Chief Financial Officer Annual Financial Statements FY 1998

Department of the Navy
Navy Working Capital Fund

March 1, 1999

DEPARTMENT OF THE NAVY
NAVY WORKING CAPITAL FUND

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Introduction

These financial statements report on the financial position and results of operations of the Department of the Navy (DoN) Navy Working Capital Fund (NWCF) for Fiscal Year (FY) 1998. They are prepared pursuant to the requirements of the Chief Financial Officer's Act (CFO) of 1990 as amended by the Government Management Reform Act (GMRA) of 1994 and the Department of Defense (DoD) implementing guidance.

The financial statements include all aspects of the DoN's supply and industrial operations. They do not include any other appropriated, trust or revolving funds. The principal statements are prepared from the same sources as are reports used to monitor and control budgetary resources. In FY 1996, the DoN's financial statements were presented for each primary and select secondary activity groups as well as a consolidated level financial statement. In FY 1997, the DoN's financial statements were presented at the consolidated level only in accordance with DoD guidance. In FY 1998, the DoN's financial statements are again presented at the consolidated level only in accordance with DoD guidance.

Description and Overview

Working capital funds were created in the DoD by the National Security Act Amendments of 1949. This legislation gave the Secretary of Defense the authority to establish working capital funds to finance inventories of supplies and for industrial activities that provide common services within the Departments and Agencies of the DoD.

Working capital funds can be broadly segregated into two functional areas: industrial operations and supply operations. Working capital funds finance the operating costs of most industrial, manufacturing, and service activities of the DoD. Industrial and service activities are given working capital to finance the cost of producing goods and services ordered by customers and subsequently receive reimbursement by billing, much as a private business does. By using money generated from sales to replenish its working capital, these funds are intended to be self-sustaining; hence the term "revolving fund." Working capital funds also finance the costs of supply operations that hold inventories of parts, subsistence, fuel, and other supplies for sale to military units.

Beginning in FY 1992, the DoD combined five industrial funds and four stock funds, and several appropriated fund support activities, including the Defense Finance and Accounting Service (DFAS) and the Defense Commissary Agency, into a single revolving fund called the Defense Business Operations Fund (DBOF). The primary goal of establishing DBOF was to focus the attention of all levels of DoD management on the total costs of carrying out certain critical DoD business operations and to manage those costs effectively. Within the DoN this combining of funds involved the Navy Industrial Fund, the Marine Corps Industrial Fund, and the DoN Stock Fund.

The Office of the Under Secretary of Defense (Comptroller) (USD(C)) centrally managed the cash balance of the DBOF. On 1 February 1995, DoD returned the management of the DBOF's cash balance to the military service and DoD component level to more appropriately align cash management with the operating entities. This action made each individual DoD component directly accountable for its respective cash balance since it was their management decisions that directly affected cash.

A further evolution of the fund occurred on 11 December 1996, when the USD(C) canceled the DBOF and established four funds: the Army Working Capital Fund, the NWCF, the Air Force Working Capital Fund, and the Defense-wide Working Capital Fund (DWCF). This decision reinforced the role of the DoD components by clearly establishing the component's responsibility to manage. Collectively, these four funds are known as the Defense Working Capital Funds.

The NWCF is a business-type financial operation, which distinguishes between capital and operating costs using standard accounting principles. A basic principle of the NWCF, like the DBOF, is to capture all the costs of operating an activity group and to reflect the total cost of doing business in stabilized prices charged to customers. It operates on a break-even basis over the long term. Profits, when they occur, are returned to customers through lower rates in subsequent years. Similarly, losses are recouped through an increase in rates in subsequent years.

The DoN has historically operated a large number of its supply and industrial facilities under revolving fund concepts. In FY 1996 the Navy Distribution Depots activity group was combined with the Supply Management (Navy) activity group. Effective 1 October 1996, the DoN merged the Logistics Support Activities activity group into the Supply Management (Navy) activity group, and transferred the Defense Automated Printing Service (DAPS) activity group to the Defense Logistics Agency (DLA). On 1 October 1997, the Navy Ordnance activities were removed from the Depot Maintenance activity group and established as a separate activity group called Ordnance. There are now seven diverse primary activity groups remaining in the DoN, covering about fifty reporting entities. These seven activity groups are (1) Supply Management, (2) Depot Maintenance, (3) Ordnance, (4) Research & Development, (5) Base Support, (6) Information Services, and (7) Transportation.

Five of the seven primary activity groups include operations so extensive as to warrant smaller "secondary" activity groups that correspond to the DoN systems command structure. For example, the activity group of Depot Maintenance consists of three secondary activity groups. Generally, primary and secondary activity group classification is based on the type of functions an activity performs for its customers, i.e., supply, industrial, or services. In FY 1998, the Naval Facilities Engineering Service Center (NFESC), previously a Research and Development secondary activity group, was reclassified under the Base Support primary business area.
The DoN also has a Component-level activity group that represents a "corporate-level" holding area for financial transactions (primarily collections and disbursements) which are pending identification to a specific activity group. A brief synopsis of the primary and associated secondary NWCF activity groups categorized by these three functions is provided below.

Supply

Supply Management - This primary activity group of Supply Management consists of two secondary activity groups, Supply Management-Navy and Supply Management-Marine Corps, which perform inventory management functions for shipboard, aviation, and amphibious reparable and consumable spare parts and commodities. In FY 1996, the Navy Distribution Depot activity group, which provided management of overseas Fleet and Industrial Support Centers (FISC), merged with Supply Management-Navy, and in FY 1997, the Logistics Support Activities activity group, which provided support functions for ashore and afloat commanders, merged into Supply Management-Navy. In FY 1998, the FISCs at Oakland and Guam were closed as part of the Base Realignment and Closure (BRAC) process.

Industrial

Depot Maintenance - This primary activity group consists of the following three secondary activity groups: (1) Naval Shipyards (NSY) with four activities, (2) Naval Aviation Depots (NADEP) with three activities, and (3) the Marine Corps Depots with two activities. The functions associated with Depot Maintenance are maintenance, repair, manufacturing, overhaul, refit and restoration, and engineering services for design and development.

Services

Transportation - This primary activity group provides service-unique vessels such as Naval Fleet Auxiliary Force (NFAF) vessels, Special Mission Ships (SMS), and Afloat Prepositioning Force-Navy (APF-N) ships for sea transportation, logistics forces, and special missions. The Military Sealift Command (MSC) manages these vessels from eight commands around the world.

Ordnance - This primary activity group consists of a headquarters, two weapon support facilities, five detachments, a Navy-wide inventory control focused division, and a technical division. Overall, the activity group coordinates Fleet/Fleet Marine requirements and issues, controls the distribution of ordnance, administers and provides waterfront support operations, performs intermediate maintenance management, and manages in-service ordnance logistics efforts for the fleet.

Research and Development - This primary activity group consists of the following five secondary activity groups: (1) Naval Air Warfare Center (NAWC), (2) Naval Surface Warfare Center (NSWC), (3) Naval Undersea Warfare Center (NUWC), (4) Space and Naval Warfare Systems Centers (SSC), and (5) Naval Research Laboratory (NRL). These activities perform a wide range of research, development, test, evaluation and engineering support functions.

Information Services - This primary activity group consists of the following three secondary activity groups: (1) Naval Computer and Telecommunications Command (NCTC), (2) Naval Reserve Information Systems Office (NRISO), and (3) Fleet Material Support Office (FMSO). These activity groups provide regional automated information systems services and design support, and design, development, maintenance, and environmental support for information technology systems used by the DoN, other DoD activities, and Federal agencies.

Overview

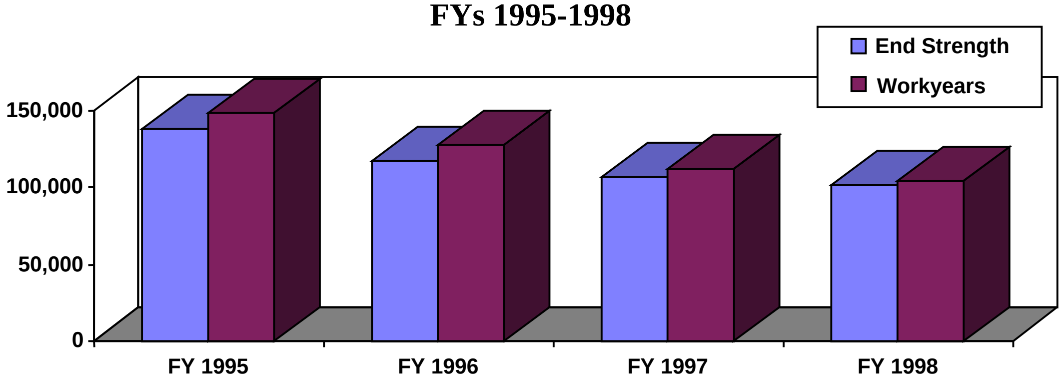
Base Support - This primary activity group is comprised of nine public works centers (PWC), one detachment, and the NFESC. The public work centers support facilities maintenance, environmental services, and utilities for the operating forces and other activities throughout the world. The NFESC provides specialized facilities engineering, design, construction, technology implementation, and management support.

Performance Measures

All NWCF activity groups use performance measures as tools in determining management and operations effectiveness. Performance measures may include cost per direct labor hour, cost per unit of sales or product, operating costs and results, capital investments, current assets, financial obligations, financial conditions, and asset management. Performance measures and information discussed below, representing an aggregation of all NWCF activity groups include the civilian and military personnel resources, sources of revenue, net operating results (NOR), cash flow, change in customer orders, and activity and systems accomplishments.

Personnel Resources

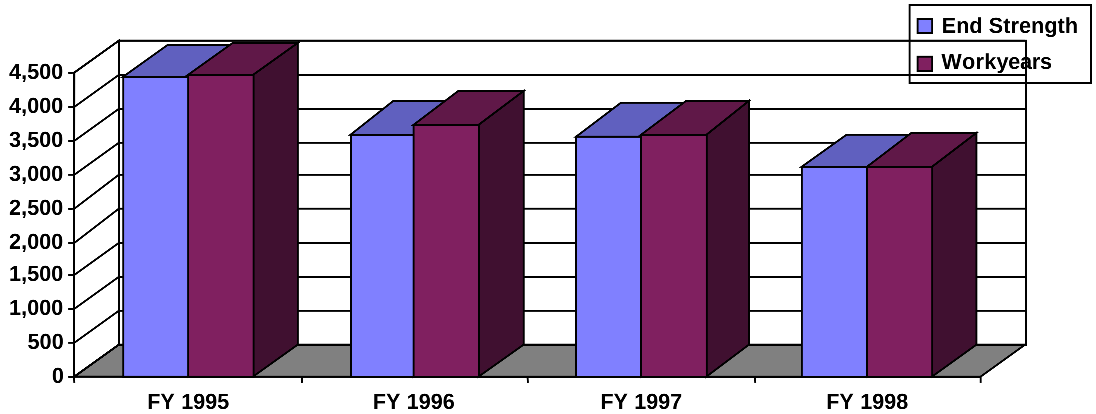
Trend Analysis of Civilian End Strength and Workyears FYs 1995-1998



Civilian Resources:	*FY 1995*	*FY 1996*	*FY 1997*	*FY 1998*
End Strength	138,034	117,298	106,645	101,961
Workyears	149,178	127,270	112,119	104,053

Civilian personnel levels in the DoN are at the lowest level since before World War II. The FY 1998 staffing levels reflect the continued downward trend of the civilian work force as a result of BRAC, reductions in force structure, decreasing workload, and management efficiency. About 49% of the DoN's civilians work at NWCF activities supporting depot level maintenance and repair of ships, aircraft, and associated equipment, development of enhanced warfighting capabilities at the Warfare Centers of Excellence, supply, and public works support. Decreases are anticipated beyond FY 1998 reflecting continued base closure actions, workload decline, and continued efforts of competition, outsourcing, and regionalization.

Trend Analysis of Military End Strength and Workyears FYs 1995-1998



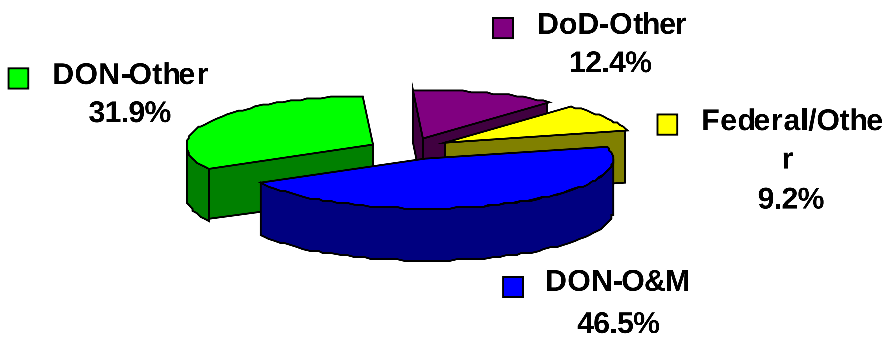
Military Resources:	*FY 1995*	*FY 1996*	*FY 1997*	*FY 1998*
End Strength	4,443	3,599	3,573	3,105
Workyears	4,477	3,743	3,599	3,124

Military personnel levels at NWCF activities reflect the same downward trend seen in the civilian workforce resulting from base closures, reductions in force structure, decreasing workload, and management efficiencies. Decreasing levels are anticipated beyond FY 1998 with further base closures and workload declines.

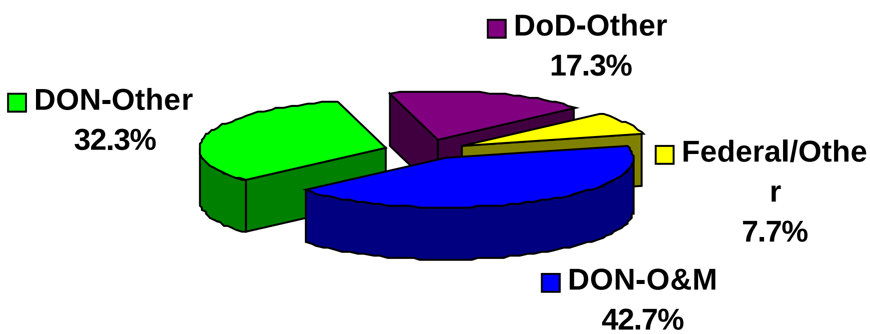
Overview

Revenue by Customer and Provider

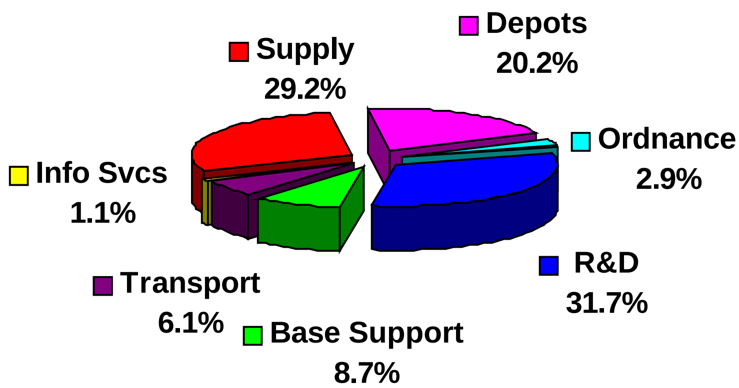
FY 1998 Revenue by Customer



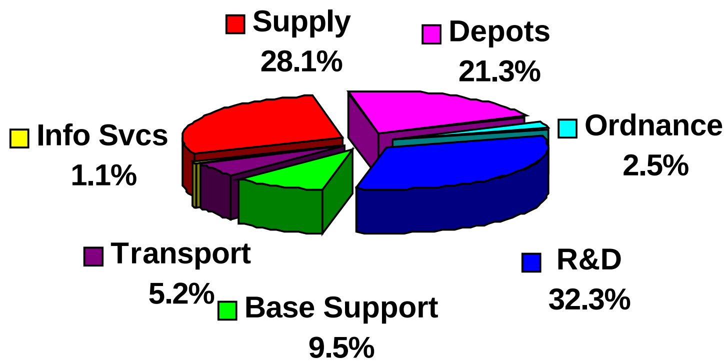
FY 1997 Revenue by Customer



FY 1998 Revenue by Provider



FY 1997 Revenue by Provider

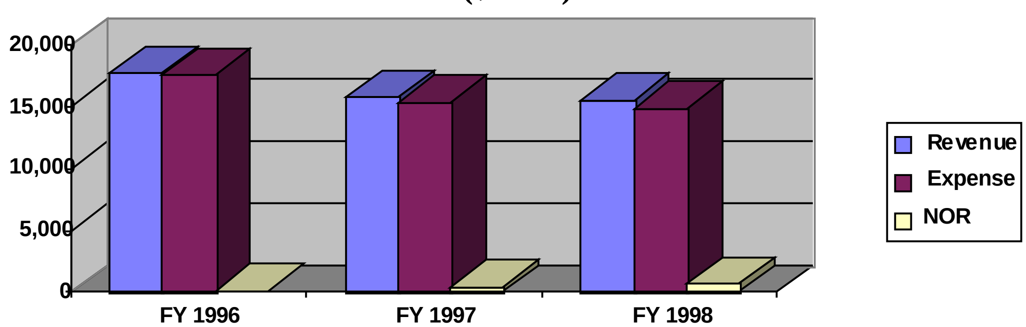


The total revenue base and thus the volume of goods and services provided to NWCF customers in FY 1998 was $21,926 million. This is consistent with the $21,921 million of revenue in FY 1997. As the pie charts indicate, the DoN Operation and Maintenance (O&M) appropriation is the largest customer of the NWCF, followed by the aggregation of other DoN appropriations which include various procurement accounts, Research, Development, Test and Evaluation, Shipbuilding and Conversion, and others. The major activity group providers of goods and services are Research and Development, Supply Management, and Depot Maintenance. These activity groups satisfy over 80 percent of the needs of the NWCF customers and remain almost unchanged from FY 1997.

Revenue, Expenses, and Net Operating Results

Industrial/Services

Trend Analysis of Revenues, Expenses, and NOR
FYs 1996-1998
($ in M)



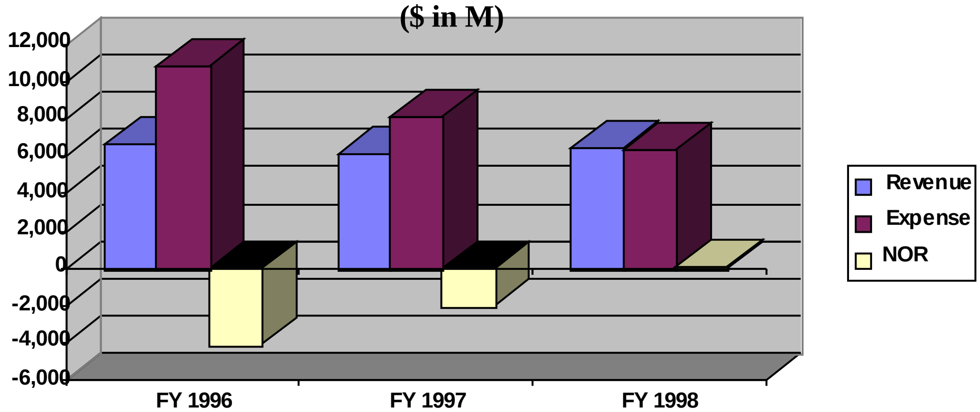
Industrial/Services ($ in M)	*FY 1996*	*FY 1997*	*FY 1998*
Revenues	17,691	15,758	15,519
Expenses	17,536	15,324	14,826
Operating Results	155	435	693

Overview

The Industrial and Services activity group's financial performance was very close to their financial plans. This resulted from fewer variations in planned customer workload versus actual customer workload and through continued efforts of NWCF managers to control costs and to adapt to changes in customer workload that did occur. The FY 1997 and FY 1998 financial results include cash surcharge revenues of $511 million and $365 million, respectively. Further, in FY 1997, the DAPS was transferred out of the NWCF. This transfer reduced revenue and expenses in FY 1997 by approximately $410 million.

Supply

Trend Analysis of Revenues, Expenses, and NOR
FYs 1996-1998
($ in M)



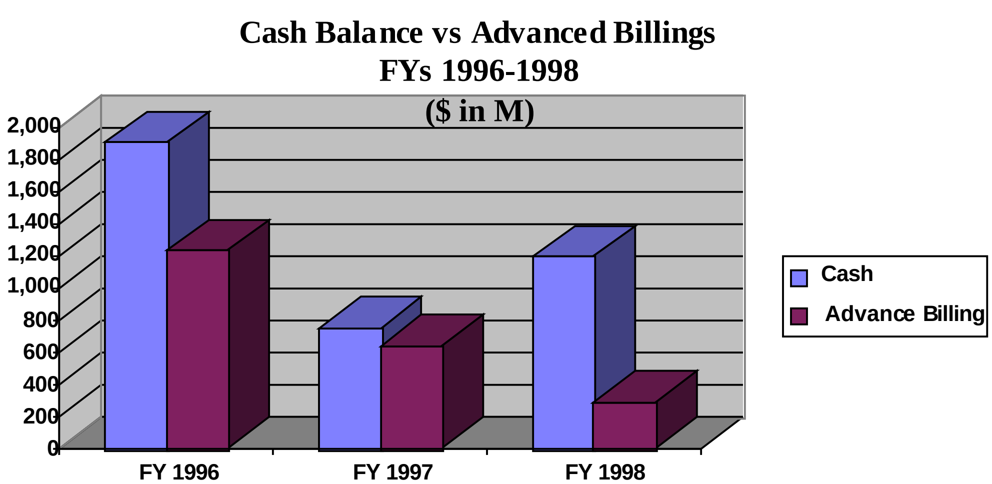
Supply: ($ in M)	*FY 1996*	*FY 1997*	*FY 1998*
Revenues	6,687	6,162	6,407
Expenses	10,764	8,118	6,344
Operating Results	-4,077	-1,956	64

The Supply Management activity group recorded significant operating losses in FY 1996 and FY 1997 and an operating gain in FY 1998. The calculations that produced the FY 1997 Operating Results revealed an error in the calculation of the FY 1996 Operating Results. Correction of this error produces a FY 1996 Operating Result of about negative $1.9 billion versus the negative $4.1 billion reported. Notwithstanding this error, the Operating Results of negative $1.9 billion in both FY 1996 and FY 1997 were not considered representative values for the Supply Management activity group. Although there was a significant improvement in the Operating Results for FY 1998, the positive $64 million still cannot be considered a representative Operating Result of this activity group. See further discussion under Financial Management Issues.

Cash Management

Cash management is the process by which managers maintain a sufficient supply of cash to meet day-to-day business needs while maintaining a reasonable allowance for emergencies. Cash management consists of developing cash plans, monitoring the execution of this cash plan, analyzing collections, disbursements and non-expenditure transfers, identification and correction of errors, and maintaining an appropriate cash balance to meet liabilities and prevent a violation of the Anti-Deficiency Act (ADA). The USD(C) policy requires each WCF to maintain a cash balance equal to seven to ten days of operating program cash disbursements plus six months of capital program cash disbursements. For the NWCF this equates to a cash balance in the range of $750 million to $950 million. In the FY 1999 DoD Appropriations Act, Congress mandated that the DWCF increase its ending FY 1999 cash balance by $1.3 billion over the ending balance for FY 1998. The NWCF portion of this increase is $227 million. The following chart displays the NWCF cash balance for the past three fiscal years.

Advance Billings



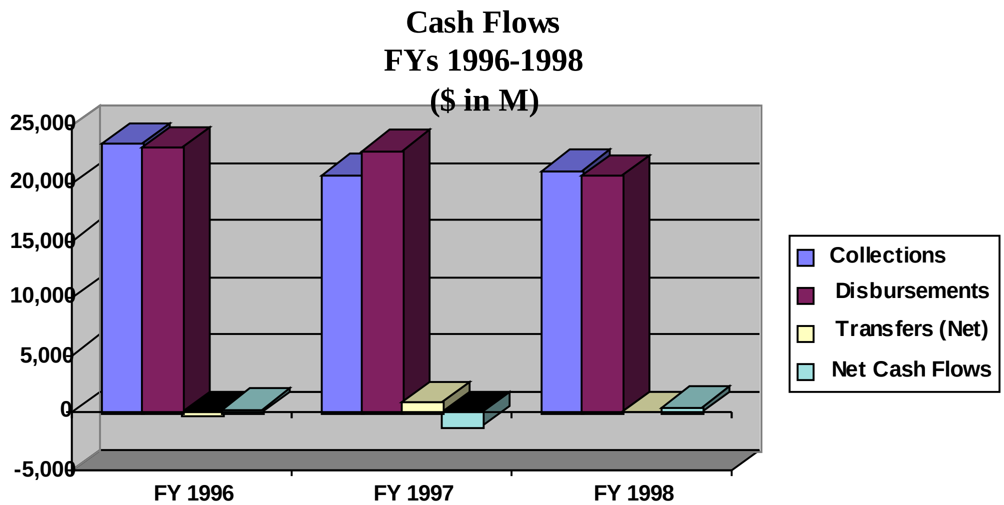
As the chart above indicates, the cash balance has been at or above the minimum level at the end of the fiscal year for the last three years. In addition to the cash balance, the chart displays the unliquidated advance billing balances remaining at the end of each fiscal year. Advance billing is the practice of having the customer pay for agreed upon work before completion of the task. Advance billing does not change the scheduled accomplishment of the work or its cost; it does, however, increase short-term cash availability.

Large scale advance billings began in FY 1993 while DBOF cash was under the management of USD(C). When cash management was returned by USD(C) to the DoD components in February 1995, the DoN received only $442 million; far less than the required minimum level. Additionally, the advance billing liability of $2,190 million being carried in the DoN segment of the DBOF at the time of the transfer greatly exceeded the cash received. These two conditions necessitated additional advance billings to ensure solvency and avoid an ADA violation.

Overview

The above chart displays the downward trend of the advance billing balance and an improving trend when compared to the cash balance. The DoN has taken actions to eliminate the need for further advance billings and liquidate the entire advance billing liability. The DoN has included specific factors in prices charged to customers to generate additional cash of about $500 million in FY 1998 and $150 million in FY 1999. In addition, Congress authorized a transfer of funds into customer accounts of the NWCF in FY 1997 to pay for increased surcharges levied by the NWCF to replenish the cash balance. These actions are anticipated to eliminate the advance billing balance by the end of FY 1999 and establish the minimum cash balance required by the NWCF. Advance billings may be necessary during this "replenishment" time period to ensure solvency.

Cash Flows



In FY 1998, the cash inflows and outflows of the NWCF represent $42 billion in throughput to the cash balance. This combination of collections ($21.1 billion), disbursements ($20.7 billion), and net cash transfers ($64 million) represents a flow of about $168 million each business day. The greatest cash flows occur in the Depot Maintenance, Supply Management, and Research and Development activity groups.

The significant net outflow of cash in FY 1997 resulted from a variety of factors. These include the net liquidation of about $600 million in advance billings in the Depot Maintenance and Research and Development activity groups and a net cash outflow in Supply Management of $550 million.

Fill Rate-Supply Management

The primary function of the Supply Management activity group is to sell material to customers. One indicator of how successful it is in satisfying customers is the Fill Rate. The Fill Rate or Supply Material Availability (SMA) as it is called in the DoN is calculated as the percent of customer requisitions satisfied from on hand wholesale managed assets. The overall DoN goal is 85%. SMA for the Navy segment and the Marine Corps segment of the Supply Management activity group is:

	Navy	Marine Corps
FY 1998	80.5%	80.0% *
FY 1997	80.4%	79.2% *
FY 1996	79.3%	73.8% *
FY 1995	78.2%	83.1%

*SMA for depot level repairable items only

For the Navy segment, the upward trend of SMA is attributable to a number of factors. Demand for wholesale managed items is declining and the number of operating units, both aviation and ships, continues to decline. Through these declines, coupled with continued decommissioning of ships and squadrons and efforts to expand asset visibility, more material becomes available from non-traditional sources vice normal procurement. Increased emphasis on fully funding repair of unserviceable assets increases their availability to satisfy the customer requirement. For the Marine Corps segment, the SMA for depot level repairable items has improved over the past fiscal year. Since the majority of consumable items were transferred to the management of the DLA, they are excluded from the SMA data. Even though the SMA is below the desired goal, the Fleet Marine Force readiness posture is at 91 percent, indicating critical supply parts are available to the customer. Inventory managers continue to monitor SMA and review backorders and repair actions to expedite material to the customer.

Ship Availability-Transportation

The mission of the Transportation activity group is to provide efficient sea transportation, combat ready logistics forces, and reliable special mission ships for the DoD in peace and war. The Military Sealift Command ships are distinct from other U.S. Navy ships in that they are non-combatants, include both government-owned and chartered vessels, and they are crewed by civilian mariners employed by the U.S. Navy and from private operating companies. Ship availability is defined as the measurement of the number of days that ships are actually available to perform the function for which they were contracted, against the number of planned days. The goal is to ensure that the ships are available for the mission to which they were assigned and is expressed as a percentage of meeting the number of planned days. Ship availability for the NFAF, APF-N, and the SMS force are displayed in the following table, in days.

Program	FY	Goal	Actual	Percent
NFAF	1998	11,800	11,638	98.6%
	1997	11,315	11,937 */**	105.5%
	1996	14,330	13,859	96.7%
APF-N	1998	5,110	5,009	98.0%
	1997	5,110	5,073 **	99.3%
	1996	5,282	5,258	99.5%
SMS	1998	8,375	8,195	97.9%
	1997	8,434	8,118 *	96.3%
	1996	4,337	3,933	90.7%

* TAGOS transferred from NFAF to SMS
** Hospital ships transferred from APF-N to NFAF

Overview

Base Support

The PWCs measure their efficiency by various standards of measurement related to the various services/utilities they provide. Below is a break out of the PWC's combined performance for these services for FYs 1996, 1997, and 1998.

Public Work Service:

		Costs Per Service/Utility		
	Measure	**FY 1996**	**FY 1997**	**FY 1998**
Utility Service				
Electricity	MWH	83.74	78.61	71.95
Potable Water	KGAL	2.37	2.47	2.12
Salt Water	KGAL	.57	.62	.48
Heating	MBTU	9.80	9.33	14.62
Steam	MBTU	14.62	15.29	13.54
Clean Steam	MBTU	13.31	15.03	14.25
Sewage	KGAL	3.88	4.00	4.10
Natural Gas	MBTU	4.21	5.38	5.21
Compressed Air	KCF	1.33	1.09	.97
Sanitation				
Refuse	CUYD	5.93	5.20	5.30
Pest Control	HOURS	37.89	38.32	33.01
Hazardous Waste I	GAL	5.86	2.54	4.81
Hazardous Waste II	LBS	1.30	1.01	.89
Environmental Eng.	HOURS	61.41	58.91	63.93
Industrial Waste	KGAL	143.58	14.26	31.67
Transportation				
Equipment Rental	HOURS	2.26	3.24	2.46
Vehicle Ops	HOURS	56.19	66.43	61.42
Vehicle Maintenance	SRO	111.95	78.45	65.62
Maintenance and Repair				
Specifics	JOBS	43,337.33	52,494.54	36,409.55
Minors	ITEMS	5,378.74	7,082.39	4,954.24
Emergency/Service	CHITS	259.51	146.47	101.89
Recurring	ITEMS	1,739.85	1,364.81	1,279.93

Supply Management

The Navy and Marine Corps supply activities measure their performance by comparing sales (revenue) with costs. Below is a breakout of the combined Navy/Marine Corps supply activities performance for FYs 1996, 1997, and 1998.

Sales ($ in Millions)			
	FY 1996	FY 1997	FY 1998
Wholesale			
Gross Sales	$3,881.7	$3,605.5	$3,989.4
Material Costs	$2,270.4	$1,994.0	$2,418.3
Purchases from Customers	337.4	273.6	239.7
Operating Costs	913.1	1,139.9	1,293.2
Total Wholesale Costs	$3,520.9	$3,407.5	$3,951.2
Cost Per Dollar of Wholesale Sales	0.907	0.945	0.990
Retail			
Gross Sales	$2,372.6	$2,139.3	$2,088.6
Material Costs	2,298.1	2,200.8	2,184.3
Purchases from Customers	28.4	21.0	22.3
Total Retail Costs	$2,326.5	$2,221.8	$2,206.6
Cost Per Dollar of Retail Sales	0.981	1.039	1.056

Trends in wholesale gross sales closely mirror customer funding levels. A downturn was experienced in FY 1997 predominately due to erosion in the Navy's outfitting accounts and Flying Hour Program shortfalls. The FY 1998 increase in wholesale gross sales resulted from Congressional plus-ups in the Flying Hour Program and an increased surcharge. Material costs closely parallel sales trends in accordance with unit cost doctrine. The FY 1998 varied slightly from this trend by benefiting from increased obligation authority for unfunded requirements carried forward from FY 1997 and unanticipated accounting adjustments in aviation organic repair. The increase in Operating Costs from FY 1996 to FY 1997 essentially reflects the impact of merging the Logistics Support Activities activity group with the Supply Management, Navy activity group in FY 1997 while the further increase in FY 1998 is largely the result of functional transfers relating to FISC regional industrial partnering and increased Navy disposal costs which are borne by this activity group. These increased operating costs had the effect of masking an 11 percent decrease in Supply Operations Costs since FY 1996.

The retail program trends has been affected by the elimination of fast moving commodities such as food, medical, clothing, and general use consumables sold through the Self Service Mart (SERVMART). Instead, the retail program has shifted towards insurance (low demand spare and repair parts) allowance materials.

Overview

Activity Accomplishments

The NWCF is composed of seven primary activity groups consisting of 17 secondary activity groupings. Facing declining workload, BRAC closings, and organizational changes, the highly skilled workforce at the NWCF activities continue to press for economies and efficiencies in all elements of their organizations. Whether their efforts have been directed at computer systems, combat systems, or the workforce itself, the NWCF activity successes have been unparalleled. The following are just a few of the many important achievements of these groups.

Supply Operations - Inventory investments at all echelons of supply management were reduced from about $32 billion in FY 1989 to about $15 billion in FY 1998 (before adjustment to approximate historical cost). This 54 percent reduction was accomplished, in part, by utilizing technologies to enhance total asset visibility; by reengineering business practices such as satisfying small purchase demand through the Purchase Card and Direct Vender Delivery programs; and by outsourcing SERVMART operations with organizations such as the General Services Administration and the National Industries for the Blind.

Depot Maintenance – In FY 1998, the NSYs have improved their schedule performance to 99.1%. NADEPS have won Environmental quality awards and the Vice President Gore's National Performance Review's "Hammer" award for reinvention efforts. The Marine Corps Depots made advances in AAV, M1A1 Tank and Light Armored Vehicle overhaul processes.

Research and Development – In FY 1998, the DoN's research activities developed and demonstrated many advances in sea, undersea, air, and land warfare technology. Examples of such advances include Submarine Periscope Detection, Electronic Countermeasures Transmitters, and Electromagnetic Turbulence Control. Examples of program specific advances include the AN/WSN-7 Ring Laser Gyro Navigator and the Towed Active Receiver Subsystem. Other advances were made in Modulating Retro Reflectors for Free Space Optical Data Transfer using Multiple Quantum Well Technology, and X-ray Backscatter Tomography.

Transportation – The MSC increased its NFAF and SMS forces by nine ships over the last three years in response to efforts to increase operational efficiency and reduce costs.

Systems Accomplishments

Defense Industrial Financial Management System (DIFMS) - DIFMS is the interim migratory finance and accounting system for the NWCF Depot Maintenance and Research and Development activity groups. Through FY 1998, six systems have been consolidated into DIFMS.   When this system initiative is completed, a total of 13 systems will have been consolidated into DIFMS. These 13 systems, which have operated on 25 operational data bases, will be collapsed into 7 DIFMS operational data bases. In addition, DIFMS has stabilized its software with on application software version thereby eliminating four previous operating versions.

Defense Working Capital Accounting System (DWAS) - DWAS is the interim migratory finance and accounting system for the NWCF Base Support activity group. The first Base Support PWC conversion to this off the shelf system is anticipated by April 1999 with all PWCs implemented by mid FY 2002. Upon completion of all PWCs, two existing systems will have been consolidated into DWAS and 10 operational data bases will have been replaced by one DWAS operational data base.

Oracle Federal Financials (previously reported as Corps of Engineers Financial Management System with name change to Defense Joint Accounting System (DJAS)). DJAS was not going to be operational by Year 2000, therefore the Transportation Command and DFAS approved a commercial off the shelf (COTS) solution for the NWCF Transportation activity group, MSC. That COTS solution is Oracle Federal Financials which will be deployed by 1 October 1999.

Material Financial Control System (MFCS) - MFCS is the interim migratory financial system for the NWCF Supply Management activity group for both the wholesale and retail segments of the inventory. During FY 1998, system software development for the allotment accounting and expenditure processing data base took place. User acceptance testing is scheduled to begin in January 1999 with conversion to the new version of MFCS in October 1999. When this system initiative is completed, a total of five systems will have consolidated into MFCS of which two shipboard systems have already been consolidated.

Financial Management Issues

Supply Management Inventory Valuation and Operating Results.

The Statement of Federal Financial Accounting Standards Number 3, Accounting for Inventory and Related Property, was issued by the Federal Accounting Standards Advisory Board (FASAB) in October 1993. The standard prescribes inventory be valued at either historical cost or latest acquisition cost. The latest acquisition cost method, which requires the recognition of an allowance account for unrealized holding gains and losses, is used in the NWCF to arrive at an approximation of historical cost of inventory. The adjustments made to the allowance account are a component of the cost of goods sold (COGS). The FASAB standard is incorporated in the DoD Financial Management Regulation (FMR) 7000.14-R, Volume 11B, which also describes procedures for implementation.

The accounting policy and procedures staff from the USD(C) and DFAS, with support from the DoN staff and the Naval Audit Service (NAS), have developed a model to calculate the value of inventory and COGS using the general ledger of the Supply Management activity group. Initially, this group encountered significant difficulties in producing reliable allowance account and COGS values. The model is now producing inventory values which are considered representative of the historical cost value. However, the calculation for the COGS is still not producing reliable results and is affecting the Net Costs of Operations.

The inventory value calculated for the Navy segment of the Supply Management activity group for FY 1998 of $14,102 million is considered representative of the historical cost value and compares favorably with the FY 1997 value of $12,692 million.

The COGS calculated for FY 1997 resulted in a Net Cost of Operations of negative $1,923.8 million. In FY 1996, the Net Cost of Operations, after adjustment for an error, was a negative $1,724.9 million. In FY 1998, the Net Cost of Operations was positive $203.8 million. None of these values should be considered reliable. One area under review that is affecting these results is the value of inventory being transferred to disposal. The value appears to be larger than warranted considering the significant quantities of inventory being returned to the supply system without cost. Another area unduly influencing the calculation is the annual standard price changes made on inventory items. There are also auditor concerns regarding the proper use of some gain and loss accounts and some equity accounts in the calculation. The USD (C), DFAS, DoN, and NAS recognize additional work must be done and a consenses reached in the model to calculate the COGS.

Cash Management.

The cash position of the NWCF is improving as noted in the charts above. However, the lack of timely reporting of collections and disbursements hampers analysis, error correction, and prevention of violations. As the accounting organization, DFAS is working to improve the accuracy and timeliness of cash reporting.

The DoN and DFAS are jointly working in several areas to improve cash management. The procedure of transferring collections and disbursements to the departmental level was eliminated for FY 1997 business. DFAS established new general ledger accounts at each activity to represent an activity level cash balance. In FY 1998, in addition to not transferring FY 1998 collections and disbursements to the departmental level, DFAS with DoN support developed procedures to move non-expenditure transfers of cash from the departmental level ledgers to the activity group level. While the non-expenditure transfers have been identified to the proper activity group and reflected in activity group reports, these transfers must still be recorded in the specific activity general ledger. This is planned to be accomplished during FY 1999. Lastly, DFAS and DoN plan to move collections and disbursements, which were transferred to the departmental level during FY 1995 and FY 1996, back to activity level ledgers. When this is completed in FY 1999, activity level ledgers will contain all cash transactions associated with that activity since cash management responsibility was returned to the DoN in FY 1995. The DoN and DFAS also continue to review activity level collection and disbursement processing procedures to identify reconciliation problems and develop methods for handling aged and pre-NWCF (i.e., DBOF) transactions.

Undistributed Disbursements and Collections.

The NWCF Fund Balance with Treasury represents the value of disbursements, collections, and non-expenditure transfers processed through the DFAS reporting network to the DoN NWCF sub-limit in the U.S. Treasury. The DFAS/DoN Centralized Expenditure and Reimbursement Processing System (CERPS) is the designated system for reporting disbursement and collection data to the U.S. Treasury. CERPS also provides transaction level disbursement and collection data to the DFAS Operating Locations (OPLOCs) for processing into each individual NWCF activity general ledger.

While the issue of Cash Management mentioned in the previous issue addresses the reestablishment of a cash balance at the activity level, the actual recording of collections, disbursements, and non-expenditure transfers at the activity level in the DBOF (After FY 1991) environment has resulted in significant problems. These problems manifest themselves as undistributed collections and undistributed disbursements and as cash reconciliation differences. Problems with undistributed values will affect all financial statements, especially the Balance Sheet and Statement of Budgetary Resources.

Significant differences exist between the disbursements and collections reported to the U.S. Treasury and the disbursements and collections recorded in the NWCF activity general ledger. The differences between the U.S. Treasury and activity ledgers are recorded in undistributed disbursement and undistributed collection accounts. When activity level values are higher than the U.S. Treasury values, these accounts contain abnormal balances. The DFAS has initiated actions to investigate potential problems with the values reported in CERPS and with activity general ledger processing. Some indications of problems are the pre-posting of transactions into the activity ledgers prior to processing officially through the CERPS. Also, it appears that specific coding in the transactions are causing collections to be processed as negative disbursements in CERPS. However, the transactions are being corrected when processed into the activity ledgers, but are not being “recycled” through CERPS. While there may be no impact upon the Fund Balance with Treasury, this causes distortions between the U.S. Treasury and activity level disbursement and collection values.

Values reported in the undistributed disbursement and collection accounts are normally reflected as reductions to the values being reported for accounts payable and accounts receivable, respectively, to simulate the distribution of the undistributed values. Since the undistributed disbursements and collections accounts contained abnormal values of over $1 billion each, increases of about $1 billion rather than reductions of $1 billion were applied to the accounts payable and accounts receivable, thus overstating the values reported in the DoN NWCF CFO for FY 1996. Since significant abnormal balances also existed in FY 1997, rather than overstate accounts payable and accounts receivable again, undistributed disbursements and undistributed collections were reported in line 4.a.(4), Other Federal Entity Liabilities, of the Statement of Financial Position. This practice remains unchanged in the FY 1998 Balance Sheet where undistributed collections and disbursements are reported on line 4.a.(4). DFAS continues to investigate cash processing and reconciliation problems.

Limitations of the Financial Statements

The financial statements have been prepared to report the financial position and NOR for the DoN, pursuant to the requirements of the 31 U.S.C. 3515(b).

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

The statements should be read with the realization that they are for a component of the U.S. Government , a sovereign entity. One implication of this is that the liabilities cannot be liquidated without legislation that provides resources to do so.

DEPARTMENT OF THE NAVY

NAVY WORKING CAPITAL FUND

PRINCIPAL FINANCIAL STATEMENTS

Department of Defense
Navy Working Capital Fund
CONSOLIDATED BALANCE SHEET
As of September 30, 1998
(in thousands)

	FY 1998
ASSETS	
1. Entity Assets:	
A. Intragovernmental	
1. Fund Balance With Treasury (Note 2)	$1,192,502
2. Investments, Net (Note 4)	0
3. Accounts Receivable, Net (Note 5)	626,261
4. Other Assets (Note 6)	276,590
B. Total Intragovernmental	$2,095,353
C. Investments, Net (Note 4)	0
D. Accounts Receivable, Net (Note 5)	270,706
E. Loans Receivable and Related Foreclosed Property, Net (Note 7)	0
F. Cash and Other Monetary Assets (Note 3)	0
G. Inventory and Related Property, Net (Note 8)	16,424,928
H. General Property, Plant and Equipment (Note 9)	4,393,806
I. Stewardship Assets (National Defense PP&E, etc.)	N/A
J. Other Assets (Note 6)	1,326,489
K. Total Entity Assets	$24,511,282
2. Non-Entity Assets:	
A. Intragovernmental	
1. Fund Balance With Treasury (Note 2)	0
2. Accounts Receivable, Net (Note 5)	0
3. Other Assets (Note 6)	0
B. Total Intragovernmental	$0
C. Accounts Receivable, Net (Note 5)	0
D. Cash and Other Monetary Assets (Note 3)	0
E. Other Assets (Note 6)	0
F. Total Non-Entity Assets	$0
3. Total Assets	$24,511,282

The accompanying notes are an integral part of these statements.

Department of Defense
Navy Working Capital Fund
CONSOLIDATED BALANCE SHEET
As of September 30, 1998
(in thousands)

	FY 1998
LIABILITIES	
4. Liabilities Covered by Budgetary Resources:	
A. Intragovernmental:	
1. Accounts Payable	$735,881
2. Environmental Cleanup (Note 11)	0
3. Debt (Note 10)	1,094,710
4. Other Liabilities (Notes 11,12, and 15)	1,367,352
B. Total Intragovernmental	$3,197,943
C. Accounts Payable	3,067,174
D. Liabilities for Loan Guarantees	0
E. Military Retirement Benefits and Other Employment Related Actuarial Liabilities (Note 13)	0
F. Environmental Cleanup (Note 11)	0
G. Other Liabilities (Notes 11,12, and 15)	873,550
H. Total Liabilities Covered by Budgetary Resources	$7,138,667
5. Liabilities Not Covered by Budgetary Resources:	
A. Intragovernmental:	
1. Accounts Payable	0
2. Debt (Note 10)	0
3. Environmental Cleanup (Note 11)	0
4. Other Liabilities (Notes 11,12, and 15)	0
B. Total Intragovernmental	$0
C. Accounts Payable	0
D. Debt (Note 10)	0
E. Military Retirement Benefits and Other Employment Related Actuarial Liabilities (Note 13)	1,176,474
F. Environmental Cleanup (Note 11)	0
G. Other Liabilities (Notes 11 and 12)	0
H. Total Liabilities Not Covered by Budgetary Resources	$1,176,474
6. Total Liabilities	$8,315,141
NET POSITION	
7. Unexpended Appropriations (Note 14)	0
8. Cumulative Results of Operations	16,196,141
9. Total Net Position	$16,196,141
10. Total Liabilities and Net Position	$24,511,282

The accompanying notes are an integral part of these statements.

Department of Defense
Navy Working Capital Fund
CONSOLIDATED STATEMENT OF NET COST
For the period ending September 30, 1998
(in thousands)

	FY 1998
1. Program Costs	
A. Intragovernemntal	$18,931,384
B. With the Public	188,409
C. Total Program Cost	$19,119,793
D. Less: Earned Revenues	(19,066,487)
E. Net Program Costs	$53,306
2. Costs Not Assigned to Programs	0
3. Less: Earned Revenues Not Attributable to Programs	0
4. Deferred Maintenance (Note 17)	0
5. Net Cost Of Operations	$53,306

Additional information included in Note 16.

The accompanying notes are an integral part of these statements.

Department of Defense
Navy Working Capital Fund
CONSOLIDATING STATEMENT OF NET COST
For the period ending September 30, 1998
(in thousands)

	FY 1998	DM-Shipyards	DM-Aviation	DM-Other (MC)
1. Program Costs				
A. Program A: Navy Working Capital Fund				
1. Intragovernmental	$18,931,384	$2,619,269	$1,527,341	$176,869
2. With the Public	188,409	7,012	40	44,875
3. Total Program Cost	$19,119,793	$2,626,281	$1,527,381	$221,744
4. Less: Earned Revenues	(19,066,487)	(2,709,688)	(1,509,053)	(211,978)
5. Net Program Costs	$53,306	($83,407)	$18,328	$9,766
2. Costs Not Assigned to Programs	0	0	0	0
3. Less: Earned Revenues Not Attributable to Programs	0	0	0	0
4. Deferred Maintenance (Note 17)	0	0	0	0
5. Net Cost Of Operations	$53,306	($83,407)	$18,328	$9,766

Additional information included in Note 16.

The accompanying notes are an integral part of these statements.

Department of Defense
Navy Working Capital Fund
CONSOLIDATING STATEMENT OF NET COST
For the period ending September 30, 1998
(in thousands)

	Ordnance	Transportation	Base Support	Information Services
1. Program Costs				
A. Program A: Navy Working Capital Fund				
1. Intragovernmental	$427,089	$1,276,887	$1,911,844	$241,506
2. With the Public	1,663	0	41,677	0
3. Total Program Cost	$428,752	$1,276,887	$1,953,521	$241,506
4. Less: Earned Revenues	(636,907)	(1,342,397)	(1,916,163)	(241,677)
5. Net Program Costs	($208,155)	($65,510)	$37,358	($171)
2. Costs Not Assigned to Programs	0	0	0	0
3. Less: Earned Revenues Not Attributable to Programs	0	0	0	0
4. Deferred Maintenance (Note 17)	0	0	0	0
5. Net Cost Of Operations	($208,155)	($65,510)	$37,358	($171)

Additional information included in Note 16.

The accompanying notes are an integral part of these statements.

Department of Defense
Navy Working Capital Fund
CONSOLIDATING STATEMENT OF NET COST
For the period ending September 30, 1998
(in thousands)

	Research & Development	Supply Management	Component	Eliminations
1. Program Costs				
A. Program A: Navy Working Capital Fund				
1. Intragovernmental	$6,874,237	$6,327,752	$408,730	($2,860,140)
2. With the Public	60,469	16,270	16,403	0
3. Total Program Cost	$6,934,706	$6,344,022	$425,133	($2,860,140)
4. Less: Earned Revenues	(6,950,864)	(6,407,900)	0	2,860,140
5. Net Program Costs	($16,158)	($63,878)	$425,133	$0
2. Costs Not Assigned to Programs	0	0	0	0
3. Less: Earned Revenues Not Attributable to Programs	0	0	0	0
4. Deferred Maintenance (Note 17)	0	0	0	0
5. Net Cost Of Operations	($16,158)	($63,878)	$425,133	$0

Additional information included in Note 16.

The accompanying notes are an integral part of these statements.

Department of Defense
Navy Working Capital Fund
CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION
For the period ending September 30, 1998
(in thousands)

	FY 1998
1. Net Cost of Operations	$53,306
2. Financing Sources (Other than Exchange Revenues):	
A. Appropriations Used	0
B. Taxes (and Other Non-exchange Revenue)	0
C. Donations (Non-exchange Revenue)	0
D. Imputed Financing	408,730
E. Transfers-In	3,934,548
F. Transfers-Out	(3,910,172)
3. Net Results of Operations	$379,800
4. Prior Period Adjustments (Note 18)	(965,226)
5. Net Change in Cumulative Results of Operations	(585,426)
6. Increase (Decrease) in Unexpended Appropriations	1,033,833
7. Change in Net Position	448,407
8. Net Position-Beginning of the Period	15,747,734
9. Net Position-End of Period	$16,196,141

Additonal information included in Note 18.

The accompanying notes are an integral part of these statements.

Department of Defense
Navy Working Capital Fund
CONSOLIDATING STATEMENT OF CHANGES IN NET POSITION
For the period ending September 30, 1998
(in thousands)

	FY 1998	DM-Shipyards	DM-Aviation
1. Net Cost of Operations	$53,306	($83,407)	$18,328
2. Financing Sources (Other than Exchange Revenues):			
A. Appropriations Used	0	0	0
B. Taxes (and Other Non-exchange Revenue)	0	0	0
C. Donations (Non-exchange Revenue)	0	0	0
D. Imputed Financing	408,730	0	0
E. Transfers-In	3,934,548	0	2,543
F. Transfers-Out	(3,910,172)	(42,256)	(7,859)
3. Net Results of Operations	$379,800	$41,151	($23,644)
4. Prior Period Adjustments (Note 18)	(965,226)	(56,291)	(58,102)
5. Net Change in Cumulative Results of Operations	(585,426)	(15,140)	(81,746)
6. Increase (Decrease) in Unexpended Appropriations	1,033,833	159,139	55,973
7. Change in Net Position	448,407	143,999	(25,773)
8. Net Position-Beginning of the Period	15,747,734	848,788	3,451
9. Net Position-End of Period	$16,196,141	$992,787	($22,322)

Additonal information included in Note 18.

The accompanying notes are an integral part of these statements.

Department of Defense
Navy Working Capital Fund
CONSOLIDATING STATEMENT OF CHANGES IN NET POSITION
For the period ending September 30, 1998
(in thousands)

	DM-Other (MC)	Ordnance	Transportation
1. Net Cost of Operations	$9,766	($208,155)	($65,510)
2. Financing Sources (Other than Exchange Revenues):			
A. Appropriations Used	0	0	0
B. Taxes (and Other Non-exchange Revenue)	0	0	0
C. Donations (Non-exchange Revenue)	0	0	0
D. Imputed Financing	0	0	0
E. Transfers-In	0	0	0
F. Transfers-Out	0	(329,757)	(75)
3. Net Results of Operations	($9,766)	($121,602)	$65,435
4. Prior Period Adjustments (Note 18)	(8,414)	(9,120)	0
5. Net Change in Cumulative Results of Operations	(18,180)	(130,722)	65,435
6. Increase (Decrease) in Unexpended Appropriations	4,681	(19,439)	46,988
7. Change in Net Position	(13,499)	(150,161)	112,423
8. Net Position-Beginning of the Period	56,658	384,357	(389,176)
9. Net Position-End of Period	$43,159	$234,196	($276,753)

Additonal information included in Note 18.

The accompanying notes are an integral part of these statements.

Department of Defense
Navy Working Capital Fund
CONSOLIDATING STATEMENT OF CHANGES IN NET POSITION
For the period ending September 30, 1998
(in thousands)

	Base Support	Information Services	Research & Development
1. Net Cost of Operations	$37,358	($171)	($16,158)
2. Financing Sources (Other than Exchange Revenues):			
A. Appropriations Used	0	0	0
B. Taxes (and Other Non-exchange Revenue)	0	0	0
C. Donations (Non-exchange Revenue)	0	0	0
D. Imputed Financing	0	0	0
E. Transfers-In	0	1,944	9,494
F. Transfers-Out	14,588	0	(84,197)
3. Net Results of Operations	($22,770)	$2,115	($58,545)
4. Prior Period Adjustments (Note 18)	4,968	(221)	(5,382)
5. Net Change in Cumulative Results of Operations	(17,802)	1,894	(63,927)
6. Increase (Decrease) in Unexpended Appropriations	95,848	(2,609)	(45,133)
7. Change in Net Position	78,046	(715)	(109,060)
8. Net Position-Beginning of the Period	574,635	(110,323)	(220,904)
9. Net Position-End of Period	$652,681	($111,038)	($329,964)

Additonal information included in Note 18.

The accompanying notes are an integral part of these statements.

Department of Defense
Navy Working Capital Fund
CONSOLIDATING STATEMENT OF CHANGES IN NET POSITION
For the period ending September 30, 1998
(in thousands)

	Supply Management	Component	Eliminations
1. Net Cost of Operations	($63,878)	$425,133	$0
2. Financing Sources (Other than Exchange Revenues):			
A. Appropriations Used	0	0	0
B. Taxes (and Other Non-exchange Revenue)	0	0	0
C. Donations (Non-exchange Revenue)	0	0	0
D. Imputed Financing	0	408,730	0
E. Transfers-In	3,920,567	0	0
F. Transfers-Out	(3,460,616)	0	0
3. Net Results of Operations	$523,829	($16,403)	$0
4. Prior Period Adjustments (Note 18)	(832,664)	0	0
5. Net Change in Cumulative Results of Operations	(308,835)	(16,403)	0
6. Increase (Decrease) in Unexpended Appropriations	888,852	(150,467)	0
7. Change in Net Position	580,017	(166,870)	0
8. Net Position-Beginning of the Period	12,367,315	2,232,933	0
9. Net Position-End of Period	$12,947,332	$2,066,063	$0

Additonal information included in Note 18.

The accompanying notes are an integral part of these statements.

Department of Defense
Navy Working Capital Fund
COMBINED STATEMENT OF BUDGETARY RESOURCES
For the period ending September 30, 1998
(in thousands)

	FY 1998
BUDGETARY RESOURCES:	
1. Budget Authority	$5,232
2. Unobligated Balance - Beginning of Period	1,988,427
3. Net Transfers Prior-Year Balance, Actual (+/-)	62,992
4. Spending Authority from Offsetting Collections	21,356,962
5. Adjustments	(308,926)
6. Total Budgetary Resources	$23,104,687
STATUS OF BUDGETARY RESOURCES:	
7. Obligations Incurred	20,472,046
8. Unobligated Balances - Available	2,632,641
9. Unobligated Balances - Not Available	0
10. Total, Status of Budgetary Resources	$23,104,687
OUTLAYS:	
11. Obligations Incurred	20,472,046
12. Less: Spending Authority From Offsetting Collections and Adjustments	(21,356,962)
13. Obligated Balance, Net - Beginning of Period	3,004,070
14. Obligated Balance Transferred, Net	1,501
15. Less: Obligated Balance, Net - End of Period	(2,502,140)
16. Total Outlays	($381,485)

Additonal information included in Note 19.

The accompanying notes are an integral part of these statements.

Department of Defense
Navy Working Capital Fund
COMBINED STATEMENT OF FINANCING
For the period ending September 30, 1998
(in thousands)

	Total
1. OBLIGATIONS AND NONBUDGETARY RESOURCES:	
A. Obligations Incurred	$20,472,046
B. Less: Spending Authority for Offsetting Collections and Adjustments	(21,356,962)
C. Donations Not in the Entity's Budget	0
D. Financing Imputed for Cost Subsidies	408,730
E. Transfers-In (Out)	24,376
F. Exchange Revenue Not in the Entity's Budget	0
G. Other	16,407
H. Total Obligations as Adjusted and Nonbudgetary Resources	($435,403)
2. RESOURCES THAT DO NOT FUND NET COST OF OPERATIONS:	
A. Change in Amount of Goods, Services, and Benefits Ordered but Not Yet Received or Provided	163,767
B. Costs Capitalized on the Balance Sheet	4,309,589
C. Financing Sources That Fund Costs of Prior Periods	0
D. Other	135,745
E. Total Resources That Do Not Fund Net Cost of Operations	$4,609,101
3. COSTS THAT DO NOT REQUIRE RESOURCES:	
A. Depreciation and Amortization	209,174
B. Revaluation of Assets and Liabilities	112,598
C. Other	(4,442,164)
D. Total Costs That Do Not Require Resources	($4,120,392)
4. Financing Sources Yet to be Provided	0
5. Net Cost of Operations	$53,306

Additional information included in Note 20.

The accompanying notes are an integral part of these statements.

NAVY WORKING CAPITAL FUND

CONSOLIDATED

FOOTNOTES TO THE PRINCIPAL STATEMENTS

Footnotes

NOTES TO THE FISCAL YEAR 1998 PRINCIPAL STATEMENTS
NAVY WORKING CAPITAL FUND
CONSOLIDATED NOTES
PERIOD ENDING 30 SEPTEMBER 1998

Note 1. Significant Accounting Policies:

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) Navy Working Capital Fund (NWCF), as required by the Chief Financial Officers (CFO) Act expanded by the Government Management Reform Act (GMRA) of 1994, and other appropriate legislation. This report has also been prepared to provide information with which Congress, agency managers, the public, and other interested parties can assess management performance. The financial statements have been prepared from the books and records of the DON, in accordance with Department of Defense (DoD) Guidance on Form and Content of DoD Audited Financial Statements, as adopted from Office of Management and Budget (OMB) Bulletin No. 97-01, “Form and Content of Agency Financial Statements”. These statements, therefore, are different from the financial reports, also prepared by DON pursuant to OMB, DoD, the Defense Finance and Accounting Service (DFAS) and DON directives, that are used to monitor and control DON’s use of budgetary resources.

The consolidated statements include the accounts and transactions of the DON NWCF activities. All policies and procedures, unless otherwise noted, are in compliance with the Assistant Secretary of the Navy (Financial Management and Comptroller) (ASN(FM&C)) guidance and the DoD Working Capital Fund guidance implemented by DFAS.

The amounts presented in the financial statements and footnotes (Fiscal Year (FY) 1998) are rounded to the nearest thousand of dollars.

B. Reporting Entity

FY 1998 represents the eighth year that the DON has prepared financial statements as required by the CFO Act. The CFO Act requires that the DON prepare and have audited, financial statements for each revolving fund and account that performed substantial commercial functions during the preceding fiscal year.

The consolidating NWCF financial statements include all activities and functions previously financed through the Navy Industrial Fund and DON Stock Fund which were converted to the Defense Business Operations Fund (DBOF) on 1 October 1991. The Under Secretary of Defense (Comptroller) (USD(C)) memorandum of 11 December 1996 eliminated the DBOF and established four working capital funds. One of the four working capital funds is

NWCF CONSOLIDATED NOTES

the NWCF. Establishment of the NWCF did not change any previous organizational reporting structure.

The following identifies the NWCF primary and secondary activity groups.

Primary and Secondary Activity Groups
Depot Maintenance - Shipyards
Depot Maintenance - Aviation
Depot Maintenance - Other (Marine Corps)
Ordnance
Transportation
Base Support
    Public Works Centers (PWCs)
    Naval Facilities Engineering Service Center (NFESC)
Information Services
    Naval Computer and Telecommunications Command (NAVCOMTELCOM)
    Navy, Fleet Material Support Office (FMSO)
    Naval Reserve Force (COMNAVRESFOR)
Research and Development
    Naval Surface Warfare Center (NSWC)
    Naval Air Warfare Center (NAWC)
    Naval Undersea Warfare Center (NUWC)
    Naval Research Laboratory (NRL)
    Space and Naval Warfare Systems Centers (SSCs)
Supply Management
    Navy
    Marine Corps
Navy Component

All significant intra-agency transactions have not been eliminated. Data to eliminate intra-agency transactions is not readily available in financial systems supporting this fund.

In FY 1996 the Navy Distribution Depots activity group was combined with the Supply Management (Navy) activity group while the Navy Logistics Support Activities activity group was combined with Supply Management (Navy) in FY 1997. The Defense Printing Service transferred from the DON Commander, Naval Supply Systems Command (COMNAVSUPSYS-COM) to the Defense Logistics Agency (DLA) on 1 October 1996. The general ledger transferred in whole to DLA at that time. However, certain residual balances on the SF 133 Report on Budget Execution continued to be reported on the Consolidated NWCF SF 133, pending DFAS guidance on the proper reporting of the transfer. Final DFAS guidance was issued in October 1998, and the residual obligated balance of $1,501 thousand was transferred to DLA. This transfer impacts the Navy Component Statement of Budgetary Resources Lines 3 and 14.

NWCF CONSOLIDATED NOTES

Some reporting entity changes occurred during FY 1998. The first change involved a re-structuring between NWCF activity groups. Since the NFESC is an integral part of the Base Support mission, Program Budget Decision (PBD) 426 of 30 December 1996 realigned the NFESC, in FY 1998, from the Research and Development activity group to the PWCs as a separate and distinct activity group within the Base Support activity group. The NFESC are a coequal of the PWCs within the Base Support activity group. This new alignment was reflected in the 30 September 1998 reports. The realignment has a neutral effect on the FY 1998 Consolidated NWCF CFO Principal Statements and Notes. The second change involved the renaming of the Depot Maintenance - Ordnance activity group. The Ordnance group is involved primarily in building, storing, and shipping of military weapons and does not fit the traditional Depot Maintenance definition. Accordingly, PBD 426 removed the Army and Navy Ordnance activities from the Depot Maintenance activity group and established them in a separate activity group called Ordnance. This change in activity group became effective on 1 October 1997, pending modification of charters and final approval of the Defense Working Capital Funds (DWCF) Corporate Board. All other aspects of the new activity group remain unchanged.

The third change involved the disestablishment of the Research and Development - Naval Command, Control, and Ocean Surveillance Center (NCCOSC) secondary activity on 1 October 1997, in accordance with the Base Realignment and Closure (BRAC) 1995. The two operating divisions were renamed as the SSC San Diego, CA and SSC Charleston, SC respectively and report directly to the Commander, Space and Naval Warfare Systems Command (COMSPAWARSYSCOM). Therefore, this is the first fiscal year for reporting the Research and Development - SSCs secondary activity group in the CFO financial statements.

C. Budgets and Budgetary Accounting

DON NWCF funded activities provide services and materials to DoD components and other federal government agencies through buyer-seller relationships. The buyers, which are the Navy NWCF activities' customers, identify requirements which justify the need for funds from Congress. DON NWCF activities operate under the revolving fund concept whereby customers reimburse the activities' NWCF to cover the cost of services or material provided. The Navy industrial activities financial management systems which operate under NWCF accumulate all cost incurred in various programs or jobs plus overhead which are subsequently billed to the customers. NWCF finances the purchase of consumable and repairable items which are held in inventory at stock activities until issued with charge to the customer and reimbursement to NWCF.

As shown below the DON NWCF recorded an operating gain in FY 1998 of $371,830 thousand.

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Total Program Costs, Earned Revenues and Net Cost of Operations
by NWCF Primary and Secondary Activity Group

(in thousands)

Activity Group	Total Program Cost	Earned Revenues	Net Cost of Operations
Depot Maintenance – Shipyards	$2,626,281	$2,709,688	($83,407)
Depot Maintenance – Aviation	1,527,380	1,509,053	18,327
Depot Maintenance – Other (Marine Corps)	221,744	211,978	9,766
Ordnance	428,752	636,907	(208,155)
Transportation	1,276,887	1,342,397	(65,510)
Base Support			
PWC's	1,877,931	1,841,587	36,344
NFESC	75,590	74,576	1,014
Information Services			
NAVCOMTELCOM	132,294	134,059	(1,765)
FMSO	91,601	88,912	2,689
COMNAVRESFOR	17,610	18,706	(1,096)
Research and Development			
NSWC	2,461,709	2,484,833	(23,124)
NAWC	2,099,233	2,103,079	(3,846)
NUWC	738,810	735,524	3,286
NRL	536,826	531,401	5,425
SSCs	1,098,127	1,096,026	2,101
Supply Management (Navy)	6,049,919	6,253,695	(203,776)
Supply Management (Marine Corps)	294,102	154,205	139,897
Navy Component			
Total	$21,554,796*	$21,926,626*	($371,830)

*These amounts do not reflect the following: (1) the eliminating entries of $2,860,140 thousand for intra-activity revenue and cost of goods and services sold, (2) the Component level adjusting entries for imputed revenues and expenses of $408,730 thousand for Office of Personnel Management Pensions and Other Retirement Benefits (ORB) (see Notes 16.H, 16.I and 18.B), and (3) the amount of change in workers' compensation from FY 1997 to FY 1998 for the Other Actuarial Liability increase of $16,403 thousand (see Notes 13,16.H and 16.I).

The net costs of operations includes the implementation by the USD(C) and DFAS of DoD Financial Management Regulation (FMR) 7000.14-R, Volume 11B procedures for Supply Management (Navy) inventory valuation and Cost of Goods Sold (COGS) model. The Navy is considered the prototype in the implementation of this model. The treatment of the Supply Management (Navy) cost of transfers to disposal overstates expenses by assigning a larger cost to disposal than is warranted considering the significant quantities of inventory that are sent to disposal which are received from customers without cost. DFAS, in their implementation of the

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USD(C) concept of Holding Gains and Losses/Cost of Goods and Services Sold (as specified in DoD FMR 7000.14-R, Volume 11B), has stated that the issue of how to consider disposal actions needs further study to counter the understatement of costs of sales and the overstatement of expenses. USD(C) has advised that the treatment of disposal actions in the operating results calculations is under review and they are considering applying customer returns without credit as an offset to disposal actions. The treatment of disposal actions is a base line requirement in moving to an accounting Net Operating Result that can be used in the budget development.

D. Basis of Accounting

Transactions are recorded on the accrual basis of accounting. Under this method, revenues are recognized when earned and expenses are recognized when a liability is incurred without regard to receipt or payment of cash. Budgetary accounting facilitates compliance with legal constraints and controls over the use of federal funds. All significant intra-agency transactions have not been eliminated. Data to eliminate intra-agency transactions is not readily available in financial systems supporting this fund.

E. Revenues and Other Financing Sources

Revenue which is earned primarily from providing services, materials and products to DON and others is recognized on a percentage of completion or material issue basis in accordance with NWCF guidance as promulgated by the USD(C). Revenue related to the distribution of inventory and procurement support is recognized at the point inventory items are sold or for the billing of work performed against reimbursable work orders. In August 1996, estimating of Revenues and Funds Collected, and sales, ceased for ships and naval activities in the Supply Management (Navy) activity group. See Note 23 Depot Maintenance - Aviation for disclosure of non-compliance with the revenue recognition policy.

F. Accounting for Intragovernmental Activities

The DON NWCF activities interact with, and are dependent upon, other financial activities of the Government as a whole. Therefore, these financial statements do not reflect the results of all financial decisions applicable to the agency as though the agency were a stand alone entity.

1. The DON's proportionate share of the public debt and related expenses of the Federal Government are not included. Debt issued by the Federal Government and the related interest costs are not apportioned to Federal agencies. The 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.

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

3. NWCF civilian employees participate in the Civil Service Retirement System (CSRS) and Federal Employees Retirement System (FERS), while military personnel are covered by the Military Retirement System (MRS). Additionally, employees and personnel covered by FERS and MRS are also covered by Social Security. The individual NWCF activity groups fund a portion of pension benefits under these retirement systems but do not disclose the assets or actuarial data on the accumulated plan benefits or unfunded pensions liabilities of its employees. Reporting such amounts is the responsibility of the Office of Personnel Management for CSRS and FERS. The NWCF Departmental level CFO statements have recognized an imputed expense for civilian employee pensions and other retirement benefits in the Statement of Net Cost and have recognized imputed revenue for the civilian employee pensions and other retirement benefits in the Statement of Changes in Net Position. The retirement actuarial liabilities for military MRS is reported on the CFO financial statements of the Military Retirement Trust Fund. In FY 1998, the individual NWCF activity groups contributed the following amounts to the retirement plans, Social Security and to the Thrift Savings Plan (TSP). See next page.

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(in thousands)

Activity Group	CSRS	FERS	MRS	Social Security	TSP	Total
Depot Maintenance – Shipyards	$57,837	$29,211	$0	$20,390	$11,444	$118,882
Depot Maintenance – Aviation	24,921	19,205		13,113	7,750	64,989
Depot Maintenance – Other (Marine Corps)	2,624	3,674		2,584	1,429	10,311
Ordnance	6,046	6,021		4,048	2,480	18,595
Transportation	8,042	9,190		9,558	3,652	30,442
Base Support						
PWCs	18,050	19,848		12,190	7,674	57,762
NFESC	952	799		793	354	2,898
Information Services						
NAVCOMTELCOM	2,772	2,035		1,320	850	6,977
FMSO *	3,875			1,314	437	5,626
COMNAVRESFOR	118	224		144	86	572
Research and Development						
NSWC	35,862	41,241		25,807	17,024	119,934
NAWC	27,461	36,483		22,545	15,114	101,603
NUWC	11,137	11,070		6,979	4,651	33,837
NRL	7,079	9,222		8,138	3,752	28,191
SSCs	13,618	12,421		7,776	5,161	38,976
Supply Management (Navy) **	34,443			14,546	5,289	54,278
Supply Management (Marine Corps)***						
Total	$254,837	$200,644	$0	$151,245	$87,147	$693,873

*Information on contributions related to the identification of specific amounts to CSRS and FERS is not readily available.

**The system (Defense Business Management System (DBMS)) supporting this activity group does not have individual CSRS and FERS contributed amounts.

***Contributions related to retirement plans are reported on statements for the Operation and Maintenance, Marine Corps appropriation.

4. Most legal actions, other than contract claims, to which the NWCF may be a named party are covered by the provisions of the Federal Tort Claims Act and the provisions of Title 10, United States Code (U.S.C.), Chapter 163, governing military claims. Either because payments under these statutes are limited to amounts well below the threshold of materiality for claims payable from the NWCF or because payments will be from the permanent, indefinite appropriation "Claims, Judgments, and Relief Acts" (the Judgment Fund), these legal actions should not materially affect the NWCF operations or financial condition. Additionally, for the Transportation

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activity group legal action to which the Department is a litigant also include, but are not limited to, the Contract Disputes Act, (CDA), Chapter 9 of Title 441 U.S.C.; Suits in Admiralty Act, Chapter 20, of Title 46 U.S.C.; and the Public Vessels Act, Chapter 22, of Title 46 U.S.C.. Payments from the Judgment Fund as a result of CDA claims are required to be reimbursed out of agency appropriations, current at the time of entry of the judgment, Title 28 U.S.C. Section 2414.

5. In FY 1998, the NWCF activity groups sold inventories or services to foreign governments 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, generally at no profit or loss to the U.S. Government. Customers are required to make payments in advance to a trust fund maintained by the Department of the Treasury from which the Military Services are reimbursed for the cost of administering and executing the sales. In FY 1998 the NWCF Supply Management activity group sold $147,134 thousand under the Foreign Military Sales (FMS) program. In FY 1998 the NWCF industrial activity groups received reimbursements of $249,774 thousand for assets sold under the FMS program. The following provides the amount of assets and services sold under the FMS program. See next page.

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(in thousands)

Activity Group	Supply Activity	Industrial Activity
Depot Maintenance – Shipyards		$ 5,877
Depot Maintenance – Aviation		32,746
Depot Maintenance - Other (Marine Corps)		841
Ordnance		15,929
Transportation		244
Base Support		
PWCs		(9)
NFESC		
Information Services		
NAVCOMTELCOM*		
FMSO		3,965
COMNAVRESFOR*		
Research and Development		
NSWC		83,695
NAWC		75,525
NUWC		30,536
NRL		425
SSCs**		
Supply Management (Navy)	$144,402	
Supply Management (Marine Corps)	2,732	
Total	$147,134	$249,774

*Sales of services to foreign governments is not applicable.

**The total amount of reimbursement for assets and services sold under the FMS program is not available due to system deficiencies in the current financial system, Defense Industrial Financial Management System (DIFMS). DIFMS currently does not provide a breakout of the required appropriation for FMS.

G. Funds with the U. S. Treasury and Cash

In a memorandum dated 5 January 1995, the USD(C) returned management of DBOF cash and its associated anti-deficiency limitations to the DON and other military components effective 1 February 1995. This action effectively merged the component's responsibility for monitoring collection and disbursement transactions, as well as taking actions to correct operational problems, with the responsibility for control over the cash balance.

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Fund Balances with Treasury are managed at the DON level of the NWCF. Fund Balances with Treasury reflect the ending FY 1997 balance plus FY 1998 collections, disbursements, and non-expenditure transfers recorded in the NWCF Treasury sub-limit 97X4930.002. The practice of closing activity collections and disbursements to the DON departmental level was discontinued 1 October 1997 (for FY 1997) and, thus, Fund Balances with Treasury were reestablished at the activity level. During FY 1998 DFAS initiated procedures to record non-expenditure transfers at the activity level vice at the departmental level. See Note 2. Plans are being formulated to move activity level collections and disbursements closed to the departmental level in FY 1995 and FY 1996 back to the activity level. Once this is accomplished, all activity level collection, disbursement, and non-expenditure transactions, effective from the date USD(C) returned management of cash to the DON, will be recorded in the activity general ledgers. Completion of this plan in FY 1999 will be contingent upon the development of procedures by DFAS.

H. Foreign Currency

Not Applicable

I. Accounts Receivable

As presented in the Consolidated NWCF Balance Sheet, Accounts Receivable includes accounts, claims, refunds and interest receivable from other entities. See Note 5.

(in thousands)

	Amount	Allowance	Total Net
Accounts Receivable			
Government	$626,261	N/A	$626,261
Public	270,911	205	270,706
Refunds			
Claims			
Total	$897,172	$205	$896,967

The financial reporting system for the Supply Management (Navy) activity group maintains summary level reporting for Accounts Receivable for non-DBMS and Material Financial Control System (MFCS) reporting activities. For these activities, a comparison is made between total Revenue from Sales of Goods and Services and total Funds Collected reported for each month, with the mathematical difference being the change in the undistributed collections balance reported for the month. Undistributed collections is netted with Accounts Receivable on the Balance Sheet. The detail Accounts Receivable records for those Supply Management (Navy) activities are maintained at the activity level. In the case of DBMS and MFCS reporting activities the Accounts Receivable balances are reported directly to DFAS-CL.

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J. Loans Receivable

There are no loans receivable recorded.

K. Inventories

Inventory for supply type activities which includes Navy-managed consumable items and repairable items, and Other Service, DLA, and General Services Administration managed items, are carried in the accounting records at Standard Price. Standard Price is composed of the cost of the material plus appropriate surcharges. In FY 1998 the Supply Management (Navy) recorded a net gain of $8,080,859 thousand as a result of Standard Price changes. Inventories for reporting purposes are revalued from Standard Price to utility value using the Latest Acquisition Cost (LAC) method prescribed by the USD(C). This revaluation results in a recognition of unrealized holding gains and losses in the Supply Management (Navy) ending inventory value. Upon adjustment for unrealized holding gains and losses, the LAC method then results in an approximation of historical cost. The FY 1996, FY 1997 and FY 1998 inventory values for Supply Management (Navy) reflect the execution by DFAS of interpreted guidance given by USD(C) which clarified and provided additional instructions to those contained in DoD FMR 7000.14-R, Volume 11B. See Note 8.A. In FY 1997 the Marine Corps was not able to certify the Supply Management (Marine Corps) activity group inventories due to business process changes and system problems. In FY 1998, the Marine Corps has resolved it systemic inventory problems by changing its business practice and policy on stock funding repairable as of 1 October 1997. See Note 23 Supply Management (Marine Corps) .

For industrial type activities, Operating Materials and Supplies are held for use on customer work. These inventories are maintained at cost, primarily using a weighted average. See Note 8.B.

L. Investments in U.S. Government Securities

There are no investments in U.S. Government Securities in the NWCF activity groups.

M. General Property, Plant and Equipment

In FY 1998 there have been significant policy changes impacting what categories of assets (e.g., National Defense Property, Plant and Equipment (PP&E), Heritage Assets and Stewardship Land) are no longer to be reported by some reporting entities on the Balance Sheet. However, "For entities operating as business-type activities, all PP&E shall be categorized as general PP&E whether or not it meets the definition of other PP&E categories (e.g., heritage Assets)." This guidance is based on paragraph 24 of the Statement of Federal Financial Accounting Standards (SFFAS) No. 6. Therefore, all NWCF PP&E continue to be categorized as General PP&E and reported on the Balance Sheet whether or not it meets the definition of other PP&E categories as

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required by SFFAS No. 6. The new FY 1998 CFO Required Supplementary Stewardship Information reporting requirements, do not apply to the Working Capital Funds activities.

The USD(C) memorandum of 26 March 1998, as modified by USD(C) memorandum of 22 October 1998 policy for computing depreciation of General PP&E, is effective for all DWCF General PP&E assets acquired on or after 1 October 2000.

The General Accounting Office (GAO) has determined that real property used by the NWCF, but under the jurisdiction of the Military Departments, represents an asset of the NWCF and such property should be reported on the financial statements as an entity asset to show the full costs of all resources and assets used in NWCF operations. DFAS is currently developing accounting and reporting procedures to allow NWCF to report finance sources and expenses associated with assets not acquired with NWCF resources (e.g., real property) as Other Revenues and Financing Sources and Depreciation and Amortization Expense.

Land, plant property, and equipment are valued at cost. Cost is based upon a specific amount paid or estimated value if a receipt document is not available. The capitalized amount includes the cost of the asset plus any additional costs such as transportation, installation and any internal costs incurred to make the asset ready for use. Based upon the current expense/ investment criteria, any piece of plant property or equipment with a unit cost of $100,000 or more and a useful life of two years or more is capitalized and depreciated. The expense/ investment criteria which is the capitalization threshold has varied by fiscal year of acquisition. The expense/investment for capital equipment and capital improvements to property was $15,000 in FY 1992 and FY 1993; $25,000 in FY 1994; $50,000 in FY 1995; and $100,000 in FY 1996, FY 1997 and FY 1998. When the expense/investment funding threshold changes, a capital asset capitalized within NWCF at a previous threshold continues to be capitalized and depreciated at the threshold at which it was originally capitalized, in accordance with DoD FMR 7000.14-R, Volume 11B.

Property and equipment in inventory prior to 1 October 1991 are depreciated using the straight line method of depreciation under the existing expected service life for each item. New property and equipment items introduced into the NWCF since 1 October 1991 are being depreciated using the straight line method under the service life schedule starting with the first full month of operation.

All maintenance and repair costs are recorded as an expense when they are incurred. Additional information regarding the value of fully depreciated and sponsor funded equipment is provided in Note 9.

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N. Prepaid and Deferred Charges

Payments in advance of the receipt of goods and services are recorded as prepaid charges and reported on Lines 1.A.(4) and 1.J of the Balance Sheet at the time of prepayment and recognized as expenditures and expenses when the related goods and services are received.

O. Leases

The following provides specific disclosure by applicable activity groups.

Depot Maintenance - Other (Marine Corps). The Depot Maintenance - Other (Marine Corps) activity group does not have any capital leases meeting the DoD FMR requirements for capitalization.

Transportation. The Military Sealift Command (MSC) Transportation activity group does not have any capitalized leases. MSC does not report the value of leased ships (Maritime Prepositioning Ships (MPS) and T5 ships) as capital leases under Line 1.H, Entity Assets, General Property, Plant and Equipment on the Balance Sheet as recommended in Naval Audit Service (NAVAUDSVC) Audit Reports 075-S-92 and 035-96. This NAVAUDSVC recommendation is still being reviewed by higher authority for a determination as to the applicability to MSC. The debt for the outstanding principal balance on these MPS ships is, however, reported on Line 1.J, Entity Assets, Other Assets and Line 4.A.(3), Liabilities Covered by Budgetary Resources (Intragovernmental Liabilities), Debt on the Balance Sheet.

Base Support.

PWCs. As of 30 September 1998, the PWCs were committed to numerous operating leases and rental agreements. Generally, these leases and agreements were for rental of equipment, space, and operating facilities. Capital leases prior to formation of NWCF were “grandfathered”, and continue to be treated as operating leases.

NFESC. During FY 1998, NFESC was committed to a small number of operating leases for office equipment such as copying machines and mobile trailers used for office space. The dollar values of these leases are immaterial and are recognized as expenses are incurred and not listed as deferred charges.

Information Services.

NAVCOMTELCOM. Generally, all leases and agreements were for rental of operating equipment. Since these leases are operating in nature, rather than capital, no capital leases are recognized on the Balance Sheet.

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FMSO. Generally, all leases and agreements were for rental of operating equipment. Since these leases are operating in nature, rather than capital, no capital leases are recognized on the Balance Sheet.

COMNAVRESFOR. Generally, all leases and agreements were for rental of operating equipment. Since these leases are operating in nature, rather than capital, no capital leases are recognized on the Balance Sheet.

Research and Development.

NRL. As of 30 September 1998, the NRL is not committed to any significant multiple-year operating leases and rental agreements for rental of equipment, space, and operating facilities. The NRL does rent equipment on annual rental contracts. Total equipment rentals including the cost of maintenance and service agreements for FY 1998 were $188 thousand.

SSCs. As of 30 September 1998, the SSC's are committed to operating leases and rental agreements. Generally, these leases and agreements are for rental of equipment, space, and operating facilities. All these leases and agreements are either renewable on an annual basis or can be canceled on short notice. Therefore, there is no significant future liability.

P. Contingencies

At any given time, DON may be a party to various legal and administrative actions and claims brought against it. These relate primarily to tort claims resulting from aircraft, ship, and vehicle accidents, medical malpractice, property and environmental damages resulting from Departmental activities, and contract disputes. As discussed under Note 1.F.4, most legal claims,
other than contract claims, to which the NWCF may be a named party are covered by the provisions of the Federal Tort Claims Act and the provisions of Title 10, U.S.C., Chapter 163 governing military claims. Either because payments under these statutes are limited to amounts well below the threshold of materiality for claims payable from the Department's appropriations or because payments will be from the permanent, indefinite appropriation "Claims, Judgments and Relief Acts" (the Judgment Fund), these legal actions should not materially affect the NWCF's operations or financial condition. Note 15 provides disclosure of non booked contingencies and related amounts. The following provides specific disclosure of known contingencies by applicable activity group.

Research and Development.

NRL. The NRL payments during FY 1998 for awards, compromises and settlements resulting from the legal actions were insignificant. As of 30 September 1998, NRL has no new adjudicated claims that are outstanding. As the ultimate resolution of legal actions still pending are not expected to materially affect the NRL's operation or financial condition, no contingent liabilities have been recognized on the Balance Sheet.

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Supply Management (Navy). The ultimate resolution of legal actions will not materially affect the agency's operations or financial condition. Therefore, no contingent liabilities related to legal actions have been recognized in the Balance Sheet.

Q. Accrued Leave

Supply Type NWCF Activities.

Navy: Civilian annual leave is earned and the accrued amounts are reduced as leave is taken. The balances for annual leave at the end of the fiscal year reflect current pay rates for the leave that is earned but not taken. Sick and other types of non-vested leave are expensed as taken. Each year, the balance in the accrued annual leave account is adjusted to reflect current pay rates.

Marine Corps: Civilian annual leave is accrued as earned and the accrued amount is reduced as leave is taken. The balances for civilian annual leave and military leave at the end of the fiscal year reflect current pay rates for the leave that is earned but not taken. Each year, the balance in the accrued annual leave account is adjusted to reflect current pay rates. To the extent current fiscal year fund balances are not available to fund annual leave earned but not taken, funding will be obtained from future financing sources. Sick and other types of non-vested leave are expensed as taken. Accruals of leave for civilian employees are reported against the Operation and Maintenance, Marine Corps appropriation.

Industrial Type NWCF Activities. Civilian accrued leave for industrial activities is accrued as it is earned and the accrual is reduced as leave is taken. At least once per year, the balance in the accrued annual leave account is adjusted to reflect current pay rates of cumulative annual leave earned but not taken. Sick and other types of non-vested leave are expensed as taken.

R. Equity

The new Balance Sheet presented for FY 1998 displays only Unexpended Appropriations and Cumulative Results of Operations (CRO) as components of the Net Position. The CRO for FY 1998 contains all transactions heretofore represented by Invested Capital, CRO, Other, and Future Funding Requirements on the FY 1997 Statement of Financial Position.

The CRO thus includes donated capital, transfers of assets in and out without reimbursement, the net results of operations (revenue minus expenses), prior period adjustments, and investments in capital assets and inventory assets. Investments in capital assets are recorded at actual cost of acquisition or construction while inventory assets are recorded using the LAC method of valuation.

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The merging of equity accounts into the CRO on the Balance Sheet and the elimination of the related footnote describing all the elements of the Net Position results from the direction of the OMB Guidance on Form and Content of Agency Financial Statements as promulgated by the DoD Guidance on Form and Content of Audited Financial Statements for reporting entities.

S. Treaties for Use of Foreign Bases

The following provides note disclosure as applicable by activity group.

Transportation. MSC has the use of land, buildings, and other facilities which are located overseas and have been obtained through various international treaties and agreements negotiated by the Department of State. Generally, treaty terms allow MSC continued use of these properties until the treaties expire. However, a determination was made that MSC does not control access.

Base Support.

PWCs. The Government of Japan is responsible for facility replacement.

Research and Development.

SSCs. While some of the SSC San Diego operations take place on foreign soil, the operations are performed as tenants to other Naval activities. The SSC San Diego, CA only significant presence is in Japan where SSC San Diego’s Systems Activity Pacific has a detachment located as a tenant to the Naval Ship Repair Facility, Yokosuka. The detachment in Yokosuka employs 17 Foreign National Indirect Hire personnel under a Master Labor Contract with Japan. However, Japan now pays the majority of the cost of these employees. The U.S. Government is liable for any shortfall that is borne by the activity for Special Measures Agreement expenses incurred which is approximately $45 thousand. These costs can be for management directed severance obligations, overtime costs or additional schedule pay costs.

T. Comparative Data

Comparative data for the prior year has not been presented because this is the first year for which financial statements are prepared using the OMB 97-01 prescribed formats. In future years, comparative data will be presented in order to provide an understanding of changes in the financial position and operations of the Consolidated NWCF.

See Note 1.B for disclosure of PBD 426 realignments in FY 1998 with regards to NFESC and the former Depot Maintenance - Ordnance. Also see the Overview and Note 23 under Base Support - PWCs and NFESC.

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U. Undelivered Orders

NWCF activities are obligated for goods which have been ordered but not yet received (undelivered orders). As of 30 September 1998 undelivered orders amounted to $3,442,045 thousand for supply type activities and $2,815,701 thousand for industrial type activities for a total of $6,257,746 thousand.

Undelivered Orders
(in thousands)

Activity Group	Supply Activities	Industrial Activities
Depot Maintenance – Shipyards		$534,092
Depot Maintenance – Aviation		211,378
Depot Maintenance – Other (Marine Corps)		32,108
Ordnance		52,964
Transportation		30,882
Base Support		
PWC's		414,117
NFESC		19,136
Information Services		
NAVCOMTELCOM		9,473
FMSO		12,953
COMNAVRESFOR		3,606
Research and Development		
NSWC		530,292
NAWC		456,003
NUWC		133,092
NRL		120,506
SSCs		255,099
Supply Management (Navy)	$3,518,490	
Supply Management (Marine Corps)*	(76,445)	
Total	$3,442,045	$2,815,701

*The Marine Corps was not able to certify the Supply Management (Marine Corps) activity group undelivered orders due to accounting system problems. See Note 23 Supply Management (Marine Corps). The primary reason for this abnormal balance for undelivered orders is due to the problem with the accounts payable function. In the past the accounts payable function had Accounts Payable matched against overstated undistributed disbursements. To correct the problem, outstanding obligations were validated against receipts. The Marine Corps and DFAS have agreed on procedures to guard against future reoccurrence and they continue on a monthly basis reviewing Accounts Payable.

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Note 2. Fund Balances with Treasury ($ in Thousands):

	Trust Funds	Revolving Funds	Appropriated Funds	Other Fund Types	Total
A. Entity Fund and Account Balances:					
Unobligated Balance Available:					
Available	$0	$2,632,641	$0	$0	$2,632,641
Restricted					
Reserve For Anticipated Resources					
Obligated Balance, Net		2,502,139			2,502,139
Unfunded Contract Authority		(3,942,278)			(3,942,278)
Unused Borrowing Authority					
Total Entity Treasury Balance	$0	$1,192,502	$0	$0	$1,192,502
B. Non-Entity Fund and Account Balance	$0	$0	$0	$0	$0

C. Other Information:

The Fund Balances with Treasury of $1,192,502 thousand reflects the FY 1997 ending balance of $746,524 thousand plus FY 1998 collections, disbursements, and non-expenditure transfers recorded in the NWCF Treasury sub-limit 97X4930.002. The Departmental reporting of the Fund Balances with Treasury is in agreement with Treasury's Fund Balance reported in TFS 6653. The following table details the amounts recorded in FY 1998:

Collections	$21,075,568
Disbursements	20,694,083
Non-expenditure Transfers, Net	64,493

The non-expenditure transfers are comprised of transfers-in of $251,809 thousand and transfers-out of $187,316 thousand. The transfers were made from or to the following NWCF activity groups:

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Activity Group	Non-Expenditure Transfers To JLSC	(in thousands) Other Non-expenditure Transfers	Total Non-expenditure Transfers
Depot Maintenance – Shipyards	($36,800)	$2,641	($34,159)
Depot Maintenance – Aviation	(31,700)	2,272	(29,428)
Depot Maintenance – Other (Marine Corps)	(1,500)		(1,500)
Ordnance		195	195
Transportation		(69,316)	(69,316)
Base Support – PWCs		23,017	23,017
Research and Development – NAWC		18,412	18,412
Research and Development – SSCs		150	150
Supply Management (Navy)	(48,000)	*201,287	153,287
Supply Management (Marine Corps)		3,300	3,300
Navy Component		535	535
Total	($118,000)	$182,493	$64,493

* Includes transfers-in of $198,100 thousand for the Consumable Item Transfer program and $3,187 thousand from the Joint Logistics Systems Center (JLSC).

Transfers of $118,000 thousand were made to JLSC to finance costs associated with the development of automated systems for the NWCF. The NWCF received transfers from the JLSC of $8,100 thousand based on under execution of the capital budget at the JLSC. These transfers were applied to Depot Maintenance - Shipyards ($2,641 thousand), Depot Maintenance - Aviation ($2,272 thousand), and Supply Management (Navy) ($3,187). The NWCF received transfers totaling $42,309 thousand ($195 thousand for Ordnance, $23,017 thousand for Base Support - PWCs, $18,562 thousand for Research and Development - NAWC and SSCs, and $535 thousand held in Navy Component pending distribution to Research and Development - NAWC) for disaster relief to repair storm damage associated with the affects of El Nino in California and typhoon PAKA in Guam. In the Transportation activity group a transfer-out of $69,316 thousand was made to the Federal Financing Bank (FFB) for the principal payment of loans related to APF-N ships. See Note 10. Lastly, the Supply Management activity group received transfers totaling $201,400 thousand from DLA ($198,100 thousand to the Navy segment and $3,300 thousand to the Marine Corps segment) to compensate the NWCF for lost income from the non-reimbursable transfer of inventory to DLA under the Consumable Item Transfer program.

Fund Balances with Treasury have been reestablished at the activity group and activity level. This effort started 1 October 1997 (for FY 1997) when the process of transferring activity level collections and disbursements to the DON departmental level at the end of each fiscal year was discontinued. During FY 1998 DFAS initiated procedures to record non-expenditure transfers at the activity level. These transfers, which were being held at the departmental level, represent transactions from FY 1995, the fiscal year Fund Balances with Treasury responsibility was returned to the DON, through FY 1998. The recording of these transfers for the disaster relief

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transfers has caused reconciliation problems between the activity level accounts and Treasury values. These will be addressed during FY 1999. Additionally, Fund Balances with Treasury contains transactions processed through Treasury but not to the activity level. Without identification of these transactions to an activity, the required reconciliation of cash cannot be completed.

Note 3. Cash and Other Monetary Assets ($ in Thousands): Not Applicable

Note 4. Investments, Net ($ in Thousands): Not Applicable

Note 5. Accounts Receivable, Net ($ in Thousands):

	(1) Gross Amount Due	(2) Allowance for Estimated Uncollectables	(3) Net Amount Due
A. Entity Receivables:			
Intragovernmental	$626,261	N/A	$626,261
With the Public	270,911	205	270,706
B. Non-Entity Receivables:			
Intragovernmental	$0	N/A	$0
With the Public			

C. Allowance Method Used: An allowance for uncollectable Accounts Receivable (Intragovernmental) has not been established. In accordance with DFAS-CL/AACA memorandum of 1 May 1998, there is no legal authority to write off intragovernmental receivables. The $205 thousand in Note 5.A Entity Receivables (With the Public) represents an accounting adjustment in the Information Services - FMSO secondary activity group for travel advances that were resident in the accounting system prior to the conversion to NWCF. This amount was erroneously reported as an allowance for estimated uncollectables at FY 1998 year-end. The $205 thousand will be expensed in FY 1999 to correct this error.

D. Other Information:

1. Included in the FY 1998 Entity Receivables (Intragovernmental) line is the value of industrial activities Navy Account 1543 Undistributed Collections – Unmatched. This is an account with a normal credit balance which impacts Accounts Receivable, Net. Depending on the amount in the account it can cause a negative (abnormal) balance in Accounts Receivable, Net. Navy Account 1543 Undistributed Collections – Unmatched represents the value of refunds/collections received which are initially posted as increases to activity level cash, but must be researched in order to determine the appropriate receivable to liquidate. In FY 1997 Navy Account 1543 Undistributed Collections – Unmatched was reported as a reduction to Entity Receivables (Governmental) Accounts Receivable, Net, however, in FY 1998 DFAS-CL

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concluded that it should be realigned and reported as a reduction to the Entity Receivable (Intragovernmental) line based on the composition and type of transactions included in Navy Account 1543. The Depot Maintenance - Shipyards, Transportation, Base Support - NFESC and Research and Development - NUWC activity groups ending FY 1998 balance in Navy Account 1543 caused an abnormal balance to be reported at the individual activity group level on Line 1.A.3. Entity Assets (Intragovernmental), Accounts Receivable, Net of the Balance Sheet and in related Note 5. Included on the FY 1998 Entity Receivables (With the Public) line is an abnormal balance of negative $205 thousand (Allowance for Estimated Uncollectables) for the Information Services – FMSO activity group as discussed in Note 5.C above. DFAS-CL has indicated that the FY 1998 Entity Receivables (With the Public) line includes an abnormal balance of negative $403 thousand for the Depot Maintenance – Aviation activity group which was caused by a DIFMS error which misclassified the Accounts Receivable. This will be corrected in FY 1999.

2. The following provides other disclosures by specific activity group.

a. **Research and Development.** The SSCs Accounts Receivable account is understated by $150 thousand due to the posting by DFAS-CL of an U.S. Treasury cash transfer to the NWCF for disaster relief associated with the affects of El Nino. When DFAS-CL adjusted the cash account for this transfer, it was offset in the undistributed collections, thus reducing the Accounts Receivable account. See Note 2, for additional information. The recording of these transfers for the disaster relief transfers has caused reconciliation problems between the activity level accounts and Treasury values.

b. **Supply Management (Navy).** Accounts Receivable, Net is overstated by $53,085 thousand due to residual records posted in the Central Data Base (CDB) during the last six years. DFAS-CL identified this condition and COMNAVSUPSYSCOM research is continuing to verify the proposed adjustments to receivables and corresponding sales. Corrective action is scheduled for completion during the first quarter of FY 1999.

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Note 6. Other Assets ($ in Thousands):

A. Other Entity Assets	
1. Intragovernmental	
(a) Assets Returned for Credit	$107,479
(b) Advances	100
(c) Deferred Charges	169,011
Total Intragovernmental	$276,590
2. Other	
(a) Advances	$169,713
(b) Travel Advances	21,214
(c) FFB Loan Principal APF-N Ships	1,094,710
(d) Fixed Assets Not in Use, Net	40,852
Total Other	$1,326,489

B. Other Information Related to Entity Assets.

1. The Other Entity Assets (Governmental), FFB Loan Principal for APF-N Ships includes the Transportation activity group outstanding principal balance of $1,094,710 thousand related to loans from the FFB for the APF-N ships. Prior to FY 1997, the principal balance was included in Line 1.b.(2), Entity Assets, Transactions with Non-Federal (Governmental) Entities, Accounts Receivable, Net of the Statement of Financial Position. So as not to distort the true value of Accounts Receivable, DFAS and the DON agreed in FY 1997 to reflect this outstanding principal balance in Line 1.b.(6), Entity Assets, Transactions with Non-Federal (Governmental) Entities, Other Non-Federal (Governmental) of the Statement of Financial Position. In FY 1998 Line 1.J, Entity Assets, Other Assets is the equivalent line on the new Balance Sheet. See Note 10.

2. Within the Research and Development, SSCs reported $11,041 thousand under Other Entity Assets (Intragovernmental) Deferred Charges which represents the Accounts Payable that has been established for the International Merchant Purchase Authorization Card (IMPAC). The current financial accounting system (DIFMS) has deficiencies when posting the bankcard expenditures. A work around was developed to ensure that IMPAC invoices are processed in a timely manner. Until the DFAS the DIFMS Central Design Agency can correct this error, this account has been established to capture the expenditures associated with the IMPAC card.

3. The following shows those NWCF activity groups with Fixed Assets Not in Use included in Other Entity Assets (Other) in Note A.2.(d) above. See next page.

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(in thousands)

Activity Group	No Fixed Assets Not in Use Included on Line 1.J “Other Assets” of Balance Sheet	Net Book Value of Fixed Assets Not in Use Included on Line 1.J “Other Assets” of Balance Sheet
Depot Maintenance – Shipyards		* $12,902
Depot Maintenance – Aviation		5,935
Depot Maintenance – Other (Marine Corps)	X	
Ordnance	X	
Transportation	X	
Base Support		
PWC’s		337
NFESC	X	
Information Services		
NAVCOMTELCOM		* 2
FMSO	X	
COMNAVRESFOR	X	
Research and Development		
NSWC		* 20,239
NAWC	X	
NUWC		* 1,421
NRL		1
SSCs		** 16
Supply Management (Navy)	X	
Supply Management (Marine Corps)	X	
Total		***$40,853

* The reported amount is the gross book value. The accumulated depreciation of “Fixed Assets Not in Use” continues to be reported under Note 9 because current systems have not been revised to implement the DFAS-CL guidance of 16 October 1997 for reporting Accumulated Depreciation - Assets Not in Use under Contra Account 1671.

** The reported amount is the gross book value. The value associated with the accumulated depreciation is included in the Note 9 other capital asset depreciation accounts, because DIFMS does not break out the depreciation associated with Fixed Assets Not in Use separately.

***The difference between this chart and related Note 6 is due to rounding.

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C. Other Non-entity Assets

1. Intragovernmental	
(a)	$0
(b)	
Total Intragovernmental	$0
2. Other	
(a)	$0
(b)	
Total Other	$0

D. Other Information Related to Non-entity Assets. In accordance with NAVAUDSVC audit report 049-98 Recommendation 41, the gross value of the FY 1998 Individual Material Readiness List (IMRL) equipment assets has not been included in the NWCF Consolidated Balance Sheet or related Note 6 Other Non-entity Assets. See Note 23 Navy Component for full disclosure of the change in NWCF departmental business practice regarding IMRL equipment assets.

Note 7. Direct Loans and Loan Guarantees, Non-Federal Borrowers ($ in Thousands):
Not Applicable

Note 8. Inventory and Related Property, Net ($ in Thousands):

Note 8.A. Inventory ($ in Thousands):

	(1) Inventory Amount	(2) Allowance for (Gains) Losses	(3) Inventory, Net	(4) Valuation Method
1. Inventory Categories:				
(a) Held for Current Sale	$19,344,589	$11,584,515	$7,760,074	LAC
(b) Held in Reserve for Future Sale				
(c) War Reserve Material	223,717	24,719	198,998	LAC
(d) Excess, Obsolete and Unserviceable	150,802		150,802	NRV
(e) Held for Repair	8,735,269	2,186,354	6,548,915	LAC
Total	$28,454,377	$13,795,588	$14,658,789	

2. Restrictions on Inventory Use, Sale, or Disposition: Generally, there are no restrictions with regard to the use, sale, or disposition to applicable DoD activities and personnel. Inventory may be sold to foreign, state and local governments, private parties and contractors in accordance with DoD, DFAS and DON policies and guidance or at the direction of the President.

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3. Other Information: Inventory applies to the supply activity group and not to the industrial activity groups. The presentation of the NWCF Supply Management War Reserve value in Note 8.A Inventory on Line 1.(c) War Reserve Material is in accordance with the DFAS informal guidance of 9 December 1998 to DFAS-CL. The following provides disclosure by activity group.

Supply Management (Navy). Inventories are carried in the accounting records at Standard Price. Standard Price is used in the day to day operations of the fund and is comprised of the cost of the material and surcharges to recover operating and inventory costs in managing the Supply Management (Navy) activity group. For reporting purposes, inventories are valued using the LAC method. Additionally, an allowance for unrealized holding gains and losses has been established to value inventory to an approximation of historical cost. The valuation is in accordance with DoD FMR 7000.14-R, Volume 11B as modified by additional guidance from USD(C) and DFAS.

Application of the LAC method requires a series of journal adjustments which: (1) remove the surcharge included in the Standard Price; (2) remove the cost to repair from the value of unserviceable inventory; (3) reduce to salvage value inventory which is not expected to survive the repair process; and (4) reduce to salvage value inventory which is categorized as Potential Reutilization/Disposal Stocks. These adjustments are applied to the total of the inventory and are considered (along with other computed factors) in the inventory valuation model developed by USD(C) and DFAS. The surcharge and estimated cost to repair are variable depending upon the material category being valued. The FY 1998 salvage rate based at the time of CFO reporting was 3.4 percent. This method reduced Standard Price inventory value by $18,017,445 thousand as follows:

	(in thousands)
Remove surcharge	$10,976,158
Remove cost to repair	2,181,594
Reduce to salvage value	4,859,693
Total reduction	$18,017,445

The necessary adjustment to inventory based on NAVAUDSVC draft audit report 98-0099, Recommendation 18, was made in FY 1998 for a net loss of $12,242 thousand. This action is complete.

The Supply Management (Navy) value of War Reserve Material is $94,824 thousand. The Supply Management (Navy) activity group does not have sponsor funded inventory.

Supply Management (Marine Corps). Inventory is valued at LAC as required by DoD accounting policies. Generally, these values are based on prices paid for recently acquired items.

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Gains and losses that result from valuation changes for stock fund items are recognized in the allowance account. Only the realized gains and losses are reflected in the Total Program Cost.

The Supply Management (Marine Corps) value of net War Reserve Material is $104,174 thousand. The Supply Management (Marine Corps) activity group does not have sponsor funded inventory.

Legend: Valuation Methods
LAC = Latest Acquisition Cost NRV = Net Realizable Value
SP = Standard Price O = Other
AC = Actual Cost

Note 8.B. Operating Material and Supplies (OM&S) ($ in Thousands):

	(1) OM&S Amount	(2) Allowance For (Gains) Losses	(3) OM&S, Net	(4) Valuation Method
1. OM&S Categories:				
(a) Held for Use	$538,147	$15,006	$523,141	Weighted Average and Other
(b) Held in Reserve for Future Use	19,589		19,589	
(c) Excess, Obsolete, and Unserviceable				
Total	$557,736	$15,006	$542,730	

2. Restrictions on operating materials and supplies: None

3. Other Information:

a. The amounts in Note 8.B Operating Materials and Supplies, and Note 8.A Inventory categories have been combined in FY 1998 under Entity Assets, Inventory and Related Property, Net on the Balance Sheet. Formerly these two inventory categories were reported separately. Because of this change in reporting requirement the NAVAUDSVC has stated, during the FY 1998 Denver CFO conference, that the Operating Materials and Supplies value must now be revalued to its historical cost, using the DoD model as required for Supply Management Inventory. USD(C) took this issue for resolution. Subsequent to the FY 1998 Denver CFO conference, DON has also requested USD(C) to provide clarifying guidance.

b. NAVAUDSVC audit report 035-96 recommended that the use of an Allowance for Losses be discontinued. The use of the allowance account allows the industrial activities to recognize normal losses for material purchases during the year of purchase. ASN(FM&C)

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memorandum of 10 June 1996 requested DFAS to prepare and coordinate the financial and accounting procedural changes for operating activities and accounting systems to discontinue the use of the Allowance for Losses. NAVAUDSVC audit report 049-98 repeated this recommendation. ASN(FM&C) memorandum 7540 FMO-24 of 2 December 1998 has again requested the assistance of DFAS to resolve this recommendation. The discontinuance of the use of the Allowance for Losses is pending DFAS issuance of guidance and implementation.

c. Operating Materials and Supplies are held at industrial activity groups for use on customer work. These inventories are maintained at cost, primarily using a weighted average. The following provides additional disclosures by activity group.

Depot Maintenance - Shipyards. Inventories of operating supplies and non-consumable items are valued at weighted average. Direct Material Inventory is valued at acquisition cost by line item. Generally, these values are based on prices paid for recently acquired items plus appropriate surcharges.

Depot Maintenance - Aviation. An allowance for inventory losses account has been established to accrue potential inventory shortfalls over the fiscal year. This activity group also manufactures inventory that is later used on customer projects. The cost to produce the manufactured inventory in FY 1998 was $9,157 thousand. The Statistical Physical Inventory Tool for Improving Inventory Reliability (SPITFIIRE) is used to sample their inventories. The SPITFIIRE program is run with a stratification mandated by the Commander, Naval Air Systems Command (COMNAVAIRSYSCOM) to ensure statistical accuracy to exclude invalid records and replace invalid records with additional samples. Additionally, SPITFIIRE is able to project the dollar amount for the error rate by the different stratifications.

Depot Maintenance - Other (Marine Corps). Inventories, including operating supplies and non-consumable items, are valued at standard prices. Generally, these prices are based on prices paid for recently acquired items plus appropriate surcharges. The standard price is updated to reflect the LAC by national stock number every month.

Ordnance. Inventories of operating supplies and non-consumable items, are valued at weighted average. Direct Material Inventory is valued at acquisition cost by line item. Generally, these values are based on prices paid for recently acquired items plus appropriate surcharges.

Transportation. There were no changes from prior year's accounting methods. All Operating Materials and Supplies are categorized as "Held for Use" because they are needed to provide services for MSC customers. All OX Cognizance Symbol material was transferred to the Navy Inventory Control Point – Mechanicsburg and DLA during FY 1994, FY 1995, and FY 1996. The current value is zero. The following is a description of MSC's active inventory categories:

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- Consumable inventories are frozen inventories for United States Navy Ship (USNS) ships based on the values for a period of three months of actual expenses. Values were examined during FY 1997 and found to be adequate. Also, a 100 percent actual physical inventory is conducted upon transfer or inactivation of the vessel.

- Ship subsistence inventories for USNS ships reflect the chief steward's on-hand inventory and is processed at the end of each month using current average unit prices. A 100 percent actual on board inventory is taken quarterly, in accordance with MSC instructions.

- For the ships for which fuel inventory are maintained, inventory is based on the bunkers available at month end, as reported by the ship operators.

- Miscellaneous materials are inventory items stored at Cheatham Annex and Oakland, CA. A 100 percent physical inventory was taken in May 1998 for Commander, Military Sealift Command West (COMSCWEST) and COMSCEAST. These inventory items are priced either at their requisition cost or capitalized cost. The latter methodology was used in cases where the original inventory taken had no unit prices. In such cases, cost was established by an outside party who was contracted to perform a physical inventory of these items. Approximately $6,000 thousand was transferred out as a result of reevaluation and the move of COMSCEAST from Bayonne, NJ to Norfolk, VA and COMSCWEST from Oakland, CA to San Diego, CA.

- MPS/T5 spares are inventory stored at the contractors' site.

Base Support.

PWCs. Operating Materials and Supplies are held for use on customer work. These materials are maintained at cost, using a weighted average. The PWCs' stocking objective is 120 days not 30 days due to the need for specialized items for seasonal services (i.e., snow removal).

NFESC. The total Operating Materials and Supplies amount of $68 thousand for this activity groups is reflected in Navy Account 1541 Unmatched - Unallocated Costs. NFESC does not maintain any Operating Materials and Supplies. All operating materials needed to perform the mission of NFESC are purchased on an as needed basis preventing inventory build-up and related costs to carry and value inventory.

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Information Services.

NAVCOMTELCOM. In accordance with DoD FMR, Volume 11B, Chapter 56, policy the $991 thousand included as Operating Materials and Supplies Held for Use are for materials and supplies that do not exceed the amount expected to be used within 30 days. Also, the $75 thousand included as Operating Materials and Supplies Held in Reserve for Future Use are for materials and supplies maintained because they are not readily available in the market or because it is likely they will be needed subsequently. Materials and supplies physical inventories were taken during the last quarter of FY 1998 using the actual cost method. No inventory adjustments resulted from those physical inventories.

COMNAVRESFOR. LAC is currently used to price inventories. Actual physical counts for Materials and Supplies inventories were taken during the last quarter of FY 1998. Resulting inventory adjustments are contained in the amounts shown in the Balance Sheet. Approximately $50 thousand of this activity groups Operating Materials and Supplies of $151 thousand is unallocated costs residing under the previous Unit Identification Code (UIC) of the activity when it came under the NAVCOMTELCOM claimancy. These unallocated costs are being researched by DFAS-CL OPLOC Pensacola and the activity to expedite corrective action. The remaining dollars consists of expendable materials and supplies for normal inventory.

Research and Development.

NSWC. Inventories of operating supplies and non-consumable items, are valued at weighted average. Direct Material Inventory is valued at acquisition cost by line item. Generally, these values are based on prices paid for recently acquired items plus appropriate surcharges.

NAWC. Inventories are valued using the weighted average method. The majority of inventory is retained for use on customer orders. An allowance for inventory losses account has been established to accrue potential inventory shortfalls over the fiscal year. This activity group manufactures inventory that is later used on customer projects. The cost to produce the manufactured inventory in FY 1998 was $0.

NUWC. Inventories of operating supplies and non-consumable items, are valued at weighted average. Direct Material Inventory is valued at acquisition cost by line item. Generally, these values are based on prices paid for recently acquired items plus appropriate surcharges.

NRL. Operating Materials and Supplies inventories Held for Use are valued at weighted average as required by DoD accounting policy. An allowance for inventory losses account has also been established to accrue potential inventory short falls over the fiscal year. $58 thousand of the total $1,350 thousand Operating Materials and Supplies for this activity group is material ordered from the General Services Administration and paid for, but which has

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not yet been received. NRL conducts annual wall-to-wall inventory of Operating Materials and Supplies inventories. The net adjustments resulting from the wall-to-wall inventories in FY 1998 was a $25 thousand loss. These inventories are not sponsor owned but are materials and supplies held for use in performing mission requirements.

SSCs. The SSC's no longer hold inventory for Operating Materials and Supplies. Shop stores were closed at the end of FY 1997 in preparation for the increased usage of the IMPAC card. Any inventory that may have been maintained during the fiscal year would have been maintained at cost, using the weighted average. The major portion of the materials and supplies are obtained through the IMPAC card. The total Operating Materials and Supplies amount of $4,715 thousand included above represents material-in-transit and will be forwarded to the ordering official upon receipt.

d. The following table identifies those industrial activity groups that do not have sponsor funded material and those that have sponsor funded material. Sponsor funded material is recorded only in a statistical account and not reported on the Balance Sheet or in the numeric portion of Note 8.B.

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Activity Group	No Sponsor Funded Material	Sponsor Funded Material	(in thousands) Amount
Depot Maintenance – Shipyards		X	$1,481
Depot Maintenance – Aviation		X	14,749
Depot Maintenance – Other (Marine Corps)	X		
Ordnance		X	10,209
Transportation	X		
Base Support			
PWC's	X		
NFESC	X		
Information Services			
NAVCOMTELCOM	X		
FMSO*			
COMNAVRESFOR	X		
Research and Development			
NSWC		X	431,583
NAWC	X		
NUWC		X	612,377
NRL	X		
SSCs		X	21,885
Total			$1,092,284

*This activity group does not have Operating Materials and Supplies.

Legend: Valuation Methods
LAC = Latest Acquisition Cost
SP = Standard Price
AC = Actual Cost
NRV = Net Realizable Value
O = Other

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Note 8.C. Stockpile Materials ($ in Thousands):

	(1) Stockpile Materials Amount	(2) Allowance for Losses	(3) Stockpile Materials, Net	(4) Valuation Method
1. Stockpile Materials:				
(a) Held for Sale*	$0	$0	$0	
(b) Held in Reserve for Future Sale				
Total	$0	$0	$0	

2. Restrictions on stockpile materials and supplies: Not Applicable

3. Other Information:

*Not held for sale in the normal course of business

Legend: Valuation Methods
LAC = Latest Acquisition Cost
SP = Standard Price
AC = Actual Cost
NRV = Net Realizable Value
O = Other

Note 8.D. Seized Property ($ in Thousands): Not Applicable

Note 8.E. Forfeited Property, Net ($ in Thousands): Not Applicable

Note 8.F. Goods Held Under Price Support and Stabilization Programs, Net ($ in Thousands): Not Applicable

Note 8.G. Work In Process ($ in Thousands):

	(1) Work in Process Amount	(2) Valuation Method
A. Work in Process:		
1. In House	$1,160,020	Actual Cost
2. Contractor	26,456	
3. Other Government Activities	36,933	
4. Government Furnished Materials		
Total	$1,223,409	

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B. Other Information: Work-in-Process at NWCF industrial activities consists of costs incurred for customers, not yet billed. Work-in-Process does not apply to the supply activity group. The FY 1998 CFO reporting requirements have combined Work-in-Process with other inventory and property categories (e.g., Inventory, and Operating Materials and Supplies) that were reported separately on the FY 1997 CFO Statement of Financial Position and related notes. Since the DoD guidance did not address Work-in-Process, with DFAS concurrence, Note 8.G Work-in-Process was added to provide disclosure of the Work-in-Process amount. $310 thousand of the Work-in-Process should have been reported as Construction-in-Progress under Note 9 General Property, Plant and Equipment. COMNAVRESFOR will work with DFAS-CL OPLOC Pensacola to correct this inaccuracy in FY 1999.

Note 8. Recap of Inventory and Other Related Property ($ in Thousands):

	Amount
Inventory, Net	$14,658,789
Operating Materials and Supplies, Net	542,730
Stockpile Materials, Net	
Seized Property, Net	
Forfeited Property, Net	
Work in Process	1,223,409
Total	$16,424,928

Note 9. General Property, Plant and Equipment (PP&E), Net ($ in Thousands):

	(1) Depreciation Method	(2) Service Life	(3) Acquisition Value	(4) Accumulated Depreciation	(5) Net Book Value
Major Classes of Assets					
A. Land	N/A	N/A	$128,355	$0	$128,355
B. Structures, Facilities and Leasehold Improvements	SL	Various	7,012,091	4,193,191	2,818,900
C. ADP Software	SL	1-5	87,300	71,235	16,065
D. Equipment	SL	Various	3,546,498	2,499,571	1,046,927
E. Assets Under Capital Lease					
F. Construction-in-Progress	N/A	N/A	364,965		364,965
G. Other	SL	Various	19,682	1,088	18,594
Total			$11,158,891	$6,765,085	$4,393,806

Legends:

Column (1) Above
Depreciation Methods

SL = Straight Line
O = Other (explain)

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H. Other Information:

1. When records are not available to support the original acquisition cost of General PP&E at the time of capitalization, estimates are used. Estimates are based on the cost of similar assets at the time of acquisition. The depreciation method is straight line. Service Life varies by class of fixed asset and activity group as shown below:

	Service Life of Major Classes of Assets			
Activity Group	**B. Structures, Facilities & Leasehold Improvements**	**C. ADP Soft-ware**	**D. Equip-ment**	**G. Other**
Depot Maintenance – Shipyards	>20	N/A	6-10	N/A
Depot Maintenance – Aviation	>20	1-5	6-12	1-5
Depot Maintenance – Other (Marine Corps)	20	N/A	10	
Ordnance	>20	1-5	6-10	N/A
Transportation	20	5	10	
Base Support				
PWCs	*20	1-5	**10	
NFESC	*20	N/A	**10	N/A
Information Services				
NAVCOMTELCOM	N/A	1-5	1-5	N/A
FMSO	N/A	N/A	1-5	N/A
COMNAVRESFOR	N/A	N/A	5-10	N/A
Research and Development				
NSWC	>20	1-5	6-10	N/A
NAWC	>20	1-5	6-12	N/A
NUWC	>20	1-5	6-10	N/A
NRL	20	5	10	N/A
SSCs	>20	N/A	Various	N/A
Supply Management (Navy)	11-20	N/A	5-20	N/A
Supply Management (Marine Corps) (Note 9 N/A)	N/A	N/A	N/A	N/A

*Except for facilities in service prior to FY 1992 for which Service Life was established upon construction based on a variable scale. **Except for General Purpose Vehicles for which depreciation is 5 years.

2. The following table identifies those industrial activities and supply activities groups that do not have sponsor funded equipment and those that have sponsor funded equipment. This sponsor funded equipment is recorded only in a statistical account and not reported on the Balance Sheet or in the numeric portion of Note 9.

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Activity Group	No Sponsor Funded Equipment	Sponsor Funded Equipment	(in thousands) Net Book Value
Depot Maintenance – Shipyards		X	$51,836
Depot Maintenance – Aviation			
IMRL*		X	45,895
Non-IMRL		X	37,108
Depot Maintenance – Other (Marine Corps)	X		
Ordnance		X	10,883
Transportation	X		
Base Support			
PWCs		X	2,419
NFESC		X	218
Information Services			
NAVCOMTELCOM	X		
FMSO	X		
COMNAVRESFOR	X		
Research and Development			
NSWC		X	176,521
NAWC			
IMRL**		X	199,238
Non-IMRL		X	228,433
NUWC		X	195,213
NRL		X	79,018
SSCs		X	61,629
Supply Management (Navy)	X		
Supply Management (Marine Corps)***	X		
Total			$1,088,411

*The net book value for IMRL equipment reported in the narrative portion only of the FY 1997 CFO Property, Plant and Equipment, Net footnote was overstated by $34,296 thousand due to a misclassification of some equipment purchased under the old Assets Capitalization Program. This overstatement in FY 1997 creates the appearance of a significant reduction in net book value in FY 1998.

**The amount reported is the gross value.

***This activity groups does not have any General PP&E.

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3. The following table provides disclosure of the fully depreciated assets included in the numeric portion of Note 9.

Activity Group	(in thousands) Amount of Fully Depreciated Assets
Depot Maintenance – Shipyards	$531,888
Depot Maintenance – Aviation	268,959
Depot Maintenance – Other (Marine Corps)	19,942
Ordnance	192,246
Transportation	9,980
Base Support	
PWCs	68,114
NFESC	
Information Services	
NAVCOMTELCOM	10,394
FMSO	
COMNAVRESFOR	543
Research and Development	
NSWC	462,179
NAWC	736,280
NUWC	105,764
NRL	183,511
SSCs	72,016
Supply Management (Navy)	478,992
Supply Management (Marine Corps)*	
Total	$3,140,808

*This activity groups does not have any General PP&E.

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4. The following table provides footnote disclosure of NWCF activity groups which still include the accumulated depreciation of "Fixed Assets Not in Use" under the numeric portion of Note 9 which deviates from the DoD guidance. For those NWCF activity groups the current systems have not been revised to implement the DFAS-CL guidance of 16 October 1997 for reporting Accumulated Depreciation - Assets Not in Use under Contra Account 1671. In the case of the SSCs activity group the accumulated depreciation of Assets Not in Use is included in the numeric portion of Note 9 other capital asset depreciation accounts, because DIFMS does not break out the depreciation associated with Fixed Assets Not in Use separately.

Activity Group	Depreciation Still Included In Note 9	Assets Not in Use Included in Note 9 But Not Depreciated
Depot Maintenance – Shipyards	X	
Depot Maintenance – Aviation		
Depot Maintenance – Other* (Marine Corps)		X
Ordnance*	X	
Transportation*		
Base Support		
PWCs		
NFESC*		
Information Services		
NAVCOMTELCOM	X	
FMSO		
COMNAVRESFOR*	X	
Research and Development		
NSWC	X	
NAWC		
NUWC	X	
NRL		
SSCs**	X	
Supply Management (Navy)*		
Supply Management (Marine Corps)***		

*This activity group had no Fixed Assets Not in Use on Line J of the Balance Sheet as of 30 September 1998.

**Navy Account 1671 Accumulated Depreciation - Assets Not in Use which is a contra account to Assets Not in Use was established and in use under the SSC's old financial system. Once the

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SSC's were converted to the DIFMS financial accounting system, the calculation for Navy Account 1671 no longer existed and the depreciation was incorporated with other accounts maintained for depreciation. This problem has been reported to DFAS the DIFMS CDA for correction.

***This activity groups does not have any General PP&E.

5. The following provides other disclosures by activity group.

Depot Maintenance – Other Marine Corps. The value of this activity group's Construction-in-Progress, $13,738 thousand is being reviewed by DFAS–KC to determine its validity.

Transportation. A liquidation write off of $192 thousand in Structures, Facilities, and Leasehold Improvements was made by COMSCWEST as a result of their move to San Diego, CA. The triennial inventory of plant property was conducted during FY 1997 for COMSC Headquarters and COMSCWEST. The physical inventory was taken during FY 1995 for COMSC Far East, and COMSC Europe. COMSCEAST is scheduled for a physical inventory in December 1998.

Based on direction provided by DFAS, fixed assets such as ships are considered as used but not owned by the Working Capital Fund activity group. In accordance with such guidance, Ships, Seasheds, Flatracks, Modular Fuel Delivery Systems, and Containership Cargo Stowage Adapters are Statistically recorded and depreciated by MSC, but not included in the Transportation activity group's CFO Balance Sheet or numeric portion of Note 9. These assets when appropriate for CFO reporting (e.g., to be reported on the Balance Sheet or to be reported as Supplementary Stewardship Information) would be reported by the DON General Funds (Index 17). The amounts for NWCF are as follows:

Account Title	(in thousands) Amount
Fixed asset-ships	$6,562,370
Accumulated depreciation	1,811,474
Net Value	$4,750,896

Information Services.

NCTC. The triennial plant inventory was completed as of 30 September 1997.

COMNAVRESFOR. An inventory of General PP&E was completed in FY 1998.

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Research and Development.

NAWC. The Assets Under Development were reduced by $25,641 thousand in compliance with FY 1997 CFO NAVAUDSVC audit finding.

Supply Management (Navy). NAVAUDSVC draft audit report 98-0099, Recommendation 40, indicated the value reported for Property, Plant and Equipment was understated by $2,389 thousand and recommended a physical inventory be conducted. A wall to wall inventory is scheduled prior to the implementation of the Defense Property Accountability System (DPAS), which is the DoD migratory system. DPAS is scheduled for implementation prior to CY 2000.

6. See Note 1.M for footnote disclosure of the General PP&E capitalization threshold policy and additional information on the depreciation policy being used by the NWCF activities**.**

Note 10. Debt ($ in Thousands):

	Beginning Balance	Net, Borrowing	Ending Balance
A. Public Debt:			
(1) Held by Government Accounts	$0	$0	$0
(2) Held by the Public			
(3) Total Public Debt	$0	$0	$0
B. Agency Debt:			
(1) Held by Government Accounts	$0	$0	$0
(2) Held by the Public			
(3) Total Agency Debt	$0	$0	$0
C. Other Debt:			
(1) Debt to the Treasury			
(2) Debt to the Federal Financing Bank	$1,164,026	$69,316	$1,094,710
(3) Debt to Other Federal Agencies			
(4) Total Other Debt	$1,164,026	$69,316	$1,094,710
D. Total Debt	$1,164,026	$69,316	$1,094,710
E. Classification of Debt :			
Intragovernmental Debt			$1,094,710
Governmental Debt			
Total Debt			$1,094,710

F. Other Information:

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The $1,094,710 thousand debt represents the Transportation activity group outstanding principal balance on the APF-N ships. See Note 2 regarding the Transportation activity group transfer-out of $69,316 thousand made to the FFB for the principal payment of loans related to APF-N ships. See Note 6 for the recognition of the Other Entity Assets (Other) related to the outstanding principal balance of $1,094,710 thousand for loans from the FFB for the APF-N ships.

The APF-N program provided ships for Time Charter to MSC to meet requirements not available in the marketplace. The program was approved by the Congress. The ships were built/converted by private Interim Vessel Owners using private, non-government financing obtained from various banking institutions. No payments were made by the government during the building/conversion phase.

When each vessel was delivered to MSC for use under the Time Charter Party, the interim financing was replaced by permanent financing, and vessel ownership was transferred to the permanent vessel owners (a trust company acting for the benefit of equity investors). The ships were financed with approximately 30 percent equity investments and 70 percent debt borrowings. The debt is in the form of loans from the FFB to the vessel owners. Capital hire payments under the Time Charter are assigned to FFB to cover the loan obligations, and to the vessel owners to cover the equity obligations.

The Time Charter Party requires MSC to pay Capital Hire twice a year. These payments cover repayment of principal and interest on the FFB loans, and any equity payments due the vessel owners. Separately, Operating Hire is paid twice a month to the vessel operators to cover crew costs, provisions, ship management, etc., and specified reimbursements such as fuel and port expenses are paid to the operators. These expenses are paid from the NWCF. APF-N Time Charters are for five years with four option renewal periods of five years each, for a total of 25 years. At the end of the contract, the ships belong to the ship owner. The government does have an option to purchase the ships, if the contract is terminated, at the greater of the fair market value or termination value.

In order to simplify the payments to the FFB and to meet their requirements, the FFB cross-disburses the semi-annual principal and interest payments directly from the NWCF. This is done instead of having MSC make Capital Hire payments to the vessel owners, who would in turn make their loan obligation payments to the FFB. This is very much the same as other Time Charters where payment is assigned directly to a bank. Equity payments, on the other hand, are made by MSC from the NWCF, upon receipt of invoices.

The Time Charters contain a clause requiring payment of stipulated termination penalties in the event the government desires to end the contracts prior to their final expiration (25 years for the APF-N). These penalties apply whether the termination results from a Termination for Convenience by the government, or by mere failure of the government to exercise its five-year renewal options. The contract requires that the ships be sold for the best price obtainable, and, if

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that is below the applicable termination value, the government makes up the difference. The Time Charters also contain casualty loss values in case of total loss of the ships which would be payable by the government to the vessel owners investors. In case of total loss the Time Charter requires the contractor to maintain casualty insurance sufficient to cover the casualty values due to the vessel owners including the amounts that they would owe to the FFB.

The DoD Appropriation Act passed in December 1985 required that 10 percent of the fifth year termination value of the vessels be obligated from Operation and Maintenance, Navy funds. This was done as each vessel was delivered.

Note 11. Other Liabilities ($ in Thousands):

Note 11.A Environmental Cleanup ($ in Thousands):

1. Environmental Cleanup Liabilities Covered by Budgetary Resources:

	Noncurrent Liability	Current Liability	Total
(a) Intragovernmental			
(1) Accrued Cleanup Costs	$0	$0	$0
(2) Other Environmental Liabilities			
Total	$0	$0	$0
(b) With the Public			
(1) Accrued Cleanup Costs	$0	$0	$0
(2) Other Environmental Liabilities			
Total	$0	$0	$0

2. Environmental Cleanup Liabilities Not Covered by Budgetary Resources:

	Noncurrent Liability	Current Liability	Total
(a) Intragovernmental			
(1) Accrued Cleanup Costs	$0	$0	$0
(2) Other Environmental Liabilities			
Total	$0	$0	$0
(b) With the Public			
(1) Accrued Cleanup Costs	$0	$0	$0
(2) Other Environmental Liabilities			
Total	$0	$0	$0

3. Other Information: Not Applicable

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Note 11.B Other Liabilities ($ in Thousands):

1. Other Liabilities Covered by Budgetary Resources:

	Noncurrent Liability	Current Liability	Total
(a) Intragovernmental			
(1) Advances from Others	$0	$1,032,346	$1,032,346
(2) Deferred Credits		63,432	63,432
(3) Deposit Funds and Suspense Account Liabilities			
(4) Liability for Borrowings to be Received			
(5) Liability for Subsidy Related to Undisbursed Loans			
(6) Other Liabilities		271,574	271,574
(7) Resources Payable to Treasury			
Total	$0	$1,367,352	$1,367,352
(b) With the Public			
(1) Accrued Funded Payroll and Benefits	$0	$724,585	$724,585
(2) Advances from Others		74,341	74,341
(3) Deferred Credits			
(4) Deposit Funds and Suspense Accounts			
(5) Other Liabilities		74,624	74,624
Total	$0	$873,550	$873,550

2. Other Information:

a. The recording of non-expenditure transfers, especially for disaster relief funds provided via special Congressional action to repair storm damage associated with the affects of El Nino in California and typhoon PAKA in Guam, has caused reconciliation problems. The reconciliation problems are between the activity level liability accounts which are overstated and the departmental liability accounts in Other Liabilities Covered by Budgetary Resources (Intragovernmental), Other Liabilities. These problems will be addressed during FY 1999. The related amounts are $23,017 thousand in the Base Support - PWCs activity group for typhoon Paka storm damage and $18,412 thousand in the Research and Development - NAWC activity group for El Nino storm damage.

b. See Note 23 for discussion on the treatment of the Undistributed Collections and Undistributed Disbursements. For the Navy industrial type activity groups and the Navy Component, SGL Accounts 1014 and 1015 have been netted against each other and displayed on the Balance Sheet, Line 4.A.4, Liabilities Covered by Budgetary Resources (Intragovernmental) Other Liabilities and Note 11, Other Liabilities Covered by Budgetary Resources

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(Intragovernmental) Other Liabilities. This display follows the practice established in FY 1997 per guidance from DFAS dated 2 December 1997.

c. The following provides other disclosures by activity group.

Transportation. Contingencies (Reserves) have been established to provide for anticipated accident and damage repairs and estimated value of claims. Their values are $1,125 thousand included in Other Liabilities Covered by Budgetary Resources (Intragovernmental), Other Liabilities and $3,558 thousand included in Other Liabilities Covered by Budgetary Resources (With the Public), Other Liabilities, respectively. It should be noted that the reserve for accident and damage repairs will be abolished and the remaining value in such account represents funds already obligated. Other Liabilities Covered by Budgetary Resources (Intragovernmental), Deferred Credits includes Military Labor in the amount of $5,981 thousand. Other Liabilities Covered by Budgetary Resources (With the Public), Accrued Funded Payroll and Benefits consists of MSC's accrued expenses for payroll and benefits in the amount of $26,209 thousand.

Base Support.

NFESC. For this activity group $81 thousand of the Other Liabilities Covered by Budgetary Resources (Intragovernmental), Deferred Credits represents military labor costs. $410 thousand represents Other Liabilities Covered by Budgetary Resources (With the Public), Advances from Others.

Information Services.

NAVCOMTELCOM. The negative ($2,948) thousand balance in Other Liabilities Covered by Budgetary Resources (Intragovernmental), Other Liabilities reflects prior year undistributed disbursements and is associated with the NAVCOMTELCOM New Orleans transfer to the COMNAVRESFOR in FY 1997. According to DFAS and DFAS-CL OPLOC Pensacola, when NAVCOMTELCOM New Orleans transferred to COMNAVRESFOR, there were collections and disbursements that had not surfaced until such time after the new balance sheets for the NAVCOMTELCOM organization and the new COMNAVRESFOR organization were created. DFAS-CL OPLOC Pensacola and DFAS-CL are preparing a solution to resolve this imbalance by the end of FY 1999.

FMSO. $15,416 thousand Other Liabilities Covered by Budgetary Resources (Intragovernmental), Other Liabilities represents the change in net outlays between FY 1997 and FY 1998.

COMNAVRESFOR. $2,948 thousand of Other Liabilities Covered by Budgetary Resources (Intragovernmental), Other Liabilities represents offsetting adjustments made by DFAS-CL OPLOC Pensacola. The offsetting adjustments of $2,948 thousand were made to the NAVCOMTELCOM financial statements in FY 1997 at the time of establishing

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COMNAVRESFOR as a separate activity group. DFAS-CL has been contacted to correct these balances.

Research and Development.

SSCs. Other Liabilities Covered by Budgetary Resources (With the Public), Accrued Funded Payroll and Benefits is overstated in the amount of $124 thousand. Unknown payroll charges were processed against the SSC San Diego, CA payroll account (vice the unallocated account) until the time that the charges could be identified. Advance billings directed by ASN(FM&C) during FY 1997 amounted to $50,000 thousand, of which $4,885 thousand remain unliquidated and are included under Other Liabilities Covered by Budgetary Resources (Intragovernmental), Advances from Others. These billings represent charges to customers in advance of performance of work based on projected workloads. Advances received from non-DoD sponsors in advance to authorize the performance of work or services amounted to $16,491 thousand and are included under Other Liabilities Covered by Budgetary Resources (With the Public), Advances from Others.

Supply Management (Navy). The necessary adjustment to Other Liabilities (Ships Stores Profits Transferable) account to close out the residual $7,000 thousand balance was made in FY 1998 based on NAVAUDSVC draft audit report 98-0099, Recommendation 55. The necessary adjustment to Other Liabilities (Unearned Revenue-Advances from Governments) Account for $4,400 thousand (reduction) was made in FY 1998 based on NAVAUDSVC draft audit report 98-0099, Recommendation 57. The necessary adjustment to the Other Federal (Intragovernmental) Liabilities Account for $4,357 thousand (reduction) based on NAVAUDSVC draft audit report 98-0099, Recommendation 51, was made in FY 1998. These actions are complete.

Navy Component. The value reported represents the net of collections and disbursements held in this activity group pending identification to another activity group. Included in Other Liabilities Covered by Budgetary Resources (Intragovernmental) Other Liabilities is $1,044,715 thousand which is an allocation of disbursements from the DWCF Corporate account. This allocation was directed by a DFAS memorandum of 10 October 1997. This directed allocation was not supported by specific transactional information which would identify the value as belonging to the NWCF. ASN(FM&C) memorandum of 24 November 1997 to DFAS challenges the validity of this decision and requests the value be reversed.

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3. Other Liabilities Not Covered by Budgetary Resources:

	Noncurrent Liability	Current Liability	Total
(a) Intragovernmental			
(1) Accounts Payable - Canceled Accounts	$0	$0	$0
(2) Custodial Liability			
(3) Deferred Credits			
(4) Liability for Borrowings to be Received			
(5) Other Actuarial Liabilities			
(6) Other Liabilities			
Total	$0	$0	$0
(b) With the Public			
(1) Account Payable Canceled	$0	$0	$0
(2) Accrued Cleanup/Cost			
(3) Accrued Unfunded Liabilities			
(4) Deferred Credits			
(5) Other Liabilities			
(6) Prior Liens Outstanding on Acquired Collateral			
Total	$0	$0	$0

4. Other Information: Not Applicable

Note 12. Leases ($ in thousands): Not Applicable

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Note 13. Pensions and Other Actuarial Liabilities ($ in Thousands):

Major Program Activities	(1) Actuarial Present Value of Projected Plan Benefits	(2) Assumed Interest Rate (%)	(3) Assets Available to Pay Benefits	(4) Unfunded Actuarial Liability
A. Pensions and Health Benefits:				
1. Military Retirement Pensions	$0		$0	$0
2. Military Retirement Health Benefits				
Total	$0		$0	$0
B. Insurance/Annuity Programs:				
1.	$0		$0	$0
2.				
3.				
Total	$0		$0	$0
C. Other:				
1. Workers' Compensation	$1,176,474		$0	$1,176,474
2.				
3.				
Total	$1,176,474		$0	$1,176,474
D. Total Lines A+B+C:	$1,176,474		$0	$1,176,474

E. Other Information:

The actuarial cost method used and assumptions: The amount of $2,390,148 thousand was provided by the Department of Labor (DOL) to DoD as the actuarial liability estimate for DON's future workers' compensation benefits (FWC). Of that amount, $1,176,474 thousand for NWCF was the result of the ASN(FM&C) FMO breaking down the DON portion provided by the DOL between the General Fund and the NWCF. The NWCF breakdown is by number of civilian employees taken from the Navy Budget Tracking System and the numbers were FY 1998 actuals. The liability for FWC benefits includes the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases. The liability is determined using a method that utilizes historical benefit payment patterns 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 OMB's economic assumptions for 10-year Treasury notes and bonds. Interest rate assumptions utilized for discounting were as follows:

1998
5.60% in year 1,
and thereafter

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The amount of change in workers' compensation from FY 1997 to FY 1998 for the Other Actuarial Liability is an increase of $16,403 thousand (FY 1998 $1,176,474 thousand minus FY 1997 $1,160,071 thousand). In accordance with DFAS guidance of 20 January 1999, the change in workers' compensation from FY 1997 to FY 1998 is reported on the Consolidated Statement of Net Cost as Program Costs (With the Public), which is reported under the Component activity group on the Consolidating Statement of Net Cost as Program Costs (With the Public). Also see Notes 1.C, 16.H and 16.I.

Note 14. Unexpended Appropriations ($ in Thousands): Not Applicable

Note 15. Contingencies ($ in Thousands): The following provides disclosure by activity group for those groups reporting contingencies. Also see related NWCF Consolidated Notes 1.F.4 and 1.P.

Depot Maintenance - Shipyards. We have been notified of a liability against the Depot Maintenance-Shipyards activity group resulting from litigation and settlement of claims before the Armed Services Board of Contract Appeals (ASBCA). These claims were against a February 1986 contract for the procurement of 23 large portal cranes by Commander, Naval Facilities Engineering Command (COMNAVFACENGCOM) Navy Crane Center; 21 of which were ordered by or subsequently transferred to Naval Shipyards. COMNAVFACENGCOM has negotiated final global settlement of those claims with the contractor. The Treasury Department has requested reimbursement for payment made by the Judgement Fund in the amount of $23 million which includes $15.4 million chargeable to NWCF. The ASN(FM&C) Office of Budget (FMB) has requested FY 2000 Capital Purchase Program authority, with the concurrence of the USD(C), to make this $15.4 million repayment in FY 2000.

Transportation. While claimants have alleged that MSC has breached various contracts, and the collective settlement amounts proposed by the claimants exceed $19,000 thousand, the actual litigative risk, as assessed by MSC's legal office, are considered minimal. Therefore, the amount of contingent liabilities resulting from claims is assessed at zero dollars.

In August 1998, MSC was alerted that the DoD, Defense Criminal Investigation Service, and Naval Criminal Investigative Service working with the Federal Bureau of Investigation, had performed a four year investigation into allegations of fraud, kickbacks, and false claims involving federal contracts with maritime companies for repairs of United States Navy ships. The investigation was initiated when allegations of fraud in the maritime industry regarding repair contracts for work onboard Naval ships were reported to law enforcement agents in June 1994. The fraud largely involved repair contracts and bid rigging. The amount of the fraud as it relates to MSC is estimated at $650 thousand.

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Base Support.

PWCs. It is estimated that claims for payments and adjudicated claims that will be outstanding as resolution of legal actions still pending will not materially affect the agency's operations or financial condition. Therefore, no contingent liabilities have been recognized in the Balance Sheet. As of January 1998, the PWCs were a party to sixteen contract appeals before the ASBCA. The total value of these appeals is $3,860 thousand of which $3,660 thousand has been recovered.

NFESC. It is estimated that claims for payments and adjudicated claims that will be outstanding as resolution of legal actions still pending will not materially affect the agency's operations or financial condition. Therefore, no contingent liabilities have been recognized in the Balance Sheet. As of January 1998, NFESC did not have any contract appeals before the ASBCA.

Research and Development.

SSCs. SSCs liabilities have not been established for pending Equal Employment Opportunity (EEO) cases as their outcome cannot be predicted. Currently there are five EEO cases that have been forwarded to the Merit Systems Protection Board and five cases forwarded to District Court where an unfavorable decision could result in a combined total of $414 thousand in damages. These payments will be made with current year overhead funds from the fiscal year in which the claim is settled. Since the NWCF is a revolving fund, there would not be any advantage to establishing a contingent liability for these cases. Liabilities have not been established for two Resource Management System contracts equaling $1,155 thousand that were transferred during BRAC consolidations. Once these cases are resolved, money will be requested from the sponsor's appropriation.

Note 16. Footnote Disclosures Related to the Statement of Net Cost ($ in Thousands):

Note 16.A. Suborganization Program Costs ($ in Thousands): Not Applicable

Note 16.B. Cost of National Defense PP&E ($ in Thousands): Not Applicable

Note 16.C. Cost of Stewardships Assets ($ in Thousands): Not Applicable

Note 16.D. Stewardship Assets Transferred ($ in Thousands): Not Applicable

Note 16.E. Exchange Revenue ($ in Thousands): Not Applicable

Note 16.F. Revenue and Expense Amounts for Foreign Military Sales (FMS) Program Procurements From Contractors ($ in Thousands): Not Applicable

Note 16.G. Benefit Program Expenses ($ in Thousands): Not Applicable

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Note 16.H. Gross Cost and Earned Revenue by Budget Functional Classification ($ in Thousands):

	Budget Function Code	Gross Cost	Earned Revenue	Net Cost
A. Department of Defense Military	051	$19,119,793	$19,066,487	$53,306
B. Water Resources by US Army Corps of Engineers	301			
C. Pollution Control and Abatement by US Army Corps of Engineers	304			
D. Federal Employee Retirement and Disability by Department of Defense Military Retirement Trust Fund	602			
E. Veterans Education, Training, and Rehabilitation by Department of Defense Education Benefits Trust Fund	702			
Total		$19,119,793	$19,066,487	$53,306

F. Other Information:

The Gross Cost of $19,119,793 thousand includes the activity groups program costs, the imputed expense for civilian employee pensions and ORBs, and the amount of change in workers' compensation from FY 1997 to FY 1998 for the Other Actuarial Liability.

Note 16.I. Imputed Expenses ($ in Thousands):

A. Other Information:

The NWCF Departmental level CFO statements have recognized an imputed expense for civilian employee pensions and ORBs in the Statement of Net Cost and have recognized imputed revenue for the civilian employee pensions and ORBs in the Statement of Changes in Net Position. Imputed pensions and ORBs expenses are displayed on Line 1.A, Program Costs (Intragovernmental) on the Consolidated Statement of Net Cost, which is reported under the Component activity group on the Consolidating Statement of Net Cost on Line 1.A.1 Program Costs (Intragovernmental). Also see Notes 1.C and 18.B. Imputed pension and ORBs was computed by DFAS as follows:

Statement of Net Cost
Imputed Pension and ORBs

	(in thousands)
CSRS/FERS Retirement	$211,148
Health	196,862
Life Insurance	720
Total	$408,730

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The amount of change in workers' compensation from FY 1997 to FY 1998 for the Other Actuarial Liability is an increase of $16,403 thousand (FY 1998 $1,176,474 thousand minus FY 1997 $1,160,071 thousand). In accordance with DFAS guidance of 20 January 1999, the change in workers' compensation from FY 1997 to FY 1998 is reported on the Consolidated Statement of Net Cost as Program Costs (With the Public), which is reported under the Component activity group on the Consolidating Statement of Net Cost as Program Costs (With the Public). Also see Notes 1.C and 13.

Note 17. Deferred Maintenance on Property, Plant & Equipment ($ in Thousands):

Note 17.A. Summary of Deferred Maintenance Amounts by Category of Property, Plant and Equipment ($ in Thousands):

As of September 30, 1998

(a) Category	(b)
1. General Property, Plant and Equipment	$718,913
2. National Defense Property, Plant and Equipment	
3. Heritage Assets	
4. Stewardship Land	
Total	$718,913

Note 17.B. General Property, Plant and Equipment Deferred Maintenance Amounts ($ in Thousands):

As of September 30, 1998

(a) Property Type/Major Class	(b)
1. Personal Property	$0
2. Real Property	
A. Buildings	433,921
B. Structures	284,101
C. Land	891
D Total Real Property	718,913
3. Total	$718,913

Narrative Statement:

Actual hands-on, on site facility inspections are essential to the accurate determination of real property maintenance and repair requirements. The Reported Backlog of Maintenance and Repair (BMAR) is based on a continuous fence-to-fence inspection of facilities at each Navy

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installation, the results of which are reported each year in the Annual Inspection Summary (AIS) collected by the Commander, Naval Facilities Engineering Command (COMNAVFACENG-COM). The AIS is an inventory of each facility's BMAR deficiencies, including the cost to repair the stated deficiency, remaining at the end of the fiscal year. Deficiencies do not include alterations, additions, equipment installation, or recurring and preventative maintenance.

The reported BMAR, referred to as critical BMAR, includes only those critical deficiencies which are a firm requirement of the installation and meet one of the following criteria:

- Environmental - A deficiency posing an unacceptable risk of environmental damage or violation of statutory or regulatory requirements.

- Loss of Mission - A deficiency which has degraded mission capability contributing to a C3 or C4 facility condition rating in a standard base report (BASEREP) mission area.

- Safety - A deficiency with a risk assessment code of 1, 2, or 3.

- Quality of Life - A deficiency which has degraded the habitability or use of the barracks, galley, Morale Welfare and Recreation facilities or other personnel support and service facilities.

No changes have been made to the condition requirements or standards from the previous BMAR reporting year.

BASEREP Rating Procedures:

C1 - Has <u>fully</u> met all demands placed upon it in a mission category throughout the reporting period.

C2 - Has <u>substantially</u> met all demands of the mission category throughout the reporting period with only minor difficulty.

C3 - Has only <u>marginally</u> met the demands of the mission category throughout the reporting period, but with major difficulty.

C4 - Has <u>not</u> met vital demand of the mission category.

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Risk assessment code is an expression of risk which combines the elements of hazard severity and mishap probability. The codes are:

1 - Critical
2 - Serious
3 - Moderate
4 - Minor
5 - Negligible

Only those deficiencies that qualify as critical BMAR per the standards described above are reported in the above table. Specific details for each of the deficiencies, by site, and location, can be obtained from a review of the summary AIS collected by COMNAVFACENGCOM. The listing is too voluminous for this narrative summary.

The cost assessment survey method is used in developing BMAR data for real property.

Note 17.C. National Defense Property, Plant and Equipment Deferred Maintenance Amounts ($ in Thousands):

As of September 30, 1998

(a) Major Type	(b)
1. Aircraft	$0
2. Ships	
3. Missiles	
4. Combat Vehicles	
5. Other Weapons Systems	
Total	$0

Narrative Statement: Not Applicable

Note 18. Footnote Disclosures Related to the Statement of Changes in Net Position ($ in Thousands):

Note 18.A. Prior Period Adjustments ($ in Thousands):

A. Prior Period Adjustments:	
1. Changes in Accounting Standards	$0
2. Errors and Omission in Prior Year Accounting Reports	55,694
3. Policy Change – Deferred AOR	(394,102)
4. Other - Model Adjustment to COGS	(626,818)
Total	($965,226)

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B. Other Information:

1. The Prior Period Adjustments includes a total negative ($389,533) thousand which represents the results from the closure of the JLSC. This was directed by USD(C) memorandum of 19 August 1998, which also provided the allocation of system development costs incurred by JLSC to the appropriate DWCF activity groups. As instructed by the USD(C) memorandum, the Navy distributed the transferred amounts among the affected NWCF activities. This distribution of the transferred amounts was provided to DFAS, who made the accounting entries based on the USD(C) memo. These system development costs were incurred from FY 1992 through 30 September 1998. The JLSC negative ($389,533) thousand was also recorded as CRO - Deferred. This is a categorization of CRO - Deferred which requires the approval of USD(C) prior to recording and represents an exclusion of the recorded amounts from customer rate setting. The following table displays the prior period adjustment amounts which were categorized as CRO - Deferred:

Activity Group	(in thousands) Deferred Amounts	Reason for Deferral
Depot Maintenance – Shipyards	($70,112)	JLSC
Depot Maintenance – Aviation	(58,102)	JLSC
Depot Maintenance – Other (Marine Corps)	(7,562)	JLSC
Ordnance	(9,120)	JLSC
Research and Development NSWC	(813)	JLSC
Supply Management (Navy)	(243,824)	JLSC
Subtotal	(389,533)	
Research and Development NSWC	(4,569)	Depreciation
Total	($394,102)	

The remaining negative ($4,569) thousand represents the amount of discontinued depreciation expense at closing activities not previously reported in the financial statements. This recording of discontinued depreciation costs is the result of Recommendation 4 of NAVAUDSVC audit report 040-97.

2. The following provides disclosure by activity group for those groups reporting prior period adjustments.

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Depot Maintenance - Shipyards. The Prior Period Adjustments - Errors and Omission in Prior Year Accounting Reports $13,821 thousand at this activity group are due to the purification of accrued expense accounts and the reconciliation of Work-in-Process accounts at the closed shipyards. This is offset by a prior year adjustment of $1,558 thousand at Norfolk Naval Shipyard for depreciation costs associated with completed projects previously reported as assets under development. The Prior Period Adjustments – Policy Change - Deferred Accumulated Operating Results (AOR) of negative ($70,112) thousand represents the results from the closure of the JLSC.

Depot Maintenance - Aviation. This activity group's negative ($58,102) thousand Prior Period Adjustments – Policy Change - Deferred AOR represents the results from the closure of the JLSC.

Depot Maintenance - Other (Marine Corps). Prior Period Adjustments to AOR total negative ($8,413) thousand. Part of the prior period adjustment is negative ($2,051) thousand for payroll and fringe benefits approved by Headquarters, Marine Corps. Additionally, this adjustment reflects USD(C) directed allocation of software development costs incurred by the JLSC for FY 1995 through FY 1998 per PBD No. 401 dated December 1997. The FY 1997 cost of $1,200 thousand is already included in the beginning AOR and beginning Funds with Treasury Operating Program, therefore it is not included in the AOR Prior Period Adjustment of negative ($6,362) thousand for FYs 1995, 1996, 1998. Following are the costs associated with each fiscal year:

(in thousands)
FY 1995 $1,100
FY 1996 $1,520
FY 1997 $1,200
FY 1998 $1,500
End of Year 1998 additional cost $2,242

Ordnance. This activity group's negative ($9,120) thousand Prior Period Adjustments – Policy Change - Deferred AOR represents the results from the closure of the JLSC.

Base Support.

PWCs. The $4,968 thousand Prior Period Adjustments - Errors and Omission in Prior Year Accounting Reports for this activity group covers travel cost corrections at PWC Pensacola, over accrual of contracts, billing reconciliation errors, and other costing errors found in the process of closing out PWC San Francisco, CA accounting records and at PWC Washington, DC.

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Information Services.

NAVCOMTELCOM. This activity group had a Prior Period Adjustment - Errors and Omission in Prior Year Accounting Reports of a negative ($212) thousand.

Research and Development.

NSWC. This activity group's negative ($5,382) thousand Prior Period Adjustments – Policy Change - Deferred AOR represents the results from the closure of the JLSC in the amount of negative ($813) thousand and depreciation in the amount of negative ($4,569) thousand.

Supply Management (Navy). The value reflected in Prior Period Adjustments – Policy Change - Deferred AOR of negative ($243,824) thousand is the result of the closure of JLSC and the transfer of their systems development costs to the DWCF activity groups. The value reflected in Prior Period Adjustments - Other - Model Adjustments to COGS of negative ($626,817) thousand relates to the COGS calculation as defined in DoD FMR 7000.14R, Volume 11B and as clarified by USD(C).

Supply Management (Marine Corps). The Prior Period Adjustments - Other represents an accounting adjustment of $37, 977 thousand made to Accounts Payable. The methodology to determine Accounts Payable Public (Commercial) is to compare the Centralized Expenditures/ Reimbursement Processing System (CERPS) payments register with commercial inventory receipts. This methodology has resulted in negative Accounts Payable (Public) due to selected registered payments exceeding inventory receipts. The Marine Corps is investigating to determine if this methodology is valid to determine the split between public and government Accounts Payable. Overall government Accounts Payable is not negative.

Note 18.B. Other Disclosures to the Statement of Changes in Net Position ($ in Thousands):

A. Other Information:

The NWCF Departmental level CFO statements have recognized an imputed expense for civilian employee pensions and ORBs in the Statement of Net Cost and have recognized imputed revenue for the civilian employee pensions and ORBs in the Statement of Changes in Net Position. Imputed pensions and ORBs revenue is displayed on Line 2.D, Imputed Financing, of the Statement of Changes in Net Position. Also see Notes 1.C, 16.H and 16.I. Imputed pension and ORBs was computed by DFAS as follows:

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Statement of Changes in Net Position
Imputed Financing

	(in thousands)
CSRS/FERS Retirement	$211,148
Health	196,862
Life Insurance	720
Total	$408,730

Note 19. Disclosures Related to the Statement of Budgetary Resources ($ in Thousands):

1. Net Amount of Budgetary Resources Obligated for Undelivered Orders at the End of Period	$5,570,574
2. Available Borrowing and Contract Authority at the End of Period	$3,942,278

3. Other Information:

The Statement of Budgetary Resources is an image of the monthly Report of Budget Execution (SF 133). These reports should be produced using budgetary accounts, however, NWCF uses proprietary accounts because its financial accounting systems were not designed to produce budgetary accounting data.

The SF 133 does not measure the NWCF's budget execution against budgetary resources. Budgetary resources are recorded in the accounting records and reported on the basis of customer orders received and contract authority invoked. On these reports, the spending authority from offsetting collections during the period of execution is based upon the approved president's budget estimate of anticipated customer orders. During the fiscal year, actual orders received could potentially exceed the estimated orders which creates a negative anticipated orders for the rest of the year. However, at 30 September, the actual customers orders are used to populate this line on the report since actual execution experience replaces the estimated values.

For the SF 133, Supply Management's revenue is defined as gross sales less credit returns. For Accounting Report (AR) 1307 and the financial statements, revenue is defined as gross sales. Credit returns are used to affect the cost of the inventory and cost of goods sold. The difference in "meanings" has caused significant variances in the reports.

On these budgetary reports, the net outlays (collections and disbursements) year to date are reported based on the amounts reported to U.S. Treasury from the CERPS. There are differences between the U.S. Treasury and the NWCF activity ledgers that are due to timing and are recorded as undistributed disbursements and collections on the departmental reports. Over previous years, reporting practices changed at the field level to reduce the large balance of undistributed. While there may be no impact upon the U.S. Treasury balance, this has created

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distortions in the Accounts Payable and Accounts Receivable from a budgetary reporting perspective on the SF 133. In addition, Accounts Payable and Accounts Receivable are handled differently on the SF 133 as compared to the AR 1307 and financial statements. In addition, problems with undistributed disbursements and collections have created abnormal balances for the receivables and payables on the SF 133. DFAS has initiated actions to investigate the problems with the values reported in CERPS and the activity ledgers. Also DON is working with USD(C), and DFAS to correct these abnormal balances.

The brought forward unobligated balance for Depot Maintenance - Shipyards, Depot Maintenance - Aviation, and Ordnance activity groups understated the DON's total budgetary resources because of the recording of the cash surcharges as obligations by DFAS at the end of FY 1997. DFAS has been notified of the erroneous transactions.

According to the DoD FMR, Volume 6B, guidance on Form and Content of DoD Audited Financial Statements, eliminating entries for this statement are deferred by the revised OMB 97-01 bulletin for FYs 1998 and 1999. See the Required Supplementary Information section of this CFO financial statements report for the disaggregated Statements of Budgetary Resources.

Note 20. Disclosures Related to the Statement of Financing ($ in Thousands):

The Statement of Financing is a new Principal Statement for FY 1998. This statement should be read in the context of a revolving fund, which generally is not funded by expiring appropriations, but rather by reimbursable orders. The NWCF does not report any liabilities not covered by budgetary resources.

Note 21. Disclosures Related to the Statement of Custodial Activity ($ in Thousands): Not Applicable

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Note 22. Inter-Agency Eliminations with Other Federal Agencies ($ in Thousands):

		(A)	(B)	(C)
Part A. Department of Defense Eliminations of Seller Activity With Other Federal Agencies Arrayed by Department of Defense Entities	**Treasury Index (T.I.) or T.I. and Appropriation**	**Accounts Receivable With Other Federal Agencies**	**Revenue With Other Federal Entities**	**Unearned Revenue from Other Federal Entities**
Department of the Army, General Funds	21	$0	$0	$0
Department of the Navy, General Funds	17			
Department of the Air Force, General Funds	57			
Department of the Army, WCF	97X4930.01			
Department of the Navy, WCF	97X4930.02		952,043	
Department of the Air Force, WCF	97X4930.03			
Defense Logistics Agency, WCF	97X4930.05xx			
Defense Finance and Accounting Service, WCF	97X4930.05xx			
Other Defense Organizations, General Funds	97-xxxx			
Other Defense Organizations, WCF	97X4930.04 97X4930.05xx			
Department of Defense Military Retirement Trust Fund	97-8097			
U.S. Army Corps of Engineers	96			
Total		$0	$952,043	$0

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Part B. Department of Defense Eliminations of Seller Activity Arrayed by Other Federal Agencies	Treasury Index	DoD Accounts Receivable Arrayed by Customer	DoD Revenue Arrayed by Customer	DoD Unearned Revenue by Customer
Executive Office of the President,DefenseSecurity Assistance Agency	11	$0	$417,064	$0
Department of Agriculture	12			
Department of Commerce	13		(224)	
Department of the Interior	14		(3,149)	
Department of Justice	15			
Department of Labor	16			
Department of State	19			
Department of the Treasury	20		204	
Office of Personnel Management	24			
Nuclear Regulatory Commission	31			
Department of Veterans Affairs	36			
General Service Administration	47		9,959	
National Science Foundation	49			
Federal Emergency Management Agency	58			
Environmental Protection Agency	68			
Department of Transportation	69		320,834	
Department for International Development	72			
Small Business Administration	73			
Department of Health and Human Services	75		1	
National Aeronautics and Space Administration	80		155,032	
Department of Housing and Urban Development	86			
Department of Energy	89		43	
Department of Education	91			
Social Security Administration	28			
Unidentifiable Federal Agency Entity	00		52,279	
Miscellaneous Identifiable Federal Agencies Not Required to Prepare CFO Audited Financial Statements	00			
Total		$0	$952,043	$0

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C. Other Information:

Note 22 eliminations are computed and schedules are prepared at three different levels. The purpose is to provide the information necessary to properly eliminate certain balances, depending on the consolidation level of the report. Level One represents sales from NWCF to Other Federal Entities (i.e., non-DoD). This data will be used to report at the U.S. Government-wide Consolidated Financial Statements level. Level One data is displayed above in the Note 22 table. Level Two and Level Three data are not displayed in Note 22, but the data is kept in separate schedules. Level Two represents sales by the NWCF to other entities within DoD. The schedule of Level Two data is used to prepare eliminating entries at the DoD Agency-wide Financial Statements level. Level Three represents (intra-agency) sales by one NWCF activity to another NWCF activity. The Level Three schedule data is used to compute the Intra-agency Eliminations column on the Consolidating NWCF statements. The results are reflected in the Consolidated NWCF CFO Financial Statements. DFAS-CL has been directed by DFAS to only recognize intra-agency eliminating entries on the FY 1998 Balance Sheet, Statement of Net Cost and Statement of Changes in Net Position. Intra-agency eliminating entries are, therefore, not recognized on the FY 1998 Statement of Budgetary Resources and Statement of Financing.

In the absence of standard USD(C) policy and procedures for intra-agency and inter-agency eliminating entries (formerly called intrafund eliminating entries), each DFAS Center was previously tasked by DFAS to evaluate the Center's capability to produce from existing systems the seller data for the numeric portion of this footnote. The data disclosed for the industrial type activities has been developed from field level revenue classification reports called the Summary Source of Revenue. The data disclosed for the supply type activities has been developed from a combination of three sources as follows: DD Form 1400(S) "Statement of Inter-Fund Transactions" which is a departmental report representing billings made via Interfund billings only, NAVCOMPT Form 148, Section A "Analysis of Reimbursable Issues and Receivables", extracts from DBMS, and the Central Data Base (CDB) trial balance. The Note 22 data for the DoD Accounts Receivable Arrayed by Customer and the DoD Unearned Revenue by Customer is not readily available in the financial systems supporting this Fund. Additionally, the supporting individual primary and secondary activity group Note 22 data is not readily available in the financial systems supporting this Fund. However, DON and DFAS are pursuing a systemic methodology for accumulating intra-agency and inter-agency data to provide the data needed for Note 22 and related Levels Two and Three schedules at each NWCF activity group level.

Until standard USD(C) policy for the treatment of intra-agency and inter-agency elimination transactions is issued and DFAS implementing procedures and controls are provided, the data disclosed may not meet the intent of the DoD Guidance on Form and Content of DoD Audited Financial Statements.

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Note 23. Other Disclosures:

A. Depot Maintenance - Aviation.

DFAS has unofficially stated that DIFMS will be updated during the Spring of FY 1999 to comply with the DFAS-CL 31 August 1998 guidance for revenue recognition. The COMNAVAIRSYSCOM letter 7045 Serial AIR-7641/080 of 2 November 1998, requested DFAS (Code IS) to advise when DIFMS would be updated to comply with the new policy. COMNAVAIRSYSCOM has not received the DFAS response.

B. Depot Maintenance - Other (Marine Corps).

The Marine Corps was not able to validate the FY 1997 Principal Statements due to inconsistent numbers reported for Accounts Payable, Other Liabilities and Net Operating Position between the financial statements and other fiscal year end reports, i.e., Year-end Closing Statement (SF 2108) and Report on Budget Execution (SF 133). The FY 1998 Principal Statements are in agreement with the AR 1307 report in these areas. We are not aware of any exceptions that would prevent the FY 1998 Principal Statements from being validated.

The Depot Maintenance - Other (Marine Corps) balance for Intragovernmental Accounts Payable was increased by undistributed disbursements of $16,085 thousand. Normally undistributed disbursements would reduce the Accounts Payable balance. Large undistributed balances appear to have resulted from a combination of factors (including erroneous charges/credits, failure to properly clear undistributed balances, and some system edit table/program logic errors) and is currently under review by Headquarters, Marine Corps and DFAS-Kansas City Center (DFAS-KC).

C. Base Support.

PWCs. At the Base Support consolidated level, effective 30 September 1998, the Base Support activity group now includes the PWCs and the NFESC. PBD No. 426, dated 30 December 1996 realigned NFESC from the Research and Development activity group to Base Support activity group. Invested Capital Used was adjusted by $7,007 thousand for the beginning balance of NFESC Capital Investments, Costs of Goods Sold and Services was adjusted $507 thousand for the beginning balance of NFESC Work-in-Process, and Capital Asset Program was adjusted to include NFESC Current Year Authority, Obligations and Outlays and to exclude NFESC Prior Year Obligations and Outlays. NFESC Prior Year amounts are reported with the Research and Development activity group for FY 1998. PWCs are in compliance with the DFAS-CL guidance of 31 August 1998 for revenue recognition.

NFESC. At the Base Support consolidated level, effective 30 September 1998, the Base Support activity group now includes the PWCs and the NFESC. PBD No. 426, dated 30 December 1996 realigned NFESC from the Research and Development activity group to Base

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Support activity group. Invested Capital Used was adjusted by $7,007 thousand for the beginning balance of NFESC Capital Investments, Costs of Goods Sold and Services was adjusted $507 thousand for the beginning balance of NFESC Work-in-Process, and Capital Asset Program was adjusted to include NFESC Current Year Authority, Obligations and Outlays and to exclude NFESC Prior Year Obligations and Outlays. NFESC Prior Year amounts are reported with the Research and Development activity group for FY 1998. NFESC complied with all existing DoD and DFAS guidance procedures. NFESC did convert to the Defense Working Capital Accounting System during FY 1998. All financial reports were generated out of DWAS and reported through the Financial Reporting System by DFAS-CL OPLOC Oakland. NFESC is in compliance with the DFAS-CL guidance of 31 August 1998 for revenue recognition.

D. Information Services.

NAVCOMTELCOM. Cost overruns were not a major problem during FY 1998. NAVCOMTELCOM has directed subordinate activities to effect timely re-negotiation before cost of performance has exceeded 75 percent of the funded amount for cost reimbursable orders. When renegotiations failed and funding is exhausted, services have been terminated. The customer and its management command were notified in writing of the planned work stoppage.

COMNAVRESFOR. Effective with FY1998 financial statement reporting, the COMNAVRESFOR secondary activity group, formerly included under the NAVCOMTELCOM activity group, has had one full year of reporting. In February of FY 1997, financial control of operations was transferred to COMNAVRESFOR. Some prior year errors have impacted FY 1998 balances and have been addressed in this report.

E. Research and Development.

NSWC. The AOR - Deferred account (Navy Account 2980) includes a negative ($4,569) thousand for previously unrecorded depreciation expense due to the closing of the Louisville Detachment on NSWC Crane’s financial statements. The NAVAUDSVC requested the ASN(FM&C) to report the depreciation of assets at closing activities that had not been previously reported on the DON NWCF Consolidating Financial Statements. The policy adopted by DON and approved by the USD(C), was that the residual value of assets purchased but not fully depreciated and recouped through depreciation charges in customer rates after the mission cease date be written off as non-recoverable for rate purposes.

NAWC. The Accounts Payable Account includes $15,216 thousand accrued expense for the remainder of outstanding cash for the El Nino Storm Damage Transfer to NAWC Weapons Division. The transfer of funds was to be Net Operating Results neutral and it would have been if the total costs had been expensed during FY 1998. However, only $3,196 thousand has been expended in FY 1998. Therefore, the remainder of the costs were accrued in FY 1998 so that it would not affect the FY 2000 rates.

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NAWC recognizes revenue on an actual cost basis and bills monthly as costs are incurred. NAWC performs work on a cost reimbursable basis. Therefore, the manner in which NAWC recognizes revenue is in accordance with DoD guidance. The NAWC secondary activity group current supporting systems is the Navy Industrial Fund Financial Management and Accounting System. The NAWC secondary activity group is scheduled to convert to DIFMS in FY 2000. If the NAWC had a fixed price order it would process properly in DIFMS.

NRL. The Balance Sheet Line 1.A.1. (Fund Balance with Treasury) and Line 4.A.1 (Accounts Payable) has been reduced by Unallocated Cost – NWCF Summary Registers. These unallocated costs include $6,257 thousand of net disbursements that have not been distributed in detail registers to the NRL through the Industrial Fund Centralized Disbursement Reimbursement System. These net disbursements were recorded only in summary registers at the appropriation/ subhead level and have not been identified by detail register, amount, or document to validate that they are NRL transactions.

SSCs. This is the first CFO statement for the SSC's. The NCCOSC was disestablished 1 October 1997 in accordance with BRAC 1995. The two operating divisions were renamed as the SSC San Diego and SSC Charleston, respectively and report directly to the COMSPAWARSYS-COM. The two activities continued to operate under a single NWCF subhead for the first quarter of fiscal year 1998. Both activities converted to the DIFMS concurrently, at which time one new subhead was added. SSC San Diego has continued to use the existing NH3P subhead, and SSC Charleston started reporting under a new NH3S subhead with the start of the second quarter. Effective January 1998, DIFMS became the official financial accounting system for the SSC's. The conversion to this system has been a difficult transition generated by catch-up processing being months behind schedule due to system deficiencies. While progress is being made, significant deficiencies or problems still exist as of 30 September 1998. Some of the major areas of concern include:

Costs are misstated due to the way DIFMS processes cash transactions.

Payments are being processed for greater than the Accounts Payable.

DIFMS applies production and general overhead to post allowance and living quarters entitlements.

Out of balance conditions between the general and subsidiary ledgers.

DIFMS calculates and reports at the customer order level vice the Accounting Classification Reference Number level as required, thus overstating unbillable Work-in-Process.

Aging of reports and break out of specified accounts (e.g., undelivered orders, acceleration) as required for specific financial statement quarterly reports is not available.

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Data by sponsor or appropriation for reporting purposes is not available.

Foreign Military Sales information is not provided as required by CFO Note 1.F.5.

Query Language Programs (QLP's) have been prepared for all problems encountered, to date, however, only a little over three hundred of the QLP's have been processed. Much manual intervention is required by the SSC's and OPLOC San Diego to make this system work. Therefore, the amounts reported in this statement have been validated to the official accounting records, but the official accounting records have not been reconciled to the appropriate general and subsidiary ledgers. Until the numerous reconciliation problems can be resolved, the SSC's will not be able to issue a 'clean' financial statement.

During FY 1996, the COMSPAWARSYSCOM Inspector General investigated (at NISE East's request) financial management practices believed to be irregular. While the majority of the findings were corrected in Fiscal Years 1996 and 1997, one remaining piece amounting to $782 thousand remained unresolved at the end of fiscal year 1997. This part was associated with the Capital Purchases Program and required reprogramming of funds and ASN (FM&C) approval. Approval was received from ASN (FM&C) on 23 July 1998. All corrective action required as a result of the FY 1996 SPAWAR IG has been corrected.

At the present time there are some known legal claims that could result in a significant financial impact on the SSC's financial position. One contract is under appeal with the ASBCA which may result in a $573 thousand payment; and the other one is a long standing claim before the SSC San Diego, CA Contracting Officer in the amount of $258 thousand. Therefore, claims in the amount of $831 thousand for two direct funded contracts have been accrued by the SSC's. The accrued expenses are included in Accounts Payable on the Balance Sheet.

F. Supply Management (Navy).

Year-end Financial Processing. NWCF activities are required to include all transactions through 30 September of the reporting fiscal year in their financial reports to higher levels. Current reporting due dates require activities to close their "books" prior to 30 September in order to be included in year-end reports. Delays resulting from Automated Data Processing scheduling and processing constraints will be encountered and result in some transactions being excluded from year-end reports. Also, financial processing will preclude some measure of transactions from processing to accounting records. These transactions are output to exception files and are reviewed, reconciled, and reprocessed to accounting records. Financial reporting deadlines provide insufficient time to affect corrections and, thus, corrections are processed and reported in subsequent reporting periods. Therefore, financial information presented in the financial statements of this activity group is not as of 30 September 1998. This is not considered material when viewing and drawing conclusions from these financial statements.

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The necessary adjustment to the Accounts Payable, Federal Account of $207 thousand (reduction) based on NAVAUDSVC draft audit report 98-0099, Recommendation 42, was made in FY 1998. This action is complete. The necessary adjustment to the Accounts Payable, Non-Federal Account of $134,423 thousand (reduction) based on NAVAUDSVC draft audit report 98-0099, Recommendation 59, was made in FY 1998. This action is complete.

The value reflected in the Statement of Net Cost, Line 1.A.4, Program Costs - Earned Revenues is increased by $136,876 thousand due to the inclusion of a Property Clearance Account. The inclusion of the Property Clearance Account is at the direction of DFAS and USD(C). The inclusion of this account in a revenue calculation is questionable since it represents timing differences between the receipt of material in the inventory accounting system and the related Accounts Payable posting for material receipt. Until the inventory accounting system and the allotment accounting system are integrated in a single system these timing differences will continue. The CFO Statement of Net Cost, Line 1.A.4, Program Costs - Earned Revenues, does not equal the AR(M)1307 Statement of Operations, Part I, Line 2. The difference is a result of the treatment of the Standard General Ledger (SGL) Account 1520C, Property Clearing Account, in the amount of $136,876 thousand. This amount is presented on Line 3, Other Revenue & Financing Sources, on the AR(M)1307 Statement of Operations. Additionally, the CFO Statement of Net Cost, Line 1.A.4, Program Costs - Earned Revenues, does not equal the SF 133, Lines 3.A.1 + 3.A.2, nor does it equal the DD 725, Column E Total. The difference is a result of the treatment of $136,876 thousand from SGL Account 1520C, Property Clearing Account; $464,827 thousand from SGL Account 1529.1E, Issues with Reimbursements-Returns; and ($4.2 thousand) from SGL 1529.1C, Recoveries for Retail Stock Losses. The $136,876 thousand is included on Line 1.A.4 of the CFO Statement of Net Cost, per guidance from DFAS. The $464,827 thousand plus ($4.2 thousand) are treated as inventory allowance accounts on the CFO Statement of Net Cost and as a revenue account on the SF 133. The difference in the treatment of these accounts is in accordance with instruction received from DFAS.

The CFO Statement of Changes in Net Position, Lines 2.E Financing Sources (Other than Exchange Revenues), Transfers In + 2.F Financing Sources (Other than Exchange Revenues), Transfers Out does not equal AR(M)1307 Statement of Financial Position, Lines 15.b.3 + 15.b.4 + 15.b.5. The difference of ($266,467 thousand) is due to the treatment of SGL Account 32114, Net Fund Balance with Treasury. This account is presented on Line 15.b.3, Fund (Cash) Transfers, of the AR(M)1307. On the CFO Statement of Changes in Net Position, this account is included as part of Line 6, Increase (Decrease) in Unexpended Appropriations.

The CFO Statement of Changes in Net Position, Line 4, Prior Period Adjustments, does not equal AR(M)1307, Part II, Line 1.2, due to differences in the beginning AOR amounts used in the COGS model. The final FY 1997 AR(M)1307 ending AOR was not based on the COGS model calculations, whereas the FY 1997 CFO ending AOR was based on the COGS model calculations.

As a result of the implementation of the USD(C) Inventory Valuation and COGS model, prior year values in Equity, Inventory, and Inventory Allowance have been impacted. With the

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implementation of the USD(C)/DFAS Inventory Valuation and COGS model for the reporting period of October 1997, one of the changes that has taken place is the use of the monthly change in SGL Account 1520C, Property Clearing Account, as inventory gains. These gains represent timing differences between he receipt of material in the inventory accounting system and the related Accounts Payable posting for material receipt. Until the inventory accounting system and the allotment accounting system are integrated in a single system these timing differences will continue. The inventory gains associated with the Property Clearing Account for FY 1998 was an increase of $136,876 thousand and is included in the Statement of Net Cost, Line 1.A.4, Program Costs - Less Earned Revenues, as directed by DFAS and USD(C). The changes associated with the USD(C) Inventory Valuation and COGS model will remain pending further guidance from USD(C) and DFAS.

The CFO Balance Sheet, Line 1.A.3, Entity Assets (Intragovernmental), Accounts Receivable, reflects a decrease of $527,489 thousand. An adjustment was made to correct a discrepancy between activity level collections and Treasury level collections which dates back to 1993. In FY 1993, a NAVCOMPT Form 621 was prepared to correct collections. However, the transaction was prepared in CERPS incorrectly. After a complete analysis, an adjustment was made to correct the problem which resulted in an increase in undistributed collections and a decrease in Accounts Receivable.

The CFO Balance Sheet, Line 4.A.4, Liabilities Covered by Budgetary Resources (Intragovernmental), Other Liabilities was affected by the accounting correction necessary in order to assimilate the MFCS Special Accounting Class 207 conversions and the correction of a $7,677,311 thousand imbalance between the Field Activity and Suballotment level of accounting. The $7,677,311 thousand difference was due to a journal voucher from FY 1994 meant to correct deficiencies between PX06 and the CDB. This led to an imbalance between the Field Activity and Suballotment levels of reporting. The Field Activity and Suballotment level balance discrepancies were corrected in the September 1998 reporting period. The correction included reversing the journal voucher made in 1994 and correcting UICs N00383, N00104, and N69117 in the CDB to balance with the correct total reported in PX06. In an effort to render a more factual Financial Position of the Supply Management (Navy) activity group, an accounting reclassification journal voucher was prepared and applied between Other Liabilities and Inventory Items for the net amount of $4,571,248 thousand. This accounting reclassification removes the abnormal balance condition in Other Liabilities and corrects a material inventory reduction caused by the MFCS conversion in process. The accounting reclassification also brings the Supply Management (Navy) activity group into compliance with NAVAUDSVC draft audit report 98-0099, Recommendation 58. Recommendation 58, recommended that the periodic net change of the Other Liabilities was also affected by the accounting correction applied to SGL Account 2920, Ships Stores Profits Transferable, and SGL Account 2311, Unearned Revenue-Advances from Government Agencies. SGL Account 2920 was the basis of Finding 14 (Recommendation 55) in NAVAUDSVC draft audit report 98-0099. Discussions between COMNAVSUPSYSCOM, DFAS-CL, and NAVAUDSVC determined that the SLG Account 29201 balance was invalid. A journal voucher was applied to remove the $7,049 thousand balance. NAVAUDSVC draft audit

NWCF CONSOLIDATED NOTES

report 98-0099, Finding 15 (Recommendation 57) identified there were no changes in the reported deposits from the Cooperative Logistic Supply Support Agreement (CLSSA) FMS reported cases since December 1994. As a result of research by DFAS-CL and the Navy International Program Office (formerly the Navy International Logistics Control Office) the SGL Account 2311 was decreased by $4,351thousand. The CLSSA FMS balances are now current.

G. Supply Management (Marine Corps).

The Marine Corps has resolved its systemic inventory problems by changing its business practice and policy on stock funding repairables as of 1 October 1997. However, the Marine Corps continues to experience problems in Accounts Payable and Undelivered Order abnormal balances and accounting for these funds in the new Standard Accounting Budgeting and Reporting Systems 2 (SABRS2).

The balance for Supply Management (Marine Corps) Accounts Payable decreased by $4,172 thousand during FY 1998 from FY 1997. The primary reason is due to problems with the accounts payable function. The deviation is due to the General Ledger Account (GLA) 2113 "Accounts Payable Commercial" abnormal balance. More commercial payments are being made than commercial receipts received. DFAS made an unanticipated adjustment to write-off all unmatched payments to reflect true undistributed disbursements during November through December 1997 and the adjustment was made after the FY 1998 Accounts Payable phasing plans were prepared (during August through September 1997 time frame).

An accounting adjustment of $37,977 thousand was made to Accounts Payable. The methodology to determine Accounts Payable Public (Commercial) is to compare CERPS payments register with commercial inventory receipts. This methodology has resulted in negative Accounts Payable (Public) due to selected registered payments exceeding inventory receipts. The Marine Corps is investigating to determine if this methodology is valid to determine the split between public and government Accounts Payable. Overall government Accounts Payable is not negative.

The undistributed disbursements are also causing the Undelivered Orders to be in an abnormal balance. The undistributed disbursement account reflects disbursements that have processed through the CERPS against subhead NC2A that have not been identified to a specific account holder. It is possible that some of the disbursements were erroneously processed under subhead NC2A. This account is worked on a regular basis to identify where the disbursement should post and corrective action initiated. DFAS has primary responsibility for working the undistributed disbursements and to correct this abnormal balance.

The Integrated Processing Team that was established in March 1997 continues to meet to discuss and resolve any inventory or financial problems that occur.

NWCF CONSOLIDATED NOTES

H. Navy Component.

The NAVAUDSVC audit report 049-98 reported that the FY 1997 NWCF CFO Consolidated Financial Statement overstated Non-Entity Assets by $393.5 million because the IMRL equipment was improperly reported as NWCF assets even though they did not meet the criteria for inclusion in accordance with DoD FMR. According to the audit report the IMRL equipment are not controlled by the NWCF activities. NAVAUDSVC Recommendation 41, recommended that ASN(FM&C) direct that the financial statements that report COMNAVAIRSYSCOM transactions include the IMRL equipment rather than the NWCF. Notwithstanding, the ASN(FM&C) 7 July 1998 response to the audit report, DON has decided to take immediate action to comply with NAVAUDSVC Recommendation 41. Therefore, the gross value of IMRL equipment will no longer be reported as Non-Entity Assets in the NWCF CFO Consolidated Financial Statement. In FY 1998 the IMRL equipment assets will be reported in the FY 1998 DON General Funds (Index 17) CFO Financial Statements as Supplementary Stewardship Information when appropriate. COMNAVAIRSYSCOM has made the determination that the IMRL equipment assets meet the definition of National Defense PP&E assets. The FY 1998 IMRL equipment gross value is $370,554 thousand. The Net Book Value of the IMRL equipment is $245,133 thousand as disclosed in Note 9 above. The Net Book Value of IMRL equipment is not included in the numeric portion of Note 9, but is provided for full disclosure of sponsor funded equipment.

I. Abnormal Balances Not Disclosed Elsewhere in the Footnotes.

A few NWCF activity groups are reflecting a negative balance in Navy Account 2110 Accounts Payable. These negative Accounts Payable balances are the result of procedures which close Navy Account 1545 Undistributed Disbursements - Unmatched to the Navy Account 2110 Accounts Payable. A negative Accounts Payable balance results when the Navy Account 1545 Undistributed Disbursements - Unmatched balance is greater then the Navy Account 2110 Accounts Payable balances which creates an abnormal balance. The Navy Account 1545 Undistributed Disbursements - Unmatched must be researched in order for it to be applied to the correct account within the Liabilities section of the statement and preclude an abnormal balance. The overall NWCF Navy Account 2110 Accounts Payable is not abnormal.

J. Undistributed Collections and Undistributed Disbursements.

The departmental level Undistributed Collections and Undistributed Disbursements are captured in DoD SGL Accounts 1014 and 1015, respectively. The DoD FMR requires that these accounts be reported as adjustments to the reported Accounts Receivable and Accounts Payable values.

The methodology for recording the Undistributed Collections and Undistributed Disbursements is different for the supply type activity groups than for the industrial type activities groups as discussed below. This inconsistent treatment between activity groups was cited by the NAVAUDSVC in draft audit report 98-0099 Finding 12, Recommendation 47.

NWCF CONSOLIDATED NOTES

In the Supply Management (Navy) activity group, Accounts Receivable and Accounts Payable were adjusted for Undistributed Collections and Undistributed Disbursements, respectively, based on percentages computed from current relationships among the four accounts. The total values of Accounts Payable and Accounts Receivable were not changed.

For the Navy industrial type activity groups and the Navy Component SGL Accounts 1014 and 1015 have been netted against each other and displayed on the Balance Sheet, Line 4.A.4, Liabilities Covered by Budgetary Resources (Intragovernmental) Other Liabilities and Note 11, Other Liabilities Covered by Budgetary Resources (Intragovernmental) Other Liabilities. The net value of Undistributed Collections and Disbursements (Navy Account 1156) is $1,867,485 thousand. This display follows the practice established in FY 1997 per guidance from DFAS dated 2 December 1997.

NWCF CONSOLIDATED NOTES

K. Unmatched Disbursements, Negative Unliquidated Obligations, and Aged In-Transit Disbursements.

(in thousands)

Treasury Index Appropriation 4930	September 1998	September 1997	Change	Percent Change
Unmatched Disbursements	$468,418	$289,887	$178,531	61.5%
Negative Unliquidated Obligations	Not Applicable	Not Applicable	-	-
Aged In-Transit Disbursements	$447,102	$928,225	($481,123)	(51.8%)
Totals	$915,520	$1,218,112	($302,592)	(24.8%)

<u>Note 24. Net Position Disclosure:</u>

The following footnote while not required by DoD is provided in accordance with the DoD Guidance on Form and Content of Audited Financial Statements to provide supplemental disclosure.

(in thousands)

	Revolving Funds	Trust Funds	Appropriated Funds	Total
	(1)	(2)	(3)	(1)+(2)+(3)
A. Unexpended Appropriations	$0	$0	$0	$0
B. Invested Capital	22,597,624			22,597,624
C. Cumulative Results of Operations:				
a. Operating	(6,007,381)			(6,007,381)
b. Deferred	(394,102)			(394,102)
D. Total	$16,196,141	$0	$0	$16,196,141

E. Other Information:

1. The CRO includes a negative ($394,102) thousand recorded as CRO - Deferred. This is a categorization of CRO which requires the approval of USD(C) prior to recording and represents an exclusion of the recorded amounts from customer rate setting. The following table displays the deferred amounts by activity group:

NWCF CONSOLIDATED NOTES

Activity Group	(in thousands) Deferred Amounts	Reason for Deferral
Depot Maintenance – Shipyards	($70,112)	JLSC
Depot Maintenance – Aviation	(58,102)	JLSC
Depot Maintenance – Other (Marine Corps)	(7,562)	JLSC
Ordnance	(9,120)	JLSC
Research and Development NSWC	(813)	JLSC
Supply Management (Navy)	(243,824)	JLSC
Subtotal	(389,533)	
Research and Development NSWC	(4,569)	Depreciation
Total	($394,102)	

Of the total negative ($389,533) thousand results from the closure of the JLSC. This was directed by USD(C) memorandum of 19 August 1998, which also provided the allocation of system development costs incurred by JLSC to the appropriate DWCF activity groups. As instructed by the USD(C) memorandum, the Navy distributed the transferred amounts among the affected NWCF activities. This distribution of the transferred amounts was provided to DFAS, who made the accounting entries based on the USD(C) memo. These system development costs were incurred from FY 1992 through 30 September 1998.

The remaining negative ($4,569) thousand represents the amount of discontinued depreciation expense at closing activities not previously reported in the financial statements. This recording of discontinued depreciation costs is the result of Recommendation 4 of NAVAUDSVC audit report 040-97.

2. The following provides other disclosures by activity group.

Depot Maintenance - Other (Marine Corps). This activity group's CRO of $43,159 thousand is being reviewed by DFAS-KC to determine the variances from the GLA balance of $44,737 thousand.

Ordnance. A transfer of $6,400 thousand was made to Naval Weapons Station (NWS) Yorktown from PWC Jacksonville, FL in the amount of $4,100 thousand and from PWC Detachment, Philadelphia, PA in the amount of $2,300 thousand to augment the NWS AOR. This equity transfer was in accordance with PBD 407 of 11 December 1996 and authorized by USD(C) on 17 September 1997. These AOR transfers were processed through the CERPS in August 1998.

NWCF CONSOLIDATED NOTES

Transportation. This activity group's CRO is a negative ($276,753) thousand balance because prior to FY 1997 activity cash was closed into Net Treasury Balance.

Information Services.

NAVCOMTELCOM. This activity group's CRO is a negative ($79,141) thousand. The largest Navy Account impacting the CRO is a negative ($93,747) thousand in Navy Account 2961, Net Treasury Balance – NWCF.

FMSO. FMSO was a new secondary activity group in FY 1997. In order to bring the activity group in line with the other industrial fund activities, it was necessary to zero out prior-to FY 1997 cash. Because Navy Account 1156 Undistributed Cash Disbursements, was a significant number, the result was an abnormal Net Position which continues in the current statements with an abnormal negative ($29,031) thousand CRO balance.

COMNAVRESFOR. The negative ($2,866) thousand CRO resulted from an adjustment of negative ($7,270) thousand made to Invested Capital by DFAS-CL OPLOC Pensacola. In separating the financial statements and making the necessary financial transfers in FY 1997, COMNAVRESFOR was set up as a separate activity group and offsetting adjustments were also made to NAVCOMTELCOM activity group. The CRO represents AOR recovery impacted by budgetary decisions made at the time of transfer and recovery of cash surcharge.

Supply Management (Navy). The $3,656,503 thousand value reflected in the Statement of Changes in Net Position, Line 2E (Transfers-In) is influenced by $14,985 thousand of Transfers-In-Without Reimbursement resulting from Fleet and Industrial Supply Center/Naval Shipyard material transfer partnerships that occurred in FY 1998.

DEPARTMENT OF THE NAVY

NAVY WORKING CAPITAL FUND

REQUIRED SUPPLEMENTARY INFORMATION

Department of Defense
Navy Working Capital Fund
DISAGGREGATED STATEMENT OF BUDGETARY RESOURCES, COMBINING
For the period ending September 30, 1998
(in thousands)

	FY 1998	DM-Shipyards	DM-Aviation
BUDGETARY RESOURCES:			
1. Budget Authority	$5,232	$0	$0
2. Unobligated Balance - Beginning of Period	1,988,427	(502,863)	526,728
3. Net Transfers Prior-Year Balance, Actual (+/-)	62,992	(34,159)	(29,428)
4. Spending Authority from Offsetting Collections	21,356,962	2,850,664	1,519,419
5. Adjustments	(308,926)	(16,148)	(7,626)
6. Total Budgetary Resources	$23,104,687	$2,297,494	$2,009,093
STATUS OF BUDGETARY RESOURCES:			
7. Obligations Incurred	20,472,046	2,429,990	1,734,190
8. Unobligated Balances - Available	2,632,641	(132,496)	274,903
9. Unobligated Balances - Not Available	0	0	0
10. Total, Status of Budgetary Resources	$23,104,687	$2,297,494	$2,009,093
OUTLAYS:			
11. Obligations Incurred	20,472,046	2,429,990	1,734,190
12. Less: Spending Authority From Offsetting Collections and Adjustments	(21,356,962)	(2,850,664)	(1,519,419)
13. Obligated Balance, Net - Beginning of Period	3,004,070	1,142,628	684,795
14. Obligated Balance Transferred, Net	1,501	0	0
15. Less: Obligated Balance, Net - End of Period	(2,502,140)	(839,517)	(801,459)
16. Total Outlays	($381,485)	($117,563)	$98,107

Additonal information included in Note 19.

The accompanying notes are an integral part of these statements.

Department of Defense
Navy Working Capital Fund
DISAGGREGATED STATEMENT OF BUDGETARY RESOURCES, COMBINING
For the period ending September 30, 1998
(in thousands)

	DM-Other (MC)	Ordnance	Transportation
BUDGETARY RESOURCES:			
1. Budget Authority	$0	$0	$0
2. Unobligated Balance - Beginning of Period	32,633	(13,598)	1,002,980
3. Net Transfers Prior-Year Balance, Actual (+/-)	(1,500)	195	(69,316)
4. Spending Authority from Offsetting Collections	164,796	612,766	1,100,150
5. Adjustments	(4,109)	(5,807)	(1,322)
6. Total Budgetary Resources	$191,820	$593,556	$2,032,492
STATUS OF BUDGETARY RESOURCES:			
7. Obligations Incurred	173,247	388,688	1,255,417
8. Unobligated Balances - Available	18,573	204,868	777,075
9. Unobligated Balances - Not Available	0	0	0
10. Total, Status of Budgetary Resources	$191,820	$593,556	$2,032,492
OUTLAYS:			
11. Obligations Incurred	173,247	388,688	1,255,417
12. Less: Spending Authority From Offsetting Collections and Adjustments	(164,796)	(612,766)	(1,100,150)
13. Obligated Balance, Net - Beginning of Period	(17,118)	14,870	(793,988)
14. Obligated Balance Transferred, Net	0	0	0
15. Less: Obligated Balance, Net - End of Period	(11,668)	(46,395)	283,335
16. Total Outlays	($20,335)	($255,603)	($355,386)

Additonal information included in Note 19.

The accompanying notes are an integral part of these statements.

Department of Defense
Navy Working Capital Fund
DISAGGREGATED STATEMENT OF BUDGETARY RESOURCES, COMBINING
For the period ending September 30, 1998
(in thousands)

	Base Support	Information Services	Research & Development
BUDGETARY RESOURCES:			
1. Budget Authority	$4,966	$266	$0
2. Unobligated Balance - Beginning of Period	164,520	104,485	(367,266)
3. Net Transfers Prior-Year Balance, Actual (+/-)	23,017	0	18,562
4. Spending Authority from Offsetting Collections	1,886,105	227,740	7,031,866
5. Adjustments	0	0	(12,907)
6. Total Budgetary Resources	$2,078,608	$332,491	$6,670,255
STATUS OF BUDGETARY RESOURCES:			
7. Obligations Incurred	1,739,130	245,358	6,621,705
8. Unobligated Balances - Available	339,478	87,133	48,550
9. Unobligated Balances - Not Available	0	0	0
10. Total, Status of Budgetary Resources	$2,078,608	$332,491	$6,670,255
OUTLAYS:			
11. Obligations Incurred	1,739,130	245,358	6,621,705
12. Less: Spending Authority From Offsetting Collections and Adjustments	(1,886,105)	(227,740)	(7,031,866)
13. Obligated Balance, Net - Beginning of Period	(21,763)	(12,923)	1,308,044
14. Obligated Balance Transferred, Net	0	0	0
15. Less: Obligated Balance, Net - End of Period	179,190	(12,384)	(661,901)
16. Total Outlays	$10,452	($7,689)	$235,982

Additonal information included in Note 19.

The accompanying notes are an integral part of these statements.

Department of Defense
Navy Working Capital Fund
DISAGGRGATED STATEMENT OF BUDGETARY RESOURCES, COMBINING
For the period ending September 30, 1998
(in thousands)

	Supply Management	Component
BUDGETARY RESOURCES:		
1. Budget Authority	$0	$0
2. Unobligated Balance - Beginning of Period	39,683	1,001,125
3. Net Transfers Prior-Year Balance, Actual (+/-)	156,587	(966)
4. Spending Authority from Offsetting Collections	5,963,456	0
5. Adjustments	(246,342)	(14,665)
6. Total Budgetary Resources	$5,913,384	$985,494
STATUS OF BUDGETARY RESOURCES:		
7. Obligations Incurred	5,884,321	0
8. Unobligated Balances - Available	29,063	985,494
9. Unobligated Balances - Not Available	0	0
10. Total, Status of Budgetary Resources	$5,913,384	$985,494
OUTLAYS:		
11. Obligations Incurred	5,884,321	0
12. Less: Spending Authority From Offsetting Collections and Adjustments	(5,963,456)	0
13. Obligated Balance, Net - Beginning of Period	1,844,396	(1,144,871)
14. Obligated Balance Transferred, Net	0	1,501
15. Less: Obligated Balance, Net - End of Period	(2,314,806)	1,723,465
16. Total Outlays	($549,545)	$580,095

Additonal information included in Note 19.

The accompanying notes are an integral part of these statements.

DEPARTMENT OF THE NAVY

NAVY WORKING CAPITAL FUND

OTHER ACCOMPANYING INFORMATION

Department of Defense
Navy Working Capital Fund
CONSOLIDATING BALANCE SHEET
As of September 30, 1998
(in thousands)

	FY 1998	DM-Shipyards	DM-Aviation	DM-Other (MC)
ASSETS				
1. Entity Assets:				
A. Intragovernmental				
1. Fund Balance With Treasury (Note 2)	$1,192,502	$176,404	($178,757)	($17,411)
2. Investments, Net (Note 4)	0	0	0	0
3. Accounts Receivable, Net (Note 5)	626,261	(33,134)	52,972	6,366
4. Other Assets (Note 6)	276,590	150,918	2,532	0
B. Total Intragovernmental	$2,095,353	$294,188	($123,253)	($11,045)
C. Investments, Net (Note 4)	0	0	0	0
D. Accounts Receivable, Net (Note 5)	270,706	159	(403)	0
E. Loans Receivable and Related Foreclosed Property, Net (Note 7)	0	0	0	0
F. Cash and Other Monetary Assets (Note 3)	0	0	0	0
G. Inventory and Related Property, Net (Note 8)	16,424,928	448,408	865,727	38,545
H. General Property, Plant and Equipment (Note 9)	4,393,806	941,780	315,143	61,553
I. Stewardship Assets (National Defense PP&E, etc.)	N/A	N/A	N/A	N/A
J. Other Assets (Note 6)	1,326,489	21,980	9,595	26
K. Total Entity Assets	$24,511,282	$1,706,515	$1,066,809	$89,079
2. Non-Entity Assets:				
A. Intragovernmental				
1. Fund Balance With Treasury (Note 2)	0	0	0	0
2. Accounts Receivable, Net (Note 5)	0	0	0	0
3. Other Assets (Note 6)	0	0	0	0
B. Total Intragovernmental	$0	$0	$0	$0
C. Accounts Receivable, Net (Note 5)	0	0	0	0
D. Cash and Other Monetary Assets (Note 3)	0	0	0	0
E. Other Assets (Note 6)	0	0	0	0
F. Total Non-Entity Assets	0	$0	$0	$0
3. Total Assets	$24,511,282	$1,706,515	$1,066,809	$89,079

The accompanying notes are an integral part of these statements.

Department of Defense
Navy Working Capital Fund
CONSOLIDATING BALANCE SHEET
As of September 30, 1998
(in thousands)

	Ordnance	Transportation	Base Support	Information Services
ASSETS				
1. Entity Assets:				
A. Intragovernmental				
1. Fund Balance With Treasury (Note 2)	$182,719	$162,822	$19,737	($10,864)
2. Investments, Net (Note 4)	0	0	0	0
3. Accounts Receivable, Net (Note 5)	47,964	(13,460)	211,063	38,107
4. Other Assets (Note 6)	267	415	2,552	1,695
B. Total Intragovernmental	$230,950	$149,777	$233,352	$28,938
C. Investments, Net (Note 4)	0	0	0	0
D. Accounts Receivable, Net (Note 5)	950	570	46,505	(205)
E. Loans Receivable and Related Foreclosed Property, Net (Note 7)	0	0	0	0
F. Cash and Other Monetary Assets (Note 3)	0	0	0	0
G. Inventory and Related Property, Net (Note 8)	7,332	34,698	62,904	2,597
H. General Property, Plant and Equipment (Note 9)	173,132	9,478	687,290	2,975
I. Stewardship Assets (National Defense PP&E, etc.)	N/A	N/A	N/A	N/A
J. Other Assets (Note 6)	448	1,095,400	1,398	161
K. Total Entity Assets	$412,812	$1,289,923	$1,031,449	$34,466
2. Non-Entity Assets:				
A. Intragovernmental				
1. Fund Balance With Treasury (Note 2)	0	0	0	0
2. Accounts Receivable, Net (Note 5)	0	0	0	0
3. Other Assets (Note 6)	0	0	0	0
B. Total Intragovernmental	$0	$0	$0	$0
C. Accounts Receivable, Net (Note 5)	0	0	0	0
D. Cash and Other Monetary Assets (Note 3)	0	0	0	0
E. Other Assets (Note 6)	0	0	0	0
F. Total Non-Entity Assets	$0	$0	$0	$0
3. Total Assets	$412,812	$1,289,923	$1,031,449	$34,466

The accompanying notes are an integral part of these statements.

Department of Defense
Navy Working Capital Fund
CONSOLIDATING BALANCE SHEET
As of September 30, 1998
(in thousands)

	Research & Development	Supply Management	Component	Eliminations
ASSETS				
1. Entity Assets:				
A. Intragovernmental				
1. Fund Balance With Treasury (Note 2)	($843,441)	$156,295	$1,544,998	$0
2. Investments, Net (Note 4)	0	0	0	0
3. Accounts Receivable, Net (Note 5)	195,238	121,145	0	0
4. Other Assets (Note 6)	18,880	99,331	0	0
B. Total Intragovernmental	($629,323)	$376,771	$1,544,998	$0
C. Investments, Net (Note 4)	0	0	0	0
D. Accounts Receivable, Net (Note 5)	9,054	214,076	0	0
E. Loans Receivable and Related Foreclosed Property, Net (Note 7)	0	0	0	0
F. Cash and Other Monetary Assets (Note 3)	0	0	0	0
G. Inventory and Related Property, Net (Note 8)	305,927	14,658,790	0	0
H. General Property, Plant and Equipment (Note 9)	1,911,255	291,200	0	0
I. Stewardship Assets (National Defense PP&E, etc.)	N/A	N/A	N/A	N/A
J. Other Assets (Note 6)	27,768	169,713	0	0
K. Total Entity Assets	$1,624,681	$15,710,550	$1,544,998	$0
2. Non-Entity Assets:				
A. Intragovernmental				
1. Fund Balance With Treasury (Note 2)	0	0	0	0
2. Accounts Receivable, Net (Note 5)	0	0	0	0
3. Other Assets (Note 6)	0	0	0	0
B. Total Intragovernmental	$0	$0	$0	$0
C. Accounts Receivable, Net (Note 5)	0	0	0	0
D. Cash and Other Monetary Assets (Note 3)	0	0	0	0
E. Other Assets (Note 6)	0	0	0	0
F. Total Non-Entity Assets	$0	$0	$0	$0
3. Total Assets	$1,624,681	$15,710,550	$1,544,998	$0

The accompanying notes are an integral part of these statements.

Department of Defense
Navy Working Capital Fund
CONSOLIDATING BALANCE SHEET
As of September 30, 1998
(in thousands)

	FY 1998	DM-Shipyards	DM-Aviation	DM-Other (MC)
LIABILITIES				
4. Liabilities Covered by Budgetary Resources:				
A. Intragovernmental :				
1. Accounts Payable	$735,881	$84,651	$250,079	$30,748
2. Environmental Cleanup (Note 11)	0	0	0	0
3. Debt (Note 10)	1,094,710	0	0	0
4. Other Liabilities (Notes 11 ,12,and 15)	1,367,352	185,150	562,908	2,610
B. Total Intragovernmental	$3,197,943	$269,801	$812,987	$33,358
C. Accounts Payable	3,067,174	247,155	199,070	6,066
D. Liabilities for Loan Guarantees	0	0	0	0
E. Military Retirement Benefits and Other Employment Related Actuarial Liabilities (Note 13)	0	0	0	0
F. Environmental Cleanup (Note 11)	0	0	0	0
G. Other Liabilities (Notes 11 , 12,and 15)	873,550	196,772	77,074	6,496
H. Total Liabilities Covered by Budgetary Resources	$7,138,667	$713,728	$1,089,131	$45,920
5. Liabilities Not Covered by Budgetary Resources:				
A. Intragovernmental:				
1. Accounts Payable	0	0	0	0
2. Debt (Note 10)	0	0	0	0
3. Environmental Cleanup (Note 11)	0	0	0	0
4. Other Liabilities (Notes 11 ,12,and 15)	0	0	0	0
B. Total Intragovernmental	$0	$0	$0	$0
C. Accounts Payable	0	0	0	0
D. Debt (Note 10)	0	0	0	0
E. Military Retirement Benefits and Other Employment Related Actuarial Liabilities (Note 13)	1,176,474	0	0	0
F. Environmental Cleanup (Note 11)	0	0	0	0
G. Other Liabilities (Notes 11 and 12)	0	0	0	0
H. Total Liabilities Not Covered by Budgetary Resources	$1,176,474	$0	$0	$0
6. Total Liabilities	$8,315,141	$713,728	$1,089,131	$45,920
NET POSITION				
7. Unexpended Appropriations (Note 14)	0	0	0	0
8. Cumulative Results of Operations	16,196,141	992,787	(22,322)	43,159
9. Total Net Position	$16,196,141	$992,787	($22,322)	$43,159
10. Total Liabilities and Net Position	$24,511,282	$1,706,515	$1,066,809	$89,079

The accompanying notes are an integral part of these statements.

	0	0	0	0

Department of Defense
Navy Working Capital Fund
CONSOLIDATING BALANCE SHEET
As of September 30, 1998
(in thousands)

	Ordnance	Transportation	Base Support	Information Services
LIABILITIES				
4. Liabilities Covered by Budgetary Resources:				
A. Intragovernmental :				
1. Accounts Payable	$44,040	($87,880)	$38,125	$38,700
2. Environmental Cleanup (Note 11)	0	0	0	0
3. Debt (Note 10)	0	1,094,710	0	0
4. Other Liabilities (Notes 11 ,12,and 15)	30,500	7,106	1,298	15,415
B. Total Intragovernmental	$74,540	$1,013,936	$39,423	$54,115
C. Accounts Payable	84,383	522,973	252,260	75,859
D. Liabilities for Loan Guarantees	0	0	0	0
E. Military Retirement Benefits and Other Employment Related Actuarial Liabilities (Note 13)	0	0	0	0
F. Environmental Cleanup (Note 11)	0	0	0	0
G. Other Liabilities (Notes 11 , 12,and 15)	19,693	29,767	87,085	15,530
H. Total Liabilities Covered by Budgetary Resources	$178,616	$1,566,676	$378,768	$145,504
5. Liabilities Not Covered by Budgetary Resources:				
A. Intragovernmental:				
1. Accounts Payable	0	0	0	0
2. Debt (Note 10)	0	0	0	0
3. Environmental Cleanup (Note 11)	0	0	0	0
4. Other Liabilities (Notes 11 ,12,and 15)	0	0	0	0
B. Total Intragovernmental	$0	$0	$0	$0
C. Accounts Payable	0	0	0	0
D. Debt (Note 10)	0	0	0	0
E. Military Retirement Benefits and Other Employment Related Actuarial Liabilities (Note 13)	0	0	0	0
F. Environmental Cleanup (Note 11)	0	0	0	0
G. Other Liabilities (Notes 11 and 12)	0	0	0	0
H. Total Liabilities Not Covered by Budgetary Resources	$0	$0	$0	$0
6. Total Liabilities	$178,616	$1,566,676	$378,768	$145,504
NET POSITION				
7. Unexpended Appropriations (Note 14)	0	0	0	0
8. Cumulative Results of Operations	234,196	(276,753)	652,681	(111,038)
9. Total Net Position	$234,196	($276,753)	$652,681	($111,038)
10. Total Liabilities and Net Position	$412,812	$1,289,923	$1,031,449	$34,466

The accompanying notes are an integral part of these statements.

0	0	0	0

Department of Defense
Navy Working Capital Fund
CONSOLIDATING BALANCE SHEET
As of September 30, 1998
(in thousands)

	Research & Development	Supply Management	Component	Eliminations
LIABILITIES				
4. Liabilities Covered by Budgetary Resources:				
A. Intragovernmental :				
1. Accounts Payable	$169,555	$167,863	$0	$0
2. Environmental Cleanup (Note 11)	0	0	0	0
3. Debt (Note 10)	0	0	0	0
4. Other Liabilities (Notes 11 ,12,and 15)	62,481	2,197,423	(1,697,539)	0
B. Total Intragovernmental	$232,036	$2,365,286	($1,697,539)	$0
C. Accounts Payable	1,316,787	362,621	0	0
D. Liabilities for Loan Guarantees	0	0	0	0
E. Military Retirement Benefits and Other Employment Related Actuarial Liabilities (Note 13)	0	0	0	0
F. Environmental Cleanup (Note 11)	0	0	0	0
G. Other Liabilities (Notes 11 , 12,and 15)	405,822	35,311	0	0
H. Total Liabilities Covered by Budgetary Resources	$1,954,645	$2,763,218	($1,697,539)	$0
5. Liabilities Not Covered by Budgetary Resources:				
A. Intragovernmental:				
1. Accounts Payable	0	0	0	0
2. Debt (Note 10)	0	0	0	0
3. Environmental Cleanup (Note 11)	0	0	0	0
4. Other Liabilities (Notes 11 ,12,and 15)	0	0	0	0
B. Total Intragovernmental	$0	$0	$0	$0
C. Accounts Payable	0	0	0	0
D. Debt (Note 10)	0	0	0	0
E. Military Retirement Benefits and Other Employment Related Actuarial Liabilities (Note 13)	0	0	1,176,474	0
F. Environmental Cleanup (Note 11)	0	0	0	0
G. Other Liabilities (Notes 11 and 12)	0	0	0	0
H. Total Liabilities Not Covered by Budgetary Resources	$0	$0	$1,176,474	$0
6. Total Liabilities	$1,954,645	$2,763,218	($521,065)	$0
NET POSITION				
7. Unexpended Appropriations (Note 14)	0	0	0	0
8. Cumulative Results of Operations	(329,964)	12,947,332	2,066,063	0
9. Total Net Position	($329,964)	$12,947,332	$2,066,063	$0
10. Total Liabilities and Net Position	$1,624,681	$15,710,550	$1,544,998	$0

The accompanying notes are an integral part of these statements.

	0	0	0	0

Appropriations, Funds, and Accounts Included in the Financial Statements

Reporting Entity:

Navy Working Capital Fund

Fund/Account Treasury Symbol and Title:

97X4930.002

Navy Working Capital Fund Activity Group Treasury Symbol and Title:

97X4930.NA1*	Depot Maintenance-Shipyards
97X4930.NA2*	Depot Maintenance-Aviation
97X4930.NA4*	Depot Maintenance-Other (Marine Corps)
97X4930.NA3*	Ordnance
97X4930.ND**	Transportation
97X4930.NE**	Base Support
97X4930.NF**	Information Services
97X4930.NH**	Research & Development
97X4930.NC**	Supply Management

Note: The '*' represents alpha or numeric characters which identify an activity or reporting segment of the activity group.

DEPARTMENT OF THE NAVY

NAVY WORKING CAPITAL FUND

AUDIT OPINION

INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
ARLINGTON, VIRGINIA 22202

March 1, 1999

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE (COMPTROLLER) AND CHIEF FINANCIAL OFFICER
DIRECTOR, DEFENSE FINANCE AND ACCOUNTING SERVICE

SUBJECT: Endorsement of the Disclaimer of Opinion on the FY 1998 Navy Working Capital Fund Financial Statements (Project No. 8FC-2029)

The Chief Financial Officers Act of 1990, as amended by the Federal Financial Management Act of 1994, requires financial statement audits by the Inspectors General. We delegated to the Naval Audit Service (NAS) the audit of the FY 1998 Navy Working Capital Fund Financial Statements. Summarized below are the NAS disclaimer of opinion on the FY 1998 Navy Working Capital Fund Financial Statements and the results of our review of the NAS audit. We endorse the disclaimer of opinion expressed by the NAS (Enclosure).

Disclaimer of Opinion. The NAS disclaimer of opinion on the FY 1998 Navy Working Capital Fund Financial Statements, dated February 9, 1999, stated that the NAS was unable to express an opinion on the financial statements. We concur with the NAS disclaimer of opinion for the reasons summarized below.

- The Navy Working Capital Fund and its accountant, the Defense Finance and Accounting Service, did not provide sufficient information to evaluate all of management's assertions and the fair presentation of the September 30, 1998, financial statements.

- NAS auditors could not verify the value of inventories reported as of September 30, 1997, and could not satisfy themselves regarding inventory quantities and values by means of other auditing procedures.

Internal Controls. The NAS determined that internal controls did not ensure that the FY 1998 Navy Working Capital Fund Financial Statements contained no material misstatements. For example, the Navy Working Capital Fund and the Defense Finance and Accounting Service did not implement controls over the valuation of Inventory and Related Property. As a result, Inventory Held for Repair and Excess, Obsolete and Unserviceable Inventories were misstated. The Department of the Navy and the Defense Finance and Accounting Service have recognized many of the financial reporting weaknesses and reported them in their FY 1998 Annual Statements of Assurance. Details on these matters and on compliance with laws and regulations will be discussed in a separate report.

Compliance With Laws and Regulations. Under the Federal Financial Management Improvement Act of 1996 and OMB Bulletin No. 98-08, "Audit Requirements for Federal Financial Statements," August 24, 1998, as amended January 25, 1999, the NAS work disclosed that financial management systems did not comply with Federal financial management system requirements, applicable Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level. For example, the Navy Working Capital Fund had not fully developed financial systems to extract and report intra-agency eliminations for Accounts Receivable and Unearned Revenue. Details on the adequacy of internal controls and on compliance with laws and regulations will be discussed in a separate report.

Review of NAS Work. To fulfill our responsibilities for determining the accuracy and completeness of the independent work conducted by the NAS, we reviewed the audit approach and planning and monitored progress at the key points. We also performed other procedures to determine the fairness and accuracy of the audit approach and conclusions.

We reviewed the NAS work on the FY 1998 Navy Working Capital Fund Financial Statements from September 22, 1998, through March 1, 1999, in accordance with generally accepted Government auditing standards. We found no indication that we could not rely on the NAS disclaimer of opinion or its related evaluation of internal controls and compliance with laws and regulations.

David K. Steensma

David K. Steensma
Deputy Assistant Inspector General
for Auditing

Enclosure

DEPARTMENT OF THE NAVY
AUDITOR GENERAL OF THE NAVY
5611 COLUMBIA PIKE
ROOM 506B, NASSIF BUILDING
FALLS CHURCH, VA. 22041-5080

IN REPLY REFER TO

Independent Auditor's Opinion on the Consolidated Financial Statements for the Fiscal Year 1998 Department of the Navy Working Capital Fund

We attempted to audit the Balance Sheet of the Consolidated Financial Statements of the Department of the Navy Working Capital Fund as of 30 September 1998, and the related Statement of Net Cost, Statement of Changes in Net Position, Statement of Budgetary Resources, and Statement of Financing for the year then ended. These financial statements are the responsibility of the Department of the Navy Working Capital Fund management.

The Department of the Navy Working Capital Fund and its accountant, the Defense Finance and Accounting Service, could not provide us sufficient information to allow us to evaluate all of management's assertions contained in the 30 September 1998 financial statement presentation. Specifically, information was not provided for Intra-agency eliminations for Accounts Receivable and Unearned Revenue. Supply Management's General Property, Plant and Equipment reported values were not supported by individual records. Operating Materials and Supplies held for use at industrial activities reported in Inventory and Related Property, Net were not revalued to historical cost and information was not available to evaluate its impact. Accounts Receivable, Net, Federal and Non-Federal and Accounts Payable, Federal and Non-Federal transactions cannot be segregated by an activity which represents a significant portion of the financial statement. We were not able to satisfy ourselves as to the effect of the issues noted through other audit tests.

Additionally, we could not verify the value of inventories reported as of 30 September 1997 and we were unable to satisfy ourselves regarding inventory quantities and value by means of other auditing procedures. Inventory amounts as of 30 September 1997 enter into the determination of program costs reported in the Statements of Net Cost and Changes in Net Position, for the fiscal year ended 30 September 1998.

The Department of the Navy Working Capital Fund and its accountant, the Defense Finance and Accounting Service, were unable to provide us with sufficient information necessary to evaluate management's assertions contained in the financial statements. Since we were unable to perform other audit tests necessary to satisfy ourselves as to the fair presentation of the statements, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on these statements.

JAMES D. WATTS
By direction

9 February 1999