Audited
Financial Statements

Fiscal Year 2005

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Fiscal Year 2005

Defense Threat Reduction Agency
Fort Belvoir, VA 22060-6201

DEFENSE THREAT REDUCTION AGENCY (DTRA)

MANAGEMENT'S DISCUSSION AND ANALYSIS (MD&A)
FISCAL YEAR 2005

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Message from the Chief Financial Officer

November 8, 2005

I am pleased to present the Defense Threat Reduction Agency (DTRA) Management's Discussion and Analysis (MD&A) for Fiscal Year 2005. This report summarizes the Agency's mission, organization, programmatic achievements, financial status, and business priorities for Fiscal Year 2005.

DTRA is a proud organization performing a vital national security mission: reducing the threat of weapons of mass destruction (WMD). We are a Defense combat support agency with more than 2,000 personnel coming from the military services, the Federal civil service, universities, non-governmental organizations, and corporate America.

DTRA works around the world to pursue and accomplish our mission by taking threat reduction to the source, stopping the spread of WMD, securing and dismantling strategic offensive arms, taking the fight to the enemy, detecting WMD threats, protecting our Nation against weapons of terror, and deterring WMD use.

DTRA is also committed to organizational excellence and sound financial management. I am pleased to report that for FY 2005, DTRA received an unqualified "clean" audit opinion on its financial statements for a fourth consecutive year. This audit result indicates that DTRA's financial statements are a reliable reflection of DTRA's financial position.

As required by Section 1116(e) of Title 31 of the U.S.C., the financial and performance information contained in this report is complete and reliable and DTRA is in substantial compliance with the requirements of the Federal Managers' Financial Integrity Act (FMFIA) and Federal Financial Management Improvement Act (FFMIA).

DTRA plays a vital role in ensuring that U.S. capabilities to combat WMD remain the best in the world, and the American people who support these activities with their tax dollars are rewarded with a substantial return on their investment.

Myron K. Kunka

Myron K. Kunka
Chief Financial Officer

Management Discussion & Analysis FY 2005

1.0 Mission, Organization, and Resources

The Defense Threat Reduction Agency (DTRA) was established on October 1, 1998 under the Defense Reform Initiative (DRI). The Department of Defense (DoD) created DTRA as a Combat Support Agency to focus department capabilities in the fight against weapons of mass destruction. DTRA provides DoD a means to deal more effectively with threats posed by nuclear, chemical, and biological weapons. The DTRA organization is a consolidation of the former On-Site Inspection Agency (OSIA), Defense Special Weapons Agency (DSWA), elements of the Offices of the Under Secretary of Defense for Policy (USD (P)), and the Assistant to the Secretary of Defense for Nuclear, Chemical and Biological Defense Programs, (ATSD (NCB)). DTRA is a DoD Agency under the authority, direction, and control of the Under Secretary of Defense for Acquisition, Technology, and Logistics (USD(AT&L)).

1.1 Mission

The mission of the DTRA is to safeguard America's interests from weapons of mass destruction (WMD), chemical, biological, radiological, nuclear and high explosives (CBRNE), by controlling and reducing the threat, and by providing quality tools and services for the warfighter. DTRA supports the three pillars of the National Strategy on combating WMD, which are nonproliferation, counterproliferation and consequence management. The Agency also supports U.S. Strategic Command in combating WMD. The following strategic goals are identified in DTRA's Strategic Plan and provide the framework for accomplishing DTRA's mission.

- **Deter the Use and Reduce the Impact of WMD** - The fundamental goal of deterring the use of WMD underpins the mission and activities of DTRA. DTRA pursues a multi-faceted approach, focusing on the U.S. nuclear force, support of missile defense programs and the science, technology, and demonstration of counterproliferation capabilities. This also enhances our support to civil and military crisis and consequence management response capabilities.

- **Reduce the Present Threat** - DTRA looks to execute and expand treaty and non-treaty efforts to control, safeguard and eliminate existing weapon capabilities, and to foster efforts to evaluate and counter WMD threats from all potential adversaries.

- **<u>Prepare for Future Threats</u>** - DTRA strives to predict emerging WMD capabilities, evaluate threats from potential adversaries, and develop new technologies to assist the warfighter of the future by providing powerful tools to counter specific threats and to protect personnel, infrastructure, and mission critical systems.

- **<u>Conduct the Right Programs in the Best Manner</u>** - DTRA is committed to being a good steward of the Nation's resources. DTRA reviews its programs regularly, incorporates best business practices, optimizes current workforce distribution, determines future needs, and builds beneficial relationships with DoD, other U.S. Government agencies, industry and international partners concerned with threat reduction.

- **<u>Develop our People and Enable Them to Succeed</u>** - DTRA is committed to attracting and retaining a trained, satisfied and highly-motivated workforce. DTRA strives to clearly articulate its values and expected behaviors encourage and reward excellence, and sustain high individual and organizational performance. Furthermore, DTRA endeavors to create an effective, healthy, safe, secure and accessible workplace.

1.2 Organization

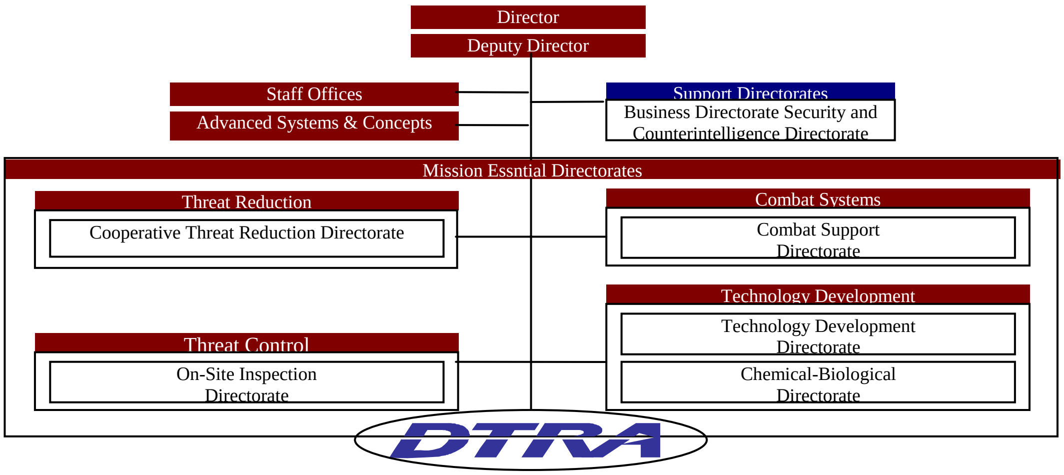
To fulfill its mission and strategic goals, DTRA operates under the authority, direction, and control of the Under Secretary of Defense for Acquisition, Technology and Logistics (USD (AT&L)). DTRA is designated as a Defense combat support agency for certain functions specified by the Secretary of Defense. Additionally, the Threat Reduction Advisory Committee (TRAC), which is composed of distinguished policy, scientific, and defense experts, was established to advise DTRA and other senior defense officials in identifying threats and emerging WMD challenges.

1.2.1 Directorates

DTRA's staff offices and support directorates perform key infrastructure and support functions for the Agency. These offices provide advice and services in the areas of security, logistics, financial management, administration, personnel, equal opportunity, information technology (IT), and acquisition. There are five directorates that directly support DTRA's critical mission: On-Site Inspection Directorate (OS), Combat Support Directorate (CS), Technology Development Directorate (TD), Chemical-Biological Defense Directorate (CB), and Cooperative Threat Reduction Directorate (CT).

In addition, DTRA is also supported by the Advanced Systems and Concepts Office (ASCO), the Business Directorate (BD), and the Security and the Counterintelligence Directorate (SC).

The FY2005 DTRA organizational structure is depicted below.



Although the Chemical-Biological Defense Directorate is a part of DTRA, funding for the Chemical-Biological Defense Program is appropriated to the Office of the Secretary of Defense (OSD) in a separate account and is not part of DTRA's direct Total Obligation Authority (TOA). As such, details of the Chemical-Biological Defense Program are not addressed in this report.

1.3 Resources

DTRA's authorization is 1,082 civilian full-time equivalent (FTE) employees and 808 active duty military. DTRA's FY 2005 Total Obligation Authority (TOA) is presented, by appropriation, in the following table.

Appropriation	FY 2005 Budget Authority (Millions)
Operation and Maintenance	$312.6
RDT&E	395.0
RDT&E (X Year Funding)	60.0
Procurement	23.3
Former Soviet Union Threat Reduction	407.8
Total	$1,198.7

1.4 Worldwide Presence

The Defense Threat Reduction Center (DTRC) was completed in September 2005. The DTRC makes significant progress toward the goal of achieving optimal organizational synergy, efficiency, and force protection by consolidating DTRA's National Capital Region (NCR) activities in one location. The DTRC is a 308,000 square foot addition to the McNamara building at the Ft. Belvoir Headquarters Complex. It accommodates approximately 1,400 people. Special spaces include a large computer center, a Sensitive Compartmented Information Facility (SCIF), and a state of the art Operations Center, a space dedicated to computer modeling of potential WMD attacks. This Modeling Center develops tests and provides modeling capability throughout DoD. The construction was programmed in the amount of $75,388,000. The design cost was approximately $5 million.

In addition to its NCR activities, DTRA maintains operations in Albuquerque, NM, San Francisco, CA, and Mercury, NV. DTRA also maintains worldwide operations in support of its missions. Germany is home to the European Operations Division of the On-Site Inspection Directorate, and provides gateway support to American inspection teams transiting from the U.S. to points further east. DTRA mans and operates the Arms Control Implementation Units located in U.S. embassies in Kazakhstan, Russia and Ukraine.

DTRA provides support for U.S. inspection, observation and portal monitoring teams through the former Soviet Union (FSU), as well as for the implementation of the Cooperative Threat Reduction program. Employees of DTRA's On-Site Inspection Directorate stationed in Japan assist U.S. inspection and observation teams traveling to Far East points of entry in the FSU. In recognition of DTRA's combat support mission, liaison personnel are located at appropriate sites to enhance responsiveness to the Combatant Commanders in meeting critical warfighting needs.

2.0 Performance, Goals, Objectives and Results

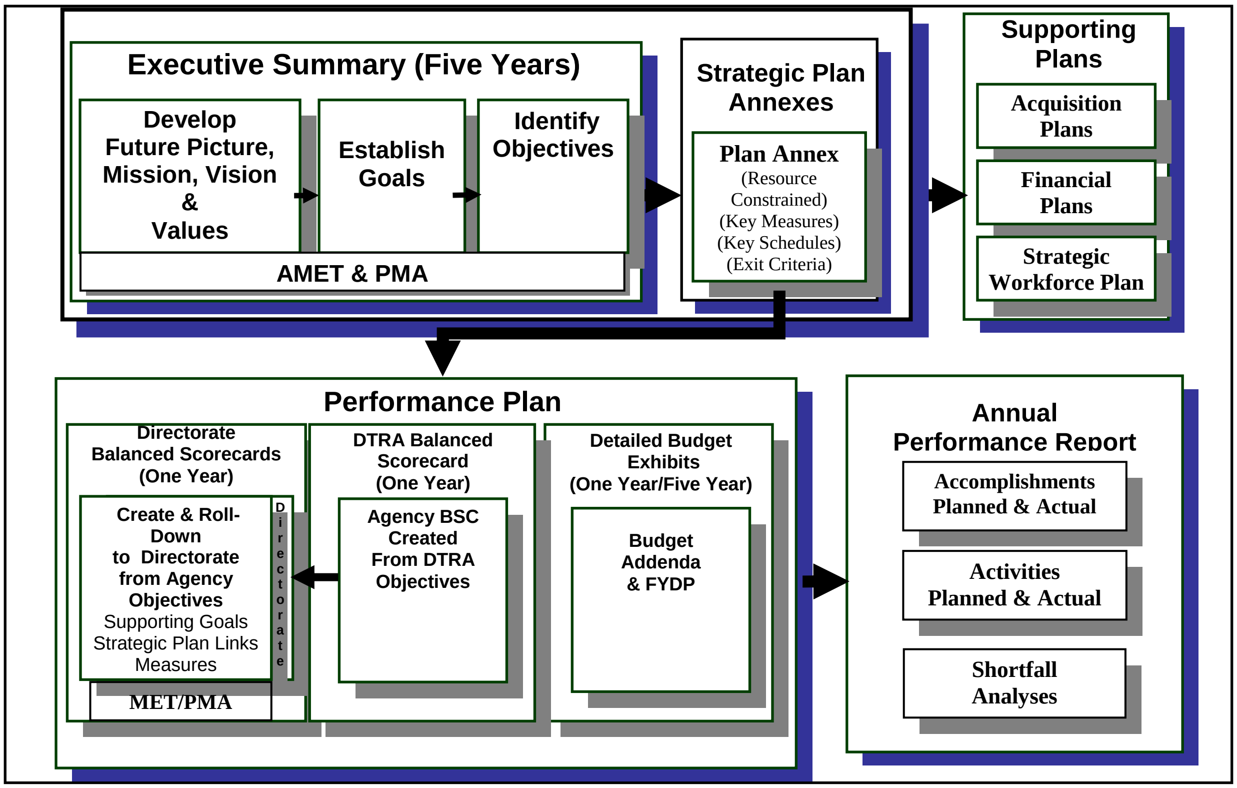
2.1 Strategic Plan

The Agency receives strategic planning guidance from the National Military Strategy and other DoD planning guidelines. Through its strategic planning process, DTRA ensures the products and services offered enhance DoD's capabilities to achieve national military objectives and operational requirements.

During FY 2005, DTRA revised its management framework in order to achieve additional integration and reduce duplicative activities. In its next strategic plan, DTRA will align and direct Agency resources and planning efforts to develop a "Future Picture" of what the Agency objectives will be in 10-15 years. Another key aspect of this revision is to integrate shaping tasks, the President's Management Agenda (PMA), Agency Mission Essential Task (AMET) List items (derived from the Joint Chiefs of Staff Uniform Joint Task List), internal mission essential tasks (METs), and other such reporting requirements into the annual DTRA and Directorate Balanced Scorecards. This will consolidate and standardize reporting.

The Agency evaluated its performance indicators to ensure they accurately reflect progress on issues, provide a good measurement of success, and focus on where DTRA resources are applied. To ensure alignment with its strategic plan, the annual DTRA scorecard will be more closely aligned with the Agency's strategic goals and objectives. Shown below is a schematic depicting DTRA's revised strategic planning and performance measurement framework, which was phased in during FY 2005.

DTRA Strategic Planning Framework 2005



2.2 Strategic Objectives

To accomplish the overall Agency mission within the organizational structure identified above, DTRA has identified four mission areas. While DTRA's directorates may focus on a particular function, there is a synergy between the directorates due to their particular expertise. Accordingly, resources have been allocated to support critical requirements across the combat support, technology development, threat control, and threat reduction mission areas.

- **<u>Combat Support</u>** – DTRA provides combat support to the Joint Chiefs of Staff (JCS), the Joint Staff, the Combatant Commanders and the military services to deter, engage, and assess the threat and challenges posed to the United States, its forces, and its allies by WMD. This mission area is primarily the responsibility of DTRA's Chemical-Biological, Combat Support and Technology Development Directorates.

- **Technology Development** – DTRA develops, manages, coordinates and conducts research and development activities to enhance and enable WMD combat support, threat control and threat reduction. This mission area is primarily the responsibility of DTRA's Technology Development and Chemical-Biological Directorates.

- **Threat Control** – DTRA shapes, manages and implements arms control and other non-treaty efforts to control, safeguard and eliminate nuclear, biological, chemical, conventional, and other special weapons. This mission area is primarily the responsibility of the On-Site Inspection Directorate.

- **Threat Reduction** - DTRA provides assistance to eligible states of the FSU to dismantle WMD and to reduce the threat of WMD proliferation. This mission area is primarily the responsibility of the Cooperative Threat Reduction Directorate.

DTRA has developed and matured a carefully crafted management framework for strategic planning, integrating Agency strategic planning and resource allocation efforts as required under the Government Performance and Results Act (GPRA). The Agency uses performance planning and measurement to ensure that the organization reaches its objectives and goals. In fiscal year 2005, DTRA used the strategic planning framework below.

2.3 Policy Goals

DTRA's policy goals are tied to the Three Pillars of National Strategy:

a. Nonproliferation. Using the full range of diplomatic, economic, informational and military instruments of national power to prevent or limit the acquisition or development of WMD capabilities. This includes:
   - Treaty verification
   - Non-treaty bilateral and multilateral cooperation
   - Safeguarding and eliminating former Soviet WMD capabilities
   - Proliferation prevention
   - Support to U.S. and foreign chemical weapons elimination

b. Counterproliferation. Using the full range of military activities to deter, identify, deny and counter adversary development, acquisition, possession, proliferation and use of WMD. This goal includes:
   - Maintain and improve U.S. nuclear deterrent
   - Radiation hardening
   - WMD agent detection, tracking and defeat
   - Chemical, Biological, Radiological, Nuclear, High Explosive (CBRNE) mitigation technologies
   - Hard and deeply buried target defeat
   - Rapid installation recovery from WMD attacks
   - Anti-terror assessments

c. Consequence Management. Mitigating the long-term effects of a WMD attack and enabling rapid recovery. This goal includes:
   - WMD effects modeling and simulation
   - Chemical, Biological, Radiological, Nuclear (CBRN) decontamination technologies
   - WMD response planning and training
   - WMD incident and accident exercise support
   - WMD reachback

2.4 Performance Goals and Assessments

Performance assessments continue to be an integral part of DTRA's strategic planning process. Beginning in FY 2002, DTRA implemented a comprehensive internal performance assessment process to identify and adopt meaningful, quantitative measures of progress and accomplishments. DTRA prepares and publishes annual performance plans for all mission areas using a Balanced Scorecard approach. These Balanced Scorecards further define the objectives of the strategic plan and measure progress using the following DoD Risk Management Perspectives:

- Providing a trained and ready force.
- Addresses our ability to recruit, retain and train sufficient numbers of quality personnel and sustain the workforce to accomplish the operational tasks.

Operational Risk:

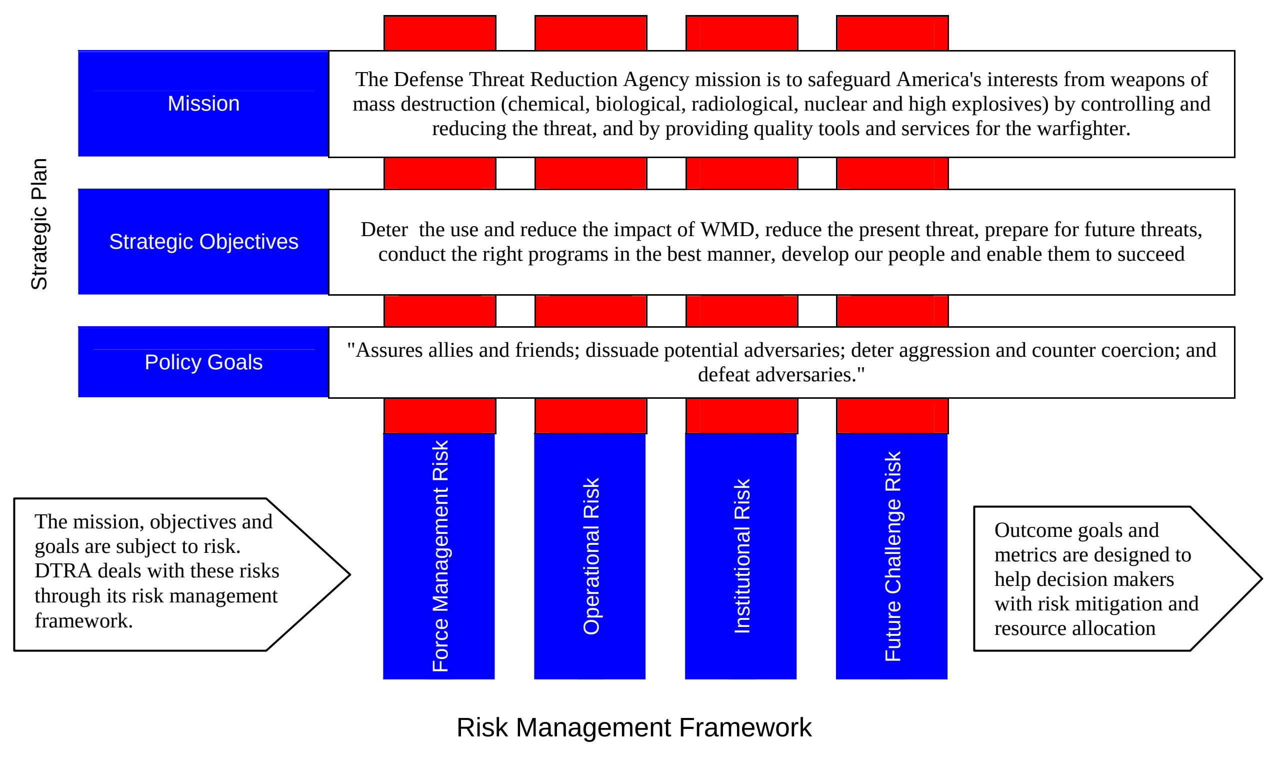
- Ensuring DTRA is ready at all times to accomplish the mission.
- Focuses on achieving mission objectives in a near-term and long-term requirements

Institutional Risk:

- Ensuring that Agency financial, acquisition, and resource management processes are streamlined and efficient.
- Covers management practices and controls that affect the efficiency with which resources are used and that shape organizational effectiveness.

Future Challenges Risk

- Anticipating future threats and adjusting capabilities to maintain a military advantage.
- Addresses new capabilities and new operational concepts needed to accomplish mission challenges. This risk management framework reflects DTRA's experiences in balancing strategy, mission and resources.



The **Risk Management Framework** ties the **Performance Plan** to the **Strategic Plan** with outcome goals and metrics designed to measure how well the Performance Plan mitigates risks.

Resource-constrained action plans are designed to clearly articulate what DTRA expects to accomplish with its planned resources, as well as how performance will be measured. During FY 2005, DTRA continued to mature its process for identification and tracking of meaningful performance metrics. By conducting quarterly performance and financial program reviews, DTRA's leadership can make any necessary course corrections to more effectively carry out its essential national security missions. The DTRA Leadership uses a color rating system to track performance and quickly identify areas that need attention. This system is shown below.

BSC Scoring Key	
(red)	Task cannot/will not be completed by due date.
(yellow)	Issues/problems possibly impacting ability to complete by due date.
(green)	Task on track to be completed by due date.
(blue)	Task completed successfully.

From an external validation perspective, two external DoD reviews – the Biennial Defense Review and the Combat Support Agency Review – provide an ongoing mechanism for continuing, independent assessment of DTRA's accomplishments.

2.5 Planned and Actual Performance

The following summaries of performance only include the programs funded within DTRA's direct TOA; therefore, the Chemical-Biological Defense Program is not included. In addition to this programmatic planned-actual performance information, Section 5.0 of this Management Discussion & Analysis presents specific goals, actions, and accomplishments associated with DTRA's success in implementing the President's Management Agenda (PMA) initiatives.

2.5.1 Combat Support

DTRA provides warfighting support to the Joint Chiefs of Staff, the Joint Staff, the Combatant Commands, and military services as they engage the threat and challenges posed to the United States, its forces and allies by WMD. DTRA supports the essential WMD response capabilities, functions, activities, and tasks necessary to sustain all elements of operating forces in theater at all levels of war. DTRA's combat support program provides operational and analytical support to DoD components and other U.S. and NATO organizations for nuclear and other WMD matters. DTRA conducts research, development, test and evaluation programs and provides technical support to DoD components and other organizations in areas related to WMD and other designated advanced weapons.

Combat Support activities include: Support to the Secretary of Defense, the Joint Chiefs of Staff, combatant commands, military departments, and DoD components for matters involving nuclear and designated special weapons. DTRA also provides direct technical support to the theater commands for forecasting potential hazards and planning for threats posed by recent activities to include support for contingency planning. Support is also provided to OSD for programs that provide oversight for DoD nuclear matters. Additional support is provided to the Joint Staff for stockpile tracking and accounting and by conducting nuclear surety inspections. Finally, the Defense Nuclear Weapons School provides training in nuclear and radiological hazards and response, and other WMD response techniques.

The balanced scorecard items tracked for the Combat Support Directorate include:

Future Challenges Risk Balanced Scorecard Item	**Evaluation**
Nuclear Weapons Technical Inspection (NWTI) program	Green
Operational Risk Balanced Scorecard Items	**Evaluation**
Manage Strategic Weapons Stockpile	Green
Protect Strategic Forces and Means	Green
Support Combatant Commander's Surveillance and Reconnaissance Requirements	Green
Coordinate Consequence Management	Green
Monitor Strategic Situation	Green
Coordinate Nuclear Surety	Green
Review Operation Plans	Green
Maintain Current Operational Readiness Status	Green
Develop Joint Force Liaison Structure	Green
Conduct Professional Education and Training	Green

Combat Support Directorate received a green score overall in the areas above. The Directorate recognized need for continued improvement in the areas of: Protect Strategic Forces and Means, which is internally funded and shortfalls have reduced the number of Balanced Survivability Assessments conducted; and Coordinate Consequence Management which had several successful exercises did not complete the Concept of Operations for Consequence Management.

In 2005, Combat Support Directorate outlined performance objectives in the Justification of Operation and Maintenance funds in the FY 2006/2007 Budget Estimates published in February 2005. The table below summarizes the planned and actual performance:

Performance Objective	FY 2005 Objectives	FY 2005 Actual Performance
Conduct Inspections of Nuclear-Capable Units	25	18
Domestic Consequence Management Exercises	11	10
Foreign Consequence Management Exercises	17	21
Joint Staff Integrated Vulnerability Assessments (JSIVA)	100	105
Mobile Training Team Visits	10	10

In FY 2005, the Combat Support Directorate executed 18 inspections of nuclear-capable units. The DTRA objective is to conduct inspections of between 20-25% of nuclear-capable units per year and that no unit will exceed 5 years between inspections. DTRA continues to conduct consequence management exercises both domestic and foreign. In addition, a number of these exercises include terrorist incident exercises, which are a sub-set of the consequence management exercises. DTRA exceeded planned JSIVA visits in U.S. Central Command (CENTCOM) due to increased requirements for Iraq.

The Combat Support Directorate is also responsible for the Defense Nuclear Weapons School (DNWS). In 2005, DNWS conducted 21 courses, 60 in-resident classes and 39 Mobile Training Team (MTT) classes. The Combat Support Directorate reported they trained a total of 2,973 students from the Combatant Commands and 1,040 students from the Non-Combatant Commands for a total of 4,013 students in FY 2005.

2.5.2 Technology Development

DTRA's technology development efforts reduce WMD threats by conducting innovative research and development that support the Nation's counterproliferation, consequence management, arms control, and combating terrorism needs. DTRA delivers research and development products that provide operational support services that reduce threats posed by WMD. Within this program area, DTRA focuses on operational applications, system applications, nuclear technology, and test and technology support.

The significant balanced scorecard items tracked for this mission area include:

Future Perspective Balanced Scorecard Item	Evaluation
Prepare for Future Threats	Green
Support Efforts to Evolve Global Strike Capabilities	Green
Operational Risk Balanced Scorecard Items	**Evaluation**
Support Consequence Management	Green

In 2005, Technology Development Directorate met the performance objectives below:

Modeling & Simulation Integration – In FY 2005, Technology Development Directorate delivered initial integrated capability for the Integrated Weapons of Mass Destruction Tools (IWMDT) version 1.0, to comply with the requirement to become Global Information Grid (GIG) compliant. The Directorate also established initial continuity of operations capability for technical reach-back support.

Consequence Assessment (CA) – In FY 2005, Technology Development Directorate implemented CA which are modularizing and integrating tools (Hazard Prediction and Assessment Capability (HPAC), Consequence Assessment Tool Set (CATS) to allow re-use in other systems such as IWMDT and Joint Effects Model (JEM). Technology Directorate also released CATS version 6.0, with upgraded GIS implementation.

Operational Support Technology – Technology Development Directorate improved Research & Development (R&D) infrastructure and Chemical, Biological, Radiological, Nuclear, High Explosive (CBRNE) tool capabilities for joint exercises, experimentations and training. In FY 2005, Technology Development Directorate completed demonstration of CBRNE tools in Global Command and Control System (GCCS).

Special Operations Forces (SOF) – Objective: provide improved capabilities for SOF to conduct Counter-Terrorism/Counter-Proliferation (CT/CP) missions against Weapons of Mass Destruction (WMD) in the Global War on Terrorism (GWOT) environment. Completed Biological

Advanced Concept Technology Demonstration (ACTD); 11 technologies successfully transitioned to Special Operations Command (SOCOM).

Hard Target Defeat – Objective: develop, demonstrate and deliver enhanced end-to-end hard target defeat capability to the warfighter. In FY 2005 completed the Thermobaric ACTD. Continued work on the Tunnel Target Defeat ACTD and Measures of Performance (MOP) Advanced Technology Demonstration (ATD) scheduled to complete FY06 and FY 2007 respectively. Both are currently on schedule.

WMD Counterforce Applications – Objective: Develop enabling technologies and deliver "go-to-war" weapons and other advanced systems to combat WMD. This is DoD's only program designed to systematically address combating WMD (attack operations) technology requirements from planning through post-strike combat assessment. In FY 2005 completed an Enhanced Energetic Kill study that looks at utilizing directed energy to better control the effects of energetic payloads for Agent Defeat. Increased control will enable calibration of the amount and timing of energy release. In FY 2005, the Technology Development Directorate conducted a Target Area Strike Support (TASS) Spiral 1 demonstration to demonstrate improved EO/IR and Battle Damage Assessment (BDA) capability.

Detection Technology – Objective: Develop next-generation detectors and monitoring equipment for detecting, locating, and identifying hazardous material, particularly special nuclear material (SNM); warheads and components; radiological dispersion devices (RDDs) and improvised nuclear devices (INDs). In FY 2005, Technology Development Directorate supported Navy Web Common Operating Picture (COP) Integrated Technology Demonstration with integration of detectors, communications onboard Spartan vessel. This demonstration was highly successful.

Radiation Hardened Microelectronics – Objective: Develops materials, process, layout, design methods, and hardness assurance methods for radiation hardened (RH) semiconductor technologies to reduce the impact of weapons of mass destruction on DoD space & missile systems. In FY 2005, Technology Development Directorate implemented 0.15-micron technology manufacturing at BAE Systems and Honeywell as part of the Radiation Hardened Microelectronics (RHM) ATD Program for Advanced Extremely High Frequency (AEHF) system. Additionally, the Directorate developed a RH nonvolatile 1-Mb magnetic random access memory (MRAM) for the Trident D5 Life Extension.

Nuclear Assessments – Objective: Provide DoD customers with Electromagnetic (EM) and high altitude nuclear effects (HANE) system hardness assessments, modeling and simulation tools, and Nuclear Weapons Effects simulations on systems to ensure system survivability and operability against nuclear weapons effects and EM threats. In FY05 established Nuclear Weapons Effects code standards and built capabilities migration into Nuclear Capabilities Server (NuCS). Performed High Altitude Electromagnetic Pulse testing and verification for Defense Information Systems Agency (DISA)/Missile Defense Agency (MDA)/Advanced Concepts Center (ACC).

2.5.3 On-Site Inspection

The United States seeks to reduce the threat from WMD in a number of ways, particularly through treaty and non-treaty efforts to control, safeguard, and eliminate existing weapons. As a focal point for implementing U.S. treaty inspection, escort, and monitoring activities, DTRA executes current arms control treaties and agreements and prepares for imminent or potential agreements. Moreover, through the implementation of both conventional and strategic arms control agreements, and experience gained from this activity, DTRA is increasingly involved in on-site activities in post-conflict stabilization operations.

As monitors for force withdrawals from regional trouble spots, DTRA inspectors provide the United States Government (USG) first hand evidence that international commitments have been fulfilled. Through the verifiable reduction of the world's stockpiles of nuclear, chemical, and conventional weapons, as well as the training and equipping of law enforcement and border personnel in the former Soviet Union (FSU), Eastern Europe and the Baltic countries, U.S. security interests are directly enhanced by the DTRA mission.

Balanced Scorecard: The significant balanced scorecard items tracked for the On-Site Inspection Directorate include:

Operational Risk Balanced Scorecard Item	Evaluation
Implement Intrusive Arms Control Inspections	Green
Counter the Proliferation of WMD in the Functional Area of Counterproliferation	Green
Maintain Sufficient Resources to Provide Specified and Requested Support to Combatant Commanders and Other DOD/GOVT Agencies	Green
Force Management Perspective Balanced Scorecard Item	**Evaluation**
Implement Intrusive Arms Control Inspections	Yellow

On-Site Inspection Directorate measures Implement Intrusive Arms Control Inspections both in the Operational Risk and Force Management risk categories. In the Force Management Perspective risk area, Implement Intrusive Arms Control was evaluated in 4th Quarter of FY 2005 as yellow for one measure due to a decrease from 90% to 80% in available Russian linguists. This decrease was not assessed as having a mission impact.

In 2005, On-Site Inspection Directorate outlined performance objectives in the Justification of Operation and Maintenance funds in the FY 2006/2007 Budget Estimates published in February 2005. The table below summarizes the planned and actual performance:

Performance Objective	FY 2005 Objectives	FY 2005 Actual Performance
Strategic Arms Reduction Activity		
Inspections	71	65
Escorts	29	23
Mock Missions	10	2
Conventional Armed Forces in Europe Treaty		
Inspections	72	80
Escorts	81	14
Mock Missions	15	14
Chemical Weapons Treaty		
Escorts	133	123
Mock Missions	5	5
Open Skies Treaty		
Inspections	9	11
Escorts	8	2
Mock Missions	12	5
International Counterproliferation Program (ICP)	82	70
Other Missions	16	11

Other significant accomplishments in FY2005 for On-Site Inspections included:

International Counterproliferation Program: Led Department of Defense/Federal Bureau of Investigation and Department of Defense/Department of Homeland Security International Counterproliferation (ICP) Program. Members of the On-Site Inspection

Directorate conducted 70 missions in 24 nations including Asia, Europe, and Central America, 47 of which were "train and equip" courses, enhancing host nations' WMD counterproliferation abilities.

Small Arms and Light Weapons (SALW): Provided technical expertise to help countries reduce the proliferation of Man-portable Air Defense Systems (MANPADS) and other SALW. Conducted 14 missions worldwide and hosted a first-ever symposium on implementation of MANPADS and SALW programs.

Plutonium Production Reactor Agreement: Inspected three shut-down nuclear reactors at 2 Russian sites and escorted Russian monitors to 2 U.S. sites.

U.S.-International Atomic Energy Agency (IAEA) Additional Protocol: Provided security countermeasures advice and assistance to the Nuclear Safeguards Implementation Working Group**.**

Chemical Weapon Convention: Participated in the international team studying and testing revised verification measures with reduced international inspector manning at U.S. Chemical Weapons Disposal Facilities.

2.5.4 Cooperative Threat Reduction

With legislation sponsored Senators Nunn and Lugar in 1991, the Cooperative Threat Reduction (CTR) program was established to respond to the threat of proliferation of the FSU arsenal of nuclear and chemical weapons, and biological weapons materials and knowledge on the territories of several New Independent States (NIS). The CTR program provides assistance to eligible states of the FSU in order to dismantle WMD and to reduce the threat of WMD proliferation.

The program objectives are: to dismantle FSU WMD and associated infrastructure; to consolidate and secure FSU WMD and related technology and materials; to increase transparency and encourage higher standards of conduct; and to support defense and military cooperation with the objective of preventing proliferation. The CTR program continues to be a key element of U.S. National Security Strategy.

The significant balanced scorecard items tracked for the Cooperative Threat Reduction Directorate include:

Operational Risk Balanced Scorecard Item	Evaluation
Complete site upgrades to consolidate and secure FSU nuclear, Chemical & Biological Weapons facilities & materials at nuclear sites	Green
Monitor 90-95% of all in/out international traffic through Uzbekistan's POEs (32 total) in order to promote comprehensive nuclear detection & capability for interdiction of illicit trafficking in nuclear weapons, fissile material, & radioactive material	Green
Construct a Chemical Weapons Destruction Facility	Yellow

Construct a Chemical Weapons Destruction Facility was scored as yellow because it was evaluated as being 10% behind the balanced scorecard metric of 63.5% complete at the end of 4th Quarter, FY 2005. The overall project status is only slightly behind schedule based upon an adjustment to metrics due to an increase in project scope.

CTR Program accomplishments in FY 2005 continued to prevent the proliferation of WMD and related materials, technologies and expertise from FSU states through the safe destruction of Soviet-era WMD associated delivery systems and related infrastructure. Since September 11th, 2001, DoD has expanded the strategic focus of the CTR program to support the Global War on Terrorism.

The CTR program accomplishments are outlined below:

Strategic Offensive Arms Elimination – Russia: The CTR Program provides equipment and services to destroy or dismantle intercontinental ballistic missiles (ICBMs), ICBM silo launchers, road and rail mobile launchers, submarine launched ballistic missiles (SLBMs), SLBM launchers, and the associated strategic nuclear submarines (SSBNs) reactor cores, and WMD infrastructure. The program also supports placement of spent naval reactor fuel when defueling SSBNs into long-term storage.

Goals: Continue to dismantle FSU WMD and associated infrastructure.

Major Accomplishments:

- Disassembled six SS-N-20 submarines launched ballistic missiles. The components of three were eliminated.
- Disassembled twelve SS-24 intercontinental ballistic missiles (ICBMs) and eliminated the components of eleven.
- Off-loaded ten SS-24 rail-mobile SS-24 ICBMs from their launchers.

- Eliminated twelve SS-24 rail-mobile launchers and rendered 44 launch associated launch cars strategically inoperable.
- Moved the last SS-24 rail-mobile ICBM train from Kostroma, ending the deployment of this missile system.
- Decommissioned three SS-25 ICBM regiments.
- Disassembled ten SS-25 ICBMs and destroyed the components of eleven ICBMs.
- Eliminated 19 SS-25 road-mobile launchers and demilitarized 53 launch-associated and special system support vehicles.
- Decommissioned twelve SS-18 ICBMs, six SS-18 silo launchers, and one associated SS-18 launch control center (LCC) silo.
- Explosively eliminated twelve SS-18 ICBM silo launchers, three associated LCC silos, and one associated training silo.
- Eliminated twenty-four SS-18 ICBMs and seven SS-19 ICBMs.
- Continued dismantlement of one Delta III class and two Typhoon class SSBNs. Completed SLBM launcher elimination on one Delta III class SSBN.
- Completed dismantlement of one Delta I class SSBN.
- Completed construction of additional spent naval fuel (SNF) cask transient storage facilities at Zvezdochka.
- Continued production of thirty-five SNF casks to support future SSBN dismantlement.
- Eliminated fifteen SS-N-18 SLBMs.
- Eliminated twelve Tu-22M bombers and ninety-five Kh-22 associated nuclear capable air-to-surface missiles (ASMs).
- Eliminated four Tu-142 maritime patrol aircraft and one strategic bomber trainer. Also eliminated associated bomber engines, auxiliary power units, ASM rotary launchers, and external pylons.

Nuclear Weapons Storage Security – Russia: The CTR Program provided hardware, software, and facilities to account for/track strategic and tactical nuclear weapons scheduled for dismantlement, and equipment, training/training-aids, and logistics support to improve the Ministry of Defense's (MOD) guard force capability to protect nuclear weapon storage areas. These efforts improve safety and security at nuclear weapons storage sites that include national stockpile sites and operational storage sites of the Russian Navy, Air Force, and Strategic Rocket Force (SRF), as well as some temporary storage locations. This program also includes Nuclear Weapons Transportation Security, which provides railcar maintenance and procurement, and transportation safety enhancements.

Goals: To enhance the safety, security, control, accounting, and centralization of nuclear weapons during storage in Russia by providing material, services, and related training to prevent their proliferation and encourage their reduction.

Major Accomplishments:

- Completed the Personnel Reliability Program with the delivery of the final 5,000 test cups.
- Conducted 10 site visits to MOD nuclear storage sites.
- Completed physical security upgrades at one MOD nuclear storage site.
- Selected a contractor for the follow-on physical security upgrade effort and placed four additional sites under contract.
- Began the production of 15 replacement guard railcars.
- Delivered one emergency support equipment transport truck.
- Installed, accepted and commissioned 16 Automated Inventory Control & Management System modules.

Chemical Weapons Destruction (CWD): The CTR Program provided for the creation of the first Russian Chemical Weapons Destruction Facility (CWDF) for nerve agent filled munitions. The project includes the design, equipment acquisition, and installation, construction, systems integration, training, and start-up of the facility as well as associated unique destruction process and equipment development. The Russian portion of this program also eliminates former Chemical Weapons Production Facilities (CWPF). This program area also includes Chemical Weapons Destruction-Albania (CWD-A), to secure and eliminate a stockpile of bulk-agent mustard, lewisite, and minimal quantities of arsenical compounds. CTR elimination efforts will dispose of the chemical agents in accordance with the Albanian government requirements under the Chemical Weapons Convention.

CWD-Russia Goals: To continue progress in the development and construction of the Russian CWDF and the destruction of the former chemical weapons production facilities at Novocheboksarsk and Volgograd.

CWDF Major Accomplishments:

- Completed and occupied the Specialists' Camp near the construction site
- Initiated development of the Automatic Process Control System
- Completed the Fire Station and the Electrical Substation
- Completed bridge refurbishment and repair
- Delivered the metal parts furnace

- Delivered the boilers for the boiler house
- Implemented an earned value management system

CWPF Major Accomplishments:

- Re-baseline of the Novocheboksarsk project
- Executed contracting strategy to execute new baseline
- Negotiated agreement for the Russian side to pay for Independent Plant #4 debts
- Completed de-militarization of the last 2 structures (bunkers) at Volgograd CWPF and closed out the project

CWD-Albania Goals: Conduct initial assessment of program needs, project planning, site preparation, and selection of destruction process.

CWD-Albania Major Accomplishments:

- Assessed and performed site preparations and road improvements. This effort was substantially complete as of the end of September 2005 with punch list item completion continuing through October 2005.
- Established the initial chemical agent characterization and environmental baseline for the site.
- Awarded contract to design, fabricate, test, assemble, and operate a system to conduct agent elimination. Work started in June 2005, including establishing an in-country office.
- Assisted the Albania MOD to present an update brief and Facility Plan to the Secretariat of the Organization for the Prohibition of Chemical Weapons.

Biological Weapons Proliferation Prevention - Former Soviet Union:

The CTR Program consolidates, secures or eliminates dangerous pathogen collections at biological research institutes; dismantles former Soviet biological weapons research and production facilities; targets cooperative biological research to prevent the proliferation of expertise on dangerous pathogens and to encourage higher standards of openness, ethics, and conduct at the scientist level; and provides biological threat agent detection and response. This program also provides bio-security and bio-safety upgrades at institutes engaged in legitimate work with especially dangerous pathogens.

Goals: To continue strengthening the basic goals of the program. These are:

- Dismantle FSU WMD and associated infrastructure

- Consolidate and secure FSU WMD and related technology and materials
- Increase transparency and encourage higher standards of conduct, and
- Support defense and military cooperation with the objective of preventing WMD proliferation.

Major Accomplishments:

- The Program continues to secure the State Research Center for Virology and Biotechnology "VECTOR," Novosibirsk, Russia, one of the two World Health Organization authorized repositories for smallpox.
- Secured the State Research Center for Applied Microbiology, Obolensk, Russia, and Russia's premier research laboratory for Bacillus anthracis.
- Secured the National Center for Disease Control, Tbilisi, Republic of Georgia.
- Removed all dual use equipment from the Bacillus anthracis weapons production facility, Stepnogorsk, Kazakhstan.
- Successfully trained more than 100 scientists who will participate in the new Threat Detection and Response system.
- Destroyed foot and mouth disease strains used for vaccine production.
- Developed the multi-year budget plans, schedules, and performance objectives for eight major projects.
- Engaged 403 former Russian biowarfare scientists in scientific projects that are aligned with non-proliferation and are open for publication in the world's scientific literature.
- In the countries of Uzbekistan, Kazakhstan, and the Republic of Georgia, CTR has eight projects and has engaged 11 Institutes and 224 scientists.
- Designed the Human Central Research Laboratory – Kazakhstan
- Designed the Human/Veterinary Central Research Laboratory – Republic of Georgia
- Designed the Human/Veterinary Central Research Laboratory – Uzbekistan
- The Cooperative Biological Research program has published 21 reports. (A report is defined as a peer reviewed publication, an abstract for a national or international conference, or a grant application submitted for international funding outside of the

International Science and Technology Center or the Science and Technology Center in Ukraine.)

- Multiple bacterial and viral strains have been shared with the U.S. Government from the Republic of Georgia and Azerbaijan.
- The CTR program provided direct scientific expertise, training, logistical, and transportation support to the Kazakhstan and Uzbekistan Governments during the 2005 Avian influenza outbreak.

Weapons of Mass Destruction Proliferation Prevention Initiative (WMD-PP): The CTR Program supports non-Russian former Soviet Union countries to prevent, deter, detect and interdict illicit trafficking in WMD or related materials; provides military, internal security forces, border guards and customs officials, equipment and infrastructure, as well as operations and maintenance training. This program also supports maritime proliferation prevention, and provides maritime surveillance equipment and procedures, repair and upgrade of existing vessels, and logistics facilities.

Goals:

- Azerbaijan: Provide Maritime Border Guards an initial operating capability to conduct the WMD-PP mission and develop an assessment of the capability.
- Kazakhstan – No FY 2005 goals since the project was just initiated on September 14, 2005.
- Ukraine- Land Border - Conduct an assessment to develop a current capability baseline of Ukraine Border Services; provide initial equipment; provide WMD-related training, both for operation of the equipment as well as follow-on maintenance requirements; and provide sustainability planning to enable transition support to the government of Ukraine.
- - Black Sea – No FY 2005 goals since the project was just approved for initiation of increment one on September 22, 2005.
- Uzbekistan: Install portal monitoring equipment at 8 vehicle/pedestrian points of entry (POEs) and 3 rail POEs; train 100% of required operators & maintenance personnel for installed monitors; Communications & Training Analyses completed by end FY05.

Major Accomplishments:

- Azerbaijan
  - Achieved initial operating capability
  - Completed Concept of Operations
  - Integrated Logistics System established

- Four sets of WMD detection equipment purchased and delivered for three boarding teams and one backup set
- Sustainment program in place for boats, radars, WMD equipment and sites/infrastructure
- Training program established and on-going
- Assessment plan and supporting metrics developed

- Kazakhstan
  - Program initiated on September 14, 2005.

- Ukraine
  - Land Border
    - Project registration with government of Ukraine
    - Provided Ukrainian Border Services a "Quick Equipment Set" of off the shelf equipment to immediately enhance mobility and surveillance capabilities.
    - Provided Ukrainian Border Services coordinated packages of equipment and associated operations and sustainment training, to enhance capabilities to deter, detect, and interdict illegal trafficking of WMD
    - Approval of methodology and metrics for project assessment
    - Initial baseline assessment and full-year assessment

  - Black Sea - Program initiated on September 22, 2005.

- Uzbekistan
  - Full operational capability for Increment One POEs attained on September 4, 2005.
  - Installation complete at 11 of 11 "most at risk" POEs.
  - Operator and maintainer training completed for personnel at these sites and all equipment transferred to operational control of State Customs Committee.
  - Communications and training analyses completed.

2.5.5 Business Directorate

The Business Directorate (BD), a consolidated supporting infrastructure, was created at the beginning of FY04 to provide essential Agency-wide administrative, resource management and technical support to the program directorates. One of the primary purposes of the creation of the Business BD was to create a fully-integrated business function that employs best practices, is efficient and responsive to customers, is performance oriented and constantly looking for new creative solutions.

The Business Directorate provides management and operational support activities for a full-range of management headquarters functions including:

- Facilities, Engineering, and Logistics Office functions
- Financial and Human Resources Management
- Information Technology Support
- Environment, Safety and Health
- Acquisition, Programming and Contracting
- Strategic Planning

In FY 2005, the Business Directorate focused on continued improvement of business processes and procedures to take the Agency to the next level of efficiency and customer service. The Business Directorate implemented its first Customer Survey for Agency wide administration, using the results to develop an integrated approach to Agency innovation and improvement efforts with the Business Management Modernization Program. The result was creation of a Business Process Improvement (BPI) Integrated Product Team (IPT) tasked to prioritize the core business processes for improvement and develop an action plan for improvement.

The balanced scorecard items tracked for the Business Directorate include:

Future Challenges Balanced Scorecard Item	**Evaluation**
Improve ability to anticipate future business capabilities and requirements	Blue
Institutional Risk Perspective Balanced Scorecard Item	**Evaluation**
Improve Information Technology/Information Management governing, designing, building and operating processes, procedures and systems in accordance with regulatory and DoD guidance	Red
Operational Risk Perspective Balanced Scorecard Item	**Evaluation**
Improve ability to evaluate DTRA performance	Blue
Improve financial and manpower management support to meet mission and DoD requirements	Green
Operational Risk Perspective Balanced Scorecard Item cont.	**Evaluation**
Enhance Environmental, Safety, and Occupational Health (ESOH) performance.	Green
Improve facilities, logistics, and engineering support to meet mission requirements	Green

The Business Directorate score of red for Improving Information Technology (IT) and Information Management (IM) is a result of not all IT/IM governance activities having been chartered or established.

In 2005, the Business Directorate outlined and met the following performance objectives:

Improved Information Technology/Information Management systems: During FY 2005, the Business Directorate did make substantial progress in improving its technology management. During FY 2005, a material weakness previously identified by the Management Control Program was corrected by implementing the software tracking procedures with the installation of the Help Desk Expert Automation Tool Asset Tracker; installation of the Next Generation Operating System (NGOS), and purchase of a Microsoft © Enterprise Software License. This will be covered in further detail in section 4.2 of this report.

Business Process Improvement: With the approval of the action plan by the Director, BD, the first Process Action Teams (PATs) were formed and began work in CY 2005. The PATs follow the DTRA process improvement methodology. This methodology includes process mapping and determining causes of problems and opportunities for improvement with the existing process, measuring current process performance, comparative research and/or benchmarking, developing recommendations for process improvement, identifying expected performance improvement, and costs associated with implementing those improvements (i.e., making a business case), and monitoring implementation, including measuring performance to see if expected improvements are realized. The following areas were identified for PAT review during CY 2005:

- Comprehensive Cost and Requirement System (CCaRS) implementation (impacts program management and budget analysis processes)
- Memoranda of Understanding (MOUs) and Memoranda of Agreement (MOAs)
- Program Review (including information technology capital planning component)
- Indefinite Delivery - Indefinite Quantity (IDIQ) Task Order Awards
- Military Inter Departmental Purchase Requests (MIPRs) and Inter-Agency Cost Reimbursement Orders (IACROs)
- Hiring (including position classification)
- Contract Closeout

Completion of the Defense Threat Reduction Center (DTRC): The construction of the DTRC was completed in September 2005, and the key turned over to DTRA. The DTRC is a 308,000 square foot addition to the McNamara building at the Ft. Belvoir Headquarters Complex. It accommodates approximately 1,400 people. Special spaces include a large computer center, a Sensitive Compartmented Information Facility (SCIF), and a state of the art Operations Center, a space dedicated to computer modeling of potential WMD attacks. This facility develops tests and provides modeling capability throughout DoD. The construction was programmed in the amount of $75,388,000. The design cost was approximately $5 million.

The DTRC is one of the first buildings constructed under the post Sept. 11 force protection construction criteria. Features of the DTRC include special structural reinforcing, blast protective windows, protected air intakes and structures preventing vehicles from approaching closer than the appropriate stand-off distances. Completion of the DTRC is a true team effort involving hundreds of DTRA employees and contractors as well as people from the Defense Logistics Agency, the U.S. Corps of Engineers, the designer, RTKL, and the construction contractor, CENTEX.

With the turnover of the key to the DTRC on Friday, Sept. 23, DTRA Security and Counterintelligence Directorate became the responsible agent to implement and enforce security of the DTRC, and to control access of the construction workers and the DTRA employees required to bring the building to final completion. Outfitting (still on-going) includes the security system, furniture, audio visual system, Operations Center equipment, high density files, Video Teleconference Center (VTC) systems, upgraded and replacement data and telecommunications infrastructure at over $30 million.

The original contract was awarded with a September 1, 2005 completion date. A well-run project of this nature normally experiences a 10% time growth, so the original planning was set to a December 1, 2005, completion date. In spite of the second wettest year in history (including a hurricane), during the excavation phase of this project, the contractor kept the time growth due to this extraordinary situation to 23 days, and held that schedule throughout the remainder of the project.

Consolidation of Finance and Accounting Functions: Implementation of Management Initiative Decision (MID) 914 Defense Agency Accounting and Finance Services, signed October 18, 2004. This effort required the modification and transfer of the paying office on all DTRA contracts, the transfer of many finance and accounting operations functions, and a shift in the focus of the DTRA Finance and Accounting Office to a managerial accounting role.

2.5.6 Advanced Systems and Concepts Office (ASCO)

The Advanced Systems and Concepts Office (ASCO) is fully engaged to develop and maintain an evolving analytical vision of necessary and sufficient capabilities to protect the U.S. and its allies from emerging WMD threats. ASCO analyzes future WMD threats, forecasts requirements, and integrates the results into the Agency's overall planning. It supports DTRA through projects that are designed to encourage alternative thinking, innovative strategies, and cross-cutting integrated approaches to WMD threats. ASCO integrates its work with the advice and recommendations of the Threat Reduction Advisory Committee (TRAC).

The balanced scorecard items tracked for the Advanced Systems Concepts Office include:

Future Challenges Balanced Scorecard Item	Evaluation
Conduct Conceptual Studies	Green

2.5.7 Security and Counterintelligence

The Security and Counterintelligence Directorate (SC) aims to protect DTRA personnel, activities, information, facilities and cyberspace. The Security and Counterintelligence Directorate produces and maintains awareness of all counterintelligence and force protection intelligence in support of Agency missions, teams and conferences in part due to the establishment of formal relationships with domestic and foreign intelligence operations. The Directorate also manages the dissemination of intelligence products and identifies the agency's intelligence needs.

The balanced scorecard items tracked for the Security and Counterintelligence Directorate include:

Operational Risk Perspective Balanced Scorecard Item	Evaluation
Stand-up and fully integrate the full suite of protection services and products into the Central Protection Center (CPC)	Green
Have all newly assigned personnel receive mandatory initial OPSEC training upon their arrival, and re-certify annually	Green
Stand-up a fully trained Computer Emergency Response Center	Green
Continue to manage the information security program in an effort to keep security violations at a minimum	Yellow

The Security and Counterintelligence Directorate received a yellow score in Managing the Information Security Program due to the number of security incidents reported in FY 2005.

2.6 Performance Trends

In FY 2005, DTRA relied on the Balanced Scorecard concept and technique to collect measurable data and report accomplishments against specific targets (this business improvement initiative was started in FY 2002). DTRA is proud of its progress to date but recognizes the need for and value of additional historical performance data on which to base future DTRA performance trends.

Under the Balanced Scorecard and President's Management Agenda (PMA) scorecard processes now in place at DTRA, performance measurement information is maturing in order to consistently identify and report performance targets and progress in future Management Discussion & Analysis. Additionally, as described in Section 5.0 of this MD&A, DTRA is making tangible progress in all PMA initiative areas.

3.0 Financial Highlights

3.1 Financial Overview

As of September 30, 2005, the financial condition of DTRA was sound, with sufficient funds to meet program needs, and with adequate control of these funds in place to ensure effective financial management.

The FY 2005 financial statements, which were produced by the Defense Finance and Accounting Service (DFAS), do not include the Chemical/Biological Defense Program, which began to be reported separately in FY 2004.

3.2 Financial Statement Analysis

3.2.1 Assets

DTRA's total assets were $1.983 billion as of September 30, 2005. This is a decrease of $163 million from September 30, 2004, and is primarily attributable to increases in program outlays of $63 million; and reduction in appropriations of $96 million. The assets reported on DTRA's Balance Sheet are summarized in the table shown below.

Asset Summary (in thousands)	FY 2005	FY 2004
Fund Balance with Treasury	$1,833,839	$2,042,532
Accounts Receivable, Net	2,575	6,756
Property, Plant and Equipment	121,041	97,140
Other Assets - Inventory	25,708	0
Total Assets	$1,983,163	$2,146,428

Fund Balance with Treasury represents DTRA's largest asset. The balance accounts for 92.5 percent of DTRA's total assets. The balance decreased 10.2 percent between 2004 and 2005.

The value of Property, Plant and Equipment accounts for more than 6.1 percent of DTRA's total assets. The increase of $24 million is due to a $32.5 million increase in Construction in Progress, a $2.5 million increase in General Property, Plant and Equipment net of current year depreciation and an $11 million decrease in Property in the Hands of Contractor. The Construction in Progress increase represents progress in completing the new Defense Threat Reduction Center.

For FY 2005, Accounts Receivable represents less than 1 percent of DTRA's total assets. In FY 2005, DTRA reduced the balance of aged receivables over 90 days by $2.64 million (41%). These reductions were due primarily to a reduction in customer orders for FY 2005.

3.2.2 Liabilities

DTRA's liabilities were $143.5 million as of September 2005, a $5.4 million or a 4 percent increase from the previous year. The increase is due to a $16.9 million increase in Accounts Payable, partly offset by a $10.5 million decrease in Environmental Liabilities. The liabilities are summarized in the table below.

Liability Summary (in thousands)	FY 2005	FY 2004
Accounts Payable	$67,150	$50,258
Salaries and Other Employment-Related	3,636	2,040
Environmental Liabilities	61,043	71,508
Other Liabilities	11,704	14,289
Total Liabilities	$143,533	$138,095

The increase in Accounts Payable is mainly due to the consolidation of DTRA's accounting functions with DFAS and increases in program execution rate.

The Environmental Liabilities are for restoration activities at Johnston Atoll and cleanup at the Nevada Test Site. The decrease of $10.5 million is primarily due to the transfer of responsibility for the complete restoration of the Johnston Atoll site to the Department of the Air Force in the 1st Quarter, FY 2005.

The decreases of $2.6 million in Other Liabilities is due to decreases in various payroll costs and Advances From Others for deposits received from Federal and non-Federal customers for work yet to be performed.

3.2.3 Net Position

The Agency's Net Position at the end of FY 2005 was $1,839 million. Net Position is the sum of the Unexpended Appropriations and Cumulative Results of Operations at the end of FY 2005.

Unexpended Appropriations represent amounts of authority which are unobligated and have not been rescinded or withdrawn, and amounts obligated for which legal liabilities for payments have been incurred. The decrease in Unexpended Appropriations between 2004 and 2005 was $247.4 million.

Cumulative Results of Operations represents the difference, since inception of an activity, between expenses and losses and financing sources, including appropriations, revenue and gains. DTRA's FY 2005 Cumulative Results of Operations was $81.9 million, versus $2.99 million in 2004. The $78.9 million increase is mainly due to an increase in spending authority from offsetting collections of $37.8 million, an increase in other resources of $28.2 million, an increase in inventory of $25.7 million, offset by decreases in resources used to finance the acquisition of assets of $7.9 million and in depreciation expense of $3.6 million.

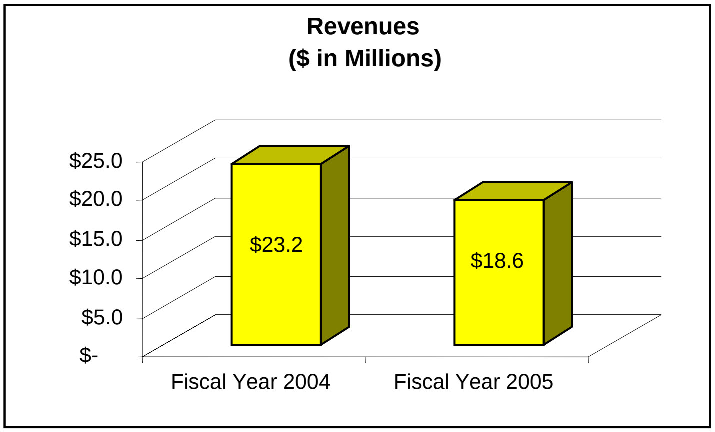
3.2.4 Costs

The Consolidated Statement of Net Cost shows that the net cost of operations for the Defense Threat Reduction Agency for fiscal year 2005 was $1,387 million, an increase of $14 million (0.1%) from fiscal year 2004. As indicated by the table below, increases occurred in several major programs to support this effort. The Consolidating Statement of Net Cost provides a more detailed breakout of DTRA's costs.

Costs			
Program Type	Fiscal Year 2005	Fiscal Year 2004	Change
	Millions		
Operation & Maintenance	$446.7	$348.9	$97.8
Procurement	$48.1	$40.5	$7.6
Research Development, Testing & Evaluation	$395.9	$558.4	$(162.5)
Cooperative Threat Reduction	$519.7	$394.2	$125.5
Other Programs	$(4.6)	$53.9	$(58.5)
Total	$1,405.8	$1,395.9	$9.9

3.2.5 Revenues

The Consolidated Statement of Net Cost shows that the total revenues received by the Defense Threat Reduction Agency for FY 2005 were $18.6 million. This is a $4.6 million (20%) decrease in revenues from FY 2004. The decrease in revenues was due to a reduction in revenue generating reimbursable programs with federal and nonfederal customers. During FY 2005, DTRA recorded $0.0 million in nonfederal revenue.



3.2.6 Budget Authority

This is the authority provided by law to incur financial obligations that will result in outlays. Specific forms of budget authority include; appropriations, borrowing authority, contract authority and appropriation transfers from other agencies. The Combined Statement of Budgetary Resources shows that the amount of budget authority the Agency had for fiscal year 2005 was $1,205 million. Net of rescission and transfer, the budget authority was $1,199 million. This is a $39 million (3%) decrease from fiscal year 2004. Decreased funding to support the Global War on

Terrorism caused this decrease and the corresponding increases to both obligations and outlays, which are discussed below.

3.2.7 Obligations

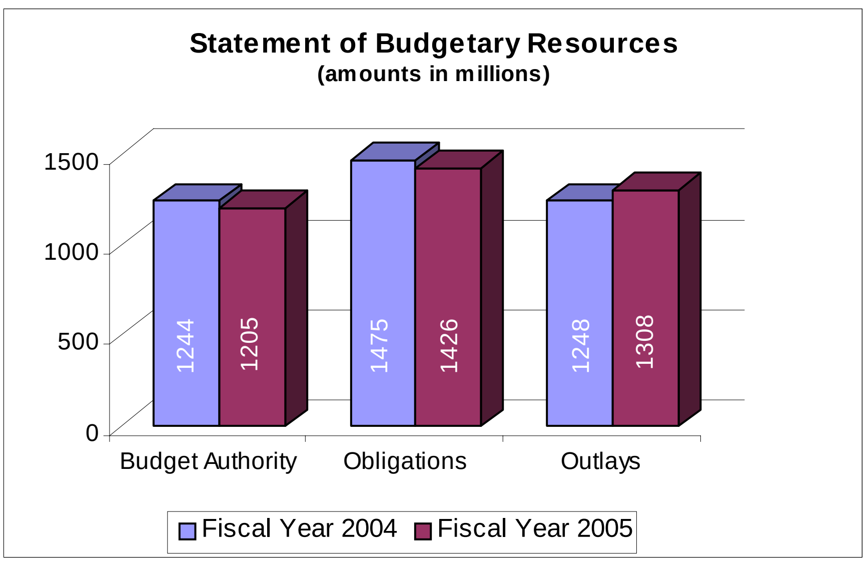
An obligation is a binding agreement that will result in outlays, immediately or in the future.

Budgetary resources must be available before obligations can be incurred legally. The Combined Statement of Budgetary Resources shows that obligations made during FY 2005 were $1,426 million, a decrease of $49 million (3%) from FY 2004.

3.2.8 Outlays

An outlay is a payment to liquidate an obligation (other than the repayment of debt principal).

Outlays generally are equal to cash disbursements, but also are recorded for cash-equivalent transactions, such as the subsidy cost of direct loans and loan guarantees, and interest accrued on issues of public debt. Outlays are the measure of government spending. The Combined Statement of Budgetary Resources shows that outlays made during fiscal year 2005 were $1,308 million, an increase of $60 million (11%) from fiscal year 2004.



4.0 Management Controls and Compliance with Laws and Regulations

4.1 Compliance with Legal and Regulatory Requirements

DTRA has worked aggressively to comply with laws made by Congress to ensure that the Federal Government provides the best possible service to the American people. Among these laws are:

- Chief Financial Officers Act of 1990
- Government Performance and Results Act of 1993
- Federal Financial Management Improvement Act of 1996
- Improper Payments Information Act of 2002
- Prompt Payment Act of 1982
- Federal Managers' Financial Integrity Act of 1982

Chief Financial Officers Act of 1996

The Chief Financial Officers Act (CFO Act) requires Federal agencies to prepare auditable annual financial statements. Since 2001 DTRA's financial statements have been audited by an independent audit firm. For FY 2001 the audit firm audited the balance sheet only and rendered an unqualified opinion on the balance sheet. Since FY 2002, all financial statements have been audited, and DTRA has consistently received an unqualified opinion on its statements.

Government Performance and Results Act

The Government Performance and Results Act of 1993 require a recurring cycle of performance reporting for Federal agencies. This cycle involves 5 year strategic plans, annual performance plans, and annual performance reports. DTRA now uses the Balanced Scorecard approach to evaluate and report performance results.

Federal Financial Management Improvement Act of 1996

The Federal Financial Management Improvement Act of 1996 requires Federal agencies to report on their compliance with Federal financial management system requirements, Federal accounting standards, and the U.S. Government Standard General Ledger. For FY 2004, DTRA's financial systems were not substantially compliant with FFMIA. Pending final DoD decisions regarding the implementation of a Business Management Modernization Program application, DTRA continues to build and sustain financial and accounting crosswalks to support integrated Agency systems reporting.

Improper Payments Information Act of 2002

The Improper Payments Information Act of 2002 requires an annual review of Agency programs and activities that may be susceptible to significant improper payments. During FY 2005, DTRA's improper payments were less than 1 percent of its total payments – that is, 0.7 percent ($3.7 million) out of $509 million. As of September 30, 2005, DTRA had $161 thousand in improper payments that were not recovered.

Prompt Payment Act

The Prompt Payment Act of 1982, as amended, provides Government-wide guidelines for establishing due dates on commercial invoices and provides for interest payment on invoices paid late. During FY 2004, DTRA effectively used electronic fund transfers to minimize the number of late payments.

Federal Managers' Financial Integrity Act

The Federal Managers' Financial Integrity Act (FMFIA) requires Federal agencies to assess the effectiveness of management, administrative and accounting controls, and financial management systems. Using self-assessments as the basis, this Act requires Agency heads to provide an annual statement of assurance on the effectiveness of the management controls and to include material weaknesses found in management controls that warrant reporting to a higher level. DTRA regularly monitors and aggressively works to improve the management control effectiveness of its operations, programs and financial systems. DTRA's 2004 Annual Statement of Assurance was submitted to the Secretary of Defense on September 27, 2004. The assurance statement is based on information gathered from various sources including managers' personal knowledge of day-to-day operations and existing controls, management program reviews, and other management-initiated evaluations.

4.2 Management's Control Program

The Defense Threat Reduction Agency's (DTRA) senior management evaluated the system of internal accounting and administrative control in effect during the Fiscal Year ending September 30, 2005. The evaluation was conducted in accordance with the guidance contained in the Office of Management and Budget (OMB) Circular No. A-123, "Management Accountability and Control." The OMB guidelines were issued in consultation with the Comptroller General of the United

States, as required by the Federal Managers' Financial Integrity Act of 1982. Included was an evaluation of whether the system of internal accounting and administrative control for DTRA is in compliance with standards prescribed by the Comptroller General.

The objectives of the system of internal accounting and administrative control of DTRA are to provide reasonable assurance that:

- The obligations and costs are in compliance with applicable laws;

- Funds, property, and other assets are safeguarded against waste, loss, unauthorized use, or misappropriation;

- Revenues and expenditures applicable to Agency operations are properly recorded and accounted for to permit the preparation of reliable accounting, financial and statistical reports and to maintain accountability over the assets.

The results indicate that the system of internal accounting and administrative control of DTRA were in effect during the fiscal year that ended September 30, 2005, taken as a whole, complies with the requirement to provide reasonable assurance that the above mentioned objectives were achieved. This position on reasonable assurance is within the limits described in the preceding paragraph.

4.2.1 Systemic Weaknesses

A systemic weakness is defined as a material weakness that affects management controls across organizational and program lines and usually affects multiple Department of Defense components. Five systemic weaknesses identified by the Office of the Secretary of Defense (OSD) were addressed in DTRA's 2004 Annual Statement of Assurance.

1. DoD Financial Management Systems and Processes - DTRA lacks an integrated financial management system. There has been significant effort on the part of the Office of the Under Secretary of Defense (Comptroller) (OUSD(C)) and the Defense Finance and Accounting Service (DFAS) to identify a future system which would support the Defense agencies. DTRA is participating with DFAS in the Defense Agency Initiative (DAI) which is working to address this material weakness for Defense agencies.

2. Management of Information Technology and Assurance - Combating Computer Software Piracy. DTRA installed the Next Generation Operating

System (Windows® XP Professional) which locked the standard Agency desktop configuration so that individual users are no longer capable of loading unauthorized software. Additionally, DTRA purchased a Microsoft© (MS) Enterprise Software License which eliminated the possibility of exceeding the number of unauthorized licenses available for installation.

3. Environmental Liabilities - DTRA concurs with the Department of Defense that estimating environmental liability (i.e., cleanup costs) represents a challenge and needs improvement. More specifically, an appropriate distribution of environmental costs between the test range users (DTRA and others) and the test range owners at the DoD-level does not yet exist. Although the DoD estimating process needs improvement, DTRA has implemented procedures and methodologies to consistently estimate, budget, and report for identified environmental restoration sites in compliance with Federal, State, and other regulatory requirements.

4. Personnel Security Investigations Program - DoD hiring is adversely affected because personnel security investigations are backlogged. DTRA mitigates this weakness through constant monitoring of open investigations with weekly status checks/updates and the use of a direct liaison to resolve hiring delays.

5. Government Card Program Management - Instances of misuse, abuse, and fraud in respect to purchase and travel card use have been attributed to inadequate DoD emphasis on proper use of the cards, poorly enforced controls and lax oversight. DTRA mitigates this weakness by performing reviews at least once every 12 months of all Approving Officials (AOs), including at least 25 percent of their cardholder accounts. During our annual assessment, we identified an instance of improper use of a convenience check which exceeded the established limit.

4.3 Material Weaknesses

4.3.1 Table II, Section 2 Material Weaknesses – Ongoing

A material weakness is defined as a weakness in management controls that warrant reporting to a higher level. In FY 2005, DTRA reported no new material weakness and two material weaknesses still outstanding from prior years. Three previously identified weaknesses were corrected in fiscal year 2005.

4.3.3.1 Material Weakness Identified During the Current Period

DTRA did not identify any material weaknesses in FY 2005.

4.3.3.2 Two Uncorrected Weaknesses Identified During Prior Periods

A - Material Weakness (uncorrected, identified in prior periods)	First Reported	Original Correction Date	New Correction Date	Appropriation
Financial Management Systems	FY 2002	1st Quarter FY 2005	4th Quarter FY 2007	O&M Dev/ Procurement

Description of the Issue - DTRA lacks an integrated business/financial management system capable of providing complete, reliable, consistent, and timely information to include auditable financial statements.

Reason for Change in Date – N/A date is unchanged.

Progress to Date - DTRA is actively participating in a joint effort to develop and procure a new business/financial system that will serve the needs of all Defense agencies through the Defense Agencies Initiative with OSD and DFAS.

B - Material Weakness (uncorrected, identified in prior periods)	First Reported	Original Correction Date	New Correction Date	Appropriation
Russian Federation Failure to Honor Commitments	FY 2002	4th Quarter FY 2003	1st Quarter FY 2006	FSU Threat Reduction PE 0901515BR

Description of the Issue - The Russian Federation has declared it no longer requires a Heptyl (rocket fuel) Conversion Plant. DTRA had worked closely with Russia to build this facility according to the stated needs. In January 2003, Russia notified the United States that the facility was no longer needed for its intended purpose and that Heptyl would be used for commercial space launch purposes. This issue was further addressed in subsequent DoD IG audits on the Solid Rocket Motor Disposition Facility and on CTR construction projects. To ensure Russia would not reverse its requirements for the Chemical Weapons Destruction Facility in Schuchye, the U.S. Government required Russian compliance with several conditions. Most conditions have been met; however, delivery of a practical plan for nerve agent elimination remains outstanding.

Reason for Change in Date - While significant progress has been made, some of the objective milestones previously identified still require action.

Progress to Date - The Russian Federation has signed the amendments to Nuclear Weapons Storage Security (NWSS)/Nuclear Weapons Transportation Security (NWTS) Implementing Agreements as well as the Chemical Weapons Elimination Agreement. Successful semi-annual Executive Review sessions were held July 2004 and the intrusive Audit and Examination of Inter-Modal Tank Containers is underway at this writing. DTRA has reached an agreement with the Russian Federation that a Joint Requirements Implementation Plan may not be required for the NWSS/NWTS Programs. Strategic risks previously documented are now being identified on a project-specific basis as part of project Milestone Decision Reviews and in monthly and quarterly project status reports. To the extent practical, DTRA will work with other DoD agencies and with the Russian Federation to ensure that Russia's delivery of a practical plan for nerve agent elimination is completed by December 2005.

4.3.3.3 Three Material Weaknesses Corrected During the Current Period

A – Material Weakness (corrected during current period)	First Reported	Date Corrected	Appropriation
Remaining Cooperative Threat Reduction (CTR) Management Challenges	FY 2005	FY 2005	FSU Threat Reduction PE0901515BR

Description of the Issue - . In a recent Government Accountability Office (GAO) audit of the Cooperative Threat Reduction (CTR) management and internal control, GAO recommended that OSD conduct performance reviews of CTR projects upon completion. Such reviews would provide a mechanism to document lessons learned and apply them to future project planning.

Resolution of the Issue - A formal, documented performance review process has been implemented to evaluate all CTR programs/projects to ensure schedule, cost, and performance risks are minimized. The following are the steps implemented to correct this weakness:

The Defense Threat Reduction Agency (DTRA) conducted a quarterly program review which included lessons learned from the first completed project (Volgograd

Chemical Weapons Production Facility). DTRA implemented processes and procedures to capture lessons learned during project implementation and at project completion.

- Lessons learned are readily accessible via the Agency's website. Documented lessons learned are a readily available reference source, allowing managers to benefit from them during project implementation and after project completion.

- The mandatory Program Management training courses for DTRA/CT program and project managers includes block of instruction on the value of lessons learned and required procedures.

- The value of the lessons learned process is stressed by CTR leadership at both the DTRA and OSD levels.

As projects are planned and implemented, Acquisition Strategy Reviews, Milestone Decision Reviews (at multiple points in a project's life cycle, to include project initiation, between phases, and at project completion), and Quarterly Program Management Reviews address actual performance and incorporate lessons learned, as appropriate. Procedures for these reviews include the mandatory requirement to identify and present lessons learned during execution of the project or lessons learned from other projects that were incorporated into the new project's acquisition strategy.

B - Material Weakness (corrected during current period)	**First Reported**	**Original Correction Date**	**Appropriation**
Inadequate Training Programs for Cooperative Threat Reduction (CTR) Program/Project Managers	FY 2004	FY 2005	FSU Threat Reduction PE 0901515BR

Description of the Issue - As reported in DTRA's FY2004 Annual Statement of Assurance, management identified a shortfall in knowledge, skills, and abilities among the existing staff that resulted in inconsistent, uncoordinated, and inadequate approaches to satisfying U.S. commitments to provide CTR assistance to various states of the former Soviet Union.

Resolution of the Issue - To correct this weakness, DTRA/CTR established a tailored program management training program that focused on successful Milestone Decision Authority review and approval (Module 1) and activities required for contract/project execution, control, and closeout (Module 2).

Module 1: Program management training course completed by all DTRA/CT staff as well as DTRA/OSD staff involved in execution of the CTR program.

Module 2: Program management training course completed by all DTRA/CT staff as well as DTRA/OSD staff involved in execution of the CTR program.

This action was completed and current DTRA/CTR program/project managers have implemented consistent, uniform, and professional approaches to activities related to CTR program/project management.

C - Material Weakness (corrected during current period)	**First Reported**	**Date Corrected**	**Appropriation**
Combating Computer Software Piracy	FY 1999	3rd Quarter FY 2005	Procurement PE 0305898BR

Description of the Issue – Combating Software Piracy

Resolution of the Issue – DTRA software tracking procedures were implemented with the installation of the Help Desk Expert Automation Tool Asset Tracker, installation of the Next Generation Operating System (NGOS), and purchase of a Microsoft© (MS) Enterprise Software License.

The installation of NGOS (Windows® XP Professional) locked the standard desktop configuration so the individual end user can no longer load unauthorized software. Additionally, the MS Enterprise License eliminated the possibility of exceeding the number of authorized licenses available for installation.

5.0 President's Management Agenda

DTRA has adopted a working habit and attitude of continuous process improvement and innovation in management techniques. The President's Management Agenda includes five Government-wide initiatives intended to improve the quality of its performance and delivery of services to the public: (1) Strategic Management of Human Capital, (2) Competitive Sourcing, (2) Improved Financial Performance, (4) Expanded Electronic Government and (5) Budget and Performance.

DTRA has taken steps leading to improvements in all five PMA initiatives, and has integrated these actions into the Agency's broader goals of continuous improvements under the Balanced Scorecard technique. It understands and has made the Administration's strategy for improving the management and performance of government an integral part of its business operations, performance measurement processes, and capabilities. DTRA has addressed each of the five initiatives with an approach to maximize our value to the public.

5.1 Strategic Human Capital Management

DTRA continues to make progress on implementation of the President's Management Agenda human capital initiative. DTRA's efforts in this area are based on building a workforce of the future, recruiting new, skilled workers, and actively working to retain people with essential technical capabilities. This also means implementing extensive training and development programs to equip DTRA employees with the skills they will need to meet future challenges.

DTRA has established an HR review process in the Annual Program Review cycle for reviewing long-term requirements. It has prepared a Strategic Workforce Plan (SWP) baseline document which links HR strategies to current and emerging Agency missions and goals. During the year, DTRA convened a Human Resources Management Committee (HRMC) as needed to discuss HR activities, priorities, and requirements.

DTRA's Human Resource and Equal Opportunity staff members meet frequently to design and coordinate strategic workforce initiatives to recognize greater emphasis on performance and accountability. DTRA has multiple outreach programs and tools to promote underrepresented audiences, such as programs to advertise in diversity publications and websites and participates in virtual/in-person job fairs.

5.2 Competitive Sourcing

DTRA has successfully controlled its operating costs by maximizing the use of competitively awarded service contracts consistent with Federal Acquisition Regulations, the Federal Activities Inventory Reform Act (FAIR) Act, and OMB Circular A-76. DTRA competitively contracts for technical services, information technology support, certain editing and publishing services, mailroom and general labor services, cleaning and building maintenance services, audit and financial services, and security services. Beginning in FY 2005, DTRA plans to study 120 positions, at a rate of 30 positions per year, for possible competitive sourcing. DTRA will continue to evaluate competitive alternatives and efficient service contracting options to maximize efficiency and minimize cost.

5.3 Improving Financial Performance

The DTRA has three primary initiatives underway to improve its financial performance: the Business Management Modernization Program, Financial Improvement Initiative, and the Financial Management Balanced Scorecard. These initiatives directly respond to financial improvement plans required by the Office of Management and Budget's guidance for the Chief Financial Officer Financial Management 5-Year Plan and Financial Management Systems Plan, as well as the Federal Financial Management Improvement Act's requirement for remediation plans.

For 3 years, DTRA received an unqualified opinion on its audited financial statements – a significant and unique accomplishment. DTRA expects to receive an unqualified opinion in FY 2005 when the audit concludes November 8, 2005. The achievement of the "clean" audit opinion is the primary measure of success and criteria for OMB's "GREEN" standing within this PMA initiative.

DTRA continues to improve upon its long-standing record of prudent fiscal management and cost control by continuing to monitor key financial management performance indicators and implement efficiency, control, and effectiveness improvements. A key aspect to this improvement is the development and maintenance of metrics related to significant financial functions in the office. The monthly metrics report now has more than 20 indicators. The metrics provide us early warning of issues that may be audit risks and also, at a more micro level, of functional areas that need improvement.

5.4 Expanding Electronic Government

Of the 25 initiatives identified by the President's Management Council, 18 involve DoD activities. DTRA is taking an active role in many of those initiatives.

DTRA considers e-Government goals during the initiation phase of every major IT project and in DTRA's entire investment review process. In recent years, DTRA has committed significant resources to e-Government modernization initiatives. DTRA is working closely with the DoD Business management Modernization Program (BMMP) to develop and implement a new, integrated technology solution for the Department. At the end of FY 2003, DTRA prepared its first IT-300 addressing administrative infrastructure systems per OSD guidance. DTRA also continues to enhance its Clinger-Cohen compliant IT Capital Planning and Investment Control Process to review and analyze technology initiatives and return-on-investment (ROI) benefits to the Agency.

In addition, 94 percent of current DTRA systems are certified and accredited for security controls – security reviews will continue toward the DTRA goal of 100 percent secured. Finally, DTRA is analyzing alternatives and initiatives to integrate E-Gov into DTRA's business environment. DTRA recognizes the importance of leveraging new technologies to create a modern IT delivery system that is architecture-based to better communicate across directorates, mission and support areas, and external stakeholders.

5.5 Budget and Performance Integration.

In FY 2005, DTRA continued to work toward budget and performance integration, as well as use of this integrated data for management decision-making. DTRA managers and executives analyze quarterly updates to the Agency Balanced Scorecard and conduct quarterly program reviews to address financial program execution information. DTRA also links performance appraisal plans for key senior leaders to the Balanced Scorecard organizational results. This technique was piloted in the Business Directorate starting in FY 2003 and continues to be expanded in FY 2005.

Additional efforts are underway to integrate performance metrics into all phases of the Agency's planning, programming, budgeting, and execution process.

5.6 Summary – President's Management Agenda Initiative (PMAI)

The Department of Defense has empowered all defense organizations to apply the principles of the President's Management Agenda in a results oriented manner thus ensuring Department-wide implementation and institutionalization.

DTRA's PMAI results for FY 2005 are as follows:

President's Management Agenda Initiative	Status
Human Capital Strategies are Linked to Agency Mission and Goals	Yellow
Organization is Re-Structured to Provide Optimal Service at the Lowest Cost	Green
Continuity of Leadership is Assured through Succession Planning and Professional Development	Green
Performance appraisals for SES and managers are linked to agency mission and cascaded throughout at least 60% of the agency	Green
Workforce is diverse including critical occupations and leadership	Green
Current and future skill gaps in critical occupations are identified and reduced	Green
Operations Security: 90% of operations are properly secured	Yellow

President's Management Agenda Initiative cont.	Status
No information technology projects are redundant with E-Gov initiatives	Yellow
Report on performance management using the Balanced Scorecard	Green
Senior managers meet at least quarterly to examine reports which integrate financial and performance information covering all major areas of responsibility	Yellow
Reports the full cost of achieving performance goals accurately in budget and performance documents and can accurately estimate the marginal cost of changing performance goals	Green
Demonstrates fair, credible and transparent performance appraisal plans and awards programs for all SES and managers, and more than 60% of the workforce that adhere to the merit system principles	Yellow

6.0 The Road Ahead – Future Challenges

DTRA's mission and roles continue to evolve and expand. Its responsibilities and operations span are affected by many different military, political, and technological factors. Undoubtedly, the future will continue to present significant external challenges to DTRA and DTRA will continue to respond by maintaining its ability to perform its mission. Factors that may affect DTRA include:

- Contingencies at home and abroad
- DoD budget constraints and changing priorities
- Increased inspection and security demands worldwide
- Evolving terrorist threats and activities
- Increased communications and technology requirements
- Globalization involving broader treaty obligations and multi-national agreements
- Increased requirements for Combatant Commanders who rely on DTRA for WMD expertise; planning and operational support; applied technology; force protection support; technical reachback; and training and exercises

DTRA understands this global and technical environment and has demonstrated prior to and since September 11, 2001, that it is committed to effective, responsive programs and activities that meet the challenges of the future to make the world safer.

In the near future, DTRA hopes to procure and implement a new core financial management system. The new system will provide the basis for greatly increased functionality and timeliness and efficiency in the production of financial information, including compliant financial statements, cost accounting and performance management information.

The new core financial system will provide the basis for implementing a cost accounting system. The advancements in financial systems will provide the basis for DTRA to support its performance measurement plans with systems for reporting on actual performance. Performance data will also be linked to the full cost of accomplishment. DTRA will be able to report the full cost of activities, develop cost information over a span of years and provide data for better decision making.

7.0 Limitations of Financial Statements

In accordance with OMB Bulletin 01-09, "Form and Content of Agency Financial Statements" and OMB Circular A-136, "Financial Reporting Requirements," we are disclosing the following limitations of DTRA's FY 2005 financial statements.

DTRA's financial statements have been prepared to report the financial position and results of operations of DTRA, pursuant to the requirements of 31 U.S.C. 3515(b). While the financial statements have been prepared from the books and records of DTRA in accordance with generally accepted accounting principles (GAAP) for federal entities and the formats prescribed by OMB, 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. At this time, the Agency is unable to implement all elements of the standards due to financial management systems limitations. DoD is in the process of implementing system improvements to address those limitations. The financial statements should be read with the realization that they are for a component of the U.S. Government, a sovereign entity.

Defense Threat Reduction Agency

Management's Discussion and Analysis (MD&A)

Fiscal Year 2005

TAB B

PRINCIPAL FINANCIAL STATEMENTS

Department of Defense
Defense Threat Reduction Agency
CONSOLIDATED BALANCE SHEET
As of September 30, 2005 and 2004
(Amounts In Thousands)

		2005 Consolidated		2004 Consolidated
ASSETS (Note 2)				
Intragovernmental:				
Fund Balance with Treasury (Note 3)	$	1,833,839	$	2,042,532
Accounts Receivable (Note 4)		1,931		6,7566
Total Intragovernmental Assets		1,835,770		2,049,288
Accounts Receivable (Note 4)		644		-
Inventory and Related Property (Note 5)		25,708		
General Property, Plant and Equipment (Note 6)		121,041		97,140
TOTAL ASSETS		1,983,163		2,146,428
LIABILITIES (Note 7)				
Intragovernmental:				
Accounts Payable (Note 8)		132		622
Other Liabilities (Note 7 and Note 10)		1,636		2,224
Total Intragovernmental Liabilities		1,768		2,846
Accounts Payable (Note 8)		67,018		49,637
Military Retirement Benefits and Other Employment-Related Actuarial Liabilities (Note 12)		2,007		2,040
Environmental Liabilities (Note 9)		61,043		71,508
Other Liabilities (Note 7 and Note 10)		11,698		12,065
TOTAL LIABILITIES		143,534		138,096
Commitments and Contingencies (Note 11)				
NET POSITION				
Unexpended Appropriations		1,757,908		2,005,345
Cumulative Results of Operations		81,721		2,987
TOTAL NET POSITION		1,839,629		2,008,332
TOTAL LIABILITIES AND NET POSITION	$	1,983,163	$	2,146,428

The accompanying notes are an integral part of these statements.

Department of Defense
Defense Threat Reduction Agency
CONSOLIDATED STATEMENT OF NET COST
For the periods ended September 30, 2005 and 2004
(Amounts In Thousands)

		2005 Consolidated		2004 Consolidated
Program Costs				
Intragovernmental Gross Costs	$	483,530	$	94,092
(Less: Intragovernmental Earned Revenue)		(18,644)		(23,574)
Intragovernmental Net Costs		464,886		70,518
Gross Costs With the Public		922,205		1,310,793
(Less: Earned Revenue From the Public)		0		365
Net Costs With the Public		922,205		1,320,158
Total Net Cost		1,387,091		1,372,676
Cost Not Assigned to Programs		-		-
(Less:Earned Revenue Not Attributable to Programs)		-		-
Net Cost of Operations	$	1,387,091	$	1,372,676

The accompanying notes are an integral part of these statements.

Department of Defense
Defense Threat Reduction Agency
CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION
For the periods ended September 30, 2005 and 2004
(Amounts In Thousands)

	2005 Consolidated	2004 Consolidated
CUMULATIVE RESULTS OF OPERATIONS		
Beginning Balances	$ 2,987	$ 27,066
Prior period adjustments (+/-)	-	-
Beginning Balances, as adjusted	2,987	27,066
Budgetary Financing Sources:		
Appropriations used	1,346,102	1,272,119
Other budgetary financing sources (+/-)	0	(1,460)
Other Financing Sources	-	-
Imputed financing from costs absorbed by others	76,716	77,938
Other	43,006	-
Total Financing Sources	1,465,825	1,348,597
Net Cost of Operations (+/-)	1,387,091	1,372,676
Ending Balances	81,721	2,987
UNEXPENDED APPROPRIATIONS		
Beginning Balances	2,005,345	2,060,249
Prior period adjustments (+/-)	-	-
Beginning Balances, as adjusted	2,005,345	2,060,249
Budgetary Financing Sources:		
Appropriations received	1,204,844	1,244,349
Appropriations transferred-in/out (+/-)	(5,130)	(10,508)
Other adjustments (rescissions, etc) (+/-)	(101,049)	(16,626)
Appropriations used	(1,346,102)	(1,272,119)
Other Financing Sources	-	-
Total Financing Sources	(247,437)	(54,904)
Ending Balances	$ 1,757,908	$ 2,005,345

The accompanying notes are an integral part of these statements.

Department of Defense
Defense Threat Reduction Agency
COMBINED STATEMENT OF BUDGETARY RESOURCES
For the periods ended September 30, 2005 and 2004
(Amounts In Thousands)

		2005 Combined		2004 Combined
BUDGETARY FINANCING ACCOUNTS				
BUDGETARY RESOURCES				
Budget Authority:				
Appropriations received	$	1,204,844	$	1,244,349
Net transfers (+/-)		(974)		(10,208)
Unobligated balance:				
Beginning of period		465,801		637,337
Net transfers, actual (+/-)		(4,156)		(300)
Spending authority from offsetting collections:				
Earned				
Collected		55,301		39,742
Receivable from Federal sources		(35,812)		(16,533)
Change in unfilled customer orders				
Advance received		(2,441)		(2,214)
Without advance from Federal sources		(7,237)		(7,576)
Subtotal		9,811		13,419
Recoveries of prior year obligations		114,050		72,645
Temporarily not available pursuant to Public Law		-		-
Permanently not available		(101,049)		(16,522)
Total Budgetary Resources	$	1,688,327	$	1,940,720

The accompanying notes are an integral part of these statements.

Department of Defense
Defense Threat Reduction Agency
COMBINED STATEMENT OF BUDGETARY RESOURCES
For the periods ended September 30, 2005 and 2004
(Amounts In Thousands)

		2005 Combined		2004 Combined
STATUS OF BUDGETARY RESOURCES				
Obligations incurred:				
Direct	$	1,411,366	$	1,460,439
Reimbursable		14,568		14,480
Subtotal		1,425,934		1,474,919
Unobligated balance:				
Apportioned		235,761		388,669
Exempt from apportionment		-		-
Other available		-		1
Unobligated Balances Not Available		26,632		77,131
Total, Status of Budgetary Resources		1,688,327		1,940,720
Relationship of Obligations to Outlays:				
Obligated Balance, Net - beginning of period		1,577,916		1,436,816
Obligated Balance transferred, net (+/-)		-		-
Obligated Balance, Net - end of period:				
Accounts receivable		(3,696)		(39,508)
Unfilled customer order from Federal sources		(22,619)		(29,856)
Undelivered orders		1,525,272		1,576,186
Accounts payable		73,124		71,095
Outlays:				
Disbursements		1,360,769		1,285,283
Collections		(52,860)		(37,529)
Subtotal		1,307,909		1,247,754
Less: Offsetting receipts		-		-
Net Outlays	$	1,307,909	$	1,247,754

The accompanying notes are an integral part of these statements.

Department of Defense
Defense Threat Reduction Agency
COMBINED STATEMENT OF FINANCING
For the periods ended September 30, 2005 and 2004
(Amounts In Thousands)

	2005 Combined	2004 Combined
Resources Used to Finance Activities:		
Budgetary Resources Obligated		
Obligations incurred	$ 1,425,934	$ 1,474,919
Less: Spending authority from offsetting collections and recoveries (-)	(123,861)	(86,064)
Obligations net of offsetting collections and recoveries	1,302,073	1,388,855
Less: Offsetting receipts (-)	-	-
Net obligations	1,302,073	1,388,855
Other Resources		
Imputed financing from costs absorbed by others	76,716	77,938
Other	43,006	-
Net other resources used to finance activities	119,722	77,938
Total resources used to finance activities	1,421,795	1,466,793
Resources Used to Finance Items not Part of the Net Cost of Operations		
Change in budgetary resources obligated for goods, services and benefits ordered but not yet provided		
Undelivered Orders (-)	50,915	(112,096)
Unfilled Customer Orders	(9,678)	(9,790)
Resources that fund expenses recognized in prior periods	(11,174)	(2,202)
Resources that finance the acquisition of assets	(38,245)	(46,118)
Other resources or adjustments to net obligated resources that do not affect net cost of operations		
Other	(43,006)	-
Total resources used to finance items not part of the net cost of operations	(51,188)	(170,206)
Total resources used to finance the net cost of operations	$ 1,370,607	$ 1,296,587

The accompanying notes are an integral part of these statements.

Department of Defense
Defense Threat Reduction Agency
COMBINED STATEMENT OF FINANCING
For the periods ended September 30, 2005 and 2004
(Amounts In Thousands)

	2005 Combined	2004 Combined
Components of the Net Cost of Operations that will not Require or Generate Resources in the Current Period:		
Components Requiring or Generating Resources in Future Period:		
Increase in annual leave liability	$ 966	$ 7,161
Increase in environmental and disposal liability	-	65,977
Other (+/-)	645	87
Total components of Net Cost of Operations that will require or generate resources in future periods	1,611	73,225
Components not Requiring or Generating Resources:		
Depreciation and amortization	3,119	2,840
Revaluation of assets or liabilities (+/-)	-	-
Other (+/-)	11,754	24
Total components of Net Cost of Operations that will not require or generate resources	14,873	2,864
Total components of net cost of operations that will not require or generate resources in the current period	16,484	76,089
Net Cost of Operations	$ 1,387,091	$ 1,372,676

The accompanying notes are an integral part of these statements.

TAB C

NOTES TO THE PRINCIPAL STATEMENTS

ORGANIZATION

The Defense Threat Reduction Agency (DTRA) was established in 1998 bringing together the organizational elements within the Department of Defense (DoD) that were involved in reducing the global threats from weapons of mass deduction. The creation of DTRA consolidated three activities: the On-Site Inspection Agency (OSIA), the Defense Special Weapons Agency (DSWA), and the Defense Technology Security Administration (DTSA). DTRA's first fiscal year of operations was 1999. The DTRA is under the Office of the Secretary of Defense for Acquisition, Technology and Logistics. The accompanying financial statements report on the activity and positions of these combined organizational units for fiscal year 2004.

MISSION

The mission of the DTRA is to safeguard America's interests from weapons of mass destruction (WMD), chemical, biological, radiological, nuclear and high explosives (CBRNE), by controlling and reducing the threat, and by providing quality tools and services for the warfighter. DTRA supports the three pillars of the National Strategy on combating WMD, which are nonproliferation, counterproliferation and consequence management. The Agency also supports U.S. Strategic Command in combating WMD. The following strategic goals are identified in DTRA's Strategic Plan and provide the framework for accomplishing DTRA's mission.

NOTES TO PRINCIPAL FINANCIAL STATEMENTS

Note 1.	Significant Accounting Policies

Basis of Presentation

These financial statements have been prepared to report the financial position and results of operations of the Defense Threat Reduction Agency (DTRA), as required by the Chief Financial Officers (CFO) Act of 1990, expanded by the Government Management Reform Act (GMRA) of 1994, and other appropriate legislation. The financial statements have been prepared from the books and records of the DTRA in accordance with the "Department of Defense Financial Management Regulation" ("DoDFMR"), Office of Management and Budget (OMB) Circular A-136, "Financial Reporting Requirements", and to the extent possible, Federal generally accepted accounting principles (GAAP). The accompanying financial statements account for all resources for which the DTRA is responsible except that information relative to classified assets, programs, and operations has been excluded from the statements or otherwise aggregated and reported in such a manner that it is no longer classified. The DTRA's financial statements are in addition to the financial reports also prepared by the DTRA pursuant to OMB directives that are used to monitor and control the DTRA's use of budgetary resources.

The DTRA is unable to fully implement all elements of Federal GAAP and OMB Circular A-136 due to limitations of its financial management processes and systems, including nonfinancial feeder systems and processes. The DTRA is able to remedy most of these deficiencies through end-of-year adjustments and accruals. The elements that are uncorrected are not material to the financial statements. The FASAB intends that application of its standards be limited to items that are material. The DTRA continues to implement process and system improvements addressing the limitations of its financial and nonfinancial feeder systems. A more detailed explanation of these financial statement elements is provided in the applicable notes.

Mission of the Reporting Entity

The mission of the DTRA is to safeguard America's interests from weapons of mass destruction (WMD), chemical, biological, radiological, nuclear and high explosives (CBRNE), by controlling and reducing the threat, and by providing quality tools and services for the warfighter. DTRA supports the three pillars of the National Strategy on combating WMD, which are nonproliferation, counterproliferation and consequence management. The Agency also supports U.S. Strategic Command in combating WMD. The following strategic goals are identified in DTRA's Strategic Plan and provide the framework for accomplishing DTRA's mission.

Appropriations and Funds

The DTRA's appropriations and funds are in the general fund account. This account is used to fund and report how the resources have been used in the course of executing the DTRA's mission. General funds are used for financial transactions arising under congressional appropriations, including personnel, operation and maintenance, research and development, procurement, and construction accounts.

Basis of Accounting

The DTRA identifies programs based upon the major appropriation groups provided by Congress and generally records transactions on a budgetary basis and not an accrual accounting basis as is required by Federal GAAP. For FY 2005, the DTRA's financial management systems are unable to meet all of the requirements for full accrual accounting. Many of the DTRA's financial and nonfinancial feeder systems and processes were designed and implemented prior to the issuance of Federal GAAP for federal agencies and, therefore, were not designed to collect and record financial information on the full accrual accounting basis as is required by Federal GAAP. The DTRA has undertaken efforts to determine the actions required to bring its financial and non-financial feeder systems and processes into compliance with all elements of Federal GAAP. Until such time as all of the DTRA's financial and non-financial feeder systems and processes are updated to collect and report financial information as required by Federal GAAP, the DTRA's financial data will be based on budgetary transactions (obligations, disbursements, and collections), transactions from nonfinancial feeder systems, and adjustments for known accruals of major items such as payroll expenses, accounts payable, and environmental liabilities. In all material respects, the financial statements are presented on the accrual basis of accounting as required.

On December 21, 2001, the Office of Management and Budget published a memorandum for chief financial officers and inspector generals entitled, "Future External Reporting Changes." Driven primarily by the President's Management Agenda, the OMB's goal is to enhance financial performance as a result of improving timeliness, reliability and usefulness of information. The OMB requires agencies to submit quarterly unaudited financial statements 21 days following the end of each quarter. The unprecedented and historic milestone commenced with the quarter ending March 31, 2004.

Revenues and Other Financing Sources

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

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

Recognition of Expenses

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

Accounting for Intragovernmental Activities

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

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

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

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

To prepare reliable financial statements, transactions occurring between entities within the DoD or between two or more federal agencies must be eliminated. Under the provisions of the DoD Financial Management Regulation, Volume 6B, Chapter 13, the DTRA obtained a waiver for 4th Quarter, FY 2005, whereby, the seller side revenues and receivables of other components were adjusted to agree with the DTRA's expenses and payables (buyer-side). In addition, other component's buyer side payables, expenses and advances were adjusted to agree with the DTRA's accounts receivables, revenues and advances (seller-side) for 4th Quarter, FY 2005 as outlined in the DoD Financial Management Regulation. For comparative purposes, the DTRA received a waiver for eliminations for 4th Quarter, FY 2004. Finally, the DTRA implemented the policies and procedures contained in the Intragovernmental Eliminations Task Force's "Intragovernmental Fiduciary Transactions Accounting Guide" for reconciling intragovernmental transactions pertaining to investments in federal securities, borrowings from Treasury and the Federal Financing Bank, Federal Employee Compensation Act transactions with the Department of Labor, and benefit program transactions with the OPM.

Transactions with Foreign Governments and International Organizations

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

Funds with the U.S. Treasury

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

In addition, the DFAS centers and the USACE Finance Center submit reports to Treasury, by appropriation, on interagency transfers, collections received and disbursements issued. The Department of the Treasury then records this information to the appropriation Fund Balance with Treasury (FBWT) account maintained in the Treasury's system. Material disclosures are provided at Note 3. Differences between accounting offices' detail-level records and Treasury's FBWT accounts are disclosed in Note 3. It specifically addresses differences caused by in-transit disbursements and unmatched disbursements which are not recorded in the accounting offices' detail-level records.

Accounts Receivable

As presented in the Balance Sheet, accounts receivable includes accounts, claims, and refunds receivable from other federal entities or from the public. Allowances for uncollectible accounts due from the public are based upon analysis of collection experience by fund type. The Department does not recognize an allowance for estimated uncollectible amounts from another federal agency. Claims against another federal agency are to be resolved between the agencies. Material disclosures are provided at Note 4.

Inventory and Related Property

The DTRA is using the purchase method of accounting for operating material and supplies, as defined in the Statement of Federal Financial Accounting Standards (SFFAS) No. 3, "Accounting for Inventory and Related Property."

General Property, Plant and Equipment

General property, plant, and equipment (PP&E) assets are capitalized at historical acquisition cost plus capitalized improvements when an asset has a useful life of 2 or more years, and when the acquisition cost equals or exceeds the DoD capitalization threshold of $100,000. Also, improvement costs over the DoD capitalization threshold of $100,000 for General PP&E should be capitalized. The Department contracted with two certified public accounting (CPA) firms to obtain an independent assessment of the validity of the General PP&E capitalization threshold. At the conclusion of the studies, both CPA firms recommended that the Department retain its current capitalization threshold of $100,000. All General PP&E, other than land, is depreciated on a straight-line basis.

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

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

Material disclosures are provided at Note 6.

Advances and Prepayments

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

Material disclosures are provided at Note 10.

Other Assets

The DTRA 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 DTRA provides financing payments. One type of financing payment that the DTRA makes, for real property, is based upon a percentage of completion. In accordance with the SFFAS No. 1, "Accounting for Selected Assets and liabilities," such payments are treated as construction-in-progress and are reported on the general PP&E line and in Note 6, General PP&E, Net.

In addition, based on the provision of the Federal Acquisition Regulation, the DTRA makes financing payments under fixed price contracts that are not based on a percentage of completion. DoD has completed a review of all applicable federal accounting standards, applicable public laws on contract financing, Federal Acquisition Regulation Parts 32, 49, and 52,; and the OMB guidance in 5 Code of Federal Regulations Part 1315, "Prompt Payment." DoD concluded that SFFAS No. 1 does not fully or adequately addresses the subject of progress payment accounting and is considering what further action is appropriate.

Contingencies and Other Liabilities

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

The DTRA loss contingencies could arise as a result of pending or threatened litigation, property or environmental damages and contract disputes.

Accrued Leave

Civilian annual leave is accrued as earned and the accrued amounts are reduced as leave is taken. The balances for annual leave at the end of the quarterly reporting period reflect current pay rates for the leave that is earned but not taken. Sick and other types of non-vested leave are expensed as taken.

Net Position

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

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

Treaties for Use of Foreign Bases

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

Comparative Data

In FY 2001, the DTRA began presenting the current and previous year's financial data for comparative purposes. This data is presented in the financial statements, as well as in the notes to the principal statements. The financial statements and accompanying notes to the financial statements report the financial position and results of operations for the 4th Quarter, FY 2005

Unexpended Obligations

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

Undistributed Disbursements and Collections

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

Intransit payments are those payments that have been made to other agencies or entities that have not been recorded in the accounting records. These payments are applied to the entities outstanding accounts payable balance. In-transit collections are those collections from other agencies or entities that have not been recorded in the accounting record. These collections are also applied to the entities accounts receivables balance.

The DoD policy is to allocate supported undistributed disbursements and collections between federal and nonfederal categories based on the percentage of Federal and nonfederal accounts payable and accounts receivable. Unsupported undistributed disbursements are recorded in accounts payable. Unsupported undistributed collections are recorded in other liabilities. For unsupported undistributed collections and disbursements, the DTRA follows this; however, for supported undistributed collections and disbursements; the DTRA records supported undistributed collections as federal accounts receivable and supported undistributed disbursements as undelivered orders.

Refer to Note 3 for Problem Disbursements.

Note 2.	Nonentity Assets

As of September 30 (Amounts In Thousands)	2005	2004
Intra-governmental Assets		
Accounts Receivable	$ -	$ 239
Total Intra-governmental Assets	-	239
Non-Federal Assets		
Accounts Receivable	(3)	-
Total Non-Federal Assets	(3)	-
Total Non-Entity Assets	(3)	239
Total Entity Assets	1,963,165	2,146,189
Total Assets	$ 1,963,165	$ 2,146,428

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

Fluctuations

Intragovernmental Assets

The decrease of $239 thousand (100%) in intragovernmental accounts receivables is the result of the collection of an outstanding receivable for the Defense Special Weapons Agency (DSWA) originally reported in the 4th Quarter, FY 2004 from a canceled appropriation.

Nonfederal Assets

The $3 thousand (100%) decrease in nonfederal accounts receivable is the result of the following; a credit balance in the accounts receivable that is for an appropriation that canceled on September 30, 2005 and for $17 thousand principle and interest assessed on a delinquent vendor account. Collection is pending for the delinquent vendor account and is estimated that this will occur during the first half of FY 2006. However, DTRA submitted a write-off package for this vendor account in April 2005. The DTRA received a $20 thousand advance from a nonfederal customer for the Space Launch Program. Upon transfer of the program to the Defense Technical

Security Administration, DTRA attempted to return the over collected funds to the customer. However, DTRA determined that the nonfederal customer had ceased operations.

Note 3. Fund Balance with Treasury

As of September 30 (Amounts In Thousands)	2005	2004
Fund Balances		
Appropriated Funds	$ 1,833,839	$ 2,040,379
Other Fund Types	-	2,153
Total Fund Balances	1,833,839	2,042,532
Fund Balances Per Treasury Versus Agency		
Fund Balance per Treasury	-	-
Fund Balance per DTRA	1,833,839	2,042,532
Reconciling Amount	$ (1,833,839)	$ (2,042,532)

Definition

The Department of Treasury reports fund balances at the appropriation basic symbol level. The Other Defense Organizations (ODO) general funs Treasury Index 97 funds are allotted at limit level. This precludes compliance by the ODO fund reporting entities, specifically the Defense Threat Reduction Agency (DTRA), form providing the Fund Balance per Treasury amounts.

Fluctuations

The $208,693 thousand (10%) decrease in FBWT Total Fund Balances is primarily due to a $96,000 thousand (46%) decrease in our annual appropriations combined with a $60,000 thousand (29%) increase in program execution outlays, and the $2,153 thousand (1%) decrease is due to the transfer of the Space Launch Program to the Defense Technical Security Administration. The final audit and reconciliation of the Space Launch activity at DTRA was completed during the 1st Quarter, FY 2005 and the account was fully liquidated.

Note References

See Note Disclosure 1.I., Significant Accounting Policies, for additional discussion on financial reporting requirements and Department of Defense policies governing Funds with the United States Treasury.

As of September 30	2003	2004	2005	(Decrease)/ Increase from FY 2004 - 2005
Disclosures Related to Problem Disbursements and In-Transit Disbursements				
(Amounts in thousands)				
Total Problem Disbursements, Absolute Value				
Unmatched Disbursements (UMDS)	$ 1,506	$ 5,502	$ 5,648	$ 146
Negative Unliquidated Obligations (NULO)	100	1	46	45
Total In-transit Disbursements, Net	$ 84,506	$ 49,696	$ 77,438	$ 27,742

Unmatched Disbursement (UMD) occurs when a payment does not match to a corresponding obligation in the accounting system.

Negative Unliquidation Obligation (NULO) occurs when a payment is made against a valid obligation, but the payment amount is greater than the amount of the obligation recorded in the official accounting system.

The in-transits represent the net value of disbursements and collections made by a Department of Defense disbursing activity on behalf of an accountable activity and have not been posted to the accounting system.

These problem disbursements represent the absolute value of the DTRA's funds that have been reported by a disbursing station to the Department of the Treasury, but have not yet been matched against the specific source obligation that gave rise to the disbursements. These payments have been made using available funds and are based on valid receiving reports for goods and services delivered under valid contracts.

Fluctuations

Unmatched Disbursements (UMD)
For 4th Quarter, FY 2005 the DTRA has an increase of $146 thousand (3%) in UMDs. The DTRA has $537 thousand (10%) in aged UMDs.

Negative Unliquidated Obligations (NULOs)
For 4th Quarter, FY 2005 the DTRA sub-allotment fund holders reported an increase of $45 thousand (4500%)in NULOs. Research should be completed during the 1st Quarter, FY 2006 to be able to connect these NULOs

Total In-transit Disbursements, Net
For 4th Quarter, FY 2005 the DTRA reported an increase of $28 million (56%) in in-transits. The DTRA has $952 thousand (1%) in aged in-transits.

Note 4.	Accounts Receivable

As of September 30	2005			2004
	Gross Amount Due	Allowance For Estimated Uncollectibles	Accounts Receivable, Net	Accounts Receivable, Net
(Amounts in thousands)				
Intragovernmental Receivables	$ 1,930	N/A	$ 1,930	$ 6,756
Nonfederal Receivables (From the Public)	$ 644	$ 0	$ 644	$ 0
Total Accounts Receivable	$ 2,574	$ 0	$ 2,574	$ 6,756

Fluctuations

The $4,826 thousand (71%) decrease in intragovernmental receivables is attributable to the effort to collect aged receivables by the Defense Threat Reduction Agency (DTRA). The DTRA has reduced the balance of accounts receivable aged over 90 days by $2,770 thousand (41%) since the 4th Quarter, FY 2004. Please see the table below for details on current accounts receivable over 90 days.

Receivables over 90 Days	**(In thousands)**
Public	$ 21
Intragovernmental	
Due within DoD	$ 19
Debt Outside DoD	$ 83
Total Intragovernmental	**$ 102**

The $644 thousand (100%) increase in nonfederal accounts receivable is attributable to the following: $366 thousand (57%) in receivables in the Space Launch Defense Program, $157 thousand (24%) of erroneous payments made by the DTRA to various vendors during Fiscal Year 2005, and the remaining amount is attributable to an increase in activity by sub-allotment holders.

The $366 thousand (57%) increase in receivables due to the Space Launch program is the result of the final audit and reconciliation of the Space Launch activity at DTRA completed during the 1st Quarter, FY 2005. It was determined that under the reimbursable agreement, DTRA was owed this amount by the intragovernmental and nonfederal trading partners.

Information Related to Accounts Receivable

Allowance Method

The DTRA has analyzed the nonfederal accounts receivable, and based on historical data has determined that all nonfederal accounts receivable are collectible. The DTRA has determined that an allowance for doubtful accounts will not be established, but will review each invoice on a case-by-case basis.

Allocation of Undistributed Collections

The policy of the Department of Defense (DoD) is to allocate supported undistributed collections between federal and nonfederal categories based on the percentage of federal and nonfederal accounts receivable.

Note References

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

Note 5.	**Inventory and Related Property**

Operating Materials and Supplies, Net

As of September 30	2005			2004	
	OM&S Gross Value	Revaluation Allowance	OM&S, Net	OM&S, Net	Valuation Method
(Amounts in thousands)					
OM&S Categories					
Held for Use	$ 25,708	$ 0	$ 25,708	$ 0	Procurement Cost
Total	$ 25,708	$ 0	$ 25,708	$ 0	

Legend for Valuation Methods:

Other Information

General Composition of OM&S

OM&S is comprised of materials used to conduct Research and Development for Weapons of Mass Destruction Deterrent Programs, including chemical, biological and radiological materials.

Fluctuations

The $25,708 thousand (100%) increase in value of the DTRA Government Furnished Material and Contractor Acquired Material in the hands of contractors is included in the OM&S values reported above. The OM&S was previously included in the General Property Plant and Equipment. The Department of Defense (DoD) is presently reviewing its process for reporting these amounts in an effort to determine the appropriate accounting treatment and the best method to annually collect and report required information without duplicating information in other existing logistics systems.

Note Reference

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

Note 6.	**General PP&E, Net**

As of September 30	2005					2004
(Amounts In Thousands)	Depreciation Amortization Method	Service Life	Acquisition Value	(Accumulated Depreciation/ Amortization)	Net Book Value	FY Book Value Net
Major Asset Classes:						
Software	S/L	2-5 or 10	17,541	-	17,541	13,745
General Equipment	S/L	5 or 10	34,991	(13,614)	21,377	33,791
Construction- -in-Progress	N/A	N/A	82,123	N/A	82,123	49,604
Total General PP&E			$134,655	$ (13,614)	$ 121,041	$ 97,140

Fluctuations

The $23,901 thousand increase (25%) in General Property Plant and Equipment (PP&E) is summarized in the following table:

The following is a summary of the changes in PP&E during the Current Fiscal Year:	(in thousands)
General Equipment	$ 1,395
Loss on Disposal of General Equipment	(243)
General Equipment Depreciation)	(2,703)
Annual Update of Property in the Hands of Contractors (net)	(10,863)
Subtotal: Total General Equipment	**(12,414)**
Acquired Internal Use Software	3,796
Construction-in-progress	32,518
Net Change in Total	**$ 23,901**

The $3,796 thousand (28%) increase in software is attributable to capitalized Business Operations Software. Business Operations Software includes internally developed systems used to fulfil the Defense Threat Reduction Agency's (DTRA) mission. The DTRA initially reported software in the 4th Quarter, FY 2004.

The $12,414 thousand (37%) decrease is primarily the result of a review during the 4th Quarter, FY 2005 of the Property in the Hands of Contractors, yielding a net reduction of $10,863 (32%) to general equipment. The categories of the general equipment are computer and network systems and research and development equipment.

The $32,519 thousand (66%) increase in construction in progress is attributable to two projects. The construction of the new Defense Threat Reduction Center accounts for $32,419 thousand (65%) of the increase, and $99 thousand (1%) of the increase is attributable to construction in Darmstadt, Germany. The activity in Darmstadt, Germany is related to the conversion of an old warehouse to office space for personnel moving from Rheinmein, Germany to Darmstadt, Germany. Both of these projects should be completed in Fiscal Year 2006.

Information Related to General Property, Plant and Equipment, Net

The value of the ODO GF PP&E real property in the possession of contractors is included in the values reported above for the Major Asset Classes of Land and Building, Structures, and Facilities. The value of General PP&E personal property (Major Asset Classes of Software and Equipment) does not include all of the General PP&E above the DoD capitalization threshold in the possession of contractors. The net book value of such property is immaterial in relation to the total General PP&E net book value. In accordance with an approved strategy with the OMB, the Government Accountability Office, and the Office of the Inspector General, the DoD is developing new policies and a contractor reporting process to capture General PP&E information for future reporting purposes for compliance with generally accepted accounting standards.

The DTRA recognizes that inclusion in the major asset class of property in the hands of the contractor, is contrary to DoD directives. However, the decision to include such property was based on an audit recommendation from the independent audit firm retained by the DTRA. The audit firm made its recommendation based on the Statement of Federal Financial Accounting Standards 6, chapter 2 and stated concepts of the Federal Accounting Standards Advisory Board. The following is a summary of the property in the hands of contractor as reported in DTRAs financial statements:

Property in Hands of Contractors	In thousands
Acquisition Value	$ 24,201
Depreciation	(6,713)
Net Book Value	**$ 17,488**

Note References

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

Note 7. Liabilities Not Covered by Budgetary Resources

As of September 30 (Amounts In Thousands)	2005	2004
Intra-governmental Liabilities		
Accounts Payable	$ -	$ (157)
Other	929	693
Total Intra-governmental Liabilities	929	536
Non-Federal Liabilities		
Accounts Payable	29	721
Military Retirement Benefits and Other Employment-Related Actuarial Liabilities	2,007	2,040
Environmental Liabilities	56,582	65,977
Other Liabilities	7,407	6,441
Total Non-Federal Liabilities	66,025	75,179
Total Liabilities Not Covered by Budgetary Resources	66,954	75,715
Total Liabilities Covered by Budgetary Resources	76,580	62,381
Total Liabilities	$ 143,534	$ 138,096

Definitions

Liabilities Not Covered by Budgetary Resources

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

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

Fluctuations

Intragovernmental Liabilities

The increase of $157 thousand (100%) in intragovernmental accounts payable is due to the liquidation in fiscal year 2005 of an abnormal balance in the accounts payable that was in a cancelled appropriation. The increase of $236 thousand (34%) in other intragovernmental liabilities other is attributable to an increase in unfunded FECA liability due to an increase in civilian personnel from 919 to 1,123 as of 4th Quarter, FY 2005.

Nonfederal Liabilities

The decrease of $690 thousand (96%) in nonfederal accounts payable is attributable to the Defense Threat Reduction Agency's (DTRA's) efforts to process invoices in a more timely manner.

The decrease of $9,395 thousand (14%) in nonfederal non-current environmental liabilities is attributable to the cancellation of $9,895 thousand in funding requirements as of October 1, 2004 for FY 2004 through FY 2009 for the Defense Environmental Restoration Program (DERP). This was offset by an increase in $500 thousand in funding in the 4th quarter 2005 for future cleanup costs at the Nevada Test Site (NTS). The liability for the Nevada Test Site (NTS) is reflected in the DTRA's December 2003 comprehensive action plan and associated cost estimates for the work required. The activities are covered under the NTS Federal Facility Agreement and Consent Order, which addresses environmental restoration under the legal authorities of the Comprehensive Environmental Response Compensation and Liability Act, the Resource Conservation and Recovery Act, the Federal Water Pollution Control Act, and various Nevada state laws.

The increase of $966 thousand (15%) in other liabilities, which is comprised of unfunded annual leave, due to the increase in civilian personnel from 919 as of September 30, 2004, to 1,123 as of September 30, 2005.

For further reference the following schedule shows the variance between FY 2005 nonfederal other liabilities and FY 2004 in the amount of $(9,152) thousand is as follows:

Note 7 Line	2005 Total	2004 Total	Variance
Nonfederal Accounts Payable	$ 29	$ 719	$ (690)
Military Retirement Benefits	$ 2,007	$ 2,040	$ (33)
Environmental liabilities	$56,582	$65,977	$(9,395)
Other liabilities	$ 7,407	$ 6,441	$ 966
Total	$66,025	$75,177	$(9,152)

Other Information Related to Liabilities not Covered by Budgetary Resources

Intragovernmental

Composition of intragovernmental other liabilities is comprised of unfunded FECA liability.

Non-Federal

Composition of the nonfederal other liabilities is comprised of accrued annual leave.

Note 8.	**Accounts Payable**

As of September 30	2005			2004
(Amounts In Thousands)	Accounts Payable	Interest, Penalties, and Administrative Fees	Total	Total
Intra-governmental Payables	$ 133	N/A	$ 133	$ 622
Non-Federal Payables (to the Public)	67,018	-	67,018	49,637
Total	$ 67,151	$ -	$ 67,151	$ 50,259

Relevant Information for Comprehension

Intragovernmental accounts payable consists of amounts owed to other federal agencies for goods or services ordered and received, but not yet paid. Interest, penalties and administrative fees are not applicable to intragovernmental payables. Non-Federal payables (to the public) are payments to Non-Federal government entities.

Fluctuation

Intragovernmental Payables

The $489 thousand (79%) decrease in intragovernmental accounts payable is attributable to the Defense Threat Reduction Agency's (DTRA) efforts to process accounts payable use the Intragovernmental Payment and Collections (IPAC) process. This process has reduced the time needed to settle intragovernmental payments. This process began in the 1st Quarter, FY 2005.

Non-Federal Payables

The $17,381 thousand (35%) increase in Non-Federal payables (to the public) is due to an increase in program execution rates during FY 2005 and is primarily driven by an increase in the Cooperative Threat Reduction agency's Russian program and is partially offset by reductions in the Unconventional Nuclear Threat, Arms Control Technology, and United Nations Special commission on Iraq programs.

Note Reference

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

Note 9. Environmental Liabilities and Disposal Liabilities

As of September 30 (Amounts In Thousands)	2005			2004
	Current Liability	Noncurrent Liability	Total	Total
Non Federal				
Accrued Environmental Restoration (DERP funded) Costs:				
Active Installations-- Environmental Restoration (ER)	$ 124	$ -	$ 124	$ 10,082
Other Accrued Environmental Costs (Non-DERP funds) Active Installations-- Environmental Corrective Action	4,337	56,582	60,919	$ 61,425
Total Environmental Liabilities:	$ 4,461	$ 56,582	$ 61,043	$ 71,508

Fluctuations

The $10,465 thousand (15%) decrease in Total Environmental Liabilities is detailed in the following schedule:

(in thousands)

Note 14 Line	2005 Total	2004 Total	Variance
Current Liability			
--DERP Funded	$ 124	$ 187	$ (63)
Non-Current Liability			
--DERP Funded	$ 0	$ 9,895	$ (9,895)
Current Liability			
Non DERP funded	$ 4,337	$ 5,344	$ (1,007)
Non-Current Liability			
Non DERP funded	$56,582	$56,082	$ 500
Total	$61,043	$71,508	$(10,465)

The $9,958 thousand (99%) decrease for Active Installations Defense Environmental Restoration Program (DERP) costs is primarily attributable to a decrease of $9,895 thousand in the DERP Funded Non-Current Liability. This decrease is due to the transfer of the responsibility for the complete restoration of the Johnston Atoll site to the Department of the Air Force in the first quarter of FY 2005.

Information Related to Environmental Liabilities

Other Accrued Environmental Costs – Non-Defense Environmental Restoration Program (Non-DERP)

- Non-federal liabilities (current) represent FY 2002 through FY 2004 funding for clean up at Nevada Test Site (NTS) that has been contracted but not disbursed, and planned commitments within the next 12 months.
- Non-federal liabilities (non-current) represent future clean-up costs for NTS.

Starting with 4th quarter FY 2005, federal agencies are required to make additional disclosures regarding environmental liabilities. The following required disclosures are applicable to the DTRA's environmental liabilities:

Disclosure (amounts in thousands)	FY 2005	FY 2004
Amount of operating and capital expenditures used to remediate legacy waste. Legacy wastes are the wastes covered by the Defense Environmental Restoration Program (DERP).	$49	$907

General Disclosures

Other required disclosures regarding the DTRA's environmental liabilities are as follows: The environmental liability portion of the cleanup cost has been fully recognized for all the currently known environmental sites needing cleanup by the DTRA at the Nevada Test Site (NTS) and Kirtland Air Force Base (KAFB), New Mexico, as of September 30, 2005. The current liability is based on FY 2003 and FY 2004 funding that has been placed on contract through the Department of Energy - National Nuclear Security Administration (NNSA) at the NTS. This liability includes the fee charged by the NNSA at the NTS to contract this effort. The estimated costs for environmental liabilities are based on engineering estimates prepared by the DTRA staff. The NTS estimates were made by the DTRA staff at NTS and the estimates for KAFB were made by the DTRA staff at KAFB.

The methods of assigning estimated total environmental costs to current operating periods include the following:

Material changes will occur in the total estimated costs of environmental restoration activities (i.e., due to changes in laws, technology or plans), and the portion of the change in estimates that relate to prior-period operations.

The DTRA is relatively certain, based on the maturity of the program at the NTS that most of the environmental liability is known and the estimates are valid.

The DTRA has only estimated the cost ($200 thousand) for KAFB, to characterize its two sites; therefore, until the results of the site characterization are complete, there is a greater amount of uncertainty for this portion of the estimated environmental liability.

The following laws and regulations cover the cleanup requirements at the NTS and KAFB:

The liabilities for the NTS are covered under the NTS Federal Facility Agreement and Consent Order (FFACO), which addresses environmental restoration under the legal authorities of the Comprehensive Environmental Response Compensation and Liability Act (CERCLA), the Resource Conservation and Recovery Act (RCRA), the Atomic Energy Act, the Federal Water Pollution Control Act, and various Nevada State laws. The liability at KAFB is for potential environmental restoration activity required under CERCLA, RCRA, and New Mexico laws and regulations.

The entire liability is for environmental restoration activities, primarily to clean up, and to prevent the spread of, environmental contamination and dispose of hazardous wastes.

Note 10.	Other Liabilities

As of September 30	2005			2004
	Current Liability	Noncurrent Liability	Total	Total
(Amounts in thousands)				
Intragovernmental				
Advances from Others	$ 200	$ 0	$ 200	$ 508
FECA Reimbursement to the Department of Labor	0	958	958	454
Other Liabilities	507	(29)	478	1,262
Total Intragovernmental Other Liabilities	$ 707	$ 929	$ 1,636	$ 2,224
Nonfederal				
Accrued Funded Payroll and Benefits	$ 3,204	$ 0	$ 3,204	$ 2,526
Advances from Others	56	0	56	2,189
Accrued Unfunded Annual Leave	7,407	0	7,407	6,441
Other Liabilities	1,031	0	1,031	909
Total Nonfederal Other Liabilities	$ 11,698	$ 0	$ 11,698	$ 12,065
Total Other Liabilities	$ 12,405	$ 929	$ 13,334	$ 14,289

Fluctuations

Intragovernmental

Advances from Others Current Liabilities

The $308 thousand (61%) decrease from FY 2004 is due to the completion of work for which we received advances and the recognition of those advances as revenue in FY 2005. Advances from Others represents deposits received from federal customers in payment for work yet to be completed by the Defense Threat Reduction Agency (DTRA). The majority is attributable to the State Department and the Air Force. These deposits were received beginning in FY 1999.

FECA – Reimbursement to Department of Labor

The $504 thousand (111%) increase in FECA reimbursement is attributable to an increase in the current portion of the unfunded FECA liability, attributable to an increase in civilian personnel on board from 919 in FY 2004 to 1,123 in FY 2005.

Other Liabilities

The $784 thousand (62%) decrease in other liabilities is attributable to the elimination of most of DTRA's funding requirement for the Voluntary Separation Incentive Program (VSIP) liability. Payments were made to the VSIP participants in the 2nd Quarter, FY 2005, leaving only a $7 thousand VSIP liability for administrative costs.

The $588 thousand (26%) decrease in total intragovernmental liabilities is the cumulative result of the following: (see explanations provided above.)

Decrease in Advances from Others	(308)
Increase in FECA Reimbursement Liability to Department of Labor	504
Decrease in Other Liabilities	(784)
Cumulative Decrease in Total Intragovernmental Liabilities	**$(588)**

Non Federal

Accrued Funded Payroll Benefits
The $678 thousand (27%) increase in current-year accrued funded payroll and benefits for the DTRA is attributable to an increase in civilian personnel on board from 919 to 1,123 as of 4th Quarter, FY 2005.

Advances from Others
The $2,133 thousand (97%) decrease in nonfederal advances from others is due to fewer deposits being received from nonfederal customers in payment for work yet to be completed by DTRA.

Accrued Unfunded Annual Leave
The $966 thousand (15%) increase in Accrued Unfunded Annual Leave liability is attributable to an increase in the civilian workforce from 919 to 1,123 as of 4th Quarter FY 2005.

Other Liabilities
The $122 thousand (13%) increase in Other Liabilities consists of employer contributions and payroll taxes payable, and is the result of the increase in civilian personnel on board.

The $367 thousand (3%) decrease in total non-federal liabilities is the cumulative result of the following: (see explanations provided above.)

Increase in Accrued Funded Payroll	$ 678
Decrease in Advances from Others	(2,133)
Increase in Accrued Unfunded Leave	966
Increase in Other Liabilities	122
Cumulative Decrease in Total Non-Federal Liabilities	**$ (367)**

Other Information Related to Other Liabilities

Composition of Intragovernmental Other Liabilities:

Total Intragovernmental Other Current and Non-Current Liabilities is comprised of Health Benefits; Retirement; and Other.

Composition of Nonfederal Other Liabilities:

Total Nonfederal Other Liabilities is comprised of employer contribution and payroll taxes payables.

Note References

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

Note 11.	Commitments and Contingencies

The Defense Threat Reduction Agency (DTRA) is a party in various administrative proceedings, legal actions, and claims brought by and against it. The DTRA General Counsel has identified one known claim, litigation, and assessment in excess of the Department of Defense threshold of $10 million or more made against the DTRA.

The plaintiff, Die Casters International, Inc, filed a complaint in the United States Court of Federal Claims on July 6, 2004. The plaintiff, Die Casters International, Inc, is seeking approximately $110 million in damages for breach of contract. The Government intends to contest this claim vigorously. The DTRA's General Counsel is unable to express an opinion concerning the likely outcome of this case.

Note 12.	Military Retirement Benefits and Other Employment Related Actuarial Liabilities

As of September 30	2005				2004
(Amounts In Thousands)	Actuarial Present Value of Projected Plan Benefits	Assumed Interest Rate (%)	(Less: Assets Available to Pay Benefits)	Unfunded Actuarial Liability	Unfunded Actuarial Liability
Other:					
FECA	$ 2,007		$ -	$ 2,007	$ 2,040
Total Military Retirement Benefits and Other Employment Related Actuarial Liabilities:	$ 2,007		$ -	$ 2,007	$ 2,040

Relevant Information for Comprehension

<u>Military Retirement</u>

The military retirement benefits and military retirement health benefits are reported separately by the Military Retirement Fund (MRF). The applicable portion of the military retirement benefits actuarial liability for the Defense Threat Reduction Agency (DTRA) is reported on the financial statements of the MRF.

<u>Reporting liability pertaining to Federal Employees Compensation Act (FECA)</u>

The actuarial liability for workers' compensation benefits is developed by the Department of Labor and provided to the Other Defense Organizations General Fund at the end of each fiscal year. The liability includes the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases. The liability is determined by using historical benefit payment patterns to predict the future payments. Cost-of-living adjustments and medical inflation factors are also included in the calculation of projected future benefits. Consistent with past practices, these projected annual benefit payments are then discounted to present value using the Office of Management and Budget's economic assumptions for 10-year Treasury notes and bonds.

Note 13.	Disclosures Related to the Statement of Net Cost

Information Related to the Statement of Net Cost

Statement of Net Cost

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

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

The 4th Quarter, FY 2005 DTRA financial statements were governed by the waiver guidelines provided in the Department of Defense Financial Management Regulation, Volume 6B, Chapter 13.

Fluctuations

Intragovernmental Gross Costs

Intragovernmental Gross Costs increased $389,438 thousand (414%). Some intragovernmental program costs were improperly identified and reported as Gross Cost with the Public in FY 2004. This resulted in understating Intragovernmental Gross Costs in the 4th Quarter FY 2004. Corrections were made in 1st Quarter, FY 2005. DTRA's program costs are accurately reported in 4th Quarter, FY 2005. (Note 18)

Gross Costs with the Public

Gross Costs with the Public decreased $379,587 (29%). Some intragovernmental program costs were improperly identified and reported as Gross Cost with the Public in FY 2004. This resulted in Gross Cost with the Public to be overstated in 4th Quarter FY 2004. Corrections were made in 1st Quarter, FY 2005. DTRA's program costs are accurately reported in 4th Quarter, FY 2005. (Note 18)

Intragovernmental Revenue

The $4,929 thousand (21%) decrease in intragovernmental earned revenue is primarily attributable to a decrease in the Weapons of Mass Destruction Combat Support programs, $4,365 thousand (89%). The Weapons of Mass Destruction Combat Support program was in support of Operation Iraqi Freedom and this mission was concluded in the 1st Quarter, FY 2005.

Earned Revenue from the Public

The $365 thousand (100%) decrease in earned revenue from the public occurred primarily because $307 thousand in public revenues was closed to Cumulative Results of Operations. The remaining $58 thousand decrease occurred due to a decrease in revenue generating services provided to the public during FY 2005.

Note 14.	Disclosures Related to the Statement of Changes in Net Position

As of September 30	2005	2005	2004	2004
	Cumulative Results of Operations	Unexpended Appropriations	Cumulative Results of Operations	Unexpended Appropriations
(Amounts in thousands)				
Imputed Financing				
Civilian CSRS/FERS Retirement	$ 2,709	$ 0	$ 2,734	$ 0
Civilian Health	3,457	0	2,911	0
Civilian Life Insurance	16	0	14	0
Total Imputed Financing	$ 6,182	$ 0	$ 5,659	$ 0

Information Related to the Statement of Net Position

Imputed Financing

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

Fluctuations

The $523 thousand (9%) increase in the Imputed Financing for Civilian Health represents the costs, as reported by the Department of Labor, for the 4th Quarter, FY 2005. The fluctuation is due to the changes in number of full-time equivalents (FTEs) within an entity at any given point in time. This is attributable to the increase in civilian personnel FTEs from 919 to 1,123 in the 4th Quarter, FY 2005.

Note 15.	**Disclosures Related to the Statement of Budgetary Resources**

As of September 30		
(Amounts In Thousands)	2005	2004
Net Amount of Budgetary Resources Obligated for Undelivered Orders at the End of the Period	$ 1,525,272	$ 1,576,186

Undelivered Orders

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

Other Disclosures

There is no direct correlation between Line 1 reported above to any specific line on the SBR. The Net Amount of Budgetary Resources Obligated for Undelivered Orders contains the following accounts: Undelivered Orders- Obligations Prepaid/Advanced, Undelivered Orders-Obligations Unpaid, and Downward/Upward Adjustments of Prior-Year Unpaid Undelivered Orders. The SBR Line 14C “Undelivered Orders” contains all of the referenced accounts excluding Undelivered Orders- Obligations Prepaid/Advanced. In addition, Line 14C includes the reporting of Undelivered Orders – Obligations Transferred.

Apportionment Categories

The Office of Management and Budget, Circular A-136, specifically requires disclosure of the amount of direct and reimbursable obligations incurred against amounts apportioned under categories A, Direct, and B, Reimbursable, and exempt from apportionment. This disclosure should agree with the aggregate of the related information as included in each reporting entity’s Report on Budget Execution (Standard Form 133) and Obligations incurred, Direct, and Obligations incurred, Reimbursable in the SBR.

Apportionment Categories for Obligations Incurred: (in thousands)

	Report on Budget Execution	Statement of Budgetary Resources
Direct Obligations, Category A	$1,359,175	$1,411,366
Reimbursable Obligations	14,567	14,568
Total Obligations	$1,373,742	$1,425,934

The difference of $52,192 thousand (100%) in direct obligations is primarily attributable to an audit adjustment recorded in 4th Quarter, FY 2004 associated with undelivered orders. After examining the Undelivered Order for 4th Quarter, FY 2004, the auditor stated, based on testing performed during the audit, that the Defense Threat Reduction Agency (DTRA) Undelivered Order were overstated compared to the obligation balance.

Spending Authority from Offsetting Collections

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

Note 16.	Disclosures Related to the Statement of Financing

The objective of the Statement of Financing is to reconcile the difference between budgetary obligations and the net cost of operations reported. It is presented as combined or combining statements rather than consolidated statements due to intragovernmental transactions not being eliminated.

Fluctuations

The increase of $11,845 thousand (48,647%) in Other Components not Requiring or generating Resources is primarily attributable to the procedural accounting changes for 4th Quarter, FY 2005 based on the DTRA receiving a waiver from elimination adjustments in the 3rd Quarter, FY 2004. The required elimination adjustments prior to DTRA receiving the waiver from elimination adjustments in the 3rd Quarter, FY 2004 created budgetary accounts that impacted the Statement of Financing (SOF) for FY 2005. Therefore, a one-time adjustment was necessary to bring the SOF into agreement with the Statement of Net Cost for 4th Quarter, FY 2005.

Note Reference

Note 1.A, Note 1.F.

Note 17.	Other

Other Disclosures

The Defense Threat Reduction Agency (DTRA) reports the following military labor costs for 4th Quarter, FY 2005:

Military Labor Costs (in thousands):		
Salaries	$	36,330
Benefits		34,205
Total	**$**	**70,535**
Total Military Assigned:		
Officers		377
Enlisted		257
Total		**634**

TAB D

SUPPORTING CONSOLIDATING/COMBINING STATEMENTS

Department of Defense
Defense Threat Reduction Agency
CONSOLIDATING BALANCE SHEET
As of September 30, 2005 and 2004
(Amounts In Thousands)

	Defense Threat Reduction Agency	Defense Technology Security Administration	On Site Inspection Agency	Defense Special Weapons Agency
ASSETS (Note 2)				
Intragovernmental:				
Fund Balance with Treasury (Note 3)	$ 1,788,401	$ 0	$ 0	$ 45,438
Accounts Receivable (Note 4)	1,931	-	0	0
Total Intragovernmental Assets	1,790,332	0	0	45,438
Accounts Receivable (Note 4)	644	-	-	-
Inventory and Related Property (Note 5)	25,708	-	0	0
General Property, Plant and Equipment (Note 6)	121,041	-	-	-
TOTAL ASSETS	$ 1,937,724	$ 0	$ 0	$ 45,438

The accompanying notes are an integral part of these statements.

Department of Defense
Defense Threat Reduction Agency
CONSOLIDATING BALANCE SHEET
As of September 30, 2005 and 2004
(Amounts In Thousands)

	Combined Total	Eliminations	2005 Consolidated	2004 Consolidated
ASSETS (Note 2)				
Intragovernmental:				
Fund Balance with Treasury (Note 3)	$ 1,833,839	$ -	$ 1,833,839	$ 2,042,532
Accounts Receivable (Note 4)	1,931	-	1,931	6,756
Total Intragovernmental Assets	1,835,770	-	1,835,770	2,049,288
Accounts Receivable (Note 4)	644	-	644	0
Inventory and Related Property (Note 5)	25,708	-	25,708	97,140
General Property, Plant and Equipment (Note 6)	121,041	-	121,041	97,140
TOTAL ASSETS	$ 1,983,163	$ -	$ 1,983,163	$ 2,146,428

The accompanying notes are an integral part of these statements.

Department of Defense
Defense Threat Reduction Agency
CONSOLIDATING BALANCE SHEET
As of September 30, 2005 and 2004
(Amounts In Thousands)

	Defense Threat Reduction Agency	Defense Technology Security Administration	On Site Inspection Agency	Defense Special Weapons Agency
LIABILITIES (Note 7)				
Intragovernmental:				
Accounts Payable (Note 8)	$ 125	$ -	$ -	$ 8
Other Liabilities (Note 7 and Note 10)	1,636	-	-	0
Total Intragovernmental Liabilities	1,760	-	-	8
Accounts Payable (Note 8)	65,236	-	-	1,782
Military Retirement Benefits and Other Employment-Related Actuarial Liabilities (Note 12)	2,007	-	-	-
Environmental Liabilities (Note 9)	61,043	-	-	-
Other Liabilities (Note 7 and Note 10)	11,698	-	-	-
TOTAL LIABILITIES	141,744	-	-	1,790
NET POSITION				
Unexpended Appropriations	1,548,255	-	-	209,653
Cumulative Results of Operations	247,725	-	-	(166,005)
TOTAL NET POSITION	1,795,981	-	-	43,648
TOTAL LIABILITIES AND NET POSITION	$ 1,937,724	$ -	$ -	$ 45,438

The accompanying notes are an integral part of these statements.

Department of Defense
Defense Threat Reduction Agency
CONSOLIDATING BALANCE SHEET
As of September 30, 2005 and 2004
(Amounts In Thousands)

	Combined Total	Eliminations	2005 Consolidated	2004 Consolidated
LIABILITIES (Note 11)				
Intragovernmental:				
Accounts Payable (Note 8)	$ 132	$ -	$ 132	$ 622
Other Liabilities (Note 7 and Note 10)	1,636	-	1,636	2,224
Total Intragovernmental Liabilities	1,768	-	1,768	2,846
Accounts Payable (Note 8)	67,018	-	67,018	49,637
Military Retirement Benefits and Other	2,007	-	2,007	2,040
Employment-Related Actuarial Liabilities (Note 12)				
Environmental Liabilities (Note 9)	61,043	-	61,043	71,508
Other Liabilities (Note 7 and Note 10)	11,698	-	11,698	12,065
TOTAL LIABILITIES	143,534	-	143,534	138,096
NET POSITION				
Unexpended Appropriations	1,757,908	-	1,757,908	2,005,345
Cumulative Results of Operations	81,721	-	81,721	2,987
TOTAL NET POSITION	1,839,629	-	1,839,629	2,008,332
TOTAL LIABILITIES AND NET POSITION	$ 1,983,163	$ -	$ 1,983,163	$ 2,146,428

The accompanying notes are an integral part of these statements.

Department of Defense
Defense Threat Reduction Agency
CONSOLIDATING STATEMENT OF NET COST
For the periods ended September 30, 2005 and 2004
(Amounts In Thousands)

	Combined Total	Eliminations	2005 Consolidated	2004 Consolidated
Program Costs				
Defense Special Weapons Agency				
Intragovernmental Gross Costs	$ 1,109	$ -	$ 1,109	$ -
(Less: Intragovernmental Earned Revenue)	0	-	0	(98)
Intragovernmental Net Costs	1,109	-	1,109	(98)
Gross Costs With the Public	5,672	-	5,672	11,076
(Less: Earned Revenue From the Public)	0	-	0	226
Net Costs With the Public	5,672	-	5,672	11,302
Total Net Cost	6,781	-	6,781	11,204
Defense Technology Security Administration				
Intragovernmental Gross Costs	-	-	-	-
(Less: Intragovernmental Earned Revenue)	-	-	-	-
Intragovernmental Net Costs	-	-	-	-
Gross Costs With the Public	-	-	-	-
(Less: Earned Revenue From the Public)	-	-	-	-
Net Costs With the Public	-	-	-	-
Total Net Cost	$ -	$ -	$ -	$ -

The accompanying notes are an integral part of these statements.

Department of Defense
Defense Threat Reduction Agency
CONSOLIDATING STATEMENT OF NET COST
For the periods ended September 30, 2005 and 2004
(Amounts In Thousands)

	Combined Total	Eliminations	2005 Consolidated	2004 Consolidated
Defense Threat Reduction Agency				
Intragovernmental Gross Costs	$ 482,421	$ -	$ 482,421	$ 94,075
(Less: Intragovernmental Earned Revenue)	(18,645)	-	(18,642)	(23,476)
Intragovernmental Net Costs	463,776	-	463,776	70,599
Gross Costs With the Public	916,325	-	916,325	1,290,602
(Less: Earned Revenue From the Public)	0	-	-	-
Net Costs With the Public	916,325	-	916,325	1,290,741
Total Net Cost	1,380,101	-	1,380,101	1,361,340
On Site Inspection Agency				
Intragovernmental Gross Costs	-	-	-	17
(Less: Intragovernmental Earned Revenue)	-	-	-	-
Intragovernmental Net Costs	-	-	-	17
Gross Costs With the Public	208	-	208	115
(Less: Earned Revenue From the Public)	-	-	-	-
Net Costs With the Public	208	-	208	115
Total Net Cost	$ 208	$ -	$ 208	$ 132

The accompanying notes are an integral part of these statements.

Department of Defense
Defense Threat Reduction Agency
CONSOLIDATING STATEMENT OF NET COST
For the periods ended September 30, 2005 and 2004
(Amounts In Thousands)

	Combined Total	Eliminations	2005 Consolidated	2004 Consolidated
Total Program Costs				
Intragovernmental Gross Costs	$ 483,530	$ -	$ 483,530	$ 94,092
(Less: Intragovernmental Earned Revenue)	(18,645)	-	(18,645)	(23,574)
Intragovernmental Net Costs	464,886	-	464,886	70,518
Gross Costs With the Public	922,205	-	922,205	1,301,793
(Less: Earned Revenue From the Public)	0	-	0	365
Net Costs With the Public	922,205	-	922,205	1,302,158
Total Net Cost	1,387,091	-	1,387,091	1,372,676
Cost Not Assigned to Programs	-	-	-	-
(Less:Earned Revenue Not Attributable to Programs)	-	-	-	-
Net Cost of Operations	$ 1,387,091	$ -	$ 1,387,091	$ 1,372,676

The accompanying notes are an integral part of these statements.

Department of Defense
Defense Threat Reduction Agency
CONSOLIDATING STATEMENT OF CHANGES IN NET POSITION
For the periods ended September 30, 2005 and 2004
(Amounts In Thousands)

	Defense Threat Reduction Agency	Defense Technology Security Administration	On Site Inspection Agency	Defense Special Weapons Agency
CUMULATIVE RESULTS OF OPERATIONS				
Beginning Balances	$ 4,088	$ -	$ 218	$ (1,318)
Prior period adjustments (+/-)	-	-	-	-
Beginning Balances, as adjusted	4,088	-	218	(1,318)
Budgetary Financing Sources:				
Appropriations used	1,338,039	-	(10)	8,073
Other budgetary financing sources (+/-)	0	-	0	0
Other Financing Sources:				
Imputed financing from costs absorbed by others	76,716	-	-	-
Other	208,984	-	-	(165,978)
Total Financing Sources	1,623,739	-	(10)	(157,906)
Net Cost of Operations (+/-)	1,380,101	-	208	6,781
Ending Balances	$ 247,725	$ -	$ 0	$ (166,005)

The accompanying notes are an integral part of these statements.

Department of Defense
Defense Threat Reduction Agency
CONSOLIDATING STATEMENT OF CHANGES IN NET POSITION
For the periods ended September 30, 2005 and 2004
(Amounts In Thousands)

	Combined Total	Eliminations	2005 Consolidated	2004 Consolidated
CUMULATIVE RESULTS OF OPERATIONS				
Beginning Balances	$ 2,988	$ -	$ 2,988	$ 27,066
Prior period adjustments (+/-)	-	-	-	-
Beginning Balances, as adjusted	2,988	-	2,988	27,066
Budgetary Financing Sources:				
Appropriations used	1,346,102	-	1,346,102	1,272,119
Other budgetary financing sources (+/-)	-	-	-	(1,460)
Other Financing Sources:				
Imputed financing from costs absorbed by others	76,716	-	76,716	77,938
Other	43,006	-	43,006	-
Total Financing Sources	1,465,823	-	1,465,823	1,348,597
Net Cost of Operations (+/-)	1,387,091	-	1,387,091	1,372,676
Ending Balances	$ 81,721	$ -	$ 81,721	$ 2,987

The accompanying notes are an integral part of these statements.

Department of Defense
Defense Threat Reduction Agency
CONSOLIDATING STATEMENT OF CHANGES IN NET POSITION
For the periods ended September 30, 2005 and 2004
(Amounts In Thousands)

	Defense Threat Reduction Agency	Defense Technology Security Administration	On Site Inspection Agency	Defense Special Weapons Agency
UNEXPENDED APPROPRIATIONS				
Beginning Balances	$ 1,778,517	$ 3	$ (5)	$ 226,830
Prior period adjustments (+/-)	-	-	-	-
Beginning Balances, as adjusted	1,778,517	3	(5)	226,830
Budgetary Financing Sources:				
Appropriations received	1,204,844	-	-	-
Appropriations transferred-in/out (+/-)	(5,130)	-	-	-
Other adjustments (rescissions, etc) (+/-)	(91,937)	(3)	(5)	(9,104)
Appropriations used	(1,338,039)	-	10	(8,073)
Other Financing Sources				
Total Financing Sources	(230,261)	(3)	5	(17,177)
Net Cost of Operations (+/-)				
Ending Balances	$ 1,548,255	$ -	$ -	$ 209,653

The accompanying notes are an integral part of these statements.

Department of Defense
Defense Threat Reduction Agency
CONSOLIDATING STATEMENT OF CHANGES IN NET POSITION
For the periods ended September 30, 2005 and 2004
(Amounts In Thousands)

	Combined Total	Eliminations	2005 Consolidated	2004 Consolidated
UNEXPENDED APPROPRIATIONS				
Beginning Balances	$ 2,005,345	$ -	$ 2,005,345	$ 2,060,249
Prior period adjustments (+/-)				
Beginning Balances, as adjusted	2,005,345	-	2,005,345	2,060,249
Budgetary Financing Sources:				
Appropriations received	1,204,844	-	1,204,844	1,244,349
Appropriations transferred-in/out (+/-)	(5,130)	-	(5,130)	(10,508)
Other adjustments (rescissions, etc) (+/-)	(101,049)	-	(101,049)	(16,626)
Appropriations used	(1,346,102)	-	(1,346,102)	(1,272,119)
Other Financing Sources				
Total Financing Sources	(247,437)	-	(247,347)	(54,904)
Net Cost of Operations (+/-)				
Ending Balances	$ 1,757,908	$ -	$ 1,757,908	$ 2,005,345

The accompanying notes are an integral part of these statements.

Department of Defense
Defense Threat Reduction Agency
COMBINING STATEMENT OF BUDGETARY RESOURCES
For the periods ended September 30, 2005 and 2004
(Amounts In Thousands)

	Defense Threat Reduction Agency	Defense Technology Security Administration	On Site Inspection Agency	Defense Special Weapons Agency
BUDGETARY FINANCING ACCOUNTS				
BUDGETARY RESOURCES				
Budget Authority:				
Appropriations received	$ 1,204,844	$ -	$ -	$ -
Net transfers (+/-)	(974)	-	-	-
Unobligated balance:				
Beginning of period	429,844	3	5	35,950
Net transfers, actual (+/-)	(4,156)	-	-	-
Spending authority from offsetting collections:				
Collected	55,301	-	-	0
Receivable from Federal sources	(35,812)	-	-	0
Change in unfilled customer orders	-	-	-	-
Advance received	(2,441)	-	-	-
Without advance from Federal sources	(7,158)	-	-	(79)
Subtotal	9,890	-	-	(79)
Recoveries of prior year obligations	100,892	-	11	13,147
Permanently not available	(91,937)	(3)	(5)	(9,104)
Total Budgetary Resources	$ 1,648,403	$ -	$ 11	$ 39,913

The accompanying notes are an integral part of these statements.

Department of Defense

Defense Threat Reduction Agency
COMBINING STATEMENT OF BUDGETARY RESOURCES
For the periods ended September 30, 2005 and 2004
(Amounts In Thousands)

	2005 Combined	2004 Combined
BUDGETARY FINANCING ACCOUNTS		
BUDGETARY RESOURCES		
Budget Authority:		
Appropriations received	$ 1,204,844	$ 1,244,349
Net transfers (+/-)	(974)	(10,208)
Unobligated balance:		
Beginning of period	465,810	637,337
Net transfers, actual (+/-)	(4,156)	(300)
Spending authority from offsetting collections:		
Collected	55,301	39,742
Receivable from Federal sources	(35,812)	(16,533)
Change in unfilled customer orders	-	-
Advance received	(2,441)	(2,214)
Without advance from Federal sources	(7,237)	(7,576)
Subtotal	9,811	13,419
Recoveries of prior year obligations	114,050	72,645
Permanently not available	(101,049)	(16,522)
Total Budgetary Resources	$ 1,688,327	$ 1,940,720

The accompanying notes are an integral part of these statements.

Department of Defense

Defense Threat Reduction Agency

COMBINING STATEMENT OF BUDGETARY RESOURCES

For the periods ended September 30, 2005 and 2004

(Amounts In Thousands)

STATUS OF BUDGETARY RESOURCES	Defense Threat Reduction Agency	Defense Technology Security Administration	On Site Inspection Agency	Defense Special Weapons Agency
Obligations incurred:				
Direct	$ 1,401,233	$ -	$ 11	$ 10,122
Reimbursable	14,568	-	-	-
Subtotal	1,415,801	-	11	10,122
Unobligated balance:				
Apportioned	205,970	-	-	29,791
Other available	-	-	-	-
Unobligated Balances Not Available	26,632	-	-	-
Total, Status of Budgetary Resources	1,648,403	-	11	39,913
Relationship of Obligations to Outlays:				
Obligated Balance, Net - beginning of period	1,387,027	-	-	190,889
Obligated Balance, Net - end of period:				
Accounts receivable	(3,696)	-	-	-
Unfilled customer order from Federal sources	(22,619)	-	-	-
Undelivered orders	1,345,409	-	-	179,862
Accounts payable	71,360	-	-	1,764
Outlays:				
Disbursements	1,354,452	-	-	6,317
Collections	(52,860)	-	-	-
Subtotal	1,301,592	-	-	6,317
Net Outlays	$ 1,301,592	$ -	$ -	$ 6,317

The accompanying notes are an integral part of these statements.

Department of Defense
Defense Threat Reduction Agency
COMBINING STATEMENT OF BUDGETARY RESOURCES
For the periods ended September 30, 2005 and 2004
(Amounts In Thousands)

	2005 Combined	2004 Combined
STATUS OF BUDGETARY RESOURCES		
Obligations incurred:		
Direct	$ 1,411,366	$ 1,460,439
Reimbursable	14,568	14,480
Subtotal	1,425,934	1,474,919
Unobligated balance:		
Apportioned	235,761	388,669
Other available	-	-
Unobligated Balances Not Available	26,632	77,131
Total, Status of Budgetary Resources	1,688,327	1,940,720
Relationship of Obligations to Outlays:		
Obligated Balance, Net - beginning of period	1,577,916	1,436,816
Obligated Balance, Net - end of period:		
Accounts receivable	(3,696)	(39,508)
Unfilled customer order from Federal sources	(22,619)	(29,856)
Undelivered orders	1,525,272	1,576,186
Accounts payable	73,124	71,095
Outlays:		
Disbursements	1,360,769	1,285,283
Collections	(52,860)	(37,529)
Subtotal	1,307,909	1,247,754
Net Outlays	$ 1,307,909	$ 1,247,754

The accompanying notes are an integral part of these statements.

Department of Defense
Defense Threat Reduction Agency
COMBINING STATEMENT OF FINANCING
For the periods ended September 30, 2005 and 2004
(Amounts In Thousands)

	Defense Threat Reduction Agency	Defense Technology Security Administration	On Site Inspection Agency	Defense Special Weapons Agency
Resources Used to Finance Activities:				
Budgetary Resources Obligated				
Obligations incurred	$ 1,415,801	$ -	$ 11	$ 10,122
Less: Spending authority from offsetting collections and recoveries (-)	(110,782)	-	(11)	(13,068)
Obligations net of offsetting collections and recoveries	1,305,019	-	-	(2,946)
Net obligations	1,305,019	-	-	(2,946)
Other Resources				
Imputed financing from costs absorbed by others	76,716	-	-	-
Others	208,984	-	-	(165,978)
Net other resources used to finance activities	285,700	-	-	(165,978)
Total resources used to finance activities	1,590,719	-	-	(168,924)

The accompanying notes are an integral part of these statements.

Department of Defense
Defense Threat Reduction Agency
COMBINING STATEMENT OF FINANCING
For the periods ended September 30, 2005 and 2004
(Amounts In Thousands)

	2005 Combined	2004 Combined
Resources Used to Finance Activities:		
Budgetary Resources Obligated		
Obligations incurred	$ 1,425,934	$ 1,474,919
Less: Spending authority from offsetting collections and recoveries (-)	(123,861)	(86,064)
Obligations net of offsetting collections and recoveries	1,302,073	1,388,855
Net obligations	1,302,073	1,388,855
Other Resources		
Imputed financing from costs absorbed by others	76,716	77,938
Others	43,006	-
Net other resources used to finance activities	119,722	77,938
Total resources used to finance activities	1,421,795	1,466,793

The accompanying notes are an integral part of these statements.

Department of Defense
Defense Threat Reduction Agency
COMBINING STATEMENT OF FINANCING
For the periods ended September 30, 2005 and 2004
(Amounts In Thousands)

	Defense Threat Reduction Agency	Defense Technology Security Administration	On Site Inspection Agency	Defense Special Weapons Agency
Resources Used to Finance Items not Part of the Net Cost of Operations				
Change in budgetary resources obligated for goods, services and benefits ordered but not yet provided				
Undelivered Orders (-)	39,698	-	(10)	11,227
Unfilled Customer Orders	(9,599)	-	-	(79)
Resources that fund expenses recognized in prior periods do not affect net cost of operations	(11,174)	-	-	-
Resources that finance the acquisition of assets	(38,244)	-	-	
Other resources or adjustments to net obligated resources that do not affect net cost of operations	(208,984)	-	-	165,978
Total resources used to finance items not part of the net cost of operations	(228,304)	-	(10)	177,126
Total resources used to finance the net cost of operations	1,362,415	-	(10)	8,202

The accompanying notes are an integral part of these statements.

Department of Defense
Defense Threat Reduction Agency
COMBINING STATEMENT OF FINANCING
For the periods ended September 30, 2005 and 2004
(Amounts In Thousands)

	2005 Combined	2004 Combined
Resources Used to Finance Items not Part of the Net Cost of Operations		
Change in budgetary resources obligated for goods, services and benefits ordered but not yet provided		
Undelivered Orders (-)	50,905	(112,096)
Unfilled Customer Orders	(9,678)	(9,760)
Resources that fund expenses recognized in prior periods do not affect net cost of operations	(11,174)	(2,202)
Resources that finance the acquisition of assets	(38,244)	(46,118)
Other resources or adjustments to net obligated resources that do not affect net cost of operations	(43,006)	-
Total resources used to finance items not part of the net cost of operations	(51,188)	(170,206)
Total resources used to finance the net cost of operations	1,370,607	1,296,587

The accompanying notes are an integral part of these statements.

Department of Defense
Defense Threat Reduction Agency
COMBINING STATEMENT OF FINANCING
For the periods ended September 30, 2005 and 2004
(Amounts In Thousands)

	Defense Threat Reduction Agency	Defense Technology Security Administration	On Site Inspection Agency	Defense Special Weapons Agency
Components of the Net Cost of Operations that will not Require or Generate Resources in the Current Period:				
Components Requiring or Generating Resources in Future Period:				
Increase in annual leave liability	965	-	-	-
Increase in environmental and disposal liability	-	-	-	-
Other (+/-)	504	-	-	141
Total components of Net Cost of Operations that will require or generate resources in future periods	1,469	-	-	141
Components not Requiring or Generating Resources:				
Depreciation and amortization	2,895	-	220	4
Revaluation of assets or liabilities (+/-)	-	-	-	-
Other (+/-)	13,321	-	(2)	(1,566)
Total components of Net Cost of Operations that will not require or generate resources	16,216	-	218	(1,562)
Total components of net cost of operations that will not require or generate resources in the current period	17,686	-	218	(1,420)
Net Cost of Operations	1,380,101	-	208	6,781

The accompanying notes are an integral part of these statements.

Department of Defense
Defense Threat Reduction Agency
COMBINING STATEMENT OF FINANCING
For the periods ended September 30, 2005 and 2004
(Amounts In Thousands)

	2005 Combined	2004 Combined
Components of the Net Cost of Operations that will not Require or Generate Resources in the Current Period:		
Components Requiring or Generating Resources in Future Period:		
Increase in annual leave liability	965	7,161
Increase in environmental and disposal liability	-	65,977
Other (+/-)	645	87
Total components of Net Cost of Operations that will require or generate resources in future periods	1,611	73,225
Components not Requiring or Generating Resources:		
Depreciation and amortization	3,119	2,840
Revaluation of assets or liabilities (+/-)	-	-
Other (+/-)	11,753	24
Total components of Net Cost of Operations that will not require or generate resources	14,873	2,864
Total components of net cost of operations that will not require or generate resources in the current period	16,483	76,089
Net Cost of Operations	1,387,091	1,372,676

The accompanying notes are an integral part of these statements.

TAB E

REQUIRED SUPPLEMENTAL STEWARDSHIP INFORMATION

Investments In Research and Development

Yearly Investment in Research and Development
For Fiscal Years (Preceding 4th Fiscal Year) through FY2004
(In Millions of Dollars)

(a) Categories	(b) FY01	© FY02	(d) FY03	(e) FY04	(f) FY05
1. Basic Research	0.000	0.000	0.000	0.000	0.000
2. Applied Research	4.212	58.452	182.453	91.738	288.316
3. Development					
Advanced Technology Development	2.202	33.656	74.895	17.354	113.462
Demonstration and Validation	0.000	0.000	0.000	0.000	0.000
Engineering and Manufacturing Development	0.000	0.000	0.000	0.000	0.000
Research, Development, Test and Evaluation	0.000	0.316	3.770	1.608	1.727
Management Support	0.000	0.000	0.000	0.000	0.000
Operational Systems Development					
Total	**6.414**	**92.424**	**261.118**	**110.700**	**403.505**

Narrative Statement

See attached.

Applied Research examples:

Outcomes from the applied research are:

Radiation Hardened Microelectronics: DTRA developed and demonstrated several radiation hardened prototype technologies. These technologies provide radiation hardening for up to 0.25 microns and initiated development of hardening for 0.15 micron technology.

Consequence Assessment: DTRA developed a atmospheric hazard prediction model to estimate the effects from CBRN events. The Hazard Prediction and Assessment Capability (HPAC) code now models incidents involving industrial facilities and transportation assets. This capability allows for the full range of CBRN assessment. Additionally, the code now has a full urban transport and dispersion capability that accounts for the uniqueness found within a city. The urban capability was used operationally during the 2004 Athens Summer Olympics and the Democratic and Republican National Conventions.

Integrated Munitions Effects. DTRA developed a target-attack planning tool for existing theater-level planning capabilities to defeating or denying a wide variety of facilities and capabilities. This planning tool, the Integrated Munitions Effects Assessment (IMEA), integrates collateral effects predictive tools, Hazard Prediction and Assessment Capability (HPAC), for a variety of applications supporting Nuclear, Biological and Chemical (NBC) target attack planning to include NBC expulsion and dispersion resulting from attacks on WMD facilities as well as acts of terrorism and hostile use of WMD to provide targeting solutions using conventional weapons for a variety of structures and equipment. It includes a high-resolution weather prediction capability that provides timely data necessary for more detailed predictions. Upgrades to the initial IMEA capability include additional target types (including complex facilities), multiple weapon effects, additional platforms, more operator-friendly displays, more WMD material types, weather interfaces and sources, and more detailed weapon input parameters (such as angle of attack).

Hard Target Defeat: DTRA developed tunnel and hard target attack technologies. These technologies include development and testing of advanced energetic materials as well as employment tactics. New explosive mixtures in penetrating warheads optimized for use against tunnels and chemical and biological targets and non-energetic warhead fills were developed. DTRA investigated fundamental properties of thermobarics and continued development of high fidelity computational fluid dynamics models for their performance and lethality. Mission critical equipment and vulnerabilities for WMD production tunnel facilities were identified. Defeat technologies to model and predict the extent of multiple weapons penetration, tunnel damage, and advanced weapon performance were developed. DTRA developed tunnel aim point optimization models to increase the effectiveness of the planning tools developed for warfighter planners and improved weapon/target interaction models of tunnels and liners to nuclear ground shock environments. DTRA completed construction of tunnel portals and tunnel at the White Sands Missile Range and, using newly developed tactics, techniques, and procedures (TTPs), conducted operational tunnel defeat demonstrations against the tunnel portals using inventory and new standoff weapons. DTRA conducted demonstration of a massive ordnance bomb against a tunnel facility at Nevada Test Site.

Special Projects: DTRA developed underground target characterization technologies to enable the Combatant Commands and Intelligence Community (IC) to find, characterize and assess tunnels and hard targets. DTRA developed and validated a remote site geology characterization process. DTRA incorporated initial nuclear and conventional weapons effects analysis and initial network analysis functionality into the Underground Target Analysis System (UTAS) software and used the tool to support targeting and IC by conducting assessments of hostile facilities based on JCS and Combatant Commanders' priorities. Characterizations of targets include three-dimensional target models. DTRA analyzed Operation Iraqi Freedom Bomb Damage Assessment (BDA) data for ground truth comparison to characterizations and assessments delivered during operations. DTRA completed a functional defeat operational demonstration on the Command, Control, Communications, and Intelligence (C3I) tunnel complex at the Nevada Test Site.

Development examples:

Four outcomes from the development and application of Weapons of Mass Destruction (WMD) Defeat Technologies to meet Counterproliferation and special weapon effects challenges are:

Second Counterproliferation (CP2) Advanced Concept Technology Demonstration (ACTD): CP2 ACTD developed and demonstrated standoff attack capabilities against WMD facilities. Final operational demonstrations and military utility assessments for the Tactical Tomahawk Penetrator Variant and Chemical Combat Assessment System have been completed. Residual components will undergo an extended user evaluation through the first quarter of calendar year 2006.

Agent Defeat, Deny, Disrupt (AD3) Program: Development and demonstration of an improved capability to hold weapons of mass destruction (WMD) targets at risk using advanced technology to defeat chemical/biological (CB) agents, deny the adversary access to agent material/facilities, and disrupt the adversary's agent-related processes. Successfully designed and conducted reduced-scale tests to characterize biological plumes and improve test and measurement techniques. Analyzed potential high explosive (HE) /incendiary fills, bomb designs, and loading weights to attain design goal of at least 2-log reduction in collateral damage than current HE fills.

Improvised Explosive Device (IED): DTRA established an IED Cell to focus on developing solutions and integrating technologies to fill gaps in IED defeat, and to avoid duplication in materiel solutions. Members interface with Services, deployed/ deploying units, Combatant Commanders and Joint Staff. DTRA delivered IED technologies (equipment) includes blast and fragmentation protective equipment, IR spotting scopes, digital cameras, robot kits, IED exploitation equipment, laser range finders, cordless spot lights, thermal imaging scopes and Z Backscatter vans.

Special Operations Forces (SOF) Support: Development and demonstration of various technologies resulted in the improved ability to provide warfighting capabilities to the Special Operations Forces (SOF) to defeat WMD. Successfully completed the Boundary Step Advanced Concept Technology Demonstration (ACTD); fourteen of the sixteen technologies were accepted by USSOCOM, the user/sponsor. The military utility assessments are continuing.

TAB F

REQUIRED SUPPLEMENTAL INFORMATION

Department of Defense
Defense Threat Reduction Agency
As of September 30, 2005
(Amounts In Thousands)

DoD Intra-governmental Asset Balances	**Treasury Index:**	**Fund Balance with Treasury**	**Accounts Receivable**
Department of Commerce	13		$ 58
Navy General Fund	17		14
Department of State	19		133
Department of the Treasury	20	1,833,839	
Army General Fund	21		1
Air Force General Fund	57		1,186
National Aeronautics and Space Administration	80		152
Other Defense Organizations General Funds	97		341
Navy Working Capital Fund	97-4930.002		47
Totals		**$ 1,833,839**	**$ 1,932**

Department of Defense
Defense Threat Reduction Agency
As of September 30, 2005
(Amounts In Thousands)

DoD Intra-governmental entity liabilities	**Treasury Index:**	**Accounts Payable**	**Other**
Department of Labor	16		958
Navy General Fund	17	2	
Department of State	19		83
Army General Fund	21	26	
Office of Personnel Management	24		507
General Service Administration	47	2	
Air Force General Fund	57	3	91
Department of Energy	89	25	
Other Defense Organizations General Funds	97		26
Other Defense Organizations Working Capital Funds	97-4930	74	
The General Fund of the Treasury	99		(29)
Totals		**$ 132**	**$ 1,636**

Department of Defense
Defense Threat Reduction Agency
As of September 30, 2004
(Amounts In Thousands)

DoD Intra-governmental revenue and related costs	Treasury Index:	Earned Revenue
Department of Agriculture	12	$ 2
Department of Commerce	13	1,359
Department of Interior	14	25
Navy General Fund	17	209
Department of State	19	786
Army General Fund	21	48
General Accounting Office	5	147
Central Intelligence Agency	56	64
Air Force General Fund	57	10,931
Homeland Security	70	243
Department of Health and Human Services	75	1
National Aeronautics and Space Administration	80	769
Department of Energy	89	225
Other Defense Organizations General Funds	97	3,420
Other Defense Organizations Working Capital Funds	97-4930	1
Navy Working Capital Fund	97-4930.002	415
Totals		**18,645**

TAB G

AUDIT OPINION

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INDEPENDENT AUDITOR'S REPORT

To the Director, Defense Threat Reduction Agency:

We have audited the Defense Threat Reduction Agency's (DTRA) Consolidated Balance Sheet, Consolidated Statement of Net Cost, Consolidated Statement of Changes in Net Position, Combined Statement of Budgetary Resources and Combined Statement of Financing (Principal Financial Statements) as of, and for the years ended, September 30, 2005 and 2004; we have examined internal control over financial reporting in place as of September 30, 2005; and we have examined compliance with laws and regulations.

In our opinion, DTRA's 2005 and 2004 Principal Financial Statements are presented fairly in all material respects.

We found:

- no material conflicts with DTRA's 2005 report on management controls prepared under the Federal Managers' Financial Integrity Act of 1982 (FMFIA),
- matters related to internal control over financial reporting that we considered to be material weaknesses and reportable conditions, and
- instances of noncompliance with selected provisions of applicable laws and regulations.

Each of these conclusions is discussed in more detail below. This report also discusses the scope of our work.

PRINCIPAL FINANCIAL STATEMENTS

In our opinion, DTRA's 2005 and 2004 Principal Financial Statements, including the notes thereto, present fairly, in all material respects, DTRA's financial position as of September 30, 2005 and 2004, and the net cost of operations, the changes in net position, the use of budgetary resources, and the use of financing resources for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

INTERNAL CONTROL

We considered DTRA's internal control in order to determine our auditing procedures for the purpose of expressing our opinion on the Principal Financial Statements. Since DTRA's financial recording and reporting, including the issuance of financial statements, are performed to a significant extent by the Defense Finance and Accounting Service (DFAS), our consideration of internal control included those aspects of internal control of DFAS which were relevant to DTRA. We limited our internal control testing to those controls necessary to achieve the objectives described in the Office of Management and Budget's (OMB) Bulletin 01-02, *Audit Requirements for Federal Financial Statements*. We did not test all internal controls relevant to operating objectives as broadly defined by the FMFIA, such as those controls relevant to assuring efficient operations. The objective of our audit was not to provide assurance on internal control. Consequently, we do not provide an opinion on internal control.

The objectives of internal control are to provide management with reasonable, but not absolute, assurance that the following objectives are met:

- transactions are properly recorded and accounted for to permit the preparation of reliable financial reports and to maintain accountability over assets;

- funds, property, and other assets are safeguarded against loss from unauthorized acquisition, use, or disposition;

- transactions, including those related to obligations and costs, are executed in compliance with laws and regulations that could have a direct and material effect on the financial statements and other laws and regulations that the Office of Management and Budget (OMB), Department of Defense (DoD) management, or the Inspector General have identified as being significant and for which compliance can be objectively measured and evaluated; and

- data that support reported performance measures are properly recorded and accounted for to permit preparation of reliable and complete performance information.

Our consideration of the internal control over financial reporting would not necessarily disclose all matters of internal control over financial reporting that might be reportable conditions. Under standards issued by the American Institute of Certified Public Accountants, reportable conditions are matters coming to our attention relating to significant deficiencies in the design or operation of internal control that, in our judgement, could adversely affect DTRA's or DFAS' ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. Material weaknesses are reportable conditions in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that errors or irregularities in amounts, which would be material in relation to the financial statements being audited or material to a performance measure or aggregation of related performance measures, may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

We noted several matters that we considered to be material weaknesses, as defined above, involving DFAS' internal control, as it relates to processing financial data for DTRA, as follows:

- significant elements of the financial statements including, but not limited to, Fund Balance with Treasury, Accounts Payable, and Property, Plant and Equipment are developed from sources other than the general ledger; and

- entries are processed to force financial data to agree with various data sources.

We noted one matter that we considered to be a reportable condition, as defined above, involving DTRA's internal control, as follows:

- DTRA does not have contingency plans for its Centralized Accounting and Financial Resource Management System (CAFRMS), which is housed at DTRA's Telegraph Road facility, or for the feeder systems on its local area network, which is housed in DTRA's Fort Belvoir facility.

The above reportable condition was cited in our audits of the 2003 and 2004 Principal Financial Statements.

We noted certain other issues related to internal control as implemented by DTRA that we have communicated to DTRA's management in a separate letter dated November 8, 2005.

COMPLIANCE WITH LAWS AND REGULATIONS

DTRA's management is responsible for complying with laws and regulations applicable to its operations. As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we performed tests of DTRA's compliance with certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of financial statement amounts, and certain other laws and regulations specified in OMB Bulletin 01-02, *Audit Requirements for Federal Financial Statements*, including the requirements referred to in the Federal Financial Management Improvement Act (FFMIA) of 1996. Since DTRA's financial recording and reporting, including the issuance of financial statements, are performed by DFAS, we considered compliance with laws and regulations by DFAS that were relevant to DTRA. We limited our tests to these provisions, and we did not test compliance with all laws and regulations applicable to DTRA. The objective of our audit of the Principal Financial Statements, including our tests of compliance with selected provisions of applicable laws and regulations, was not to provide an opinion on overall compliance with such provisions. Accordingly, we do not express such an opinion.

Reportable instances of noncompliance are failures to follow requirements, or violations of prohibitions in statutes and regulations, that cause us to conclude that the aggregation of the misstatements resulting from those failures or violations is material to the financial statements or that sensitivity warrants disclosure thereof.

The inadequacies of DFAS' internal control over financial reporting are a failure to comply with:

- the Budget and Accounting Procedures Act of 1950, which requires an accounting system that provides full disclosure of the results of financial operations, adequate financial information needed in the management of operations and formulation and execution of the budget, and effective control over income, expenditures, funds, property, and other assets;

- the Federal Managers' Financial Integrity Act of 1982, which requires implementation of internal accounting and administrative controls that provide reasonable assurance that (1) obligations and costs are in compliance with applicable laws, (2) funds, property, and other assets are safeguarded against waste, loss, unauthorized use, or misappropriation, and (3) revenues and expenditures applicable to agency operations are properly recorded and accounted for to permit the preparation of accounts and reliable financial and statistical reports to maintain accountability over the assets;

- the Chief Financial Officers Act of 1990, which requires the development and maintenance of an integrated accounting and financial management system that (1) complies with applicable accounting principles, standards and requirements, and internal control standards, (2) complies with such policies and requirements as may be prescribed by the Director, OMB, (3) complies with any other requirements applicable to such systems, and (4) provides for (i) complete, reliable, consistent, and timely information that is prepared on a uniform basis and that is responsive to the financial information needs of management, (ii) the development and reporting of cost information, (iii) the integration of accounting and budgeting information, and, (iv) the systematic measurement of performance; and

- OMB Circular A-127, *Financial Management Systems*, which requires agencies to establish and maintain an accounting system that provides for (1) complete disclosure of the financial results of the activities of the agency, (2) adequate financial information for agency management and for formulation and execution of the budget, and (3) effective control over revenue, expenditures, funds, property, and other assets.

In addition, the DoD OIG has identified the following reportable noncompliances with laws and regulations by DFAS which are relevant to DFAS' processing of financial data for DTRA:

- DoD financial management systems do not properly account for assets and liabilities in accordance with SFFAS No.1;

- DoD financial management systems do not account for accounts receivable and accounts payable in accordance with SFFAC No. 1; and

- DoD financial management systems do not implement the United States Standard General Ledger at the transaction level.

RESPONSIBILITIES AND METHODOLOGY

DTRA management has the responsibility for:

- preparing the Principal Financial Statements in conformity with accounting principles generally accepted in the United States of America;
- establishing and maintaining effective internal control; and
- complying with laws and regulations.

Our responsibility is to express an opinion on the Principal Financial Statements based on our audit. Auditing standards generally accepted in the United States of America require that we plan and perform the audit to obtain reasonable assurance about whether the Principal Financial Statements are free of material misrepresentation and presented fairly in accordance with accounting principles generally accepted in the United States of America. We considered DTRA's and DFAS' internal control for the purpose of expressing our opinion on the Principal Financial Statements and not to provide an opinion on internal control. We are also responsible for testing compliance with selected provisions of applicable laws and regulations that may materially affect the financial statements.

In order to fulfill these responsibilities, we

- examined, on a test basis, evidence supporting the amounts and disclosures in the Principal Financial Statements;
- assessed the accounting principles used and significant estimates made by management;
- evaluated the overall presentation of the Principal Financial Statements;
- obtained an understanding of the internal control over financial reporting by obtaining an understanding of the relevant internal controls, determined whether internal controls had been placed ion operation, assessed control risk and performed tests of controls;
- obtained an understanding of internal control over performance measures, including obtaining an understanding of the design of internal controls relating to the existence and completeness assertions and determined whether they had been placed in operation;
- tested, or obtained evidence of, compliance with selected provisions of laws and regulations that may have a direct and material effect the Principal Financial Statements;

- obtained written representations from management; and

- performed other procedures as we considered necessary in the circumstances.

Our audits were conducted in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, and OMB Bulletin 01-02. We believe that our audits provide a reasonable basis for our opinion.

The Management's Discussion and Analysis (MD&A), and Required Supplementary Information are not a required part of the Principal Financial Statements, but are supplementary information required by OMB Circular A-136, *Financial Reporting Requirements* and DoD Financial Management Regulation 1700.14-R, Volume 6B, *Form and Content of the Department of Defense Audited Financial Statements*, and the Federal Accounting Advisory Standards Board. We have applied certain limited procedures which consisted primarily of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

This report is intended for the information of DTRA management. This restriction is not intended to limit the distribution of this report, which is a matter of public record.

Leonard G. Birnbaum and Company, LLP

Alexandria, Virginia
November 8, 2005