

Department of Defense
Department of the Navy
CONSOLIDATED BALANCE SHEET
As of December 31, 2006 and 2005

	2007 Consolidated	2006 Consolidated
	<hr/>	<hr/>
1. ASSETS (Note 2)		
A. Intragovernmental:		
1. Fund Balance with Treasury (Note 3)		
a. Entity	\$ 187,460,764,858.14	\$ 94,584,525,041.84
b. Non-Entity Seized Iraqi Cash	0.00	0.00
c. Non-Entity-Other	355,502,937.89	259,216,468.09
2. Investments (Note 4)	9,686,252.46	9,484,013.50
3. Accounts Receivable (Note 5)	143,261,487.87	152,031,529.08
4. Other Assets (Note 6)	466,053,317.52	531,043,052.72
5. Total Intragovernmental Assets	<hr/> \$ 188,435,268,853.88	<hr/> \$ 95,536,300,105.23
B. Cash and Other Monetary Assets (Note 7)	\$ 184,346,019.96	\$ 262,715,377.03
C. Accounts Receivable, Net (Note 5)	3,341,711,950.98	3,570,566,836.74
D. Loans Receivable (Note 8)	0.00	0.00
E. Inventory and Related Property, Net (Note 9)	60,117,791,152.31	58,832,249,976.77
F. General Property, Plant and Equipment, Net (Note 10)	187,582,931,858.89	159,869,625,708.62
G. Investments (Note 4)	0.00	0.00
H. Other Assets (Note 6)	7,857,323,212.64	7,347,586,379.63
2. TOTAL ASSETS	<hr/> <hr/> \$ 447,519,373,048.66	<hr/> <hr/> \$ 325,419,044,384.02
3. LIABILITIES (Note 11)		
A. Intragovernmental:		
1. Accounts Payable (Note 12)	\$ 1,100,192,881.03	\$ 988,086,805.74
2. Debt (Note 13)	0.00	0.00
3. Other Liabilities (Note 15 & 16)	4,427,745,251.78	4,285,046,589.45
4. Total Intragovernmental Liabilities	<hr/> \$ 5,527,938,132.81	<hr/> \$ 5,273,133,395.19
B. Accounts Payable (Note 12)	\$ 872,169,644.79	\$ 1,211,637,345.42
C. Military Retirement and Other Federal Employment Benefits (Note 17)	1,513,643,894.37	1,532,819,451.36
D. Environmental and Disposal Liabilities (Note 14)	18,965,063,536.81	18,258,544,637.25
E. Loan Guarantee Liability (Note 8)	0.00	0.00
F. Other Liabilities (Note 15 & Note 16)	5,681,476,690.21	4,731,233,266.43
4. TOTAL LIABILITIES	<hr/> \$ 32,560,291,898.99	<hr/> \$ 31,007,368,095.65
5. NET POSITION		
A. Unexpended Appropriations - Earmarked Funds (Note 23)	\$ 1,549,698.83	\$ 2,218,618.41
B. Unexpended Appropriations - Other Funds	191,576,684,573.00	98,389,261,028.35
C. Cumulative Results of Operations - Earmarked Funds	19,863,451.35	20,833,231.08
D. Cumulative Results of Operations - Other Funds	223,360,983,426.49	195,999,363,410.53
6. TOTAL NET POSITION	<hr/> \$ 414,959,081,149.67	<hr/> \$ 294,411,676,288.37
7. TOTAL LIABILITIES AND NET POSITION	<hr/> <hr/> \$ 447,519,373,048.66	<hr/> <hr/> \$ 325,419,044,384.02

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CONSOLIDATED STATEMENT OF NET COST
 For the periods ended December 31, 2006 and 2005

	2007 Consolidated	2006 Consolidated
1. Program Costs		
A. Gross Costs	\$ 38,415,988,164.44	\$ 31,741,011,510.64
B. (Less: Earned Revenue)	(1,400,117,353.60)	(1,048,332,881.94)
C. Net Program Costs	<u>\$ 37,015,870,810.84</u>	<u>\$ 30,692,678,628.70</u>
2. Cost Not Assigned to Programs	0.00	0.00
3. (Less: Earned Revenue Not Attributable to Programs)	0.00	0.00
4. Net Cost of Operations	<u><u>\$ 37,015,870,810.84</u></u>	<u><u>\$ 30,692,678,628.70</u></u>

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CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION

For the periods ended December 31, 2006 and 2005

	2007 Earmarked Funds	2007 All Other Funds
CUMULATIVE RESULTS OF OPERATIONS		
1. Beginning Balances	\$ 18,843,309.18	\$ 223,833,047,703.09
2. Prior Period Adjustments:		
2.A. Changes in accounting principles (+/-)	0.00	0.00
2.B. Corrections of errors (+/-)	0.00	0.00
3. Beginning balances, as adjusted	18,843,309.18	223,833,047,703.09
4. Budgetary Financing Sources:		
4.A. Other adjustments (rescissions, etc.)	0.00	0.00
4.B. Appropriations used	0.00	36,338,320,754.68
4.C. Nonexchange revenue	189,942.10	15,928,657.53
4.D. Donations and forfeitures of cash and cash equivalents	5,698,863.49 0.00	0.00 0.00
4.E. Transfers-in/out without reimbursement	0.00	0.00
4.F. Other budgetary financing sources	0.00	0.00
5. Other Financing Sources:		
5.A. Donations and forfeitures of property	0.00	0.00
5.B. Transfers-in/out without reimbursement (+/-)	0.00	38,556,699.96
5.C. Imputed financing from costs absorbed by others	0.00	146,131,758.65
5.D. Other (+/-)	0.00	0.00
6. Total Financing Sources	5,888,805.59	36,538,937,870.82
7. Net Cost of Operations (+/-)	4,868,663.42	37,011,002,147.42
8. Net Change	1,020,142.17	(472,064,276.60)
9. Cumulative Results of Operations	19,863,451.35	223,360,983,426.49
UNEXPENDED APPROPRIATIONS		
10. Beginning Balances	\$ 1,549,698.83	\$ 99,697,751,327.68
11. Prior Period Adjustments:		
11.A. Changes in accounting principles	0.00	0.00
11.B. Corrections of errors	0.00	0.00
12. Beginning balances, as adjusted	1,549,698.83	99,697,751,327.68
13. Budgetary Financing Sources:		
13.A. Appropriations received	0.00	128,591,944,000.00
13.B. Appropriations transferred-in/out	0.00	90,096,000.00
13.C. Other adjustments (rescissions, etc)	0.00	(464,786,000.00)
13.D. Appropriations used	0.00	(36,338,320,754.68)
14. Total Budgetary Financing Sources	0.00	91,878,933,245.32
15. Unexpended Appropriations	1,549,698.83	191,576,684,573.00
16. Net Position	21,413,150.18	414,937,667,999.49

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CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION

For the periods ended December 31, 2006 and 2005

	2007 Eliminations	2007 Consolidated
CUMULATIVE RESULTS OF OPERATIONS		
1. Beginning Balances	\$ 0.00	\$ 223,851,891,012.27
2. Prior Period Adjustments:		
2.A. Changes in accounting principles (+/-)	0.00	0.00
2.B. Corrections of errors (+/-)	0.00	0.00
3. Beginning balances, as adjusted	0.00	223,851,891,012.27
4. Budgetary Financing Sources:		
4.A. Other adjustments (rescissions, etc.)	0.00	0.00
4.B. Appropriations used	0.00	36,338,320,754.68
4.C. Nonexchange revenue	0.00	16,118,599.63
4.D. Donations and forfeitures of cash and cash equivalents	0.00	5,698,863.49
4.E. Transfers-in/out without reimbursement	0.00	0.00
4.F. Other budgetary financing sources	0.00	0.00
5. Other Financing Sources:		
5.A. Donations and forfeitures of property	0.00	0.00
5.B. Transfers-in/out without reimbursement (+/-)	0.00	38,556,699.96
5.C. Imputed financing from costs absorbed by others	0.00	146,131,758.65
5.D. Other (+/-)	0.00	0.00
6. Total Financing Sources	0.00	36,544,826,676.41
7. Net Cost of Operations (+/-)	0.00	37,015,870,810.84
8. Net Change	0.00	(471,044,134.43)
9. Cumulative Results of Operations	0.00	223,380,846,877.84
UNEXPENDED APPROPRIATIONS		
10. Beginning Balances	\$ 0.00	\$ 99,699,301,026.51
11. Prior Period Adjustments:		
11.A. Changes in accounting principles	0.00	0.00
11.B. Corrections of errors	0.00	0.00
12. Beginning balances, as adjusted	0.00	99,699,301,026.51
13. Budgetary Financing Sources:		
13.A. Appropriations received	0.00	128,591,944,000.00
13.B. Appropriations transferred-in/out	0.00	90,096,000.00
13.C. Other adjustments (rescissions, etc)	0.00	(464,786,000.00)
13.D. Appropriations used	0.00	(36,338,320,754.68)
14. Total Budgetary Financing Sources	0.00	91,878,933,245.32
15. Unexpended Appropriations	0.00	191,578,234,271.83
16. Net Position	0.00	414,959,081,149.67

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CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION

For the periods ended December 31, 2006 and 2005

	2006 Earmarked Funds	2006 All Other Funds
CUMULATIVE RESULTS OF OPERATIONS		
1. Beginning Balances	\$ 23,557,785.21	\$ 192,496,532,994.92
2. Prior Period Adjustments:		
2.A. Changes in accounting principles (+/-)	0.00	0.00
2.B. Corrections of errors (+/-)	0.00	0.00
3. Beginning balances, as adjusted	23,557,785.21	192,496,532,994.92
4. Budgetary Financing Sources:		
4.A. Other adjustments (rescissions, etc.)	0.00	0.00
4.B. Appropriations used	192,532.96	34,030,659,503.25
4.C. Nonexchange revenue	81,871.22	0.00
4.D. Donations and forfeitures of cash and cash equivalents	4,313,809.74 0.00	0.00 0.00
4.E. Transfers-in/out without reimbursement	0.00	0.00
4.F. Other budgetary financing sources	0.00	0.00
5. Other Financing Sources:		
5.A. Donations and forfeitures of property	0.00	0.00
5.B. Transfers-in/out without reimbursement (+/-)	0.00	17,381,706.15
5.C. Imputed financing from costs absorbed by others	0.00	140,155,066.86
5.D. Other (+/-)	0.00	0.00
6. Total Financing Sources	4,588,213.92	34,188,196,276.26
7. Net Cost of Operations (+/-)	7,312,768.05	30,685,365,860.65
8. Net Change	(2,724,554.13)	3,502,830,415.61
9. Cumulative Results of Operations	20,833,231.08	195,999,363,410.53
UNEXPENDED APPROPRIATIONS		
10. Beginning Balances	\$ 2,311,151.37	\$ 89,737,564,531.60
11. Prior Period Adjustments:		
11.A. Changes in accounting principles	0.00	0.00
11.B. Corrections of errors	0.00	0.00
12. Beginning balances, as adjusted	2,311,151.37	89,737,564,531.60
13. Budgetary Financing Sources:		
13.A. Appropriations received	100,000.00	42,236,061,000.00
13.B. Appropriations transferred-in/out	0.00	512,892,000.00
13.C. Other adjustments (rescissions, etc)	0.00	(66,597,000.00)
13.D. Appropriations used	(192,532.96)	(34,030,659,503.25)
14. Total Budgetary Financing Sources	(92,532.96)	8,651,696,496.75
15. Unexpended Appropriations	2,218,618.41	98,389,261,028.35
16. Net Position	23,051,849.49	294,388,624,438.88

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CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION

For the periods ended December 31, 2006 and 2005

	2006 Eliminations	2006 Consolidated
CUMULATIVE RESULTS OF OPERATIONS		
1. Beginning Balances	\$ 0.00	\$ 192,520,090,780.13
2. Prior Period Adjustments:		
2.A. Changes in accounting principles (+/-)	0.00	0.00
2.B. Corrections of errors (+/-)	0.00	0.00
3. Beginning balances, as adjusted	0.00	192,520,090,780.13
4. Budgetary Financing Sources:		
4.A. Other adjustments (rescissions, etc.)	0.00	0.00
4.B. Appropriations used	0.00	34,030,852,036.21
4.C. Nonexchange revenue	0.00	81,871.22
4.D. Donations and forfeitures of cash and cash equivalents	0.00	4,313,809.74
4.E. Transfers-in/out without reimbursement	0.00	0.00
4.F. Other budgetary financing sources	0.00	0.00
5. Other Financing Sources:		
5.A. Donations and forfeitures of property	0.00	0.00
5.B. Transfers-in/out without reimbursement (+/-)	0.00	17,381,706.15
5.C. Imputed financing from costs absorbed by others	0.00	140,155,066.86
5.D. Other (+/-)	0.00	0.00
6. Total Financing Sources	0.00	34,192,784,490.18
7. Net Cost of Operations (+/-)	0.00	30,692,678,628.70
8. Net Change	0.00	3,500,105,861.48
9. Cumulative Results of Operations	0.00	196,020,196,641.61
UNEXPENDED APPROPRIATIONS		
10. Beginning Balances	\$ 0.00	\$ 89,739,875,682.97
11. Prior Period Adjustments:		
11.A. Changes in accounting principles	0.00	0.00
11.B. Corrections of errors	0.00	0.00
12. Beginning balances, as adjusted	0.00	89,739,875,682.97
13. Budgetary Financing Sources:		
13.A. Appropriations received	0.00	42,236,161,000.00
13.B. Appropriations transferred-in/out	0.00	512,892,000.00
13.C. Other adjustments (rescissions, etc)	0.00	(66,597,000.00)
13.D. Appropriations used	0.00	(34,030,852,036.21)
14. Total Budgetary Financing Sources	0.00	8,651,603,963.79
15. Unexpended Appropriations	0.00	98,391,479,646.76
16. Net Position	0.00	294,411,676,288.37

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COMBINED STATEMENT OF BUDGETARY RESOURCES
 For the periods ended December 31, 2006 and 2005

	<u>2007 Combined</u>	<u>2006 Combined</u>
BUDGETARY FINANCING ACCOUNTS		
BUDGETARY RESOURCES:		
1. Unobligated balance, brought forward, October 1	\$ 20,835,974,465.33	\$ 17,128,478,891.28
2. Recoveries of prior year unpaid obligations	1,518,749,703.15	1,462,423,588.43
3. Budget authority		
3.A. Appropriation	129,730,063,454.44	125,396,895,718.12
3.B. Borrowing authority	0.00	0.00
3.C. Contract authority	0.00	0.00
3.D. Spending authority from offsetting collections		
3.D.1 Earned		
3.D.1.a. Collected	1,661,968,195.69	1,861,851,686.82
3.D.1.b. Change in receivables from Federal sources	41,916,431.59	(771,952,193.87)
3.D.2 Change in unfilled customer orders		
3.D.2.a. Advance received	23,822,665.40	98,379,661.86
3.D.2.b. Without advance from Federal sources	2,453,231,707.09	2,040,367,291.35
3.D.3. Anticipated for rest of year, without advances	0.00	228,700,000.00
3.D.4. Previously unavailable	0.00	0.00
3.D.5. Expenditure transfers from trust funds	0.00	0.00
3.E. Subtotal	<u>133,911,002,454.21</u>	<u>128,854,242,164.28</u>
4. Nonexpenditure transfers, net, anticipated and actual	90,096,000.00	512,892,000.00
5. Temporarily not available pursuant to Public Law	(1,132,101,000.00)	(83,156,159,000.00)
6. Permanently not available	(464,786,000.00)	(66,597,000.00)
7. Total Budgetary Resources	<u><u>\$ 154,758,935,622.69</u></u>	<u><u>\$ 64,735,280,643.99</u></u>

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COMBINED STATEMENT OF BUDGETARY RESOURCES
For the periods ended December 31, 2006 and 2005

	2007 Combined	2006 Combined
Status of Budgetary Resources:		
8. Obligations incurred:		
8.A. Direct	\$ 53,057,800,795.00	\$ 30,600,436,066.95
8.B. Reimbursable	1,958,470,970.71	3,351,387,959.28
8.C. Subtotal	<u>55,016,271,765.71</u>	<u>33,951,824,026.23</u>
9. Unobligated balance:		
9.A. Apportioned	97,435,033,752.05	28,670,819,537.75
9.B. Exempt from apportionment	0.00	74,024.00
9.C. Subtotal	<u>97,435,033,752.05</u>	<u>28,670,893,561.75</u>
10. Unobligated balance not available	2,307,630,104.93	2,112,563,056.01
11. Total status of budgetary resources	<u><u>\$ 154,758,935,622.69</u></u>	<u><u>\$ 64,735,280,643.99</u></u>
Change in Obligated Balance:		
12. Obligated balance, net		
12.A. Unpaid obligations, brought forward, October 1	78,088,019,583.29	72,093,186,783.26
12.B. Less: Uncollected customer payments from Federal sources, brought forward, October 1	<u>\$ (2,971,157,160.24)</u>	<u>\$ (3,400,813,853.87)</u>
12.C. Total unpaid obligated balance	75,116,862,423.05	68,692,372,929.39
13. Obligations incurred net (+/-)	<u>\$ 55,016,271,765.71</u>	<u>\$ 33,951,824,026.23</u>
14. Less: Gross outlays	(38,393,608,417.19)	(35,849,439,215.42)
15. Obligated balance transferred, net		
15.A. Actual transfers, unpaid obligations (+/-)	0.00	0.00
15.B. Actual transfers, uncollected customer payments from Federal sources (+/-)	<u>0.00</u>	<u>0.00</u>
15.C. Total Unpaid obligated balance transferred, net	0.00	0.00
16. Less: Recoveries of prior year unpaid obligations, actual	<u>(1,518,749,703.15)</u>	<u>(1,462,423,588.43)</u>
17. Change in uncollected customer payments from Federal sources (+/-)	(2,495,148,138.68)	(1,268,415,097.48)
18. Obligated balance, net, end of period		
18.A. Unpaid obligations	93,191,933,228.66	68,733,148,005.64
18.B. Less: Uncollected customer payments (+/-) from Federal sources (-)	<u>(5,466,305,298.92)</u>	<u>(4,669,228,951.35)</u>
18.C. Total, unpaid obligated balance, net, end of period	<u>87,725,627,929.74</u>	<u>64,063,919,054.29</u>
Net Outlays		
19. Net Outlays:		
19.A. Gross outlays	38,393,608,417.19	35,849,439,215.42
19.B. Less: Offsetting collections	(1,685,790,861.09)	(1,960,231,348.68)
19.C. Less: Distributed Offsetting receipts	<u>(24,404,076.97)</u>	<u>(32,785,645.33)</u>
19.D. Net Outlays	<u><u>\$ 36,683,413,479.13</u></u>	<u><u>\$ 33,856,422,221.41</u></u>

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COMBINED STATEMENT OF BUDGETARY RESOURCES
 For the periods ended December 31, 2006 and 2005

	<u>2007 Combined</u>	<u>2006 Combined</u>
NONBUDGETARY FINANCING ACCOUNTS		
BUDGETARY RESOURCES		
1. Unobligated balance, brought forward, October 1	\$ 0.00	\$ 0.00
2. Recoveries of prior year unpaid obligations	0.00	0.00
3. Budget authority		
3.A. Appropriation	0.00	0.00
3.B. Borrowing authority	0.00	0.00
3.C. Contract authority	0.00	0.00
3.D. Spending authority from offsetting collections		
3.D.1 Earned		
3.D.1.a. Collected	0.00	0.00
3.D.1.b. Change in receivables from Federal sources	0.00	0.00
3.D.2 Change in unfilled customer orders		
3.D.2.a. Advance received	0.00	0.00
3.D.2.b. Without advance from Federal sources	0.00	0.00
3.D.3 Anticipated for rest of year, without advances	0.00	0.00
3.D.4 Previously unavailable	0.00	0.00
3.D.5 Expenditure transfers from trust funds	0.00	0.00
3.E. Subtotal	<u>0.00</u>	<u>0.00</u>
4. Nonexpenditure transfers, net, anticipated and actual	0.00	0.00
5. Temporarily not available pursuant to Public Law	0.00	0.00
6. Permanently not available	0.00	0.00
7. Total Budgetary Resources	<u><u>\$ 0.00</u></u>	<u><u>\$ 0.00</u></u>

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CONSOLIDATED STATEMENT OF FINANCING
For the periods ended December 31, 2006 and 2005

	2007 Consolidated	2006 Consolidated
	<hr/>	<hr/>
Resources Used to Finance Activities:		
Budgetary Resources Obligated		
1. Obligations incurred	\$ 55,016,271,765.71	\$ 33,951,824,026.23
2. Less: Spending authority from offsetting collections and recoveries (-)	(5,699,688,702.92)	(4,691,070,034.59)
3. Obligations net of offsetting collections and recoveries	49,316,583,062.79	29,260,753,991.64
4. Less: Offsetting receipts (-)	(24,404,076.97)	(32,785,645.33)
5. Net obligations	<hr/> 49,292,178,985.82	<hr/> 29,227,968,346.31
Other Resources		
6. Donations and forfeitures of property	0.00	0.00
7. Transfers in/out without reimbursement (+/-)	38,556,699.96	17,381,706.15
8. Imputed financing from costs absorbed by others	146,131,758.65	140,155,066.86
9. Other (+/-)	0.00	0.00
10. Net other resources used to finance activities	<hr/> 184,688,458.61	<hr/> 157,536,773.01
11. Total resources used to finance activities	<hr/> \$ 49,476,867,444.43	<hr/> \$ 29,385,505,119.32
Resources Used to Finance Items not Part of the Net Cost of Operations		
12. Change in budgetary resources obligated for goods, services and benefits ordered but not yet provided		
12a. Undelivered Orders (-)	(15,382,419,806.77)	2,850,754,229.84
12b. Unfilled Customer Orders	2,477,054,372.49	2,138,746,953.21
13. Resources that fund expenses recognized in prior periods	(678,706,043.72)	(205,807,714.23)
14. Budgetary offsetting collections and receipts that do not affect net cost of operations	24,404,076.97	0.00
15. Resources that finance the acquisition of assets	(3,080,652,813.05)	(6,273,364,471.46)
16. Other resources or adjustments to net obligated resources that do not affect net cost of operations		
16a. Less: Trust or Special Fund Receipts Related to exchange in the Entity's Budget (-)	0.00	0.00
16b. Other (+/-)	(38,556,699.96)	(17,381,706.15)
17. Total resources used to finance items not part of the net cost of operations	<hr/> \$ (16,678,876,914.04)	<hr/> \$ (1,507,052,708.79)
18. Total resources used to finance the net cost of operations	<hr/> \$ 32,797,990,530.39	<hr/> \$ 27,878,452,410.53

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CONSOLIDATED STATEMENT OF FINANCING
For the periods ended December 31, 2006 and 2005

	<u>2007 Consolidated</u>	<u>2006 Consolidated</u>
Components of the Net Cost of Operations that will not Require or Generate Resources in the Current Period:		
Components Requiring or Generating Resources in Future Period:		
19. Increase in annual leave liability	292,366.35	258,830,468.94
20. Increase in environmental and disposal liability	1,696,174,723.67	1,208,094,019.00
21. Upward/Downward reestimates of credit subsidy expense (+/-)	0.00	0.00
22. Increase in exchange revenue receivable from the public (-)	0.00	0.00
23. Other (+/-)	1,372,849,210.94	37,390,425.22
24. Total components of Net Cost of Operations that will require or generate resources in future periods	<u>3,069,316,300.96</u>	<u>1,504,314,913.16</u>
Components not Requiring or Generating Resources:		
25. Depreciation and amortization	2,275,409,260.56	3,939,158,748.89
26. Revaluation of assets or liabilities (+/-)	158,478,506.95	627,372,535.38
27. Other (+/-)		
27a. Trust Fund Exchange Revenue	0.00	0.00
27b. Cost of Goods Sold	0.00	0.00
27c. Operating Material & Supplies Used	(1,323,157,242.69)	(3,247,413,283.29)
27d. Other	37,833,454.67	(9,206,695.97)
28. Total components of Net Cost of Operations that will not require or generate resources	<u>1,148,563,979.49</u>	<u>1,309,911,305.01</u>
29. Total components of net cost of operations that will not require or generate resources in the current period	<u>\$ 4,217,880,280.45</u>	<u>\$ 2,814,226,218.17</u>
30. Net Cost of Operations	<u><u>\$ 37,015,870,810.84</u></u>	<u><u>\$ 30,692,678,628.70</u></u>

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

These financial statements have been prepared to report the financial position and results of operations of the Department of the Navy (DON) General Fund (GF), 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 DON in accordance with the “Department of Defense Financial Management Regulation” Office of Management and Budget (OMB) Circular A-136, Financial Reporting Requirements, and to the extent possible, generally accepted accounting principles (GAAP). The accompanying financial statements account for all resources for which DON GF is responsible. Information relative to classified assets, programs, and operations is aggregated and reported in such a manner that it is not discernable.

The DON is unable to fully implement all elements of GAAP and OMB Circular A-136 due to limitations of its financial management processes and systems, and nonfinancial systems and processes that feed into the financial statements. The DON derives its reported values and information for major asset and liability categories, largely from nonfinancial systems, such as inventory systems and logistic systems. These systems were designed to support reporting requirements for maintaining accountability over assets and reporting the status of Federal appropriations rather than preparing financial statements in accordance with GAAP. The DON continues to implement process and system improvements addressing these limitations. The DON currently has six auditor identified financial statement material weaknesses: (1) accuracy and complete reporting of accounts payable, (2) identifying and reporting environmental disposal liabilities, (3) military equipment reporting, (4) valuation of inventory and operating materials and supplies (5) Fund Balance with Treasury, and (6) real property.

Fiscal year (FY) 2007 represents the twelfth year that DON has prepared audited financial statements as required by CFO Act and GMRA.

1.B. Mission of the Reporting Entity

The Department of the Navy (DON) was created on April 30, 1798 by an act of Congress (I Stat. 533; 5 U.S.C. 411-12). The overall mission of DON is to maintain, train, and equip combat-ready Navy and Marine Corps forces capable of winning wars, deterring aggression and maintaining freedom of the seas.

1.C. Appropriations and Funds

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

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

Revolving funds receive their initial funding through an appropriation or a transfer of resources from existing appropriations or funds and use those capital resources to finance the initial startup. Financial resources to replenish the initial working capital and to permit continuing operations are generated by the acceptance of customer orders on a reimbursable basis. The National Defense Sealift Fund is DON General Fund's only revolving fund.

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

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

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

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

The DON GF is a party to allocation transfers with other federal agencies as a receiving (child) entity. Allocation transfers are legal delegations by one department of its authority to obligate budget authority and outlay funds, to another department. Generally, all financial activity related to these allocation transfers (e.g. budget authority, obligations, outlays) is reported in the financial statements of the parent entity. The DON receives allocation transfers, as the child, from the U.S. Forest Service and the Federal Highway Administration. The DON also receives allocation transfers, as the child, from the Executive Office of the President for the Foreign Military Financing Program, as well as for the International Military Education and Training program. However, DoD is responsible for reporting these child allocations to the parent. The DON does issue allocation transfers, as the parent, to other federal agencies.

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

Entity Accounts:

General Accounts

17 X 0380	Coastal Defense Augmentation, Navy
17 0703	Family Housing, Navy and Marine Corps
17 0730	Family Housing Construction, Navy and Marine Corps
17 0735	Family Housing Operation and Maintenance, Navy and Marine Corps
17 X 0810	Environmental Restoration, Navy
17 1000	Medicare Eligible Retiree Health Care Fund, Military Personnel Navy
17 1001	Medicare Eligible Retiree Health Care Fund, Military Personnel Marine Corps
17 1002	Medicare Eligible Retiree Health Care Fund, Reserve Personnel Navy
17 1003	Medicare Eligible Retiree Health Care Fund, Reserve Personnel Marine Corps
17 1105	Military Personnel, Marine Corps
17 1106	Operation and Maintenance, Marine Corps
17 1107	Operation and Maintenance, Marine Corps Reserve
17 1108	Reserve Personnel, Marine Corps
17 1109	Procurement, Marine Corps
17 1110*	Basic Allowance for Housing, Marine Corps
17 1111*	Basic Allowance for Housing, Marine Corps Reserve
17 1112*	Facilities Sustainment, Restoration and Modernization, Marine Corps
17 1113*	Facilities Sustainment, Restoration and Modernization, Marine Corps Reserve
17 1205	Military Construction, Navy and Marine Corps
17 1235	Military Construction, Navy Reserve
17 1236	Payments to Kaho Olawe Island Conveyance, Remediation and Environmental Restoration Fund, Navy
17 1319	Research, Development, Test and Evaluation, Navy
17 1405	Reserve Personnel, Navy
17 1406*	Basic Allowance for Housing, Navy Reserve
17 1453	Military Personnel, Navy
17 1454*	Basic Allowance for Housing, Navy
17 1506	Aircraft Procurement, Navy
17 1507	Weapons Procurement, Navy
17 1508	Procurement of Ammunition, Navy and Marine Corps
17 1611	Shipbuilding and Conversion, Navy
17 1804	Operation and Maintenance, Navy
17 1805*	Facilities Sustainment, Restoration and Modernization, Navy
17 1806	Operation and Maintenance, Navy Reserve
17 1807*	Facilities Sustainment, Restoration and Modernization, Navy
17 1810	Other Procurement, Navy
* Pending enactment	of the FY 2007 Military Construction Authorization Act

Revolving Funds

17 X 4557	National Defense Sealift Fund, Navy
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Earmarked Trust Funds

17 X 8716	Department of the Navy General Gift Fund
17 X 8723	Ships Stores Profits, Navy
17 X 8733	United States Naval Academy General Gift Fund

Earmarked Special Funds

17 X 5095	Wildlife Conservation, Military Reservations, Navy
17 X 5185	Kaho Olawe Island Conveyance, Remediation and Environmental Restoration Fund, Navy
17 X 5429	Roosmoor Liquidating Trust Settlement Account
17 X 5562	Ford Island Improvement Account

General Fund Receipt, Deposit, Suspense, and Clearing Accounts

17 1XXX	Receipt Accounts
17 3XXX	Receipt Accounts
17 X 6XXX	Deposit Funds

Parent-Child (Allocation) Transfer Accounts

17 11 1081	International Military Education and Training Funds, appropriated to the President
17 11 X 1081	International Military Education and Training Funds, appropriated to the President
17 11 1082	Foreign Military Financing Program Funds appropriated to the President
17 12 X 1105B	State and Private Forestry, Forest Service
17 69 X 8083	Federal-Aid Highways (Liquidation of Contract Authorization), Federal Highway Administration

1.D. Basis of Accounting

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

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

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

1.E. Revenues and Other Financing Sources

The DON receives congressional appropriations as financing sources for general funds on either an annual, multi-year basis, or no-year basis. When authorized by legislation, these appropriations are supplemented by revenues generated by sales of goods or services. The DON recognizes revenue as a result of costs incurred or services provided to other Federal agencies and the public. Full cost pricing is DON's standard policy for services provided as required by OMB Circular A-25. The DON recognizes revenue when earned within the constraints of current system capabilities. In other instances, revenue is recognized when bills are issued.

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

1.F. Recognition of Expenses

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

1.G. Accounting for Intragovernmental Activities

Preparation of reliable financial statements requires the elimination of transactions occurring among entities within DON, within DoD, or between two or more federal agencies. However, DON cannot consistently and accurately identify all of its intragovernmental transactions by customer because DON's accounting systems do not track all buyer and seller data needed to match related transactions. For the DON GF, the Defense Finance and Accounting Service (DFAS) is responsible for eliminating transactions and balances between components or activities of DON. Seller entities

within DoD provided summary seller-side balances for revenue, accounts receivable, and unearned revenue to the buyer-side internal DoD accounting offices. In most cases, the buyer-side records are adjusted to agree with DoD seller-side balances. Intra-DoD intragovernmental balances are then eliminated when DoD financial statements are prepared. The DON properly eliminates the revenue resulting from intra-DoD sales of capitalized assets. The DoD is developing long-term system improvements that will include sufficient up-front edits and controls to eliminate the need for after-the-fact reconciliations. The volume of intragovernmental transactions is so large that after-the-fact reconciliation cannot be accomplished effectively with existing or foreseeable resources.

The Department of the Treasury Financial Management Service (FMS) is responsible for eliminating transactions between DoD and other federal agencies. The Treasury Financial Manual, Part 2 – Chapter 4700, “Agency Reporting Requirements for the Financial Report of the United States Government” and the Treasury’s “Federal Intragovernmental Transaction Accounting Policy Guide” provide guidance for reporting and reconciling intragovernmental balances. While DON is unable to fully reconcile all intragovernmental transactions with all federal partners, DON is able to reconcile balances pertaining to investments in federal securities, borrowings from the U.S. Treasury and the Federal Financing Bank, Federal Employees’ Compensation Act transactions with the Department of Labor (DOL), and benefit program transactions with the Office of Personnel Management (OPM). The DoD’s proportionate share of public debt and related expenses of the federal government are not included. The federal government does not apportion debt and its related costs to federal agencies. The DoD’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 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.

1.H. Transactions with Foreign Governments and International Organizations

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

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

The DON’s monetary financial resources are maintained in U.S. Treasury accounts. The disbursing offices of the Defense Finance and Accounting Service (DFAS), the Military Services, the U. S. Army Corps of Engineers (USACE), and the Department of State’s financial service centers process the majority of DON’s cash collections, disbursements, and adjustments worldwide. Each disbursing station prepares monthly reports that

provide information to the U.S. Treasury on check issues, electronic fund transfers, interagency transfers and deposits.

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

1.J. Foreign Currency

Cash is the total of cash resources under the control of DON, which includes coin, paper currency, negotiable instruments, and amounts held for deposit in banks and other financial institutions. Foreign currency consists of the total U.S. dollar equivalent of both purchased and nonpurchased foreign currencies held in foreign currency fund accounts. Cash and foreign currency is classified as nonentity and, therefore, is restricted. Amounts reported consist primarily of cash and foreign currency held by Disbursing Officers to carry out their paying, collecting, and foreign currency accommodation exchange missions.

The DON conducts a significant portion of its operations overseas. The Congress established a special account to handle the gains and losses from foreign currency transactions for five general fund appropriations (Operations and Maintenance, Military Personnel, Military Construction, Family Housing Operations and Maintenance, and Family Housing Construction.) The gains and losses are computed as the variance between the exchange rate current at the date of payment and a budget rate established at the beginning of each fiscal year. Foreign currency fluctuations related to other appropriations require adjustments to the original obligation amount at the time of payment. The DON does not separately identify foreign currency fluctuations.

1.K. Accounts Receivable

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

1.L. Direct Loans and Loan Guarantees

Not applicable.

1.M. Inventories and Related Property

The DON values Operating Materials and Supplies (OM&S) using several valuation methods. Most OM&S is valued at an approximation of historical cost using latest acquisition cost adjusted for holding gains and losses. The latest acquisition cost method is used because legacy inventory systems were designed for materiel management rather

than accounting. Although these systems provide visibility and accountability over inventory items, they do not maintain historical cost data necessary to comply with the SFFAS No. 3, "Accounting for Inventory and Related Property." Additionally, these systems cannot produce financial transactions using the USSGL, as required by the Federal Financial Management Improvement Act of 1996 (P.L. 104-208). By utilizing new systems development processes, DON is continuing to transition the balance of OM&S to the moving average cost method. However, since the on-hand balances which transitioned were not, for the most part, baselined to auditable historical cost, the reported values remain non-compliant with SFFAS No. 3 and GAAP

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

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

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

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

1.N. Investments

For the Trust Funds, DON reports investments in U.S. Treasury securities at cost, net of amortized premiums or discounts. Premiums or discounts amortize into interest income over the term of the investment using the effective interest rate method or another method obtaining similar results. The DON's intent is to hold investments to maturity, unless

they are needed to finance claims or otherwise sustain operations. Consequently, no provision is made for unrealized gains or losses on these securities.

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

1.O. General Property, Plant and Equipment

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

In FY 2006 the capitalization threshold was revised from \$100,000 to \$20,000 for real property. The DON has not implemented the \$20,000 real property capitalization threshold yet pending an evaluation of real property systems, processes, and procedures that will have to be revised in order to implement the lowered threshold. The current \$100,000 capitalization threshold remains unchanged for the remaining General PP&E categories.

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

Prior to FY 1996, General PP&E was capitalized if it had an acquisition cost of \$15,000, \$25,000, and \$50,000 for FY 1993, 1994, and 1995, respectively, and an estimated useful life of two or more years. General PP&E previously capitalized at amounts below \$100,000 were written off DON General Fund financial statements in FY 1998.

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

The DoD is developing new policies and a contractor reporting process that will provide appropriate General PP&E information for future financial statement reporting purposes. Accordingly, DON reports only government property in the possession of contractors that is maintained in DON's property systems. The DoD has issued new property accountability and reporting requirements that requires DON to maintain, in its 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.

1.P. Advances and Prepayments

The DON records payments in advance of the receipt of goods and services as advances or prepayments and reports them as assets on the Balance Sheet. The DON recognizes advances and prepayments as expenses when it receives the related goods and services.

1.Q. Leases

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

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

1.R. Other Assets

The DON 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, DON provides financing payments. One type of financing payment that DON 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 on the Balance Sheet and in the related note.

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

Contract financing payments are defined in the Federal Acquisition Regulations (FAR), Part 32, as authorized disbursements of monies to a contractor prior to acceptance of supplies or services by the Government. These payments are designed to alleviate the potential financial burden on contractors performing on certain long-term contracts and

facilitate competition for defense contracts. Contract financing payments clauses are incorporated in the contract terms and conditions and may include advance payments, performance-based payments, commercial advance and interim payments, progress payments based on cost, and interim payments under certain cost-reimbursement contracts. Contract financing payments do not include invoice payments, payments for partial deliveries, lease and rental payments, or progress payments based on a percentage or stage of completion, which the Defense Federal Acquisitions Regulations Supplement (DFARS) authorizes only for construction of real property, shipbuilding, and ship conversion, alteration, or repair. Progress payments for real property are reported as Construction in Progress in Note 10.

1.S. Contingencies and Other Liabilities

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

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

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

1.T. Accrued Leave

The DON reports as liabilities military leave and civilian earned leave except sick leave that has been accrued and not used as of the Balance Sheet date. Sick leave is expensed as taken. The liability reported at the end of the accounting period reflects the current pay rates.

1.U. Net Position

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

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

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

1.V. Treaties for Use of Foreign Bases

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

1.W. Comparative Data

The Financial Statements and accompanying Notes to the Financial Statements report the financial position and results of operations for FY 2007. Financial statement fluctuations greater than two percent of total assets on the Balance Sheet or greater than ten percent from the prior period presented, but no less than \$100 thousand, are explained within the Notes to the Financial Statements.

1.X. Unexpended Obligations

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

1.Y. Undistributed Disbursements and Collection

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

1.Z. Data Collection Approach

The DON financial statements include information from both financial systems and nonfinancial feeder systems. The Defense Finance and Accounting Service, Cleveland (DFAS-CL) and Kansas City (DFAS-KC) collect the financial system information and incorporate it into the financial statements. The DON collects financial information from nonfinancial feeder systems through a data call process and submits it to DFAS-CL and DFAS-KC for incorporation into the financial statements. DFAS also collects information from multiple sources, such as intragovernmental data from DON's trading partners, which is incorporated into the financial statements. Beginning FY 2007, DON completed migration from the DON Data Collection Instrument to the Defense Departmental Reporting System (DDRS) Data Collection Module (DCM). The DDRS DCM captures certain required financial information from feeder systems for the General Fund (GF) financial statements. The DDRS DCM identifies the information requirements to the source provider, provides an audit trail, and integrates data into the financial statement preparation process.

Note 2.	Nonentity Assets
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As of December 31	2007	2006
1. Intragovernmental Assets		
A. Fund Balance with Treasury	\$ 355,502,937.89	\$ 259,216,468.09
B. Accounts Receivable	0.00	0.00
C. Total Intragovernmental Assets	\$ 355,502,937.89	\$ 259,216,468.09
2. Nonfederal Assets		
A. Cash and Other Monetary Assets	\$ 184,346,019.96	\$ 262,715,377.03
B. Accounts Receivable	3,170,730,631.26	3,061,625,669.60
C. Other Assets	0.00	0.00
D. Total Nonfederal Assets	\$ 3,355,076,651.22	\$ 3,324,341,046.63
3. Total Nonentity Assets	\$ 3,710,579,589.11	\$ 3,583,557,514.72
4. Total Entity Assets	\$ 443,808,793,459.55	\$ 321,835,486,869.30
5. Total Assets	\$ 447,519,373,048.66	\$ 325,419,044,384.02

Information Related to Nonentity Assets

Definitions

Entity accounts.

Assets that DON has the authority to use, or those that management is legally obligated to use to meet entity obligations.

Nonentity accounts.

Assets held by an entity, but are not available for use in the operations of the entity.

Other Disclosures

Nonentity Assets.

For 1st Quarter, FY 2007, DON holds \$3.7 billion nonentity assets. These assets are not available for use by DON in its day-to-day operations but DON maintains stewardship accountability and reporting responsibility. There are three categories of significant nonentity assets held by DON: (1) the Intragovernmental Fund Balance with Treasury, (2) the Nonfederal Cash and Other Monetary Assets, and (3) the Nonfederal Accounts Receivable.

Nonentity Nonfederal Accounts Receivable (Public).

For 1st Quarter, FY 2007, the DON holds \$3.2 billion of nonentity nonfederal accounts receivable. The primary component is a principal amount of \$1.3 billion, representing advance payments made to contractors and \$1.3 billion in associated accrued interest which remains in litigation. These receivable balances are being reported in nonentity accounts

receivable since the original appropriation year has been cancelled, and any funds collected as a result of this litigation would go to the Department of the Treasury.

Intragovernmental Fund Balance with Treasury.

This asset category, in the amount of \$355.6 million, represents amounts in DON's deposit and receipt fund accounts that are not available for DON's use in normal operations. An example of these accounts is the savings plans that were established by Congress to benefit deployed sailors and Marines.

Cash and Other Monetary Assets.

This asset category, in the amount of \$184.3 million, represents disbursing officers' cash and undeposited collections as reported on the Statement of Accountability. These assets are held by DON disbursing officers as agents of the Treasury and are not available for DON's use in normal operations.

Note 3.	Fund Balance with Treasury
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As of December 31	2007	2006
1. Fund Balances		
A. Appropriated Funds	\$ 184,412,347,605.80	\$ 91,997,660,017.18
B. Revolving Funds	3,035,053,437.81	2,572,053,994.39
C. Trust Funds	11,004,332.05	12,110,633.52
D. Special Funds	2,359,482.48	2,700,396.75
E. Other Fund Types	355,502,937.89	259,216,468.09
F. Total Fund Balances	\$ 187,816,267,796.03	\$ 94,843,741,509.93
2. Fund Balances Per Treasury Versus Agency		
A. Fund Balance per Treasury	\$ 187,160,534,045.93	\$ 58,106,707,222.87
B. Fund Balance per DON	187,816,267,796.03	94,843,741,509.93
3. Reconciling Amount	\$ (655,733,750.10)	\$ (36,737,034,287.06)

Fluctuations and Abnormalities

The overall increase in FBWT of \$93.0 billion, 98%, 1st Quarter, FY 2007 when compared with 1st Quarter, FY 2006 reflects the fact that Department of Defense, including DON, was operating under Continuing Resolution Authority (CRA) in 1st Quarter, FY 2006. Under CRA a full years' budget authority and related FBWT is not provided to the affected Federal agencies. In FY 2007, the DoD Appropriation Act was passed by the Congress and signed by the President; thus the budget authority and related FBWT reflects full funding. However, the FY 2007 Military Construction appropriation remains under CRA.

Explanation of Reconciliation Amount

The total reconciling amount of \$655.7 million (Line 3) is primarily due to \$823.2 million in Continuing Resolution Authority related to the Military Construction account. The Military Construction FBWT has been recorded in the DON's ledgers, but Treasury has not yet recognized the FBWT. This is offset by \$126.5 million in other reconciling differences, including FBWT recorded to invalid program years in the Treasury ledgers. The invalid program years, primarily an extended availability Shipbuilding and Conversion, Navy appropriation in the amount of \$120.5 million, represent duplicative reporting at Treasury. The DON and DFAS are working with Treasury to resolve the issue.

Status of Fund Balance with Treasury

As of December 31	2007	2006
1. Unobligated Balance		
A. Available	\$ 97,434,950,907.05	\$ 28,442,119,537.75
B. Unavailable	2,307,630,104.93	2,112,563,056.01
2. Obligated Balance not yet Disbursed	\$ 93,191,933,228.66	\$ 68,733,148,005.64
3. Nonbudgetary FBWT	\$ 357,606,327.28	\$ 234,528,319.07
4. NonFBWT Budgetary Accounts	\$ (5,475,852,771.89)	\$ (4,678,617,408.54)
5. Total	<u>\$ 187,816,267,796.03</u>	<u>\$ 94,843,741,509.93</u>

Other Information Related to Status of Fund Balance with Treasury

Fluctuations and Abnormalities

Total Status of FBWT increased \$93.0 billion, 98%, 1st Quarter, FY 2007 when compared with 1st Quarter, FY 2006. As disclosed above, for the same reason that, from a proprietary perspective, Total Fund Balances increased due to having an appropriation act in FY 2007, the Total Status of FBWT, which is a budgetary perspective, increased as well. Unobligated balances available and obligations not yet disbursed increased by a total of \$93.4 billion.

Definitions

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

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

Obligated Balance not yet Disbursed represents funds that have been obligated for goods that have not been received or services that have not been performed.

Non-Budgetary Fund Balance with Treasury (FBWT) includes entity and nonentity FBWT accounts which do not have budgetary authority, such as unavailable receipt accounts or clearing accounts.

Non-FBWT Budgetary Accounts include budgetary accounts that do not affect FBWT, such as contract authority, borrowing authority, unfilled customer orders, and investment accounts. This category reduces the Status of Fund Balance with Treasury. Neither contract authority nor borrowing authority applies to the DON General Fund.

Other Disclosures

Unobligated, Unavailable balances are restricted to future use and are not apportioned for current use.

Although funds have been appropriated, expired single year appropriations such as Operation and Maintenance and Military Pay accounts, are not generally available for obligation because the period for obligation established by law has lapsed. Multi-year accounts and "X" or no year accounts are restricted based on their appropriation type. Trust funds and Earmarked funds are restricted to their intended use.

Disclosures Related to Suspense/Budget Clearing Accounts

As of December 31	2005	2006	2007	(Decrease)/ Increase from FY 2006 - 2007
Account				
F3845 – Personal Property Proceeds	\$ 0.00	\$ 0.00	\$ 0.00	0.00
F3875 – Disbursing Officer Suspense	(212,416,423.84)	(19,391,294.58)	4,701,257.34	24,092,551.92
F3880 – Lost or Cancelled Treasury Checks	4,767,243.34	3,864,156.35	3,498,320.99	(365,835.36)
F3882 – Uniformed Services Thrift Savings Plan Suspense	3,886,272.17	32,634,181.10	46,475,113.89	13,840,932.79
F3885 – Interfund/IPAC Suspense	(52,421,916.02)	(9,161,010.79)	(6,096,188.94)	3,064,821.85
F3886 – Thrift Savings Plan Suspense	9,482.50	7,297.98	(187,525.73)	(194,823.71)
Total	\$ (256,175,341.85)	\$ 7,953,330.06	\$ 48,390,977.55	\$ 40,437,647.49

Fluctuations and Abnormalities

The total amount in Suspense/Budget Clearing Accounts increased \$40.4 million, 508%, 1st Quarter, FY 2007 from 1st Quarter, FY 2006. Account F3875 – Disbursing Officer Suspense increased \$24.1 million, 124% from the prior period credit balance as a result of efforts to clear aged suspended transactions over the past year. These efforts are part of the DON Financial Improvement Program and include an analysis of the types of inflows into the suspense accounts. Additionally, DON is establishing policies and procedures to ensure accurate and consistent use of these accounts. Account F3882 - Uniformed Services Thrift Savings Plan, increased \$13.8 million, 42%, 1st Quarter, FY 2007 from 1st Quarter, FY 2006. The amounts in this account, which was established in FY 2002, represent a timing difference between the posting of the Thrift Savings Plan deductions by the National Finance Center and the posting of these amounts in the DON's accounting systems in the following month.

Disclosures Related to Suspense/Budget Clearing Accounts

In general, Suspense and Budget Clearing accounts temporarily hold collection or disbursements until they can be assigned or identified to the valid appropriation.

Account F3885 – Interfund/IPAC Suspense has a credit balance of \$6.1 million. This account represents those intragovernmental disbursements and collections that have not yet been processed into the DON's accounting systems.

Account F3886, representing the civilian Thrift Savings Plan suspense, has a credit balance of \$187.5 thousand. The amounts in this account, representing withholdings from employees earnings and the government contribution, represent a timing difference between the posting of the Thrift Savings Plan

deductions by the National Finance Center and the posting of these amounts in the DON's accounting systems in the following month.

The F3880 suspense account reported a positive balance of \$3.5 million. This amount represents the balance of Treasury checks that (1) have either been lost by the payee and need to be reissued, (2) have never been cashed by the payee, or (3) have been cancelled by the Treasury and need to be transferred to the original appropriation.

Disclosures Related to Problem Disbursements and In-Transit Disbursements
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As of December 31	2005	2006	2007	(Decrease)/ Increase from FY 2006 to 2007
1. Total Problem Disbursements, Absolute Value				
A. Unmatched Disbursements (UMDs)	\$ 330,180,000.00	\$ 1,140,742,960.91	\$ 915,602,423.18	\$ (225,140,537.73)
B. Negative Unliquidated Obligations (NULO)	47,520,000.00	54,799,090.25	23,650,284.29	(31,148,805.96)
2. Total In-transit Disbursements, Net	\$ (58,904.00)	\$ (141,582,388.23)	\$ 114,823,342.78	256,405,731.01

Fluctuations and Abnormalities

Unmatched Disbursements (UMDs) have decreased by \$225.1 million, 20%, 1st Quarter, FY 2007 from 1st Quarter, FY 2006. Negative Unliquidated Obligations (NULOs) have decreased \$31.1 million, 57% from the comparative period. The DON and DFAS have partnered to reduce UMD and NULO balances and the significant reductions are reflective of those efforts. In 2nd Quarter, FY 2005, DFAS-Cleveland expanded the scope of the definition of an UMD. Formerly, transactions that had not yet reached an accounting station were defined as undistributed. Now these transactions are being defined as an UMD. This change in practice was the primary driver behind the increase from FY 2005 to FY 2006.

In-Transit Disbursements, Net increased \$256.4 million, 189%, 1st Quarter, FY 2007 from the credit balance reflected in 1st Quarter, FY 2006. This increase reflects a concerted effort by DON and DFAS to identify systemic errors and implement corrective actions through synchronization of edit tables to validate data between systems.

In March 2006, DON submitted a plan of action and milestones to the Under Secretary of Defense (Comptroller) that describes how the DON will work in conjunction with DFAS to resolve aged problem disbursements.

Definitions

An Unmatched Disbursement (UMD) occurs when a payment is not matched to a corresponding obligation in the accounting system.

Absolute Value is the sum of the positive values of debit and credit transactions without regard to the sign (plus or minus).

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

In-Transit Disbursements, Net represent the net value of disbursements and collections made by a DoD disbursing activity on behalf of an accountable activity which have not been posted in an accounting system.

Other Disclosures

The elimination of both Problem Disbursements and In-transits is one of the highest financial management priorities of OUSD(C). Problem Disbursements and In-transits represent a significant financial management concern since: (1) accuracy of accounting reports is affected; (2) availability of funds is more difficult to determine, and (3) the required research and resolution process becomes much more labor intensive as the age of the problem disbursements increase. As a result, DON has efforts underway to improve the systems and to resolve previous problem disbursements and process in-transit disbursements.

The problem disbursements reported by DON are in balance with the problem disbursement metric furnished to DFAS Arlington.

Note 4.	Investments and Related Interest
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As of December 31	2007				
	Cost	Amortization Method	Amortized (Premium) / Discount	Investments, Net	Market Value Disclosure
1. Intragovernmental Securities					
A. Nonmarketable, Market-Based					
1. Military Retirement Fund	\$ 0.00		\$ 0.00	\$ 0.00	\$ 0.00
2. Medicare Eligible Retiree Health Care Fund	0.00		0.00	0.00	0.00
3. US Army Corps of Engineers	0.00		0.00	0.00	0.00
4. Other Funds	9,615,424.22		(34,790.65)	9,580,633.57	9,580,633.57
5. Total Nonmarketable, Market-Based	9,615,424.22		(34,790.65)	9,580,633.57	9,580,633.57
B. Accrued Interest	105,618.89			105,618.89	105,618.89
C. Total Intragovernmental Securities	\$ 9,721,043.11		\$ (34,790.65)	\$ 9,686,252.46	\$ 9,686,252.46
2. Other Investments					
A. Total Other Investments	\$ 0.00		\$ 0.00	\$ 0.00	N/A
3. Intragovernmental Securities					
A. Nonmarketable, Market-Based					
1. Military Retirement Fund	\$ 0.00		\$ 0.00	\$ 0.00	\$ 0.00
2. Medicare Eligible Retiree Health Care Fund	0.00		0.00	0.00	0.00
3. US Army Corps of Engineers	0.00		0.00	0.00	0.00
4. Other Funds	9,421,028.60		(3,078.48)	9,417,950.12	9,417,950.12
5. Total Nonmarketable, Market-Based	9,421,028.60		(3,078.48)	9,417,950.12	9,417,950.12
B. Accrued Interest	66,063.38			66,063.38	66,063.38
C. Total Intragovernmental Securities	\$ 9,487,091.98		\$ (3,078.48)	\$ 9,484,013.50	\$ 9,484,013.50
4. Other Investments					
A. Total Other Investments	\$ 0.00		\$ 0.00	\$ 0.00	N/A

Other Disclosures

The two DON Trust Funds holding interest-bearing securities are the Naval Academy General Gift Fund and the Navy General Gift Fund, which have a total Investment net value of \$9.7 million (including \$105.6 thousand of accrued interest). These investments are Nonmarketable Market-Based U.S. Treasury securities reported at cost, net of amortized premiums and discounts. In accordance with the Statement of Federal Financial Accounting Standards No. 27, "Identifying and Reporting Earmarked Funds," DON Trust Funds are classified and reported as earmarked funds.

Intragovernmental Investments for Earmarked Funds.

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

Note 5.	Accounts Receivable
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As of December 31	2007			2006
	Gross Amount Due	Allowance For Estimated Uncollectibles	Accounts Receivable, Net	Accounts Receivable, Net
1. Intragovernmental Receivables	\$ 143,261,487.87	N/A	\$ 143,261,487.87	\$ 152,031,529.08
2. Nonfederal Receivables (From the Public)	\$ 3,356,012,074.18	\$ (14,300,123.20)	\$ 3,341,711,950.98	\$ 3,570,566,836.74
3. Total Accounts Receivable	\$ 3,499,273,562.05	\$ (14,300,123.20)	\$ 3,484,973,438.85	\$ 3,722,598,365.82

Information Related to Accounts Receivable

Nonfederal Receivables.

Allowance Method

Based upon an extensive analysis of historic public receivables, the allowance for 1st Quarter, FY 2007 was determined to be \$14.3 million.

Intragovernmental Accounts Receivable Adjustments

Allocation of Undistributed Collections.

Undistributed collections are allocated between federal and nonfederal categories based on the percentage of federal and nonfederal Accounts Receivable as submitted in the field level general ledgers. This allocation was suggested as appropriate in a DFAS Arlington memorandum of October 4, 2000, which required disclosure to the audit community of the applicable methodology used to allocate undistributed collections. For 1st Quarter, FY 2007 \$680.6 million in undistributed collections was allocated to accounts receivable.

Elimination Adjustments.

The DON's accounting systems do not consistently capture trading partner data at the transaction level in a manner that facilitates trading partner reconciliations. Therefore, DON was unable to reconcile intragovernmental accounts receivable balances with the Accounts Payable balances of its intragovernmental trading partners. Through the ongoing Business Transformation Agency effort, the Department intends to develop long-term systems improvements that will capture the data necessary to perform reconciliations.

Intrafund transactions (within DON GF) are eliminated based upon trading partner information obtained from the Naval Personnel Command, the Naval Air Systems Command Enterprise Resource Planning system, the Standard Budget Accounting Reporting System (SABRS), the Standard Accounting and Reporting System – Field Level (STARS-FL), and the Standard Accounting and Reporting System – Headquarters Module (STARS-HQ). The elimination data obtained from these systems included seller appropriation, grantor (buyer) appropriation, grantor subhead, grantor code, reimbursable source code, accounts receivable, revenue, unearned revenue, and amount collected.

Aged Accounts Receivable

As of December 31	2007		4th Quarter 2006	
	Intragovernmental	Nonfederal	Intragovernmental	Nonfederal
CATEGORY				
Nondelinquent				
Current	\$ 419,142,434.02	\$ 198,756,582.68	\$ 381,171,729.65	\$ 535,982,738.91
Noncurrent	5,863,924.64	287,693,411.30	30,402,235.00	7,548,632.00
Delinquent				
1 to 30 days	\$ 17,276,887.23	\$ 14,244,548.61	\$ 2,188,010.88	\$ 7,022,483.38
31 to 60 days	6,746,600.38	7,009,859.37	1,100,987.38	4,737,053.10
61 to 90 days	5,890,409.47	12,667,062.99	1,150,263.30	9,686,722.45
91 to 180 days	3,856,954.50	20,253,290.12	7,408,852.37	10,597,988.02
181 days to 1 year	15,481,630.25	30,547,783.69	5,820,810.31	26,743,006.15
Greater than 1 year and less than or equal to 2 years	11,725,344.50	51,776,953.18	2,085,470.77	44,235,185.07
Greater than 2 years and less than or equal to 6 years	30,627,583.10	68,115,919.14	31,744,754.00	58,556,433.84
Greater than 6 years and less than or equal to 10 years	1,369,901.49	366,223,828.03	259,431.00	362,475,549.29
Greater than 10 years	0.00	2,624,628,272.57	0.00	2,605,292,456.67
Subtotal	\$ 517,981,669.58	\$ 3,681,917,511.68	\$ 463,332,544.66	\$ 3,672,878,248.88
Less Supported Undistributed Collections	(354,657,847.48)	(325,905,437.50)	(257,152,416.36)	(434,700,117.49)
Less Eliminations	(20,062,334.23)	0.00	(46,909,829.49)	0.00
Less Other	0.00	0.00	0.00	0.00
Total	\$ 143,261,487.87	\$ 3,356,012,074.18	\$ 159,270,298.81	\$ 3,238,178,131.39

Information Related to Aged Accounts Receivables

Nondelinquent Accounts Receivables are receivables outstanding for 30 days or less or those not yet due under the contract or billing document pertaining to the receivable. Current nondelinquent accounts receivable are those that are due in the next twelve months. Noncurrent nondelinquent accounts receivable include out-of-service debt that are due beyond the next twelve months, and are valued at \$293.6 million for 1st Quarter, FY 2007. These accounts are not considered delinquent since the associated repayment schedules allow for repayment after a 30-day period. The DON is actively pursuing collection action on all accounts receivable, both public and intragovernmental, in accordance with guidance in the DoD Financial Management Regulation, Volume 4, Chapter 3 and OMB Circular A-129 "Policies for Federal Credit Programs and Non-Tax Receivables".

For public debt, these collection actions include referring delinquent vendor debt to the Debt Management Office (DMO) for servicing no later than 60 days after the payment due date, and coordinating with DMO to further refer such debt over 180 days delinquent to Treasury for further collection action. As of 1st Quarter, FY 2007, \$373.0 million of public receivables has been referred to DMO for debt collection. A current example of collection actions related to public debt is a partnership between DON and DFAS to identify habitually delinquent public entities and develop standard processes with a goal of improving the joint business relationship.

For delinquent intragovernmental debt, collection actions include detailed research of subsidiary accounting transactions with DFAS, the compilation and review of dispute packages, and consultation and negotiation with debtor agencies to resolve outstanding receivables.

It must be recognized that, in certain instances, the status of litigation impacts the ability of the DON to actively pursue collection action on public debt.

Information Related to Aging Category Variances

The accounts receivable aging schedule prior year column represents 4th Quarter, FY 2006 ending balances, rather than the ending balances as 1st Quarter, FY 2006. Therefore, the prior year accounts receivable balance on the aging schedule will not agree with the prior year balance on the Balance Sheet nor the prior year balance in the first schedule in this note.

Accounts receivable in every category are aging. In general, these are considered temporary backlogs due to a transfer of functions between Defense Finance and Accounting Service (DFAS) sites.

The DON has over 100,000 individual debts that range in value from a few dollars to \$2.6 billion. There are almost 63,000 nondelinquent debts and over 37,000 delinquent debts. These debts are managed in multiple debt systems, by multiple debt management offices, and for entity debts, are accounted for in multiple field accounting systems by seven different field accounting offices. General trends are highlighted below.

In the nondelinquent category, total current debts have decreased \$299.3 million, 33%, since 4th Quarter, FY 2006 while noncurrent debts have increased \$255.6 million, 674% since 4th Quarter, FY 2006.

In the delinquent category, the same trends are noted. For example, in the 1-30 day delinquent category, total debts have increased \$22.3 million, 242% since 4th Quarter, FY 2006. An additional \$7.9 million, 136% is in the 31-60 day category while an additional \$7.7 million, 71% has moved to the 61-90 day category. An additional \$6.1 million, 34% is in the 91-180 day category, while an additional \$13.5 million, 41% is in the 181 day-1 year category. Finally, an additional \$17.2 million, 37% is in the 1-2 year category.

Note 6.	Other Assets
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As of December 31	2007	2006
1. Intragovernmental Other Assets		
A. Advances and Prepayments	\$ 466,053,317.52	\$ 531,043,052.72
B. Other Assets	0.00	0.00
C. Total Intragovernmental Other Assets	\$ 466,053,317.52	\$ 531,043,052.72
2. Nonfederal Other Assets		
A. Outstanding Contract Financing Payments	\$ 7,455,927,705.66	\$ 6,825,306,702.84
B. Other Assets (With the Public)	401,395,506.98	522,279,676.79
C. Total Nonfederal Other Assets	\$ 7,857,323,212.64	\$ 7,347,586,379.63
3. Total Other Assets	\$ 8,323,376,530.16	\$ 7,878,629,432.35

Fluctuations and AbnormalitiesIntragovernmental Other Assets.

The DON reported a decrease of \$65.0 million, 12%, in Total Intragovernmental Other Assets, (Line 1.C), 1st Quarter, FY 2007 when compared with 1st Quarter, FY 2006. The four primary factors contributing to the decrease are:

- A decrease in Advances and Prepayments of \$116.8 million with Navy Working Capital Fund due to the completion of the USS Ohio conversion in 2nd Quarter, FY 2006.
- A decrease in Advances and Prepayments of \$127.7 million with Department of Interior (DoI). Recent audits have focused attention on the contracting relationship between the DoD and DoI and the level of advances provided to DoI have declined in conjunction with these audits.
- An increase in Advances and Prepayments of \$113.1 million with Air Force General Fund. The increase is a result of increased DON activity with Air Force classified programs in the area of aircraft procurement and research, development, test, and evaluation during 1st Quarter, FY 2007.
- An increase in Advances and Prepayments of \$74.2 million with Department of Transportation, specifically the Maritime Administration for shipping and port services. An analysis of historical data was used as a baseline to record the current estimate for accounts payable.

Information Related to Other AssetsIntragovernmental Other Assets - Advances and Prepayment.

The buyer-side advances to others amounts were adjusted to agree with seller-side advances from others on the books of other DoD reporting entities (Level Two trading partners). Additionally, the buyer-side prepayment balances were adjusted to agree with seller-side deferred credits on the books of other DoD reporting entities. Material differences may exist as advances and prepayments to Other Federal Agencies (Level One trading partners) were estimated since DON

accounting systems are unable to identify the agency that is being advanced money from the buyer side perspective. The estimates were based upon historical trading partner data obtained from the Intragovernmental Review and Analysis System (IRAS).

Nonfederal Other Assets - Outstanding Contract Financing Payments.

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

The Contract Financing Payment balance of \$7.5 billion is comprised of \$7.1 billion in contract financing payments and an additional \$343.6 million in estimated future funded payments that will be paid to the contractor upon delivery and Government acceptance of a satisfactory product. (See additional discussion in Note 15, Other Liabilities).

Nonfederal Other Assets, Other Assets (With the Public).

The Other Assets (With the Public) includes advance pay to DON military personnel, travel advances, and miscellaneous advances to contractors and the assets related to the estimated future funded outstanding contract financing payments.

Note 7.	Cash and Other Monetary Assets
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As of December 31	2007	2006
1. Cash	\$ 142,008,579.09	\$ 201,927,472.86
2. Foreign Currency	42,337,440.87	60,787,904.17
3. Other Monetary Assets	0.00	0.00
4. Total Cash, Foreign Currency, & Other Monetary Assets	\$ 184,346,019.96	\$ 262,715,377.03

Fluctuations and Abnormalities

Total Cash, Foreign Currency and Other Monetary Assets (Line 4) decreased \$78.4 million, 30% 1st Quarter, FY 2007 when compared with 1st Quarter, FY 2006. The Marine Corps Expeditionary Forces, Camp Lejeune was deployed in 1st Quarter, FY 2006. Upon their return from the overseas deployment in 2nd Quarter, FY 2006, their Disbursing Officer dissolved the Limited Depository Account, containing cash and foreign currency that had been held in the National Bank of Kuwait. This Limited Depository Account, in accordance with DoD FMR guidelines, is part of the Disbursing Officer's accountability for public funds.

Definitions

Cash - the total of cash resources under the control of DON, which includes coin, paper currency, purchased foreign currency, negotiable instruments, and amounts on deposit in banks and other financial institutions.

Foreign Currency - consists of the total U.S. dollar equivalent of nonpurchased foreign currencies held in foreign currency fund accounts.

Restriction on Cash, Foreign Currency and Other Monetary Assets – total cash, foreign currency and other monetary assets reported are classified as nonentity, which means that the assets are not available for DON's use in normal operations. Therefore, total cash, foreign currency and other monetary assets, totaling \$184.3 million is restricted.

Other Disclosures

Cash and Foreign Currency consists primarily of cash held by Disbursing Officers to carry out their payment, collection, and foreign currency accommodation exchange mission. The primary source of the amounts reported is DoD Disbursing Officers, Statement of Accountability.

The DON translates foreign currency to U.S. dollars utilizing the Department of the Treasury Prevailing Rate of Exchange. This rate is the most favorable rate that would legally be available to the U.S. Government's acquisition of foreign currency for its official disbursement and accommodation of exchange transactions.

Note 8.	Direct Loan and/or Loan Guarantee Programs
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As of December 31

Direct Loan and/or Loan Guarantee Programs

Direct Loans Obligated After FY 1991

As of December 31	2007	2006
Loan Programs		
1. Military Housing Privatization Initiative		
A. Loans Receivable Gross	\$ 0.00	\$ 0.00
B. Interest Receivable	0.00	0.00
C. Foreclosed Property	0.00	0.00
D. Allowance for Subsidy Cost (Present Value)	0.00	0.00
E. Value of Assets Related to Direct Loans	\$ 0.00	\$ 0.00
2. Foreign Military Financing Account		
A. Loans Receivable Gross	\$ 0.00	\$ 0.00
B. Interest Receivable	0.00	0.00
C. Foreclosed Property	0.00	0.00
D. Allowance for Subsidy Cost (Present Value)	0.00	0.00
E. Value of Assets Related to Direct Loans	\$ 0.00	\$ 0.00
3. Total Loans Receivable	\$ 0.00	\$ 0.00

Total Amount of Direct Loans Disbursed

As of December 31	2007	2006
Direct Loan Programs		
1. Military Housing Privatization Initiative	\$ 0.00	\$ 0.00
2. Foreign Military Financing Account	0.00	0.00
3. Total	\$ 0.00	\$ 0.00

Subsidy Expense for Post FY 1991 Direct Loan

As of December 31

2007	Interest Differential	Defaults	Fees	Other	Total
1. New Direct Loans Disbursed:					
Military Housing Privatization Initiative	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
Foreign Military Financing Account	0.00	0.00	0.00	0.00	0.00
2006	Interest Differential	Defaults	Fees	Other	Total
2. New Direct Loans Disbursed:					
Military Housing Privatization Initiative	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
Foreign Military Financing Account	0.00	0.00	0.00	0.00	0.00
2007	Modifications	Interest Rate Reestimates	Technical Reestimates	Total Reestimates	Total
3. Direct Loan Modifications and Reestimates:					
Military Housing Privatization Initiative	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
Foreign Military Financing Account	0.00	0.00	0.00	0.00	0.00
2006	Modifications	Interest Rate Reestimates	Technical Reestimates	Total Reestimates	Total
4. Direct Loan Modifications and Reestimates:					
Military Housing Privatization Initiative	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
Foreign Military Financing Account	0.00	0.00	0.00	0.00	0.00
		2007	2006		
5. Total Direct Loan Subsidy Expense:					
Military Housing Privatization Initiative	\$ 0.00	\$ 0.00	0.00	0.00	0.00
Foreign Military Financing Account	0.00	0.00	0.00	0.00	0.00

Subsidy Rate for Direct Loans

As of December 31	Interest Differential	Defaults	Fees and other Collections	Other	Total
Direct Loan Programs					
1. Military Housing Privatization Initiative	0.00%	0.00%	0.00%	0.00%	0.00%
2. Foreign Military Financing Account	0.00%	0.00%	0.00%	0.00%	0.00%

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

As of December 31	2007		2006	
1. Beginning Balance of the Subsidy Cost Allowance	\$	0.00	\$	0.00
2. Add: Subsidy Expense for Direct Loans Disbursed during the Reporting Years by Component				
A. Interest Rate Differential Costs	\$	0.00	\$	0.00
B. Default Costs (Net of Recoveries)		0.00		0.00
C. Fees and Other Collections		0.00		0.00
D. Other Subsidy Costs		0.00		0.00
E. Total of the above Subsidy Expense Components	\$	0.00	\$	0.00
3. Adjustments				
A. Loan Modifications	\$	0.00	\$	0.00
B. Fees Received		0.00		0.00
C. Foreclosed Property Acquired		0.00		0.00
D. Loans Written Off		0.00		0.00
E. Subsidy Allowance Amortization		0.00		0.00
F. Other		0.00		0.00
G. Total of the above Adjustment Components	\$	0.00	\$	0.00
4. Ending Balance of the Subsidy Cost Allowance before Re-estimates	\$	0.00	\$	0.00
5. Add or Subtract Subsidy Re-estimates by Component				
A. Interest Rate Re-estimate	\$	0.00	\$	0.00
B. Technical/Default Reestimate		0.00		0.00
C. Total of the above Reestimate Components	\$	0.00	\$	0.00
6. Ending Balance of the Subsidy Cost Allowance	\$	0.00	\$	0.00

Defaulted Guaranteed Loans from Post FY 1991 Guarantees
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As of December 31	2007	2006
Loan Guarantee Program(s)		
1. Military Housing Privatization Initiative		
A. Defaulted Guaranteed Loans Receivable, Gross	\$ 0.00	\$ 0.00
B. Interest Receivable	0.00	0.00
C. Foreclosed Property	0.00	0.00
D. Allowance for Subsidy Cost (Present Value)	0.00	0.00
E. Value of Assets Related to Defaulted Guaranteed Loans Receivable, Net	\$ 0.00	\$ 0.00
2. Armament Retooling & Manufacturing Support Initiative		
A. Defaulted Guaranteed Loans Receivable, Gross	\$ 0.00	\$ 0.00
B. Interest Receivable	0.00	0.00
C. Foreclosed Property	0.00	0.00
D. Allowance for Subsidy Cost (Present Value)	0.00	0.00
E. Value of Assets Related to Defaulted Guaranteed Loans Receivable, Net	\$ 0.00	\$ 0.00
3. Total Value of Assets Related to Defaulted Guaranteed Loans Receivable	\$ 0.00	\$ 0.00

Guaranteed Loans Outstanding

As of December 31	Outstanding Principal of Guaranteed Loans, Face Value	Amount of Outstanding Principal Guaranteed
Guaranteed Loans Outstanding		
1. Military Housing Privatization Initiative	\$ 0.00	\$ 0.00
2. Armament Retooling & Manufacturing Support Initiative	\$ 0.00	\$ 0.00
3. Total	\$ 0.00	\$ 0.00
2007		
New Guaranteed Loans Disbursed		
1. Military Housing Privatization Initiative	\$ 0.00	\$ 0.00
2. Armament Retooling & Manufacturing Support Initiative	\$ 0.00	\$ 0.00
3. Total	\$ 0.00	\$ 0.00
2006		
New Guaranteed Loans Disbursed		
1. Military Housing Privatization Initiative	\$ 0.00	\$ 0.00
2. Armament Retooling & Manufacturing Support Initiative	\$ 0.00	\$ 0.00
3. Total	\$ 0.00	\$ 0.00

Liabilities for Post FY 1991 Loan Guarantees, Present Value

As of December 31	2007	2006
Loan Guarantee Program(s)		
1. Military Housing Privatization Initiative	\$ 0.00	\$ 0.00
2. Armament Retooling & Manufacturing Support Initiative	0.00	0.00
3. Total	\$ 0.00	\$ 0.00

Subsidy Expense for Post FY 1991 Loan Guarantees

As of December 31

2007	Interest Differential	Defaults	Fees	Other	Total
1. New Loan Guarantees Disbursed:					
Military Housing Privatization Initiative	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
Armament Retooling & Manufacturing Support Initiative	0.00	0.00	0.00	0.00	0.00
Total	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
2006	Interest Differential	Defaults	Fees	Other	Total
2. New Loan Guarantees Disbursed:					
Military Housing Privatization Initiative	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
Armament Retooling & Manufacturing Support Initiative	0.00	0.00	0.00	0.00	0.00
Total	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
2007	Modifications	Interest Rate Reestimates	Technical Reestimates	Total Reestimates	Total
3. Modifications and Reestimates:					
Military Housing Privatization Initiative	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
Armament Retooling & Manufacturing Support Initiative	0.00	0.00	0.00	0.00	0.00
Total	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
2006	Modifications	Interest Rate Reestimates	Technical Reestimates	Total Reestimates	Total
4. Modifications and Reestimates:					
Military Housing Privatization Initiative	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
Armament Retooling & Manufacturing Support Initiative	0.00	0.00	0.00	0.00	0.00
Total	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
2007	2006				
5. Total Loan Guarantee:					
Military Housing Privatization Initiative	\$ 0.00	\$ 0.00			
Armament Retooling & Manufacturing Support Initiative	0.00	0.00			
Total	\$ 0.00	\$ 0.00			

Subsidy Rates for Loan Guarantees

As of December 31	Interest Supplements	Defaults	Fees and other Collections	Other	Total
Loan Guarantee Programs:					
1. Military Housing Privatization Initiative	0.00%	0.00%	0.00%	0.00%	0.00%
2. Armament Retooling & Manufacturing Support Initiative	0.00%	0.00%	0.00%	0.00%	0.00%

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

As of December 31	2007		2006	
1. Beginning Balance of the Loan Guarantee Liability	\$	0.00	\$	0.00
2. Add: Subsidy Expense for Guaranteed Loans Disbursed during the Reporting Years by Component				
A. Interest Supplement Costs	\$	0.00	\$	0.00
B. Default Costs (Net of Recoveries)		0.00		0.00
C. Fees and Other Collections		0.00		0.00
D. Other Subsidy Costs		0.00		0.00
E. Total of the above Subsidy Expense Components	\$	0.00	\$	0.00
3. Adjustments				
A. Loan Guarantee Modifications	\$	0.00	\$	0.00
B. Fees Received		0.00		0.00
C. Interest Supplements Paid		0.00		0.00
D. Foreclosed Property and Loans Acquired		0.00		0.00
E. Claim Payments to Lenders		0.00		0.00
F. Interest Accumulation on the Liability Balance		0.00		0.00
G. Other		0.00		0.00
H. Total of the above Adjustments	\$	0.00	\$	0.00
4. Ending Balance of the Loan Guarantee Liability before Reestimates	\$	0.00	\$	0.00
5. Add or Subtract Subsidy Reestimates by Component				
A. Interest Rate Reestimate		0.00		0.00
B. Technical/default Reestimate		0.00		0.00
C. Total of the above Reestimate Components	\$	0.00	\$	0.00
6. Ending Balance of the Loan Guarantee Liability	\$	0.00	\$	0.00

Administrative Expenses

Note 9.	Inventory and Related Property
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As of December 31	2007	2006
1. Inventory, Net	\$ 0.00	\$ 0.00
2. Operating Materials & Supplies, Net	60,117,791,152.31	58,832,249,976.77
3. Stockpile Materials, Net	0.00	0.00
4. Total	\$ 60,117,791,152.31	\$ 58,832,249,976.77

Inventory, Net

As of December 31	2007			2006		Valuation Method
	Inventory, Gross Value	Revaluation Allowance	Inventory, Net	Inventory, Net		
1. Inventory Categories						
A. Available and Purchased for Resale	\$ 0.00	\$ 0.00	0.00	\$ 0.00	0.00	LAC,MAC
B. Held for Repair		0.00	0.00		0.00	LAC,MAC
C. Excess, Obsolete, and Unserviceable		0.00	0.00		0.00	NRV
D. Raw Materials		0.00	0.00		0.00	MAC,SP,LAC
E. Work in Process		0.00	0.00		0.00	AC
F. Total	\$ 0.00	\$ 0.00	0.00	\$ 0.00	0.00	

Legend for Valuation Methods:

Adjusted LAC = Latest Acquisition Cost, adjusted for holding gains and losses
 SP = Standard Price
 AC = Actual Cost

NRV = Net Realizable Value
 O = Other
 MAC = Moving Average Cost

Not applicable.

Operating Materials and Supplies, Net

As of December 31	2007			2006	Valuation Method
	OM&S Gross Value	Revaluation Allowance	OM&S, Net	OM&S, Net	
1. OM&S Categories					
A. Held for Use	\$ 54,813,516,723.40	\$ 0.00	\$ 54,813,516,723.40	\$ 53,630,981,817.55	SP, LAC
B. Held for Repair	6,372,603,020.50	(1,068,328,591.59)	5,304,274,428.91	5,201,268,159.22	SP, LAC
C. Excess, Obsolete, and Unserviceable	758,118,084.84	(758,118,084.84)	0.00	0.00	NRV
D. Total	\$ 61,944,237,828.74	\$ (1,826,446,676.43)	\$ 60,117,791,152.31	\$ 58,832,249,976.77	

Legend for Valuation Methods:

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

NRV = Net Realizable Value

SP = Standard Price

O = Other

AC = Actual Cost

2. Restrictions on Operating Materials and Supplies (OM&S):

There are no known restrictions on the use of OM&S.

3. Other Information Related to Operating Materials and Supplies

Information Related to Operating Material and Supplies, Net

General Composition of Operating Materials and Supplies (OM&S).

OM&S includes spare and repair parts, ammunition, conventional missiles, torpedoes, aircraft configuration pods, and centrally managed aircraft engines. The general composition of OM&S is as follows:

	<u>As of December 31, 2006</u>
<i>(Amounts in thousands)</i>	
Ammunition and Munitions	\$ 35,277,469
Appropriation Purchase Account (APA)	
Principal End and Secondary Items	10,954,674
Sponsor Owned Material	11,302,048
Real-time Reutilization Asset	
Management (RRAM)	2,200,154
Other	383,446
Total	<u>\$ 60,117,791</u>

Balances.

The Statement of Federal Financial Accounting Standards (SFFAS) No. 3 "Accounting for Inventory and Related Property" requires disclosure of the amount of OM&S held for "Future Use." This information is not captured by current OM&S systems which were designed for material management rather than accounting purposes.

Decision Criteria For Identifying The Category To Which Operating Materials And Supplies Are Assigned.

In order to standardize the reporting categories of Held for Use; Held for Repair; and Excess, Obsolete and Unserviceable, DON implemented the Under Secretary of Defense (Comptroller) (USD(C)) condition code crosswalk as defined in the memorandum "Accounting for Excess, Unserviceable, and Obsolete Inventory and Operating Materials and Supplies" dated August 12, 2002. In addition, the condition code crosswalk was amended to include code "V" in the Excess, Obsolete, Unserviceable category in September 2002. OM&S is reported as follows:

OM&S Category	Condition Codes
Held for Use	A, B, C, D
Held for Repair	E, F, G, J, K, L, M, N, R
Excess, Obsolete, Unserviceable	P, H, S, V

Condition Codes are used for material management purposes and are defined in the Naval Supply Systems Command (NAVSUP) Publication 409.

Valuation Method for OM&S.

On July 6, 2001, OUSD(C) issued a memorandum requiring Moving Average Cost (MAC) as the approved valuation method for Inventory Held for Sale and Operating Materials and Supplies. The memorandum directs each Military Department and Defense Agency responsible for material amounts of inventory or operating materials and supplies to implement the moving average cost valuation method as systems are renovated or replaced. The DON is participating in a DoD Business Transformation Agency effort that is currently designing and updating the Business Enterprise Architecture (BEA). The BEA includes guidance on transition plan strategy concepts, considerations, processes, and principles. MAC will be implemented as existing OM&S systems are renovated or replaced. Until then, DON continues to value OM&S using different valuation methodologies such as standard purchase price or actual cost. These valuation methodologies vary by system.

Other Disclosures

Ammunition and Munitions.

Ammunition and Munitions are maintained and valued in the Conventional Ammunition Integrated Management System Open System Environment (CAIMS-OSE).

APA Principal End and Secondary Items.

Principal and Secondary Items include OM&S items such as shipboard hull, mechanical and electronic equipment, and uninstalled aircraft engines. They are items of such importance that central inventory control is required. They normally possess one of the following characteristics: (a) essential for combat or training; (b) high dollar value; (c) difficult to procure or produce; or (d) critical basic materials or components.

Sponsor Owned Material (SOM).

SOM is defined as programmatic material required in support of Program Manager's mission requirements for production, life cycle maintenance, and installation of systems and equipment consistent with the mission charter. The material usage may involve, but is not limited to: item fabrication, assembly, testing, manufacture, development, repair, or research and development.

Real-time Reutilization Asset Management (RRAM).

Material maintained and valued in RRAM is considered excess to the owner, but may not be excess to the Navy. Standard price is used to value all stock-numbered items. Part-numbered items are valued by best available information.

Other Operating Materials & Supplies.

Other OM&S consists primarily of Fleet Hospitals held by the Bureau of Medicine and Surgery and War Reserve material in possession of the U.S. Coast Guard.

Stockpile Materials, Net

As of December 31	2007			2006		Valuation Method
	Stockpile Materials Amount	Allowance for Gains (Losses)	Stockpile Materials, Net	Stockpile Materials, Net		
1. Stockpile Materials Categories						
A. Held for Sale	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00	0.00	AC, LCM
B. Held in Reserve for Future Sale	0.00	0.00	0.00	0.00	0.00	AC, LCM
C. Total	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00	0.00	

Legend for Valuation Methods:

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

NRV = Net Realizable Value
 LCM = Lower of Cost or Market
 O = Other

Not applicable.

Note 10. General PP&E, Net

As of December 31	2007					2006
	Depreciation/ Amortization Method	Service Life	Acquisition Value	(Accumulated Depreciation/ Amortization)	Net Book Value	Prior FY Net Book Value
1. Major Asset Classes						
A. Land	N/A	N/A	\$ 618,689,345.00	N/A	\$ 618,689,345.00	\$ 612,047,424.00
B. Buildings, Structures, and Facilities	S/L	20 Or 40	33,717,576,268.00	\$ (20,448,614,697.66)	13,268,961,570.34	13,739,012,431.64
C. Leasehold Improvements	S/L	lease term	7,775,419.15	(851,938.64)	6,923,480.51	7,038,097.81
D. Software	S/L	2-5 Or 10	3,817,887.44	(3,765,004.36)	52,883.08	105,766.10
E. General Equipment	S/L	5 or 10	2,845,088,980.13	(2,285,150,273.07)	559,938,707.06	477,404,838.51
F. Military Equipment	S/L	Various	301,578,757,098.00	(130,900,869,854.00)	170,677,887,244.00	142,120,000,000.00
G. Assets Under Capital Lease	S/L	lease term	114,695.76	(13,381.17)	101,314.59	112,784.16
H. Construction-in- Progress	N/A	N/A	2,450,377,314.31	N/A	2,450,377,314.31	2,913,904,366.40
I. Other			0.00	0.00	0.00	0.00
J. Total General PP&E			\$ 341,222,197,007.79	\$ (153,639,265,148.90)	\$ 187,582,931,858.89	\$ 159,869,625,708.62

¹ Note 15 for additional information on Capital Leases

Legend for Valuation Methods:

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

Fluctuations and Abnormalities

Total Department of the Navy (DON) General Plant, Property, and Equipment, Net (GPP&E) increased \$27.7 billion, 17%, 1st Quarter, FY 2007 when compared with 1st Quarter, FY 2006. This increase is a result of a change in methodology for reporting military equipment. The change in methodology resulted in an increase of \$28.6 billion in military equipment. Beginning with 3rd Quarter, FY 2006 the DON began using internal records for determining the value of military equipment. Previously, including 1st Quarter, FY 2006 military equipment was valued using Bureau of Economic Analysis (BEA) data. The increase in military equipment was offset by slight decreases in real property and construction-in progress.

Other Information Related to General PP&E, Net

The DON has the use of land, buildings, and other overseas facilities that are obtained through various international treaties and agreements negotiated by the Department of State. Generally, treaty terms allow the DON continued use of these properties until the treaties expire. There are no other known restrictions on General PP&E.

Military Equipment.

In accordance with the requirements of SFFAS No. 23, "Eliminating the Category National Defense Property, Plant, and Equipment," beginning in FY 2003, DON capitalized military equipment into General PP&E at estimated historical cost using information obtained from the Bureau of Economic Analysis (BEA). In FY 2006, the

DON began valuing these assets using actual expenditure data and moved away from the BEA cost-estimation methodology. The move from the BEA model was made at 3rd Quarter, FY 2006, thus FY 2007 values for military equipment above are based on actual data, however FY 2006 comparative balances for 1st and 2nd quarters were not restated.

Property in the Possession of Contractors.

The value of DON's General PP&E real property in the possession of contractors is included in the values reported above for the Major Asset Classes of Land and Buildings, Structures, and Facilities. The value of General PP&E personal property (Major Asset Classes of Software and Equipment) does not include all of the General PP&E above DoD capitalization threshold in the possession of contractors. The net book amount of such property is immaterial in relation to the total General PP&E net book value. Per an approved strategy with Office of Management Budget (OMB), Government Accountability Office (GAO) and DoD Inspector General, DoD is developing new policies and a contractor reporting process to capture General PP&E information for future reporting purposes for compliance with Federal General Accepted Accounting Principles (GAAP).

The DON does not have any General PP&E for which the acquisition cost is unknown.

Heritage Assets and Stewardship Land.

Relationship of Heritage Assets to Department of the Navy's (DON's) Mission.

The overall mission of DON is to control and maintain freedom of the seas; project power beyond the sea; and influence events and advance U.S. interests across the full spectrum of military operations. As this mission has been executed DON has become a large-scale owner of historic buildings, structures, districts, archeological sites and artifacts, ships, aircraft, and other cultural resources. Protection of these components of the nation's heritage is an essential part of DON's mission; DON is committed to responsible cultural resources stewardship.

Stewardship Policies for Heritage Assets and Description of Each Major Category of Heritage Assets.

The overall policy for DON's stewardship policies for heritage assets is contained in the Secretary of the Navy Instruction 4000.35A, "DON Cultural Resources Program."

- Heritage Assets are items that are unique for one of more of the following reasons: (1) historical or natural significance; (2) cultural, educational or artistic importance; or (3) significant architectural characteristics. The process used to define items as having heritage significance varies between categories and type of assets being evaluated. Subject matter experts, including historians and curators, play a significant role in the definition process. In all cases, a myriad of federal statutes, regulations, and other guidelines mandate heritage significance or provide guidance in its determination.
- Preservation considerations are incorporated into routine DON management of historic buildings, structures, districts, sites, ships, aircraft and other cultural resources. Compliance with cultural resources protection requirements is incorporated as appropriate into other DON planning processes, including but not limited to master planning, environmental planning, budgeting/programming, and facilities management. When functionally appropriate and economically prudent,

DON gives preference to the rehabilitation or adaptive use of historic properties over new construction or leasing.

- The appropriate consultation is initiated with State Historic Preservation Officers, Tribal Historic Preservation Officers, Advisory Council on Historic Preservation, Native Americans, Native Hawaiians, and other interested agencies and publics whenever DON conducts or supports undertakings that may affect any National Register resource.
- DON designated staff maintain an awareness of specific legal obligations regarding its management of cultural resources such as establishing a program to locate and inventory all cultural resources under DON control and to evaluate them against National Register eligibility criteria for possible nomination to the National Register.
- Cultural resources management, including consultation, takes place at the lowest appropriate level in the chain of command.
- Archeological sites under the control of DON are excavated only to the extent required for evaluation and identification, unless scientific or programmatic considerations, or concerns about the integrity or security of a site, make more extensive excavation necessary or advisable.
- Archaeological Sites are locations that contain the remains of past human activity of various sorts that are listed or eligible for listing on the National Register of Historic Places.
- Buildings and Structures are listed as or determined eligible for listing on the National Register of Historic Places, including Multi-Use Heritage Assets.
- Cemeteries are government owned burial grounds on which gravesites of prominent historical figures may be located in addition to other gravesites.
- Major Collections include archeological artifacts that are maintained and inventoried by cubic feet, archival items that are maintained and inventoried by linear feet, and artwork and historical artifacts that are maintained and inventoried by individual items.
- Monuments and Memorials are those items that are built or placed to commemorate a person or event, preserve the memory of a historical event, or is shown or maintained for its historical interest.

Relationship of Stewardship Land to Department of the Navy's (DON's) Mission.

The overall mission of DON is to control and maintain freedom of the seas; project power beyond the sea; and influence events and advance U.S. interests across the full spectrum of military operations. As this mission has been executed DON has accumulated several hundred installations throughout the United States. These installations provide the capability to organize, train, and equip the DON to perform its mission.

Stewardship Land Policy.

The DON Stewardship Land policy is the same as that which DON maintains over all land and installations. The DON strives to be a responsible steward of the land and to maintain it in a way that both protects human health and the environment and allows training and support of fleet readiness. The DON works to develop and improve partnerships with the communities in which its installations are located, the federal regulatory agencies such as U.S. Environmental Protection Agency, state regulatory

agencies, and within the military services by sharing lessons learned and transfer of technologies.

Stewardship Land is defined as the type of land not acquired for or in connection with land, on which General Plant and Equipment is located. For DON, Stewardship Land includes land acquired through public domain, land set aside, and donated land. Some of this land is used as a buffer around the perimeter of DON installations and may include, but is not limited to, grazing lands and forestry maintenance areas.

The DON did not receive any stewardship land by donation or devise during 1st Quarter, FY 2007. The DON's heritage asset system does not identify methodology of obtaining heritage assets nor does it maintain costs, therefore we are unable to determine the number and value heritage assets that may have been obtained through donation or devise during 1st Quarter, FY 2007.

Other Disclosures

Real Property.

The Internet Naval Facility Asset Database Store (iNFADS) provides real property values for financial statement reporting purposes.

Leasehold Improvements.

The DON's iNFADS real property system does not track leasehold improvements as a separate component of a building's total value. However, DON collects this information through a data call and began recognizing the leasehold improvement values beginning in FY 2004.

Software.

The DON uses the Defense Property Accountability System (DPAS) to capture costs associated with Internal Use Software.

Construction-in-Progress (CIP).

The CIP balances were obtained from the Facilities Information System (FIS). The value of construction that is performed for the benefit of external customers, such as Air Force and several of the Defense Agencies is provided to Air Force, the Defense Agencies, and the Defense Finance and Accounting Service. The value of construction for external customers is not included in DON CIP balances except in cases where the DON will be the preponderant user of the facility. Since preponderant user policy does not apply to medical facilities, the CIP value is included in the DON's CIP.

Preponderant Use.

Per the DoD FMR, Volume 4, Chapter 6, legal ownership is not always the determinant factor when establishing which DoD Component recognizes a particular General PP&E asset for accounting and reporting purposes. If the following four criteria are met, the preponderant user should report the property regardless of legal ownership or funding source:

- The asset embodies a probable future benefit;
- The DoD Component that reports the asset obtains the benefit and controls access to the benefit inherent in the asset;

- The transaction or event giving the Component the right to, and control over, the benefit has already occurred; and
- The predominantly used assets, taken as a whole, are material to the Component's financial statements.

In accordance with an Office of the Under Secretary of Defense (Comptroller) memorandum of July 5, 2005, the military departments and DoD activities meeting the criteria of preponderant user are responsible for reconciliation of preponderant use property. A milestone of the DON Financial Improvement Plan (FIP) is to reconcile with DoD activities and to ensure that the DON real property database recognizes the preponderant user. As these efforts are completed and reconciliations are documented, DON General Fund will make the adjustments to the General Property, Plant and Equipment line.

Assets Under Capital Lease

As of December 31	2007	2006
1. Entity as Lessee, Assets Under Capital Lease		
A. Land and Buildings	\$ 0.00	\$ 0.00
B. Equipment	114,695.76	114,695.76
C. Accumulated Amortization	(13,381.17)	(1,911.60)
D. Total Capital Leases	\$ 101,314.59	\$ 112,784.16

2. Description of Lease Arrangements

Currently only one equipment lease is reported through the data call process. The DON Financial Improvement Program recently completed a survey of major commands to determine if additional capital leases existed. After the survey responses are reviewed, it is expected that improvements to the entire reporting process will be implemented. Expected completion date of this effort is FY 2008.

Note 11.	Liabilities Not Covered by Budgetary Resources
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As of December 31	2007	2006
1. Intragovernmental Liabilities		
A. Accounts Payable	\$ 0.00	\$ 0.00
B. Debt	0.00	0.00
C. Other	3,644,870,629.65	3,493,267,676.41
D. Total Intragovernmental Liabilities	\$ 3,644,870,629.65	\$ 3,493,267,676.41
2. Nonfederal Liabilities		
A. Accounts Payable	\$ 37,298,941.02	\$ 28,048,894.52
B. Military Retirement and Other Federal Employment Benefits	1,513,643,894.37	1,532,819,451.36
C. Environmental Liabilities	17,587,053,155.80	17,534,734,637.25
D. Other Liabilities	4,572,369,270.63	3,833,473,686.51
E. Total Nonfederal Liabilities	\$ 23,710,365,261.82	\$ 22,929,076,669.64
3. Total Liabilities Not Covered by Budgetary Resources	\$ 27,355,235,891.47	\$ 26,422,344,346.05
4. Total Liabilities Covered by Budgetary Resources	\$ 5,205,056,007.52	\$ 4,585,023,749.60
5. Total Liabilities	\$ 32,560,291,898.99	\$ 31,007,368,095.65

An explanation of fluctuations and abnormalities for Liabilities Covered by Budgetary Resources is included in the specific note for that liability. See Notes 12 through 17.

Definitions

- Liabilities Covered by Budgetary Resources are those that are incurred by the reporting entity, which are covered by realized budgetary resources as of the balance sheet date. Budgetary resources encompass not only new budget authority, but also other resources available to cover liabilities for specified purposes in a given year.
- Realized budgetary resources include:
 - (1) New budget authority
 - (2) Spending authority from offsetting collections (credited to an appropriation or fund account)
 - (3) Recoveries of unexpired budget authority through downward adjustments of prior year obligations
 - (4) Unobligated balances of budgetary resources at the beginning of the year or net transfers of prior year balances during the year, and
 - (5) Permanent indefinite appropriations or borrowing authority, which have been enacted and signed into law as of the balance sheet date, provided that the resources may be apportioned by OMB without further action by the Congress or without a contingency first having to be met.

- Conversely, Liabilities Not Covered by Budgetary Resources are those liabilities which are not considered covered by realized budgetary resources as of the balance sheet date. Budgetary Authority to satisfy these liabilities is expected to be provided in a future Defense Appropriations Act. When that future budgetary authority is provided, these respective liabilities will be recorded as Covered by Budgetary Resources with an associated funded expense. To prevent overstatement on the Balance Sheet and Statement of Net Cost, the liabilities previously recorded as Not Covered by Budgetary Resources and the associated unfunded expenses are reversed.

Other Disclosures

Military Retirement Benefits and Other Employment Related Actuarial Liabilities (Line 2.B) includes \$1.5 billion in Federal Employee’s Compensation Act (FECA) actuarial liabilities.

Intragovernmental Liabilities – Other (Not covered by Budgetary Resources) (Line 1.C) includes the following:

	<u>As of December 31, 2006</u>
<i>(Amounts in thousands)</i>	
FECA due to	
Department of Labor (DoL)	\$398,988
Unemployment	74,969
Liabilities to Treasury	<u>3,170,914</u>
Total	<u><u>\$3,644,871</u></u>

Liabilities to Treasury.

The primary component of the \$3.2 billion liability to Treasury is a principal amount of \$1.3 billion, representing advance payments made to contractors and \$1.3 billion in associated accrued interest which remains in litigation. This amount in litigation is reported as an unfunded liability to Department of the Treasury. Collections on this debt will be due and payable to Treasury as the original appropriation is in a cancelled status. See Notes 2 and 5 for further disclosure.

Nonfederal Liabilities – Other (Not covered by Budgetary Resources) (Line 2.D) includes the following:

	<u>As of December 31, 2006</u>
<i>(Amounts in thousands)</i>	
Annual Leave	\$2,214,428
Military Equipment – Non-nuclear Non	
Environmental Disposal Liabilities	272,309
Disposal Liabilities for Excess/Obsolete Structures	631,835
Contract Incentives	70,448
Estimated Contingent Legal Liability	1,379,349
Other	4,000
Total	<u><u>\$4,572,369</u></u>

Note 12.	Accounts Payable
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As of December 31	2007			2006
	Accounts Payable	Interest, Penalties, and Administrative Fees	Total	Total
1. Intragovernmental Payables	\$ 1,100,192,881.03	\$ N/A	\$ 1,100,192,881.03	\$ 988,086,805.74
2. Nonfederal Payables (to the Public)	872,169,644.79	0.00	872,169,644.79	1,211,637,345.42
3. Total	\$ 1,972,362,525.82	\$ 0.00	\$ 1,972,362,525.82	\$ 2,199,724,151.16

4. Other Information Related to Accounts Payable

Fluctuation and Abnormalities

Intragovernmental Payables.

The DON reported an increase of \$112.1 million, 11%, in Intragovernmental Payables, 1st Quarter, FY 2007 compared with 1st Quarter, FY 2006. The trading partner process largely drives the balances in Intragovernmental payables. Upon receipt of accounts receivable data reported by our trading partners, DON records compensating accounts payable. For agencies that do not provide account receivable data in a timely manner, DON records accounts payable estimates based upon historical data. The total Level One (business conducted with other non DoD Federal Agencies) Intragovernmental accounts payable amount recorded in 1st Quarter, FY 2007 was \$425.3 million. The Level One estimate is updated quarterly.

The majority of the increase in Intragovernmental payables was with:

- Department of Energy (DOE) (Level One) for \$46.3 million. The Naval Sea Systems Command has reimbursable agreements with DOE related to the nuclear power program.
- Air Force General Fund (Level 2) for \$24.0 million. The DON has provided reimbursable funding to the Air Force for classified programs in the area of aircraft procurement and research, development, test, and evaluation
- United States Postal Service (USPS) for \$11.3 million. No accrual for payables to USPS was recognized in 1st Quarter, FY 2006.

Nonfederal Payables.

Nonfederal payables decreased \$339.5 million or 28%, 1st Quarter, FY 2007 compared to 1st Quarter, FY 2006. In 1st Quarter, FY 2007, DON implemented guidance issued by the Office of the Under Secretary of Defense (Comptroller) to allocate undistributed disbursements to accounts payable. The amount allocated to nonfederal payables in 1st Quarter, FY 2007 was \$578.6 million. The application of undistributed disbursements reduces accounts payable balances. Offsetting this decrease was an increase in nonfederal payables in the Navy procurement accounts of \$235.9 million; Aircraft Procurement, specifically the F-A 18 E/F "Hornet" program accounted for the majority of this increase.

Definitions

Intragovernmental Accounts Payable.

This line 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.

Nonfederal Payables (to the Public).

This line represents amounts owed to nonfederal government entities and individuals.

Undistributed Disbursements.

Undistributed Disbursements are the difference between disbursements recorded at the detailed level to a specific obligation or payable in the activity field records versus those reported by the Department of the Treasury. This should agree with the undistributed disbursements reported on monthly accounting reports. Generally, timing issues between systems cause undistributed disbursements. In-transit disbursements are payments that have been made by other agencies, entities, or systems that have not yet been recorded in DON's accounting records. For 1st Quarter, FY 2007, total supported undistributed disbursements were \$1.1 billion.

Intragovernmental Elimination.

Regarding interagency purchases; DON accounting systems do not capture trading partner data at the transaction level in a manner that facilitates trading partner aggregations. Therefore, DON was unable to fully reconcile intragovernmental accounts payable to the related intragovernmental accounts receivable on another agencies' records that generated the payable.

Therefore, DoD summary level seller accounts receivables were compared to DON's accounts payable. An adjustment was posted to DON's accounts payable based on the comparison with the accounts receivable of DoD Components providing goods and services to DON.

The DoD intends to develop long-term systems improvements that will include sufficient up-front edits and controls to eliminate the need for after-the-fact reconciliations. The volume of intragovernmental transactions is so large that after-the-fact reconciliation cannot be accomplished with existing or foreseeable resources. In the interim, DFAS is leading an effort to identify alternative means of capturing and recognizing buyer side trading partner data.

Other Disclosures

Payables, more than any other liability, are subject to the vagaries of the business cycle, contract terms, the timing of the receipt of invoices for goods and services, and the subsequent liquidation of those invoices; thus variances from the previous reporting period are not uncommon. Payables are temporary liabilities and are expected to be liquidated within the next payment cycle.

Judgment Fund Liabilities.

The DON must reimburse the Department of the Treasury for payments made from the Judgment Fund on its behalf. These payments are a result of claims being resolved under the Contracts Dispute Act. In addition, the Notification of Federal Antidiscrimination and Retaliatory Act (No FEAR) was implemented on October 1, 2003. This law requires all agencies to reimburse the Judgment Fund for cases covered by the No FEAR Act. For 1st Quarter, FY 2007, DON reported \$288.4 thousand for No FEAR Act liabilities.

Note 13.	Debt
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As of December 31	2007			2006	
	Beginning Balance	Net Borrowing	Ending Balance	Net Borrowing	Ending Balance
1. Agency Debt (Intragovernmental)					
A. Debt to the Treasury	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
B. Debt to the Federal Financing Bank	0.00	0.00	0.00	0.00	0.00
C. Total Agency Debt	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
2. Total Debt	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00

Not Applicable

Note 14.	Environmental Liabilities and Disposal Liabilities
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As of December 31	2007			2006
	Current Liability	Noncurrent Liability	Total	Total
1. Environmental Liabilities-- Nonfederal				
A. Accrued Environmental Restoration Liabilities				
1. Active Installations—Installation Restoration Program (IRP) and Building Demolition and Debris Removal (BD/DR)	\$ 398,226,000.00	\$ 1,940,908,000.00	\$ 2,339,134,000.00	\$ 2,618,652,000.00
2. Active Installations—Military Munitions Response Program (MMRP)	60,153,000.00	615,148,000.00	675,301,000.00	559,651,000.00
3. Formerly Used Defense Sites—IRP and BD/DR	0.00	0.00	0.00	0.00
4. Formerly Used Defense Sites--MMRP	0.00	0.00	0.00	0.00
B. Other Accrued Environmental Liabilities—Active Installations				
1. Environmental Corrective Action	0.00	44,513,101.00	44,513,101.00	29,861,342.00
2. Environmental Closure Requirements	0.00	772,812,573.00	772,812,573.00	195,176,594.00
3. Environmental Response at Operational Ranges	0.00	41,816,486.00	41,816,486.00	0.00
4. Other	0.00	2,616,615.00	2,616,615.00	0.00
C. Base Realignment and Closure (BRAC)				
1. Installation Restoration Program	202,657,845.00	1,596,859,486.00	1,799,517,331.00	1,079,256,000.00
2. Military Munitions Response Program	2,922,275.00	101,892,930.00	104,815,205.00	65,236,000.00
3. Environmental Corrective Action / Closure Requirements	11,065,682.00	42,255,914.00	53,321,596.00	0.00
4. Other	0.00	0.00	0.00	0.00
D. Environmental Disposal for Weapons Systems Programs				
1. Nuclear Powered Aircraft Carriers	0.00	5,671,610,721.38	5,671,610,721.38	6,742,200,000.00
2. Nuclear Powered Submarines	399,503,082.51	3,293,877,904.24	3,693,380,986.75	6,195,500,000.00
3. Other Nuclear Powered Ships	227,317,935.00	66,658,995.00	293,976,930.00	332,300,000.00
4. Other National Defense Weapons Systems	87,230,243.50	147,610,643.18	234,840,886.68	440,711,701.25
5. Chemical Weapons Disposal Program	0.00	0.00	0.00	0.00
6. Other	0.00	3,237,406,105.00	3,237,406,105.00	0.00
2. Total Environmental Liabilities	\$ 1,389,076,063.01	\$ 17,575,987,473.80	\$ 18,965,063,536.81	\$ 18,258,544,637.25

Other Category Disclosure Comparative

	2007	2006
(Amounts in thousands)		
Other Accrued Environmental Costs- Other	\$2,617	\$0
Total	\$2,617	\$0
Base Realignment and Closure- Other	\$0	\$0
Total	\$0	\$0
Environmental Disposal for Weapon Systems Programs- Other	\$3,237,406	\$0
Total	\$3,237,406	\$0

The “Other” type of environmental liabilities under Other Accrued Environmental Costs (Line 1.B.4.) represents an environmental estimate for disposal of Polychlorinated Biphenyls (PCBs) transformers located at various Navy installations. Under the Department of the Navy (DON) Financial Improvement Program, during FY 2006 Navy completed a fence to fence survey of all installations and 1st Quarter, FY 2007 is the first time reporting the results of that effort. Therefore, there is no comparative 1st Quarter, FY 2006 data.

The “Other” type of environmental liabilities under Disposal for Weapons Systems Programs (Line 1.D.6) represents Spent Nuclear Fuel. Per a Government Accountability Office audit recommendation and completion of a milestone of the DON Financial Improvement Program, DON began recognizing an estimated environmental disposal liability associated with Spent Nuclear Fuel during 3rd Quarter, FY 2006. Therefore, there is no comparative 1st Quarter, FY 2006 data. Spent Nuclear Fuel is the used fuel that is removed from the nuclear reactors of nuclear powered ships and submarines. The estimate includes shipping, processing, and storing the spent nuclear fuel.

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

Other Information Related to Environmental Liabilities

1. Applicable Laws and Regulations of Cleanup Requirements

The following is a summary of significant laws that affect DON’s conduct of environmental policy and regulations.

The National Environmental Policy Act (NEPA) of 1970 requires DON to consider the environmental impacts of proposed actions in the decision making process. Per DON regulations, the action proponent will determine the level or amount of NEPA documentation required. The Resource Conservation and Recovery Act (RCRA) of 1976 as amended by the Hazardous and Solid Waste Amendments (HSWA) of 1984, was the first comprehensive federal effort to deal with safe disposal of all types of hazardous wastes, and provides for “cradle to grave” tracking of hazardous wastes. Permits are required for treatment, storage or disposal. Requirements for underground storage tanks (USTs) are also contained in RCRA.

The Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA), commonly referred to as the Superfund legislation, provided Federal agencies authority to respond to the release or the substantial threat of release of hazardous substances into the environment. CERCLA was amended several times; one of the

amendments was the Superfund Amendments and Reauthorization Act (SARA) of 1986. This amendment established procedures to ensure that actual or threatened hazardous substance releases have proper responses. The procedures address reporting, investigations, remedy selection, and responsive provisions. Another amendment to CERCLA was the Community Environmental Response Facilitation Act (CERF) of 1992. The DON must identify real property on each facility that is not contaminated and that offers the greatest opportunity for expedited reuse and redevelopment. When property is transferred DON is still responsible for any remediation or corrective action or any response action found to be necessary after the transfer.

The Clean Water Act (CWA) of 1977, Section 405 Disposal of Sewage Sludge, amended the Federal Water Pollution Control Act. The purpose of CWA is to restore and maintain the integrity of the nation's waters and the implementing regulations established closure and post closure requirements for sewage sludge disposal. To help protect the nation's drinking water supply, including underground injections through a permitting scheme, is the purpose of the Safe Drinking Water Act of 1974 (Well Head Protection Areas). The Clean Air Act (CAA) of 1990 established standards/limitations to prevent and control air pollutant discharges that could harm human health and natural resources. Requirements ensure that units can no longer operate when they are shut down. Finally, the Toxic Substances Control Act (TSCA) of 1976 was implemented to understand the health risks of chemical substances by developing production and health risk data from the manufacturers. Based on the data, the Environmental Protection Agency has promulgated regulations for specific chemicals. The control of polychlorinated biphenyls (PCBs) is a good example. The control addresses spill cleanup and removal and disposal of units containing PCBs.

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

2. Methods for Assigning Total Cleanup Costs to Current Operating Periods

Accrued Environmental Restoration (Defense Environmental Restoration Program (DERP) Funded Liabilities.

Active Installations – Environmental Restoration (ER): Accrued restoration (cleanup) liabilities represent the cost to correct past environmental areas that are funded under the Defense Environmental Restoration Program in accordance with “Management Guidance for DERP,” and “Environmental and Non-Environmental Liabilities,” Chapter 13 of Volume 4 of Department of Defense Financial Management Regulation (DoD FMR). These liabilities relate to Plant, Property and Equipment, including acquired land and Stewardship Land, as those major asset categories are described in Chapter 6 of Volume 4 of DoD FMR. Environmental restoration activities may be conducted at operating installations, at Formerly Used Defense Sites (FUDS), and at Closed, Transferred, and Transferring Ranges. Environmental restoration measurements involve the use of cost estimates that consider, on

a current cost basis, the anticipated costs of the level of effort required to affect the restoration, as well as applicable legal and/or regulatory requirements. Program management and support costs are included in the estimates. The estimates are based on DON's cost-to-complete (CTC) module of the Normalization of Data System (NORM). Verification, validation, and accreditation of CTC module was completed in FY 2002. Such cost estimates are based on the current technology available. The DON, as the baseline for environmental restoration (cleanup) liability measurement (i.e., the current cost to acquire the required services), used the site inventory and estimated cost data prepared for DERP report to the Congress. The Accrued Environmental Restoration (Cleanup) Costs do not include the costs of environmental compliance; pollution prevention, conservation activities, contamination or spills associated with current operations or treaty obligations, all of which are accounted for as part of ongoing operations. The DON Environmental Restoration (ER, N) Program includes 3,704 clean-up sites at active installations while those installations covered by Base Realignment and Closure (BRAC) funding include 1,148 clean-up sites. The Marine Corps is included in these programs. In addition, the DON Environmental Corrective Action Program at BRAC installations included 610 sites.

Active Installations – Military Munitions Response Program: This area represents the environmental liabilities associated with the identification, investigation and removal and remedial actions to address environmental contamination at ranges that were closed prior to September 30, 2002. The contamination may include munitions, chemical residues from military munitions and munitions scrap at ranges on active installations that pose a threat to human health or the environment. The amount reported is the portion of the liability that can be estimated based on site level investigations and characterizations. The estimate produced is based on site-specific information and use of cost models validated in accordance with DoD Instruction 5000.61, "DoD Modeling and Simulation, Verification, Validation, and Accreditation" of May 2003. Total liabilities (cost-to-complete) are not estimated until there is sufficient site-specific data available to estimate the total liability. However, DON uses the cost of the study as the estimate until the study is completed. Beginning in FY 2001, DON began an inventory of closed ranges and transferring ranges under the Military Munitions Response Program (MMRP) or Unexploded Ordnance (UXO) program. The inventory was completed September 2002 and currently contains 221 closed ranges at active installations and 28 sites (transferring ranges) at BRAC installations.

Environmental Disposal for Weapons Systems Programs – This area represents environmental liabilities associated with the Nuclear Powered Aircraft Carriers and Submarines, Other Nuclear Powered Ships, Conventional Ships, and Spent Nuclear Fuel. During FY 2006, under DON Financial Improvement Program, DON completed a review of the estimating methodology for determining the cost for disposal of ships and submarines. This review resulted in an environmental and nonenvironmental liability estimate that more accurately reflects the true costs of disposal. The estimating methodology is based on average cost per class of ship rather than an average applied to all ships regardless of class. This change in estimating methodology was implemented during 3rd Quarter, FY 2006 and resulted in an overall decrease in the estimated environmental liability for nuclear powered ships and submarines and conventional ships. However this decrease was offset by recognizing an estimated liability for spent nuclear fuel beginning in 3rd Quarter, FY 2006.

3. Description of the Types of Environmental Liabilities and Disposal Liabilities

Accrued Environmental Restoration (DERP Funded) Cost Liabilities.

The DON Environmental Restoration includes those sites that have been identified as legacy cleanup sites. For 1st Quarter, FY 2007, DON estimated and reported \$3.0 billion for environmental restoration liabilities. This amount is comprised of \$2.3 billion in Active Installations - Environmental Restoration (ER) liabilities and \$675.3 million in Active Installations – ER for Closed Ranges, liabilities, which represents UXO. The DoD FMR, Volume 6B, Chapter 10 requires that “any estimate produced must be based on site specific information and use cost models validated in accordance with DoD Instruction 5000.61.” The DON is supporting this requirement by continuing to validate its range inventory as well as by pursuing the process of obtaining valid cost estimates for each range.

Other Accrued Environmental Costs (Non-DERP funds).

The DON defines Non-DERP environmental units as those sites associated with on-going operations such as solid waste management unit cleanup, landfill closure, permitted facilities, removal, replacement, retro fill, and/or disposal of polychlorinated biphenyls (PCBs) transformers, underground storage tank remedial investigation and closure. As part of the DON Financial Improvement Program efforts, the Navy completed surveying, identifying, and estimating, Non-DERP units and began recognizing the estimated environmental liability 1st Quarter, FY 2007. For 1st Quarter, FY 2007, the total Other Accrued Environmental Liabilities is \$861.8 million. Of the total, the Navy portion is \$635.3 million while the Marine Corps portion is \$226.5 million.

Base Realignment and Closure (BRAC).

BRAC environmental sites are environmental sites at DON installations that are or will be closed under the congressionally mandated Base Realignment and Closure process. For 1st Quarter, FY 2007, DON estimated and reported \$2.0 billion for BRAC funded environmental restoration liabilities. This amount includes \$1.8 billion for environmental restoration (ER) program, \$104.8 million for Military Munitions Response Program, and \$53.3 million for corrective action and closure requirements. Military Munitions Response Program includes military munitions, chemical residues from military munitions, and munitions scrap at locations on or associated on or associated with a military range on a BRAC installation.

Environmental Disposal for Weapons Systems Programs.

Environmental Disposal for Weapon Systems are those estimates associated with the environmental disposal costs for DON nuclear weapons programs that includes Nuclear Powered Aircraft Carriers and Submarines and Other Nuclear Powered Ships, Conventional Ships, and Spent Nuclear Fuel. The DON reported an environmental disposal liability for Weapons Systems Programs of \$13.1 billion in 1st Quarter, FY 2007. This amount includes nuclear powered aircraft carriers of \$5.7 billion, nuclear powered submarines of \$3.7 billion, other nuclear powered ships of \$294.0 million, other national defense weapons systems (conventional ships) of \$234.8 million, and spent nuclear fuel (Other) of \$3.2 billion.

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

For both current and prior periods, the changes due to price growth (inflation) and increases in labor rates and materials have been offset by a change in the estimating methodology for weapons systems. This change in estimating methodology resulted in an overall decrease in

the estimated environmental disposal liability. However, this decrease was offset by recognizing an estimated liability for spent nuclear fuel beginning with 3rd Quarter, FY 2006. Currently, there are no indications that any of the environmental liabilities for any category will be adjusted due to deflation. As of 1st Quarter, FY 2007, there are no changes to the environmental liability estimates due to changes in laws, regulations, and in agreements with regulatory agencies. The DON does not have any estimates that were changed due to advances in technology.

5. Description of the Level of Uncertainty Regarding the Accounting Estimates used to calculate the Reported Environmental Liabilities

The environmental liabilities for DON are based on accounting estimates that require certain judgments and assumptions that DON believes are reasonable based upon information available to us at the time of calculating the estimates. The actual results may vary materially from the accounting estimates if agreements with regulatory agencies require remediation to a different degree than anticipated when calculating the estimates. The liabilities can be further impacted if further investigation of the environmental sites discloses contamination different than known at the time of the estimates.

Overall, DON has a reasonable level of confidence in the estimates recognized on the face of the financial statements. This reasonable level of confidence in the estimates is based on the fact that the estimates for DERP/BRAC programs are based on the Cost to Complete (CTC) module of the NORM System. A verification, validation, and accreditation was completed by a third party for CTC module of NORM, while the environmental program managers continue to validate the data. For the Weapons systems, the environmental program managers base their environmental disposal estimates on actual costs for similar projects. A change in the overall methodology in weapons systems reflects a more accurate estimate of what it will cost to dispose of the weapons systems. Given the fact that the planned date for opening the Department of Energy's (DOE) planned waste repository has been delayed, there is uncertainty associated with the estimate for spent nuclear fuel. As DOE's plans are solidified, DON's estimates for spent nuclear fuel will change accordingly.

The DON believes that the current environmental liabilities for BRAC are reasonable, based upon information available at the time in calculating the estimates. However, as the FY 2005 BRAC closure activities are implemented over the next several fiscal years, the actual results may vary materially from the accounting required estimates. The variance will depend on additional information gleaned from planned or ongoing studies of the extent and concentration of site environmental contamination. In addition to the possibility of the estimates changing on current identified sites, DON may incur additional environmental cleanup and restoration costs if new sites are identified as BRAC activities are implemented.

The DON believes that the environmental liabilities for Other Accrued Environmental Liabilities (Non-DERP) for 1st Quarter, FY 2007 are reasonable, based upon the information available at the time in calculating the estimates and completing the fence to fence survey. However, as internal controls are implemented to sustain this effort, changes to some of the estimates could occur. In addition to the possibility of some of the estimates changing for the current list of identified units, DON may incur additional units and changes to estimates as the inventory of units are reviewed annually.

Environmental Disclosures

As of December 31	2007	2006
A. Amount of operating and capital expenditures used to remediate legacy waste. Legacy wastes are the remediation efforts covered by IRP, MMRP, and BD/DR regardless of funding source.	90,992,088.00	0.00
B. The unrecognized portion of the estimated total cleanup costs associated with general property, plant, and equipment.	1,456,473,688.41	0.00
C. The estimated cleanup costs associated with general property, plant, and equipment placed into service during each fiscal year.	47,463,656.45	0.00
D. Changes in total cleanup costs due to changes in laws, regulations, and/or technology.	0.00	0.00
E. Portion of the changes in estimated costs due to changes in laws and technology that is related to prior periods.	0.00	0.00

Explanations

Line A. For 1st Quarter, FY 2007, of the total \$91.0 million, \$30.5 million is related to DERP while \$60.5 million is related to BRAC corrective action and restoration programs. Since this disclosure schedule was not a requirement until 3rd Quarter, FY 2006, data is not available for comparison purposes.

Line B. The unrecognized portion of the estimated total cleanup costs is associated with Nuclear Powered Carriers and Submarines, Conventional Ships, Spent Nuclear Fuel, and Non-DERP. Of the total \$1.5 billion, \$36.1 million is associated with conventional ships while the remainder, \$1.4 billion is associated with Nuclear Powered Carriers and Submarines and Spent Nuclear Fuel and \$57.2 million is associated with Non-DERP. Since this disclosure schedule was not a requirement until 3rd Quarter, FY 2006, data is not available for comparison purposes.

Line C. The estimated cleanup costs associated with general property, plant, and equipment placed into service during 1st Quarter FY, 2007 is \$47.5 million. This amount is associated with environmental disposal of weapons systems programs. Since this disclosure schedule was not a requirement until 3rd Quarter, FY 2006, data is not available for comparison purposes.

Lines D. and E. Through our quarterly data call process, for 1st Quarter, FY 2007, DON determined that there are no changes to the environmental liability estimates due to changes in laws, regulations, in agreements with regulatory agencies, and advances in technology. Since this disclosure schedule was not a requirement until 3rd Quarter, FY 2006, data is not available for comparison purposes.

Note 15.	Other Liabilities
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As of December 31	2007			2006
	Current Liability	Noncurrent Liability	Total	Total
1. Intragovernmental				
A. Advances from Others	\$ 0.00	\$ 0.00	\$ 0.00	\$ 31,305,082.00
B. Deposit Funds and Suspense Account Liabilities	339,574,280.36	0.00	339,574,280.36	226,574,988.60
C. Disbursing Officer Cash	184,346,019.96	0.00	184,346,019.96	262,715,377.03
D. Judgment Fund Liabilities	0.00	0.00	0.00	0.00
E. FECA Reimbursement to the Department of Labor	482,109,305.96	154,669,745.37	636,779,051.33	604,097,516.61
F. Other Liabilities	3,267,045,900.13	0.00	3,267,045,900.13	3,160,353,625.21
G. Total Intragovernmental Other Liabilities	\$ 4,273,075,506.41	\$ 154,669,745.37	\$ 4,427,745,251.78	\$ 4,285,046,589.45
2. Nonfederal				
A. Accrued Funded Payroll and Benefits	\$ 283,576,505.66	\$ 0.00	\$ 283,576,505.66	\$ 481,968,098.50
B. Advances from Others	229,366,515.00	0.00	229,366,515.00	218,289,158.09
C. Deferred Credits	0.00	0.00	0.00	0.00
D. Deposit Funds and Suspense Accounts	32,326,053.35	0.00	32,326,053.35	0.00
E. Temporary Early Retirement Authority	0.00	0.00	0.00	0.00
F. Nonenvironmental Disposal Liabilities				
(1) Military Equipment (Nonnuclear)	12,781,508.59	272,308,825.24	285,090,333.83	1,447,741,242.15
(2) Excess/Obsolete Structures	59,412,000.00	626,206,000.00	685,618,000.00	235,897,000.00
(3) Conventional Munitions Disposal	0.00	0.00	0.00	0.00
G. Accrued Unfunded Annual Leave	2,214,428,499.18	0.00	2,214,428,499.18	2,179,200,169.93
H. Capital Lease Liability	128,076.93	0.00	128,076.93	112,784.16
I. Other Liabilities	173,594,923.69	1,777,347,782.57	1,950,942,706.26	168,024,813.60
J. Total Nonfederal Other Liabilities	\$ 3,005,614,082.40	\$ 2,675,862,607.81	\$ 5,681,476,690.21	\$ 4,731,233,266.43
3. Total Other Liabilities	\$ 7,278,689,588.81	\$ 2,830,532,353.18	\$ 10,109,221,941.99	\$ 9,016,279,855.88

Fluctuations and Abnormalities

Nonfederal Other Liabilities.

The DON reported an increase of \$950.2 million, 20% in Nonfederal Other Liabilities (Line 2.J.) 1st Quarter, FY 2007 when compared with 1st Quarter, FY 2006. The reason for this increase is DON implementing a new methodology for estimating contingent legal liabilities and reporting that estimate for the first time in 1st Quarter, FY 2007.

Other Disclosures

Due to the inherent uncertainties of litigation, lawyers generally refrain from expressing judgments as to outcomes except in those relatively few clear cases. As such, the likelihood of an unfavorable outcome or potential liability is provided as an overall assessment of all cases currently pending and not on an individual case basis. The likelihood of an unfavorable or potential liability was determined by using an average of the data from the preceding three years and the current year-to-date. The total dollar amount of the cases closed was divided by the total dollar amount claimed in those closed cases for each of the last three years plus current quarter which were then used to calculate the average. This average represents the percentage that has historically been paid on claims. It is based entirely on historical data. The merits of each individual case have not been taken into consideration. In response to a recommendation resulting from the Department of Defense, Inspector General audit, "Financial Management: DoD Process for Reporting Contingent Legal Liabilities," the DON is recognizing an estimate for contingent legal liabilities for the first time. Until sufficient historical data can be collected for the Navy Working Capital Fund, the estimate will consider all DON funding sources together. The estimate for those cases considered probably to result in an adverse judgment against DON is \$1.4 billion.

For FY 2006, the DON does not have any delinquent amounts due to the Department of Labor (DOL) for the FECA bill. The FY 2007 FECA bill is due to DOL 30 days after the appropriation bill is passed and signed.

Intragovernmental Other Liabilities:

Other Liabilities - Other (Line 1.F) includes the following:

	<i>As of</i> <u>December 31, 2006</u>
<i>(Amounts in thousands)</i>	
Liability to Treasury & Others	\$3,171,300
Unemployment Compensation	74,969
Employment Benefit	20,777
Total Intragovernmental Other Liabilities	<u>\$3,267,046</u>

Nonfederal Other Liabilities:

Other Liabilities - Other (Line 2.I) includes the following:

	<i>As of</i> <u>December 31, 2006</u>
<i>(Amounts in thousands)</i>	
Contract Holdbacks	\$152,867
Litigation Settlement	4,000
Employer Contributions (taxes)	636
Contract Incentives	70,448
Estimated Legal Contingent Liability	1,379,349
Outstanding Contract Financing Contingent Liability	343,643
Total Intragovernmental Other Liabilities	<u>\$1,950,943</u>

Contingent Liabilities balance includes \$343.6 million in estimated future contract financing payments that will be paid to the contractor upon delivery and Government acceptance of a satisfactory product. In accordance with contract terms, specific rights to the contractor's work vests with the Government when a specific type of contract financing payments is made, thereby protecting taxpayer funds in the event of contract nonperformance. These rights should not be misconstrued as the rights of ownership. The Department is under no obligation to pay the contractor for amounts greater than the amounts authorized in the contract until delivery and Government acceptance of a satisfactory product. Because it is probable that the contractor will complete its efforts and deliver a satisfactory product to the Department and the amount of potential future payments are estimable; the Department has recognized a contingent liability for estimated future payments, which are conditional pending delivery and Government acceptance of a satisfactory product.

Capital Lease Liability

As of December 31	2007				2006	
	Asset Category					
	Land and Buildings	Equipment	Other	Total	Total	
1. Future Payments Due						
A. 2007	\$ 0.00	\$ 128,076.93	\$ 0.00	\$ 128,076.93	\$	112,784.16
B. 2008	0.00	0.00	0.00	0.00	\$	0.00
C. 2009	0.00	0.00	0.00	0.00	\$	0.00
D. 2010	0.00	0.00	0.00	0.00	\$	0.00
E. 2011	0.00	0.00	0.00	0.00	\$	0.00
F. 2012	0.00	0.00	0.00	0.00	\$	0.00
G. After 5 Years	0.00	0.00	0.00	0.00	\$	0.00
<hr/>						
H. Total Future Lease Payments Due	\$ 0.00	\$ 128,076.93	\$ 0.00	\$ 128,076.93	\$	112,784.16
I. Less: Imputed Interest Executory Costs	0.00	0.00	0.00	0.00	\$	0.00
<hr/>						
J. Net Capital Lease Liability	\$ 0.00	\$ 128,076.93	\$ 0.00	\$ 128,076.93	\$	112,784.16
<hr/>						
2. Capital Lease Liabilities Covered by Budgetary Resources				\$ 128,076.93	\$	112,784.16
3. Capital Lease Liabilities Not Covered by Budgetary Resources				\$ 0.00	\$	0.00

4. Other Information Related to Capital Lease Liability

Note 16. Commitments and Contingencies**Legal Contingencies:**

The Department of the Navy (DON) is a party in various administrative proceedings and legal actions, with claims including environmental damage claims, equal opportunity matters, and contractual bid protests. These proceedings and actions arise in the normal course of operations and their ultimate disposition is unknown. The DON will accrue contingent liabilities for legal actions in those instances where the DON's Office of General Counsel considers an adverse decision probable and the amount of loss is measurable. In the event of an adverse judgment against the Government, some of the liabilities may be payable from the Judgment Fund. Others may be payable from DON's resources, either directly or by reimbursement to the Judgment Fund. The DON records Judgment Fund liabilities in Accounts Payable, which are detailed in Note 12.

For fiscal year 2006, the DON General Fund materiality threshold for reporting litigation, claims, or assessments was \$56.1 million. The materiality threshold for FY 2007 has not yet been set. Based on information contained in the FY 2006 Preliminary and Final Legal Representation Letters, management does not have sufficient reason to believe that it is likely that the Government will be liable for the amounts claimed in individual or aggregated cases.

The DON currently has sixteen cases; fifteen against the Navy and one against the United States Marine Corps, that meet the existing FY 2006 DON General Fund materiality threshold. DON legal counsel was unable to express an opinion concerning the likely outcome of these sixteen cases. This declaration is fully supported by the Preliminary and Final Legal Representation letters and the subsidiary management summary schedule.

Due to the inherent uncertainties of litigation, lawyers generally refrain from expressing judgments as to outcomes except in those relatively few clear cases. As such, the likelihood of an unfavorable outcome or potential liability is provided as an overall assessment of all cases currently pending and not on an individual case basis. The likelihood of an unfavorable or potential liability was determined by using an average of the data from the preceding three years and the current year-to-date. The total dollar amount of the cases closed was divided by the total dollar amount claimed in those closed cases for each of the last three years plus current quarter which were then used to calculate the average. This average represents the percentage that has historically been paid on claims. It is based entirely on historical data. The merits of each individual case have not been taken into consideration. In response to a recommendation resulting from the Department of Defense, Inspector General audit, "Financial Management: DoD Process for Reporting Contingent Legal Liabilities," the DON is recognizing an estimate for contingent legal liabilities for the first time. Until sufficient historical data can be collected for the Navy Working Capital Fund, the estimate will consider all DON funding sources together.

The estimate for those cases considered reasonably possible to result in an adverse judgment against DON is \$1.4 billion.

Other Commitments and Contingencies

The DON has recorded a contingent liability in the amount of \$37.3 million for obligations related to cancelled appropriations.

The DON has recorded a contingent liability in the amount of \$70.4 million for Contract Incentives.

Note 17.	Military Retirement and Other Federal Employment Benefits
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As of December 31	2007				2006
	Present Value of Benefits	Assumed Interest Rate (%)	(Less: Assets Available to Pay Benefits)	Unfunded Liability	Present Value of Benefits
1. Pension and Health Actuarial Benefits					
A. Military Retirement Pensions	\$ 0.00		\$ 0.00	\$ 0.00	\$ 0.00
B. Military Retirement Health Benefits	0.00		0.00	0.00	0.00
C. Military Medicare-Eligible Retiree Benefits	0.00		0.00	0.00	0.00
D. Total Pension and Health Actuarial Benefits	\$ 0.00		\$ 0.00	\$ 0.00	\$ 0.00
2. Other Actuarial Benefits					
A. FECA	\$ 1,513,643,894.37		\$ 0.00	\$ 1,513,643,894.37	\$ 1,532,819,451.36
B. Voluntary Separation Incentive Programs	0.00		0.00	0.00	0.00
C. DoD Education Benefits Fund	0.00		0.00	0.00	0.00
D. Total Other Actuarial Benefits	\$ 1,513,643,894.37		\$ 0.00	\$ 1,513,643,894.37	\$ 1,532,819,451.36
3. Other Federal Employment Benefits	\$ 0.00		\$ 0.00	\$ 0.00	\$ 0.00
4. Total Military Retirement and Other Federal Employment Benefits:	\$ 1,513,643,894.37		\$ 0.00	\$ 1,513,643,894.37	\$ 1,532,819,451.36

Actuarial Cost Method Used:

Assumptions:

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

Other Information Related to Military Retirement Benefits and Other Employment Related Actuarial Liabilities

Military Retirement Pensions.

The portion of the military retirement benefits actuarial liability applicable to DON is reported on the financial statements of the Military Retirement Fund (MRF).

Military Retirement Health Benefits.

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

Federal Employees' Compensation Act (FECA).

Actuarial Cost Method Used and Assumptions:

The DON's actuarial liability for workers' compensation benefits is developed by the

Department of Labor and provided to DON at the end of each fiscal year. The liability for future workers' compensation (FWC) benefits includes the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases, plus a component for incurred but not reported claims. The liability is determined using a method that utilizes historical benefit payment patterns related to a specific incurred period to predict the ultimate payments related to that period. Consistent with past practice, these projected annual benefit payments have been discounted to present value using the Office of Management and Budget's economic assumptions for 10-year Treasury notes and bonds. Interest rate assumptions utilized for discounting were as follows:

FY 2007

5.170 % in Year 1

5.313 % in Year 2 and thereafter

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

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

<u>CBY</u>	<u>COLA</u>	<u>CPIM</u>
2006	3.50%	4.00%
2007	3.13%	4.01%
2008	2.40%	4.01%
2009	2.40%	4.013%
2010+	2.43%	4.09%

The model's resulting projections were analyzed to insure that the estimates were reliable. The analysis was based on four tests: (1) a sensitive analysis of the model to economic assumptions, (2) a comparison of the percentage change in the liability amount by agency to the percentage change in the actual incremental payments, and (3) a comparison of the incremental paid losses per case (a measure of case-severity) in CBY 2006 to the average pattern observed during the most current three charge back years, and (4) a comparison of the estimated liability per case in the 2006 projection to the average pattern for the projections of the most recent three years.

The estimate was allocated between General Fund and Navy Working Capital Fund using a percentage based on the number of civilian employees taken from the Navy Budget Tracking System. The following table details the numbers used in support of the allocation:

	<u>Personnel</u>	<u>Allocation %</u>
DON General Fund	84,068	44%
Navy Working Capital Fund	108,166	56
Total	192,344	100%

Note 18.	General Disclosures Related to the Statement of Net Cost
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Intragovernmental Costs and Exchange Revenue		
As of December 31	2007	2006

As of December 31	2007	2006
1. Intragovernmental Costs	\$ 12,670,999,267.32	\$ 11,514,401,927.25
2. Public Costs	25,744,988,897.12	20,226,609,583.39
3. Total Costs	\$ 38,415,988,164.44	\$ 31,741,011,510.64
4. Intragovernmental Earned Revenue	\$ (623,861,869.70)	\$ (620,331,355.39)
5. Public Earned Revenue	(776,255,483.90)	(428,001,526.55)
6. Total Earned Revenue	\$ (1,400,117,353.60)	\$ (1,048,332,881.94)
7. Net Cost of Operations	\$ 37,015,870,810.84	\$ 30,692,678,628.70

Net Costs of Operations

The DON reported an increase in the Net Cost of Operations of \$6.3 billion, 21%, 1st Quarter, FY 2007 when compared to 1st Quarter, FY 2006. The pertinent changes are described below in the disclosure for Total Costs and Earned Revenue.

Total Costs

Total Costs increased \$6.7 billion, 21% from the comparative period. Public Costs increased \$5.5 billion, 27%. The major drivers of the increase in Public costs were:

- Asset capitalization of Military Equipment decreased from \$5.8 billion in 1st Quarter, FY 2006 to \$2.8 billion in 1st Quarter FY 2007. Due to systemic deficiencies, when assets are acquired, expenses are recognized and then later decremented when the assets are capitalized. Therefore, the comparative decrease in assets capitalized through 1st Quarter, FY 2007 reflect an increase in costs of \$3.0 billion. When the difference in depreciation of military equipment is accounted for, the total increase in Public Costs related to military equipment capitalization is \$4.6 billion.
- The DON recognized contingent legal liabilities of \$1.4 billion for the first time in 1st Quarter, FY 2007. Contingent legal liabilities were not recognized in 1st Quarter, FY 2006.

Intragovernmental Costs increased \$1.2 billion, 10% from the comparative period. The major drivers of the increase in Intergovernmental Costs were recognized from the following DON trading partners that provided increased levels of goods and services.

Other Federal Agencies

- Exchange transactions with the Office of Personnel Management increased \$301.0 million from 1st Quarter, FY 2006.

- Exchange transactions with The Department of Transportation increased \$115.1 million from 1st Quarter, FY 2006.
- Exchange transactions with the Department of Energy increased \$156.0 million from 1st Quarter, FY 2006.

DoD Components

- Defense Logistics Agency Supply Management exchange transactions increased \$155.3 million and \$72.7 million respectively with the Navy and Marine Corps, General Fund totaling \$228.0 million.
- United States Transportation Command provided increased level of transportation services of \$93.7 million.
- Goods and services provided by the Navy Working Capital Fund increased \$73.9 million and \$57.6 million to the Navy and Marine Corps respectively for a total increase of \$131.5 million.

Total Earned Revenue

Total Earned Revenue increased \$351.7 million, 34% from the comparative period. The majority of the total increase is in Public Earned Revenue which increased \$348.3 million, 81%, 1st Quarter, FY 2007 from 1st Quarter, FY 2006. The major driver of the increase in Public Earned Revenue was:

- Navy Military construction building and structures asset capitalization increased \$397.0 million due to completion of construction projects and increased additions through 1st Quarter, FY 2007 that were not reflected in 1st Quarter, FY 2006. FY 2007 increases in acquisition value of General PP&E were recorded in Other Gains (USSGL 7190), which had a positive impact on public revenues. In FY 2006 General PP&E did not increase to the same level as FY 2007, therefore the increase on revenue between years.

Other Disclosures Related to the Statement of Net Cost

Intragovernmental costs and revenues are related to transactions made between two reporting entities within the Federal Government.

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

The Statement of Net Cost 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 DON's financial management systems are unable to meet all of the requirements for full accrual accounting. Many of DON's financial and nonfinancial feeder systems and processes were designed and implemented prior to the issuance of Generally Accepted Accounting Principles (GAAP) for federal agencies. These systems were not designed to collect and record financial information on the full accrual accounting basis as required by GAAP. Most of DON's legacy systems were designed to record information on a budgetary basis. Considering these systems limitations, the DON is unable to compare its intragovernmental costs and revenues with the corresponding balances of its intragovernmental trading partners.

The DON has undertaken efforts to determine the actions required to bring its financial and nonfinancial feeder systems and processes into compliance with all elements of GAAP. One such action is the revision of its accounting systems to record transactions based on the US Standard General Ledger (USSGL). Until such time as all of the DON's financial and nonfinancial feeder systems and processes are updated to collect and report financial information as required by GAAP, DON's financial data will be largely 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.

Heritage Asset Disclosure

The DON's accounting systems do not capture information relative to Heritage Assets separately and distinctly from normal operations. The DON has not had any transfers of heritage assets or any donations of heritage assets.

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

As of December 31	2007		2006	
	Cumulative Results of Operations	Unexpended Appropriations	Cumulative Results of Operations	Unexpended Appropriations
1. Prior Period Adjustments				
Increases (Decreases) to Net Position Beginning Balance				
A. Changes in Accounting Standards	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
B. Errors and Omissions in Prior Year Accounting Reports	0.00	0.00	0.00	0.00
C. Total Prior Period Adjustments	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
2. Imputed Financing				
A. Civilian CSRS/FERS Retirement	\$ 47,343,011.77	\$ 0.00	\$ 51,972,672.66	\$ 0.00
B. Civilian Health	96,341,560.00	0.00	81,407,326.00	0.00
C. Civilian Life Insurance	231,847.52	0.00	243,561.69	0.00
D. Judgment Fund	2,215,339.36	0.00	6,531,506.51	0.00
E. IntraEntity	0.00	0.00	0.00	0.00
F. Total Imputed Financing	\$ 146,131,758.65	\$ 0.00	\$ 140,155,066.86	\$ 0.00

Other Disclosures

Appropriations Received on the Statement of Changes in Net Position (SOCNP) does not agree with Appropriations Received on the Statement of Budgetary Resources due to differences between proprietary and budgetary accounting concepts and reporting requirements. The difference of \$1.1 billion between the Statement of Changes in Net Position (SOCNP) Appropriations Received and the Statement of Budgetary Resources (SBR) Appropriations Received is related to the Continuing Resolution Authority for the Military Construction account. Per Treasury guidance, full budget authority is recorded in the SBR, but only the amounts authorized under the Continuing Resolution Authority are recorded in the SOCNP. An additional difference of \$5.9 million is due to the values for Trust Funds and Special Receipt Accounts in Appropriated Trust or Special Fund Receipts (USSGL 4114) not being included in the Appropriations Received line of SOCNP.

Statement of Federal Financial Accounting Standards Number 27, "Identifying and Reporting Earmarked Funds," effective for reporting years after FY 2005, required that DoD modify the Statement of Changes in Net Position. The Federal Accounting Standards Advisory Board determined that restatement of prior comparative balances would not be allowed. To meet the requirement, additional columns were added to separately display gross amounts for earmarked funds, and all other (non-earmarked) funds. In the Statement of Changes in Net Position, all offsetting balances (i.e. transfers-in and transfers out, revenues and expenses) for intra-DoD

activity between earmarked and other (non-earmarked) funds are reported on the same lines. This results in an eliminations column, which appears to contain no balances. In reality, the column contains all appropriate elimination entries, but all net to zero within each respective line.

Imputed Financing.

The amounts the Department of Defense remits to the Office of Personnel Management (OPM) by and for employees covered by the Civil Service Retirement System (CSRS), the Federal Employees' Retirement System (FERS), the Federal Employees' Health Benefits (FEHB) program, and the Federal Employees' Group Life Insurance (FEGLI) program do not fully cover the government's cost to provide these benefits. An imputed cost is recognized as the difference between the government's cost of providing these benefits to employees and the Agency's contributions for them. The OPM provides the cost factors to the Defense Finance and Accounting Service (DFAS) for the computation of imputed financing costs. These costs are provided by DFAS to the Office of the Under Secretary of Defense (Personnel and Readiness) for validation and approval. The approved imputed costs are provided to the DoD reporting entities for inclusion in their financial statements.

Judgment Fund.

Treasury provided information related to amounts paid for Judgment Fund liabilities under the Contracts Dispute Act and the Notification of Federal Antidiscrimination and Retaliatory Act (No FEAR Act) on behalf of DON, which DON is required to repay. Judgment Fund payments made out of the following Treasury appropriations do not require reimbursement and therefore represent imputed financing to DON: 20X1740 and 20X1742. Only those payments made from Treasury appropriation 20X1743 and that portion of 20X1741 that is related to the No FEAR Act are required to be repaid by DON.

Description of the Other lines.

Other Adjustments (recessions, etc.) (Line 13.C) is the account for adjustments made to Unexpended Appropriations.

Note 20.	Disclosures Related to the Statement of Budgetary Resources
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As of December 31	2007	2006
1. Net Amount of Budgetary Resources Obligated for Undelivered Orders at the End of the Period	\$ 98,430,496,308.05	\$ 73,541,307,229.79
2. Available Borrowing and Contract Authority at the End of the Period	0.00	0.00

3. Other Information Related to the Statement of Budgetary Resources (SBR)

Apportionment Categories for Obligations Incurred

On the Statement of Budgetary Resources: Obligations Incurred includes \$53.0 billion of Direct Program Obligations and \$2.0 billion of Reimbursable Program Obligations.

On the Report on Budget Execution (SF-133):

- Direct Obligations, Category A, amounts apportioned quarterly, are \$23.5 billion.
- Direct Obligations, Category B, amounts apportioned on a basis other than quarterly, are \$29.2 billion.
- Total Direct Obligations are therefore \$52.7 billion.
- Category B Reimbursable Obligations are \$2.1 billion.
- The \$204.9 million difference reflects adjustments recorded on the SBR to reconcile to trading partner data, record fringe benefit accruals, and recognize other adjustments.

Intraentity Transactions

Intraentity transactions have not been eliminated because the statements are presented as combined and combining.

Permanent, Indefinite Appropriations.

DON has two permanent, indefinite appropriations.

National Defense Sealift Fund.

The National Defense Sealift Fund (NDSF) is operated under the authority of 10 U.S. Code 2218, which provides for the construction (including design of vessels), purchase, alteration, and conversion of Department of Defense (DoD) sealift vessels; operation, maintenance, and lease or charter of DoD vessels for national defense purposes; installation and maintenance of defense features for national defense purposes on privately owned and operated vessels that are constructed in the United States and documented under the laws of the United States; research and development relating to national defense sealift; and expenses for maintaining the National Defense Reserve Fleet (NDRF) including the acquisition, alteration or conversion of vessels built in U.S. shipyards for NDRF. As of 1st Quarter, FY 2007, one transfer for \$11.6 million from the Shipbuilding and Conversion, Navy appropriation to the NDSF was recorded; no transfers from NDSF have occurred.

Environmental Restoration, Navy.

Environmental Restoration, Navy (ER, N) is a transfer account that funds environmental restoration, reduction and recycling of hazardous waste, removal of unsafe buildings and debris, and similar purposes. Funds are to remain available until transferred, and remain available for the same purpose and same time period as the appropriations to which transferred. As of 1st Quarter, FY 2007 there have been no transfers either to or from ER, N.

Differences between the SBR and the SF-133 Report on Budget Execution

Differences exist between the SF-133 and the SBR for a number of reasons; including accruals recorded for fringe benefits, liabilities recorded for the Judgment Fund, and accruals recorded for trading partner advances and liabilities.

Other Disclosures

Unobligated budget authority is the difference between the obligated balance and the total unexpended balance. It represents that portion of the unexpended balance unencumbered by recorded obligations. Appropriations are provided on an annual, multi-year, and no-year basis. An appropriation expires on the last day of its period of availability and is no longer available for new obligations when in an expired status. Unobligated balances retain their fiscal year identity in an expired account for an additional five fiscal years. The unobligated balance remains available to make legitimate obligation adjustments, i.e., to record previously unrecorded obligations and to make upward obligation adjustments in previously underestimated obligations for five years. At the end of the fifth year the budget authority is canceled. Thereafter, the budget authority is not available for any purpose.

Information about legal limitations and restrictions affecting the use of the unobligated balance of budget authority is specifically stated by program and fiscal year in the applicable appropriation language or in the alternative provisions section at the end of the appropriations act.

As noted above, the National Defense Sealift Fund, a revolving fund, received a transfer of \$11.6 million in 1st Quarter, FY 2007 from the Shipbuilding and Conversion, Navy appropriation. A transfer of resources to a revolving fund is considered a capital infusion.

Note 21.	Disclosures Related to the Statement of Financing
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General Observations

Budgetary data is not in agreement with proprietary expenses and assets capitalized. This causes a difference in net cost between the Statement of Net Cost and the Statement of Financing. Adjustments are posted to the Statement of Financing for these differences. For 1st Quarter, FY 2007, an adjustment of \$47.7 million was made to Resources that Finance the Acquisition of Assets of the Statement of Financing so that proprietary accounts reconcile with the budgetary accounts. The alignment was made per Office of the Under Secretary of Defense (Comptroller) guidance.

Other Disclosures

The increase in resources that finance the acquisition of assets is primarily due to the implementation of SFFAS No. 23 "Eliminating the Category of National Defense Property, Plant, and Equipment." Correspondingly, there is also an increase in the reported depreciation for the military equipment.

The Statement of Financing is presented as a consolidated statement. However, the following Statement of Financing lines are presented as combined instead of consolidated due to interagency budgetary transactions not being eliminated:

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

Adjustments in funds which are temporarily not available pursuant to Public Law, and those that are permanently not available (included in the "Adjustments" line on the Statement of Budgetary Resources), are not included in "Spending Authority From Offsetting Collections and Adjustments" line on the Statement of Budgetary Resources or on the Statement of Financing. The Statement of Financing was expanded to further articulate and detail the relationship between new obligations from budgetary accounting and net cost of operations from proprietary accounting.

Description of the Other lines.

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

The Other resources or adjustments to net obligated resources that do not affect the net cost of operations: the balance of \$38.6 million consists primarily of the value of donated fuel. This fuel was donated by other nations to the United States military in support of the Global War on Terror.

Components Requiring or Generating Resources in Future Periods --

The Other is related to future periods and the balance of \$1.4 billion consists primarily of an unfunded liability reflecting an estimate for potential contingent legal liabilities.

Components not Requiring or Generating Resources --

The Other not requiring or generating resources has a balance of \$37.8 million and consists primarily of the value of donated fuel. This fuel was donated by other nations to the United States military in support of the Global War on Terror.

The total components requiring or generating resources in future periods reflected on the Statement of Financing is \$3.1 billion in 1st Quarter, FY 2007. This amount, in addition to the estimate for potential contingent legal liabilities of \$1.4 billion noted above, reflects changes in accruals of unfunded liabilities which included but are not limited to; unused annual leave, environmental and non environmental disposal, litigation, Federal Employees' Compensation Act (FECA), unemployment compensation, canceled year accounts payable, and contract incentives. The total of \$27.4 billion in Liabilities Not Covered by Budgetary Resources included on the Balance Sheet, Note 11, (Line 3), and included on the Balance Sheet includes the aforementioned items and liabilities to Treasury for nonentity accounts receivable of the DON. Collections on nonentity receivables would not require or generate resources for the DON as they are deposited at Treasury and belong to the general cash balances of the United States Government.

Note 22.

Disclosures Related to the Statement of Custodial Activity

Not Applicable.

Note 23.**Earmarked Funds****BALANCE SHEET**As of December 31,
2006

	Military Retirement Fund	Medicare Eligible Retiree Health Care Fund	Other Earmarked Funds	Eliminations	Total
ASSETS					
Fund balance with Treasury	\$ 0.00	\$ 0.00	\$ 13,363,814.53	\$ 0.00	\$ 13,363,814.53
Investments	0.00	0.00	9,686,252.46	0.00	9,686,252.46
Accounts and Interest Receivable	0.00	0.00	0.00	0.00	0.00
Other Assets	0.00	0.00	17,919.85	0.00	17,919.85
Total Assets	\$ 0.00	\$ 0.00	\$ 23,067,986.84	\$ 0.00	\$ 23,067,986.84

**LIABILITIES and NET
POSITION**

Military Retirement Benefits and Other Federal Employment Benefits	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
Other Liabilities Unexpended Appropriations	0.00	0.00	1,654,836.66	0.00	1,654,836.66
Cumulative Results of Operations	0.00	0.00	1,549,698.83	0.00	1,549,698.83
Total Liabilities and Net Position	\$ 0.00	\$ 0.00	\$ 23,067,986.84	\$ 0.00	\$ 23,067,986.84

**STATEMENT OF NET
COST**For the period ended
December 31, 2006

Program Costs	\$ 0.00	\$ 0.00	\$ 4,868,663.42	\$ 0.00	\$ 4,868,663.42
Less Earned Revenue	0.00	0.00	0.00	0.00	0.00
Net Program Costs	\$ 0.00	\$ 0.00	\$ 4,868,663.42	\$ 0.00	\$ 4,868,663.42
Less Earned Revenues Not Attributable to Programs	0.00	0.00	0.00	0.00	0.00
Net Cost of Operations	\$ 0.00	\$ 0.00	\$ 4,868,663.42	\$ 0.00	\$ 4,868,663.42

**STATEMENT OF
CHANGES IN NET
POSITION**For the period ended
December 31, 2006

Net Position Beginning of the Period	\$ 0.00	\$ 0.00	\$ 20,393,008.01	\$ 0.00	\$ 20,393,008.01
Net Cost of Operations	0.00	0.00	4,868,663.42	0.00	4,868,663.42
Budgetary Financing Sources	0.00	0.00	5,888,805.59	0.00	5,888,805.59
Other Financing Sources	0.00	0.00	0.00	0.00	0.00
Change in Net Position	\$ 0.00	\$ 0.00	\$ 1,020,142.17	\$ 0.00	\$ 1,020,142.17
Net Position End of Period	\$ 0.00	\$ 0.00	\$ 21,413,150.18	\$ 0.00	\$ 21,413,150.18

Fluctuations and Abnormalities

Earmarked funds were required to be reported and disclosed separately from other funds beginning 1st Quarter, FY 2006. For DON General Fund, a reclassification to the new earmarked funds reporting attribute was performed, beginning balances were transferred from the previous attributes, and the status of the earmarked funds is displayed in this Note to the financial statements.

Other Disclosures

Earmarked funds are financed by specifically identified revenues and are required by statute to be used for designated activities or purposes. The DON has seven earmarked funds. Four are categorized as Special Funds and three are categorized as Trust Funds. A list of these earmarked funds and a brief description of each follows below. There have been no changes in legislation during or subsequent to the reporting period that significantly changes the purpose of any of the seven funds or that redirects a material portion of the accumulated balances of any of the seven funds.

Special Earmarked Funds

Wildlife Conservation, Military Reservations, Navy --

This fund, authorized by 16 United States Code 670b, provides for the development and conservation of fish and wildlife and recreational facilities on military installations. Proceeds from the sale of fishing and hunting permits are used for these programs at Navy and Marine Corps installations charging such user fees. These programs are carried out through cooperative plans agreed upon by the local representatives of the Secretary of Defense, the Secretary of the Interior, and the appropriate agency of the State in which the installation is located.

Kaho'olawe Island Conveyance, Remediation and Environmental Restoration Fund, Navy --

This fund, authorized by 107 United States Statute 1483, was established to recognize and fulfill the commitments made on behalf of the United States to the people of Hawaii and to return to the State of Hawaii the Island of Kaho'olawe. Congress has found it to be in the national interest and an essential element in the federal government's relationship with the State of Hawaii the conveyance, clearance or removal of unexploded ordnance, environmental restoration, control of access to the Island and future use of the Island be undertaken in a manner consistent with the enhancement of that relationship, the Department of Defense's military mission, the federal interest, and applicable provisions of law.

Roosmoor Liquidating Trust Settlement Account --

The Roosmoor Liquidating Trust account was established by Section 2208 of Public Law 104-106; the National Defense Authorization Act of 1996. Per the statute, monies awarded the United States when litigation is settled in favor of the Roosmoor Liquidating Trust is deposited into this account. The monies are made available to DON solely for the acquisition or construction of military family housing in, or in the vicinity of San Diego, California.

Ford Island Improvement Account --

The Ford Island Improvement fund is authorized by 10 United States Code 2814 and was established to carry out improvements to property and facilities that will deliver overall benefits to DON at the Pearl Harbor Naval Complex at Ford Island, Hawaii. Ford Island is a central feature in the Pearl Harbor National Historic Landmark. The Ford Island legislation allows DON to sell or lease properties in Hawaii and use the proceeds to develop Ford Island.

Trust Earmarked Funds

Department of the Navy General Gift Fund --

This trust fund is authorized by 10 United States Code 2601. Under the provisions of this statute, the Secretary of the Navy may accept, hold, administer, and spend any gift, devise, or bequest of real or personal property, made on the condition that they be used for the benefit, or in connection with the establishment, operation, or maintenance of a school, hospital, library, museum, cemetery, or other institution under the jurisdiction of the Department of the Navy.

Ships Stores Profit, Navy --

This trust fund is authorized under 10 United States Code 7220. Deposits to this fund are derived from profits realized through the operation of ships' stores and from the acceptance of gifts accepted for the purpose of providing recreation, amusement, and contentment for enlisted members of the Navy and Marine Corps.

U.S. Naval Academy General Gift Fund --

This trust fund is authorized by 10 United States Code 6973. Under the provisions of this statute, the Secretary of the Navy may accept, hold, administer, and spend any gift, devise, or bequest of personal property, made on the condition that it they used for the benefit, or in connection with the United States Naval Academy, or the Naval Academy Museum, its collections, or its services.

Note 24.	Other Disclosures
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As of December 31	2007			
	Asset Category			
	Land and Buildings	Equipment	Other	Total
1. ENTITY AS LESSEE-				
Operating Leases				
Future Payments Due				
Fiscal Year				
2007	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00
2008	13,853,346.43	0.00	572,000.00	14,425,346.43
2009	11,169,119.00	0.00	80,975.00	11,250,094.00
2010	11,314,027.81	0.00	82,999.38	11,397,027.19
2011	11,553,249.09	0.00	85,074.36	11,638,323.45
2012	11,840,702.02	0.00	87,201.22	11,927,903.24
After 5 Years	0.00	0.00	0.00	0.00
Total Future Lease Payments Due	\$ 59,730,444.35	\$ 0.00	\$ 908,249.96	\$ 60,638,694.31

Fluctuations and Abnormalities

Although a comparative column is not shown, the DON reported a decrease of \$34.1 million in Operating Leases Future Payments Due in 1st Quarter, FY 2007 when compared to 1st Quarter, FY 2006. This decrease is due to the ongoing effort to validate operating leases throughout the Navy shore establishment.

Lessee – A person or entity that receives the use and possession of leased property (e.g. real estate or equipment) from a lessor in exchange for a payment of funds.

Operating Lease - A lease that does not substantially transfer all the benefits and risk of ownership; payments are charged to expense over the lease term as they become payable.

Other Disclosures

The values reported for operating leases is derived from the DON data collection process. This process only provides summary level values at this time. Lease periods vary and are not expected to be renewed at the end of the lease term. There are no material escalation clauses or contingent rental restrictions. Data is gathered from existing leases, General Service Administration bills, and Interservice Support Agreements. Future year projections use the Consumer Price Index (CPI), rather than the DoD inflation factor. The CPI more accurately impacts increases to the leases, especially those at commercial lease sites.

Note 25.	Restatements
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Not applicable for 1st Quarter, FY 2007.