government Owned Land | 4,981 | 0 | 0 | 4,981 |
| 9111 | State Owned Land | 5 | 0 | 0 | 5 |
| 9120 | Withdrawn Public land | 6,405 | 0 | 0 | 6,405 |
| 9130 | Licensed and Permitted Land | 187 | 0 | 0 | 187 |
| 9140 | Public Land | 11 | 0 | 0 | 11 |
| 9210 | Land Easement | 218 | 0 | 0 | 218 |
| 9220 | In-leased Land | 21 | 0 | 0 | 21 |
| 9230 | Foreign Land | 1 | 0 | 0 | 1 |
| Grand Total | | | | | 11,829 |
| TOTAL - All Other Land | | | | | 5,408 |
| TOTAL - Stewardship Land | | | | | 6,421 |

NOTE 11. LIABILITIES NOT COVERED BY BUDGETARY RESOURCES

| As of September 30 | 2016 | 2015 |
|--|---------------|---------------|
| (Amounts in thousands) | | |
| 1. Intragovernmental Liabilities | | |
| A. Accounts Payable | \$ 0 | \$ 0 |
| B. Debt | 0 | 0 |
| C. Other | 321,150 | 364,322 |
| D. Total Intragovernmental Liabilities | \$ 321,150 | \$ 364,322 |
| 2. Nonfederal Liabilities | | |
| A. Accounts Payable | \$ 646,175 | \$ 455,940 |
| B. Military Retirement and Other Federal Employment Benefits | 1,238,941 | 1,239,177 |
| C. Environmental and Disposal Liabilities | 24,017,204 | 25,109,476 |
| D. Other Liabilities | 4,575,860 | 4,153,086 |
| E. Total Nonfederal Liabilities | \$ 30,478,180 | \$ 30,957,679 |
| 3. Total Liabilities Not Covered by Budgetary Resources | \$ 30,799,330 | \$ 31,322,001 |
| 4. Total Liabilities Covered by Budgetary Resources | \$ 9,956,180 | \$ 11,388,158 |
| 5. Total Liabilities | \$ 40,755,510 | \$ 42,710,159 |

Information Related to Liabilities Not Covered by Budgetary Resources

Intragovernmental Liabilities, Other, consist of Federal Employees' Compensation Act (FECA) and other unfunded employment-related liabilities.

Nonfederal accounts payable not covered by budgetary resources represent amounts that are related to canceled appropriations. These amounts will require resources funded from future-year appropriations.

Military Retirement and Other Federal Employment Benefits consist of various employee actuarial liabilities not due and payable during the current fiscal year. These liabilities consist primarily of the FECA benefits liability of \$1.2 billion. Refer to Note 17, *Military Retirement and Other Federal Employment Benefits*, for additional details and disclosures.

Environmental Liabilities represent the Department's liability for existing and anticipated environmental cleanup and disposal (see Note 14).

Nonfederal Other Liabilities primarily consist of \$3.6 billion in unfunded annual leave and \$0.5 billion of contingent legal liabilities.

Liabilities such as *Environmental Liabilities* and *Military Retirement and Other Federal Employment Benefits* are not covered by budgetary resources because there are no current or immediate appropriations available for liquidation. These liabilities will require resources funded from future-year appropriations.

NOTE 12. ACCOUNTS PAYABLE

As of September 30

(Amounts in thousands)

| | 2016 | | |
|--|---------------------|--|---------------------|
| | Accounts Payable | Interest, Penalties, and Administrative Fees | Total |
| 1. Intragovernmental Payables | \$ 1,619,144 | \$ N/A | \$ 1,619,144 |
| 2. Nonfederal Payables (to the Public) | 1,285,623 | 23,809 | 1,309,432 |
| 3. Total | \$ 2,904,767 | \$ 23,809 | \$ 2,928,576 |

As of September 30

(Amounts in thousands)

| | 2015 | | |
|--|---------------------|--|---------------------|
| | Accounts Payable | Interest, Penalties, and Administrative Fees | Total |
| 1. Intragovernmental Payables | \$ 1,744,839 | \$ N/A | \$ 1,744,839 |
| 2. Nonfederal Payables (to the Public) | 495,325 | 21,590 | 516,915 |
| 3. Total | \$ 2,240,164 | \$ 21,590 | \$ 2,261,754 |

Accounts payable include amounts owed to federal and nonfederal entities for goods and services received by the Army General Fund. While the Army General Fund ERP systems track intragovernmental accounts payable transactions by customer, the Army General Fund legacy systems do not. Buyer-side accounts payable are adjusted to agree with intraagency seller-side accounts receivable. Accounts payable were adjusted by reclassifying amounts between federal and nonfederal accounts payable and applying both supported and unsupported undistributed disbursements at the reporting entity level.

NOTE 13. DEBT

The Army General Fund has no intragovernmental loan or non-federal debt.

NOTE 14. ENVIRONMENTAL AND DISPOSAL LIABILITIES

As of September 30

(Amounts in thousands)

1. Environmental Liabilities--Nonfederal

A. Accrued Environmental Restoration Liabilities

| | | | | |
|---|----|-----------|----|------------|
| 1. Active Installations—Installation Restoration Program (IRP) and Building Demolition and Debris Removal (BD/DR) | \$ | 2,297,527 | \$ | 2,162,067 |
| 2. Active Installations—Military Munitions Response Program (MMRP) | | 946,678 | | 1,144,773 |
| 3. Formerly Used Defense Sites—IRP and BD/DR | | 3,019,361 | | 3,055,005 |
| 4. Formerly Used Defense Sites--MMRP | | 7,699,415 | | 10,767,920 |

B. Other Accrued Environmental Liabilities—Non-BRAC

| | | | | |
|---|--|-----------|--|---------|
| 1. Environmental Corrective Action | | 619,742 | | 542,126 |
| 2. Environmental Closure Requirements | | 1,289,702 | | 185,971 |
| 3. Environmental Response at Operational Ranges | | 62,367 | | 75,002 |
| 4. Asbestos | | 1,125,311 | | 241,759 |
| 5. Non-General Equipment | | 0 | | 0 |
| 6. Other | | 568,022 | | 0 |

C. Base Realignment and Closure Installations

| | | | | |
|---|--|---------|--|---------|
| 1. Installation Restoration Program | | 625,293 | | 569,880 |
| 2. Military Munitions Response Program | | 631,932 | | 396,779 |
| 3. Environmental Corrective Action / Closure Requirements | | 193,431 | | 204,735 |
| 4. Asbestos | | 0 | | 0 |
| 5. Non-Military Equipment | | 0 | | 0 |
| 6. Other | | 0 | | 0 |

D. Environmental Disposal for General Equipment / Weapons Programs

| | | | | |
|---|--|---|--|---|
| 1. Nuclear Powered General Equipment / Spent Nuclear Fuel | | 0 | | 0 |
| 2. Non-Nuclear Powered General Equipment | | 0 | | 0 |
| 3. Other Weapons Systems | | 0 | | 0 |

E. Chemical Weapons Disposal Program

| | | | | |
|---|--|-----------|--|-----------|
| 1. Chemical Demilitarization - Chemical Materials Agency (CMA) | | 2,657,991 | | 3,046,397 |
| 2. Chemical Demilitarization - Assembled Chemical Weapons Alternatives (ACWA) | | 4,488,009 | | 5,116,279 |
| 3. Other | | 0 | | 0 |

2. Total Environmental Liabilities

| | | | |
|----|------------|----|------------|
| \$ | 26,224,781 | \$ | 27,508,693 |
|----|------------|----|------------|

Information Related to Environmental and Disposal Liabilities

Types of Environmental and Disposal Liabilities (E&DL) Identified

The Army's reported E&DL consists of both event-driven and asset-driven liabilities. Event-driven liabilities are caused by the release of contamination to the environment that will require future cleanup. Asset-driven liabilities are the environmental disposal costs incurred at the end of the asset's useful life. The Army's Note 14 E&DL are reported in five general categories:

- 1.A Accrued Environmental Restoration Liabilities (Active Installations and Formerly Used Defense Sites (FUDS));
- 1.B Other Environmental Liabilities (Non-BRAC);
- 1.C Base Realignment and Closure (BRAC) Installations;
- 1.D Environmental Disposal for General Equipment Liabilities; and
- 1.E Chemical Weapons Disposal Program.

These categories were modified for FY 2016 reporting, when compared to prior year reporting periods. The Army General Fund addresses event-driven liabilities for the Defense Environmental Restoration Program (DERP) requirements at Active Installations, BRAC, FUDS (Lines 1.A and 1.C) and environmental restoration or corrective action not covered by DERP (Line 1.B). Other Environmental Liabilities (Line 1.B) also includes operational assets such as buildings (asbestos, lead based paint, other environmental issues), underground storage tanks (USTs), above ground storage tanks (ASTs), landfills, and deactivated nuclear power plants, which will incur costs during

closure. FY 2016 is the first year for reporting General Equipment Liabilities (Line 1.D) on the financial statement. Finally, the Army reports disposal liabilities for Chemical Weapons Disposal Programs (Line 1.E), which includes the destruction of the entire United States' stockpile of chemical agents and munitions and disposal of non-stockpile chemical material. This includes binary chemical weapons, old chemical weapons recovered as part of remediation and recovery operations, and miscellaneous materiel associated with chemical weapon production, storage, testing, maintenance, and disposal. For each category, the E&DL reflects the future work required to address legal requirements.

The Army reports a \$0 balance for line items where another Department of Defense (DoD) Entity serves as the DoD Executive Agent. Executive agents are responsible for identifying funding requirements and disclosing financial information regarding the progress of these programs. The Department of the Navy is the Executive Agent for Environmental Liabilities due to Nuclear Powered Military Equipment and Spent Nuclear Fuel. The Army is the Executive agent for FUDS and Environmental Liabilities related to the chemical weapons program. The Army reports the Environmental Liabilities for both of these programs on its financial statement.

Applicable Laws and Regulations

The Army GF addresses cleanup of contamination resulting from past waste disposal practices, leaks, spills and other past activities. This cleanup requirement applies to releases of hazardous substances and wastes that created a public health or environmental risk and risk from exposure to unexploded ordnance, discarded military munitions, and munitions constituents at other than operational ranges. DERP was established by Section 211 of the Superfund Amendments and Reauthorization Act of 1986 codified in Title 10 of the United States Code (USC) 2700 et. seq. The Army General Fund is also required to clean up contamination resulting from waste disposal practices, leaks, spills (not governed by DoD Instruction (DoDI) 4715.05, *Environmental Compliance at Installations Outside the United States*) and other activities at overseas locations in accordance with DoD policy as prescribed in DoD Instruction 4715.08, *Remediation of Environmental Contamination Outside the United States*, under the Army Compliance Cleanup Program. Cleanup Sites located overseas that qualify for cleanup cannot be part of an imminent installation/site handover to host nation governments where a residual value determination may occur as part of the turnover.

The Federal Accounting Standards Advisory Board (FASAB) published Technical Bulletin (TB) 2006-1 (FASAB TB 2006-1), *Recognition and Measurement of Asbestos- Related Cleanup Costs* and Technical Release 10, *Implementation Guidance on Asbestos Cleanup Costs Associated with Facilities and Installed Equipment*, which clarifies reporting of liabilities arising from asbestos-related cleanup.

The Army General Fund includes requirements to destroy the chemical stockpile and nonstockpile as part of the Chemical Demilitarization Program. The 1986 Defense Authorization Act (Public Law 99-145, as amended by subsequent Acts), directed the DoD to destroy the unitary chemical stockpile while providing for maximum protection of the environment, public, and personnel involved in the destruction effort. The 1993 Defense Authorization Act (PL 102-484) required the establishment of the nonstockpile Chemical Material Project to safely dispose of all nonstockpile material. The destruction operations being carried out using the facilities and equipment developed and fielded as part of the program are also subject to numerous federal and state environmental regulations.

Applicable laws and regulations addressing environmental restoration and closure include:

- ☐ Comprehensive Environmental Response, Compensation, and Liability Act
- ☐ Superfund Amendments and Reauthorization Act
- ☐ Clean Water Act
- ☐ Safe Drinking Water Act
- ☐ Clean Air Act
- ☐ Resource Conservation and Recovery Act
- ☐ Toxic Substances Control Act
- ☐ Medical Waste Tracking Act

- ☐ Atomic Energy Act
- ☐ Nuclear Waste Policy Act
- ☐ National Defense Authorization Acts
- ☐ DoDI 4715.08, Remediation of Environmental Contamination Outside the United States

Methods for Assigning Estimated Total Cleanup Costs to Current Operating Periods

The Army General Fund uses engineering estimates and independently validated models to estimate environmental cleanup liabilities. The Remedial Action Cost Engineering and Requirements (RACER) system is the Army's preferred model for DERP and non-DERP event-driven liabilities. The Army General Fund relies upon the Air Force, which is the RACER executive agent, to validate the model in accordance with DoDI 5000.61, *DoD Modeling and Simulation (M&S) Verification, Validation, and Accreditation (VV&A)*, and primarily uses the model to estimate liabilities based on data collected during a preliminary assessment, site inspection, and remedial investigation. The Army generally uses engineering estimates to estimate environmental cleanup project once the feasibility study phase is complete.

For asset-driven liabilities, the Army General Fund uses the real property inventory and cost factors derived using industry standards or historical costs to develop environmental closure liabilities. Examples of asset-driven liabilities include the environmental costs associated with a building, storage tanks, and operating landfills. Environmental closure liabilities for individual building demolition will vary significantly, so environmental building demolition liabilities are reported in aggregate using cost factors updated annually and the real property building square footage inventory. Asbestos disposal costs cannot be adequately estimated due to the ubiquitous nature of non-friable asbestos. However, the Army uses experience with pre-demolition building surveys to develop cost factors for asbestos survey and mitigation. In 1990, the US Environmental Protection Agency (USEPA) banned the use of asbestos-containing materials in construction. Therefore, asbestos mitigation Environmental Liability only includes facilities put into service before 1990 using the square footage of buildings put in service before 1990 and an asbestos mitigation cost factor.

Storage Tanks, which typically contain petroleum, oil or lubricants, are assets that will incur environmental costs at the end of the asset's useful life. Disposal costs include removal of the storage tank and associated piping; however, the Army's experience with similar efforts, suggests petroleum releases are usually encountered when closing many storage tanks. As a result, closure costs includes tank removal, over excavation of contaminated soil, and limited groundwater sampling. Cost estimates for storage tank closure were developed for three categories (based on tank volume): Category 1 (0- 999 gallons), Category 2 (1,000 – 9,999 gallons), Category 3 (greater than 10,000 gallons), RACER cost estimates using local cost factors and were used along with the inventory of tanks in each category to develop the reported Environmental Liability.

Permitted landfill closure liabilities are estimated using federal solid waste closure requirements. The future closure costs for operating landfills consider the type of landfill (e.g., hazardous waste or sanitary/municipal) and acreage. Reported Environmental Liability also include post-closure requirements (i.e. 30 years of groundwater monitoring). RACER estimates were developed using local cost factors, type, and size of each operating landfill in the Army's real property inventory.

Per Army Regulation 50-7 (*Army Reactor Program*) and 10 CFR 51.82, decommissioning of the Army's deactivated nuclear power plants is required within 60 years of shutdown. The deactivation dates for the three reactors are as follows:

- ☐ SM-1 (Fort Belvoir) – 1972
- ☐ SM-1A (Fort Greely) – 1973
- ☐ MH-1A (*Sturgis Barge*) – 1976

Given the 60 year required timeline, the earliest required completion date is 2032 for the SM-1 reactor. Closure liability estimates are developed using costs associated with the decommissioning of similar facilities, site-specific data collected during historical records reviews and site characterization, and professional engineering

judgment based upon industry standards. The estimates are indexed annually to reflect current year cost for environmental liabilities determination.

The Army General Fund is continuing to work to gather and report E&DL for equipment, as per FASAB Technical Release 11, *Implementation Guidance on Cleanup Costs Associated with Equipment*. The determination of Environmental Liability for individual items of Army equipment is difficult to estimate due to the fact that most of the future Environmental Liability determinants are covered as part of the operational process costs to upkeep equipment. However, the Army is using the Master Divestiture List (MDL) as the basis for determining equipment Environmental Liability. The list also partly represents the universe of Army general equipment and provides demilitarization (DEMIL) cost equipment disposal. The demilitarization process of equipment disposal is a distinct process from which the equipment Environmental Liability is currently determined. The DEMIL process however generates an estimate that is inflated because the process cannot easily differentiate routine from non-routine process costs.

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

The Army General Fund estimates are updated annually to reflect changes in previously unknown information, better site characterization, re-estimation based on different assumptions, and lessons learned. Environmental Liabilities may change in the future due to changes in laws and regulations, agreements with regulatory agencies, and advances in technology. Environmental Liabilities may also change due to updated criteria and new ways of determining current categories on the financial statement.

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

The Environmental Liabilities for the Army General Fund are based on accounting estimates, which require certain judgments and assumptions that are believed to be reasonable based upon information available to the Army at the time of calculating the estimates. The actual results may vary materially from the accounting estimates if agreements with regulatory agencies require remediation to a different degree than anticipated when calculating the estimates. Environmental Liabilities can be further impacted if investigation of environmental sites discloses contamination levels different from those known at the time of the estimates. The Army will make every effort to lessen this uncertainty and capture any changes in the Roll Forward period as per the FASAB handbook.

The Army General Fund has reported asbestos survey costs but estimating the amount of non-friable asbestos removal/disposal at the time of building renovation or demolition, per FASAB TB 2006-1, presents too much uncertainty to recognize on the balance sheet. If recent experience holds true, asbestos mitigation related costs for all facilities including survey costs could be \$3.54 per square foot, or \$2.6 billion.

The Army General Fund is uncertain regarding the costs for remediation activities in conjunction with returning overseas military facilities to host nations. The Army General Fund is currently unable to provide a reasonable estimate because the extent of remediation required is not known and criteria for overseas site cleanup has changed significantly since the publishing of DoDI 4715.08. The updated test for new sites to qualify for overseas cleanup is more stringent than in the past as per the issuance of DoDI 4715.08.

The Army General Fund is also uncertain regarding the costs for cleanup associated with general equipment. The Army General Fund is currently unable to provide a reasonable estimate due to the fact that a large portion of Army's equipment is disposed of as a routine part of current operations, while other equipment is recycled. Some equipment does not present a liability for the Army since they are disposed of through various governmental sales program (e.g. foreign military sales, Defense Logistics Agency equipment sales, and others)

Other Accrued Environmental Liabilities - Non BRAC consists of low-level radioactive waste.

NOTE 15. OTHER LIABILITIES

As of September 30
(Amounts in thousands)

| | 2016 | | |
|--|---------------------|----------------------|----------------------|
| | Current Liability | Noncurrent Liability | Total |
| 1. Intragovernmental | | | |
| A. Advances from Others | \$ 14,527 | \$ 0 | \$ 14,527 |
| B. Deposit Funds and Suspense Account Liabilities | 818,285 | 0 | 818,285 |
| C. Disbursing Officer Cash | 916,885 | 0 | 916,885 |
| D. Judgment Fund Liabilities | 12,214 | 0 | 12,214 |
| E. FECA Reimbursement to the Department of Labor | 103,548 | 125,934 | 229,482 |
| F. Custodial Liabilities | 3,147 | 1,000 | 4,147 |
| G. Employer Contribution and Payroll Taxes Payable | 127,088 | 0 | 127,088 |
| H. Other Liabilities | 79,713 | 0 | 79,713 |
| I. Total Intragovernmental Other Liabilities | \$ 2,075,407 | \$ 126,934 | \$ 2,202,341 |
| 2. Nonfederal | | | |
| A. Accrued Funded Payroll and Benefits | \$ 810,745 | \$ 0 | \$ 810,745 |
| B. Advances from Others | 1,256,566 | 0 | 1,256,566 |
| C. Deferred Credits | 0 | 0 | 0 |
| D. Deposit Funds and Suspense Accounts | 325,795 | 0 | 325,795 |
| E. Temporary Early Retirement Authority | 0 | 0 | 0 |
| F. Nonenvironmental Disposal Liabilities | | | |
| (1) Military Equipment (Nonnuclear) | 0 | 0 | 0 |
| (2) Excess/Obsolete Structures | 0 | 0 | 0 |
| (3) Conventional Munitions Disposal | 0 | 5,974 | 5,974 |
| G. Accrued Unfunded Annual Leave | 3,637,509 | 0 | 3,637,509 |
| H. Capital Lease Liability | 0 | 0 | 0 |
| I. Contract Holdbacks | 287,317 | 0 | 287,317 |
| J. Employer Contribution and Payroll Taxes Payable | 162,881 | 0 | 162,881 |
| K. Contingent Liabilities | 72,942 | 1,600,710 | 1,673,652 |
| L. Other Liabilities | 432 | 0 | 432 |
| M. Total Nonfederal Other Liabilities | \$ 6,554,187 | \$ 1,606,684 | \$ 8,160,871 |
| 3. Total Other Liabilities | \$ 8,629,594 | \$ 1,733,618 | \$ 10,363,212 |

As of September 30
(Amounts in thousands)

| | 2015 | | |
|--|-------------------|----------------------|---------------|
| | Current Liability | Noncurrent Liability | Total |
| 1. Intragovernmental | | | |
| A. Advances from Others | \$ 22,349 | \$ 0 | \$ 22,349 |
| B. Deposit Funds and Suspense Account Liabilities | 775,693 | 0 | 775,693 |
| C. Disbursing Officer Cash | 852,357 | 0 | 852,357 |
| D. Judgment Fund Liabilities | 23,088 | 0 | 23,088 |
| E. FECA Reimbursement to the Department of Labor | 102,704 | 130,633 | 233,337 |
| F. Custodial Liabilities | 40,931 | 1,254 | 42,185 |
| G. Employer Contribution and Payroll Taxes Payable | 192,724 | 0 | 192,724 |
| H. Other Liabilities | 113,434 | 0 | 113,434 |
| I. Total Intragovernmental Other Liabilities | \$ 2,123,280 | \$ 131,887 | \$ 2,255,167 |
| 2. Nonfederal | | | |
| A. Accrued Funded Payroll and Benefits | \$ 2,593,869 | \$ 0 | \$ 2,593,869 |
| B. Advances from Others | 1,393,196 | 0 | 1,393,196 |
| C. Deferred Credits | 0 | 0 | 0 |
| D. Deposit Funds and Suspense Accounts | 152,362 | 0 | 152,362 |
| E. Temporary Early Retirement Authority | 0 | 0 | 0 |
| F. Nonenvironmental Disposal Liabilities | | | |
| (1) Military Equipment (Nonnuclear) | 0 | 0 | 0 |
| (2) Excess/Obsolete Structures | 0 | 0 | 0 |
| (3) Conventional Munitions Disposal | 0 | 5,974 | 5,974 |
| G. Accrued Unfunded Annual Leave | 3,381,305 | 0 | 3,381,305 |
| H. Capital Lease Liability | 0 | 0 | 0 |
| I. Contract Holdbacks | 380,194 | 0 | 380,194 |
| J. Employer Contribution and Payroll Taxes Payable | 130,281 | 0 | 130,281 |
| K. Contingent Liabilities | 112,457 | 1,295,730 | 1,408,187 |
| L. Other Liabilities | 0 | 0 | 0 |
| M. Total Nonfederal Other Liabilities | \$ 8,143,664 | \$ 1,301,704 | \$ 9,445,368 |
| 3. Total Other Liabilities | \$ 10,266,944 | \$ 1,433,591 | \$ 11,700,535 |

Advances from Others

Advances from Others represent liabilities for collections received to cover future expenses or acquisition of assets.

Deposit Fund and Suspense Accounts

Deposit funds and Suspense Accounts represent liabilities for receipts held in suspense temporarily for distribution to another fund or entity or held as an agent for others and paid at the direction of the owner.

Disbursing Officers Cash

Disbursing Officers Cash represents liabilities for currency on hand, cash on deposit at designated depositories, cash in the hands of deputy disbursing officers, cashiers and agents, negotiable instruments on hand, etc.

Custodial Liabilities

Custodial Liabilities represent liabilities for collections reported as non-exchange revenues in which the Army is acting on behalf of another Federal entity.

Intragovernmental Other Liabilities Composition

Intragovernmental Other Liabilities consist of the unemployment compensation liability and other unfunded employment benefits.

Estimated Future Contract Financing Payments

Contingent liabilities include \$668.4 million related to contracts authorizing progress payments based on cost as defined in the Federal Acquisition Regulation (FAR). In accordance with contract terms, specific rights to the contractors' work vest with the Federal Government when a specific type of contract financing payment is made. This action protects taxpayer funds in the event of contract nonperformance. It is DoD policy that these rights should not be misconstrued as rights of ownership. The Army General Fund is under no obligation to pay contractors for amounts greater than the amounts of progress payments authorized in contracts until delivery and government acceptance. The Army General Fund has recognized a contingent liability for the estimated unpaid costs that are considered conditional for payment pending delivery and government acceptance for the following reasons: (1) the contractors will probably complete their efforts and deliver satisfactory products, and (2) the amount of contractor costs incurred but not yet paid are estimable.

Total contingent liabilities for progress payments based on cost represent the difference between the estimated costs incurred to date by contractors and amounts authorized to be paid under progress payments based on cost provisions within the FAR. Estimated contractor-incurred costs are calculated by dividing the cumulative unliquidated progress payments based on cost by the contract-authorized progress payment rate. The balance of unliquidated progress payments based on cost is deducted from the estimated total contractor-incurred costs to determine the contingency amount.

NOTE 16. COMMITMENTS AND CONTINGENCIES

Information Related to Commitments and Contingencies

The Army General Fund is a party in various administrative proceedings and legal actions related to claims for environmental damage, equal opportunity matters, and contractual bid protests.

The Army General Fund has accrued contingent liabilities for legal actions when the Office of General Counsel (OGC) considers an adverse decision is probable and the amount of loss is measurable. In the event of an adverse judgment against the Federal Government, some of the liabilities may be payable from the U.S. Treasury Judgment Fund. The Army General Fund reports contingent liabilities in Note 15, *Other Liabilities*.

Nature of Contingency

The Management's Schedule of Information derived from the FY 2016 Army Legal Representation Letter outlines claims against the Army General Fund totaling approximately \$111.0 billion for which the Army OGC is unable to express an opinion. The historical payout percentage for these cases is less than 1 percent. To determine the historical payout, the Army OGC divides the total amount reported as a payout in the fiscal year by the total amount claimed in the Army Legal Representation Letter.

The Army General Fund has other contingent liabilities for which the possibility of loss is considered reasonable. These liabilities are not accrued in the Army General Fund's financial statements. As of September 30, 2016, the Army General Fund had \$275.0 million in claims considered reasonably possible. Estimates for litigations, claims, and assessments are required to be fully supported.

Estimates in the Management Schedule of Information will not always agree with amounts, displayed below, that were reported by the OGC subordinate commands because the Management Schedule of Information amounts are subject to a materiality threshold – currently \$25.4 million.

(Amounts in thousands)

| Title of Contingent Liabilities | Estimate |
|---------------------------------|-------------------|
| U.S. Army Litigation Division | \$ 10,934 |
| Contract Appeals Division | \$ 54,479 |
| USACE | \$ 536,600 |
| Total | \$ 602,013 |

Other Information Pertaining to Commitments

The Army General Fund is a party in numerous individual contracts that contain clauses, such as price escalation, award fee payments, or dispute resolution, that may result in a future outflow of budgetary resources. Currently, the Army General Fund automated system processes have limited capability to capture these potential liabilities; therefore, the amounts reported may not fairly present the Army General Fund's commitments and contingencies.

NOTE 17. MILITARY RETIREMENT AND OTHER FEDERAL EMPLOYMENT BENEFITS

As of September 30

(Amounts in thousands)

| | 2016 | | |
|--|---------------------|--|----------------------|
| | Liabilities | (Less: Assets Available to Pay Benefits) | Unfunded Liabilities |
| 1. Pension and Health Benefits | | | |
| A. Military Retirement Pensions | \$ 0 | \$ 0 | \$ 0 |
| B. Military Pre Medicare-Eligible Retiree Health Benefits | 0 | 0 | 0 |
| C. Military Medicare-Eligible Retiree Health Benefits | 0 | 0 | 0 |
| D. Total Pension and Health Benefits | \$ 0 | \$ 0 | \$ 0 |
| 2. Other Benefits | | | |
| A. FECA | \$ 1,238,941 | \$ 0 | \$ 1,238,941 |
| B. Voluntary Separation Incentive Programs | 0 | 0 | 0 |
| C. DoD Education Benefits Fund | 0 | 0 | 0 |
| D. Other | 0 | 0 | 0 |
| E. Total Other Benefits | \$ 1,238,941 | \$ 0 | \$ 1,238,941 |
| 3. Total Military Retirement and Other Federal Employment Benefits: | \$ 1,238,941 | \$ 0 | \$ 1,238,941 |

As of September 30

(Amounts in thousands)

| | 2015 | | |
|--|---------------------|--|----------------------|
| | Liabilities | (Less: Assets Available to Pay Benefits) | Unfunded Liabilities |
| 1. Pension and Health Benefits | | | |
| A. Military Retirement Pensions | \$ 0 | \$ 0 | \$ 0 |
| B. Military Pre Medicare-Eligible Retiree Health Benefits | 0 | 0 | 0 |
| C. Military Medicare-Eligible Retiree Health Benefits | 0 | 0 | 0 |
| D. Total Pension and Health Benefits | \$ 0 | \$ 0 | \$ 0 |
| 2. Other Benefits | | | |
| A. FECA | \$ 1,239,177 | \$ 0 | \$ 1,239,177 |
| B. Voluntary Separation Incentive Programs | 0 | 0 | 0 |
| C. DoD Education Benefits Fund | 0 | 0 | 0 |
| D. Other | 0 | 0 | 0 |
| E. Total Other Benefits | \$ 1,239,177 | \$ 0 | \$ 1,239,177 |
| 3. Total Military Retirement and Other Federal Employment Benefits: | \$ 1,239,177 | \$ 0 | \$ 1,239,177 |

Information Related to Military Retirement and Other Federal Employment Benefits

Federal Employees' Compensation Act (FECA)

The Army's actuarial liability for workers' compensation benefits is developed by the Department of Labor and provided to the Army at the end of each fiscal year. The liability 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 actuarial liability for the FECA decreased \$235.6 million between FY 2015 and FY 2016.

Actuarial Cost Method

The liability is determined using a method that utilizes historical benefit payment patterns related to a specific incurred period to predict the ultimate payments.

Assumptions

The projected annual benefit payments are discounted to the present value using the Office of Management and Budget's economic assumptions for 10-year U.S. Treasury notes and bonds. Cost-of-living adjustments (COLA) and medical inflation factors (CPIM) provided by the Department of Labor are also applied to the calculation of projected future benefits. The estimated actuarial liability is updated only at the end of each fiscal year.

Interest rate assumptions utilized for discounting were as follows:

Discount Rates

For wage benefits:

2.781% in Year 1 and years thereafter.

For medical benefits:

2.261% in Year 1 and years thereafter.

To provide more specifically for the effects of the inflation on the liability for future workers' compensation benefits, COLAs and CPIMs were applied to the calculation of projected future benefits. The actual rates for these factors for the charge-back year (CBY) 2016 were used to adjust the historical payments associated with the methodology to current year constant dollars.

The compensation COLAs and CPIMs used in the projections for various CBYs were as follows:

| CBY | COLA | CPIM |
|------|-------|-------|
| 2016 | N/A | N/A |
| 2017 | 1.31% | 2.99% |
| 2018 | 1.13% | 3.09% |
| 2019 | 1.23% | 3.40% |
| 2020 | 1.45% | 3.68% |
| 2021 | 1.85% | 3.87% |

The resulting projections from the model were analyzed to ensure that the estimates were reliable. The analysis was based on four tests: (1) a sensitivity analysis of the model in comparison to economic assumptions; (2) a comparison, by agency, of the percentage change in the liability amount to the percentage change in the actual incremental payments; (3) a comparison of the incremental paid losses per case (a measure of case-severity) in CBY 2016 to the average pattern observed during the most current three CBYs; and (4) a comparison of the estimated liability per case in the CBY 2016 projection to the average pattern for the projections of the most recent three years.

Other Disclosures

Actuarial liabilities are computed for employee compensation benefits as mandated by FECA. The Office of Personnel Management provides updated Army actuarial liabilities during the 4th Quarter of each fiscal year. The Army General Fund computes its portion of the total Army actuarial liability based on the percentage of its FECA expense to the total Army FECA expense.

NOTE 18. GENERAL DISCLOSURES RELATED TO THE STATEMENT OF NET COST

Intragovernmental Costs and Exchange Revenue

As of September 30

(Amounts in thousands)

Military Personnel

| | 2016 | 2015 |
|--|----------------------|----------------------|
| 1. Gross Cost | | |
| A. Intragovernmental Cost | \$ 29,793,689 | \$ 28,465,425 |
| B. Nonfederal Cost | 27,762,649 | 30,173,586 |
| C. Total Cost | \$ 57,556,338 | \$ 58,639,011 |
| 2. Earned Revenue | | |
| A. Intragovernmental Revenue | \$ (370,082) | \$ (343,038) |
| B. Nonfederal Revenue | (1,716) | 0 |
| C. Total Revenue | \$ (371,798) | \$ (343,038) |
| 3. Losses/(Gains) from Actuarial Assumption Changes for Military Retirement Benefits | \$ 0 | \$ 0 |
| Total Net Cost | \$ 57,184,540 | \$ 58,295,973 |

Operations, Readiness & Support

| | | |
|--|----------------------|----------------------|
| 1. Gross Cost | | |
| A. Intragovernmental Cost | \$ 7,748,564 | \$ 6,156,343 |
| B. Nonfederal Cost | 54,561,902 | 50,525,380 |
| C. Total Cost | \$ 62,310,466 | \$ 56,681,723 |
| 2. Earned Revenue | | |
| A. Intragovernmental Revenue | \$ 3,735,286 | \$ 4,909,662 |
| B. Nonfederal Revenue | (598,896) | 7,952 |
| C. Total Revenue | \$ 3,136,390 | \$ 4,917,614 |
| 3. Losses/(Gains) from Actuarial Assumption Changes for Military Retirement Benefits | \$ 0 | \$ 0 |
| Total Net Cost | \$ 65,446,856 | \$ 61,599,337 |

Procurement

| | | |
|--|----------------------|----------------------|
| 1. Gross Cost | | |
| A. Intragovernmental Cost | \$ 838,386 | \$ 1,347,870 |
| B. Nonfederal Cost | 16,635,683 | 13,914,129 |
| C. Total Cost | \$ 17,474,069 | \$ 15,261,999 |
| 2. Earned Revenue | | |
| A. Intragovernmental Revenue | \$ (1,339,406) | \$ (1,699,966) |
| B. Nonfederal Revenue | (114,763) | (99,594) |
| C. Total Revenue | \$ (1,454,169) | \$ (1,799,560) |
| 3. Losses/(Gains) from Actuarial Assumption Changes for Military Retirement Benefits | \$ 0 | \$ 0 |
| Total Net Cost | \$ 16,019,899 | \$ 13,462,439 |

Research, Development, Test & Evaluation

| | | |
|--|---------------------|---------------------|
| 1. Gross Cost | | |
| A. Intragovernmental Cost | \$ 1,081,758 | \$ 1,156,807 |
| B. Nonfederal Cost | 10,360,823 | 9,723,654 |
| C. Total Cost | \$ 11,442,581 | \$ 10,880,461 |
| 2. Earned Revenue | | |
| A. Intragovernmental Revenue | \$ (4,153,233) | \$ (3,865,809) |
| B. Nonfederal Revenue | (88,612) | (212,891) |
| C. Total Revenue | \$ (4,241,845) | \$ (4,078,700) |
| 3. Losses/(Gains) from Actuarial Assumption Changes for Military Retirement Benefits | \$ 0 | \$ 0 |
| Total Net Cost | \$ 7,200,736 | \$ 6,801,761 |

Intragovernmental Costs and Exchange Revenue

As of September 30

(Amounts in thousands)

Family Housing & Military Construction

| | 2016 | 2015 |
|--|---------------------|----------------------|
| 1. Gross Cost | | |
| A. Intragovernmental Cost | \$ 466,263 | \$ 557,055 |
| B. Nonfederal Cost | 7,816,790 | 16,293,793 |
| C. Total Cost | \$ 8,283,053 | \$ 16,850,848 |
| 2. Earned Revenue | | |
| A. Intragovernmental Revenue | \$ (4,380,342) | \$ (5,260,074) |
| B. Nonfederal Revenue | (516,778) | (281,942) |
| C. Total Revenue | \$ (4,897,121) | \$ (5,542,016) |
| 3. Losses/(Gains) from Actuarial Assumption Changes for Military Retirement Benefits | \$ 0 | \$ 0 |
| Total Net Cost | \$ 3,385,932 | \$ 11,308,832 |

Consolidated

| | | |
|--|-----------------------|-----------------------|
| 1. Gross Cost | | |
| A. Intragovernmental Cost | \$ 39,928,661 | \$ 37,683,500 |
| B. Nonfederal Cost | 117,137,846 | 120,630,542 |
| C. Total Cost | \$ 157,066,507 | \$ 158,314,042 |
| 2. Earned Revenue | | |
| A. Intragovernmental Revenue | \$ (6,507,777) | \$ (6,259,225) |
| B. Nonfederal Revenue | (1,320,765) | (586,475) |
| C. Total Revenue | \$ (7,828,542) | \$ (6,845,700) |
| 3. Losses/(Gains) from Actuarial Assumption Changes for Military Retirement Benefits | \$ 0 | \$ 0 |
| 4. Costs Not Assigned to Programs | \$ 0 | \$ 0 |
| 5. (Less: Earned Revenues) Not Attributed to Programs | \$ 0 | \$ 0 |
| Total Net Cost | \$ 149,237,965 | \$ 151,468,342 |

Information Related to the Statement of Net Cost

Definitions

Intragovernmental costs and revenue represent transactions made between two reporting entities within the Federal Government.

Public costs and revenue are exchange transactions made between the reporting entity and a nonfederal entity.

Other Information Regarding Costs

The Statement of Net Cost (SNC) represents the net cost of programs and organizations of the Federal Government supported by appropriations or other means. The intent of the SNC is to provide gross and net cost information related to the amount of output or outcome for a given program or organization administered by a responsible reporting entity. The DoD's current processes and systems do not capture and report accumulated costs for major programs based upon the performance measures as required by the Government Performance and Results Act. The DoD is in the process of reviewing available data and developing a cost reporting methodology as required by SFFAS No. 4, *Managerial Cost Accounting Concepts and Standards for the Federal Government*, as amended by SFFAS No. 30, *Inter-Entity Cost Implementation*.

The amounts presented in the Consolidated SNC are based on funding, obligation, accrual, and disbursing transactions, which are not always recorded using accrual accounting. The Army General Fund systems do not always record the transactions on an accrual basis as required by the generally accepted accounting principles. The information presented also includes data from nonfinancial feeder systems to ensure that all cost and financing sources are captured for the Army General Fund.

Additional Disclosures

The Army General Fund systems do not track intragovernmental transactions by customer at the transaction level. Buyer-side expenses are adjusted to agree with internal seller-side revenues. Expenses are generally adjusted by reclassifying amounts between federal and nonfederal expenses. Intradepartmental revenues and expenses are then eliminated.

The Army General Fund accounting systems do not capture information relative to heritage assets separately and distinctly from normal operations. The Army General Fund is not able to separately identify the costs of acquiring, constructing, improving, reconstructing, or renovating heritage assets. The Army Financial Improvement Plan outlines tasks to identify and report costs associated with heritage assets separately by 4th Quarter, FY 2017.

The abnormal revenue balance impacting the "Operations, Readiness & Support" program is attributable to the current business practice which includes elimination reporting for the Army General Fund as a whole in this program group.

NOTE 19. DISCLOSURES RELATED TO THE STATEMENT OF CHANGES IN NET POSITION

Other Financing Sources, Other

Other Financing Sources, Other primarily consist of gains and losses that resulted from adjustments necessary to balance the Army General Fund's feeder systems with DoD's financial reporting system and to correct inherent limitations of the current financial systems.

Appropriations Received

The Appropriations Received line item on the Statement of Changes in Net Position (SCNP) does not agree with the Appropriations line item on the Statement of Budgetary Resources (SBR). The \$406.9 million difference is due to additional resources included in the Appropriations line item on the SCNP.

| Year Ended September 30, 2016 (Amounts in millions) | Total | |
|--|-------|-----------|
| Reconciliation of Appropriations on the Statement of Budgetary Resources to Appropriations Received on the Statement of Changes in Net Position | | |
| Appropriations, Statement of Budgetary Resources | \$ | 147,453.3 |
| Appropriations Received, Statement of Changes in Net Position | \$ | 147,860.2 |
| Total Reconciling Amount | \$ | 406.9 |
| Items Reported as Reductions to Appropriations, Statement of Budgetary Resources | | |
| Permanent Reductions | \$ | (1,780.1) |
| Temporary Reductions | \$ | (1.4) |
| Items Reported as Additions to Appropriations, Statement of Budgetary Resources | | |
| Transfers | \$ | 1,349.9 |
| Items Not Reported as Appropriations Received on the Statement of Changes in Net Position | | |
| Dedicated Appropriations and Earmarked Receipts | \$ | 24.7 |
| Total Reconciling Items | \$ | 406.9 |

Eliminations

In the SCNP, all offsetting balances (i.e., transfers-in and transfers-out, revenues and expenses) for intra-entity activity between Funds from Dedicated Collections and All Other Funds are reported on the same lines. The Eliminations column contains all appropriate elimination entries, which net to zero within each respective line, except for intra-entity imputed financing costs.

NOTE 20. DISCLOSURES RELATED TO THE STATEMENT OF BUDGETARY RESOURCES

| As of September 30 | 2016 | 2015 |
|--|---------------|---------------|
| <i>(Amounts in thousands)</i> | | |
| 1. Net Amount of Budgetary Resources Obligated for Undelivered Orders at the End of the Period | \$ 91,734,644 | \$ 93,873,145 |
| 2. Available Borrowing and Contract Authority at the End of the Period | 0 | 0 |

Information Related to the Statement of Budgetary Resources

Undelivered Orders

Undelivered Orders presented in the Statement of Budgetary Resources (SBR) include Undelivered Orders-Unpaid for both direct and reimbursable funds.

Reporting of Appropriations Received

The Appropriations line on the SBR does not agree with the Appropriations Received line on the SCNP because of differences between proprietary and budgetary accounting concepts and reporting requirements. Refer to Note 19, *Disclosures Related to the Statement of Changes in Net Position*, for further information.

Presentation of Statement of Budgetary Resources

The SBR includes intra-entity transactions because the statements are presented as combined.

Breakdown of Apportionment Categories

The amount of direct and reimbursable obligations incurred against amounts apportioned under Category A (apportioned by fiscal quarter), Category B (apportioned by project or activity), and Exempt from Apportionment is as follows:

| Type | Budgetary | |
|---------------------------|----------------------------|----------------------------------|
| | Direct (\$ in billions) | Reimbursable (\$ in billions) |
| Category A | \$124.8 | \$5.0 |
| Category B | \$39.4 | \$16.8 |
| Exempt from Apportionment | * | ** |
| Total | \$163.2 | \$21.8 |

| Type | Non-Budgetary | |
|------------|----------------------------|----------------------------------|
| | Direct (\$ in millions) | Reimbursable (\$ in millions) |
| Category A | — | — |

* The Exempt from Apportionment amount is \$15 Million.

** The Exempt from Apportionment amount is \$0 Million.

The above disclosure agrees (1) with the aggregate of the related information as reported on the SF 133, Report on Budget Execution, and (2) with Obligations Incurred as reported on the SBR.

Reconciliation of Combined SBR to President's Budget

| As of September 30 | Fiscal Year 2016 As Reported | | | |
|--------------------------------------|------------------------------|----------------------|---------------------------------|---------------------|
| <i>(Amounts in billions)</i> | Budgetary Resources | Obligations Incurred | Distributed Offsetting Receipts | Agency Outlays, Net |
| Combined SBR | \$ 218.7 | \$ 185.0 | \$ 0.4 | \$ 149.4 |
| Differences: | | | | |
| Adjustments to SBR | | | | |
| Other | | | (0.4) | 0.4 |
| Budget of the U.S. Government | \$ 218.7 | \$ 185.0 | \$ 0 | \$ 149.8 |

The differences reported in Other are due to the Distributed Offsetting Receipts reported by Army in its FY 2016 SBR, but not by Treasury in its reported outlays.

NOTE 21. RECONCILIATION OF NET COST OF OPERATIONS TO BUDGET

For the Years Ended September 30

(Amounts in thousands)

Resources Used to Finance Activities:**Budgetary Resources Obligated:**

| | | |
|--|----------------|----------------|
| 1. Obligations incurred | \$ 185,011,939 | \$ 184,224,655 |
| 2. Less: Spending authority from offsetting collections and recoveries (-) | (40,900,336) | (37,404,927) |
| 3. Obligations net of offsetting collections and recoveries | \$ 144,111,603 | \$ 146,819,728 |
| 4. Less: Offsetting receipts (-) | (362,062) | (930,148) |
| 5. Net obligations | \$ 143,749,541 | \$ 145,889,580 |

Other Resources:

| | | |
|--|----------------|----------------|
| 6. Donations and forfeitures of property | 0 | 76 |
| 7. Transfers in/out without reimbursement (+/-) | 2,138,368 | 2,226,375 |
| 8. Imputed financing from costs absorbed by others | 940,948 | 991,360 |
| 9. Other (+/-) | 19,325,732 | (8,433,930) |
| 10. Net other resources used to finance activities | \$ 22,405,048 | \$ (5,216,119) |
| 11. Total resources used to finance activities | \$ 166,154,589 | \$ 140,673,461 |

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 (-) | \$ 2,138,500 | \$ 12,135,697 |
| 12b. Unfilled Customer Orders | 1,392,488 | (2,814,076) |
| 13. Resources that fund expenses recognized in prior Periods (-) | (1,299,158) | (4,528,637) |
| 14. Budgetary offsetting collections and receipts that do not affect Net Cost of Operations | 31,569 | 587,158 |
| 15. Resources that finance the acquisition of assets (-) | (12,245,725) | (14,825,120) |
| 16. Other resources or adjustments to net obligated resources that do not affect Net Cost of Operations: | | |
| 16a. Less: Trust or Special Fund Receipts Related to exchange in the Entity's Budget (-) | 0 | 0 |
| 16b. Other (+/-) | (21,133,608) | 6,550,650 |
| 17. Total resources used to finance items not part of the Net Cost of Operations | \$ (31,115,934) | \$ (2,894,328) |
| 18. Total resources used to finance the Net Cost of Operations | \$ 135,038,655 | \$ 137,779,133 |

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 | \$ 6,844 | \$ 34 |
| 20. Increase in environmental and disposal liability | 0 | 0 |
| 21. Upward/Downward reestimates of credit subsidy expense (+/-) | 0 | 0 |
| 22. Increase in exchange revenue receivable from the public (-) | 4,709 | (35,913) |
| 23. Other (+/-) | 578,003 | 3,461,295 |
| 24. Total components of Net Cost of Operations that will Require or Generate Resources in future periods | \$ 589,556 | \$ 3,425,416 |

Components not Requiring or Generating Resources:

| | | |
|--|----------------|----------------|
| 25. Depreciation and amortization | \$ 14,937,472 | \$ 12,136,274 |
| 26. Revaluation of assets or liabilities (+/-) | 0 | 0 |
| 27. Other (+/-) | | |
| 27a. Trust Fund Exchange Revenue | 0 | 0 |
| 27b. Cost of Goods Sold | 0 | 0 |
| 27c. Operating Material and Supplies Used | 8,060 | (4) |
| 27d. Other | (1,335,778) | (1,872,477) |
| 28. Total Components of Net Cost of Operations that will not Require or Generate Resources | \$ 13,609,754 | \$ 10,263,793 |
| 29. Total components of Net Cost of Operations that will not Require or Generate Resources in the current period | \$ 14,199,310 | \$ 13,689,209 |
| 30. Net Cost of Operations | \$ 149,237,965 | \$ 151,468,342 |

Information Related to the Reconciliation of Net Cost of Operations to Budget

Required Disclosures

Due to the limitations of the Army General Fund financial systems, budgetary data do not agree with proprietary expenses and capitalized assets. The difference between budgetary and proprietary data is a previously identified deficiency.

The amount of the adjustment to the note schedule to bring it into balance with the Statement of Net Cost totaled \$835.8 million and was reported in the category of Other Components Not Requiring or Generating Resources.

The Reconciliation of Net Cost of Operations to Budget is intended to explain and define the relationship between net obligations from budgetary accounting and net cost of operations from proprietary accounting. The following Reconciliation of Net Cost of Operations to Budget lines are presented as combined instead of consolidated, as intra-agency budgetary transactions are not 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

Budgetary Resources Obligated, Other include (1) other gains and losses and (2) gains and losses on disposition of assets which resulted from adjustments necessary to balance the Army General Fund's feeder systems with DoD's financial reporting system and to correct inherent limitations of the current financial systems.

Other Resources or Adjustments to Net Obligated Resources that do not affect Net Cost of Operations, Other include financing sources transferred in and out without reimbursement, other gains and losses, and gains and losses on disposition of assets.

Components Requiring or Generating Resources in Future Period, Other represent increases in future-funded expenses for conventional disposal costs and contingent liabilities for contract appeals and tort claims.

Components not Requiring or Generating Resources, Other are comprised of other expenses not requiring budgetary resources for the Iraqi Relief and Reconstruction Fund--a transfer fund in which the Army General Fund executes the funding on behalf of the Executive Office of the President. The U.S. Treasury requires that the execution for this type of transfer is presented on the Army General Fund financial statements. This line also includes the current year change in Construction-in-Progress balances.

NOTE 22. DISCLOSURES RELATED TO INCIDENTAL CUSTODIAL COLLECTIONS

The Army General Fund does not collect incidental custodial revenues.

NOTE 23. FUNDS FROM DEDICATED COLLECTIONSAs of September 30 (*Amounts in thousands*)**BALANCE SHEET****ASSETS**

| | 2016 | | |
|----------------------------------|------------------|--------------|--------------------|
| | Total Funds | Eliminations | Consolidated Total |
| Fund balance with Treasury | \$ 62,474 | \$ 0 | \$ 62,474 |
| Investments | 2,257 | 0 | 2,257 |
| Accounts and Interest Receivable | 0 | 0 | 0 |
| Other Assets | 152 | 0 | 152 |
| Total Assets | \$ 64,883 | \$ 0 | \$ 64,883 |

LIABILITIES and NET POSITION

| | | | |
|---|-------------------|-------------|-------------------|
| Accounts Payable and Other Liabilities | (2,210) | 0 | (2,210) |
| Total Liabilities | \$ (2,210) | \$ 0 | \$ (2,210) |
| Unexpended Appropriations | 0 | 0 | 0 |
| Cumulative Results of Operations | 67,093 | 0 | 67,093 |
| Total Liabilities and Net Position | \$ 64,883 | \$ 0 | \$ 64,883 |

STATEMENT OF NET COST

For the period ended September 30

| | | | |
|---|------------------|-------------|------------------|
| Program Costs | \$ 10,166 | \$ 0 | \$ 10,166 |
| Less Earned Revenue | 0 | 0 | 0 |
| Net Program Costs | \$ 10,166 | \$ 0 | \$ 10,166 |
| Less Earned Revenues Not Attributable to Programs | 0 | 0 | 0 |
| Net Cost of Operations | \$ 10,166 | \$ 0 | \$ 10,166 |

STATEMENT OF CHANGES IN NET POSITION

For the period ended September 30

| | | | |
|--------------------------------------|------------------|-------------|------------------|
| Net Position Beginning of the Period | \$ 55,779 | \$ 0 | \$ 55,779 |
| Net Cost of Operations | 10,166 | 0 | 10,166 |
| Budgetary Financing Sources | 31,503 | 0 | 31,503 |
| Other Financing Sources | (10,023) | 0 | (10,023) |
| Change in Net Position | \$ 11,314 | \$ 0 | \$ 11,314 |
| Net Position End of Period | \$ 67,093 | \$ 0 | \$ 67,093 |

As of September 30 (Amounts in thousands)

BALANCE SHEET

ASSETS

| | 2015 | | |
|----------------------------------|------------------|--------------|--------------------|
| | Total Funds | Eliminations | Consolidated Total |
| Fund balance with Treasury | \$ 58,797 | \$ 0 | \$ 58,797 |
| Investments | 2,177 | 0 | 2,177 |
| Accounts and Interest Receivable | 0 | 0 | 0 |
| Other Assets | (77) | 0 | (77) |
| Total Assets | \$ 60,897 | \$ 0 | \$ 60,897 |

LIABILITIES and NET POSITION

| | | | |
|---|------------------|-------------|------------------|
| Accounts Payable and Other Liabilities | 5,117 | 0 | 5,117 |
| Total Liabilities | \$ 5,117 | \$ 0 | \$ 5,117 |
| Unexpended Appropriations | 0 | 0 | 0 |
| Cumulative Results of Operations | 55,780 | 0 | 55,780 |
| Total Liabilities and Net Position | \$ 60,897 | \$ 0 | \$ 60,897 |

STATEMENT OF NET COST

For the period ended September 30

| | | | |
|---|------------------|-------------|------------------|
| Program Costs | \$ 11,158 | \$ 0 | \$ 11,158 |
| Less Earned Revenue | (52) | 0 | (52) |
| Net Program Costs | \$ 11,106 | \$ 0 | \$ 11,106 |
| Less Earned Revenues Not Attributable to Programs | 0 | 0 | 0 |
| Net Cost of Operations | \$ 11,106 | \$ 0 | \$ 11,106 |

STATEMENT OF CHANGES IN NET POSITION

For the period ended September 30

| | | | |
|--------------------------------------|------------------|-------------|------------------|
| Net Position Beginning of the Period | \$ 37,731 | \$ 0 | \$ 37,731 |
| Net Cost of Operations | 11,106 | 0 | 11,106 |
| Budgetary Financing Sources | 26,948 | 0 | 26,948 |
| Other Financing Sources | 2,207 | 0 | 2,207 |
| Change in Net Position | \$ 18,049 | \$ 0 | \$ 18,049 |
| Net Position End of Period | \$ 55,780 | \$ 0 | \$ 55,780 |

Information Related to Funds from Dedicated Collections

Funds from dedicated collections are financed by specifically identified revenues, required by statute to be used for designated activities or purposes, and remain available over time. The Army General Fund has identified the following such funds and their related statutory citations:

Sale of Hunting and Fishing Permits. Fees are received from individuals for the issuance of special hunting and fishing permits. The funds for this account are used for wildlife, fish, and game conservation and rehabilitation on military reservations. Title 10, United States Code (USC) 670b gives the authority to collect and distribute funds for the intended purposes.

Restoration of Rocky Mountain Arsenal. Funds are received from private industry for the cleanup of contaminated areas of Rocky Mountain Arsenal. Public Law (PL) 99 661, Section 1367, provides the authority for this explicit use.

Royalties for Use of DoD-Military Insignia and Trademarks. Funds are received from the sale of commemorative memorabilia, trademarks, and licensing activities. The funds are used to replenish inventory stock for such items and other related commemorative program expenses. The authority to create expenditures originates from PL 102 484, Section 378.

Forest and Wildlife Conservation, Military Reservations. Funds are received from the sales of forest products harvested from forests on military installations and distributed to the respective states involved in the sales. Each state is entitled to 40% of the sales of products from its forest after reimbursement of DoD appropriations for the costs of production. Title 10, USC 2665 provides authority for this fund and for payments to the states.

National Science Center. Funds received from the collection of fees are used for the operation and maintenance of the National Science Center as authorized under PL 99-145, Defense Authorization Act, 1986, Section 1459.

Bequest of Major General Fred C. Ainsworth to Walter Reed Army Medical Center. Funds received from interest on investments are used for purchasing supplies and equipment for the library at the Walter Reed Army Medical Center. The Army cannot currently identify the statutory citation that provides authority for the use of this fund. The appropriation for this fund is 21X8063.

Department of the Army General Gift Fund. Funds are received from private parties and estates are used for various purposes. Title 10, USC 2601 establishes the authority governing the use of this fund.

NOTE 24. FIDUCIARY ACTIVITIES

Schedule of Fiduciary Activity

For the Years Ended September 30

(Amounts in thousands)

| | 2016 | 2015 |
|--|-------------|----------|
| 1. Fiduciary net assets, beginning of year | \$ 5,281 | \$ 4,790 |
| 2. Fiduciary revenues | 0 | 0 |
| 3. Contributions | (526) | 382 |
| 4. Investment earnings | 0 | 0 |
| 5. Gain (Loss) on disposition of investments, net | 0 | 0 |
| 6. Administrative and other expenses | 0 | 0 |
| 7. Distributions to and on behalf of beneficiaries | (15,142) | 109 |
| 8. Increase/(Decrease) in fiduciary net assets | \$ (15,668) | \$ 491 |
| 9. Fiduciary net assets, end of period | \$ (10,387) | \$ 5,281 |

Schedule of Fiduciary Net Assets

As of September 30

(Amounts in thousands)

FIDUCIARY ASSETS

| | | |
|------------------------------|-------------|----------|
| 1. Cash and cash equivalents | \$ (10,387) | \$ 5,281 |
| 2. Investments | 0 | 0 |
| 3. Other Assets | 0 | 0 |

FIDUCIARY LIABILITIES

| | | |
|----------------------|------|------|
| 4. Less: LIABILITIES | \$ 0 | \$ 0 |
|----------------------|------|------|

5. TOTAL FIDUCIARY NET ASSETS

| | |
|-------------|----------|
| \$ (10,387) | \$ 5,281 |
|-------------|----------|

Fiduciary activities are those Federal Government activities that relate to the collection or receipt of cash or other assets in which nonfederal individuals or entities have an ownership interest that the Federal Government must uphold. Fiduciary activities also include managing, protecting, accounting for, investing, and disposing of such cash or other assets. The DoD has a fiduciary duty to the Savings Deposit Program in which the Army General Fund participates. Public Law 89-538 authorizes DoD, through the Savings Deposit Program, to collect a voluntary allotment from the current pay of members of the armed forces deployed outside the United States or its possessions in designated areas. The Army General Fund collects the savings and allotments of soldiers, and the collections and accrued earned interest are transferred to the Navy General Fund, the program's executive agent. These fiduciary assets are not assets of the Army General Fund and are not recognized on its Balance Sheet. Detail on contributions and distributions on behalf of beneficiaries are provided by the U.S. Treasury.

The fiduciary activity (contributions less distributions to and on behalf of beneficiaries) amount is provided by the U.S. Treasury. The true balance should not be abnormal and research is underway to identify the necessary corrective action.

NOTE 25. OTHER DISCLOSURES

The Army General Fund has no other required disclosures.

NOTE 26. RESTATEMENTS

The Army General Fund has no prior periods restatements.



FISCAL YEAR 2016 REQUIRED SUPPLEMENTARY STEWARDSHIP INFORMATION

The following summarizes nonfederal physical property. Investments in non-federal physical property refer to those expenses incurred by the Army for the purchase, construction, or major renovation of physical property owned by state and local governments, including major additions, alterations, and replacements; the purchase of major equipment; and the purchase of improvement to other physical assets. A schedule of estimated investments values of state and local government-owned properties that are used by the federal government is shown below.

Nonfederal Physical Property: Yearly Investments in State and Local Governments for Fiscal Years 2012 through 2016

(Amounts in millions)

| Categories | FY 2016 | FY 2015 | FY 2014 | FY 2013 | FY 2012 |
|-------------------------------------|---------------|---------------|---------------|---------------|---------------|
| Transferred Assets: | | | | | |
| 1. National Defense Mission-Related | \$21.2 | \$21.2 | \$21.2 | \$20.8 | \$32.4 |
| Funded Assets: | | | | | |
| 2. National Defense Mission-Related | 0 | 0 | 0 | 0 | 0 |
| Totals | \$21.2 | \$21.2 | \$21.2 | \$20.8 | \$32.4 |

The Army General Fund incurs investments in nonfederal physical property for the purchase, construction, or major renovation of physical property owned by state and local governments, including major additions, alterations, and replacements; the purchase of major equipment; and the purchase or improvement of other nonfederal assets. In addition, nonfederal physical property investments include federally-owned physical property transferred to state and local governments.

Investment values included in this report are based on nonfederal physical property outlays (expenditures). Outlays are used because current DoD accounting systems are unable to capture and summarize costs in accordance with federal accounting standards.

The following table summarizes basic research, applied research, and development investments and provides examples of each.

Yearly Investments in Research and Development for Fiscal Years 2012 through 2016

(Amounts in millions)

| Categories | FY 2016 | FY 2015 | FY 2014 | FY 2013 | FY 2012 |
|---|----------------|------------------|------------------|------------------|------------------|
| Basic Research | \$453.0 | \$444.3 | \$437.6 | \$354.3 | \$356.5 |
| Applied Research | 1,045.7 | 935.2 | 858.5 | 876.7 | 1,102.4 |
| Development | | | | | |
| Advanced Technology Development | 1,175.6 | 1,128.0 | 1,104.9 | 1,016.3 | 1,151.0 |
| Advanced Component Development and Prototypes | 460.4 | 421.3 | 511.1 | 491.7 | 737.3 |
| Systems Development and Demonstration | 1,870.0 | 1,924.1 | 2,550.4 | 2,962.0 | 2,823.8 |
| Research, Development, Test and Evaluation Management Support | 1,196.0 | 1,268.4 | 1,277.6 | 1,275.3 | 1,320.6 |
| Operational Systems Development | 1,283.2 | 1,270.9 | 1,261.8 | 1,150.3 | 1,173.4 |
| Total | 7,483.9 | \$7,392.2 | \$8,001.9 | \$8,126.6 | \$8,665.0 |

Narrative Statement

Research and development(R&D) programs are classified in the following seven Budget Activities (BAs): Basic Research (BA1), Applied Research (BA2), Advanced Technology Development (BA3), Advanced Component Development and Prototypes (BA4), Systems Development and Validation (BA5), RDTE Management Support (BA6), and Operational Systems Development (BA7). The definition of each type of RDTE Budget Activity and representative examples of the research being conducted in each BA is explained below.

Basic Research (BA1) is the systematic study to gain knowledge or understanding of the fundamental aspects of phenomena and observable facts without specific applications, processes, or products in mind. Basic research includes all scientific study and experimentation directed toward increasing fundamental knowledge and understanding in those fields of the physical, engineering, environmental, and life sciences related to long-term

national security needs. It is farsighted, high payoff research that provides the basis for technological progress. Major outputs are scientific studies and research papers.

The following are two representative program examples for this BA:

Defense Research Sciences (PE 0601102A): This Program Element (PE) builds fundamental scientific knowledge contributing to the sustainment of U.S. Army scientific and technological superiority in land warfighting capability and solving military problems related to long-term national security needs, investigates new concepts and technologies for the Army's future force, and provides the means to exploit scientific breakthroughs and avoid technological surprises. This PE fosters innovation in Army niche areas (e.g., lightweight armor, energetic materials, and night vision capability) and areas where there is no commercial investment due to limited markets (e.g., vaccines for tropical diseases). It also focuses university single investigator research on areas of high interest to the Army (e.g., high-density compact power and novel sensor phenomenologies). The in-house portion of the program capitalizes on the Army's scientific talent and specialized facilities to transition knowledge and technology into appropriate developmental activities. The extramural program leverages the research efforts of other government agencies, academia, and industry.

University and Industry Research Centers (PE 0601104A): This PE fosters university- and industry-based research to provide a scientific foundation for enabling technologies for future force capabilities. Broadly, the work in this PE falls into three categories: Collaborative Technology Alliances/Collaborative Research Alliances (CTAs/CRAs), University Centers of Excellence (COE), and University Affiliated Research Centers (UARCs). The Army formed CTAs to leverage large investments by the commercial sector in basic research areas that are of great interest to the Army. CTAs are industry-led partnerships between industry, academia, and the Army Research Laboratory (ARL) to incorporate the practicality of industry, the expansion of the boundaries of knowledge from universities, and Army scientists to shape, mature, and transition technology relevant to the Army mission. CTAs have been competitively established in the areas of Micro Autonomous Systems Technology (MAST), Network Sciences, Robotics, and Cognition and Neuroergonomics. CRAs are academia-led partnerships, which leverage the cutting-edge innovation found in the academic environment. CRAs have been established in the areas of Multi-Scale Materials Modeling (electronic materials and materials in extreme environments) and in cyber security. The COEs focus on expanding the frontiers of knowledge in research areas where the Army has enduring needs, and couples state-of-the-art research programs at academic institutions with broad-based graduate education programs to increase the supply of scientists and engineers in automotive and rotary wing technology.

Also included in PE 0601104A are Army Educational Outreach Program (AEOP) and activities to stimulate interest in science, math, and technology among middle and high school students. This PE includes support for basic research at three Army UARCs, which have been created to exploit opportunities to advance new capabilities through a sustained long-term multidisciplinary effort. The Institute for Soldier Nanotechnologies focuses on Soldier protection by emphasizing revolutionary materials research for advanced Soldier protection and survivability. The Institute for Collaborative Biotechnologies focuses on enabling network centric-technologies, and broadening the Army's use of biotechnology for the development of bio-inspired materials, sensors, and information processing. The Institute for Creative Technologies is a partnership with academia and the entertainment and gaming industries to leverage innovative research and concepts for training and simulation. Examples of specific research of mutual interest to the entertainment industry and the Army are technologies for realistic immersion in synthetic environments, networked simulation, standards for interoperability, and tools for creating simulated environments. This PE also includes the Historically Black Colleges and Universities and Minority Institution (HBCU/MI) Centers of Excellence that address critical research areas for Army Transformation.

Applied Research (Budget Activity 2) is the systematic study to gain knowledge or understanding necessary for determining the means by which a recognized and specific need may be met. It is the practical application of such knowledge or understanding for the purpose of meeting a recognized need. This research points toward specific military needs with a view toward developing and evaluating the feasibility and practicability of proposed solutions and determining their parameters. Major outputs are scientific studies, investigations, research papers, hardware components, software codes, and limited construction of, or part of, a weapon system to include non-system specific development efforts.

The following are two representative program examples for this BA:

Combat Vehicle and Automotive Technology (PE 0602601A): This PE researches, designs, and evaluates combat and tactical vehicle automotive technologies that enable the Army to have a lighter, more survivable, more mobile, and more deployable force. Project C05 investigates, researches, and evaluates advanced ground vehicle design and occupant protection technologies in such areas as armor concepts, ballistic defeat mechanisms, blast mitigation, survivability modeling and simulation (M&S), hit avoidance, kill avoidance, safety, sensors, counter-measures, instrumentation, and survivability packaging concepts to achieve superior survivability/protection for Soldiers and military ground vehicles. Survivability technologies will be designed for integration into the Modular Active Protection System (MAPS). Project H77 funds the National Automotive Center (NAC), which was chartered by the Secretary of the Army to conduct shared government and industry, or “dual use,” technology programs to leverage commercial investments in automotive technology research and development for Army ground combat and tactical vehicle applications. Project H91 designs, matures, and evaluates a variety of innovative and enabling technologies in the areas of electrical power, thermal management, propulsion, mobility, power for advanced survivability, vehicle diagnostics, fuels, lubricants, water purification, intelligent systems, autonomy-enabled systems, and other component technologies to enhance the mobility, power and energy and reduce the logistic chain of combat and tactical vehicles. This PE executes the Army's Combat Vehicle Prototyping (CVP) program to mature, integrate, and demonstrate ground vehicle leap-ahead technologies in support of future combat vehicles.

Ballistics Technology (PE 0602618A): This Program Element (PE) investigates and evaluates materials and technologies, and designs and develops methodologies and models required to enable enhanced lethality and survivability. Project H80 focuses on applied research of lightweight armors and protective structures for the Soldier and vehicles; kinetic energy active protection; crew and components protection from ballistic shock and mine-blast; insensitive propellants/munitions formulations; novel multi-function warhead concepts; affordable precision munitions design; and techniques, methodologies, and models to analyze combat effectiveness, and identify vulnerabilities of current and emerging technologies; and developing a demonstrator with associated methods and tools for injury prediction of vehicle occupants during under-body blast events.

Advanced Technology Development (Budget Activity 3) is the systematic use of the knowledge or understanding gained from research directed toward proof of technological feasibility and assessment of operations and producibility rather than the development of hardware for service use. It employs demonstration activities intended to prove or test a technology or method and projects within this Budget Activity have a direct relevance to identified military needs.

The following are two representative examples for this BA:

Advanced Tactical Computer Science and Sensor Technology (PE 0603772A): This program element (PE) matures and demonstrates technologies that allow the Warfighter to effectively collect, analyze, transfer, and display situational awareness information in a network-centric battlefield environment. It matures and demonstrates architectures, hardware, software and techniques that enable Synchronized mission command (MC) during rapid, mobile, dispersed, and Joint operations. Project 101 matures software, algorithms, services, and devices to more effectively integrate MC across all echelons and enable more effective utilization of Warfighter resources including intelligent power management and distribution through accelerated information to decisions and rapid MC on the move. Project 243 matures and demonstrates signal processing and information/intelligence fusion software, algorithms, services, and systems for Army sensors; radio frequency (RF) systems to track and identify enemy forces and personnel; and multi-sensor control and correlation software and algorithms to improve reconnaissance, surveillance, tracking, and target acquisition.

Medical Advanced Technology (PE 0603002A): This Program Element (PE) matures and demonstrates advanced medical technologies including drugs, vaccines, medical diagnostic devices, measures for identification and vector control, and developing medical practices and procedures to effectively protect and improve the survivability of United States Forces across the entire spectrum of military operations. Tri-Service coordination and cooperative efforts are focused in four principal medical areas: Combat Casualty Care, Military Operational Medicine, Militarily Relevant Infectious Diseases, and Clinical and Rehabilitative Medicine. Promising medical technologies are refined and validated through extensive testing, which is closely monitored by the U.S. Food and Drug Administration (FDA) and Environmental Protection Agency (EPA), as part of their processes for

licensing and/or approving new medical products. The FDA requires medical products to undergo extensive preclinical testing in animals and/or other models to obtain preliminary effectiveness and safety information before they can be tested in human clinical trials. Clinical trials are conducted in three phases to prove the safety of a drug, vaccine, or device for the targeted disease or medical condition, starting in Phase 1 with a small number of healthy volunteers. Following Phase 1, Phase 2 clinical trials will provide expanded safety data and evaluate the effectiveness of a drug, vaccine, or medical device in a larger population of patients having the targeted disease or medical condition. Each successive phase includes larger numbers of human subjects and requires FDA cognizance prior to proceeding. Work conducted in this PE primarily focuses on late stages of technology maturation activities required to conduct Phases 1 and 2 clinical trials. Some high-risk technologies may require additional maturation with FDA guidance prior to initiating these clinical trials. Such things as proof of product stability and purity are necessary to meet FDA standards before entering later stages of testing and prior to transitioning into a formal acquisition program where large Phase 3 pivotal trials will be conducted for licensure. Activities in this PE may include completion of preclinical animal studies and Phase 1 and 2 clinical studies involving human subjects according to FDA and EPA requirements. Promising medical technologies that are not regulated by the FDA are modeled, prototyped, and tested in relevant environments.

Advanced Component Development and Prototypes (ACD&P, BA 4) evaluates integrated technologies in as realistic an operating environment as possible to assess the performance or cost reduction potential of advanced technology. Programs in this phase are generally system specific. Major outputs of ACD&P are hardware and software components, or complete weapon systems ready for operational and developmental testing and field use.

The following is a representative example for this BA:

Aviation - Advanced Development (PE 0603801A): This program provides advanced development aviation support of tactical programs associated with air mobility, advanced maintenance concepts and equipment, and Aircrew Integrated Systems. This program demonstrates the feasibility and maturity of new technology and gains understanding in order to evaluate utility of this technology to expedite delivery of new capabilities for Army aviation rotary-wing assets. Additionally, the aviation ground support equipment assets enhance the functionality of current and future aircraft by (1) improving the effectiveness of maintenance and servicing operations through validating new maintenance concepts to improve man and machine interfaces; (2) improving aircraft maintenance processes; (3) reducing operation and support costs; and (4) inserting diagnostic technologies to replace obsolete and unsupportable equipment.

System Development and Demonstration (BA5) involves programs that have passed Milestone B approval and are conducting engineering and manufacturing development tasks aimed at meeting validated requirements prior to full-rate production. It consists primarily of pre-production efforts, such as logistics and repair studies. Major outputs are weapons systems finalized for complete operational and developmental testing.

The following is a representative example for this BA:

Patriot/Medium Extended Air Defense System Combined Aggregate Program (CAP) (PE 0604869A): The Medium Extended Air Defense System (MEADS) program is a tri-national, co-development program among the United States, Germany, and Italy to replace the U.S. Patriot air defense systems, Patriot and Hawk systems in Germany, and Nike Hercules systems in Italy. The North Atlantic Treaty Organization (NATO) MEADS Management Agency (NAMEADSMA) is the NATO contracting authority that manages the system acquisition, and the MEADS program, itself, on behalf of participating nations. Within the Patriot/MEADS CAP, there are two synergistic efforts: (1) an international MEADS development effort managed by NAMEADSMA; and (2) a U.S. effort to inject U.S.-specific capability requirements into the MEADS major end items. The MEADS will provide joint and coalition forces with critical asset and defended area protection against multiple and simultaneous attacks by short- to medium-range ballistic missiles, cruise missiles, unmanned aerial vehicles and tactical air-to-surface missiles. The Missile Segment Enhancement (MSE) missile has been accepted as the baseline missile for MEADS. It is being developed for the Patriot system to meet U.S. operational requirements. The MSE will provide a more agile and lethal interceptor that increases the engagement envelope/defended area of the Patriot and the MEADS systems. The PAC-3 MSE improves upon the current PAC-3 missile capability by providing a higher performance solid rocket motor, modified lethality enhancer, more responsive control surfaces, upgraded guidance software, and insensitive munitions improvements.

RDTE Management Support (BA6) is support for installations and operations for general R&D use. This category includes costs associated with test ranges, military construction maintenance support for laboratories, operation and maintenance of test aircraft and ships, and studies and analyses in support of the R&D program.

The following is a representative example for this BA:

Army Test Ranges and Facilities (0605601A): This program funds the indirect test costs associated with rapidly-testing field systems and equipment needed in support of the War on Terror, such as individual Soldier protection equipment and countermeasures for improvised explosive devices (IEDs) and up-armoring the Army's wheeled vehicle fleet. This project sustains the developmental test and evaluation capability required to support Army as well as joint service or other service systems' hardware and technologies. Unclassified systems scheduled for developmental testing encompass the entire spectrum of weapons systems. Capabilities are also required to support system-of-systems and network-centric systems to include future combat system testing.

This project provides the institutional funding required to operate the developmental test activities required by DoD program executive officers; program and product managers; and research, development, and engineering centers. This project resources four DoD major range and test facility bases: White Sands Missile Range, New Mexico; Aberdeen Test Center, Maryland; Electronic Proving Ground, Arizona; and Yuma Proving Ground, Arizona, and includes management of natural environmental testing at Cold Regions Test Center, Fort Greely and Fort Wainwright, Alaska, and the Tropic Regions Test Center at various locations. This project also funds the Army's developmental test capability at Aviation Technical Test Center and Redstone Technical Test Center, Alabama. Test planning and safety verification at Headquarters, U.S. Army Developmental Test Command, Maryland, is also supported by this program.

Operational Systems Development (BA7) includes development efforts to upgrade systems that have been fielded or have received approval for full rate production and anticipate production funding in the current or subsequent fiscal year. All items are major line item projects that appear as RDT&E Costs of Weapon System Elements in other programs.

The following is a representative example for this BA:

Information Systems Security Program (0303140A): The Communications Security Equipment Program develops information systems security (ISS) equipment and techniques required to combat threat signal intelligence capabilities and to ensure the integrity of data networks. The Army's Research, Development, Test, and Evaluation ISS program objective is to implement National Security Agency-developed security technology in Army information systems. Communications security equipment technology ensures total signal and data security for all Army information systems to include any operational enhancement and specialized configurations.

FISCAL YEAR 2016 REQUIRED SUPPLEMENTARY INFORMATION

Real Property Deferred Maintenance and Repairs

For Fiscal Years Ended September 30, 2016 & September 30, 2015

(Amounts in millions)

| Property Type | Prior Fiscal Year (PFY) 2015 | | | Current Fiscal Year (CFY) 2016 | | |
|---------------|------------------------------|---|--|--------------------------------|---|--|
| | Plant Replacement Value | Required Work (Deferred maintenance and repair) | Percentage (Required Work/Plant Replacement Value) | Plant Replacement Value | Required Work (Deferred maintenance and repair) | Percentage (Required Work/Plant Replacement Value) |
| Category 1 | \$239,967 | \$27,677 | 12% | \$351,173 | \$53,842 | 15% |
| Category 2 | \$100 | \$8 | 8% | \$6,272 | \$1,890 | 30% |
| Category 3 | \$5,376 | \$1,417 | 26% | \$16,719 | \$4,683 | 28% |

Narrative Statement

Per DoD Financial Management Regulation 7000.14-R (February 2012), Volume 6B, Chapter 12; Para 120302. B.1., the Army's deferred maintenance estimates for FY 2016 include all facilities in which DoD has ownership interest under the control of the Army.

The deferred maintenance estimates are based on the facility Q-ratings reported in the Installation Status Report (ISR) 4th Quarter 2016 or Q-ratings obtained by application of business rules described below. For FY 2016, the Q-rating values range from 0 to 100. Deferred maintenance and repair is calculated as follows:

$$\text{Deferred Maintenance and Repair} = (100 - \text{Q-rating}) \times 0.01 \times \text{plant replacement value (PRV)}.$$

Q-ratings are determined by the ISR for the majority of facilities, and by business rule for the remaining facilities. During ISR data collection, facility occupants evaluate the condition of each facility against published standards. The inspection generates a quality improvement cost estimate for each facility based on the condition rating of each component of the facility, and the component improvement cost factor. Improvement cost factors are developed using industry standards for each facility component within each facility type. The business rule assignment of Q-ratings is as follows: 95 if the facility is no more than 5 years old; 85 if the facility is permanent or semi-permanent construction and between 5 and 15 years old; 70 if the facility is permanent or semi-permanent construction and more than 15 years old; 40 if the facility is temporary construction and more than 5 years old; 95 if the asset is a lease. For assets with a Non-Functional operational status, assigned Q-ratings are 95 if the reason code is RENO, 70 if the reason code is ENVR, and 40 if the reason code is DAMG. Acceptable operating condition represents facilities with no deferred maintenance.

Facilities with an ownership interest of "FEE" and "ONFG" are included in the data set; relocatable buildings are excluded.

Property Categories are as follows:

- ☐ Category 1: Buildings, Structures, and Utilities that are enduring and required to support an ongoing mission including multi-use Heritage Assets. (Fee owned facilities that are Permanent, Semi-Permanent, or Temporary with an Operational Status of "Active" or "Semi-Active" are included, less those with a disposal reason code other than blank.)
- ☐ Category 2: Buildings, Structures, and Utilities that are Heritage Assets – these have an operational status of closed and are not maintained. (Facilities with an Operational Status of "Closed" as well as a historical status code indicating the asset has been determined to have historic/ architectural/ cultural significance or "NEV" for not yet evaluated. Codes of DNR (designation rescinded), DNE (not eligible), NCE (non-contributing element) and blanks are excluded.)
- ☐ Category 3: Buildings, Structures, and Utilities that are excess to requirements or planned for replacement or disposal including multi-use Heritage Assets. (Facilities with an Operational Status of "Caretaker", "Excess", "Non-Functional", "Out-grant", "Surplus", plus "Closed" non-heritage assets plus "Active" and "Semi-active" with a disposal reason code.)

The increase in the overall deferred maintenance estimates in FY 2016 is due to two factors. Prior to FY 2016 deferred maintenance estimates were determined only for assets which had been inspected; FY 2016 estimates also include business rule rated assets not generally inspected. In addition, component improvement cost factors now more appropriately incorporate the Office of the Undersecretary of Defense predominant use methodology.

Equipment Deferred Maintenance and Repair for Fiscal Year Ended September 30, 2016

(Amounts in thousands)

| Major Categories | PY (FY15) DM&R | CY (FY16) OP-30/PB-45/ PB-61 Amounts | Adjustments | CY (FY16) Totals |
|--|------------------|---|-------------|------------------|
| Aircraft | \$0 | \$151 | \$0 | \$151 |
| Automotive Equipment | 306,355 | 344,215 | 0 | 344,215 |
| Combat Vehicles | 10,740 | 186,947 | 0 | 186,947 |
| Construction Equipment | 5,831 | 18,022 | 0 | 18,022 |
| Electronics and Communications Systems | 9,771 | 26,015 | 0 | 26,015 |
| General Purpose Equipment | 461,989 | 239,140 | 0 | 239,140 |
| Missiles | 193 | 30,236 | 0 | 30,236 |
| Ordnance Weapons and Munitions | 33,994 | 7,380 | 0 | 7,380 |
| Other | 10,504 | 65,382 | 0 | 65,382 |
| Ships | 0 | 341 | 0 | 341 |
| Grand Total | \$839,377 | \$917,829 | \$0 | \$917,829 |

The OP-30 from the FY 2016 president's budget was used to compile the deferred depot level maintenance.

Depot Maintenance Operations and Planning System is the automated system for capturing depot-level deferred maintenance data. The data is for subactivity group 123, all active components.

Funding provided to support the Program Objective Memorandum (POM) 12-16 for depot maintenance adequately supported the Army's most critical modernization and equipping strategies. The program ensured that Soldiers have the equipment needed to execute their assigned mission as they progress through the Army Force Generation (ARFORGEN) cycle. The bottom-line is that depot maintenance requirements continue to grow while the Army continues to get fewer resources with reduced budgets.

The funding also provided the resources necessary for Land Forces Depot Maintenance to meet the requirements of an Army transitioning from operations in theater to home station training – an expeditionary Army engaged in full spectrum operation (FSO) training and poised for future contingency response. In recent years, the Army has leveraged Overseas Contingency Operation (OCO) dollars to offset depot maintenance through equipment reset for redeploying units. Redeployed units will demand greater equipment to support FSO training and future contingencies. To meet the exigencies of war, Army has generated a digitally dependent force. The digitally integrated Army of today is far different from the analog Army that went to war at the beginning of the decade. These technologies must now be sustained.

Heritage Assets and Stewardship Land Condition Information for Fiscal Year Ended September 30, 2016

The conditions of archeological sites across the Army remain varied from poor to excellent based on a number of factors including the environmental setting and natural disasters, the type of the site, and impacts from Army activities. If an Army activity has the potential to adversely impact an archeological site eligible for the National Register, the Garrison's Installation Cultural Resources Management Plan (ICRMP) contains provisions for how the installation might proceed to avoid, minimize, or mitigate those impacts. The ICRMPs provide installations the information and tools necessary to manage their cultural resources, including archeological sites, in compliance with federal requirements. These plans provide for site protection, site condition monitoring, and mitigation procedures for adverse impacts to sites. Overall, the conditions of sites on Army installations are fair, based on the Army's cultural resource management procedures.

STATEMENT OF DISAGGREGATED BUDGETARY RESOURCES

For the Years Ended September 30, 2016 and 2015

| <i>(Amounts in thousands)</i> | Research, Development, Test & Evaluation | Procurement | Military Personnel | Family Housing & Military Construction |
|--|---|---------------|--------------------|---|
| Budgetary Resources: | | | | |
| Unobligated balance brought forward, Oct 1 | \$ 3,560,683 | \$ 8,731,883 | \$ 1,287,803 | \$ 5,869,809 |
| Adjustment to unobligated balance, brought forward, Oct 1 (+ or -) | | | | |
| Unobligated balance brought forward, Oct 1, as adjusted | \$ 3,560,683 | \$ 8,731,883 | \$ 1,287,803 | \$ 5,869,809 |
| Recoveries of prior year unpaid obligations | 775,648 | 2,782,267 | 4,924,481 | 861,409 |
| Other changes in unobligated balance (+ or -) | (477,199) | (668,943) | (697,467) | (30,373) |
| Unobligated balance from prior year budget authority, net | \$ 3,859,132 | \$ 10,845,207 | \$ 5,514,817 | \$ 6,700,845 |
| Appropriations (discretionary and mandatory) | 7,852,444 | 18,444,578 | 57,935,519 | 1,142,352 |
| Spending Authority from offsetting collections (discretionary and mandatory) | 4,279,140 | 1,939,488 | 331,118 | 4,281,354 |
| Total Budgetary Resources | \$ 15,990,716 | \$ 31,229,273 | \$ 63,781,454 | \$ 12,124,551 |
| Status of Budgetary Resources: | | | | |
| New obligations and upward adjustments (total) | \$ 12,491,037 | \$ 22,376,650 | \$ 62,509,395 | \$ 6,578,738 |
| Unobligated balance, end of year | | | | |
| Apportioned, unexpired accounts | 2,601,517 | 7,556,262 | 84,132 | 4,064,559 |
| Exempt from apportionment, unexpired accounts | 0 | 0 | 0 | 0 |
| Unapportioned, unexpired accounts | 0 | 52,291 | 0 | 97,584 |
| Unexpired unobligated balance, end of year | 2,601,517 | 7,608,553 | 84,132 | 4,162,144 |
| Expired unobligated balance, end of year | 898,162 | 1,244,069 | 1,187,927 | 1,383,669 |
| Total unobligated balance, end of year | \$ 3,499,679 | \$ 8,852,622 | \$ 1,272,059 | \$ 5,545,813 |
| Total Budgetary Resources | \$ 15,990,716 | \$ 31,229,272 | \$ 63,781,454 | \$ 12,124,551 |
| Change in Obligated Balance: | | | | |
| Unpaid obligations: | | | | |
| Unpaid obligations, brought forward, Oct 1 | \$ 7,581,473 | \$ 24,997,018 | \$ 6,465,946 | \$ 9,930,086 |
| New obligations and upward adjustments | 12,491,038 | 22,376,650 | 62,509,395 | 6,578,738 |
| Outlays (gross) (-) | (11,587,278) | (18,238,500) | (59,203,224) | (6,494,899) |
| Recoveries of prior year unpaid obligations (-) | (775,648) | (2,782,267) | (4,924,481) | (861,409) |
| Unpaid obligations, end of year | 7,709,585 | 26,352,901 | 4,847,636 | 9,152,516 |
| Uncollected payments: | | | | |
| Uncollected payments, Fed sources, brought forward, Oct 1 (-) | (3,512,978) | (3,341,534) | (31,713) | (8,166,629) |
| Change in uncollected payments, Fed sources (+ or -) | (212,266) | 83,177 | (28) | 416,044 |
| Uncollected payments, Fed sources, end of year (-) | (3,725,244) | (3,258,357) | (31,741) | (7,750,585) |
| Memorandum Entries: | | | | |
| Obligated balance, start of year (+ or -) | \$ 4,068,496 | \$ 21,655,484 | \$ 6,434,233 | \$ 1,763,457 |
| Obligated balance, end of year (+ or -) | \$ 3,984,341 | \$ 23,094,544 | \$ 4,815,896 | \$ 1,401,931 |
| Budget Authority and Outlays, Net: | | | | |
| Budget authority, gross (discretionary and mandatory) | \$ 12,131,584 | \$ 20,384,066 | \$ 58,266,637 | \$ 5,423,706 |
| Actual offsetting collections (discretionary and mandatory) (-) | (4,071,307) | (2,024,226) | (331,157) | (4,697,398) |
| Change in uncollected customer payments from Federal Sources (discretionary and mandatory) (+ or -) | (212,267) | 83,177 | (28) | 416,044 |
| Recoveries of prior year paid obligations (discretionary and mandatory) | 4,433 | 1 | 67 | 0 |
| Budget Authority, net (discretionary and mandatory) | \$ 7,852,443 | \$ 18,443,018 | \$ 57,935,519 | \$ 1,142,352 |
| Outlays, gross (discretionary and mandatory) | 11,587,278 | 18,238,500 | 59,203,224 | 6,494,899 |
| Actual offsetting collections (discretionary and mandatory) (-) | (4,071,307) | (2,024,226) | (331,157) | (4,697,398) |
| Outlays, net (discretionary and mandatory) | 7,515,971 | 16,214,274 | 58,872,067 | 1,797,501 |
| Distributed offsetting receipts (-) | 0 | 0 | 0 | 0 |
| Agency Outlays, net (discretionary and mandatory) | \$ 7,515,971 | \$ 16,214,274 | \$ 58,872,067 | \$ 1,797,501 |

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

Department of Defense –Department of the Army

STATEMENT OF DISAGGREGATED BUDGETARY RESOURCES

For the Years Ended September 30, 2016 and 2015

*(Amounts in thousands)***Budgetary Resources:**

| | Operations, Readiness & Support | 2016 Combined | 2015 Combined |
|--|---------------------------------|----------------|----------------|
| Unobligated balance brought forward, Oct 1 | \$ 15,780,636 | \$ 35,230,814 | \$ 42,912,597 |
| Adjustment to unobligated balance, brought forward, Oct 1 (+ or -) | | | |
| Unobligated balance brought forward, Oct 1, as adjusted | \$ 15,780,636 | \$ 35,230,814 | \$ 42,912,597 |
| Recoveries of prior year unpaid obligations | 10,188,077 | 19,531,882 | 19,843,020 |
| Other changes in unobligated balance (+ or -) | (2,948,392) | (4,822,374) | (8,014,898) |
| Unobligated balance from prior year budget authority, net | \$ 23,020,321 | \$ 49,940,322 | \$ 54,740,719 |
| Appropriations (discretionary and mandatory) | 62,078,401 | 147,453,294 | 147,266,432 |
| Spending Authority from offsetting collections (discretionary and mandatory) | 10,511,375 | 21,342,475 | 17,448,318 |
| Total Budgetary Resources | \$ 95,610,097 | \$ 218,736,091 | \$ 219,455,469 |

Status of Budgetary Resources:

| | | | |
|--|---------------|----------------|----------------|
| New obligations and upward adjustments (total) | \$ 81,056,119 | \$ 185,011,939 | \$ 184,224,655 |
| Unobligated balance, end of year | | | |
| Apportioned, unexpired accounts | 1,972,878 | 16,279,348 | 17,476,932 |
| Exempt from apportionment, unexpired accounts | 33,498 | 33,498 | 34,321 |
| Unapportioned, unexpired accounts | 9,228 | 159,103 | 351,578 |
| Unexpired unobligated balance, end of year | 2,015,603 | 16,471,949 | 17,862,831 |
| Expired unobligated balance, end of year | 12,538,376 | 17,252,203 | 17,367,983 |
| Total unobligated balance, end of year | \$ 14,553,979 | \$ 33,724,152 | \$ 35,230,814 |
| Total Budgetary Resources | \$ 95,610,098 | \$ 218,736,091 | \$ 219,455,469 |

Change in Obligated Balance:**Unpaid obligations:**

| | | | |
|---|---------------|---------------|----------------|
| Unpaid obligations, brought forward, Oct 1 | \$ 50,843,777 | \$ 99,818,300 | \$ 111,937,128 |
| New obligations and upward adjustments | 81,056,118 | 185,011,939 | 184,224,655 |
| Outlays (gross) (-) | (74,189,738) | (169,713,639) | (176,500,463) |
| Recoveries of prior year unpaid obligations (-) | (10,188,077) | (19,531,882) | (19,843,020) |
| Unpaid obligations, end of year | 47,522,080 | 95,584,718 | 99,818,300 |

Uncollected payments:

| | | | |
|---|-------------|--------------|--------------|
| Uncollected payments, Fed sources, brought forward, Oct 1 (-) | (7,873,589) | (22,926,443) | (26,393,857) |
| Change in uncollected payments, Fed sources (+ or -) | (1,722,145) | (1,435,218) | 3,467,414 |
| Uncollected payments, Fed sources, end of year (-) | (9,595,734) | (24,361,661) | (22,926,443) |

Memorandum Entries:

| | | | |
|---|---------------|---------------|---------------|
| Obligated balance, start of year (+ or -) | \$ 42,970,187 | \$ 76,891,857 | \$ 85,543,271 |
| Obligated balance, end of year (+ or -) | \$ 37,926,345 | \$ 71,223,057 | \$ 76,891,857 |

Budget Authority and Outlays, Net:

| | | | |
|---|---------------|----------------|----------------|
| Budget authority, gross (discretionary and mandatory) | \$ 72,589,776 | \$ 168,795,769 | \$ 164,714,750 |
| Actual offsetting collections (discretionary and mandatory) (-) | (8,809,148) | (19,933,236) | (21,029,321) |
| Change in uncollected customer payments from Federal Sources (discretionary and mandatory) (+ or -) | (1,722,144) | (1,435,218) | 3,467,414 |
| Recoveries of prior year paid obligations (discretionary and mandatory) | 19,919 | 24,420 | 115,150 |
| Budget Authority, net (discretionary and mandatory) | \$ 62,078,403 | \$ 147,451,735 | \$ 147,267,993 |
| Outlays, gross (discretionary and mandatory) | 74,189,738 | 169,713,639 | 176,500,463 |
| Actual offsetting collections (discretionary and mandatory) (-) | (8,809,148) | (19,933,236) | (21,029,321) |
| Outlays, net (discretionary and mandatory) | 65,380,590 | 149,780,403 | 155,471,142 |
| Distributed offsetting receipts (-) | (362,062) | (362,062) | (930,148) |
| Agency Outlays, net (discretionary and mandatory) | \$ 65,018,528 | \$ 149,418,341 | \$ 154,540,994 |

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





INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
4800 MARK CENTER DRIVE
ALEXANDRIA, VIRGINIA 22350-1500

November 9, 2016

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

SUBJECT: Independent Auditor's Report on the Army General Fund FY 2016
and FY 2015 Basic Financial Statements
(Project No. D2016-D000FI-0136.000, Report No. DODIG-2017-010)

Report on the Basic Financial Statements

Public Law 101-576, "Chief Financial Officers Act of 1990," as amended, requires the DoD Inspector General to audit the accompanying Army General Fund consolidated balance sheet as of September 30, 2016, and 2015, and the related consolidated statement of net cost, consolidated statement of changes in net position, combined statement of budgetary resources, and notes to the basic statements (basic financial statements).

Management's Responsibility for the Annual Financial Statements

Army management is responsible for the annual financial statements. Management is responsible for (1) preparing financial statements that conform with U.S. generally accepted accounting principles (U.S. GAAP); (2) establishing, maintaining, and assessing internal control to provide reasonable assurance that they met broad control objectives of Public Law 97-255, "Federal Managers' Financial Integrity Act of 1982" (FMFIA); (3) ensuring that the Army's financial management systems substantially comply with Public Law 104-208, "Federal Financial Management Improvement Act of 1996" (FFMIA) requirements; and (4) complying with applicable laws and regulations.

Auditor's Responsibility

Our responsibility is to express an opinion on the basic financial statements based on conducting the audit in accordance with generally accepted government auditing standards and the Office of Management and Budget (OMB) Bulletin No. 15-02, "Audit Requirements for Federal Financial Statements," August 4, 2015. However, based on the matters described in the Basis for Disclaimer of Opinion paragraph, we were unable to obtain sufficient appropriate evidence to provide a basis for the audit opinion.

Basis for Disclaimer of Opinion

Section 1008(d) of the FY 2002 National Defense Authorization Act limits the DoD Inspector General to performing only those audit procedures required by generally accepted government auditing standards that are consistent with the representations made by management. Army management asserted to us that the Army General Fund FY 2016 and FY 2015 Basic Financial Statements would not substantially conform to U.S. GAAP and that Army General Fund financial management and feeder systems were unable to adequately support material amounts on the basic financial statements as of September 30, 2016. Accordingly, we did not perform all the auditing procedures required by generally accepted government auditing standards and OMB Bulletin No. 15-02 to determine whether material amounts on the basic financial statements were presented fairly. We considered the scope limitation in forming our conclusions on the basic financial statements.

Disclaimer of Opinion

Because of the significance of the matters described in the Basis for Disclaimer of Opinion paragraph, we could not obtain sufficient appropriate evidence to provide a basis for an audit opinion. Accordingly, we do not express an opinion on the Army General Fund FY 2016 and FY 2015 Basic Financial Statements. Thus, the basic financial statements may have undetected misstatements that are both material and pervasive.

Other Information in the Annual Financial Statements

We performed our audit to form an opinion on the basic financial statements as a whole. Army management presented the Management's Discussion and Analysis, Required Supplementary Stewardship Information, Required Supplementary Information, and Other Information for additional analysis as part of the annual financial statements. These elements are not required parts of the basic financial statements. Therefore, we do not express an opinion or provide any assurance on the information. We reviewed the other information for inconsistencies with the audited basic financial statements.

Based on our limited review, we found material inconsistencies between the information and the basic financial statements and applicable sections of OMB Circular No. A-136, (Revised), "Financial Reporting Requirements," October 7, 2016, and DoD Regulation 7000.14-R, "Financial Management Regulation," volume 6b, "Form and Content of the Department of Defense Audited Financial Statements." Specifically, Management's Discussion and Analysis did not contain sufficient information specific to the Army General Fund to meet guidance requirements.

Report on Compliance With Applicable Provisions of Laws, Regulations, Contracts, and Grant Agreements

We limited our audit to determining compliance with provisions of applicable laws and regulations, contracts, and grant agreements that have a direct and material effect on the basic financial statements, and compliance with OMB regulations and audit requirements for financial reporting because management represented that instances of noncompliance identified in prior audits continue to exist. Therefore, we did not determine whether the Army General Fund complied with all applicable laws and regulations, contracts, and grant agreements related to financial reporting. It was not our objective to provide an opinion on compliance with certain provisions of laws and regulations, contracts, and grant agreements, and accordingly, we do not express such an opinion.

See Attachment 1 for additional details on internal control and compliance with legal and other regulatory requirements.

Agency Comments and Our Evaluation

We provided a draft of this report to the Deputy Assistant Secretary of the Army (Financial Operations), who provided technical comments we have incorporated, as appropriate. The Deputy Assistant Secretary expressed continuing commitment to address the problems this report outlines. See Attachment 2 for the full text of the management comments.

This report will be made publicly available pursuant to section 8M, paragraph (b)(1)(A) of the Inspector General Act of 1978, as amended. However, this report is intended solely for the information and use of Congress; the OMB; the U.S. Government Accountability Office; the Under Secretary of Defense (Comptroller)/Chief Financial Officer, DoD; Army management; and the DoD Office of Inspector General. It is not intended to be used and should not be used by anyone else.

We appreciate the courtesies extended to the staff. Please direct questions to me at (703) 601-5945 or (DSN) 329-5945.



Lorin T. Venable, CPA

Assistant Inspector General

Financial Management and Reporting

Attachments: As stated

Report on Internal Control Over Financial Reporting

Internal Control Compliance

In planning our audit, we considered the Army General Fund's internal control over financial reporting. We did this to determine our procedures for auditing the basic financial statements appropriate to the circumstances, for the purposes of expressing our opinion on the basic financial statements, but not appropriate to the purpose of expressing an opinion on the effectiveness of the internal control. Accordingly, we do not express an opinion on internal control over financial reporting.

Management Responsibilities

Management is responsible for implementing and maintaining effective internal controls to include providing reasonable assurance that Army personnel recorded, processed, and summarized accounting data properly; met the requirements of applicable laws and regulations; and safeguarded assets against misappropriation and abuse.

Auditor's Responsibilities

Our purpose was not to express an opinion on internal controls over financial reporting, and we do not do so. However, the following material weaknesses continue to exist that could adversely affect the Army General Fund's financial operations.

Previously Identified Material Weaknesses

Management acknowledged that previously identified material weaknesses continued to exist. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the Army General Fund's financial statements will not be prevented, or detected and corrected, on a timely basis. The following material weaknesses continue to exist.

Financial Management Systems. The Army and its service providers have not implemented sufficient effective information technology controls to protect the Enterprise Resource Planning and related feeder systems financial data. Specifically, the Army and its service provider did not consistently:

- implement application, operating system, and database access controls around the authorization, provisioning, monitoring, and de-activation of end users, super users, and system administrative/backend support users, including the periodic review of user accounts to determine the need for

continued and appropriate access based on least privilege provisions. Furthermore, the Army and its service providers did not consistently implement application, database, and operating system user account and password parameters in accordance with applicable requirements.

- establish comprehensive processes to identify, evaluate, restrict, and document the combination of incompatible application, database, and operating system privileges.
- implement a comprehensive application, operating system, and database configuration change management process, to include timing for installation of critical patch updates and proper configuration of production settings to prevent direct changes from being made in the production environment.
- design and implement a formal vulnerability management program, to include the operating systems and databases supporting the production environment.
- perform effective daily operating system backup procedures and maintain evidence of operating system and database backups when performed for certain financial systems.

Fund Balance With Treasury. The DoD has had long-standing problems in reconciling transaction activity in its Fund Balance with Treasury accounts. Appropriation balances recorded in the accounting records do not agree with balances held at Treasury. Collections and disbursements at the detailed transaction level do not reconcile with the records of the Department of the Treasury.

The Fund Balance with Treasury reconciliation is a key control for supporting the existence, completeness, accuracy of the budgetary authority and outlays reported on the schedule. The monthly reconciliation was not properly designed as follows:

- The Army did not perform a reconciliation at the detailed appropriation level, which compares its proprietary cash to budgetary cash to determine that certain budgetary balances exist, are complete, and are accurate.
- The Army's service provider did not record adjustments at the transactional level to enable the service provider to support the adjustments to account for variances between Treasury and Army records.

- At yearend, a variance existed between the recorded Treasury cash balance and the recorded Army cash balance due to timing differences and adjustments recorded in the general ledger. The Army was unable to provide documents to demonstrate that these differences were resolved.

Accounts Receivable. The Army has not complied with policies and procedures regarding referrals to the Debt Management Office of the Department of the Treasury and for write-offs of 2-year-old debt. There was a lack of controls to ensure all entitlement system receivables (vendor pay, civilian pay, and interest) are recorded in the accounting systems and accounts receivable balances are supportable at the transaction level. The weakness applies to both public and intragovernmental receivables at the Army General Fund-level.

Inventory and Related Property (Operating Materials and Supplies). Army systems do not maintain historical cost data necessary to comply with Statement of Federal Financial Accounting Standards No. 3, "Accounting for Inventory and Related Property." Instead, inventories are valued and reported at approximate historical cost using latest acquisition cost adjusted for holding gains and losses. Army systems are also unable to produce financial transactions using the U.S. Government Standard General Ledger.

General Property, Plant, and Equipment. The Army has acknowledged that it has not recorded real property and military equipment at acquisition or historical cost and did not include all the costs needed to bring these assets to a form and location suitable for their intended use. The Army also does not have an accountability system for all its Military Table of Equipment unit property books that complies with the FFMIA.

Accounts Payable. The Army is unable to account for and report accounts payable properly. Due to the material weakness in accounting and financial feeder systems, the DoD is generally unable to determine whether undistributed disbursements and collections should be applied to federal or nonfederal accounts payable and accounts receivable at the time accounting reports are prepared. Accordingly, DoD policy is to allocate supported undistributed disbursements and collections between Federal and non-Federal categories based on the percentage of distributed federal and nonfederal accounts payable and accounts receivable. Both supported and unsupported undistributed disbursements and collections are then applied to reduce accounts payable and accounts receivable accordingly. In addition, Army accounting systems do

not capture trading partner data at the transaction level in a manner that facilitates trading partner aggregations for intra-agency sales. Therefore, the Army has acknowledged that it was unable to reconcile intragovernmental accounts payable to the related intragovernmental accounts receivable that generated the payables.

Environmental Liabilities. The Army has not properly estimated and reported its Environmental Liabilities. For example, the processes used to report Environmental Liabilities for the Defense Environmental Restoration Program, Base Realignment and Closure, and the non-Defense Environmental Restoration Program on the financial statements were not adequate to establish or maintain sufficient documentation and audit trails.

Statement of Net Cost. The financial information contained in the statement of net cost is not presented by programs that align with major goals and outputs described in the DoD strategic and performance plans required by the Government Performance and Results Act of 1993. Because financial processes and systems do not correlate costs with performance measures, revenues and expenses are reported by appropriation categories. The amounts presented in the statement of net cost are based on funding, obligation, and disbursing transactions, which are not always recorded using accrual accounting. The Army systems do not always record the transactions on an accrual basis as required by U.S. GAAP. To capture all cost and financing sources for the Army, the information presented also includes data from non-financial feeder systems. In addition, Army General Fund budgetary and proprietary information does not correlate.

Statement of Budgetary Resources. Army accounting systems did not provide or capture the data needed for obligations incurred or prior year obligations recovered. Although the Army developed an alternative methodology to calculate these items, the amount of distortion cannot be reliably determined. In addition, the Army did not effectively implement internal controls over financial reporting to support the financial reporting process for the schedule of budgetary activity. Specifically, improvements are needed in management's process to verify complete and accurate recording of transactions in the general ledger, prepare required disclosures, and follow other accounting practices.

Deficiencies were identified related to the Army's ability to provide documentation over the U.S. Government Standard General Ledger accounts used to process transactions in several systems, and instances of individual transactions posting to inaccurate accounts were identified.

- The Army records transactions in its legacy financial accounting systems using transaction codes as part of a line of accounting. The Army converts the transaction codes to general ledger accounts that are not compliant with the U.S. Government Standard General Ledger within one of these legacy financial accounting systems.
- The Army has not developed a complete listing of all potential general ledger posting logics available within the main financial accounting system of record and the supply system.

Also, the information presented in the Army General Fund statement of budgetary resources does not completely agree with the information submitted in the yearend "Reports on Budget Execution and Budgetary Resources."

Intragovernmental Eliminations. The Army General Fund is unable to collect, exchange, and reconcile buyer and seller Intragovernmental transactions, resulting in adjustments that cannot be verified. This is primarily because of systems' limitations, as the majority of the systems currently used within the DoD do not allow the capture of buyer-side information for use in reconciliations and eliminations. Both DoD and Army accounting systems were unable to capture trading partner data at the transaction level to facilitate required trading partner eliminations and DoD guidance did not require adequate support for eliminations. In addition, DoD procedures required that buyer-side transaction data be forced to agree with seller-side transaction data without performing proper reconciliations.

Accounting Adjustments. Because of inadequate financial management systems and processes, journal voucher adjustments and data calls were used to prepare the Army General Fund basic financial statements. For FY 2016 yearend, Defense Finance and Accounting Service personnel identified that they did not adequately support \$196.7 billion in journal voucher adjustments used to prepare the Army General Fund basic financial statements. In addition, the Army had internal control deficiencies over journal entries and other adjustments to the general ledger. Improvements are needed in management's process to provide complete and timely populations of journal vouchers and provide appropriate supporting documentation for manual adjustments.

Abnormal Account Balances. Defense Finance and Accounting Service personnel did not detect, report, or take action to eliminate abnormal balances included in the Army General Fund accounting records. Abnormal balances not only distort the Army General Fund financial statements, but also indicate internal control and operational deficiencies and may conceal instances of fraud.

Contingency Payment Audit Trails. The Army acknowledged that the maintenance of substantiating documents by certifying and entitlement activities creates significant challenges in tracing audit trails for support of financial statements. Payments that are not properly supported do not provide the necessary assurance that funds were used as intended.

Reconciliation of Net Cost of Operations to Budget. Due to the limitations of the Army General Fund financial systems, budgetary data do not agree with proprietary expenses and capitalized assets. The Army could not reconcile the information reported in Note 21 with the Army General Fund statement of net cost without preparing \$1.1 billion in unsupported adjustments.

Material Weaknesses Identified During the Fiscal Year

Five new material weaknesses were identified during the FY 2015 schedule of budgetary activity audit and were included in the FY 2016 Army Annual Statement of Assurance.

The five new material weaknesses were:

Completeness. Army management has deficiencies in the ability to provide complete and reconciled transaction populations.

- **Reconciling Information Included in Different Systems.** The Army did not design and implement controls to validate that information is transferred completely and accurately between feeder systems, from feeder systems to the general ledger systems/legacy financial accounting systems, and to the main financial accounting system of record and the financial reporting system.
- **Internal Control Gaps.** The Army did not consistently develop and implement internal controls to reconcile information from source documents to systems to mitigate risk of misstatement.

- **Completeness of Control Populations and Other Control Deficiencies.** The Army had deficiencies in providing complete populations and in the operating effectiveness of controls related to the completeness of balances in the general ledger.
- **Incomplete Balances Due to Ineffective Cut-off and Suspense Transactions.** The Army did not design and implement controls to ensure that the Army has proper cut-off of financial transactions between accounting periods and to resolve suspense and collection error report balances at yearend.

Evidential Matter – Supporting Documentation. The Army did not consistently have sufficient evidential matter readily available to demonstrate that contractual services, military payroll, civilian payroll, reimbursable authority, and other disbursement and collection transactions were properly reported in the schedule of budgetary activity. Specifically, evidential matter:

- was not readily available and provided for review by the agreed upon due date;
- was provided for review, but the amount on the evidential matter did not agree to the general ledger detail used to prepare the schedule;
- was insufficient or could not be linked to the transaction recorded in the general ledger used to prepare the schedule; and
- was inappropriately reviewed/approved.

Service Provider Oversight. The Army did not have policies and procedures to assess service providers that host and manage financial systems that support amounts reported on the Army's schedule of budgetary activity. Specifically, the Army did not consistently perform and document an understanding of the services provided and the related service organization control reports to determine whether the scope of the service organization report met the Army's needs for obtaining assurance regarding service provider controls. Furthermore, the Army did not identify relevant risks of misstatement associated with the Army's internal control over financial reporting which are in part or exclusively mitigated by controls performed by service providers. The Army needed to evaluate the complementary user entity controls in the service organization control reports, subservice organizations used by the service provider, and test results included in the reports.

Accrual Estimation Methodology. The Army did not develop and implement accrual estimation methodologies to help verify that the balances in the schedule of budgetary activity reflected accrual transactions. Specifically, the Army did not develop and implement a process to estimate and record reimbursable authority received as of yearend, and record certain non-payroll obligations incurred and decreases to undelivered orders for goods or services contracted or received as of yearend. The Army also did not establish a process to perform a look-back analysis to determine whether its major procurement system non-payroll accrual methodology was reasonable and provide sufficient evidence to support and identify the civilian payroll and military payroll obligations incurred but not paid as of yearend.

Financial Management Improvements. The Army did not establish an effective control environment over financial management. The Army did not consistently develop and implement effective oversight of financial management and consistently establish effective financial management reporting structure and responsibilities. The Army did not fully train and consistently hold those involved in initiating, processing, and recording financial transactions accountable. As a result, the Army was unable to respond consistently to requests to demonstrate that financial transactions were properly processed and recorded. The Army also did not identify or have sufficient subject matter experts that understand Army financial operations. The Army could not explain or provide documentation to demonstrate that controls were properly designed and implemented. In addition, Army transactions were not properly recorded in accordance with the accounting standards.

Previously Identified Significant Deficiencies

A previously identified significant deficiency continued to exist for the Army General Fund. A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a deficiency or a combination of deficiencies in internal control that is less severe than a material weakness yet important enough to merit attention by those charged with governance. The following deficiency continues to exist.

- **Contingent Legal Liabilities.** Although the Army Office of General Counsel provided information in the response to the legal representation request, Army management did not report an estimated range of loss for all cases categorized as Unable to Determine. According to the Government Accountability Office Financial Audit Manual, section 1002.31, when legal

counsel does not indicate whether the unfavorable outcome is probable or remote, management and the auditor should conclude that the outcome is reasonably possible, and management should determine the disclosure.

These financial management control deficiencies may cause inaccurate management information. As a result, the Army management decisions based in whole or in part on this information may be adversely affected. Financial information reported by the Army may also contain misstatements resulting from these deficiencies. Internal control work we conducted as part of our prior audits would not necessarily disclose all material weaknesses and significant deficiencies. We did not identify material weaknesses that were not reported as such in the Army General Fund's FMFIA report.

Report on Compliance With Applicable Provisions of Laws, Regulations, Contracts, and Grant Agreements

U.S. generally accepted government auditing standards and OMB guidance require auditors to report on entities' compliance with selected provisions of laws and regulations, contracts, and grant agreements. Management is responsible for compliance with existing laws and regulations, contracts, and grant agreements related to financial reporting. Management has also acknowledged to us that previously reported instances of noncompliance continue to exist. Therefore, we did not determine whether the Army General Fund complied with selected provisions of all applicable laws and regulations, contracts, and grant agreements related to financial reporting. We caution that other noncompliance may have occurred and not been detected. Furthermore, the results of our limited procedures may not be sufficient for other purposes. Our objective was not to, and we do not, express an opinion on compliance with applicable laws, regulations, contracts, and grant agreements. Because of other scope limitations discussed in this report, we limited our work to determining compliance with selected provisions of the applicable laws and regulations.

Antideficiency Act

Section 1341, title 31, United States Code (31 U.S.C. § 1341 [1990]), limits the Army and its agents to making or authorizing expenditures or obligations that do not exceed the available appropriations or funds. Additionally, the Army or its agents may not contract or obligate for the payment of money before an appropriation is made available for that contract or obligation unless otherwise authorized by law. As stated in 31 U.S.C. § 1517 (2004), the Army and its agents are prohibited from making or authorizing expenditures of obligations exceeding an apportionment or the amount

permitted by prescribed regulations. According to 31 U.S.C. § 1351 (2004), if an officer or employee of an executive agency violates the Antideficiency Act (ADA), the head of the agency must report immediately to the President and Congress all relevant facts and a statement of actions taken. During FY 2016, the Army General Fund reported 35 ADA violations within one completed case.

DoD Regulation 7000.14-R, "Financial Management Regulation," volume 14, chapter 7, "Antideficiency Act Report," establishes timeframes for identifying and reporting ADA violations. The regulation states that the formal investigation and reporting on ADA violations should take no more than 15 months. Five investigations of potential ADA violations have been open for more than 15 months.

Compliance With FFMIA Requirements

The FFMIA requires the Army to establish and maintain financial management systems that comply substantially with the Federal financial management systems requirements, applicable Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level. For areas in which an agency is not in compliance, OMB A-136 requires the agency to identify remediation activities planned or underway to bring the systems into substantial compliance with the FFMIA. The DoD Financial Improvement and Audit Readiness Plan Status Report, May 2016, identifies actions the Army is taking to improve the Army General Fund financial statements. The Army is committed to achieving and sustaining audit readiness, which includes plans for improving financial management systems.

For FY 2016, the Deputy Assistant Secretary of the Army (Financial Operations) acknowledged that the Army General Fund did not substantially comply with the FFMIA. The Deputy Assistant Secretary also acknowledged to us that Army General Fund financial management and feeder systems could not provide adequate evidence supporting various material amounts on the financial statements and that previously identified material weaknesses continue. The financial management and feeder systems did not substantially comply with the Federal financial management systems requirements, Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level as of September 30, 2016. Therefore, based on the representation of the Deputy Assistant Secretary of the Army (Financial Operations), we did not substantiate whether the Army General Fund complied with FFMIA and OMB implementation guidance.

Recommendations

This report does not include recommendations to correct the material weaknesses and instances of noncompliance with laws and regulations, because previous audit reports contained recommendations for corrective actions or because current audit projects will include appropriate recommendations.



DEPARTMENT OF THE ARMY
OFFICE OF THE ASSISTANT SECRETARY OF THE ARMY
FINANCIAL MANAGEMENT AND COMPTROLLER
109 ARMY PENTAGON
WASHINGTON DC 20310-0109

SAFM-FO

4 November 2016

MEMORANDUM FOR Deputy Inspector General for Auditing, Department of Defense

SUBJECT: Management Response to the Fiscal Year 2016 Army General Fund Financial Statement Audit Report

1. We appreciate the efforts and professionalism your staff exhibited during the audit of the fiscal year (FY) 2016 Army General Fund Financial Statements. We also appreciate the opportunity to comment on the draft report provided to us on November 2, 2016.
2. We concur with the findings identified in the draft Report on Internal Control and will ensure our corrective action plans address the findings identified. We will continue work with our stakeholders correcting issues related to our general ledger, journal voucher adjustments, enterprise resource system posting logic, and abnormal balances.
3. We will document actions taken to correct material weaknesses, and address Schedule of Budgetary Activity (SBA) findings during FY 2017.
4. The results of continued audit readiness efforts, including corrective actions arising from the ongoing SBA audits, will indicate progress toward resolving longstanding financial reporting material weaknesses and will in turn highlight outstanding issues that present risks to the FY 2018 financial statement audit.
5. The audit report includes a significant deficiency with the legal representation process. We stand by our position that the accounting classification of contingent liabilities differs from the legal classification of outcomes. To meet financial reporting requirements, for FY 2016, we reported cases categorized as "Unable to Determine" as "Reasonably Possible", but did not disclose a range of loss. To identify the likelihood of loss before cases are heard or judgments rendered could adversely jeopardize the Army's position with the cases. For FY 2017 reporting, we will work with our general counsel to provide an estimate for cases for which we make the financial reporting change to "Reasonably Possible".
6. The point of contact for this action is [REDACTED]. She can be reached by telephone at [REDACTED], or by e-mail at [REDACTED].

MILLER.WESLEY.C
.1104827051

Digitally signed by
MILLER.WESLEY.C.1104827051
DN: cn=U.S. Government, ou=DoD, ou=PM,
ou=USA, cn=MILLER.WESLEY.C.1104827051
Date: 2016.11.04 15:38:30 -0400

Wesley C. Miller
Deputy Assistant Secretary Army
(Financial Operations)

Attachment 2
Page 1 of 1

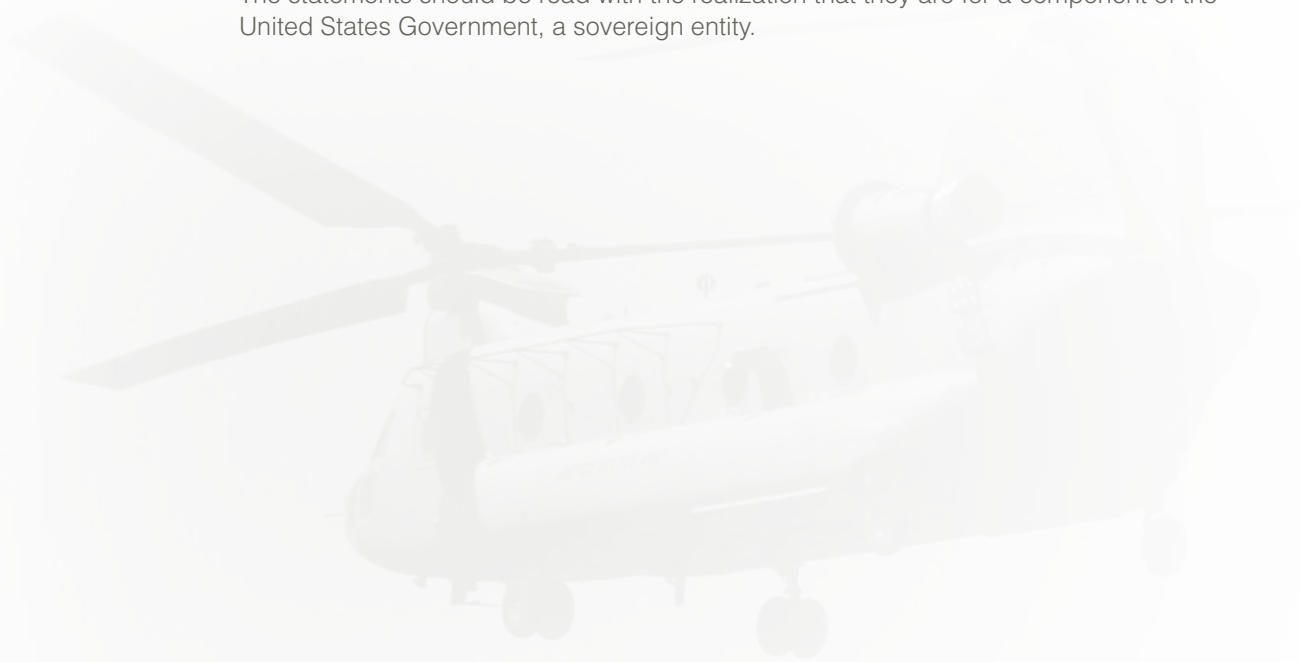


LIMITATIONS OF THE FINANCIAL STATEMENTS

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

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

The statements should be read with the realization that they are for a component of the United States Government, a sovereign entity.



CONSOLIDATED BALANCE SHEET

As of September 30, 2016 and 2015

(Amounts in thousands)

| | 2016 Consolidated | 2015 Consolidated |
|---|----------------------|----------------------|
| ASSETS (Note 2) | | |
| Intragovernmental: | | |
| Fund Balance with Treasury (Note 3) | \$ 1,321,157 | \$ 1,810,386 |
| Accounts Receivable (Note 5) | 338,341 | 302,109 |
| Total Intragovernmental Assets | \$ 1,659,498 | \$ 2,112,495 |
| Cash and Other Monetary Assets (Note 7) | \$ 4,960 | \$ 4,150 |
| Accounts Receivable, Net (Note 5) | 30,518 | 55,343 |
| Inventory and Related Property, Net (Note 9) | 17,948,351 | 19,484,195 |
| General Property, Plant and Equipment, Net (Note 10) | 1,715,087 | 1,738,658 |
| Other Assets (Note 6) | 62,396 | 97,125 |
| TOTAL ASSETS | \$ 21,420,810 | \$ 23,491,966 |
| STEWARDSHIP PROPERTY, PLANT & EQUIPMENT (Note 10) | | |
| LIABILITIES (Note 11) | | |
| Intragovernmental: | | |
| Accounts Payable (Note 12) | \$ 135,044 | \$ 105,764 |
| Other Liabilities (Note 15) | 97,091 | 112,060 |
| Total Intragovernmental Liabilities | \$ 232,135 | \$ 217,824 |
| Accounts Payable (Note 12) | \$ 84,216 | \$ 171,556 |
| Military Retirement and Other Federal Employment Benefits (Note 17) | 256,749 | 265,430 |
| Other Liabilities (Note 15) | 337,801 | 366,229 |
| TOTAL LIABILITIES | \$ 910,901 | \$ 1,021,039 |
| COMMITMENTS AND CONTINGENCIES (NOTE 16) | | |
| NET POSITION | | |
| Unexpended Appropriations - Other Funds | \$ 122,870 | \$ 107,258 |
| Cumulative Results of Operations - Other Funds | 20,387,039 | 22,363,669 |
| TOTAL NET POSITION | \$ 20,509,909 | \$ 22,470,927 |
| TOTAL LIABILITIES AND NET POSITION | \$ 21,420,810 | \$ 23,491,966 |

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

Department of Defense – Army Working Capital Fund

CONSOLIDATED STATEMENT OF NET COST

For the Years Ended September 30, 2016 and 2015

(Amounts in thousands)

| | 2016 Consolidated | 2015 Consolidated |
|--|---------------------|---------------------|
| Program Costs | | |
| Gross Costs | \$ 20,466,537 | \$ 21,764,515 |
| Operations, Readiness & Support | 20,466,537 | 21,764,515 |
| (Less: Earned Revenue) | \$ (18,924,538) | \$ (20,384,862) |
| Net Cost before Losses/(Gains) from Actuarial Assumption Changes for Military Retirement Benefits | \$ 1,541,999 | \$ 1,379,653 |
| Net Program Costs Including Assumption Changes | \$ 1,541,999 | \$ 1,379,653 |
| Net Cost of Operations (Note 18) | <u>\$ 1,541,999</u> | <u>\$ 1,379,653</u> |

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

CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION

For the Years Ended September 30, 2016 and 2015

(Amounts in thousands)

| | 2016 Consolidated | 2015 Consolidated |
|---|-------------------|-------------------|
| CUMULATIVE RESULTS OF OPERATIONS | | |
| Beginning Balances | \$ 22,363,669 | \$ 23,777,211 |
| Prior Period Adjustments: | | |
| Beginning balances, as adjusted | \$ 22,363,669 | \$ 23,777,211 |
| Budgetary Financing Sources: | | |
| Other adjustments (rescissions, etc.) | 3 | 2 |
| Appropriations used | 179,820 | 273,770 |
| Nonexchange revenue | 77 | (537) |
| Transfers-in/out without reimbursement | (888,000) | (554,614) |
| Other budgetary financing sources | (3) | (2) |
| Other Financing Sources: | | |
| Transfers-in/out without reimbursement (+/-) | (4,891) | (7,981) |
| Imputed financing from costs absorbed by others | 133,945 | 127,635 |
| Other (+/-) | 144,418 | 127,838 |
| Total Financing Sources | \$ (434,631) | \$ (33,889) |
| Net Cost of Operations (+/-) | 1,541,999 | 1,379,653 |
| Net Change | \$ (1,976,630) | \$ (1,413,542) |
| Cumulative Results of Operations | \$ 20,387,039 | \$ 22,363,669 |
| UNEXPENDED APPROPRIATIONS | | |
| Beginning Balances | \$ 107,258 | \$ 142,301 |
| Beginning balances, as adjusted | \$ 107,258 | \$ 142,301 |
| Budgetary Financing Sources: | | |
| Appropriations transferred-in/out (+/-) | \$ 195,432 | \$ 238,727 |
| Appropriations used | (179,820) | (273,770) |
| Total Budgetary Financing Sources | \$ 15,612 | \$ (35,043) |
| Unexpended Appropriations | 122,870 | 107,258 |
| Net Position | \$ 20,509,909 | \$ 22,470,927 |

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

Department of Defense – Army Working Capital Fund

COMBINED STATEMENT OF BUDGETARY RESOURCES

For the Years Ended September 30, 2016 and 2015

(Amounts in thousands)

| | 2016 Combined | 2015 Combined |
|--|----------------------|----------------------|
| Budgetary Resources: | | |
| Unobligated balance brought forward, Oct 1 | \$ 2,523,448 | \$ 2,783,613 |
| Adjustment to unobligated balance, brought forward, Oct 1 (+ or -) | 2,083,886 | |
| Unobligated balance brought forward, Oct 1, as adjusted, | \$ 4,607,334 | \$ 2,783,613 |
| Recoveries of prior year unpaid obligations | 971,226 | 1,154,192 |
| Other changes in unobligated balance (+ or -) | (1,372,823) | (1,225,397) |
| Unobligated balance from prior year budget authority, net | \$ 4,205,737 | \$ 2,712,408 |
| Appropriations (discretionary and mandatory) | 195,432 | 238,727 |
| Contract Authority (discretionary and mandatory) | 5,548,089 | 5,496,570 |
| Spending Authority from offsetting collections (discretionary and mandatory) | 4,672,241 | 4,938,550 |
| Total Budgetary Resources | \$ 14,621,499 | \$ 13,386,255 |
| Status of Budgetary Resources: | | |
| New obligations and upward adjustments (total) | \$ 10,587,864 | \$ 10,862,807 |
| Unobligated balance, end of year | | |
| Apportioned, unexpired accounts | 1,949,749 | 2,523,448 |
| Unapportioned, unexpired accounts | 2,083,886 | 0 |
| Unexpired unobligated balance, end of year | 4,033,635 | 2,523,448 |
| Unobligated balance, end of year | \$ 4,033,635 | \$ 2,523,448 |
| Total Budgetary Resources | \$ 14,621,499 | \$ 13,386,255 |
| Change in Obligated Balance: | | |
| Unpaid obligations: | | |
| Unpaid obligations, brought forward, Oct 1 | \$ 9,011,140 | \$ 7,143,397 |
| New obligations and upward adjustments | 10,587,864 | 10,862,807 |
| Outlays | (13,214,411) | (7,840,872) |
| Recoveries of prior year unpaid obligations (-) | (971,226) | (1,154,192) |
| Unpaid obligations, end of year | 5,413,367 | 9,011,140 |
| Uncollected payments: | | |
| Uncollected pymts, Fed sources, brought forward, Oct 1 (-) | (8,670,641) | (7,016,482) |
| Change in uncollected pymts, Fed sources (+ or -) | 2,764,881 | (1,654,159) |
| Uncollected pymts, Fed sources, end of year (-) | (5,905,760) | (8,670,641) |
| Memorandum Entries | | |
| Obligated balance, start of year (+ or -) | \$ 340,499 | \$ 126,915 |
| Obligated balance, end of year (+ or -) | \$ (492,393) | \$ 340,499 |
| Budget Authority and Outlays, Net: | | |
| Budget authority, gross (discretionary and mandatory) | \$ 10,415,762 | \$ 10,673,847 |
| Actual offsetting collections (discretionary and mandatory) (-) | (13,417,750) | (8,131,973) |
| Change in uncollected customer payments from Federal | 2,764,881 | (1,654,159) |
| Budget Authority, net (discretionary and mandatory) | \$ (237,107) | \$ 887,715 |
| Outlays, gross (discretionary and mandatory) | \$ 13,214,411 | \$ 7,840,872 |
| Actual offsetting collections (discretionary and mandatory) (-) | (13,417,750) | (8,131,973) |
| Outlays, net (discretionary and mandatory) | (203,339) | (291,101) |
| Agency Outlays, net (discretionary and mandatory) | \$ (203,339) | \$ (291,101) |

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

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES

1.A. Basis of Presentation

These financial statements have been prepared to report the financial position and results of operations of the Army Working Capital Fund (WCF), as required by the *Chief Financial Officers Act of 1990*, expanded by the *Government Management Reform Act of 1994* and other appropriate legislation. The financial statements have been prepared from the books and records of the Army WCF in accordance with, and to the extent possible, U.S. generally accepted accounting principles (U.S. GAAP) promulgated by the Federal Accounting Standards Advisory Board; the Office of Management and Budget (OMB) Circular No. A-136, *Financial Reporting Requirements*; and the Department of Defense (DoD) Financial Management Regulation (FMR). The accompanying financial statements account for all resources for which the Army WCF is responsible unless otherwise noted.

The Army WCF is unable to fully implement all elements of U.S. GAAP and the OMB Circular No. A-136, due to limitations of financial and nonfinancial management processes and systems that support the financial statements. Although the Army WCF now derives reported values and information for major asset and liability categories from the Logistic Modernization Program (LMP) system, LMP contains certain system and posting deficiencies such as budgetary to proprietary imbalances, incomplete and incorrect trading partner data, recoveries of prior year funds, and incomplete accounting information for outgoing Military Interdepartmental Procurement Requests (MIPRs). In addition, LMP contains erroneous and incomplete account balances resulting from their migration from the legacy systems. The Army WCF financial statements and LMP are also compromised by reliance on data from off-line procurement systems, entitlement systems, property systems, debt management and claims systems, and off-line Treasury cash reconciliation processes. The Army WCF is in the process of determining correct migration balances, and continues to implement U.S. GAAP principles, process and system improvements, and compensating controls addressing these limitations.

The Army WCF currently has 11 auditor identified financial statement material weaknesses: (1) Financial Management Systems; (2) Fund Balance with Treasury; (3) Inventory; (4) General Property, Plant and Equipment; (5) Accounts Payable; (6) Abnormal Account Balances; (7) Statement of Net Cost; (8) Statement of Budgetary Resources; (9) Intragovernmental Eliminations; (10) Other

Accounting Entries; and (11) Reconciliation of Net Cost of Operations to Budget.

1.B. Mission of the Reporting Entity

The Army mission is to support the national security and defense strategies by providing well-trained, well-led, and well-equipped forces to the combatant commanders. This mission encompasses the intent of the Congress, as defined in Title 10 of the U.S. Code, to preserve the peace and security and provide for the defense of the U.S., its territories, commonwealths, and possessions, and any areas occupied by the U.S.; support national policies; implement national objectives; and overcome any nations responsible for aggressive acts that imperil the peace and security of the U.S.

The Army WCF is part of the Defense Working Capital Fund, and is divided into two separate business areas: Supply Management and Industrial Operations. These business areas ensure delivery of critical items, such as petroleum products, repair parts, consumable supplies, depot maintenance services, munitions, and weapons to support the deployment and projection of lethal force as required by the nation.

1.C. Appropriations and Funds

The Army WCF receives appropriations and funds as defense working capital (revolving) funds and uses them to execute its mission and subsequently report on resource usage.

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

1.D. Basis of Accounting

The Army WCF's financial management systems are unable to meet all full accrual accounting requirements. This is primarily because many of the Army Working Capital Fund financial and nonfinancial systems and processes were designed prior to the legislative mandate to produce financial statements in accordance with U.S. GAAP.

The Army WCF's financial statements and supporting trial balances are compiled from the underlying proprietary and budgetary financial data and trial balances of the Army WCF sub-entities. Reportable data is also derived from payroll systems, entitlement systems, property systems, debt management and claims systems, off-line Treasury cash reconciliation processes, and additional interfacing accruals such as procurement accounts payable and Federal Employees' Compensation Act (FECA) liabilities. Some of the sub-entity level trial balances may reflect known abnormal balances resulting largely from business and system processes. At the consolidated Army WCF level, these abnormal balances may not be evident. Disclosures of abnormal balances are made in the applicable footnotes, but only to the extent that the abnormal balances are evident at the consolidated level.

The DoD is continuing the actions required to bring its financial and nonfinancial feeder systems and processes into compliance with U.S. GAAP. One such action is the current revision of accounting systems to record transactions based on the United States Standard General Ledger (USSGL). Until all of the Army WCF's financial and nonfinancial feeder systems and processes are able to collect and report financial information as required by U.S. GAAP, there will be instances when the Army WCF's financial data will be derived from nonfinancial feeder systems.

1.E. Revenues and Other Financing Sources

The Army WCF is divided into two separate business areas: Industrial Operations and Supply Management. Industrial Operations activities recognize revenue according to the percentage-of-completion method, while the Supply Management activities recognize revenue from the sale of inventory items.

1.F. Recognition of Expenses

For financial reporting purposes, DoD policy requires the recognition of operating expenses in the period incurred. The Army WCF now derives the majority of its reported data from LMP which is designed to collect and record financial information for accruals. However, estimates are made for some major items such as payroll expenses, entitlement systems accruals, unbilled revenue, transportation expenses and work by performing activities on outgoing MIPRs. The Army WCF continues to implement process and system improvements to address these limitations.

1.G. Accounting for Intragovernmental Activities

Accounting standards require an entity to eliminate intra-entity activity and balances from consolidated financial statements to prevent overstatement for business with itself. However, the Army WCF cannot accurately identify intragovernmental transactions by customer because: (1) the Army Enterprise Systems Integration Program (AESIP) vendor master does not capture the correct buyer and seller data at the transaction level; and (2) the standard line of accounting (SLOA) has not been implemented by reciprocal trading partners. In addition, the Army WCF cannot determine the correct reciprocal trading partner dollar amounts and necessary eliminations due to numerous deficient business processes such as: (1) buyer and seller systems do not contain the same information, the same accounts, or the same dollar balances; (2) buyer and seller systems are not real time – and do not post transactions and balances at the same time; (3) trading partners are not subject to enforceable agreements for standardization of reciprocal transactions and accounts; (4) buyer and seller transactions do not reside in a standardized, centralized tracking system; and, (5) trading partner information is often not correct, or available, when performing activities solicit third parties to perform actual work (e.g., third party commercial contractors).

Generally, seller entities within the DoD provide summary seller-side balances for revenue, accounts receivable, and unearned revenue to the buyer-side internal accounting offices. In most cases, the buyer-side records are adjusted to agree with DoD seller-side balances and are then eliminated. LMP implemented a standard financial information structure (SFIS) in FY 2013 and 2015 which incorporated data elements and attributes to enable the Army WCF to more correctly report, reconcile, and eliminate intragovernmental balances.

The Treasury Financial Manual Part 2 – Chapter 4700, *Agency Reporting Requirements for the Financial Report of the United States Government*, provides guidance for reporting and reconciling intragovernmental balances. While the Army WCF is unable to fully reconcile intragovernmental transactions with all federal agencies, Army WCF is able to reconcile balances pertaining to Federal Employees' Compensation Act transactions with the Department of Labor and benefit program transactions with the Office of Personnel Management.

Imputed financing represents the cost paid on behalf of the Army WCF by another Federal entity. The Army WCF recognizes imputed costs for: (1) employee

pension, post-retirement health, and life insurance benefits; and (2) post-employment benefits for terminated and inactive employees to include unemployment and workers compensation under the *Federal Employees' Compensation Act*.

The DoD'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 DoD's financial statements do not report any public debt, interest or source of public financing, whether from issuance of debt or tax revenues.

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

1.H. Transactions with Foreign Governments and International Organizations

Each year, Army WCF 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, DoD has authority to sell defense articles and services to foreign countries and international organizations generally at no profit or loss to the Federal Government. Payment in U.S. dollars is required in advance.

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

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

In addition, DFAS submits reports to the U.S. Treasury by appropriation on interagency transfers, collections received, and disbursements issued. The U.S. Treasury records these transactions to the applicable Fund Balance with Treasury (FBWT) account. On a monthly basis, Army WCF's FBWT is reviewed

and adjusted, as required, to agree with the U.S. Treasury accounts.

1.J. Cash and Other Monetary Assets

There are no restrictions on cash or the use or conversion of foreign currencies. Cash is the total of cash resources under the control of DoD including coin, paper currency, negotiable instruments, and amounts held for deposit in banks and other financial institutions.

1.K. Accounts Receivable

Accounts receivable from other federal entities or the public include accounts receivable, claims receivable, and refunds receivable. Allowances for uncollectible accounts due from the public are based upon an analysis of collection experience grouped by age categories. The DoD does not recognize an allowance for estimated uncollectible amounts from other federal agencies as receivables from other federal agencies are considered to be inherently collectible. Claims for accounts receivables from other federal agencies are resolved between the agencies in accordance with the Intragovernmental Business Rules published in the Treasury Financial Manual.

1.L. Direct Loans and Loan Guarantees

Not applicable.

1.M. Inventories and Related Property

The Army WCF manages only military or government-specific materiel under normal conditions. Materiel is a unique term that relates to military force management, and includes items such as ships, tanks, self-propelled weapons, aircraft, etc., and related spares, repair parts, and support equipment. Items commonly used in and available from the commercial sector are not managed in Army WCF materiel management activities. Operational cycles are irregular and the military risks associated with stock-out positions have no commercial parallel. The Army WCF holds materiel based on military need and support for contingencies.

The Army WCF values 100 percent of its resale inventory using the moving average cost method.

Army complies with SFFAS No. 3, *Interpretation 7, Items Held for Remanufacture*. SFFAS 3 and *Interpretation 7* require that inventory held for repair and resale reflect all capitalized rebuild costs to include the cost of the unserviceable carcasses. LMP capitalizes those costs in a Work in Process account. Fully repaired and rebuilt items are capitalized as Inventory Held for Sale. Unserviceable

carcasses waiting for induction to repair programs will continue to be accounted for as Inventory Held for Remanufacture.

The Army WCF recognizes excess, obsolete, and unserviceable inventory at net zero realizable value pending development of an effective means of valuing such materiel.

Contractor acquired inventory may not be properly accounted for due to system limitations.

Inventory available and purchased for resale includes consumable spare and repair parts and repairable items owned and managed by Army WCF. This inventory is retained to support military or national contingencies. Inventory held for repair is damaged inventory that requires repair to make it suitable for sale. Often, it is more economical to repair these items rather than to procure them. The Army WCF customers often rely on weapon systems and machinery no longer in production. As a result, Army WCF 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 (1) costs related to the production or servicing of items, including direct material, labor and applied overhead; (2) the value of finished products or completed services that are yet to be placed in service; and (3) munitions in production and depot maintenance work with associated costs incurred in the delivery of maintenance services.

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

Not applicable.

1.O. General Property, Plant and Equipment

The Army WCF's General Property, Plant & Equipment (PP&E) capitalization threshold is \$250 thousand. The capitalization threshold applies to asset acquisitions and modifications/improvements placed into service after September 30, 2013. PP&E assets acquired prior to October 1, 2013 were capitalized at prior threshold levels (\$100 thousand for equipment and \$20 thousand for real property) and are carried at their remaining net book values.

The Army WCF capitalizes all PP&E used in the performance of its mission. These assets are capitalized as General PP&E, whether or not they meet the definition of any other PP&E category.

When it is in the best interest of the government, the Army WCF provides government property to contractors to complete contract work. The Army WCF 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 meets or exceeds the DoD capitalization threshold, federal accounting standards require that it be reported on Army WCF's Balance Sheet.

The DoD developed policy and a reporting process for contractors with government-furnished equipment that provides appropriate General PP&E information for financial statement reporting. The DoD requires the Army WCF maintain, in their property systems, information on all property furnished to contractors. These actions are structured to capture and report the information necessary for compliance with federal accounting standards. The Army WCF has not fully implemented this policy primarily due to system limitations.

1.P. Advances and Prepayments

When advances are permitted by law, legislative action, or presidential authorization, DoD's policy is to record advances or prepayments in accordance with U.S. GAAP. As such, payments made in advance of the receipt of goods and services should be reported as an asset on the Balance Sheet. The DoD's policy is to expense and/or properly classify assets when the related goods and services are received. The Army WCF has implemented this policy for advances identified as military and civil service employee pay advances, travel advances, and advances in contract feeder systems.

1.Q. Leases

Lease payments for the rental of equipment and operating facilities are classified as either capital or operating leases. When a lease is essentially equivalent to an installment purchase of property (a capital lease), and the value equals or exceeds the current capitalization thresholds, Army WCF records the applicable asset as though purchased, with an offsetting liability, and depreciates it. The Army WCF records the asset and the liability at 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 Army WCF, 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 risks of ownership. Payments for operating leases are expensed over the lease term as they become payable.

Vehicle leases with General Services Administration (GSA) entered into by the Army WCF are the largest component of operating leases and are based on costs gathered from existing leases, GSA bills, and interservice support agreements.

1.R. Other Assets

The Army WCF other assets include travel advances, credits due for returns and estimated future payments to contractors (future contract financing payments) upon delivery and government acceptance of satisfactory products.

The Army WCF conducts business with commercial contractors under two primary types of contracts: fixed price and cost reimbursable. To alleviate the potential financial burden on the contractor that long-term contracts can cause, the Army WCF may provide financing payments. Contract financing payments are defined in the *Federal Acquisition Regulations, Part 32*, as authorized disbursements to a contractor prior to acceptance of supplies or services by the government. 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. It is DoD policy to record certain contract financing payments as *Other Assets*. The Army WCF has fully implemented this policy. Estimated future payments to contractors are offset by a contingent liability.

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

1.S Contingencies and Other Liabilities

The SFFAS No. 5, *Accounting for Liabilities of the Federal Government*, as amended by the 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 Army WCF recognizes contingent liabilities when past events or exchange transactions occur, a future loss is probable, and the loss amount can be reasonably estimated.

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

1.T Accrued Leave

The Army WCF reports liabilities for accrued compensatory and annual leave for civilians. Sick leave for civilians is expensed as taken. The liabilities are based on current pay rates.

1.U Net Position

Net Position consists of unexpended appropriations and cumulative results of operations. Unexpended appropriations represent the amounts of budget 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 between expenses and losses, and financing sources (including appropriations, revenue, and gains) since inception. The cumulative results of operations also include donations and transfers in and out of assets that were not reimbursed.

1.V Treaties for Use of Foreign Bases

Not applicable.

1.W Undistributed Disbursements and Collections

Undistributed disbursements and collections represent the difference between disbursements and collections matched at the transaction level to specific obligations, payables, or receivables in the source systems and those reported by the U.S. Treasury.

Supported disbursements and collections have corroborating documentation for the summary level adjustments made to accounts payable and accounts

receivable. Unsupported disbursements and collections do not have supporting documentation for the transactions and most likely would not meet audit scrutiny. However, both supported and unsupported adjustments may have been made to the Army WCF accounts payable and accounts receivable trial balances prior to validating underlying transactions.

Due to noted material weakness in current accounting and financial feeder systems, the DoD generally cannot determine whether undistributed disbursements and collections should be applied to federal or nonfederal accounts payable/receivable at the time accounting reports are prepared. Accordingly, the DoD policy is to allocate supported undistributed disbursements and collections between federal and nonfederal categories based on the percentage of distributed federal and nonfederal accounts payable and accounts receivable. Unsupported undistributed disbursements and collections are also applied to reduce accounts payable and accounts receivable, respectively.

1.X. *Fiduciary Activities*

Not applicable.

1.Y. *Military Retirement and Other Federal Employment Benefits*

Not applicable.

1.Z. *Significant Events*

During the final two quarters of FY 2015, and the initial two quarters of FY 2016, a comprehensive analysis was undertaken to determine differences in

amounts reported for the Army WCF in the Statement of Budgetary Resources (SBR) relative to the source budgetary account balances residing in the LMP. As a result of this analysis, adjustments were made during 3rd quarter, FY 2016 to the Army WCF/LMP budgetary account balances totaling \$23.4 billion. These adjustments reduced erroneous unapportioned budget authority in the Army WCF/LMP from \$23.4 billion to zero; increased Contract Authority Carried Forward \$13.2 billion; increased Budgetary Cash \$7.9 billion; and reduced current year budget authority \$2.2 billion. These adjustments also reduced the variance between LMP and the formal SBR from \$21.1 billion to approximately \$230.0 million.

During the past 10 years, disbursements, collections and related obligations resulting from internal work between the Army WCF Supply Management and Industrial Operations were not reported to Treasury - and not reported on the SBR. The cumulative total of these unreported transactions were \$4.8 billion. In order to correct the Army WCF cash reporting, and to reflect correct budgetary authority and execution, these transactions are being reported to Treasury for FY 2016. At the direction of the OMB, the Army WCF was required to submit a "backdated package" to the U.S. Treasury and the OMB in order to ensure that these transactions were recorded as backdated and prior year events. Since both the unreported disbursements and unreported collections totaled \$4.7 billion, the overall net impact to the Army WCF Fund Balance with Treasury nets to a zero change. However, the FY 2016 Army WCF statements of budget authority and budget execution will reflect net prior year adjustments of \$2.1 billion.

NOTE 2. NONENTITY ASSETS

As of September 30

(Amounts in thousands)

1. Intragovernmental Assets

- A. Fund Balance with Treasury
- B. Accounts Receivable
- C. Other Assets
- D. Total Intragovernmental Assets

| | 2016 | 2015 |
|-----------------------------------|---------------|---------------|
| A. Fund Balance with Treasury | \$ 0 | \$ 0 |
| B. Accounts Receivable | 0 | 0 |
| C. Other Assets | 0 | 0 |
| D. Total Intragovernmental Assets | \$ 0 | \$ 0 |
| 2. Nonfederal Assets | | |
| A. Cash and Other Monetary Assets | \$ 0 | \$ 0 |
| B. Accounts Receivable | 132 | 56 |
| C. Other Assets | 0 | 0 |
| D. Total Nonfederal Assets | \$ 132 | \$ 56 |
| 3. Total Nonentity Assets | \$ 132 | \$ 56 |
| 4. Total Entity Assets | \$ 21,420,678 | \$ 23,491,910 |
| 5. Total Assets | \$ 21,420,810 | \$ 23,491,966 |

Assets are categorized as either entity or nonentity. Entity assets consist of resources that are available for use in the operations of the entity.

Non-entity assets are not available for the use in the Army WCF's normal operations. The Army WCF has stewardship accountability and reporting responsibility for nonentity assets.

These nonentity assets are for interest, penalties and administrative fees to be collected for out-of-service debts into a receipt account and then forwarded to the U.S. Treasury.

NOTE 3. FUND BALANCE WITH TREASURY

| As of September 30 | 2016 | 2015 |
|--|---------------------|---------------------|
| <i>(Amounts in thousands)</i> | | |
| 1. Fund Balances | | |
| A. Appropriated Funds | \$ 0 | \$ 0 |
| B. Revolving Funds | 1,321,157 | 1,810,386 |
| C. Trust Funds | 0 | 0 |
| D. Special Funds | 0 | 0 |
| E. Other Fund Types | 0 | 0 |
| F. Total Fund Balances | <u>\$ 1,321,157</u> | <u>\$ 1,810,386</u> |
| 2. Fund Balances Per Treasury Versus Agency | | |
| A. Fund Balance per Treasury | \$ 1,321,157 | \$ 1,810,386 |
| B. Fund Balance per Army WCF | 1,321,157 | 1,810,386 |
| 3. Reconciling Amount | <u>\$ 0</u> | <u>\$ 0</u> |

Status of Fund Balance with Treasury

| As of September 30 | 2016 | 2015 |
|---|---------------------|---------------------|
| <i>(Amounts in thousands)</i> | | |
| 1. Unobligated Balance | | |
| A. Available | \$ 1,949,749 | \$ 2,523,449 |
| B. Unavailable | 2,083,886 | 0 |
| 2. Obligated Balance not yet Disbursed | \$ 5,413,367 | \$ 9,011,141 |
| 3. Nonbudgetary FBWT | \$ 0 | \$ 0 |
| 4. NonFBWT Budgetary Accounts | \$ (8,125,845) | \$ (9,724,204) |
| 5. Total | <u>\$ 1,321,157</u> | <u>\$ 1,810,386</u> |

The Status of Fund Balance with Treasury (FBWT) reflects the budgetary resources to support FBWT and is a reconciliation between budgetary and proprietary accounts. It primarily consists of unobligated and obligated balances. The balances reflect the budgetary authority remaining for disbursements against current or future obligations.

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

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

Non-FBWT Budgetary Accounts reduces the Status of FBWT. For the Army WCF these include unfilled orders without advances, reimbursements earned receivable, and contract authority.

NOTE 4. INVESTMENTS AND RELATED INTEREST

Not applicable.

NOTE 5. ACCOUNTS RECEIVABLE

| As of September 30 (Amounts in thousands) | 2016 | | |
|--|-------------------|--|--------------------------|
| | Gross Amount Due | Allowance For Estimated Uncollectibles | Accounts Receivable, Net |
| 1. Intragovernmental Receivables | \$ 338,341 | N/A | \$ 338,341 |
| 2. Nonfederal Receivables (From the Public) | \$ 30,612 | \$ (94) | \$ 30,518 |
| 3. Total Accounts Receivable | <u>\$ 368,953</u> | <u>\$ (94)</u> | <u>\$ 368,859</u> |

| As of September 30 (Amounts in thousands) | 2015 | | |
|--|-------------------|--|--------------------------|
| | Gross Amount Due | Allowance For Estimated Uncollectibles | Accounts Receivable, Net |
| 1. Intragovernmental Receivables | \$ 302,109 | N/A | \$ 302,109 |
| 2. Nonfederal Receivables (From the Public) | \$ 55,873 | \$ (530) | \$ 55,343 |
| 3. Total Accounts Receivable | <u>\$ 357,982</u> | <u>\$ (530)</u> | <u>\$ 357,452</u> |

Accounts receivable represent the Army WCF claim for payment from other entities. The Army WCF only recognizes an allowance for uncollectible amounts from the public. Claims with other federal agencies are resolved in accordance with the Intragovernmental Business Rules.

NOTE 6. OTHER ASSETS

| As of September 30 (Amounts in thousands) | 2016 | | 2015 | |
|--|-----------|---------------|-----------|---------------|
| | | | | |
| 1. Intragovernmental Other Assets | | | | |
| A. Advances and Prepayments | \$ | 0 | \$ | 0 |
| B. Other Assets | | 0 | | 0 |
| C. Total Intragovernmental Other Assets | <u>\$</u> | <u>0</u> | <u>\$</u> | <u>0</u> |
| 2. Nonfederal Other Assets | | | | |
| A. Outstanding Contract Financing Payments | \$ | 62,343 | \$ | 97,075 |
| B. Advances and Prepayments | | 53 | | 50 |
| C. Other Assets (With the Public) | | 0 | | 0 |
| D. Total Nonfederal Other Assets | <u>\$</u> | <u>62,396</u> | <u>\$</u> | <u>97,125</u> |
| 3. Total Other Assets | <u>\$</u> | <u>62,396</u> | <u>\$</u> | <u>97,125</u> |

Contract terms and conditions for certain types of contract financing payments convey certain rights to the Army WCF protecting the contract work from state or local taxation, liens or attachment by the contractors' 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 Army WCF. The Army WCF does not have the right to take the work, except as provided in contract clauses related to termination or acceptance. The Army WCF is not obligated to make payment to the contractor until delivery and acceptance.

Outstanding Contract Financing Payments includes \$54.3 million in contract financing payments and an additional \$8.0 million in estimated future payments to contractors upon delivery and government acceptance of a satisfactory product. Refer to Note 15, *Other Liabilities*, for further information.

NOTE 7. CASH AND OTHER MONETARY ASSETS

| As of September 30 | 2016 | 2015 |
|---|-----------------|-----------------|
| <i>(Amounts in thousands)</i> | | |
| 1. Cash | \$ 4,960 | \$ 4,150 |
| 2. Foreign Currency | 0 | 0 |
| 3. Other Monetary Assets | 0 | 0 |
| 4. Total Cash, Foreign Currency, & Other Monetary Assets | <u>\$ 4,960</u> | <u>\$ 4,150</u> |

There are no restrictions on cash or the use or conversion of foreign currencies.

NOTE 8. DIRECT LOAN AND LOAN GUARANTEES

Not applicable.

NOTE 9. INVENTORY AND RELATED PROPERTY

| As of September 30 | 2016 | 2015 |
|--|----------------------|----------------------|
| <i>(Amounts in thousands)</i> | | |
| 1. Inventory, Net | \$ 17,948,351 | \$ 19,484,195 |
| 2. Operating Materiel & Supplies, Net | 0 | 0 |
| 3. Stockpile Materiel, Net | 0 | 0 |
| 4. Total | <u>\$ 17,948,351</u> | <u>\$ 19,484,195</u> |

Inventory, Net

| As of September 30 | 2016 | | | |
|--|------------------------|-----------------------|-------------------|------------------|
| <i>(Amounts in thousands)</i> | Inventory, Gross Value | Revaluation Allowance | Inventory, Net | Valuation Method |
| 1. Inventory Categories | | | | |
| A. Available and Purchased for Resale | \$ 10,580,199 | \$ 0 | 10,580,199 | MAC, |
| B. Held for Repair | 5,060,652 | 0 | 5,060,652 | SC |
| C. Excess, Obsolete, and Unserviceable | 142,003 | (142,003) | 0 | NRV |
| D. Raw Materiel | 1,188,212 | 0 | 1,188,212 | MAC |
| E. Work in Process | 1,119,288 | 0 | 1,119,288 | AC, SC |
| F. Total | <u>\$ 18,090,354</u> | <u>\$ (142,003)</u> | <u>17,948,351</u> | |

| As of September 30 | 2015 | | | |
|--|------------------------|-----------------------|-------------------|------------------|
| <i>(Amounts in thousands)</i> | Inventory, Gross Value | Revaluation Allowance | Inventory, Net | Valuation Method |
| 1. Inventory Categories | | | | |
| A. Available and Purchased for Resale | \$ 12,264,388 | \$ 0 | 12,264,388 | MAC |
| B. Held for Repair | 5,770,877 | 0 | 5,770,877 | SC |
| C. Excess, Obsolete, and Unserviceable | 204,210 | (204,210) | 0 | NRV |
| D. Raw Materiel | 1,448,930 | 0 | 1,448,930 | MAC |
| E. Work in Process | 0 | 0 | 0 | AC, SC |
| F. Total | <u>\$ 19,688,405</u> | <u>\$ (204,210)</u> | <u>19,484,195</u> | |

Legend for Valuation Methods:

NRV = Net Realizable Value MAC = Moving Average Cost SC = Standard Cost AC = Actual Cost

There are restrictions on the use, sale, and disposition of inventory classified as war reserve materiel valued at a moving average cost of \$1.8 billion which includes petroleum products, subsistence items, spare parts, and medical materiel.

The categories listed comprise Inventory, Net. The Army WCF assigns inventory items to a category based upon the type and condition of the asset. Inventory Available and Purchased for Resale includes spare and repair parts, clothing and textiles and petroleum products. Inventory Held for Repair consists of damaged materiel held

as inventory that is more economical to repair than to dispose. Excess, Obsolete, and Unserviceable Inventory consists of scrap materiel or items that cannot be economically repaired and are awaiting disposal. Raw Materiel consists of items consumed in the production of goods for sale or in the provision of services for a fee.

The value of the Army WCF Government Furnished Materiel (GFM) and contractor-acquired materiel in the hands of the contractors are not included in the inventory values reported above. The DoD is presently reviewing its process for reporting these amounts in an effort to determine the appropriate accounting treatment.

NOTE 10. GENERAL PP&E, NET

As of September 30

| (Amounts in thousands) | 2016 | | | | |
|--|---|--------------|---------------------|---|---------------------|
| | Depreciation/ Amortization Method | Service Life | Acquisition Value | (Accumulated Depreciation/ Amortization) | Net Book Value |
| 1. Major Asset Classes | | | | | |
| A. Land | N/A | N/A | \$ 10,007 | N/A | \$ 10,007 |
| B. Buildings, Structures, and Facilities | S/L | 20 or 40 | 2,334,132 | \$ (1,677,643) | 656,489 |
| C. Leasehold Improvements | S/L | lease term | 0 | 0 | 0 |
| D. Software | S/L | 2-5 or 10 | 1,544,059 | (1,125,031) | 419,028 |
| E. General Equipment | S/L | Various | 1,841,448 | (1,439,884) | 401,564 |
| F. Assets Under Capital Lease | S/L | lease term | 668 | (195) | 473 |
| G. Construction-in-Progress | N/A | N/A | 227,526 | N/A | 227,526 |
| H. Other | | | 0 | 0 | 0 |
| I. Total General PP&E | | | \$ 5,957,840 | \$ (4,242,753) | \$ 1,715,087 |

As of September 30

| (Amounts in thousands) | 2015 | | | | |
|--|---|--------------|---------------------|---|---------------------|
| | Depreciation/ Amortization Method | Service Life | Acquisition Value | (Accumulated Depreciation/ Amortization) | Net Book Value |
| 1. Major Asset Classes | | | | | |
| A. Land | N/A | N/A | \$ 10,008 | N/A | \$ 10,008 |
| B. Buildings, Structures, and Facilities | S/L | 20 or 40 | 2,281,813 | \$ (1,624,465) | 657,348 |
| C. Leasehold Improvements | S/L | lease term | 0 | 0 | 0 |
| D. Software | S/L | 2-5 or 10 | 1,355,144 | (975,178) | 379,966 |
| E. General Equipment | S/L | Various | 1,830,428 | (1,389,433) | 440,995 |
| F. Assets Under Capital Lease | S/L | lease term | 0 | 0 | 0 |
| G. Construction-in-Progress | N/A | N/A | 246,770 | N/A | 246,770 |
| H. Other | | | 3,571 | 0 | 3,571 |
| I. Total General PP&E | | | \$ 5,727,734 | \$ (3,989,076) | \$ 1,738,658 |

Legend for Valuation Methods: S/L = Straight Line N/A = Not Applicable

Assets Under Capital Lease

As of September 30

(Amounts in thousands)

1. Entity as Lessee, Assets Under Capital Lease

| | 2016 | 2015 |
|--------------------------------|---------------|-------------|
| A. Land and Buildings | \$ 668 | \$ 0 |
| B. Equipment | 0 | 0 |
| C. Accumulated Amortization | (195) | 0 |
| D. Total Capital Leases | \$ 473 | \$ 0 |

NOTE 11. LIABILITIES NOT COVERED BY BUDGETARY RESOURCES

| As of September 30 | 2016 | | 2015 | |
|--|------|---------|------|-----------|
| (Amounts in thousands) | | | | |
| 1. Intragovernmental Liabilities | | | | |
| A. Accounts Payable | \$ | 0 | \$ | 0 |
| B. Debt | | 0 | | 0 |
| C. Other | | 47,629 | | 50,057 |
| D. Total Intragovernmental Liabilities | \$ | 47,629 | \$ | 50,057 |
| 2. Nonfederal Liabilities | | | | |
| A. Accounts Payable | \$ | 0 | \$ | 0 |
| B. Military Retirement and Other Federal Employment Benefits | | 256,749 | | 265,430 |
| C. Environmental and Disposal Liabilities | | 0 | | 0 |
| D. Other Liabilities | | 0 | | 0 |
| E. Total Nonfederal Liabilities | \$ | 256,749 | \$ | 265,430 |
| 3. Total Liabilities Not Covered by Budgetary Resources | \$ | 304,378 | \$ | 315,487 |
| 4. Total Liabilities Covered by Budgetary Resources | \$ | 606,523 | \$ | 705,552 |
| 5. Total Liabilities | \$ | 910,901 | \$ | 1,021,039 |

Intragovernmental Other Liabilities represent future-funded Federal Employee's Compensation Act (FECA) liabilities billed to the Army WCF by the Department of Labor (DOL) for payment made by DOL to Army beneficiaries.

Military Retirement and Other Federal Employment Benefits consists of various employee actuarial liabilities not due and payable during the current fiscal year. These liabilities primarily consist of \$256.7 million for FECA actuarial reserve. Refer to Note 17, *Military Retirement and Other Federal Employment Benefits*, for additional details and disclosures.

NOTE 12. ACCOUNTS PAYABLE

| As of September 30 | 2016 | | | | |
|--|------------------|---------|--|-----|------------|
| <i>(Amounts in thousands)</i> | Accounts Payable | | Interest, Penalties, and Administrative Fees | | Total |
| 1. Intragovernmental Payables | \$ | 135,044 | \$ | N/A | \$ 135,044 |
| 2. Nonfederal Payables (to the Public) | | 84,216 | | 0 | 84,216 |
| 3. Total | \$ | 219,260 | \$ | 0 | \$ 219,260 |

| As of September 30 | 2015 | | | | |
|--|------------------|---------|--|-----|------------|
| <i>(Amounts in thousands)</i> | Accounts Payable | | Interest, Penalties, and Administrative Fees | | Total |
| 1. Intragovernmental Payables | \$ | 105,764 | \$ | N/A | \$ 105,764 |
| 2. Nonfederal Payables (to the Public) | | 171,556 | | 0 | 171,556 |
| 3. Total | \$ | 277,320 | \$ | 0 | \$ 277,320 |

Accounts Payable include amounts owed to federal and nonfederal entities for goods and services received by the Army WCF. Buyer-side accounts payable are adjusted to agree with interagency seller-side accounts receivable by reclassifying amounts between federal and nonfederal accounts payable and applying supported and unsupported undistributed disbursements at the reporting entity level.

The Army WCF cannot accurately identify intragovernmental transactions by customer because: (1) the Army Enterprise Systems Integration Program (AESIP) and the System for Award Management (SAM) (vendor master) do not capture the correct buyer and seller data at the transaction level; and, (2) the standard line of accounting (SLOA) has not been implemented by reciprocal trading partners.

NOTE 13. DEBT

Not applicable.

NOTE 14. ENVIRONMENTAL AND DISPOSAL LIABILITIES

Not applicable.

NOTE 15. OTHER LIABILITIESAs of September 30
(Amounts in thousands)

| | 2016 | | | 2015 |
|--|-------------------|----------------------|-------------------|-------------------|
| | Current Liability | Noncurrent Liability | Total | Total |
| 1. Intragovernmental | | | | |
| A. Advances from Others | \$ 36,091 | \$ 0 | \$ 36,091 | \$ 39,932 |
| B. Deposit Funds and Suspense Account Liabilities | 0 | 0 | 0 | 0 |
| C. Disbursing Officer Cash | 0 | 0 | 0 | 0 |
| D. Judgment Fund Liabilities | 0 | 0 | 0 | 0 |
| E. FECA Reimbursement to the Department of Labor | 21,371 | 26,259 | 47,630 | 50,057 |
| F. Custodial Liabilities | 132 | 0 | 132 | 56 |
| G. Employer Contribution and Payroll Taxes Payable | 13,238 | 0 | 13,238 | 22,015 |
| H. Other Liabilities | 0 | 0 | 0 | 0 |
| I. Total Intragovernmental Other Liabilities | \$ 70,832 | \$ 26,259 | \$ 97,091 | \$ 112,060 |
| 2. Nonfederal | | | | |
| A. Accrued Funded Payroll and Benefits | \$ 159,252 | \$ 0 | \$ 159,252 | \$ 198,459 |
| B. Advances from Others | 59,648 | 0 | 59,648 | 62,436 |
| C. Deferred Credits | 0 | 0 | 0 | 0 |
| D. Deposit Funds and Suspense Accounts | 4,960 | 0 | 4,960 | 4,150 |
| E. Temporary Early Retirement Authority | 0 | 0 | 0 | 0 |
| F. Nonenvironmental Disposal Liabilities | | | | |
| (1) Military Equipment (Nonnuclear) | 0 | 0 | 0 | 0 |
| (2) Excess/Obsolete Structures | 0 | 0 | 0 | 0 |
| (3) Conventional Munitions Disposal | 0 | 0 | 0 | 0 |
| G. Accrued Unfunded Annual Leave | 0 | 0 | 0 | 0 |
| H. Capital Lease Liability | 0 | 0 | 0 | 0 |
| I. Contract Holdbacks | 58 | 0 | 58 | 252 |
| J. Employer Contribution and Payroll Taxes Payable | 5,820 | 0 | 5,820 | 10,630 |
| K. Contingent Liabilities | 0 | 8,046 | 8,046 | 10,777 |
| L. Other Liabilities | 100,017 | 0 | 100,017 | 79,525 |
| M. Total Nonfederal Other Liabilities | \$ 329,755 | \$ 8,046 | \$ 337,801 | \$ 366,229 |
| 3. Total Other Liabilities | \$ 400,587 | \$ 34,305 | \$ 434,892 | \$ 478,289 |

Advances from Others represent liabilities for collections received to cover future expenses or acquisitions of assets.

Custodial Liabilities represents liabilities for collections reported as non-exchange revenues where the Army WCF is acting on behalf of another Federal entity.

Nonfederal Other Liabilities of \$100.0 million is for industrial operations service accruals.

Contingent liabilities include \$8.0 million related to contracts authorizing progress payments based on cost as defined in the *Federal Acquisition Regulation* (FAR). In accordance with contract terms, specific rights to a contractor's work vests with the federal government when a specific type of contract financing payment is made. This action protects taxpayer funds in the event of contractor nonperformance. These rights should not be misconstrued as rights of ownership. The Army WCF is under no obligation to pay contractors for amounts

in excess of progress payments authorized in contracts until delivery and government acceptance. Due to the probability the contractors will complete their efforts and deliver satisfactory products, and because the amount of contractor costs incurred but yet unpaid are estimable, the Army WCF has recognized a contingent liability for the estimated unpaid costs considered conditional for payment pending delivery and government acceptance.

Total contingent liabilities for progress payments based on cost represent the difference between the estimated costs incurred to date by contractors and amounts authorized to be paid under progress payments based on cost provisions within the FAR. Estimated contractor-incurred costs are calculated by dividing the cumulative unliquidated progress payments based on costs by the contractor-authorized progress payment rate. The balance of unliquidated progress payments based on cost is deducted from the estimated total contractor-incurred costs to determine the contingency amount.

Capital Lease Liability

Not applicable.

NOTE 16. COMMITMENTS AND CONTINGENCIES

The Army WCF may be a party in various administrative proceedings and legal actions related to claims for environmental damage, equal opportunity matters, and contractual bid protests. The Army WCF is not aware of any contingent liabilities for legal actions.

Additionally, the Army WCF is a party in numerous individual contracts that contain clauses, such as price escalation, award fee payments, or dispute resolution, that may result in a future outflow of budgetary resources. Currently, the Army WCF automated system processes have limited capability to capture these potential liabilities; therefore, the amounts reported may not fairly present the Army WCF's commitments and contingencies. The Army WCF records contingent liabilities in Note 15, *Other Liabilities*.

NOTE 17. MILITARY RETIREMENT AND OTHER FEDERAL EMPLOYMENT BENEFITS

| As of September 30 <i>(Amounts in thousands)</i> | 2016 | | | 2015 |
|--|-------------------|--|----------------------|----------------------|
| | Liabilities | (Less: Assets Available to Pay Benefits) | Unfunded Liabilities | Unfunded Liabilities |
| 1. Pension and Health Benefits | | | | |
| A. Military Retirement Pensions | \$ 0 | \$ 0 | \$ 0 | \$ 0 |
| B. Military Pre Medicare-Eligible Retiree Health Benefits | 0 | 0 | 0 | 0 |
| C. Military Medicare-Eligible Retiree Health Benefits | 0 | 0 | 0 | 0 |
| D. Total Pension and Health Benefits | \$ 0 | \$ 0 | \$ 0 | \$ 0 |
| 2. Other Benefits | | | | |
| A. FECA | \$ 256,749 | \$ 0 | \$ 256,749 | \$ 265,430 |
| B. Voluntary Separation Incentive Programs | 0 | 0 | 0 | 0 |
| C. DoD Education Benefits Fund | 0 | 0 | 0 | 0 |
| D. Other | 0 | 0 | 0 | 0 |
| E. Total Other Benefits | \$ 256,749 | \$ 0 | \$ 256,749 | \$ 265,430 |
| 3. Total Military Retirement and Other Federal Employment Benefits: | \$ 256,749 | \$ 0 | \$ 256,749 | \$ 265,430 |

The Army WCF complies with SFFAS No. 33, *Pensions, Other Retirement Benefits, and Other Postemployment Benefits: Reporting the Gains and Losses from Changes in Assumptions and Selecting Discount Rates and Valuation Dates*.

Federal Employees Compensation Act (FECA) Actuarial liabilities are computed for employee compensation benefits as mandated by the FECA. The Office of Personnel Management provides updated Army actuarial

liabilities during the 4th Quarter of each fiscal year. The Army WCF computes its portion of the total Army actuarial liability based on the percentage of the Army WCF FECA expense to the total Army FECA expense.

The Army WCF actuarial liability for workers' compensation benefits is developed by the Department of Labor (DOL) and provided to the Army WCF at the end of each fiscal year. The liability includes the estimated liability for death, disability, medical, and miscellaneous costs for approved compensation cases, plus a component for incurred but not reported claims. In FY 2015, the DOL refined the approach for selecting the Cost of Living Adjustment (COLA) factors, Consumer Price Index Medical (CPIM) factors, and discount rates by averaging the COLA rates, CPIM factors, and discount rate estimates to reflect historical trends; DOL has continued this approach in FY 2016. The actuarial liability for FECA decreased \$8.7 million between FY 2015 and FY 2016.

DOL selected the COLA factors, CPIM factors, and discount rate by averaging the COLA rates, CPIM rates, and interest rates for the current and prior four years for FY 2016 and FY 2015, respectively. This approach for selecting the factors and discount rate was refined in FY 2015, as using averaging renders estimates that reflect historical trends over five years. DOL selected the interest rate assumptions whereby projected annual payments were discounted to present value based on interest rate assumptions on the U.S. Department of the Treasury's Yield Curve for Treasury Nominal Coupon Issues (the TNC Yield Curve) to reflect the average duration of income payments and medical payments. Discount rates were based on averaging the TNC Yield Curves for the current and prior four years for FY 2016 and FY 2015, respectively. Interest rate assumptions utilized for FY 2016 discounting were as follows:

Discount Rates

For wage benefits:

2.781% in Year 1 and years thereafter;

For medical benefits:

2.261% in Year 1 and years thereafter.

To provide more specifically for the effects of inflation on the liability for future workers' compensation benefits, wage inflation factors (COLAs) and medical inflation factors (CPIMs) were applied to the calculation of projected future benefits. The actual rates for these factors for the charge back year (CBY) 2016 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 CBY were as follows:

| CBY | COLA | CPIM |
|------|-------|-------|
| 2016 | N/A | N/A |
| 2017 | 1.31% | 2.99% |
| 2018 | 1.13% | 3.09% |
| 2019 | 1.23% | 3.40% |
| 2020 | 1.45% | 3.68% |
| 2021 | 1.85% | 3.87% |

[and thereafter]

To test the reliability of the model, DOL made comparisons between projected payments in the last year to actual amounts by agency. Changes in the liability from last year's analysis to this year's analysis were also examined by agency, with any significant differences by agency inspected in greater detail. DOL determined the model has been stable, and has projected the actual payments by agency well.

NOTE 18. GENERAL DISCLOSURES RELATED TO THE STATEMENT OF NET COST

Intragovernmental Costs and Exchange Revenue

For the Years Ended September 30

(Amounts in thousands)

Operations, Readiness & Support

| | 2016 | 2015 |
|--|----------------------------|----------------------------|
| 1. Gross Cost | | |
| A. Intragovernmental Cost | \$ 742,660 | \$ 1,309,371 |
| B. Nonfederal Cost | 19,723,877 | 20,455,144 |
| C. Total Cost | <u>\$ 20,466,537</u> | <u>\$ 21,764,515</u> |
| 2. Earned Revenue | | |
| A. Intragovernmental Revenue | \$ (8,137,232) | \$ (8,008,236) |
| B. Nonfederal Revenue | (10,787,306) | (12,376,626) |
| C. Total Revenue | <u>\$ (18,924,538)</u> | <u>\$ (20,384,862)</u> |
| 3. Losses/(Gains) from Actuarial Assumption Changes for Military Retirement Benefits | \$ 0 | \$ 0 |
| Total Net Cost | <u>\$ 1,541,999</u> | <u>\$ 1,379,653</u> |

Consolidated

| | | |
|--|----------------------------|----------------------------|
| 1. Gross Cost | | |
| A. Intragovernmental Cost | \$ 742,660 | \$ 1,309,371 |
| B. Nonfederal Cost | 19,723,877 | 20,455,144 |
| C. Total Cost | <u>\$ 20,466,537</u> | <u>\$ 21,764,515</u> |
| 2. Earned Revenue | | |
| A. Intragovernmental Revenue | \$ (8,137,232) | \$ (8,008,236) |
| B. Nonfederal Revenue | (10,787,306) | (12,376,626) |
| C. Total Revenue | <u>\$ (18,924,538)</u> | <u>\$ (20,384,862)</u> |
| 3. Losses/(Gains) from Actuarial Assumption Changes for Military Retirement Benefits | \$ 0 | \$ 0 |
| 4. Costs Not Assigned to Programs | \$ 0 | \$ 0 |
| 5. (Less: Earned Revenues) Not Attributed to Programs | \$ 0 | \$ 0 |
| Total Net Cost | <u>\$ 1,541,999</u> | <u>\$ 1,379,653</u> |

The Statement of Net Cost (SNC) represents the net cost of programs and organizations of the Federal Government that are supported by appropriations or other means. The intent of the SNC is to provide gross and net cost information related to the amount of output or outcome for a given program or organization administered by a responsible reporting entity. The DoD's current processes and systems do not capture and report accumulated costs for major programs based upon the performance measures as required by the Government Performance and Results Act. The DoD is in the process of reviewing available data and developing a cost reporting methodology as required by the Statement of Federal Financial Accounting Standards (SFFAS) No. 4, *Managerial Cost Accounting Concepts and Standards for the Federal Government*, as amended by SFFAS No. 30, *Inter-entity Cost Implementation*.

Intragovernmental costs and revenue represent transactions made between two reporting entities within the Federal Government.

Public costs and revenues are exchange transactions made between the reporting entity and a nonfederal entity.

Nonfederal Costs and Revenues include Nonfederal gains and losses which are driven by inventory transactions within LMP. All inventory in LMP is considered nonfederal.

The Army WCF systems do not track intragovernmental transactions by customer. Buyer-side expenses are adjusted to agree with internal seller-side revenues. Expenses were adjusted by reclassifying amounts between federal and nonfederal expenses. Intradepartmental revenues and expenses are then eliminated.

NOTE 19. DISCLOSURES RELATED TO THE STATEMENT OF CHANGES IN NET POSITION

Other Financing Sources, Other on the Statement Changes in Net Position consists of other gains and other losses from non-exchange activity primarily attributable to intragovernmental transfers-in/out for which trading partners could not be identified.

NOTE 20. DISCLOSURES RELATED TO THE STATEMENT OF BUDGETARY RESOURCES

| For the Years Ended September 30 | 2016 | 2015 |
|--|--------------|--------------|
| (Amounts in thousands) | | |
| 1. Net Amount of Budgetary Resources Obligated for Undelivered Orders at the End of the Period | \$ 4,771,736 | \$ 8,333,491 |
| 2. Available Borrowing and Contract Authority at the End of the Period | 0 | 0 |

Abnormal balances are found on the trial balance for the 48XX (Undelivered Orders – Obligations Paid/Unpaid) and 49XX (Delivered Orders – Obligations Paid/Unpaid) series accounts at the object class level. These accounts are normal at the summary level by USSGL account. In 4th Quarter, FY 2013, DDRS-AFS began capturing amounts by object class detail at the USSGL account level. Historical detail was not captured at this level in the source accounting system (LMP) resulting in amounts not properly flowing to the correct object class.

The Army WCF obligations represent reimbursable obligations of \$10.4 billion and direct obligations of \$208.8 million in apportionment category B, apportioned by project or activity.

The Army WCF Statement of Budgetary Resources includes intraentity transactions because the statements are presented as combined.

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

The Army WCF received appropriations in FY 2016 in the amount of \$18.4 million to fund War Reserve materiel, \$32.0 million for Paladin Integrated Management Engines, and \$145.0 million for Arsenal Sustainment Initiative.

During the final two quarters of FY 2015, and the initial two quarters of FY 2016, a comprehensive analysis was undertaken to determine differences in amounts reported for the Army WCF in the Statement of Budgetary Resources (SBR) relative to the source budgetary account balances residing in the LMP. As a result of this analysis, adjustments were made during 3rd quarter, FY 2016 to the Army WCF/LMP budgetary account balances totaling \$23.4 billion. These adjustments reduced erroneous unapportioned budget authority in the Army WCF/LMP from \$23.4 billion to zero; increased Contract Authority Carried Forward \$13.2 billion; increased Budgetary Cash \$7.9 billion; and reduced current year budget authority \$2.2 billion. These adjustments also reduced the variance between LMP and the formal SBR from \$21.1 billion to approximately \$230.0 million.

During the past 10 years, disbursements, collections and related obligations resulting from internal work between the Army WCF Supply Management and Industrial Operations were not reported to Treasury - and not reported on the SBR. The cumulative total of these unreported transactions were \$4.8 billion. In order to correct the Army WCF cash reporting, and to reflect correct budgetary authority and execution, these transactions are being reported to Treasury for FY 2016. At the direction of the OMB, the Army WCF was required to submit a "backdated package" to the U.S. Treasury and the OMB in order to ensure that these transactions were recorded as backdated and prior year events. Since both the unreported disbursements and unreported collections totaled \$4.7 billion, the overall net impact to the Army WCF Fund Balance with Treasury nets to a zero change. However, the FY 2016 Army WCF statements of budget authority and budget execution will reflect net prior year adjustments of \$2.1 billion.

NOTE 21. RECONCILIATION OF NET COST OF OPERATIONS TO BUDGET

For the Years Ended September 30

(Amounts in thousands)

Resources Used to Finance Activities:

Budgetary Resources Obligated:

| | | | | |
|--|----|--------------|----|--------------|
| 1. Obligations incurred | \$ | 10,587,864 | \$ | 10,862,807 |
| 2. Less: Spending authority from offsetting collections and recoveries (-) | | (11,624,095) | | (10,940,323) |
| 3. Obligations net of offsetting collections and recoveries | \$ | (1,036,231) | \$ | (77,516) |
| 4. Less: Offsetting receipts (-) | | 0 | | 0 |
| 5. Net obligations | \$ | (1,036,231) | \$ | (77,516) |

Other Resources:

| | | | | |
|--|----|-----------|----|---------|
| 6. Donations and forfeitures of property | | 0 | | 0 |
| 7. Transfers in/out without reimbursement (+/-) | | (4,891) | | (7,981) |
| 8. Imputed financing from costs absorbed by others | | 133,945 | | 127,635 |
| 9. Other (+/-) | | 144,418 | | 127,838 |
| 10. Net other resources used to finance activities | \$ | 273,472 | \$ | 247,492 |
| 11. Total resources used to finance activities | \$ | (762,759) | \$ | 169,976 |

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 (-) | \$ | 3,561,754 | \$ | (1,963,259) |
| 12b. Unfilled Customer Orders | | (2,810,998) | | 1,616,469 |
| 13. Resources that fund expenses recognized in prior Periods (-) | | (11,108) | | 0 |
| 14. Budgetary offsetting collections and receipts that do not affect Net Cost of Operations | | 0 | | 0 |
| 15. Resources that finance the acquisition of assets (-) | | (2,953,019) | | (2,808,160) |
| 16. Other resources or adjustments to net obligated resources that do not affect Net Cost of Operations: | | | | |
| 16a. Less: Trust or Special Fund Receipts related to exchange in the Entity's Budget (-) | | 0 | | 0 |
| 16b. Other (+/-) | | (139,528) | | (119,856) |
| 17. Total resources used to finance items not part of the Net Cost of Operations | \$ | (2,352,899) | \$ | (3,274,806) |
| 18. Total resources used to finance the Net Cost of Operations | \$ | (3,115,658) | \$ | (3,104,830) |

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 | \$ | 0 | \$ | 0 |
| 20. Increase in environmental and disposal liability | | 0 | | 0 |
| 21. Upward/Downward reestimates of credit subsidy expense (+/-) | | 0 | | 0 |
| 22. Increase in exchange revenue receivable from the public (-) | | (810) | | (3,448) |
| 23. Other (+/-) | | 0 | | 30,186 |
| 24. Total components of Net Cost of Operations that will Require or Generate Resources in future periods | \$ | (810) | \$ | 26,738 |

Components not Requiring or Generating Resources:

| | | | | |
|--|----|-------------|----|-----------|
| 25. Depreciation and amortization | \$ | 245,907 | \$ | 294,231 |
| 26. Revaluation of assets or liabilities (+/-) | | 2,742,426 | | (859,988) |
| 27. Other (+/-) | | | | |
| 27a. Trust Fund Exchange Revenue | | 0 | | 0 |
| 27b. Cost of Goods Sold | | 4,168,495 | | 5,952,394 |
| 27c. Operating Material and Supplies Used | | 0 | | 0 |
| 27d. Other | | (2,498,361) | | (928,892) |
| 28. Total Components of Net Cost of Operations that will not Require or Generate Resources | \$ | 4,658,467 | \$ | 4,457,745 |
| 29. Total components of Net Cost of Operations that will not Require or Generate Resources in the current period | \$ | 4,657,657 | \$ | 4,484,483 |
| 30. Net Cost of Operations | \$ | 1,541,999 | \$ | 1,379,653 |

Due to the Army WCF's financial systems limitations, budgetary data do not agree with proprietary expenses and capitalized assets. This difference is a previously identified deficiency.

Gains/Losses were adjusted by \$1.7 billion to bring the note schedule into agreement with the Statement of Net Cost.

Reconciliation of Net Cost of Operations to Budget lines are presented as combined instead of consolidated as intraagency budgetary transactions are not eliminated:

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

Other Resources. Other consists of other gains and other losses from non-exchange activity primarily attributable to intragovernmental transfers-in/out for which trading partners could not be identified.

Other Resources or adjustments to net obligated resources that do not affect Net Cost of operations, Other consists of other gains and losses from non-exchange activity primarily attributable to intragovernmental transfers-in/out for which trading partners could not be identified and the correction of prior period adjustments that did not meet the materiality thresholds.

Components Requiring or Generating Resources in Future Period, Other consists of FECA expense.

Components not Requiring or Generating Resources Other, Other consists of cost capitalization offsets. Agencies must first record all expenses to Operating Expenses/Program Costs. These expenses are then offset using the Cost Capitalization Offset account when the costs are capitalized to the appropriate "in-process type" account.

■ NOTE 22. DISCLOSURES RELATED TO INCIDENTAL CUSTODIAL COLLECTIONS

Not applicable.

■ NOTE 23. FUNDS FROM DEDICATED COLLECTIONS

Not applicable.

■ NOTE 24. FIDUCIARY ACTIVITIES

Not applicable.

NOTE 25. OTHER DISCLOSURES

As of September 30

Asset Category

(Amounts in thousands)

1. ENTITY AS LESSEE-Operating Leases

Future Payments Due

Fiscal Year

2017

639

2,292

12,910

15,841

2018

651

2,294

13,201

16,146

2019

665

2,296

13,383

16,344

2020

678

2,299

13,481

16,458

2021

692

2,301

13,785

16,778

After 5 Years

712

225

44,406

45,343

Total Future Lease Payments Due

\$

4,037

\$

11,707

\$

111,166

126,910

NOTE 26. RESTATEMENTS

Not applicable.



**INSPECTOR GENERAL**

DEPARTMENT OF DEFENSE
4800 MARK CENTER DRIVE
ALEXANDRIA, VIRGINIA 22350-1500

November 9, 2016

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

SUBJECT: Independent Auditor's Report on the Army Working Capital Fund
FY 2016 and FY 2015 Basic Financial Statements
(Project No. D2016-D000FI-0135.000, Report No. DODIG-2017-009)

Report on the Basic Financial Statements

Public Law 101-576, "Chief Financial Officers Act of 1990," as amended, requires the DoD Inspector General to audit the accompanying Army Working Capital Fund consolidated balance sheet as of September 30, 2016, and 2015, and the related consolidated statement of net cost, consolidated statement of changes in net position, combined statement of budgetary resources, and notes to the basic statements (basic financial statements).

Management's Responsibility for the Annual Financial Statements

Army management is responsible for the annual financial statements. Management is responsible for (1) preparing financial statements that conform with U.S. generally accepted accounting principles (U.S. GAAP); (2) establishing, maintaining, and assessing internal control to provide reasonable assurance that they met broad control objectives of Public Law 97-255, "Federal Managers' Financial Integrity Act of 1982" (FMFIA); (3) ensuring that the Army's financial management systems substantially comply with Public Law 104-208, "Federal Financial Management Improvement Act of 1996" (FFMIA) requirements; and (4) complying with applicable laws and regulations.

Auditor's Responsibility

Our responsibility is to express an opinion on the basic financial statements based on conducting the audit in accordance with generally accepted government auditing standards and the Office of Management and Budget (OMB) Bulletin No. 15-02, "Audit Requirements for Federal Financial Statements," August 4, 2015. However, based on the matters described in the Basis for Disclaimer of Opinion paragraph, we were unable to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

Basis for Disclaimer of Opinion

Section 1008(d) of the FY 2002 National Defense Authorization Act limits the DoD Inspector General to performing only those audit procedures required by generally accepted government auditing standards that are consistent with the representations made by management. Army management asserted to us that the Army Working Capital Fund FY 2016 and FY 2015 Basic Financial Statements would not substantially conform to U.S. GAAP and that Army Working Capital Fund financial management and feeder systems were unable to adequately support material amounts on the basic financial statements as of September 30, 2016. Accordingly, we did not perform all the auditing procedures required by generally accepted government auditing standards and OMB Bulletin No. 15-02 to determine whether material amounts on the basic financial statements were presented fairly. We considered the scope limitation in forming our conclusions on the basic financial statements.

Disclaimer of Opinion

Because of the significance of the matters described in the Basis for Disclaimer of Opinion paragraph, we could not obtain sufficient appropriate evidence to provide a basis for an audit opinion. Accordingly, we do not express an opinion on the Army Working Capital Fund FY 2016 and FY 2015 Basic Financial Statements. Thus, the basic financial statements may have undetected misstatements that are both material and pervasive.

Other Information in the Annual Financial Statements

We performed our audit to form an opinion on the basic financial statements as a whole. Army management presented the Management's Discussion and Analysis, Required Supplementary Information, and Other Information for additional analysis as part of the annual financial statements. These elements are not required parts of the basic financial statements. Therefore, we do not express an opinion or provide any assurance on the information. We reviewed the other information for inconsistencies with the

audited basic financial statements. Based on our limited review, we found material inconsistencies between the information and the basic financial statements and applicable sections of OMB Circular No. A-136 (Revised), "Financial Reporting Requirements," October 7, 2016, and DoD Regulation 7000.14-R, "Financial Management Regulation," volume 6b, "Form and Content of the Department of Defense Audited Financial Statements." Specifically, Management's Discussion and Analysis did not contain sufficient information specific to the Army Working Capital Fund to meet guidance requirements.

Report on Compliance With Applicable Provisions of Laws, Regulations, Contracts, and Grant Agreements

We limited our audit to determining compliance with provisions of applicable laws and regulations, contracts, and grant agreements that have a direct and material effect on the basic financial statements, and compliance with OMB regulations and audit requirements for financial reporting because management represented that instances of noncompliance identified in prior audits continue to exist. Therefore, we did not determine whether the Army Working Capital Fund complied with all applicable laws and regulations, contracts, and grant agreements related to financial reporting. It was not our objective to provide an opinion on compliance with certain provisions of laws and regulations, contracts, and grant agreements, and accordingly, we do not express such an opinion.

See Attachment 1 for additional details on internal control and compliance with legal and other regulatory requirements.

Agency Comments and Our Evaluation

We provided a draft of this report to the Deputy Assistant Secretary of the Army (Financial Operations), who provided technical comments we have incorporated as appropriate. The Deputy Assistant Secretary expressed continuing commitment to address the problems this report outlines. See Attachment 2 for the full text of the management comments.

This report will be made publicly available pursuant to section 8M, paragraph (b)(1)(A) of the Inspector General Act of 1978, as amended. However, this report is intended solely for the information and use of Congress; the OMB; the U.S. Government Accountability Office; Under Secretary of Defense (Comptroller)/Chief Financial Officer, DoD; Army management; and the DoD Office of Inspector General. It is not intended to be used and should not be used by anyone else.

We appreciate the courtesies extended to the staff. Please direct questions to me at (703) 601-5945 or (DSN) 329-5945.

A handwritten signature in cursive script that reads "Lorin T. Venable".

Lorin T. Venable, CPA

Assistant Inspector General

Financial Management and Reporting

Attachments: As stated

Report on Internal Control Over Financial Reporting

Internal Control Compliance

In planning our audit, we considered the Army Working Capital Fund's internal control over financial reporting. We did this to determine our procedures for auditing the basic financial statements appropriate to the circumstances, for the purposes of expressing our opinion on the basic financial statements, but not appropriate to the purpose of expressing an opinion on the effectiveness of the internal control. Accordingly, we do not express an opinion on internal control over financial reporting.

Management Responsibilities

Management is responsible for implementing and maintaining effective internal controls to include providing reasonable assurance that Army personnel recorded, processed, and summarized accounting data properly; met the requirements of applicable laws and regulations; and safeguarded assets against misappropriation and abuse.

Auditor's Responsibilities

Our purpose was not to express an opinion on internal controls over financial reporting, and we do not do so. However, the following material weaknesses continue to exist that could adversely affect the Army Working Capital Fund's financial operations.

Previously Identified Material Weaknesses

Management acknowledged that previously identified material weaknesses continued to exist. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the Army Working Capital Fund's financial statements will not be prevented, or detected and corrected, on a timely basis. The following material weaknesses continue to exist.

Financial Management Systems. Army Working Capital Fund systems do not meet the requirements for full accrual accounting. The systems do not collect and record financial information as required by U.S. GAAP.

The Army derives reported values and information for major asset and liability categories from the Logistics Modernization Program system. However, the Logistics Modernization Program system contains certain system and posting deficiencies as well as erroneous and incomplete account balances. In addition, the Army Working Capital

Fund financial statements and the Logistics Modernization Program system continue to rely on data from non-financial feeder systems. The financial and non-financial feeder systems do not contain the required system integration to provide a transaction-level audit trail for the amounts reported in the proprietary and budgetary general ledger accounts.

The Government Accountability Office's Report No. GAO-14-51, "Army Should Track Financial Benefits Realized from its Logistics Modernization Program," November 2013, cites Army officials as stating that although the Logistics Modernization Program system is functional, it does not support certain critical requirements that have emerged since its initial development, such as automatically tracking repair and manufacturing operations on the shop floor of depots and arsenals. The report further stated the current system will not enable the Army to generate auditable basic financial statements by FY 2017, the statutory deadline for this goal. The recommendations from this report remain outstanding.

DoD Inspector General Report No. DODIG-2014-066, "Logistics Modernization Program System Not Configured to Support Statement of Budgetary Resources," May 5, 2014, states that Army financial managers did not assess the DoD transaction codes to determine applicability to Army Working Capital Fund business areas or to incorporate existing manual workarounds. Changes made within the Logistics Modernization Program system, based upon the recommendations from this report, are to be completed at the end of first quarter FY 2017.

Fund Balance With Treasury. According to Statement of Federal Financial Accounting Standards No. 1, "Accounting for Selected Assets and Liabilities," Fund Balance with Treasury is the aggregate amount of funds in the entity's accounts with Treasury for which the entity is authorized to make expenditures and pay liabilities. DoD Inspector General Report No. DODIG-2014-066 states that Army financial managers did not accomplish the reengineering needed to integrate the Treasury reconciliation function into the Logistics Modernization Program system or provide the capability to receive cash management files directly from Treasury to reconcile them. This requires the Army Working Capital Fund to adjust its balances to agree with the U.S. Treasury amounts each month.

Inventory. The Army reported its entire resale inventory in the Logistics Modernization Program system, which is capable of recording inventory using moving average cost. However, the Army reported within its Annual Statement of Assurance for FY 2016 that current inventory balances in the financial statements are not reliable.

Inventory control procedures do not effectively provide assurance that inventory recorded in the financial statements exists and is complete. In addition, the moving average cost used for reporting inventory did not accurately reflect the historical cost of the inventory or produce an auditable approximation of historical cost as required by Statement of Federal Financial Accounting Standards No. 3, "Accounting for Inventory and Related Property." DoD Inspector General Report No. DODIG-2016-108, "Army Needs Greater Emphasis on Inventory Valuation," July 12, 2016, states that despite the Logistics Modernization Program system having the functionality to compute moving average cost, U.S. Army Materiel Command did not properly record 83 of 128 nonstatistically sampled items from 18 of 557 plants in a manner that reasonably approximated historical cost. U.S. Army Materiel Command did not establish controls to identify and correct improper moving average cost values, prevent improper data from updating within the Logistics Modernization Program system during end-of-day reconciliations, or properly establish data for Non Army Managed Items unit of measure elements in the system. Finally, the Army did not develop a comprehensive strategy for implementing moving average cost as the methodology for valuing its inventory in the Logistics Modernization Program system. The Army's plan of corrective actions for the recommendations from this report is scheduled to be completed at the end of FY 2017.

DoD Inspector General Report No. DODIG-2015-128, "Army Needs to Improve Processes Over Government-Furnished Material Inventory Actions," May 21, 2015, states that Army Working Capital Fund activities expensed Government-furnished material upon shipment to contractors, which understated the inventory assets on the balance sheet. The Army did not integrate accountability reporting into the Logistics Modernization Program system. Consequently, the system could not be used to identify what Government-furnished material contractors had on hand and when Government-furnished material was consumed by contractors or otherwise returned to the Army. Additionally, the Army did not have a reporting mechanism to track receipt and consumption of Government-furnished material required for quarterly reports to contract administration offices. The Army's plan of corrective actions for the recommendations from this report is scheduled to be completed at the end of FY 2017.

General Property, Plant, and Equipment. The reported value of Army Working Capital Fund's General Property, Plant, and Equipment is unreliable because the Army lacks the documentation needed to support the historical acquisition costs of its assets. In addition, the Army has not fully implemented DoD Instruction 5000.64,

“Accountability and Management of DoD Equipment and Other Accountable Property,” May 19, 2011, that requires an entity to maintain information in its property systems on all property furnished to contractors.

Accounts Payable. Statement of Federal Financial Accounting Standards No. 1, “Accounting for Selected Assets and Liabilities,” requires intragovernmental transactions to be reported separately from amounts owed to the public. The Army acknowledged that Army Working Capital Fund’s systems do not track intragovernmental transactions by customer at the transaction level. As a result, the Army relied on unsupported adjustments processed by Defense Finance and Accounting Service personnel to report accounts payable balances. Additionally, DoD Inspector General Report No. DODIG-2012-087, “Logistics Modernization Program System Procure-to-Pay Process Did Not Correct Material Weaknesses,” May 29, 2012, states that the Procure-to-Pay business processes developed for use within the Logistics Modernization Program system did not properly approve, verify, or reconcile transactions or record and document business events accurately, including accounts payable. The Army reported within its Annual Statement of Assurance for FY 2016 that the Logistics Modernization Program system still cannot generate an accounts payable upon acceptance of goods until they actually arrive at their final destination.

Statement of Budgetary Resources. OMB Circular No. A-136 (Revised) states that the entity should develop the statement of budgetary resources predominantly from the budgetary general ledger accounts, in accordance with budgetary accounting rules. In FY 2013, the Army began using the data from the Army Working Capital Fund budgetary general ledger accounts reported by the Logistics Modernization Program system to populate the statement of budgetary resources. However, Defense Finance and Accounting Service personnel continue to enter a significant number of adjustments into the Defense Departmental Reporting System–Budgetary module to reconcile the trial balance data. The Army performed a comprehensive analysis to determine differences reported in the statement of budgetary resources relative to the source budgetary account balances residing in Logistics Modernization Program system. As a result of this analysis, adjustments were made during the third quarter FY 2016 in the Logistics Modernization Program system totaling \$23.4 billion.

Additionally, DoD Inspector General Report No. DODIG-2014-066 states that the Logistics Modernization Program system did not contain the Budget-to-Report business process functionality to report the data needed to prepare the Army Working

Capital Fund statement of budgetary resources. The system omitted this functionality because Army financial managers did not provide correct system configuration to the Logistics Modernization Program Product Management Office. The Army's plan of correction actions for the recommendations from this report remain outstanding.

Statement of Net Cost. The financial information in the Statement of Net Cost is not presented by programs that align with major goals and outputs described in the DoD strategic and performance plans required by the Government Performance and Results Act of 1993. This was not possible because Army Working Capital Fund financial management systems did not accurately account for intragovernmental transactions or capture actual costs. Some information in the Army Working Capital Fund's statement of net cost was based on non-financial feeder systems. Additionally, a significant portion of the costs and revenues reported within this statement are recorded within general ledger accounts for gains and losses which further complicates aligning the costs and revenues by major goals and outputs.

Intragovernmental Eliminations. The Army Working Capital Fund was unable to collect, exchange, or reconcile buyer and seller intragovernmental transactions, resulting in adjustments that were not verifiable. DoD Inspector General Report No. DODIG-2012-087 stated that the Logistics Modernization Program system did not capture the correct Standard Financial Information Structure business partner information at the transaction level needed to facilitate reconciling and eliminating intragovernmental transactions. The corrective actions planned for the recommendations from this report remain outstanding. DoD procedures require that the Army adjust its buyer-side transaction data to agree with seller-side transaction data from other Government entities, without the entities performing proper reconciliations. As a result, Defense Finance and Accounting Service personnel made \$2.9 billion in adjustments to Army Working Capital Fund accounts to force the accounts to agree with the corresponding records of intragovernmental trading partners.

Accounting Adjustments. Defense Finance and Accounting Service personnel made unsupported accounting adjustments, valued at \$4.7 billion, to reclassify amounts based on problems with the posting logic. The unsupported accounting adjustments represent a material uncertainty regarding the line-item balances on the Army Working Capital Fund FY 2016 Basic Financial Statements.

Reconciliation of Net Cost of Operations to Budget. Statement of Federal Financial Accounting Standards No. 7, “Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting,” requires a reconciliation of proprietary and budgetary information to assist users in understanding the relationship of the data. The Army could not reconcile the information reported in Note 21 of the Army Working Capital Fund FY 2016 Basic Financial Statements without preparing \$1.7 billion in unsupported adjustments to gain and loss accounts to force costs to match obligation information. The Army reported in the FY 2016 Annual Statement of Assurance the need for an interim solution to perform tie point analysis between the budgetary and proprietary accounts. In addition, the Army reported that additional work needs to be done to correct existing data before it makes system and process changes.

Abnormal Account Balances. In FY 2016, the Army Working Capital Fund Industrial Operations and Supply Management activities (limit-level) reported 33 limits with abnormal account balances, with an absolute value of \$3.5 billion, in the balance sheet. Army and Defense Finance and Accounting Service personnel used the abnormal balances to compute the amounts reported for such items as Fund Balance with Treasury; Accounts Receivable; Advance and Prepayments; General Property, Plant, and Equipment; Inventory; and Accounts Payable. In addition, the posting accounts used to develop the proprietary and budgetary trial balances in the Logistics Modernization Program system contained at least 820 abnormal account balances with an absolute value of \$130.0 billion. However, the roll-up of limit-level account balances to produce amounts on the financial statements hid abnormal account balances identified in the posting accounts.

These financial management control deficiencies may cause inaccurate management information. As a result, the Army management decisions based in whole or in part on this information may be adversely affected. Financial information reported by the Army may also contain misstatements resulting from these deficiencies. Internal control work we conducted as part of our prior audits would not necessarily disclose all material weaknesses and significant deficiencies. We did not identify material weaknesses that were not reported as such in the Army Working Capital Fund’s FMFIA report.

Report on Compliance With Applicable Provisions of Laws, Regulations, Contracts, and Grant Agreements

U.S. generally accepted government auditing standards and OMB guidance require auditors to report on entities' compliance with selected provisions of laws and regulations, contracts, and grant agreements. Management is responsible for compliance with existing laws and regulations, contracts, and grant agreements related to financial reporting. Management has also acknowledged to us that previously reported instances of noncompliance continue to exist. Therefore, we did not determine whether the Army Working Capital Fund complied with selected provisions of all applicable laws and regulations, contracts, and grant agreements related to financial reporting. We caution that other noncompliance may have occurred and not been detected. Furthermore, the results of our limited procedures may not be sufficient for other purposes. Our objective was not to, and we do not, express an opinion on compliance with applicable laws, regulations, contracts, and grant agreements. Because of other scope limitations discussed in this report, we limited our work to determining compliance with selected provisions of the applicable laws and regulations.

Antideficiency Act

Section 1341, title 31, United States Code (31 U.S.C. § 1341 [1990]), limits the Army and its agents to making or authorizing expenditures or obligations that do not exceed the available appropriations or funds. Additionally, the Army or its agents may not contract or obligate for the payment of money before an appropriation is made available for that contract or obligation unless otherwise authorized by law. As stated in 31 U.S.C. § 1517 (2004), the Army and its agents are prohibited from making or authorizing expenditures or obligations exceeding an apportionment or the amount permitted by prescribed regulations. According to 31 U.S.C. § 1351 (2004), if an officer or employee of an executive agency violates the Antideficiency Act (ADA), the head of the agency must report immediately to the President and Congress all relevant facts and a statement of actions taken. During FY 2016, the Army Working Capital Fund reported no ADA violations.

Compliance With FFMIA Requirements

The FFMIA requires the Army to establish and maintain financial management systems that comply substantially with the Federal financial management systems requirements, applicable Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level. For areas in which an agency is not in

compliance, OMB A-136 requires the agency to identify remediation activities planned or underway to bring the systems into substantial compliance with the FFMIA. The DoD Financial Improvement and Audit Readiness Plan Status Report, May 2016, identifies actions the Army is taking to improve the Army Working Capital Fund financial statements. The Army is committed to achieving and sustaining audit readiness, which includes plans for improving financial management systems.

For FY 2016, the Deputy Assistant Secretary of the Army (Financial Operations) acknowledged that the Army Working Capital Fund did not substantially comply with the FFMIA. The Deputy Assistant Secretary also acknowledged to us that Army Working Capital Fund financial management and feeder systems could not provide adequate evidence supporting various material amounts on the financial statements and that previously identified material weaknesses continue. The financial management and feeder systems did not substantially comply with the Federal financial management systems requirements, Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level as of September 30, 2016. Therefore, based on the representation of the Deputy Assistant Secretary of the Army (Financial Operations), we did not substantiate whether the Army Working Capital Fund complied with FFMIA and OMB implementation guidance.

Recommendations

This report does not include recommendations to correct the material weaknesses and instances of noncompliance with laws and regulations, because previous audit reports contained recommendations for corrective actions or because current audit projects will include appropriate recommendations.



DEPARTMENT OF THE ARMY
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FINANCIAL MANAGEMENT AND COMPTROLLER
 109 ARMY PENTAGON
 WASHINGTON DC 20310-0109

SAFM-FO
 2016

4 November 2016

MEMORANDUM FOR Deputy Inspector General for Auditing, Department of Defense

SUBJECT: Management Response to the Fiscal Year 2016 Army Working Capital Fund Financial Statement Audit Report

1. We appreciate the efforts and professionalism your staff exhibited during the audit of the fiscal year 2016 Army Working Capital Fund Financial Statements. We also appreciate the opportunity to comment on the draft report provided to us on November 2, 2015.
2. We concur with the findings identified in the draft report on Internal Control. Our audit readiness corrective action plans will continue to address the findings identified. We will continue working with our stakeholders to correct issues related to our general ledger, journal vouchers, adjustments, posting logic, and abnormal balances. Our audit readiness support contractor will continue efforts to review field-level operational data, internal controls, and system controls necessary to ensure accuracy of the financial statements. Our service provider, the Defense Finance and Accounting Service, is continuing corrective actions for the Fund Balance with Treasury reconciliation. During fiscal year 2017, the Army will undergo an audit of Statement of Budgetary Resources performed by an Independent Public Accounting firm.
3. We continue improvements to Logistics Modernization Program and implementing other financial improvement initiatives. We will improve trading partner reporting and enable reconciliation of intragovernmental transactions between Federal agencies with these initiatives. The goal is for these actions to result in supportable quarterly reporting to Treasury and the Office of Management and Budget, and ultimately correct a long-standing material weakness.
4. The point of contact for this action is [REDACTED]. She can be reached by telephone at [REDACTED], or by e-mail at [REDACTED].

MILLER.WESLEY.C.
 1104827051

Wesley C. Miller
 Deputy Assistant Secretary Army
 (Financial Operations)

Digitally signed by MILLER.WESLEY.C.1104827051
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 Date: 2016.11.04 15:48:41 -0400



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FISCAL YEAR 2016 UNITED STATES ARMY ANNUAL FINANCIAL REPORT

We are interested in your feedback regarding the content of this report.
Please feel free to e-mail your comments to AAFS@hqda.army.mil or write to:

DEPARTMENT OF THE ARMY
Office of the Deputy Assistant Secretary of the Army
(Financial Management and Comptroller)

Office of the Financial Reporting Directorate
Room 3A312, 109 Army Pentagon
Washington, DC 20310-0109

*Additional copies of this report can be obtained by sending a written request to the e-mail or mailing address listed above.
You may also view this document at: <http://www.asafrn.army.mil/fo/fod/cfo/cfo.asp>*

THE SOLDIER'S CREED

I am an American Soldier.
I am a Warrior and a member of a team.
I serve the people of the United States
and live the Army Values.

I will always place the mission first.
I will never accept defeat.
I will never quit.
I will never leave a fallen comrade.

I am disciplined, physically and mentally tough, trained and proficient in my
warrior tasks and drills.
I always maintain my arms, my equipment and myself.

I am an expert and I am a professional.

I stand ready to deploy, engage, and destroy the enemies of the United States of
America in close combat.

I am a guardian of freedom and the
American way of life.

I am an American Soldier.

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