Department of the Navy

ANNUAL FINANCIAL REPORT

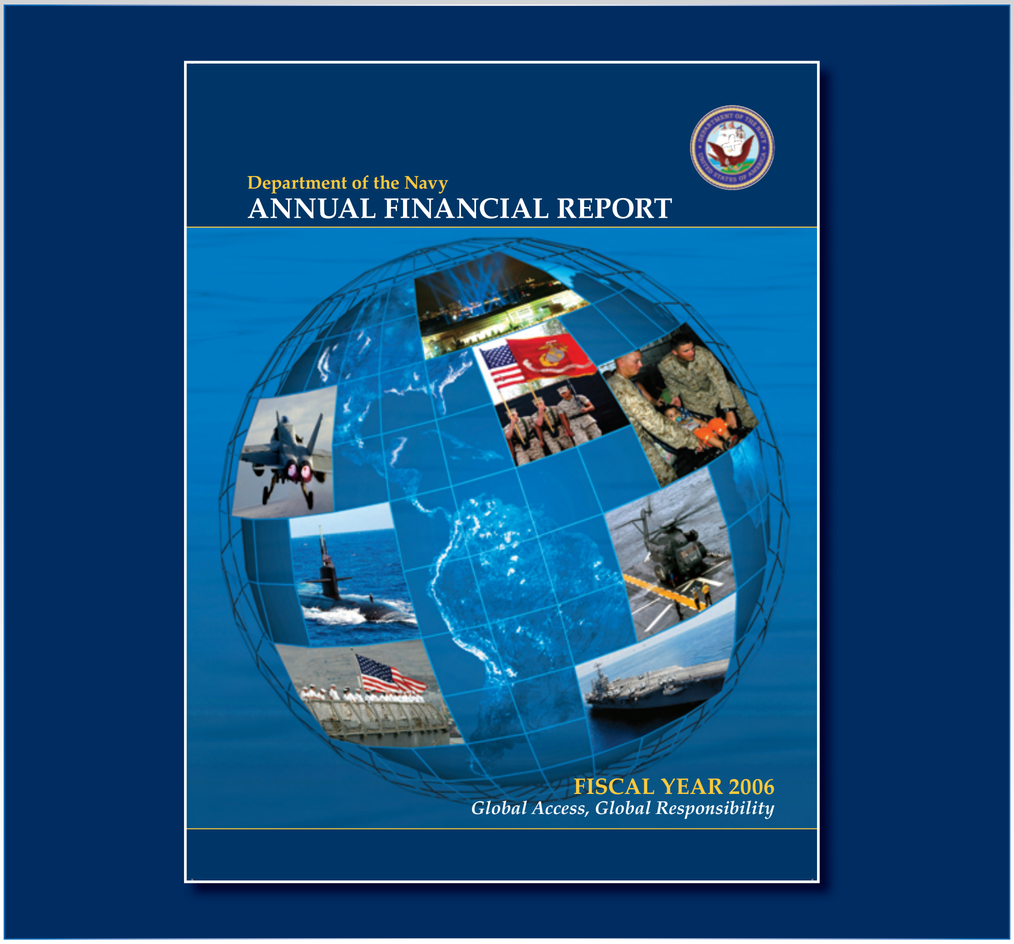
FISCAL YEAR 2007

Transformation: Balancing Today's Fight and Tomorrow's Force

2006 Silver Vision Award

Department of the Navy

Fiscal Year 2006 Annual Financial Report



VISION AWARDS 2006 SILVER LACP OVERALL

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The Honorable Donald C. Winter
Secretary of the Navy

THE SECRETARY OF THE NAVY
WASHINGTON, D.C. 20350-1000

November 2007

To meet the ongoing demands of the Global War on Terror today and the uncertain threats of tomorrow, the Department of the Navy continues to respond with strength, urgency and innovation. We enter the new fiscal year with the announcement of a landmark maritime strategy that will serve our Nation well and deep into the 21st Century. We are building a more flexible Fleet for the future, enhancing expeditionary warfare capacity, recapitalizing combat capability, and establishing a more collective and cooperative maritime posture globally. It is indeed an exciting time.

Internally, we are implementing methods to increase efficiency and maximize the return on our investments. The Navy is developing an Enterprise Framework providing better visibility of the people, funding, and material needed to deliver war-fighting readiness. This year the Navy Enterprise Resource Planning (N-ERP) Program moved past a major milestone from vision to implementation. Over the years to come, it will be the vehicle for increasing standardization, modernization, and transparency in our cost management framework. The Marine Corps continues to transform its business operations while also rightsizing a larger and more capable Corps. Throughout the Department, the continuous process improvement methodology, Lean Six-Sigma (LSS), is becoming a part of our culture, organizations and thought processes, delivering the same kind of positive returns found in the private sector. LSS will improve quality of work-life and speed up decision-making while reducing total cost of ownership. Department-wide initiatives such as LSS and N-ERP work collectively to support an overarching business transformation strategy fundamentally changing and strengthening the foundation of our business operations.

The strength of the Department continues to be best represented by our people. The recruitment, development, and retention of quality personnel are vital to our continued success. America's naval forces are combat-ready due to the dedication and motivation of individual Sailors, Marines, Civilians, and their families. The Department is committed to taking care of them by sustaining our quality of service/quality of life programs, providing the necessary training, compensation, and promotion opportunities while striving for reasonable operational and personnel tempo. Finally, I continue to be inspired by those Sailors and Marines who have sacrificed so much in service to our country. We will not forget those wounded warriors and will ensure they receive the services and attention they deserve.

While the Department will continue to evolve to meet rapidly changing threats, our commitment to safeguarding the people and resources of our Navy-Marine Corps Team remains a fundamental part of our strategy. We are responsible to Congress and the Nation for providing effective national security along with fiscal accountability. The Department of the Navy's Fiscal Year 2007 Annual Financial Report, *Transformation: Balancing Today's Fight and Tomorrow's Force*, represents our enduring commitment to the proper stewardship of public resources critical for the defense of our Nation and the protection of our war-fighters.

Donald C. Winter

Rear Admiral Stanley D. Bozin

Office of the Assistant Secretary of the Navy
(Financial Management and Comptroller)

THE ASSISTANT SECRETARY OF THE NAVY
(FINANCIAL MANAGEMENT AND COMPTROLLER)
1000 NAVY PENTAGON
WASHINGTON, DC 20350-1000

October 2007

Building the strength of our Department of the Navy financial management team, we continued to make great progress in applying a broad-based business transformation strategy during Fiscal Year 2007. Navy and Marine Corps financial managers have documented and improved business practices, added new elements to our human capital strategy, and emphasized more effective communication with customers and stakeholders. Our primary job continues to be that of improving the flow of relevant and reliable financial information, adding value to the operational and resource allocation decisions made by the Department's senior leadership.

Specific examples of success stories exist at all levels. Within the Headquarters and at specific activities, we implemented a more precise cash forecasting process within the $25 billion Navy Working Capital Fund, improving stability of operating cash. We have institutionalized a Financial Efficiency Index measuring how effectively the Department is executing the President's budget, using it and other measures of effectiveness to stimulate a more results-oriented culture, similar to that envisioned by the National Security Personnel System. We have applied the Lean Six Sigma (LSS) process improvement methodology to standardize and refine a variety of financial processes such as reimbursable orders and financial reporting. LSS provides the foundation supporting our ongoing evaluation of sound internal controls while also sustaining audit readiness efforts already implemented.

During Fiscal Year 2007, we also made considerable progress expanding our Financial Improvement Program (FIP)--a component of the Department of Defense Financial Improvement and Audit Readiness Plan—integrating and aligning all elements of business transformation. For example, we have established standard financial processes within the Navy Enterprise Resource Planning program, a modern integrated and automated system currently being implemented, first at the Naval Air Systems Command and ultimately throughout our supporting business enterprises between now and FY 2013. Testing of controls over financial reporting as prescribed by Office of Management and Budget Circular A-123, Appendix A, the federal version of Sarbannes-Oxley, continues to expand as part of the FIP. The Marine Corps moves closer to audit readiness and major elements of the Navy Working Capital Fund are on a similar track to demonstrate audit readiness. Finally, our business transformation strategy addresses all elements of business—our people, processes and systems—with a goal of producing high quality information that will both inform decision-making and result in auditable financial reports.

Reliable financial information will enhance public confidence in our management of valuable taxpayer dollars. The Department of the Navy's 2007 Annual Financial Report, *Transformation: Balancing Today's Fight and Tomorrow's Force*, reflects our enduring commitment to the proper stewardship of public resources and continuous improvement in fiscal transparency and accountability.

S. D. BOZIN
By direction

Management's Discussion and Analysis

OCTOBER 2006

Former President of the United States, George H. W. Bush, speaks at the christening of the tenth and final Nimitz-class aircraft carrier—George H. W. Bush (CVN 77).

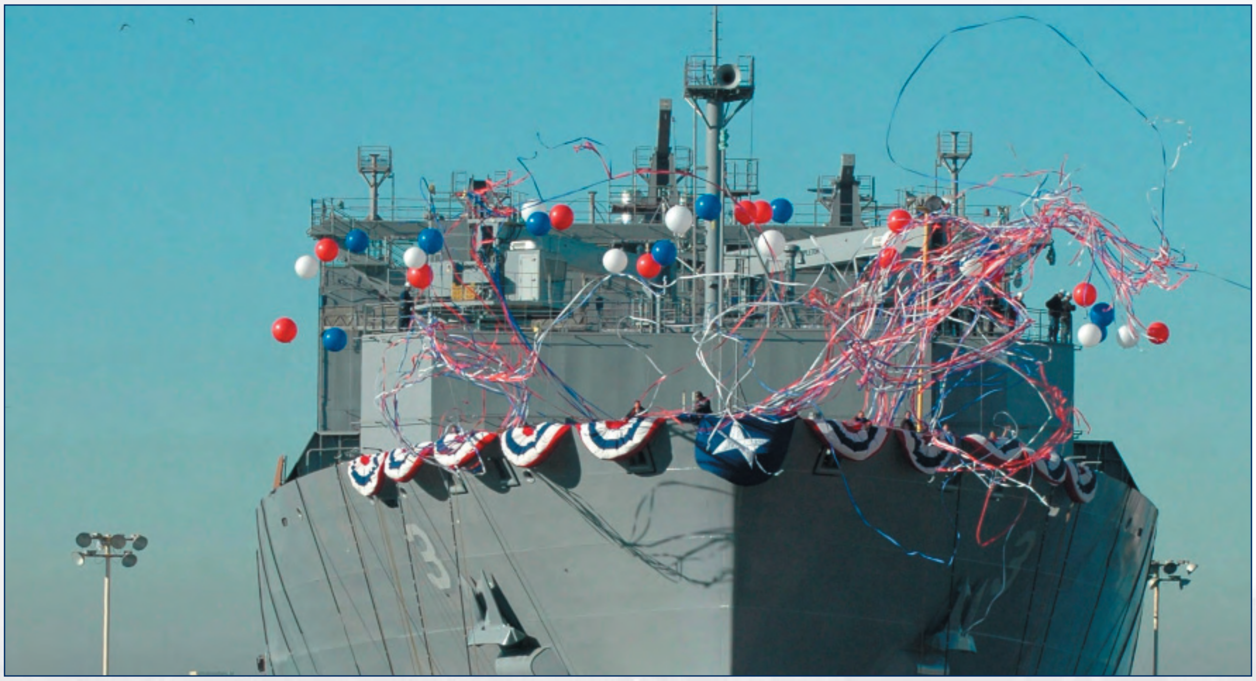
U.S. Marines and Sailors from Battalion Landing Team 1st Battalion, 5th Marine Regiment of the 31st Marine Expeditionary Unit conduct a long-range helicopter-borne raid using CH-53E Super Stallion helicopters. Executed with the assistance of the Philippine Air Force, the raid was part of the bilateral training exercises, Talon Vision and Amphibious Landing Exercise, which ran concurrently October 16 – 31.

NOVEMBER 2006

The dedication ceremony of the National Museum of the Marine Corps was held on November 10, 2006.

General Michael W. Hagee (right) passes the official battle colors of the Marine Corps to General James T. Conway (left) during the passage of command ceremony on November 13, 2006 at Marine Barracks Washington, DC. General Conway was appointed the 34th Commandant of the Marine Corps. General Hagee retired after 42 years of distinguished military service.

DECEMBER 2006



The newest Military Sealift Command advanced auxiliary dry cargo/ammunition ship, USNS Alan Shepard (T-AKE 3), is launched into the San Diego Bay. The USNS Alan Shepard is named after Rear Admiral Alan Bartlett Shepard, the first American astronaut in space and the fifth person to walk on the moon.

A U.S. Navy Lieutenant Commander visits a tent city in Dire Dawa, Ethiopia after severe flooding devastated the Ogaden region in August 2006. The U.S. Navy is part of the humanitarian relief effort to ease the suffering of nearly 217,000 people displaced by the flood.

JANUARY 2007

The Honorable Donald C. Winter, Secretary of the Navy, speaks during the official naming ceremony of the USS Gerald R. Ford (CVN 78), the first aircraft carrier that honors the 38th President of the United States.

Nimitz-class aircraft carrier, USS John C. Stennis (CVN 74), makes an early morning arrival in San Diego. The Stennis is stopping in San Diego to embark Carrier Air Wing Nine (CVW 9) and will be joined by the USS Antietam (CG 54) and the USS Preble (DDG 88) to begin a regularly scheduled deployment in support of combat operations in the Global War on Terror.

FEBRUARY 2007

Nimitz-class aircraft carrier, USS Dwight D. Eisenhower (CVN 69), conducts a replenishment at sea with Military Sealift Command fast combat support ship, USNS Arctic (T-AOE 8). The Eisenhower and embarked Carrier Air Wing Seven (CVW 7) are on a regularly scheduled deployment to Afghanistan in support of Operation Enduring Freedom.

Nimitz-class aircraft carrier, USS Ronald Reagan (CVN 76), arrives in Sasebo, Japan, for a scheduled port visit. The Reagan is currently in the 7th Fleet area of responsibility as part of a deployment to promote peace, cooperation and stability in the region.

MARCH 2007

RIVRON-1, part of the newly formed Naval Expeditionary Combat Command, deployed March 8 to the Middle East to conduct maritime security operations with Marines from the II Marine Expeditionary Force. The deployment marks the first for a U.S. Navy riverine squadron since the Vietnam War.

Sailors take their final walk down the brow of aircraft carrier, USS John F. Kennedy (CV 67), during the historic decommissioning ceremony on March 23. The Kennedy served its country for more than 38 years.

APRIL 2007

An EA-18G Growler, the Navy's next-generation electronic attack aircraft, made its first appearance at Naval Air Station Whidbey Island, Washington on April 9.

Amphibious assault ship, USS Bonhomme Richard (LHD 6), departs Naval Base San Diego for a six-month deployment to the Persian Gulf in support of U.S. Combatant Commanders fighting the Global War on Terror.

MAY 2007

Sailors man the newest Virginia-class nuclear attack submarine, USS Hawaii (SSN 776), during the commissioning ceremony on May 5 in New London, Connecticut.

One thousand twenty-eight Midshipmen graduated from the U.S. Naval Academy in Annapolis, Maryland on May 25, 2007.

JUNE 2007

Sailors man the rails of the newest Arleigh Burke-class guided-missile destroyer, USS Kidd (DDG 100), during an evening commissioning ceremony on June 9 in Galveston, Texas. The new destroyer honors Medal of Honor recipient Rear Admiral Isaac Campbell Kidd, Sr., who was killed on the bridge of his flagship USS Arizona on December 7, 1941.

Military Sealift Command hospital ship, USNS Comfort (T-AH 20), is at anchor off the coast of Guatemala during a scheduled stop. The Comfort is on a four-month humanitarian deployment to Latin America and the Caribbean and will ultimately provide medical treatment to approximately 85,000 patients in a dozen countries.

JULY 2007

Sailors and Marines man the rails aboard amphibious assault ship, USS Essex (LHD 2), during a scheduled port visit in Australia after the completion of Exercise Talisman Saber 2007. Talisman Saber is a joint and combined biennial exercise between Australia and the United States designed to prepare both nations in crisis action planning and execution of contingency operations.

A Seaman scans the horizon on the USS Pearl Harbor (LSD 52) during Partnership of the Americas (POA) 2007 deployment. The POA's focus is on enhancing relationships with partner nations through a variety of exercises and events at sea and on shore throughout Latin America and the Caribbean.

AUGUST 2007

Personnel from Navy Mobile Diving and Salvage Unit (MDSU) 2 supervise a diver as he conducts search and recovery operations in the Mississippi River after the collapse of the I-35 bridge.

A Marine attached to Regimental Combat Team (RCT) 6 gives a line of Iraqi children high fives during Operation Alljah. The Marines of RCT 6, Iraqi soldiers, and Iraqi police are working together during Operation Alljah to provide better security and safer neighborhoods for the citizens of Fallujah.

SEPTEMBER 2007

Admiral Gary Roughead (center) reports to Secretary of the Navy Donald C. Winter as the 29th Chief of Naval Operations (CNO) during an informal change of office ceremony held at the Pentagon, September 29, 2007. Admiral Roughead relieved Admiral Michael G. Mullen (left), who became the Chairman, Joint Chiefs of Staff at a change-of-command ceremony during October 2007.

Sailors aboard amphibious assault ship USS Kearsarge (LHD 3) take a moment of silence to remember the victims of the September 11 terrorist attacks. The Kearsarge is deployed in the Persian Gulf in support of maritime operations.

The Department of the Navy

Founded April 30, 1798

Our Mission: Maintain, train and equip combat-ready Naval forces capable of winning wars, deterring aggression and maintaining freedom of the seas.

The official seal of the Department of the Navy is engraved on the Navy and Marine Memorial. The memorial is dedicated to the thousands of Americans who have perished in the service of the Nation at sea and to those whose destiny still is linked with our naval and maritime services.

Introduction

The Department of the Navy (DON) remained focused on accomplishing its mission in the Global War on Terror. Naval forces provided the bulk of the nation's worldwide rotational military presence and an increasing portion of the required support for ground units in Operations Enduring Freedom and Iraqi Freedom. These operations supported our nation's interests by continuing deterrence intelligence, surveillance and reconnaissance missions, expanded maritime interception operations, counter-piracy, and deterrence patrols.

Yet, while focusing on the present missions of the Global War on Terror, DON continued to invest in capabilities that address the diverse strategic challenges of the post 9/11 security environment. These naval capabilities range from next-generation ships and aircraft to enhanced expeditionary warfare techniques. Additionally, continued investment in enterprise-wide business transformation initiatives has facilitated DON's progression toward improved efficiency and a performance-based organization focused on giving optimal support to the war-fighter.

The Fiscal Year 2007 Management's Discussion and Analysis (MD&A) provides perspective on the breadth and depth of the DON mission and the resources appropriated to it by Congress. It includes an overview of DON strategic performance; systems, controls, and legal compliance; and financial condition and results of operations. The following sections comprise the FY 2007 MD&A:

- Organization and Mission
- Strategic Management
- Management Assurances
- Financial Condition and Results of Operations
- Looking Forward: Fiscal Year 2008 and Beyond

Organization and Mission

From the corpsmen on the hospital ship MERCY on a humanitarian mission to Indonesia, to the Sailors on Navy ships protecting shipping lanes in international waters, to Marines on the ground in Iraq trying to bring peace to a troubled land, all of them make me feel honored to belong to an organization dedicated to answering the nation's call to service.

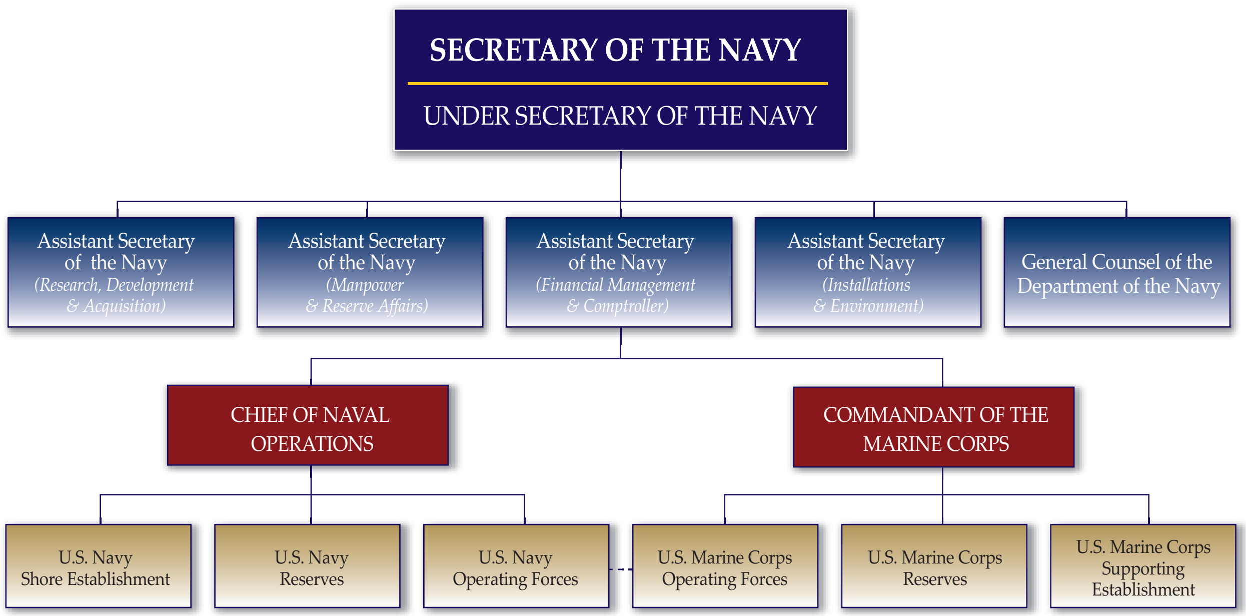
- The Honorable Donald C. Winter, Secretary of the Navy, April 2007

The DON is separately organized under the Secretary of the Navy, a civilian appointed by the President, who conducts all Department affairs under the authority, direction, and control of the Secretary of Defense (Sections 5011 and 5013, Title 10 U.S. Code).

Under the purview of the Secretary of the Navy are key military leaders—the Chief of Naval Operations, a four-star Admiral, and the Commandant of the Marine Corps, a four-star General. The Chief of Naval Operations is responsible to the Secretary of the Navy for the command and operating efficiency of the U.S. Navy (Section 5033, Title 10 U.S. Code). The Commandant of the Marine Corps is responsible to the Secretary of the Navy for the performance of the U.S. Marine Corps (Section 5043, Title 10 U.S. Code).

The U.S. Navy and the U.S. Marine Corps together comprise DON's naval contribution to the U.S. Joint Force. Both Services have numerous major commands that operate under the authority and responsibility of a commander or other designated official and typically support a network of subordinate commands. Each major command has a clearly defined mission that supports the overall DON mission in support of the Department of Defense's responsibilities.

The chart on the following page provides a simplified illustration of the DON organizational structure. The full structure is shown online at *http://www.navy.mil* under "Navy Organization."



* *Dashed line signifies collaboration of the U.S. Navy and the U.S. Marine Corps operating forces.*

United States Navy

The Navy shall be organized, trained, and equipped primarily for prompt and sustained combat incident to operations at sea. It is responsible for the preparation of naval forces necessary for the effective prosecution of war except as otherwise assigned and, in accordance with integrated joint mobilization plans, for the peacetime components of the Navy to meet the needs of war. (Section 5062, Title 10 U.S. Code)

Founded October 13, 1775

http://www.navy.mil

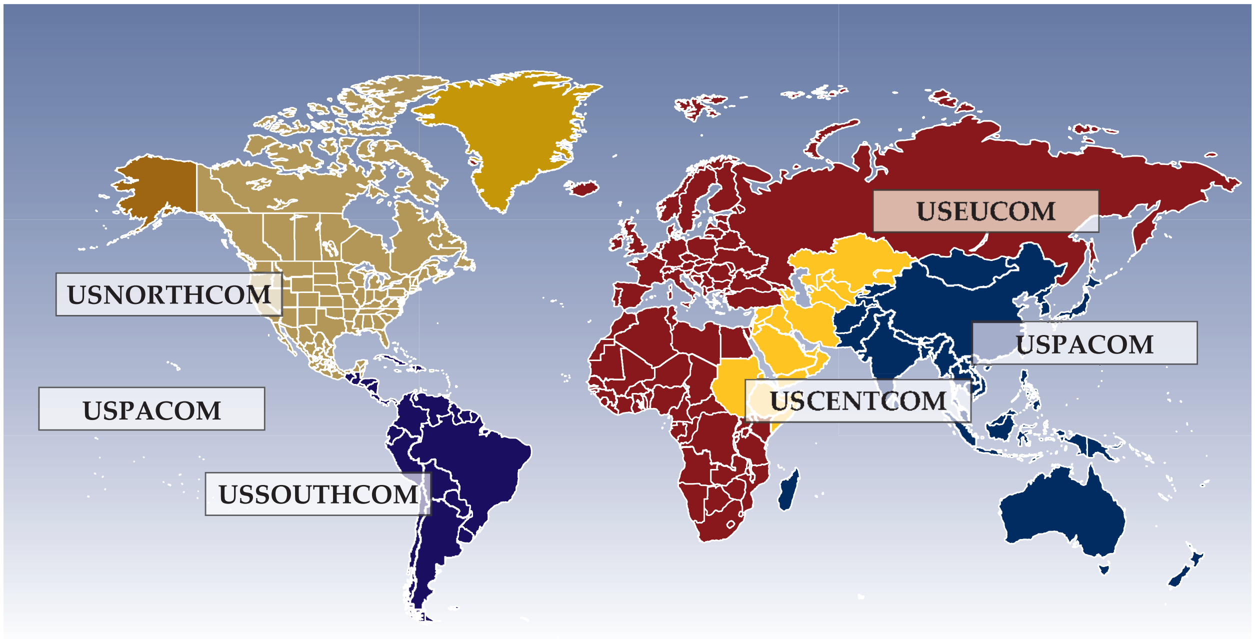
United States Marine Corps

The Marine Corps shall be organized, trained, and equipped to provide fleet marine forces of combined arms, together with supporting air components, for service with the fleet in the seizure or defense of advanced naval bases and for the conduct of such land operations as may be essential to the prosecution of a naval campaign. (Section 5063, Title 10 U.S. Code)

Founded November 10, 1775

http://www.usmc.mil

As team members of the U.S. Joint Force, DON provides Naval Components to support the nine Combatant Commands, which are comprised of five Geographic Commands and four Functional Commands (see illustrations).



Geographic Commands

1. **U.S. Pacific Command (USPACOM):** U.S. Pacific Fleet, 3rd and 7th Fleets (*www.cpf.navy.mil*); U.S. Marine Corps Forces, Pacific and Fleet Marine Force, Pacific (*www.mfp.usmc.mil*)

2. **U.S. Central Command (USCENTCOM):** U.S. Naval Forces Central Command and 5th Fleet (*www.cusnc.navy.mil*); U.S. Marine Corps Forces Central Command (*www.marcent.usmc.mil*)

3. **U.S. European Command (USEUCOM):** U.S. Naval Forces Europe and 6th Fleet (*www.naveur.navy.mil*); U.S. Marine Corps Forces, Europe (*www.mfe.usmc.mil*)

4. **U.S. Southern Command (USSOUTHCOM):** U.S. Naval Forces Southern Command (*www.cusns.navy.mil*); U.S. Marine Corps Forces, South (*www.mfs.usmc.mil*)

5. **U.S. Northern Command (USNORTHCOM):** USNORTHCOM has few permanently assigned forces. However, naval personnel (civilians and uniformed services) are among the civil service employees and uniformed service members at USNORTHCOM headquarters (Peterson Air Force Base, Colorado) (*www.northcom.mil*)

Functional Commands

U.S. Joint Forces Command	U.S. Strategic Command
U.S. Fleet Forces Command, 2nd and 3rd Fleets (*www.cffc.navy.mil*) U.S. Marine Corps Forces Command (*www.jfcom.mil/about/com_marfor.htm*)	U.S. Fleet Forces Command (*www.cffc.navy.mil*) U.S. Marine Corps Forces, Strategic Command (*www.marforstrat.usmc.mil*)
U.S. Special Operations Command	**U.S. Transportation Command**
U.S. Naval Special Warfare Command (*www.navsoc.navy.mil*) U.S. Marine Corps Forces, Special Operations Command (*www.marsoc.usmc.mil*)	Military Sealift Command (*www.msc.navy.mil*)

USS Kitty Hawk (CV 63) pulls along side the Military Sealift Command underway replenishment oiler USNS Rappahannock (T-AO 204) during replenishment at sea. The Kitty Hawk is currently deployed in the South China Sea on a regularly scheduled deployment.

The Silent Drill Team performs a synchronized drill movement during the Marine Corps Air Station (MCAS) Beaufort's annual Battle Color Ceremony at the MCAS parade field in South Carolina.

Strategic Management

The diverse strategic challenges of the 21st century have compelled DON to balance the enduring requirements for traditional naval capabilities with those needed to confront and influence the highly dynamic security environment. Non-traditional missions, such as counter-terrorism, disaster relief, humanitarian assistance, and counter-piracy, have become integral to the overall DON mission. These new missions require DON to change rapidly and become a more agile, effective, and efficient enterprise in support of the war-fighter.

A Cooperative Strategy for 21st Century Seapower focuses on the near-term development of the Navy and Marine Corps team to meet the emerging global threats and challenges of this new era. This strategy reinforces and expands operational concepts that will enhance America's ability to project offensive power, defensive assurance, and operational independence across the globe. It also emphasizes the soft elements of seapower, such as humanitarian assistance, to use America's best characteristics to serve her best interests.

Enterprise-wide business transformation, including initiatives pursuant to DON Financial Management Strategic Plan will dramatically change DON's ability to execute programs and support mission goals. This transformation will result in improved efficiency, better decision-making, and a performance-based culture.

The following is a discussion of DON strategic performance in terms of FY 2007 enterprise-wide objectives.

Objective 1: Provide a Total Naval Workforce Capable and Optimized to Support the National Defense Strategy

The development and retention of quality people are vital to our continued success. America's naval forces are combat-ready due to the dedication and motivation of individual Sailors, Marines, civilians, and their families.

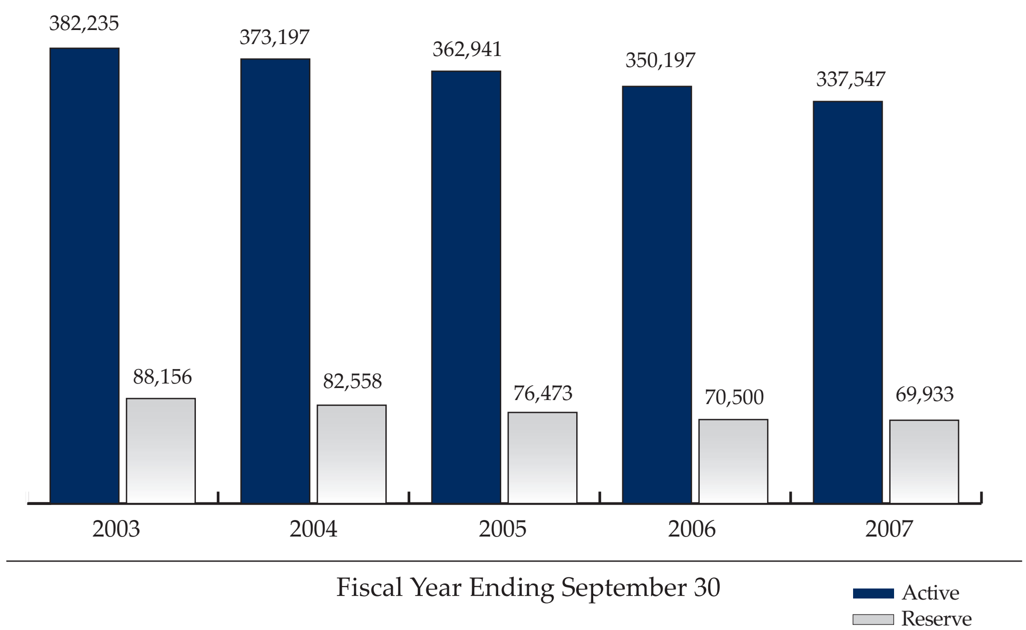
- The Honorable Donald C. Winter, Secretary of the Navy, March 2007

The DON continued to focus on sizing, shaping, and stabilizing the Total Naval Workforce—Sailors, Marines, and civilians—to provide maximum flexibility in applying the right skill sets to projected requirements in the most cost efficient manner.

U.S. Navy

Aggressive transformation of U.S. Navy forces continued in FY 2007, contributing to an overall decline in operating forces (see chart). The Navy reduced the size of its active and reserve components by 12% and 21%, respectively, from FY 2003 to FY 2007. These reductions, however, are more about shaping the force to enhance the Navy's ability to meet the deployment requirements of the Global War on Terror, Homeland Defense, and stability operations. With more efficient and automated ships, planes, and combat systems entering service in future years, personnel reductions are inevitable; yet, the skill level and specialization requirements will increase. Through its *Strategy for Our People*, the Navy plans to satisfy future war-fighting needs by attracting, retaining, and better educating forces capable of adapting and responding to mission needs.

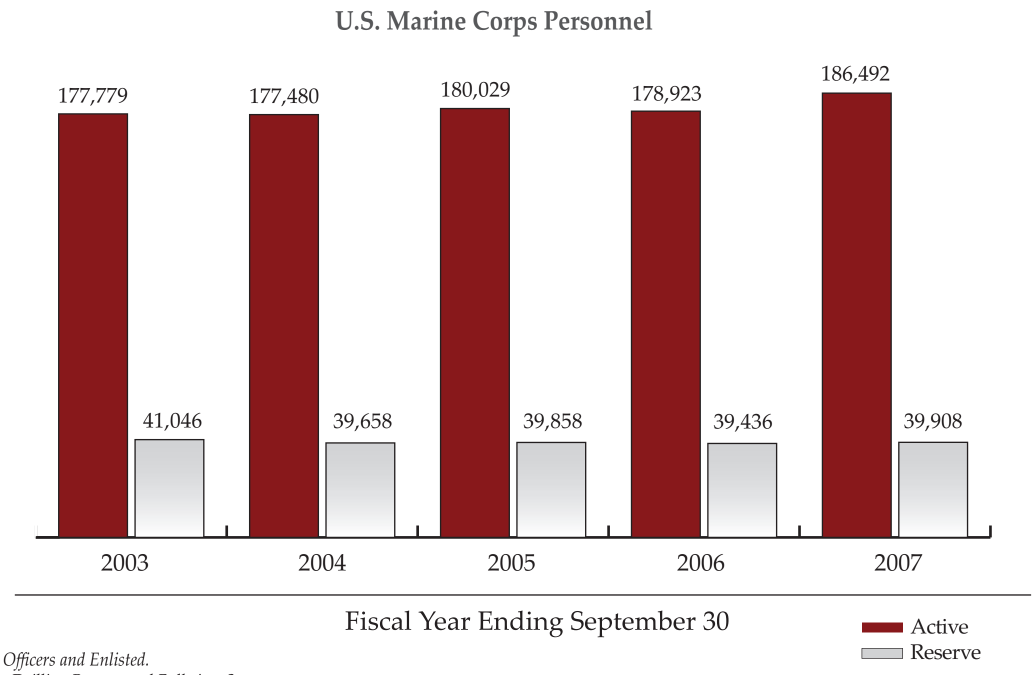
U.S. Navy Personnel



Active = Officers, Enlisted, and Midshipmen.
Reserve = Drilling Reserve and Full-time Support.

U.S. Marine Corps

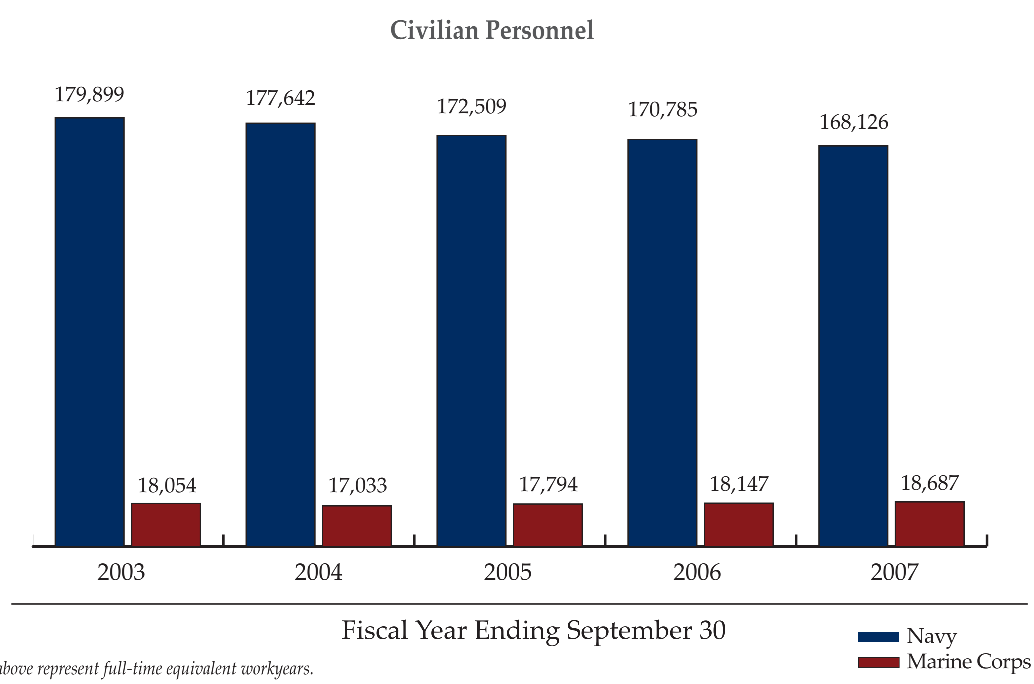
The U.S. Marine Corps continued to reshape its forces to meet the growing demands of the Global War on Terror and to provide trained forces in support of other contingencies. The Marine Corps increased the size of its active component by 5% and reduced the size of its reserve component by 3% from FY 2003 to FY 2007 (see chart). However, the Marine Corps active component is expected to increase to 202,000 by FY 2011 as approved by the President. The additional forces will enhance the Marine Corps' ability to operate at the "sustained rate of deployment" (i.e., maintain operations indefinitely without drastic changes to procedures, policies, organization, or operations). Additionally, the Marine Corps anticipates continued success in meeting recruiting and retention goals to maintain the planned force level.



Active = Officers and Enlisted.
Reserve = Drilling Reserve and Full-time Support.

Navy and Marine Corps Civilian Personnel

Civilian workforce transformation continued in FY 2007 in tandem with military force transformation. From FY 2003 to FY 2007, the total number of Navy and Marine Corps civilian personnel full-time equivalents declined by 6% (see chart). This decline occurred as DON benefited from strategic sourcing initiatives to privatize commercial-type functions and streamline core processes. The DON will continue to study military and civilian positions and to identify military billets that are not "military essential" for conversion to civilian employees or contractor support.



Figures above represent full-time equivalent workyears.

Training and Education

Training and education are critical to the continued growth and development of our Sailors and Marines and enhance their contribution to our joint war-fighting ability. In FY 2007, the Navy began implementation of Spiral One Sea Warrior. This initiative is the first implementation of a family of training, education and career management systems. The Sea Warrior initiative promotes mission success by delivering the right Sailors, with the right skills, at the right time, and to the right places. The Navy also continued to develop its language, regional expertise, and cultural programs, which facilitate our capability to communicate with and comprehend adversaries, enduring allies, and emerging partners. Similarly, the U.S. Naval Academy expanded its foreign language programs in Chinese, Arabic, Russian, and Japanese.

Marine Corps training and education remained stalwart components of an individual Marine's professional development. The Military Occupational Specialty (MOS) Roadmaps, in particular, continued to guide Marines through general and specific career training, education requirements, and opportunities to successfully navigate their tour of duty, skill progression, unit training, and voluntary education. Institutionally, MOS Roadmaps will increase the combat effectiveness of all Marine organizations.

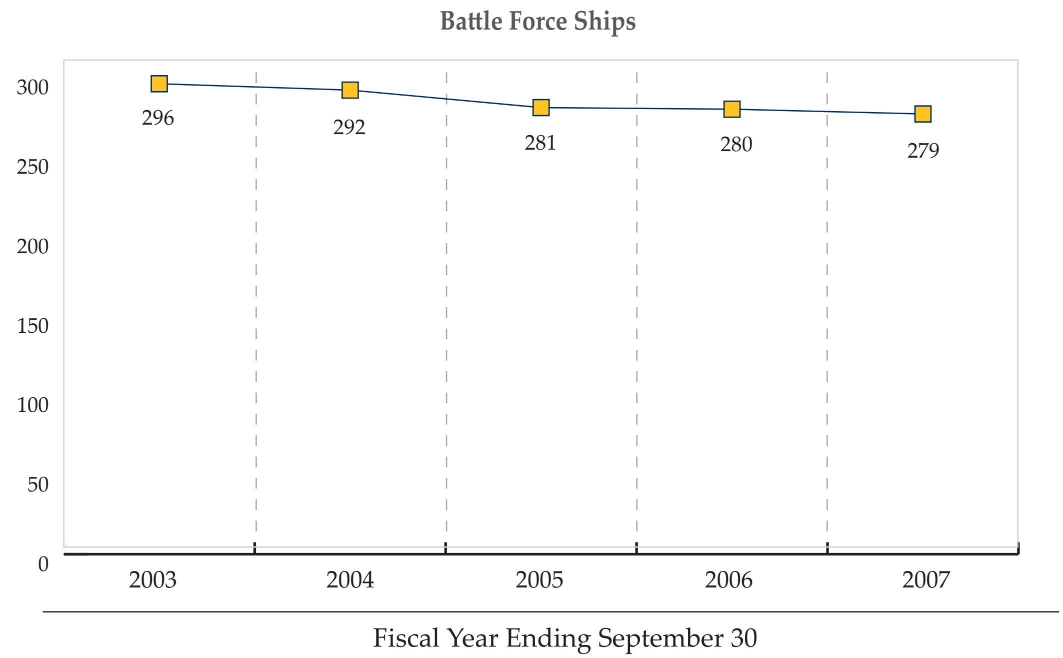
Additionally, Marine Corps' distributed operations in FY 2007 placed a premium on the situational awareness and judgment of junior leaders, thereby necessitating enhancements to professional development. These enhancements include foreign language and culture training that have been designed to empower individual Marines to assume greater responsibilities and decentralized decision-making and to operate in diverse cultures.

Objective 2: Use the Navy-Marine Corps Team to Aggressively Prosecute the Global War on Terror

The DON continued to support the Global War on Terror with naval combat forces that are capable and relevant to the missions assigned. The Navy's Fleet Response Plan and Marine Air-Ground Task Force are two significant elements of naval combat support; a brief discussion of each follows.

Fleet Response Plan

The Navy continued to support the Global War on Terror with adaptable, flexible, and sustainable forces enabled by the Fleet Response Plan (FRP). Battle force ships are integral to FRP, which is structured to provide six ready carriers in less than 30 days with an additional surge in 90 days. While the overall inventory of battle force ships has decreased (see chart), FRP seeks to offset this slight decline by increasing the availability of battle force ships. The ability to surge dramatically shortens response times to any contingency and enables the U.S. to increase the global presence of its military force as required to support emergent requirements in the Global War on Terror.



Battle force ships comprise aircraft carriers, fleet ballistic missle submarines, guided missle submarines, surface combatants, nuclear attack submarines, amphibious warfare ships, combat logistics ships, mine warfare ships, and support ships. See the Naval Vessel Register at http://www.nvr.navy.mil for more information on battle force ships.

Marine Air-Ground Task Force

The Marine Corps continued to demonstrate their versatility and flexibility across the spectrum of the Global War on Terror. In particular, the Marine Air-Ground Task Force continued to provide the joint force with a mix of combat and non-lethal actions; interagency capabilities and joint warfare applications; innovative use of airpower; and synchronization of intelligence activities. The overall structure of Marine Corps operating forces has remained relatively steady (see chart) but is expected to increase over the next five years.

Marine Corps Operating Forces

Fiscal Year Ending September 30

Marine Corps Land Forces	2003	2004	2005	2006	2007
Marine Expeditionary Forces	3	3	3	3	3
Marine Expeditionary Brigades	4	4	4	3	3
Marine Battalions, Active & Reserve	72	72	73	69	71

Objective 3: Build the Navy-Marine Corps Force for Tomorrow

Our future Navy-Marine Corps Force will remain a forward-deployed, expeditionary force with global speed and persistence. Operating alongside our joint and maritime partners, our future force will provide both actionable intelligence through persistent Maritime Domain Awareness and the ability to take action where and when the threat is identified.

To build our future Navy-Marine Corps Force today, DON continued to invest in new generation capabilities and business transformation. A brief discussion of ship construction, aircraft procurement, and business transformation efforts in FY 2007 follows.

Ship Construction

The future fleet of ships, as represented in our 30-year shipbuilding plan, will sustain operations in forward areas longer, be able to respond more quickly to emerging contingencies, and generate more sorties and simultaneous attacks against greater numbers of multiple targets and with greater effect than our current fleet. The DON continued to see the future fleet take shape with ongoing ship construction programs including:

- *Dry Cargo and Ammunition Ship (T-AKE)*
- *Guided-Missile Destroyers (DDG)*
- *Nuclear-Powered Attack Submarine (SSN)*
- *Amphibious Helicopter Assault – Replacement (LHA(R))*
- *Carrier Replacement Program (CVN 77)*
- *Amphibious Platform Dock Ship (LPD 17)*
- *Littoral Combat Ship (LCS)*
- *Amphibious Assault Ship (LHD 1)*

Aircraft Procurement

The DON is in the midst of an extensive, long-term consolidation and recapitalization of all naval aircraft in order to develop the optimum balance between requirements and usage. To sustain global air superiority, DON has invested in several naval aviation acquisition programs. Some examples of aircraft that DON procured in FY 2007 are listed below.

NAVY AIRCRAFT:

- *F/A-18 E/F Super Hornet* – long-range, multi-mission, all-weather strike fighter.
- *EA-18G Growler* – next-generation electronic attack aircraft.
- *MH-60S Knighthawk, MH-60R Seahawk* – multi-mission combat helicopters.
- *MQ-8B Fire Scout* – vertical take-off and landing tactical unmanned aerial vehicle.

MARINE CORPS AIRCRAFT:

- ***MV-22B Osprey*** – vertical/short take-off and landing, multi-purpose tactical transport.
- ***AH-1Z*** / ***UH-1Y*** – utility and attack helicopters.
- ***KC-130J*** – multi-mission, tactical aerial refueler/transport aircraft.

The Department will continue to seek ways to transform the way we do business resulting in improved efficiency, better decision-making, and an organizational culture that is performance-based.

- The Honorable Donald C. Winter, Secretary of the Navy, March 2007

The DON continued to demonstrate progress in its business transformation efforts, specifically through the initiatives discussed below. These initiatives are aligned with Department of Defense business transformation efforts, including the Financial Improvement and Audit Readiness Plan and the Business Enterprise Architecture. Collectively, these DON initiatives will create a business environment that produces more accurate and timely financial information that will then be available to senior managers for decision making purposes and ultimately enable DON to achieve a favorable audit opinion on its consolidated financial statements.

Lean Six Sigma

During FY 2007, DON began broad implementation of Lean Six Sigma, one of the Secretary of the Navy's priority initiatives for improving DON's overall effectiveness and efficiency. Lean Six Sigma is an industry-proven continuous process improvement methodology. The DON's major commands have successfully launched Lean Six Sigma training programs and are applying Lean Six Sigma concepts, techniques, and tools to various segments of their business operations.

National Security Personnel System

The DON continued to transition its workforce to the National Security Personnel System (NSPS) in FY 2007. Authorized by Congress, NSPS provides Department of Defense leaders the right tools to manage the civilian workforce, facilitate competition for high quality talent, offer compensation competitive with the private sector, and reward outstanding service. The Strategic Systems Program (SSP), Headquarters successfully completed its transition to NSPS in October 2006. Many of the DON's major commands began their conversion efforts in FY 2007; these include the Fleet Forces Command, Bureau of Naval Personnel, Naval Facilities Engineering Command (NAVFAC), Space and Naval Warfare Systems Command (SPAWAR), and Naval Special Warfare Command. Other major commands, such as the Naval Air Systems Command (NAVAIR); the Commander, Navy Installations Command (CNIC); the Bureau of Medicine and Surgery (BUMED); and the Military Sealift Command expect to transition to NSPS beyond FY 2007.

Navy Enterprise Resource Planning System

NAVAIR is the first of the DON's major commands to implement the Navy Enterprise Resource Planning (ERP) Program; implementation began on October 1, 2007. Navy ERP will integrate and improve Navy processes for logistics, acquisition, and financial operations. The Navy ERP Program is the cornerstone of the DON's business transformation strategy and a key enabler of the Navy's Enterprise vision to transform business processes and generate efficiencies to improve combat capabilities.

Other major acquisition commands have begun preparation for implementation of the Navy ERP in subsequent fiscal years. These include SPAWAR, Naval Sea Systems Command (NAVSEA), Naval Supply Systems Command (NAVSUP), and SSP.

Navy and Marine Corps Financial Improvement

The DON's major commands remained focused on improving the quality and timeliness of financial management information pursuant to the DON Financial Improvement Program (FIP). The DON FIP is the integrating financial element of the DON's business transformation strategy.

The overall goal of the DON FIP is to transform the business environment to support timely, accurate, and reliable financial information for decision-making, ultimately leading to a "clean" audit opinion on the consolidated DON financial statements.

Representative examples of significant accomplishments under the DON FIP for the Navy include:

- Completion of initial discovery efforts, which involved the major commands documenting, evaluating, and testing their business processes, systems, and internal controls.
- Assertion of audit readiness for DON General Fund Environmental Disposal Liabilities for Weapons Systems, and Cash and Other Monetary Assets.
- Modeling the Department of Defense's "segment" approach to audit readiness under the Office of the Under Secretary of Defense (Comptroller)'s revised audit strategy. A segment is a material component of the enterprise-wide financial environment, such as an individual financial statement line item, a group of related line items, or a business process.

The Marine Corps continued to progress toward audit readiness by improving its financial management practices, identifying material deficiencies, and documenting policies, processes, and procedures. As a result, the Marine Corps has developed a strategy and associated timeline to assert certain elements of audit readiness in December 2008. Representative examples of significant accomplishments under its Financial Improvement Initiative include:

- Review of transactional accuracy of the Standard Accounting, Budgeting, and Reporting System, the primary Marine Corps financial system, specifically with regard to data entry and trading partner information.
- Audit Readiness Summits with field level activities to deepen the awareness of the audit process and requirements.
- Validation of real property business processes and internal controls, which received a favorable evaluation from the Naval Audit Service.

Base Realignment and Closure

The DON continued to implement recommendations pursuant to the Base Realignment and Closure (BRAC) Act of 2005. BRAC 2005 is the means for reconfiguring the current infrastructure into one where operational capacity maximizes war-fighting capability and efficiency. The DON's implementation plan meets the statutory requirement for closure and realignment by September 15, 2011. Some of the other major commands affected by BRAC 2005 in FY 2007 include NAVAIR; NAVSEA; NAVSUP; NAVFAC; Bureau of Naval Personnel; Commander, Navy Reserve Forces Command; BUMED; and SPAWAR.

Objective 4: Emphasize Safety

The DON continued to focus on improving the safety of the workforce and workplace. While DON has much work to do to achieve the Secretary of Defense challenge to reduce mishap rates by 75% by the end of FY 2008, significant progress has been made in FY 2007. Specifically, FY 2007 was the best year recorded for the following safety metrics:

- Total Class A Operational Mishaps for Navy and Combined Navy/Marine Corps
- Total Aviation Class A Flight Mishaps for Combined Navy/Marine Corps
- Off-Duty Recreational Fatalities for Navy

The DON will continue to work toward becoming an organization with a world-class safety record, where no mishap is accepted as the cost of doing business.

Objective 5: Reinforce Ethics as a Foundation of Exemplary Conduct within DON

During FY 2007, DON made strides in reinforcing ethics as a foundation of exemplary conduct. The Secretary of the Navy, Chief of Naval Operations, and Commandant of the Marine Corps set forth their respective ethics messages that explained the importance of ethics and inspired DON personnel to make ethics a part of the culture. Also, Navy completed a survey that assessed the value of Ethics Counselors to DON leadership. Results of the survey data indicated that leadership and their attorney counselors believe that the ethics advice provided is important, sound, and timely. A second survey, which is expected to be fielded in early FY 2008, will assess DON's ethics culture. The expectation is that, once the survey is completed and the data analyzed, DON will be able to develop and execute initiatives to enhance the value of ethics to the culture. These are a few examples that illustrate how DON's ethics culture has taken shape and will continue to evolve.

Management Assurances

Commanders and managers throughout DON must ensure the integrity of their programs and operations. Part of this responsibility entails compliance with federal requirements for financial management systems, financial reporting, and internal controls. Below is a brief discussion of DON compliance with Federal requirements for FY 2007.

Systems

Federal Financial Management Improvement Act of 1996

The Federal Financial Management Improvement Act (FFMIA) of 1996 requires agencies to implement and maintain financial management systems that comply with Federal systems requirements, applicable federal accounting standards, and the U.S. Standard General Ledger at the transaction level. While some financial or financial feeder systems can comply with these standards, implementation of the Navy ERP will provide a standard compliant financial backbone. The Navy ERP will be compliant with the Department of Defense Standard Financial Information Structure, which includes support for the U.S. Standard General Ledger at the transaction level.

Financial Reporting

Chief Financial Officers Act of 1990, as amended by the Government Management Reform Act of 1994

The Chief Financial Officers Act of 1990, as amended by the Government Management Reform Act of 1994, requires agencies to produce auditable annual financial statements. The DON has been producing annual financial statements for the Navy Working Capital Fund since FY 1991 and the General Fund since FY 1996. In FY 2007, the DON FIP, as a supporting initiative of the Office of the Secretary of Defense Financial Improvement and Audit Readiness plan, made significant progress toward the goal of audit readiness by continuing to document financial processes, assess risks, and test internal controls.

Government Performance and Results Act of 1993

The Government Performance and Results Act (GPRA) of 1993 requires agencies to engage in strategic planning and performance management for the purpose of improving the effectiveness and efficiency of programs they administer. Broad application of Lean Six Sigma as well as implementation of metrics, such as the Financial Efficiency Index – a comprehensive measure of how well DON is executing its budget – and the transition to NSPS have moved DON forward toward a more outcome-oriented, performance-based culture.

Inspector General Act of 1978

The Inspector General Act of 1978, as amended, requires agencies to provide an explanation for all audit reports that have open recommendations exceeding one year. As of September 30, 2007, DON had 47 audit reports open for more than one year, with potential monetary benefits of $54.2 million. The DON closed out and implemented recommendations from 67 audit reports in FY 2007 with claimed monetary benefits of $98.3 million.

Improper Payments Information Act of 2002

The Improper Payments Information Act of 2002 seeks to reduce improper payments throughout the Federal Government by requiring agencies to report on programs and activities that are susceptible to improper payments. Improper payments are those that should not have been made or that were disbursed in incorrect amounts. The DON programs and activities that have reporting responsibilities under the Improper Payments Information Act include Personnel Support Activities and Detachments, which calculate travel payments, and Disbursing Officers aboard ships and at other isolated locations. Note, however, that the Defense Finance and Accounting Service performs the vast majority of DON's entitlement computation and disbursement functions.

For FY 2007, DON identified $1.4 million of potentially improper payments. This amount is significantly less than the threshold of $10 million, as established by the Office of Management and Budget (OMB). The DON is instituting internal controls, where applicable, to reduce the occurrence of improper payments in the future.

Internal Controls

Federal Managers' Financial Integrity Act of 1982

The Federal Managers' Financial Integrity Act (FMFIA) of 1982 requires agencies to evaluate their system of internal accounting and administrative controls and to report on the effectiveness of these controls in an annual statement of assurance. The Sarbanes-Oxley Act of 2002, which applies to publicly traded companies, led to the Federal Government's reevaluation of internal control policies under FMFIA. Consequently, OMB issued a revised version of Circular A-123 in December 2004, *Management's Responsibility for Internal Control*. Appendix A of the revised circular requires agencies to provide a separate statement of assurance on the effectiveness of financial reporting controls.

The FY 2007 DON evaluation of its management controls indicated that DON's system of administrative and operational internal controls overall, in effect as of June 30, 2007, provided qualified assurance, with the exception of seven material weaknesses, that controls are in place, operating effectively, and being used. The DON has planned aggressive corrective action to strengthen internal controls; it has targeted three of the material weaknesses to be ready for closure during FY 2008, with ongoing remediation programs established for the remaining weaknesses. Increased attention throughout the preparation of the FY 2007 Statement of Assurance and the resulting transparency of the reporting process ensure that the internal controls over DON's operational, administrative, and business processes are reasonably sound.

Despite the fact that significant progress has been made in improving overall audit readiness, several weaknesses in DON's internal controls over financial reporting remain. The OMB A-123 coverage only includes those areas that have been fully remediated. The FY 2007 FMFIA Annual Statement of Assurance is available at *http://www.fmo.navy.mil.*

Financial Condition and Results of Operations

The DON continues to address the financial management challenges outlined in the accompanying independent auditor's reports. These challenges prevent the DON from producing auditable financial statements in the near-term for the DON General Fund (GF) and Navy Working Capital Fund (NWCF). As previously highlighted in sections "Strategic Management" and "Management Assurances," respectively, achievements under the DON FIP and Managers' Internal Control Program (MICP) in FY 2007 have facilitated DON's progress toward improving the quality and reliability of its financial information. Most notably, the Marine Corps is close to asserting audit readiness and should be the first Military Service to produce auditable financial statements. The Marine Corps began preparing subsidiary financial statements in FY 2006.

The DON FIP strategy relies on the modernization of the DON systems environment, including implementation of the Navy ERP; improved business processes, including Lean Six Sigma efforts; and ensuring personnel are both trained and properly incentivized through the NSPS initiative. The DON FIP also places emphasis on the need for an effective internal control environment, as addressed by the MICP and implementation of OMB Circular A-123, Appendix A.

Overview of Financial Results

For financial reporting purposes, DON is organized into two reporting entities: DON GF and NWCF, which include the respective U.S. Marine Corps (USMC) GF and Navy Working Capital Fund-Marine Corps (NWCF-MC). Effective FY 2006, USMC was deemed a subsidiary reporting entity and therefore has a separate set of subsidiary financial statements that are included in this year's DON Annual Financial Report.

DON General Fund

The DON GF supports overall Departmental operations. Enacted appropriations from Congress comprise the majority of the General Fund account structure, which includes five major appropriation groups:

- Operation and Maintenance
- Military Personnel
- Procurement
- Research, Development, Test, and Evaluation
- Military Construction

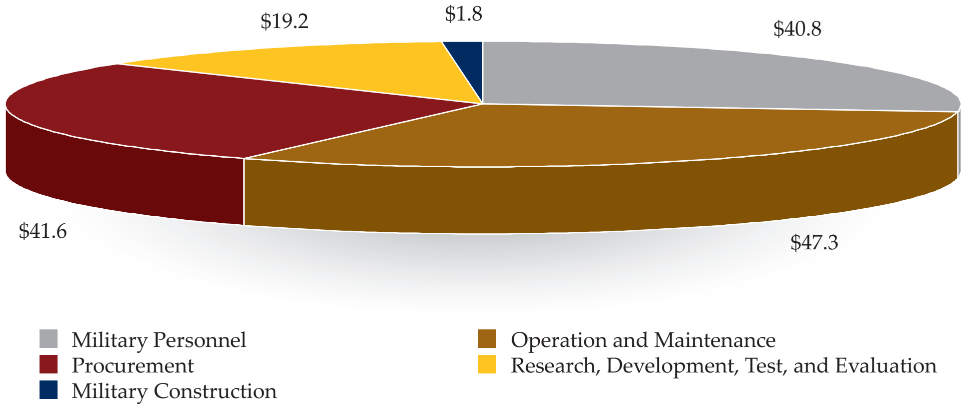
Enacted appropriations from Congress flow through the Office of Management and Budget and the Office of the Secretary of Defense to the Office of the Secretary of the Navy where they are allocated to administering offices and major commands. The administering offices and major commands, which in turn obligate the appropriations to fund operational expenses and capital investments, are required to exercise a system of effective control over financial operations.

Major Sources and Uses of Funds

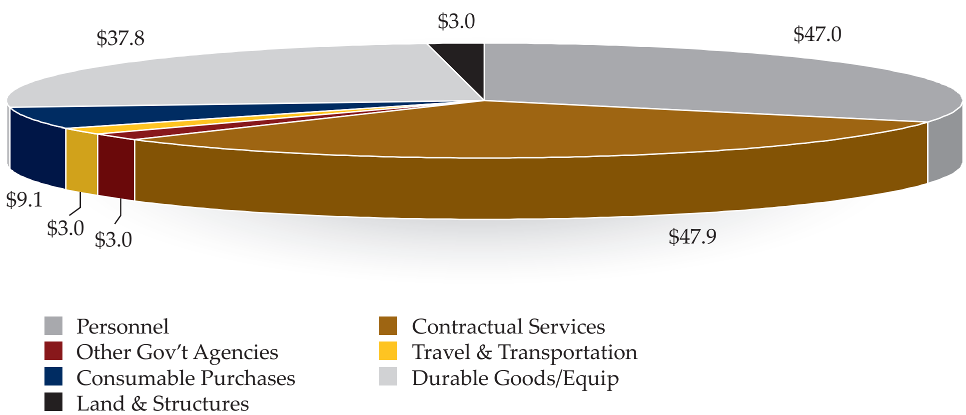
Enacted appropriations increased by $5.2 billion, 4% or a total of $150.8 Billion when compared with FY 2006. The majority of the $5.2 billion increase was in the Operation and Maintenance, and Procurement accounts. Though general categories of funds use remained relatively stable, Contractual Services and Personnel remain the largest groups, followed by Procurement of Durable Goods and Equipment.

More information on DON GF budgetary resources is available in the Combined Statement of Budgetary Resources and Note 20.

DON General Fund Major Sources of Funding in FY 2007 ($ in Billions)



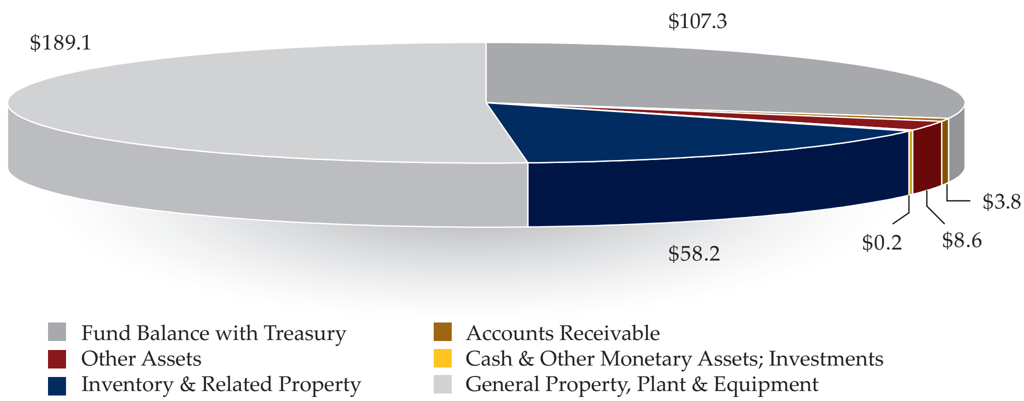
DON General Fund Major Uses of Funding in FY 2007 ($ in Billions)



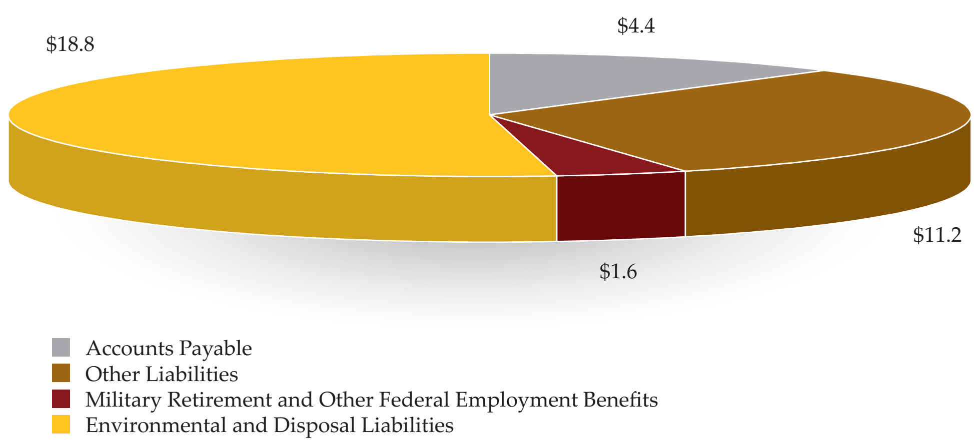
Financial Position

As of September 30, 2007, net position totaled $331.1 billion, which represents an increase of $7.5 billion, or 2%. Changes in General Property, Plant, and Equipment, and Fund Balance with Treasury accounted for the majority of the $12.4 billion overall increase in total assets. Also, changes in Accounts Payable (Intragovernmental and Nonfederal) and Other Liabilities (Nonfederal) accounted for the majority of the $4.8 billion increase in total liabilities.

FY 2007 Total Assets, DON General Fund ($ in Billions)



FY 2007 Total Liabilities, DON General Fund ($ in Billions)



Navy Working Capital Fund

The NWCF is a revolving fund established to meet the diverse requirements of the Navy and Marine Corps operating forces. Under the revolving fund concept, an appropriation or a transfer of funds finances initial NWCF operations. General or appropriated fund payments from customers for goods delivered or services performed subsequently replenish this initial working capital investment and sustain a continuous cycle of operations, minimizing the need for additional annual appropriations by Congress.

The goal of NWCF is to break even over time by matching revenues earned to costs incurred. Achievement of this goal is occasionally complicated by the requirement that NWCF business areas maintain stable budget-driven prices for goods and services, to protect customers from unforeseen price fluctuations.

Navy Working Capital Fund Business Activities By Business Area

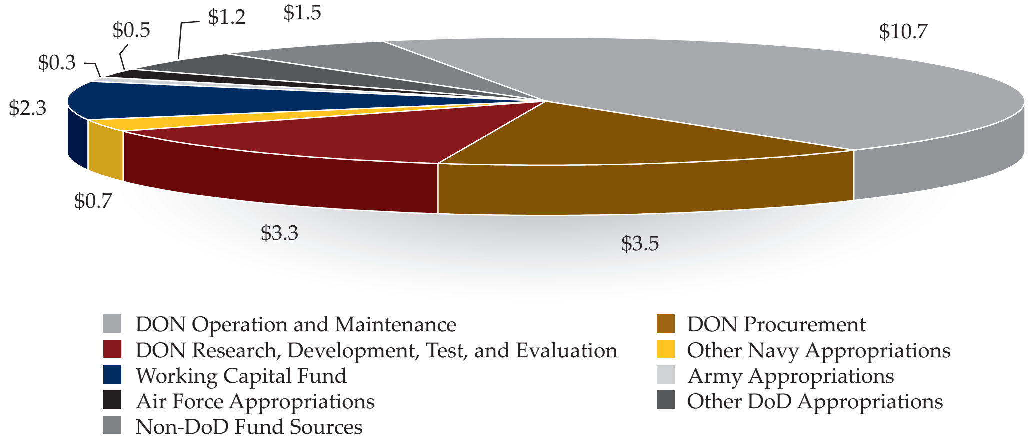
Supply Management	Depot Maintenance
Supply Management, Navy (*https://www.navsup.navy.mil*) Supply Management, Marine Corps (*http://www.logcom.usmc.mil*)	Depot Maintenance, Shipyards (See Note below) (*http://www.navsea.navy.mil*) Depot Maintenance, Aviation (*http://www.navair.navy.mil*) Depot Maintenance, Marine Corps (*http://www.logcom.usmc.mil*)
Base Support	**Transportation**
Facilities Engineering Commands (*https://portal.navfac.navy.mil*) Naval Facilities Engineering Service Centers (*https://portal.navfac.navy.mil*)	Military Sealift Command (*http://www.msc.navy.mil*)
Research and Development	
Naval Research Laboratory* (*http://www.nrl.navy.mil*) Naval Surface Warfare Centers (*http://www.navsea.navy.mil*) Naval Undersea Warfare Centers (*http://www.navsea.navy.mil*)	Naval Air Warfare Centers (*http://www.navair.navy.mil*) Space and Naval Warfare Systems Centers (*http://enterprise.spawar.navy.mil*) *Also see Office of Naval Research (*http://www.onr.navy.mil*)

Note: Depot Maintenance, Shipyards transferred to DON GF effective FY 2007. Any FY 2007 financial data reflects transactions on residual NWCF workload started, but not completed, prior to October 1, 2006.

Major Sources and Uses of Funds

Revenue decreased by $0.1 billion, or 0.5%, and total costs decreased by $0.5 billion, or 2%, between FY 2006 to FY 2007. The decrease in both revenue and costs reflected the net impact of workload changes and the realignment of Depot Maintenance, Shipyards to DON GF. Major sources and uses of funding in FY 2007 are displayed below.

NWCF Major Sources of Funding in FY 2007 ($ in Billions)



Note: Dollar amounts may not match Principal Statements because of intra-Department of Defense eliminations.

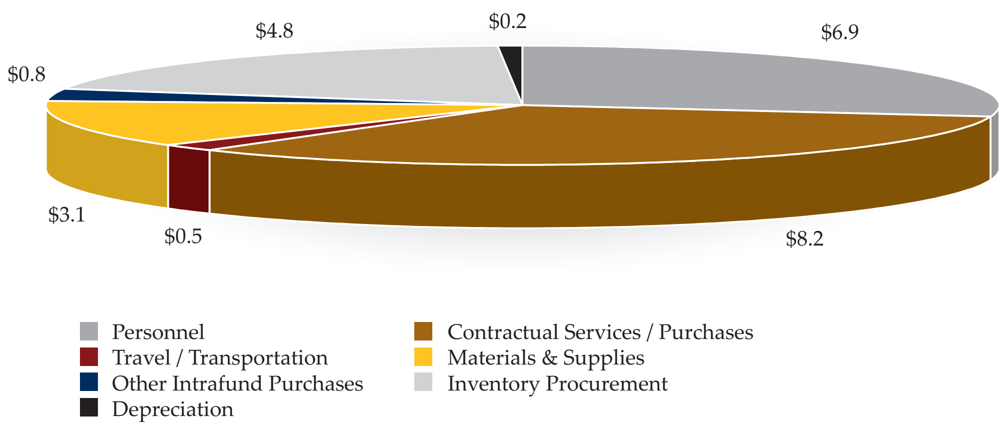
Other Navy Appropriations include the Family Housing appropriation and the National Defense Sealift Fund.

Working Capital Fund data represents revenue earned from NWCF and NWCF-MC as well as from other DoD working capital funds, including the Army, Air Force, and other Defense Agencies.

Other DoD Appropriations include fund sources such as Operation and Maintenance, Defense; Research, Development, Test & Evaluation, Defense; and Defense Procurement appropriations.

Non-DoD Fund Sources include Other Federal and Nonfederal Agencies and Foreign Military Sales customers. Examples of Other Federal Agencies include the State Department, the Department of Homeland Security, and the Coast Guard. Examples of Nonfederal Agencies include state and local governments.

NWCF Major Uses of Funding in FY 2007 ($ in Billions)

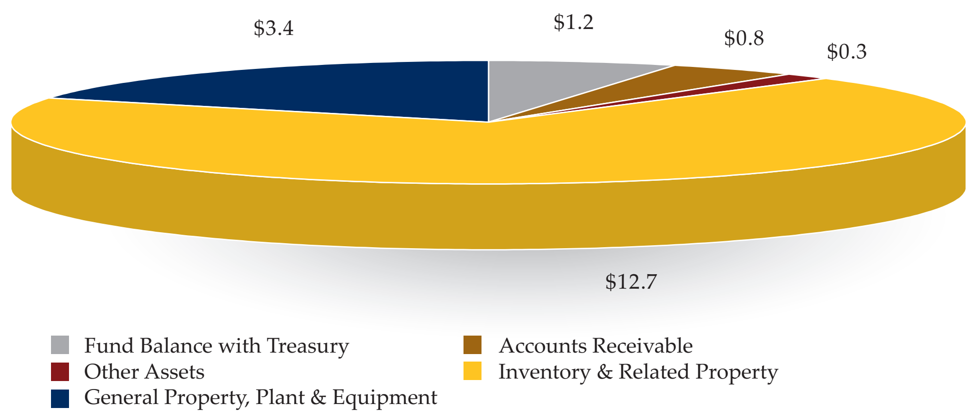


Note: Dollar amounts may not match Principal Statements because of intra-Department of Defense eliminations.

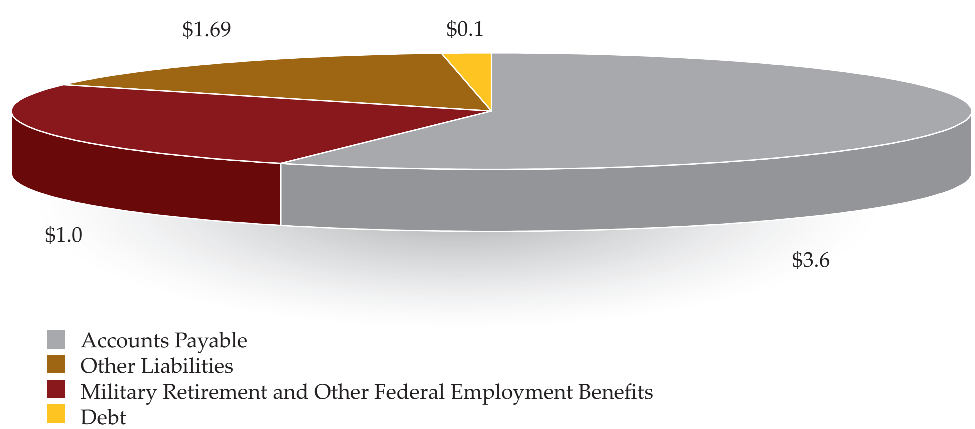
Financial Position

As of September 30, 2007, net position totaled $12.0 billion, which represents a decrease of $1.0 billion, or 7%. A decrease in Inventory and Related Property contributed to the $1.4 billion overall decrease in total assets. Also, a decrease in the actuarial liability for workers' compensation benefits contributed to the $0.4 billion overall decrease in total liabilities.

FY 2007 Total Assets, NWCF ($ in Billions)



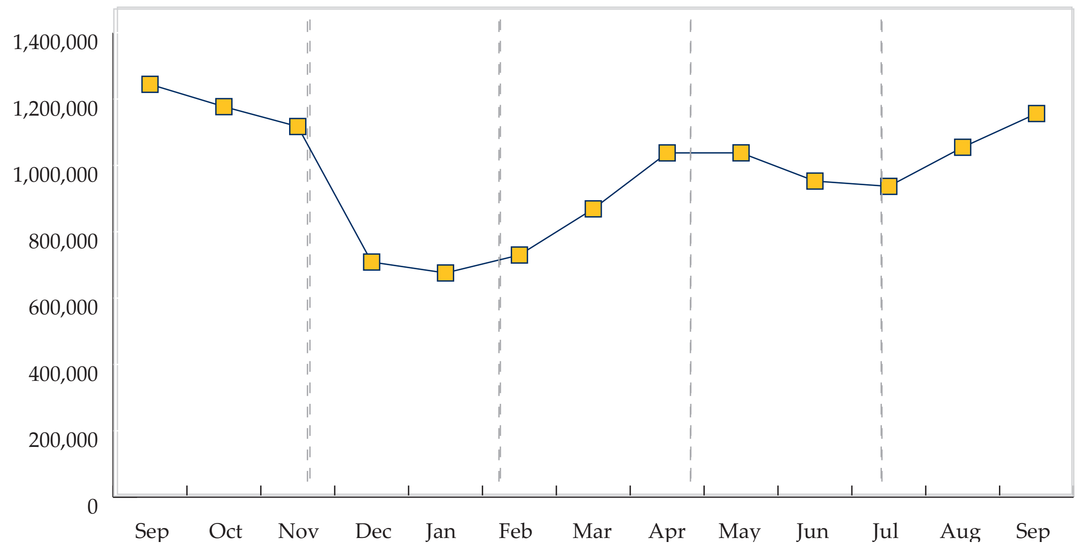
FY 2007 Total Liabilities, NWCF ($ in Billions)



Cash Management

The DON manages working capital fund cash at the Departmental level. It must maintain cash levels at seven to ten days of operational costs, plus have sufficient cash reserves to meet six months of projected capital outlays, as required by the Department of Defense Financial Management Regulation. For FY 2007, the seven-day cash requirement was $770 million and the ten-day requirement was $1.1 billion.

Navy Working Capital Fund Cash Balances
September 30, 2006 to September 30, 2007 ($ in Thousands)



The NWCF finished FY 2007 with an ending cash balance of $1.1 billion. This stabilized balance enables DON to maintain the seven- and ten-day cash metric through FY 2009. Primary contributing factors to the FY 2007 ending cash balance are briefly described below.

- $112.5 million fuel supplemental received from the Defense Logistics Agency, which was subsequently distributed among the following NWCF business activities—Military Sealift Command, Naval Air Warfare Centers, Facilities Engineering Command, Naval Aviation Depots, Naval Undersea Warfare Center, and the Naval Surface Warfare Center.

- $91.0 million paid by the Depot Maintenance, Shipyards to the Treasury Miscellaneous Receipts Account for annual leave liability, as required for their transition from NWCF to DON GF.

- $83.5 million received by Supply Management, Navy for inventory augmentation.

- $32.4 million received by Supply Management, Marine Corps for war reserve materiel.

Cash Management Initiative. A tool was developed to assist with the cash reconciliation process. The tool reconciles NWCF cash balances to the U.S. Treasury; calculates associated journal vouchers to cash; and provides an audit trail. This tool was fully deployed to NWCF activities in January 2007 and was then transitioned to Defense Finance and Accounting Service. This effort was considered a successful Lean Six Sigma Green Belt project. Use of this tool is estimated to reduce the time devoted to reconciliation functions by as much as 40% and aided in the preparation of the FY 2009 DON budget submission.

In addition, during July 2007, NWCF executed an "absolute" cash realignment among business activity groups, resulting in providing these activities with greater visibility and transparency of cash values. This was the first cash rebalancing since 1997.

Finally, a cash management and forecasting tool was deployed to all Industrial activities during FY 2007. The tool was used to support submission of the FY 2009 DON and Office of the Secretary of Defense budgets.

Looking Forward: Fiscal Year 2008 and Beyond

The Navy and Marine Corps must remain prepared at all times to conduct Naval operations at sea. Such traditional priorities as force projection from the sea, supremacy in the littorals, and protection of vital sea lanes will always be our core missions.

- The Honorable Donald C. Winter, Secretary of the Navy, June 2007

Safety will remain a DON priority objective in FY 2008 (see FY 2008 DON objectives at http://www.navy.mil). Pictured above is the Strike Fighter Squadron (VFA) 87, which was among 20 recipients of the DON Safety Excellence Award for 2007.

The DON anticipates U.S. Navy end strength to stabilize at approximately 323,000 by 2011.

The Marine Corps will focus on increasing its active component end strength to 202,000 Marines by 2011.

The DON will continue to invest in several key procurement programs to enhance riverine warfare capabilities.

The Mine Resistant Ambush Protected (MRAP) vehicle will continue to provide deployed Marine units with protection from improvised explosive devices. Pictured above is a variant of the MRAP Joint Explosive Ordnance Disposal Rapid Response Vehicle undergoing the first of four test explosions at the Aberdeen Test Center in Maryland.

A Cooperative Strategy for 21st Century Seapower represents the first time that U.S. maritime forces—the Navy, Marine Corps, and Coast Guard—have collaborated to create a unified maritime strategy. This new enduring strategy will apply maritime power to the crucial responsibility of protecting U.S. vital interests in an increasingly interconnected and uncertain world.

2007

General Fund
Principal Statements

2007 Annual Financial Report
2007 Annual Financial Report 2007 Annual Financial Report

Limitations to the Financial Statements

The principal financial statements have been prepared to report the financial position and results of operations of the entity, pursuant to the requirements of 31 United States Code 3515 (b). While the statements have been prepared from the books and records of the entity in accordance with Generally Accepted Accounting Principles for Federal entities and the formats prescribed by 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.

Principal Statements

The Fiscal Year 2007 Department of the Navy General Fund Principal Statements and related notes are presented in the format prescribed by the Department of Defense Financial Management Regulation 7000.14, Volume 6B. The statements and related notes summarize financial information for individual funds and accounts within the General Fund for the fiscal year ending September 30, 2007, and are presented on a comparative basis with information previously reported for the fiscal year ending September 30, 2006.

The following statements comprise the Department of the Navy General Fund Principal Statements:

- Consolidated Balance Sheet
- Consolidated Statement of Net Cost
- Consolidated Statement of Changes in Net Position
- Combined Statement of Budgetary Resources

The Principal Statements and related notes have been prepared to report financial position pursuant to the requirements of the Chief Financial Officers Act of 1990, as amended by the Government Management Reform Act of 1994. The accompanying notes should be considered an integral part of the Principal Statements.

Department of Defense
Department of the Navy General Fund

CONSOLIDATED BALANCE SHEET

As of September 30, 2007 and 2006
($ in Thousands)

	2007 Consolidated	2006 Consolidated
ASSETS (Note 2)		
Intragovernmental:		
Fund Balance with Treasury (Note 3)		
Entity	$ 106,827,806	$ 95,941,461
Non-Entity Seized Iraqi Cash	0	0
Non-Entity - Other	516,593	474,507
Investments (Note 4)	9,756	9,751
Accounts Receivable (Note 5)	206,091	159,270
Other Assets (Note 6)	400,261	468,259
Total Intragovernmental Assets	107,960,507	97,053,248
Cash and Other Monetary Assets (Note 7)	142,971	176,306
Accounts Receivable, Net (Note 5)	3,613,512	3,231,414
Loans Receivable (Note 8)	0	0
Inventory and Related Property, Net (Note 9)	58,249,650	58,794,634
General Property, Plant and Equipment, Net (Note 10)	189,054,744	186,979,669
Investments (Note 4)	0	0
Other Assets (Note 6)	8,175,144	8,608,875
TOTAL ASSETS	367,196,528	354,844,146
LIABILITIES (Note 11)		
Intragovernmental:		
Accounts Payable (Note 12)	1,495,517	1,035,043
Debt (Note 13)	0	0
Other Liabilities (Note 15 & Note 16)	4,642,819	4,460,153
Total Intragovernmental Liabilities	6,138,336	5,495,196
Accounts Payable (Note 12)	2,948,867	1,265,536
Military Retirement and Other Federal Employment Benefits (Note 17)	1,648,124	1,513,644
Environmental and Disposal Liabilities (Note 14)	18,789,725	17,268,813
Loan Guarantee Liability (Note 8)	0	0
Other Liabilities (Note 15 & Note 16)	6,594,994	5,749,764
TOTAL LIABILITIES	36,120,046	31,292,953
NET POSITION		
Unexpended Appropriations - Earmarked Funds (Note 23)	0	1,550
Unexpended Appropriations - Other Funds	109,221,612	99,697,752
Cumulative Results of Operations - Earmarked Funds	24,258	18,843
Cumulative Results of Operations - Other Funds	221,830,612	223,833,048
TOTAL NET POSITION	331,076,482	323,551,193
TOTAL LIABILITIES AND NET POSITION	$ 367,196,528	$ 354,844,146

The accompanying notes are an integral part of the statements.

Department of Defense

Department of the Navy General Fund

CONSOLIDATED STATEMENT OF NET COST

For the Years Ended September 30, 2007 and 2006

($ in Thousands)

	2007 Consolidated	2006 Consolidated
Program Costs		
Gross Costs	$ 152,141,735	$ 129,530,253
Less: Earned Revenue	(4,375,830)	(3,912,287)
Net Costs	147,765,905	125,617,966
Costs Not Assigned to Programs	0	0
Less: Earned Revenue Not Attributable to Programs	0	0
Net Cost of Operations	$ 147,765,905	$ 125,617,966

The accompanying notes are an integral part of the statements.

Department of Defense
Department of the Navy General Fund

CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION

For the Years Ended September 30, 2007 and 2006
($ in Thousands)

	Earmarked Funds	Other Funds
CUMULATIVE RESULTS OF OPERATIONS		
Beginning Balances	$ 18,843	$ 223,833,048
Prior Period Adjustments:		
Changes in accounting principles (+/-)	0	0
Correction of errors (+/-)	0	0
Beginning Balances, as adjusted	18,843	223,833,048
Budgetary Financing Sources:		
Other adjustments (rescissions, etc) (+/-)	0	0
Appropriations used	1,550	139,860,423
Nonexchange revenue	462	(1)
Donations and forfeitures of cash and cash equivalents	22,172	0
Transfers in/out without reimbursement (+/-)	189	166,000
Other budgetary financing sources (+/-)	0	0
Other Financing Sources:		
Donations and forfeitures of property	0	0
Transfers in/out without reimbursement (+/-)	0	91,282
Imputed financing from costs absorbed by others	0	730,190
Other (+/-)	0	4,896,617
Total Financing Sources	24,373	145,744,511
Net Cost of Operations (+/-)	18,958	147,746,947
Net Change	5,415	(2,002,436)
Cumulative Results of Operations	$ 24,258	$ 221,830,612
UNEXPENDED APPROPRIATIONS		
Beginning Balances	$ 1,550	$ 99,697,751
Prior Period Adjustments (+/-)		
Changes in accounting principles (+/-)	0	0
Correction of errors (+/-)	0	0
Beginning Balances, as adjusted	1,550	99,697,751
Budgetary Financing Sources:		
Appropriations received	0	150,734,232
Appropriations transferred-in/out (+/-)	0	(21,826)
Other adjustments (rescissions, etc) (+/-)	0	(1,328,122)
Appropriations used	(1,550)	(139,860,423)
Total Budgetary Financing Sources	(1,550)	9,523,861
Unexpended Appropriations	0	109,221,612
Net Position	$ 24,258	$ 331,052,224

The accompanying notes are an integral part of the statements.

Department of Defense

Department of the Navy General Fund

CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION

For the Years Ended September 30, 2007 and 2006

($ in Thousands)

	2007 Consolidated	2006 Consolidated
CUMULATIVE RESULTS OF OPERATIONS		
Beginning Balances	$ 223,851,891	$ 192,520,091
Prior Period Adjustments:		
Changes in accounting principles (+/-)	0	0
Correction of errors (+/-)	0	23,218,292
Beginning Balances, as adjusted	223,851,891	215,738,383
Budgetary Financing Sources:		
Other adjustments (rescissions, etc) (+/-)	0	0
Appropriations used	139,861,973	132,896,926
Nonexchange revenue	461	564
Donations and forfeitures of cash and cash equivalents	22,172	18,858
Transfers in/out without reimbursement (+/-)	166,189	50,000
Other budgetary financing sources (+/-)	0	0
Other Financing Sources:		
Donations and forfeitures of property	0	0
Transfers in/out without reimbursement (+/-)	91,282	187,068
Imputed financing from costs absorbed by others	730,190	578,058
Other (+/-)	4,896,617	0
Total Financing Sources	145,768,884	133,731,474
Net Cost of Operations (+/-)	147,765,905	125,617,966
Net Change	(1,997,021)	8,113,508
Cumulative Results of Operations	$ 221,854,870	$ 223,851,891
UNEXPENDED APPROPRIATIONS		
Beginning Balances	$ 99,699,301	$ 89,739,876
Prior Period Adjustments (+/-)		
Changes in accounting principles (+/-)	0	0
Correction of errors (+/-)	0	0
Beginning Balances, as adjusted	99,699,301	89,739,876
Budgetary Financing Sources:		
Appropriations received	150,734,232	145,492,245
Appropriations transferred-in/out (+/-)	(21,826)	617,410
Other adjustments (rescissions, etc) (+/-)	(1,328,122)	(3,253,303)
Appropriations used	(139,861,973)	(132,896,926)
Total Budgetary Financing Sources	9,522,311	9,959,426
Unexpended Appropriations	109,221,612	99,699,302
Net Position	$ 331,076,482	$ 323,551,193

Department of Defense
Department of the Navy General Fund

COMBINED STATEMENT OF BUDGETARY RESOURCES

For the Years Ended September 30, 2007 and 2006
($ in Thousands)

	2007 Combined	2006 Combined
BUDGETARY FINANCING ACCOUNTS		
Budgetary Resources:		
Unobligated balance, brought forward, October 1	$ 20,835,975	$ 17,128,479
Recoveries of prior year unpaid obligations	16,508,300	5,261,990
Budget Authority:		
Appropriations received	150,757,067	145,511,602
Borrowing authority	0	0
Contract authority	0	0
Spending authority from offsetting collections:		
Earned		
Collected	7,690,260	7,767,620
Change in receivables from Federal sources	317,620	(948,730)
Change in unfilled customer orders		
Advances received	50,491	54,329
Without advance from Federal sources	7,319	519,073
Anticipated for rest of year, without advances	0	0
Previously unavailable	0	0
Expenditure Transfers from trust funds	0	0
Subtotal	158,822,757	152,903,894
Nonexpenditure Transfers, net, anticipated and actual	144,174	667,410
Temporarily not available pursuant to Public Law	0	0
Permanently not available	(1,328,122)	(3,253,303)
Total Budgetary Resources	194,983,084	172,708,470
Status of Budgetary Resources:		
Obligations incurred:		
Direct	163,297,807	146,006,781
Reimbursable	7,750,730	5,865,715
Subtotal	171,048,537	151,872,496
Unobligated balance:		
Apportioned	21,765,826	19,197,595
Exempt from apportionment	0	0
Subtotal	21,765,826	19,197,595
Unobligated balances not available	2,168,721	1,638,379
Total Status of Budgetary Resources	$ 194,983,084	$ 172,708,470

The accompanying notes are an integral part of the statements.

Department of Defense

Department of the Navy General Fund

COMBINED STATEMENT OF BUDGETARY RESOURCES

For the Years Ended September 30, 2007 and 2006

($ in Thousands)

	2007 Combined	2006 Combined
RELATIONSHIP OF OBLIGATIONS TO OUTLAYS		
Change in Obligated Balance:		
Obligated balance, net		
Unpaid obligations, brought forward, October 1	$ 78,088,020	$ 72,093,186
Less: Uncollected customer payments from Federal sources, brought forward, October 1	(2,971,157)	(3,400,814)
Total Unpaid Obligated Balance	75,116,863	68,692,372
Obligations incurred, net (+/-)	171,048,537	151,872,496
Less: Gross outlays	(146,437,179)	(140,615,673)
Obligated balance transferred, net		
Actual transfers, unpaid obligations (+/-)	0	0
Actual transfers, uncollected customer payments from Federal sources (+/-)	0	0
Total Unpaid Obligated Balance Transferred, net	0	0
Less: Recoveries of prior year unpaid obligations, actual	(16,508,300)	(5,261,990)
Change in uncollected customer payments from Federal sources (+/-)	(324,938)	429,657
Obligated balance, net, end of period		
Unpaid obligations	86,191,077	78,088,020
Less: Uncollected customer payments from Federal sources	(3,296,095)	(2,971,157)
Total Unpaid Obligated Balance, net, end of period	82,894,982	75,116,863
Net Outlays:		
Gross Outlays	146,437,179	140,615,673
Less: Offsetting collections	(7,740,753)	(7,821,950)
Less: Distributed Offsetting receipts	(270,572)	(149,284)
Net Outlays	$ 138,425,854	$ 132,644,439

The accompanying notes are an integral part of the statements.

2007

General Fund

Notes to the Principal Statements

2007 Annual Financial Report

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Note 1. Significant Accounting Policies

1.A. Basis of Presentation

These financial statements have been prepared to report the financial position and results of operations of the Department of the Navy (DON) General Fund (GF), as required by the Chief Financial Officers (CFO) Act of 1990, expanded by the Government Management Reform Act (GMRA) of 1994, and other appropriate legislation. The financial statements have been prepared from the books and records of DON GF in accordance with the "Department of Defense (DoD) Financial Management Regulation," the Office of Management and Budget (OMB) Circular A-136, "Financial Reporting Requirements," and to the extent possible, generally accepted accounting principles (GAAP). Effective 4th Quarter, Fiscal Year (FY) 2007, DON GF no longer publishes consolidating/combining financial statements. The accompanying financial statements account for the resources for which DON GF is responsible to report within the context of current DoD reporting policy.

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

The DON GF is unable to fully implement all elements of GAAP and the OMB Circular A-136 due to limitations of its financial and nonfinancial management processes and systems that feed into the financial statements. The DON GF derives its reported values and information for major asset and liability categories largely from nonfinancial systems, such as inventory and logistic systems. These systems were designed to support reporting requirements for maintaining accountability over assets and reporting the status of federal appropriations rather than preparing financial statements in accordance with GAAP. The DON GF continues to implement process and system improvements addressing these limitations.

The DoD currently has several auditor identified financial statement material weaknesses including those for financial management systems, intragovernmental eliminations, and unsupported accounting entries. Of the DoD reported material weaknesses, the DON has the following: (1) Fund Balance with Treasury, (2) completeness of general equipment, (3) real property, (4) valuation of operating materiels and supplies, (5) military equipment reporting, (6) accuracy and complete reporting of accounts payable, and (7) identifying and reporting environmental disposal liabilities.

FY 2007 represents the twelfth year that DON GF has prepared financial statements pursuant to the CFO Act and GMRA.

1.B. Mission of the Reporting Entity

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

1.C. Appropriations and Funds

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

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

Working capital funds, or revolving funds, receive funding to establish an initial corpus through an appropriation or a transfer of resources from existing appropriations or funds. The corpus finances operations and transactions that flow through the fund. The revolving fund resources the goods and services sold to customers on a reimbursable basis and maintains the corpus. Reimbursable receipts replenish the corpus and generally are available in their entirety for use without further congressional action. At various times, Congress provides additional appropriations to supplement the revolving fund as an infusion of cash when revenues are inadequate to cover costs within the corpus. The National Defense Sealift Fund is DON GF's only revolving fund.

Trust funds contain receipts and expenditures of funds held in trust by the government for use in carrying out specific purposes or programs in accordance with the terms of the donor, trust agreement, or statute. Certain trust and special funds may be designated as earmarked funds. Earmarked funds are financed by specifically identified revenues, required by statute to be used for designated activities, benefits or purposes, and remain available over time. Earmarked funds also have a requirement to account for and report on the receipt, use, and retention of revenues and other financing sources that distinguish them from general revenues.

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

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

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

The DON GF is a party to allocation transfers as the child from the EOP for the Foreign Military Financing Program, as well as for the International Military Education and Training program. These funds meet the OMB exception; however, activities for these funds are reported in the DoD financial statements, not the DON's. The DON GF also receives allocation transfers, as the child, from the U.S. Forest Service and the Federal Highway Administration and reports financial activity for those funds to the parent.

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

Entity Accounts:

General Accounts

17 X 0380	Coastal Defense Augmentation, Navy
17 0703	Family Housing, Navy and Marine Corps
17 0730	Family Housing Construction, Navy and Marine Corps
17 0735	Family Housing Operation and Maintenance, Navy and Marine Corps
17 X 0810	Environmental Restoration, Navy
17 1000	Medicare Eligible Retiree Health Care Fund, Military Personnel Navy
17 1001	Medicare Eligible Retiree Health Care Fund, Military Personnel Marine Corps
17 1002	Medicare Eligible Retiree Health Care Fund, Reserve Personnel Navy
17 1003	Medicare Eligible Retiree Health Care Fund, Reserve Personnel Marine Corps
17 1105	Military Personnel, Marine Corps

17	1106	Operation and Maintenance, Marine Corps
17	1107	Operation and Maintenance, Marine Corps Reserve
17	1108	Reserve Personnel, Marine Corps
17	1109	Procurement, Marine Corps
17	1205	Military Construction, Navy and Marine Corps
17	1235	Military Construction, Navy Reserve
17	1236	Payments to Kaho Olawe Island Conveyance, Remediation and Environmental Restoration Fund, Navy
17	1319	Research, Development, Test and Evaluation, Navy
17	1405	Reserve Personnel, Navy
17	1453	Military Personnel, Navy
17	1506	Aircraft Procurement, Navy
17	1507	Weapons Procurement, Navy
17	1508	Procurement of Ammunition, Navy and Marine Corps
17	1611	Shipbuilding and Conversion, Navy
17	1804	Operation and Maintenance, Navy
17	1806	Operation and Maintenance, Navy Reserve
17	1810	Other Procurement, Navy

Revolving Funds

17 X 4557	National Defense Sealift Fund, Navy

Earmarked Trust Funds

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

Earmarked Special Funds

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

General Fund Receipt, Deposit, Suspense, and Clearing Accounts

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

Parent-Child (Allocation) Transfer Accounts

17 11 1081	International Military Education and Training Funds, appropriated to the President
17 11 X1081	International Military Education and Training Funds, appropriated to the President
17 11 1082	Foreign Military Financing Program Funds, appropriated to the President
17 12 X1105B	State and Private Forestry, Forest Service
17 69 X 8083	Federal-Aid Highways (Liquidation of Contract Authorization), Federal Highway Administration

1.D. Basis of Accounting

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

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

In addition, DoD policy requires identification of program costs based upon the major appropriation groups provided by the Congress. Current processes and systems do not capture and report accumulated costs for major programs based upon the performance measures as required by the Government Performance and Results Act. The DoD reporting entities are working towards a cost reporting methodology that meets the need for cost information required by the Statement of Federal Financial Accounting Standard (SFFAS) No. 4, "Managerial Cost Accounting Concepts and Standards for the Federal Government."

1.E. Revenues and Other Financing Sources

The DON GF receives congressional appropriations as financing sources on either an annual or multi-year basis. When authorized by legislation, these appropriations are supplemented by revenues generated by sales of goods or services. The DON GF recognizes revenue as a result of costs incurred for goods or services provided to other federal agencies and the public. The price charged for goods and services furnished by DON GF depends on whether that good or service is provided to, or for the benefit of, a DoD Component, a non-DoD federal agency, a private party, or a foreign military sales customer. Full cost pricing is DON GF's standard policy for services provided as required by OMB Circular A-25, "User Charges." The DON GF recognizes revenue when earned within the constraints of current system capabilities. In some instances, revenue is recognized when bills are issued.

The DON GF does not include nonmonetary support provided by U.S. allies for common defense and mutual security in amounts reported in the Statement of Net Cost and the Note 21, "Reconciliation of Net Cost of Operations to Budget." The U.S. has cost sharing agreements with other countries. Examples include countries where there is a mutual or reciprocal defense agreement, where U.S. troops are stationed, or where the U.S. Fleet is in a port.

1.F. Recognition of Expenses

For financial reporting purposes, DoD policy requires the recognition of operating expenses in the period incurred. However, because DON's GF financial and nonfinancial feeder systems were not designed to collect and record financial information on the full accrual accounting basis, accruals are made for major items such as payroll expenses, accounts payable, environmental liabilities, and unbilled revenue. In the case of Operating Materiels and Supplies (OM&S), operating expenses are initially recognized when the items are purchased. Subsequent adjustments to operating expenses are recognized when OM&S is recorded as an asset or consumed in operations. Efforts are underway to transition towards the consumption method for recognizing OM&S expenses.

1.G. Accounting for Intragovernmental Activities

At the U.S. government level, preparation of reliable government wide financial statements requires the elimination of transactions occurring among sub-entities within a reporting entity, and between two or more federal agencies. However, DON GF cannot accurately identify all intragovernmental transactions by customer because DON's GF systems do not track the necessary detail at the transaction level. For the DON GF, balances between sub-entities are eliminated prior to the preparation of the DON GF financial statements. Generally, seller entities within DoD provided summary seller-side balances for revenue, accounts receivable, and unearned revenue to the buyer-side internal DoD accounting offices. In most cases, the buyer-side records are adjusted to agree with DoD seller-side balances. Intra-DoD intragovernmental balances are then eliminated for the DoD financial statements. The volume of intragovernmental transactions is so large that after-the-fact reconciliation cannot be accomplished effectively with existing or foreseeable resources. The DoD is developing long-term system improvements to ensure accurate intragovernmental information and to include sufficient up-front edits and controls eliminating the need for after-the-fact reconciliations.

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

The DoD's proportionate share of public debt and related expenses of the Federal Government is not included. The Federal Government does not apportion debt and its related costs to federal agencies. The DoD reporting entities' financial statements, therefore, do not report any portion of the public debt or interest thereon, nor do the statements report the source of public financing whether from issuance of debt or tax revenues.

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

1.H. Transactions with Foreign Governments and International Organizations

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

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

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

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

1.J. Foreign Currency

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

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

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

1.K. Accounts Receivable

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

1.L. Direct Loans and Loan Guarantees

Not applicable.

1.M. Inventories and Related Property

Related property is comprised of Operating Materiels and Supplies (OM&S). The DON GF uses both the consumption method and the purchase method of accounting for OM&S. Items that are centrally managed and stored, such as ammunition and engines, are generally recorded using the consumption method and are reported on the Balance Sheet as an asset. When current systems cannot fully support the consumption method, DON GF uses the purchase method. Under the purchase method, materiels and supplies are not recorded as an asset, but rather, are expensed when purchased. During FY 2007, DON GF expensed significant amounts using the purchase method because the systems could not support the consumption method or management deemed that the item was in the hands of the end user. This is a material weakness for DoD and DON GF and systems are under development to correct this weakness. Once the proper systems are in place, these items will be accounted for using the consumption method of accounting.

The DON GF values OM&S assets using several valuation methods. Most OM&S is valued at an approximation of historical cost using latest acquisition cost adjusted for holding gains and losses. The latest acquisition cost method is used because legacy logistics systems were designed for materiel management rather than accounting purposes. Although these systems provide visibility and accountability over inventory and related property items, they do not maintain historical cost data necessary to comply with SFFAS No. 3, "Accounting for Inventory and Related Property." Additionally, these legacy inventory systems cannot produce financial transactions using the USSGL, as required by the Federal Financial Management Improvement Act of 1996 (P.L. 104-208). By utilizing new systems development processes, DON is continuing to transition the balance of the OM&S to the moving average cost method. However, since the on-hand balances which were transitioned were not, for the most part, baselined to auditable historical cost, the reported values remain noncompliant with SFFAS No. 3 and GAAP.

The DON GF manages only military or government specific materiel under normal conditions. Materiel is a unique term that relates to military force management, and includes items such as weapons system spare parts and repair parts necessary to equip, operate, maintain, and support military activities without distinction as to its application for administrative or combat purposes. Items commonly used in and available from the commercial sector are not managed in DON GF materiel management activities. Operational cycles are irregular and the military risks associated with stock-out positions have no commercial parallel. The DON GF holds materiel based on military need and support for contingencies.

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

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

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

For the trust funds, DON GF reports investments in U.S. Treasury securities at cost, net of amortized premiums or discounts. Premiums or discounts are amortized over the term of the investment using the effective interest rate method or another method obtaining similar results. The DON GF's intent is to hold investments to maturity. Consequently, a provision is not made for unrealized gains or losses on these securities.

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

1.O. General Property, Plant, and Equipment

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

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

In FY 2006, DoD revised the real property capitalization threshold from $100 thousand to $20 thousand. The DON GF has not implemented the $20 thousand real property capitalization threshold, pending an evaluation of real property systems, processes, and procedures that will have to be revised in order to implement the lowered threshold. The current $100 thousand capitalization threshold remains unchanged for the remaining General Property, Plant, and Equipment (PP&E) categories.

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

General PP&E previously capitalized at amounts below $100 thousand were written off DON GF financial statements in FY 1998.

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

The DoD is developing new policies and a contractor reporting process for Government Furnished Equipment that will provide appropriate General PP&E information for future financial statement reporting purposes. Currently, not all DON GF government property in the possession of contractors is maintained in DON's property systems or reported on the balance sheet. The DoD has issued new property accountability and reporting requirements that require DoD components to maintain, in their property systems, information on all property furnished to contractors. This action and other proposed actions are structured to capture and report the information necessary for compliance with Federal accounting standards.

1.P. Advances and Prepayments

The DoD policy is to record advances and prepayments in accordance with GAAP. As such, payments made in advance of the receipt of goods and services are to be reported as an asset on the Balance Sheet. The DoD policy is to expense and/or properly classify assets when the related goods and services are subsequently received. Due to system limitations, not all DON GF advances and prepayments are properly classified as assets when payment is made in advance of the receipt of goods and services.

1.Q. Leases

Lease payments for the rental of equipment and operating facilities are classified as either capital or operating leases. The DON GF currently has no capital leases. An operating lease does not substantially transfer all of the benefits or risks of ownership. Payments for operating leases are charged to expense over the lease term as it becomes payable.

Office space leases entered into by DON GF are the largest component of operating leases. These costs were gathered from existing leases, General Service Administration (GSA) bills, and Interservice Support Agreements. Future year projections use the Consumer Price Index (CPI) rather than the DoD inflation factor. The CPI impacts increases to the leases, especially those at commercial lease sites. Equipment leases have a variety of lease terms, which are not expected to be renewed upon expiration. Other operating leases are generally one-year leases.

1.R. Other Assets

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

The DON GF conducts business with commercial contractors under two primary types of contracts: fixed price and cost reimbursable. To alleviate the potential financial burden on the contractor that long-term contracts can cause, DON GF may provide financing payments. Contract financing payments are defined in the Federal Acquisition Regulations, Part 32, as authorized disbursements of monies to a contractor prior to acceptance of supplies or services by the Government. Contract financing payments clauses are incorporated in the contract terms and conditions and may include advance payments, performance-based payments, commercial advance and interim payments, progress payments based on cost, and interim payments under certain cost-reimbursement contracts.

Contract financing payments do not include invoice payments, payments for partial deliveries, lease and rental payments, or progress payments based on a percentage or stage of completion, which the Defense Federal Acquisition Regulation Supplement authorizes only for construction of real property, shipbuilding, and ship conversion, alteration, or repair. Progress payments for real property are reported as Construction in Progress. It is DoD policy to record certain contract financing payments as Other Assets.

1.S. Contingencies and Other Liabilities

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

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

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

1.T. Accrued Leave

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

1.U. Net Position

Net Position consists of unexpended appropriations and cumulative results of operations. Unexpended Appropriations represent the amounts of authority that are unobligated and have not been rescinded or withdrawn. Unexpended appropriations also represent amounts obligated for which legal liabilities for payments have not been incurred. Cumulative Results of Operations represent the net difference, since inception of an activity, between expenses and losses and financing sources (including appropriations, revenue, and gains). Beginning with FY 1998, the cumulative results also include donations and transfers in and out of assets without reimbursement.

1.V. Treaties for Use of Foreign Bases
The DON has the use of land, buildings, and other overseas facilities that are obtained through various international treaties and agreements negotiated by the Department of State. The DON purchases capital assets overseas with appropriated funds; however, the host country retains title to land and improvements. Generally, treaty terms allow DON continued use of these properties until the treaties expire. In the event treaties or other agreements are terminated, whereby use of the foreign bases is prohibited, losses are recorded for the value of any nonretrievable capital assets. The settlement due to the U.S. or host nation is negotiated and takes into account the value of capital investments and may be offset by the cost of environmental cleanup. The DON GF does not recognize imputed costs or imputed financing for overseas facilities.

1.W. Comparative Data
Not applicable.

1.X. Unexpended Obligations
The DON GF obligates funds to provide goods and services for outstanding orders not yet delivered. The financial statements do not reflect this liability for payment for goods and services not yet delivered, unless title passes.

1.Y. Undistributed Disbursements and Collections
Undistributed disbursements and collections represent the difference between disbursements and collections matched at the transaction level to a specific obligation, payable, or receivable in the fund holder's accounting records as opposed to those reported by the U.S. Treasury. These amounts should agree with the undistributed amounts reported on the monthly accounting reports. In-transit payments are those payments that have been made by other agencies or entities that have not been recorded in the DON's GF accounting records. These payments are applied to the DON's GF outstanding accounts payable balance. In-transit collections are those collections from other agencies or entities that have not been recorded in the DON's GF accounting records. These collections are applied to accounts receivable.

The DoD policy is to allocate supported undistributed disbursements and collections between federal and nonfederal categories based on the percentage of distributed federal and nonfederal accounts payable and accounts receivable. Unsupported undistributed disbursements are recorded in accounts payable. Unsupported undistributed collections are recorded in other liabilities.

1.Z. Significant Events
Beginning 4th Quarter, FY 2007, DoD reporting entities began presenting the Statement of Financing (SOF) as a note in accordance with OMB Circular A-136. The SOF will no longer be considered a basic statement and is now referred to as "Reconciliation of Net Cost of Operations to Budget."

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

Note 2. Nonentity Assets

As of September 30		2007		2006
(Amounts in Thousands)				
1. Intragovernmental Assets				
A. Fund Balance with Treasury	$	516,593	$	474,507
B. Accounts Receivable		0		0
C. Total Intragovernmental Assets	$	516,593	$	474,507
2. Nonfederal Assets				
A. Cash and Other Monetary Assets	$	142,971	$	176,306
B. Accounts Receivable		3,303,128		3,142,047
C. Other Assets		0		0
D. Total Nonfederal Assets	$	3,446,099	$	3,318,353
3. Total Nonentity Assets	$	3,962,692	$	3,792,860
4. Total Entity Assets	$	363,233,836	$	351,051,286
5. Total Assets	$	367,196,528	$	354,844,146

Standard Disclosures
Nonentity assets are assets for which Department of the Navy (DON) maintains stewardship accountability and responsibility to report, but are not available for DON's normal operations.

Intragovernmental Fund Balance with Treasury
This nonentity asset category represents amounts in DON's deposit fund accounts such as the savings plans that were established by Congress to benefit deployed sailors and Marines, receipts fund accounts such as Fines, Penalties, and Forfeitures that are used to temporarily hold amounts until they are remitted to the U.S. Treasury, and certain suspense accounts such as the Uniformed Services Thrift Savings Plan. Amounts in deposit, receipt, and suspense accounts are not available for DON's use in normal operations.

Cash and Other Monetary Assets
This nonentity asset category represents disbursing officers' cash, foreign currency, and undeposited collections as reported on the Disbursing Officer's Statement of Accountability. These assets are held by DON disbursing officers as agents of the U.S. Treasury and are not available for DON's use in normal operations.

Nonentity Nonfederal Accounts Receivable (Public)
The primary component of nonentity accounts receivable is an advance payment made to a contractor, and associated accrued interest, which remains in litigation. These receivable balances are being reported in nonentity accounts receivable since the original appropriation year has been cancelled, and any funds collected as a result of this litigation would be remitted to the U.S. Treasury.

Note 3. Fund Balance with Treasury

As of September 30		2007		2006
(Amounts in Thousands)				
1. Fund Balances				
A. Appropriated Funds	$	105,133,424	$	93,541,772
B. Revolving Funds		1,678,815		2,387,470
C. Trust Funds		13,182		9,917
D. Special Funds		2,385		2,302
E. Other Fund Types		516,593		474,507
F. Total Fund Balances	$	107,344,399	$	96,415,968
2. Fund Balances Per Treasury Versus Agency				
A. Fund Balance per Treasury	$	108,480,114	$	97,613,850
B. Fund Balance per DON		107,344,399		96,415,968
3. Reconciling Amount	$	1,135,715	$	1,197,882

Standard Disclosures
The total reconciling amount of $1.1 billion in Fund Balance with Treasury (FBWT) is primarily due to cancelled appropriations and unavailable receipt accounts. Cancelled appropriations and unavailable receipt accounts are not available as of the end of the reporting period; therefore, excluded from DON's FBWT but remained in fund balance reported by Treasury.

Other Fund Types (Line 1.E) consists primarily of amounts in the following deposit and receipt accounts: Pay of the Navy Deposit Fund, Pay of the Marine Corps Deposit Fund, and Withheld State and Local Taxes.

Status of Fund Balance with Treasury

As of September 30		2007		2006
(Amounts in Thousands)				
1. Unobligated Balance				
A. Available	$	21,765,826	$	19,197,595
B. Unavailable		2,168,721		1,638,379
2. Obligated Balance not yet Disbursed		86,191,076		78,088,020
3. Nonbudgetary FBWT		524,455		472,698
4. NonFBWT Budgetary Accounts		(3,305,679)		(2,980,724)
5. Total	$	107,344,399	$	96,415,968

Standard Disclosures
The Status of FBWT consists of obligated and unobligated balances. These balances reflect the budgetary authority remaining for disbursements against current or future obligations.

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

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

Non-Budgetary FBWT includes entity and nonentity FBWT accounts that do not have budgetary authority, such as unavailable receipt accounts or clearing accounts. For DON General Fund (GF), Non-Budgetary FBWT consists of balances in receipt accounts and clearing accounts.

Non-FBWT Budgetary Accounts represent adjustments to budgetary accounts that do not affect FBWT. For DON GF, Non-FBWT Budgetary Accounts include Trust Fund investments in U.S. Treasury securities, unfilled customer orders without advance, and reimbursements receivable. This category reduces the Status of FBWT.

Unobligated balances are segregated to show available and unavailable amounts in the note schedule. Unobligated, Unavailable balances are restricted to future use and are not apportioned for current use.

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

Disclosures Related to Suspense/Budget Clearing Accounts

As of September 30	2005	2006	2007	(Decrease)/ Increase from FY 2006 - 2007
(Amounts in Thousands)				
Account				
F3845 – Personal Property Proceeds	$ 0	$ 0	$ 0	$ 0
F3875 – Disbursing Officer Suspense	(27,725)	72	6,412	6,340
F3880 – Lost or Cancelled Treasury Checks	3,946	3,378	1,765	(1,613)
F3882 – Uniformed Services Thrift Savings Plan Suspense	32,891	46,500	50,154	3,654
F3885 – Interfund/IPAC Suspense	(53,025)	(5,260)	(314)	4,946
F3886 – Thrift Savings Plan Suspense	429	(28)	(64)	(36)
Total	$ (43,484)	$ 44,662	$ 57,953	$ 13,291

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

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

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

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

Disclosures Related to Problem Disbursements and In-Transit Disbursements

As of September 30	2005	2006	2007	(Decrease)/ Increase from FY 2006 to 2007
(Amounts in Thousands)				
1. Total Problem Disbursements, Absolute Value				
A. Unmatched Disbursements (UMDs)	$ 1,313,996	$ 984,547	$ 832,273	$ (152,274)
B. Negative Unliquidated Obligations (NULO)	17,086	15,396	9,840	(5,556)
C. In-Transit Disbursements	551,540	554,690	737,572	182,882
Total	$ 1,882,622	$ 1,554,633	$ 1,579,685	$ 25,052

Standard Disclosures

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

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

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

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

Starting 2nd Quarter, FY 2007, in-transit disbursements are reported as absolute value as opposed to net amounts disclosed in prior years. This reporting change applies to amounts in the note schedule for both the current and comparative years.

Note 4. Investments and Related Interest

As of September 30	2007								
		Cost	Amortization Method		Amortized (Premium) / Discount		Investments, Net		Market Value Disclosure
(Amounts in Thousands)									
1. Intragovernmental Securities									
A. Nonmarketable, Market-Based									
1. Military Retirement Fund	$	0		$	0	$	0	$	0
2. Medicare Eligible Retiree Health Care Fund		0			0		0		0
3. US Army Corps of Engineers		0			0		0		0
4. Other Funds		9,630			(14)		9,616		9,657
5. Total Nonmarketable, Market-Based		9,630			(14)		9,616		9,657
B. Accrued Interest		140					140		140
C. Total Intragovernmental Securities	$	9,770		$	(14)	$	9,756	$	9,797
2. Other Investments									
A. Total Investments	$	0		$	0	$	0		N/A

As of September 30	2006								
		Cost	Amortization Method		Amortized (Premium) / Discount		Investments, Net		Market Value Disclosure
(Amounts in Thousands)									
1. Intragovernmental Securities									
A. Nonmarketable, Market-Based									
1. Military Retirement Fund	$	0		$	0	$	0	$	0
2. Medicare Eligible Retiree Health Care Fund		0			0		0		0
3. US Army Corps of Engineers		0			0		0		0
4. Other Funds		9,633			(23)		9,610		9,610
5. Total Nonmarketable, Market-Based		9,633			(23)		9,610		9,610
B. Accrued Interest		141					141		141
C. Total Intragovernmental Securities	$	9,774		$	(23)	$	9,751	$	9,751
2. Other Investments									
A. Total Investments	$	0		$	0	$	0		N/A

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

Other Funds (Line 1.A.4) represents DON Trust Fund holdings in interest-bearing securities for the Naval Academy General Gift Fund and the Navy General Gift Fund. These investments are Nonmarketable Market-Based U.S. Treasury securities reported at cost, net of amortized premiums and discounts. In accordance with the Statement of Federal Financial Accounting Standards No. 27, "Identifying and Reporting Earmarked Funds," DON Trust Funds are classified and reported as earmarked funds.

Note 5. Accounts Receivable

As of September 30	2007			2006
	Gross Amount Due	Allowance For Estimated Uncollectibles	Accounts Receivable, Net	Accounts Receivable, Net
(Amounts in Thousands)				
1. Intragovernmental Receivables	$ 206,091	N/A	$ 206,091	$ 159,270
2. Nonfederal Receivables (From the Public)	$ 3,628,112	$ (14,600)	$ 3,613,512	$ 3,231,414
3. Total Accounts Receivable	$ 3,834,203	$ (14,600)	$ 3,819,603	$ 3,390,684

Aged Accounts Receivable

As of September 30	2007				2006			
	Intragovernmental		Nonfederal		Intragovernmental		Nonfederal	
(Amounts in Thousands)								
CATEGORY								
Nondelinquent								
Current	$	387,831	$	518,742	$	381,172	$	535,983
Noncurrent		29,655		(1,573)		30,402		7,549
Delinquent								
1 to 30 days	$	17,579	$	10,410	$	2,188	$	7,022
31 to 60 days		5,321		4,928		1,101		4,737
61 to 90 days		785		13,781		1,150		9,687
91 to 180 days		3,928		48,514		7,409		10,598
181 days to 1 year		407		51,844		5,821		26,743
Greater than 1 year and less than or equal to 2 years		355		35,641		2,085		44,235
Greater than 2 years and less than or equal to 6 years		5,430		35,643		31,745		58,556
Greater than 6 years and less than or equal to 10 years		228		376,441		259		362,476
Greater than 10 years		0		2,679,506		0		2,605,292
Subtotal	$	451,519	$	3,773,877	$	463,332	$	3,672,878
Less Supported Undistributed Collections		(148,319)		(145,765)		(257,152)		(434,700)
Less Eliminations		(97,109)		0		(46,910)		0
Less Other		0		0		0		0
Total	$	206,091	$	3,628,112	$	159,270	$	3,238,178

Information Related to Aged Accounts Receivable

Nondelinquent accounts receivable consists of receivables outstanding for 30 days or less or those not yet due under the contract or billing document pertaining to the receivable. Current nondelinquent accounts receivable are those that are due in the next twelve months. Noncurrent nondelinquent accounts receivable include out-of-service debt that is due beyond the next twelve months. These accounts are not considered delinquent since the associated repayment schedules allow for repayment after a 30-day period. Noncurrent nondelinquent reflects an abnormal balance of $1.6 million for FY 2007. This abnormal balance was reported by DFAS Japan and is related to the reimbursement of foreign national labor in yen by the Japanese government. The abnormal balance is expected to be cleared in 1st Quarter, FY 2008, pending a more favorable exchange rate, by transferring the foreign currency gain to the foreign currency fluctuation account. The Department of the Navy (DON) is actively pursuing collection action on all accounts receivable, both public and intragovernmental, in accordance with guidance in the Department of Defense Financial Management Regulation, Volume 4, Chapter 3, and Office of Management and Budget Circular A-129, "Policies for Federal Credit Programs and Non-Tax Receivables."

For public debt, these collection actions include referring delinquent vendor debt to the Debt Management Office (DMO) for servicing no later than 60 days after the payment due date, and coordinating with DMO to further refer such debt over 180 days delinquent to Treasury for further collection action. A current example of collection actions related to public debt is a partnership between DON and Defense Finance and Accounting Service (DFAS) to identify habitually delinquent public entities and develop standard processes with a goal of improving the joint business relationship. For delinquent intragovernmental debt, collection actions include detailed research of subsidiary accounting transactions with DFAS, the compilation and review of dispute packages, and consultation and negotiation with debtor agencies to resolve outstanding receivables.

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

Note 6. Other Assets

As of September 30	2007	2006
(Amounts in Thousands)		
1. Intragovernmental Other Assets		
A. Advances and Prepayments	$ 400,261	$ 468,259
B. Other Assets	0	0
C. Total Intragovernmental Other Assets	$ 400,261	$ 468,259
2. Nonfederal Other Assets		
A. Outstanding Contract Financing Payments	$ 7,757,776	$ 8,154,326
B. Other Assets (With the Public)	417,368	454,549
C. Total Nonfederal Other Assets	$ 8,175,144	$ 8,608,875
3. Total Other Assets	$ 8,575,405	$ 9,077,134

Standard Disclosures

Nonfederal Other Assets - Outstanding Contract Financing Payments

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

The Outstanding Contract Financing Payment balance of $7.8 billion is comprised of $7.5 billion in contract financing payments and an additional $288.0 million in estimated future payments that will be paid to the contractor upon future delivery and Government acceptance of a satisfactory product. (See additional discussion in Note 15, Other Liabilities).

Nonfederal Other Assets, Other Assets (With the Public)

Other Assets (With the Public) includes advance pay to DON military personnel, travel advances to military and civilian personnel, and miscellaneous advances to contractors that are not considered outstanding contract financing payments.

Note 7. Cash and Other Monetary Assets

As of September 30	2007	2006
(Amounts in Thousands)		
1. Cash	$ 107,615	$ 173,389
2. Foreign Currency	35,356	2,917
3. Other Monetary Assets	0	0
4. Total Cash, Foreign Currency, & Other Monetary Assets	$ 142,971	$ 176,306

Standard Disclosures

Cash and Other Monetary Assets consists primarily of cash held by Department of the Navy (DON) Disbursing Officers to carry out their payment, collection, and foreign currency accommodation exchange mission. Foreign currency is also held in overseas banks in support of contingency operations. The primary source of the amounts reported is the Disbursing Officers Statements of Accountability. The DON Disbursing Officers are agents of the U.S. Treasury.

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

Foreign Currency - consists of the total U.S. dollar equivalent of foreign currencies.

Restriction on Cash, Foreign Currency and Other Monetary Assets – total cash, foreign currency and other monetary assets reported are nonentity assets that are not available for DON's use in normal operations. Therefore, the $143.0 million in cash and foreign currency is restricted as to its use. There are no known restrictions on the conversion of foreign currency to U.S. dollars or other foreign currencies as it is held by Disbursing Officers in support of their payment and foreign currency accommodation exchange mission.

Note 8. Direct Loan and/or Loan Guarantee Programs

Not applicable.

Note 9. Inventory and Related Property

As of September 30	2007	2006
(Amounts in Thousands)		
1. Inventory, Net	$ 0	$ 0
2. Operating Materiels & Supplies, Net	58,249,650	58,794,634
3. Stockpile Materiels, Net	0	0
4. Total	$ 58,249,650	$ 58,794,634

Inventory, Net

Not applicable.

Operating Materiel and Supplies, Net

As of September 30	2007 OM&S Gross Value	2007 Revaluation Allowance	2007 OM&S, Net	2006 OM&S, Net	Valuation Method
(Amounts in Thousands)					
1. OM&S Categories					
A. Held for Use	$ 52,673,901	$ (829)	$ 52,673,072	$ 53,664,746	SP, LAC, MAC
B. Held for Repair	6,685,107	(1,108,529)	5,576,578	5,129,888	SP, LAC, MAC
C. Excess, Obsolete, and Unserviceable	553,334	(553,334)	0	0	NRV
D. Total	$ 59,912,342	$ (1,662,692)	$ 58,249,650	$ 58,794,634	

Legend for Valuation Methods:

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

Standard Disclosures

Restrictions on the use of Operating Materiels and Supplies (OM&S)
There are no known restrictions on the use of OM&S.

General Composition of OM&S
OM&S includes spare and repair parts, ammunition, conventional missiles, torpedoes, aircraft configuration pods, and centrally managed aircraft engines. The general composition of OM&S is Ammunitions and Munitions, Principal End and Secondary Items, Sponsor Owned Materiel (SOM), Real-time Reutilization Asset Management (RRAM) Materiel and Other OM&S.

Ammunition and Munitions are maintained in the Department of the Navy (DON) Ordinance Information System and valued at latest acquisition cost.

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

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

Materiel maintained and valued in RRAM is considered excess to the owner, or materiel manager responsible for the materiel, but may not be excess to DON. Standard price is used to value all stock-numbered items. Part-numbered items are valued by best available information.

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

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

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

Condition Codes are used for materiel management purposes and are defined in the Naval Supply Systems Command Publication 409.

Valuation Method for OM&S
On July 6, 2001, OUSD(C) issued a memorandum directing each Military Department and Defense Agency to implement the Moving Average Cost (MAC) valuation method for Inventory Held for Sale and OM&S as they renovated or replaced their systems. MAC will be implemented as existing OM&S systems are renovated or replaced. Until then, DON continues to value OM&S using different valuation methodologies such as standard purchase price or historical cost. These valuation methodologies vary by system.

Stockpile Materiel, Net

Not applicable.

Note 10. General PP&E, Net

As of September 30	2007					2006
	Depreciation/ Amortization Method	Service Life	Acquisition Value	(Accumulated Depreciation/ Amortization)	Net Book Value	Prior FY Net Book Value
(Amounts in Thousands)						
1. Major Asset Classes						
A. Land	N/A	N/A	$ 603,841	N/A	$ 603,841	$ 611,761
B. Buildings, Structures, and Facilities	S/L	20 or 40	33,379,057	(20,881,702)	12,497,355	13,062,195
C. Leasehold Improvements	S/L	lease term	7,283	(1,092)	6,191	6,894
D. Software	S/L	2-5 or 10	9,881	(7,883)	1,998	106
E. General Equipment	S/L	5 or 10	10,618,149	(5,841,922)	4,776,227	558,351
F. Military Equipment	S/L	Various	303,449,456	(135,029,474)	168,419,982	170,343,508
G. Assets Under Capital Lease	S/L	lease term	0	0	0	104
H. Construction-in- Progress	N/A	N/A	2,749,150	N/A	2,749,150	2,396,750
I. Other			0	0	0	0
J. Total General PP&E			$ 350,816,817	$ (161,762,073)	$ 189,054,744	$186,979,669

Legend for Valuation Methods:

S/L = Straight Line

N/A = Not Applicable

Standard Disclosures

Restrictions on the Use or Convertibility of General Property, Plant, and Equipment (PP&E)

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

Military Equipment

In accordance with the requirements of Statement of Federal Financial Accounting Standards No. 23, “Eliminating the Category National Defense Property, Plant, and Equipment,” beginning in FY 2003, Department of Defense (DoD) reporting entities capitalized military equipment into General PP&E at estimated historical cost using information obtained from the Bureau of Economic Analysis (BEA). Effective 3rd Quarter, FY 2006, DoD replaced BEA estimation methodology with one that is based on departmental internal records for military equipment. In 4th Quarter, FY 2007, DON GF implemented the revised DoD definition of military equipment, which excludes training devices and simulators. Implementing the new definition resulted in a reduction of $4.2 billion in the net book value of Military Equipment with an offsetting increase to General Equipment.

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

Stewardship Policies for Heritage Assets and Description of Each Major Category of Heritage Assets
The overall policy for DON's stewardship policies for heritage assets is contained in the Secretary of the Navy Instruction 4000.35A, "DON Cultural Resources Program."

- Heritage Assets are items that are unique for one or more of the following reasons: historical or natural significance; cultural, educational, or artistic importance; or significant architectural characteristics. The process used to define items as having heritage significance varies between categories and type of assets being evaluated.

- Consultation, as appropriate, is initiated with State Historic Preservation Officers, Tribal Historic Preservation Officers, Advisory Council on Historic Preservation, Native Americans, Native Hawaiians, and other interested agencies whenever DON conducts or supports undertakings that may affect any National Register resource. Preservation considerations are incorporated into routine DON management of historic buildings, structures, districts, sites, ships, aircraft, and other cultural resources.

- Archaeological Sites are locations that contain the remains of past human activity of various sorts that are listed or eligible for listing on the National Register of Historic Places. These sites are excavated only to the extent required for evaluation and identification.

- Buildings and Structures are listed as or determined eligible for listing on the National Register of Historic Places, including Multi-Use Heritage Assets.

- Cemeteries are government owned burial grounds on which gravesites of prominent historical figures may be located in addition to other gravesites.

- Major Collections include archeological artifacts that are maintained and inventoried by cubic feet, archival items that are maintained and inventoried by linear feet, and artwork and historical artifacts that are maintained and inventoried by individual items.

- Monuments and Memorials are those items that are built or placed to commemorate a person or event, preserve the memory of a historical event, or are shown or maintained for its historical interest.

Stewardship Land Policy
The DON Stewardship Land policy is the same as that which DON maintains over all land and installations. The DON strives to be a responsible steward of the land and to maintain it in a way that both protects human health and the environment and allows training and support of fleet readiness. For DON, Stewardship Land includes land acquired through public domain, land set aside, and donated land. Some of this land is used as a buffer around the perimeter of DON installations and may include, but is not limited to, grazing lands and forestry maintenance areas.

The DON did not receive any stewardship land by donation or devise in FY 2007. The DON's heritage asset system does not identify the method by which heritage assets were obtained nor does it maintain costs, therefore we are unable to determine the number and value of heritage assets that may have been obtained through donation or devise. Examples of heritage assets that are obtained on a regular basis include artwork and historical artifacts, such as papers and mementos that have been donated by former sailors, Marines, and their families.

Assets Under Capital Lease

As of September 30	2007	2006
(Amounts in Thousands)		
1. Entity as Lessee, Assets Under Capital Lease		
A. Land and Buildings	$ 0	$ 0
B. Equipment	0	115
C. Accumulated Amortization	0	(11)
D. Total Capital Leases	$ 0	$ 104

Note 11. Liabilities Not Covered by Budgetary Resources

As of September 30	2007	2006
(Amounts in Thousands)		
1. Intragovernmental Liabilities		
A. Accounts Payable	$ 0	$ 0
B. Debt	0	0
C. Other	3,938,842	3,770,838
D. Total Intragovernmental Liabilities	$ 3,938,842	$ 3,770,838
2. Nonfederal Liabilities		
A. Accounts Payable	$ 10,568	$ 37,299
B. Military Retirement and Other Federal Employment Benefits	1,646,486	1,513,644
C. Environmental Liabilities	18,305,233	16,773,218
D. Other Liabilities	5,052,597	3,735,957
E. Total Nonfederal Liabilities	$ 25,014,884	$ 22,060,118
3. Total Liabilities Not Covered by Budgetary Resources	$ 28,953,726	$ 25,830,956
4. Total Liabilities Covered by Budgetary Resources	$ 7,166,320	$ 5,461,997
5. Total Liabilities	$ 36,120,046	$ 31,292,953

Standard Disclosures

Liabilities Covered by Budgetary Resources are those that are incurred by the reporting entity, which are covered by realized budgetary resources as of the balance sheet date. Budgetary resources encompass not only new budget authority, but also other resources available to cover liabilities for specified purposes in a given year.

Realized budgetary resources include:

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

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

For the Department of the Navy General Fund, liabilities to U.S. Treasury are not covered by budgetary resources since they are based on nonentity accounts receivable and other nonentity assets. Accounts payable not covered by budgetary resources is related to cancelled year accounts payable that are not budgeted. Military retirement and other federal employment benefits are future actuarial liabilities. Environmental liabilities are estimates related to future events, such as cleanup of nuclear powered assets that will be budgeted for when those assets are removed from service. Finally, other liabilities for annual leave, estimated legal contingent liabilities, and the disposal of excess structures are not currently budgeted for but will become funded as future events occur.

Intragovernmental Liabilities – Other (Not Covered by Budgetary Resources) (Line 1.C) consists primarily of liabilities to U.S. Treasury related to nonentity assets, and Federal Employees' Compensation Act (FECA) due to the Department of Labor.

Military Retirement and Other Federal Employment Benefits not covered by budgetary resources are comprised of various employee actuarial liabilities not due and payable during the current fiscal year. These liabilities are primarily comprised of FECA actuarial liabilities to employees. Refer to Note 17, Military Retirement and Other Federal Employment Benefits, for additional details and disclosures.

Nonfederal Liabilities – Other (Not Covered by Budgetary Resources) (Line 2.D) consists primarily of liabilities for annual leave, estimated legal contingencies, and for the disposal of excess and obsolete structures.

Note 12. Accounts Payable

As of September 30	2007						2006	
	Accounts Payable		Interest, Penalties, and Administrative Fees		Total		Total	
(Amounts in Thousands)								
1. Intragovernmental Payables	$	1,495,517	$	N/A	$	1,495,517	$	1,035,043
2. Nonfederal Payables (to the Public)		2,948,867		0		2,948,867		1,265,536
3. Total	$	4,444,384	$	0	$	4,444,384	$	2,300,579

Standard Disclosures

Department of the Navy (DON) General Fund (GF) accounting systems do not track intragovernmental transactions by customer at the transaction level which is required to facilitate reconciliation of intragovernmental accounts payable to the related intragovernmental accounts receivable on other agencies' records that generated DON GF's payable. Therefore, DON GF buyer-side accounts payable and expense balances were adjusted to match seller-side accounts receivable and revenue balances. This is accomplished by reclassifying amounts between federal and nonfederal cost categories, and accruing additional costs when necessary.

Note 13. Debt

Not applicable.

Note 14. Environmental Liabilities and Disposal Liabilities

As of September 30	2007			2006
	Current Liability	Noncurrent Liability	Total	Total
(Amounts in Thousands)				
1. Environmental Liabilities-- Nonfederal				
A. Accrued Environmental Restoration Liabilities				
1. Active Installations—Installation Restoration Program (IRP) and Building Demolition and Debris Removal (BD/DR)	$ 361,010	$ 1,890,641	$ 2,251,651	$ 2,329,220
2. Active Installations—Military Munitions Response Program (MMRP)	71,694	708,063	779,757	685,000
3. Formerly Used Defense Sites—IRP and BD/DR	0	0	0	0
4. Formerly Used Defense Sites--MMRP	0	0	0	0
B. Other Accrued Environmental Liabilities—Active Installations				
1. Environmental Corrective Action	1,545	44,431	45,976	40,637
2. Environmental Closure Requirements	308	728,588	728,896	185,833
3. Environmental Response at Operational Ranges	877	24,688	25,565	0
4. Other	0	971	971	0
C. Base Realignment and Closure (BRAC)				
1. Installation Restoration Program	362,935	1,316,760	1,679,695	1,117,093
2. Military Munitions Response Program	4,253	144,507	148,760	112,849
3. Environmental Corrective Action / Closure Requirements	20,859	19,432	40,291	67,462
4. Other	0	0	0	0
D. Environmental Disposal for Weapons Systems Programs				
1. Nuclear Powered Aircraft Carriers	0	5,665,804	5,665,804	5,604,268
2. Nuclear Powered Submarines	484,006	3,202,362	3,686,368	3,377,665
3. Other Nuclear Powered Ships	226,908	66,536	293,444	277,608
4. Other National Defense Weapons Systems	815	204,326	205,141	233,772
5. Chemical Weapons Disposal Program	0	0	0	0
6. Other	0	3,237,406	3,237,406	3,237,406
2. Total Environmental Liabilities	$ 1,535,210	$ 17,254,515	$ 18,789,725	$ 17,268,813

Standard Disclosures

(Amounts in Thousands)	2007	2006
Other Accrued Environmental Costs – Other	$971	$0

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

(Amounts in Thousands)	2007	2006
Environmental Disposal for Weapon Systems Programs - Other	$3,237,406	$3,237,406

The "Other" type of environmental liabilities under Disposal for Weapons Systems Programs (Line 1.D.6) represents Spent Nuclear Fuel, which is the used fuel that is removed from the nuclear reactors of nuclear powered ships and submarines. The estimate includes shipping, processing, and storing the Spent Nuclear Fuel.

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

1. Applicable Laws and Regulations of Cleanup Requirements
The following is a summary of significant laws that affect DON's conduct of environmental policy and regulations.

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

The Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA), commonly referred to as the Superfund legislation, provided Federal agencies authority to respond to the release or the substantial threat of release of hazardous substances into the environment. CERCLA was amended several times; one of which was the Superfund Amendments and Reauthorization Act of 1986. It established procedures to ensure that actual or threatened hazardous substance releases have proper responses. Another amendment to CERCLA was the Community Environmental Response Facilitation Act of 1992. The DON must identify real property on each facility that is not contaminated and that offers the greatest opportunity for expedited reuse and redevelopment. When property is transferred, DON is still responsible for any remediation or corrective action or any response action found to be necessary after the transfer.

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

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

2. Methods for Assigning Total Cleanup Costs to Current Operating Periods
Accrued Environmental Restoration (Defense Environmental Restoration Program (DERP) Funded Liabilities)

Active Installations – Environmental Restoration: Accrued restoration (cleanup) liabilities represent the cost to correct past environmental areas that are funded under the Defense Environmental Restoration Program in accordance with "Management Guidance for DERP," and "Environmental and Non-Environmental Liabilities," Chapter 13 of Volume 4 of Department of Defense Financial Management Regulation (DoD FMR). These liabilities relate to Plant, Property, and Equipment, including acquired land and Stewardship Land, as those major asset categories are described in Chapter 6 of Volume 4 of DoD FMR. Environmental restoration activities may be conducted at operating installations, at Formerly Used Defense Sites, and at Closed, Transferred, and Transferring Ranges. Environmental restoration measurements involve the use of cost estimates that consider, on a current cost basis, the anticipated costs of the level of effort required to affect the restoration, as well as applicable legal and/or regulatory requirements. Program management and support costs are included in the estimates. The estimates are based on DON's cost-to-complete (CTC) module of the Normalization of Data System (NORM). Verification, validation, and accreditation of CTC module was completed in FY 2002. Such cost estimates are based on the current technology available. The DON, as the baseline for environmental restoration (cleanup) liability measurement (i.e., the current cost to acquire the required services), used the site inventory and estimated cost data prepared for DERP report to the Congress. The Accrued Environmental Restoration (Cleanup) Costs do not include the costs of environmental compliance; pollution prevention, conservation activities, contamination, or spills associated with current operations or treaty obligations, all of which are accounted for as part of ongoing operations. The DON Environmental Restoration Program includes 3,704 clean-up sites at active installations while those installations covered by Base Realignment and Closure (BRAC) funding include 1,148 clean-up sites. The Marine Corps is included in these programs. In addition, the DON Environmental Corrective Action Program at BRAC installations includes 610 sites.

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

Environmental Disposal for Weapons Systems Programs: This area represents environmental liabilities associated with the Nuclear Powered Aircraft Carriers and Submarines, Other Nuclear Powered Ships, Conventional Ships, and Spent Nuclear Fuel. During FY 2006, under DON FIP, DON completed a review of the estimating methodology for determining the cost for disposal of ships and submarines. This review resulted in an environmental and nonenvironmental liability estimate that more accurately reflects the true costs of disposal. The estimating methodology is based on average cost per class of ship rather than an average applied to all ships regardless of class.

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

Accrued Environmental Restoration (DERP Funded) Liabilities

The DON Environmental Restoration includes those sites that have been identified as legacy cleanup sites. For FY 2007, DON estimated and reported $3.0 billion for environmental restoration liabilities. This amount is comprised of $2.2 billion in Active Installations – Installation Restoration Program (IRP) liabilities and $779.8 million in Active Installations – MMRP, liabilities, which represents UXO. The DoD FMR, Volume 6B, Chapter 10 requires that "any estimate produced must be based on site specific information and use cost models validated in accordance with DoD Instruction 5000.61." The DON is supporting this requirement by continuing to validate its range inventory as well as by pursuing the process of obtaining valid cost estimates for each range.

Other Accrued Environmental Costs (Non-DERP funds)

The DON defines Non-DERP environmental units as those sites associated with on-going operations such as solid waste management unit cleanup, landfill closure, permitted facilities, removal, replacement, retro fill, and/or disposal of PCBs transformers, underground storage tank remedial investigation and closure. As part of DON FIP efforts, the Navy completed surveying, identifying, and estimating, Non-DERP units and began recognizing the estimated environmental liability 1st Quarter, FY 2007. For FY 2007, the total Other Accrued Environmental Liabilities is $801.4 million. Of the total, the Navy portion is $576.8 million while the Marine Corps portion is $224.6 million.

Base Realignment and Closure (BRAC)

BRAC environmental sites are environmental sites at DON installations that are or will be closed under the congressionally mandated BRAC process. For FY 2007, DON estimated and reported $1.9 billion for BRAC funded environmental restoration liabilities. This amount includes $1.7 billion for IRP, $148.8 million for MMRP, and $40.3 million for environmental corrective action and closure requirements. MMRP includes military munitions, chemical residues from military munitions, and munitions scrap at locations on or associated with a military range on a BRAC installation.

Environmental Disposal for Weapons Systems Programs

Environmental Disposal for Weapons Systems are those estimates associated with the environmental disposal costs for DON Nuclear Weapons Programs that includes Nuclear Powered Aircraft Carriers and Submarines and Other Nuclear Powered Ships, Conventional Ships, and Spent Nuclear Fuel. The DON reported an environmental disposal liability for Weapons Systems Programs of $13.1 billion in FY 2007. This amount includes Nuclear Powered Aircraft Carriers of $5.7 billion, Nuclear Powered Submarines of $3.7 billion, Other Nuclear Powered Ships of $293.4 million, Other National Defense Weapons Systems (Conventional Ships) of $205.1 million, and Spent Nuclear Fuel (Other) of $3.2 billion.

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

For both current and prior periods, the changes due to price growth (inflation) and increases in labor rates and materials have been offset by a change in the estimating methodology for weapons systems. This change in estimating methodology resulted in an overall decrease in the estimated environmental disposal liability. However, this decrease was offset by recognizing an estimated liability for spent nuclear fuel beginning with 3rd Quarter, FY 2006. Currently, there are no indications that any of the environmental liabilities for any category will be adjusted due to deflation. As of FY 2007, there are no changes to the environmental liability estimates due to changes in laws, regulations, and in agreements with regulatory agencies. The DON does not have any estimates that were changed due to advances in technology.

5. Description of the Level of Uncertainty Regarding the Accounting Estimates Used to Calculate the Reported Environmental Liabilities

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

Overall, DON has a reasonable level of confidence in the estimates recognized on the face of the financial statements. This reasonable level of confidence in the estimates is because the estimates for DERP/BRAC programs are based on the CTC module of the NORM System. A verification, validation, and accreditation were completed by a third party for CTC module of NORM, while the environmental program managers continue to validate the data.

For the Weapons systems, the environmental program managers base their environmental disposal estimates on actual costs for similar projects. A change in the overall methodology in weapons systems reflects a more accurate estimate of what it will cost to dispose of the weapons systems. Given the fact that the planned date for opening DOE’s planned waste repository has been delayed, there is uncertainty associated with the estimate for spent nuclear fuel. As DOE’s plans are solidified, DON’s estimates for spent nuclear fuel will change accordingly.

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

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

Environmental Disclosures

As of September 30	2007	2006
(Amounts in Thousands)		
A. The unrecognized portion of the estimated total cleanup costs associated with general property, plant, and equipment.	1,521,867	1,423,683
B. Changes in total cleanup costs due to changes in laws, regulations, and/or technology.	0	0
C. Portion of the changes in estimated costs due to changes in laws and technology that is related to prior periods.	0	0

Line A. The unrecognized portion of the estimated total cleanup costs is associated with Nuclear Powered Carriers and Submarines, Conventional Ships, Spent Nuclear Fuel, and Non-DERP. Of the total $1.5 billion, $1.4 billion is associated with Nuclear Powered Carriers and Submarines and Spent Nuclear Fuel, $45.2 million is associated with conventional ships while the remainder of $66.5 million is associated with Non-DERP. Contributing to the increase is a result of DON, in 1st Quarter, FY 2007, recognizing and accruing environmental liabilities (Non-DERP) associated with assets placed in service after September 30, 1997.

Lines B and C. Through our quarterly data call process for FY 2007, DON determined that there were no changes to the environmental liability estimates due to changes in laws, regulations, in agreements with regulatory agencies, and advances in technology.

Note 15. Other Liabilities

As of September 30	2007 Current Liability	2007 Noncurrent Liability	2007 Total	2006 Total
(Amounts in Thousands)				
1. Intragovernmental				
A. Advances from Others	$ 0	$ 0	$ 0	$ 0
B. Deposit Funds and Suspense Account Liabilities	516,593	0	516,593	474,507
C. Disbursing Officer Cash	142,971	0	142,971	176,306
D. Judgment Fund Liabilities	0	0	0	0
E. FECA Reimbursement to the Department of Labor	244,318	315,622	559,940	557,343
F. Other Liabilities	3,423,315	0	3,423,315	3,251,997
G. Total Intragovernmental Other Liabilities	$ 4,327,197	$ 315,622	$ 4,642,819	$ 4,460,153
2. Nonfederal				
A. Accrued Funded Payroll and Benefits	$ 818,017	$ 0	$ 818,017	$ 445,018
B. Advances from Others	256,035	0	256,035	205,544
C. Deferred Credits	0	0	0	0
D. Deposit Funds and Suspense Accounts	4,173	0	4,173	42,257
E. Temporary Early Retirement Authority	0	0	0	0
F. Nonenvironmental Disposal Liabilities				
(1) Military Equipment (Nonnuclear)	8,183	262,959	271,142	285,201
(2) Excess/Obsolete Structures	75,955	587,018	662,973	685,618
(3) Conventional Munitions Disposal	0	0	0	0
G. Accrued Unfunded Annual Leave	2,386,889	0	2,386,889	2,738,551
H. Capital Lease Liability	0	0	0	0
I. Other Liabilities	1,840,247	355,518	2,195,765	1,347,575
J. Total Nonfederal Other Liabilities	$ 5,389,499	$ 1,205,495	$ 6,594,994	$ 5,749,764
3. Total Other Liabilities	$ 9,716,696	$ 1,521,117	$ 11,237,813	$ 10,209,917

Standard Disclosures

Nonfederal Other Liabilities includes Contingent Liabilities of $288.0 million for estimated future contract financing payments that will be paid to the contractor upon delivery and Government acceptance of a satisfactory product. In accordance with contract terms, specific rights to the contractor's work vests with the Government when a specific type of contract financing payments is made; thereby protecting taxpayer funds in the event of contract nonperformance. These rights should not be misconstrued as the rights of ownership. The Department of the Navy (DON) General Fund (GF) is under no obligation to pay the contractor for amounts greater than the amounts authorized in the contract until delivery and Government acceptance of a satisfactory product. As it is probable that the contractor will complete its efforts and deliver a satisfactory product and the amount of potential future payments are estimable, DON GF has recognized a contingent liability for estimated future payments, which are conditional pending delivery and Government acceptance of a satisfactory product.

Intragovernmental Other Liabilities - Other (Line 1.F)
Other Liabilities - Other consists primarily of a liability to the U.S. Treasury. The liability represents principal and accrued interest associated with pending litigation.

Nonfederal Other Liabilities - Other Liabilities - Other (Line 2.I)
Other Liabilities - Other consists primarily of estimated legal contingent liabilities and outstanding contract financing contingent liabilities.

Methodology Used for Estimated Legal Contingent Liabilities
Due to the inherent uncertainties of litigation, lawyers generally refrain from expressing judgments as to outcomes except in those relatively few clear cases. In response to a Department of Defense (DoD), Inspector General Audit, "DoD Process for Reporting Contingent Legal Liabilities," DON developed a methodology to determine an estimate for contingent legal liabilities. Beginning with 1st Quarter, FY 2007 DON recognized and disclosed an estimate for contingent legal liabilities. The methodology considers the likelihood of an unfavorable outcome or potential liability is provided as an overall assessment of all cases currently pending and not on an individual case basis. The likelihood of an unfavorable or potential liability was determined by using an average of the data from current year-to-date and the preceding four years. The total dollar amount of the cases closed was divided by the total dollar amount claimed in those closed cases for each of the last four years plus the current year, which were then used to calculate the average. This average is based entirely on historical data and represents the percentage that has historically been paid on claims. The merits of each individual case have not been taken into consideration. Until sufficient historical data can be collected for the Navy Working Capital Fund (NWCF), the estimated legal liability for the DON GF will consider all DON funding sources together. The estimate for those cases considered probable to result in an adverse judgment against DON is $1.7 billion.

Capital Lease Liability

Not applicable.

Note 16. Commitments and Contingencies

Standard Disclosures

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

For FY 2007, DON General Fund (GF) materiality threshold for reporting litigation, claims, or assessments is $64.4 million. The DON Office of General Counsel conducts a review of litigation and claims threatened or asserted involving DON General Fund to which Office of General Counsel attorneys devoted substantial attention in the form of legal consultation or representation.

The DON currently has 12 cases; 11 associated with the Navy and 1 associated with the United States Marine Corps that meet the existing FY 2007 DON GF materiality threshold of $64.4 million. DON legal counsel was unable to express an opinion concerning the likely outcome of 11 of 12 cases. Based on information contained in the FY 2007 preliminary and final Legal Representation Letters, management does not have sufficient reason to believe that it is likely that the Government will be liable for the amounts claimed in individual or aggregated cases.

Due to the inherent uncertainties of litigation, lawyers generally refrain from expressing judgments as to outcomes except in those relatively few clear cases. In response to a Department of Defense (DoD), Inspector General Audit, "DoD Process for Reporting Contingent Legal Liabilities," DON developed a methodology to determine an estimate for contingent legal liabilities. Beginning with 1st Quarter, FY 2007, DON recognized and disclosed an estimate for contingent legal liabilities. The methodology considers the likelihood of an unfavorable outcome or potential liability is provided as an overall assessment of all cases currently pending and not on an individual case basis. The likelihood of an unfavorable or potential liability was determined by using an average of the data from the current year-to-date and the preceding four years. The total dollar amount of the cases closed was divided by the total dollar amount claimed in those closed cases for each of the last four years plus current year, which were then used to calculate the average. This average is based entirely on historical data and represents the percentage that has historically been paid on claims. The merits of each individual case have not been taken into consideration. The estimate for those cases considered reasonably possible to result in an adverse judgment against DON is $1.7 billion. Until sufficient historical data can be collected for the Navy Working Capital Fund, the DON GF estimate will consider all DON funding sources together.

The DON is a party in numerous individual contracts that contain clauses, such as price escalation, award fee payments, or dispute resolution, that may or may not result in a future outflow of expenditures. Currently, DON does not have a systemic process by which it captures or assesses these potential contingent liabilities; therefore, the amounts reported may not fairly present DON contingent liabilities.

The DON GF has recorded in Note 12 a contingent liability in the amount of $10.6 million for obligations related to cancelled appropriations.

The DON GF has recorded in Note 15 a contingent liability in the amount of $74.3 million for Contract Incentives.

Note 17. Military Retirement and Other Federal Employment Related Benefits

As of September 30	2007 Present Value of Benefits	2007 Assumed Interest Rate (%)	2007 (Less: Assets Available to Pay Benefits)	2007 Unfunded Liability	2006 Present Value of Benefits
(Amounts in Thousands)					
1. Pension and Health Actuarial Benefits					
A. Military Retirement Pensions	$ 0		$ 0	$ 0	$ 0
B. Military Retirement Health Benefits	0		0	0	0
C. Military Medicare-Eligible Retiree Benefits	0		0	0	0
D. Total Pension and Health Actuarial Benefits	$ 0		$ 0	$ 0	$ 0
2. Other Actuarial Benefits					
A. FECA	$ 1,646,486		$ 0	$ 1,646,486	$ 1,513,644
B. Voluntary Separation Incentive Programs	0		0	0	0
C. DoD Education Benefits Fund	0		0	0	0
D. Total Other Actuarial Benefits	$ 1,646,486		$ 0	$ 1,646,486	$ 1,513,644
3. Other Federal Employment Benefits	$ 1,638		$ (1,638)	$ 0	$ 0
4. Total Military Retirement and Other Federal Employment Benefits:	$ 1,648,124		$ (1,638)	$ 1,646,486	$ 1,513,644

Standard Disclosures

Federal Employees' Compensation Act

Actuarial Cost Method Used and Assumptions:

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

FY 2007
4.930 % in Year 1
5.078 % in Year 2 and thereafter

To provide more specifically for the effects of inflation on the liability for future workers' compensation benefits, wage inflation factors (cost of living adjustments or COLAs) and medical inflation factors (consumer price index medical or CPIMs) were applied to the calculation of projected future benefits. The actual rates for these factors for the charge back year (CBY) 2007 were also used to adjust the methodology's historical payments to current year constant dollars.

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

CBY	COLA	CPIM
2007	2.63%	3.74%
2008	2.90%	4.04%
2009	2.47%	4.00%
2010	2.37%	3.94%
2011+	2.30%	3.94%

The model's resulting projections were analyzed to ensure that the estimates were reliable. The analysis was based on four tests: (1) a sensitive analysis of the model to economic assumptions; (2) a comparison of the percentage change in the liability amount by agency to the percentage change in the actual incremental payments; (3) a comparison of the incremental paid losses per case (a measure of case-severity) in CBY 2007 to the average pattern observed during the most current three CBYs; and (4) a comparison of the estimated liability per case in the 2007 projection to the average pattern for the projections of the most recent three years.

Other Federal Employment Benefits
Other federal employment benefits (Line 3) consist primarily of voluntary separation incentive pay for former employees.

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

As of September 30		2007		2006
(Amounts in Thousands)				
1. Intragovernmental Costs	$	40,664,719	$	40,177,296
2. Public Costs		111,477,016		89,352,957
3. Total Costs	$	152,141,735	$	129,530,253
4. Intragovernmental Earned Revenue	$	(3,466,409)	$	(2,551,473)
5. Public Earned Revenue		(909,421)		(1,360,814)
6. Total Earned Revenue	$	(4,375,830)	$	(3,912,287)
7. Net Cost of Operations	$	147,765,905	$	125,617,966

Standard Disclosures
Intragovernmental costs and revenues are related to transactions made between two reporting entities, one entity being the Department of the Navy (DON) General Fund (GF), within the Federal Government.

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

The DON's GF financial management systems are unable to meet all of the requirements for full accrual accounting. Many of DON's financial and nonfinancial feeder systems and processes were designed and implemented prior to the issuance of generally accepted accounting principles (GAAP) for federal agencies. Most of DON's legacy systems were designed to record information on a budgetary basis, and do not track intragovernmental transactions by customer at the transaction level. Considering these systems limitations, DON GF is unable to accurately compare its intragovernmental costs and revenues with the corresponding balances of its intragovernmental trading partners. Therefore, DON GF buyer-side accounts payable and expense balances were adjusted to match seller-side accounts receivable and revenue balances. This is accomplished by reclassifying amounts between federal and public cost categories, and accruing additional costs when necessary.

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

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

The DON's accounting systems do not capture information relative to Heritage Assets separately and distinctly from normal operations.

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

As of September 30	2007 Cumulative Results of Operations	2007 Unexpended Appropriations	2006 Cumulative Results of Operations	2006 Unexpended Appropriations
(Amounts in Thousands)				
1. Prior Period Adjustments Increases (Decreases) to Net Position Beginning Balance				
A. Changes in Accounting Standards	$ 0	$ 0	$ 0	$ 0
B. Errors and Omissions in Prior Year Accounting Reports	0	0	23,218,292	0
C. Total Prior Period Adjustments	$ 0	$ 0	$ 23,218,292	$ 0
2. Imputed Financing				
A. Civilian CSRS/FERS Retirement	$ 240,087	$ 0	$ 219,410	$ 0
B. Civilian Health	398,231	0	327,916	0
C. Civilian Life Insurance	1,224	0	1,066	0
D. Judgment Fund	90,648	0	29,666	0
E. IntraEntity	0	0	0	0
F. Total Imputed Financing	$ 730,190	$ 0	$ 578,058	$ 0

Standard Disclosures
Appropriations Received on the Statement of Changes in Net Position (SCNP) does not agree with Appropriations Received on the Statement of Budgetary Resources (SBR) due to differences between proprietary and budgetary accounting concepts and reporting requirements. The difference of $22.8 million is due to the values for Trust Funds and Special Receipt Accounts not being included in the Appropriations Received line of the SCNP. Refer to Note 20 for additional details.

In the SCNP, all offsetting balances (i.e. transfers-in and transfers-out, revenues and expenses) for intra-Department of the Navy (DON) General Fund activity between earmarked and other (non-earmarked) funds are reported on the same lines. This results in an eliminations column, which appears to contain no balances. In reality, the column contains all appropriate elimination entries, but all net to zero within each respective line.

The Earmarked Cumulative Results of Operations ending balance on the SCNP does not agree with the Earmarked Cumulative Results reported on the Balance Sheet because the cumulative results on the Balance Sheet are presented net of eliminations.

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

Description of Other Lines on the SCNP
Other Financing Sources – Other (Line 5.D) represents net gains and losses recorded in relation to the capitalization of assets such as Real Property, Construction in Progress, Operating Materiel and Supplies, and Military Equipment.

Other Adjustments (Line 13.C) represents reductions to budget authority and rescissions in accordance with Public Law.

Note 20. Disclosures Related to the Statement of Budgetary Resources

As of September 30	2007	2006
(Amounts in Thousands)		
1. Net Amount of Budgetary Resources Obligated for Undelivered Orders at the End of the Period	$ 88,903,894	$ 83,047,974
2. Available Borrowing and Contract Authority at the End of the Period	0	0

Standard Disclosures
Apportionment Categories for Obligations Incurred
On the Statement of Budgetary Resources (SBR): Obligations Incurred includes $163.3 billion of Direct Program Obligations and $7.8 billion of Reimbursable Program Obligations.

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

- Direct Obligations, Category A, amounts apportioned quarterly, are $86.0 billion.
- Direct Obligations, Category B, amounts apportioned on a basis other than quarterly, are $77.2 billion.
- Total Direct Obligations are therefore $163.2 billion.
- The $120.0 million difference in direct obligations between the SBR and SF-133 is due to adjustments on the SBR to recognize fringe benefits, reclassify reimbursable obligations as noted below, and recognize other adjustments not captured in the field accounting systems.
- Category B Reimbursable Obligations are $7.9 billion.
- The $157.0 million difference in reimbursable obligations between the SBR and SF-133 results from a reclassification adjustment to record trading partner data.

<u>Other Disclosures</u>
The SBR includes intraentity transactions because the statements are presented as combined.

As noted above, in terms of obligations, differences exist between the SF-133 and the SBR for a number of reasons; including accruals recorded for fringe benefits, liabilities recorded for the Judgment Fund, and accruals recorded for trading partner advances and liabilities.

Appropriations Received on the Statement of Changes in Net Position (SCNP) does not agree with Appropriations Received on the SBR due to differences between proprietary and budgetary accounting concepts and reporting requirements. The difference of $22.8 million is due to the values for Trust Funds and Special Receipt Accounts not being included in the Appropriations Received line of the SCNP.

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

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

<u>Permanent, Indefinite Appropriations</u>
The National Defense Sealift Fund (NDSF) is operated under the authority of 10 U.S. Code 2218, which provides for the construction (including design of vessels), purchase, alteration, and conversion of Department of Defense (DoD) sealift vessels; operation, maintenance, and lease or charter of DoD vessels for national defense purposes; installation and maintenance of defense features for national defense purposes on privately owned and operated vessels that are constructed in the United States and documented under the laws of the United States; research and development relating to national defense sealift; and expenses for maintaining the National Defense Reserve Fleet, including the acquisition, alteration or conversion of vessels. For FY 2007, three transfers totaling $25.6 million from NDSF to Shipbuilding and Conversion, Navy appropriation were recorded; no transfers to NDSF occurred.

The Environmental Restoration, Navy (ER, N) appropriation is a transfer account that funds environmental restoration, reduction, and recycling of hazardous waste, removal of unsafe buildings and debris, and similar purposes. Funds remain available until transferred and remain available for the same purpose and same time period as the appropriations to which transferred. For FY 2007 one transfer from ER, N for $301.5 million to the Operation and Maintenance, Navy appropriation was recorded; no transfers to ER, N occurred.

Note 21. Reconciliation of Net Cost of Operations to Budget

As of September 30	2007	2006
(Amounts in Thousands)		
Resources Used to Finance Activities:		
Budgetary Resources Obligated:		
1. Obligations incurred	$ 171,048,537	$ 151,872,496
2. Less: Spending authority from offsetting collections and recoveries (-)	(24,573,990)	(12,654,282)
3. Obligations net of offsetting collections and recoveries	$ 146,474,547	$ 139,218,214
4. Less: Offsetting receipts (-)	(270,572)	(149,284)
5. Net obligations	$ 146,203,975	$ 139,068,930
Other Resources:		
6. Donations and forfeitures of property	0	0
7. Transfers in/out without reimbursement (+/-)	91,282	187,068
8. Imputed financing from costs absorbed by others	730,190	578,058
9. Other (+/-)	4,896,617	0
10. Net other resources used to finance activities	$ 5,718,089	$ 765,126
11. Total resources used to finance activities	$ 151,922,064	$ 139,834,056
Resources Used to Finance Items not Part of the Net Cost of Operations:		
12. Change in budgetary resources obligated for goods, services and benefits ordered but not yet provided:		
12a. Undelivered Orders (-)	$ (5,855,322)	$ (6,657,708)
12b. Unfilled Customer Orders	57,810	573,402
13. Resources that fund expenses recognized in prior Periods (-)	(4,161,568)	(101,501)
14. Budgetary offsetting collections and receipts that do not affect Net Cost of Operations	270,572	149,284
15. Resources that finance the acquisition of assets (-)	(9,847,856)	(28,364,037)
16. Other resources or adjustments to net obligated resources that do not affect Net Cost of Operations:		
16a. Less: Trust or Special Fund Receipts Related to exchange in the Entity's Budget (-)	0	0
16b. Other (+/-)	(4,987,899)	(187,068)
17. Total resources used to finance items not part of the Net Cost of Operations	$ (24,524,263)	$ (34,587,628)
18. Total resources used to finance the Net Cost of Operations	$ 127,397,801	$ 105,246,428

As of September 30	2007	2006
(Amounts in Thousands)		
Components of the Net Cost of Operations that will not Require or Generate Resources in the Current Period:		
Components Requiring or Generating Resources in Future Period:		
19. Increase in annual leave liability	$ 1,808,214	$ 43,363
20. Increase in environmental and disposal liability	1,522,737	230,378
21. Upward/Downward reestimates of credit subsidy expense (+/-)	0	0
22. Increase in exchange revenue receivable from the public (-)	0	0
23. Other (+/-)	3,727,419	208,377
24. Total components of Net Cost of Operations that will Require or Generate Resources in future periods	$ 7,058,370	$ 482,118
Components not Requiring or Generating Resources:		
25. Depreciation and amortization	$ 8,560,724	$ 21,243,453
26. Revaluation of assets or liabilities (+/-)	36,616	1,865,416
27. Other (+/-)		
27a. Trust Fund Exchange Revenue	0	0
27b. Cost of Goods Sold	0	0
27c. Operating Materiel and Supplies, Used	4,665,050	(3,209,774)
27d. Other	47,344	(9,675)
28. Total Components of Net Cost of Operations that will not Require or Generate Resources	$ 13,309,734	$ 19,889,420
29. Total components of Net Cost of Operations that will not Require or Generate Resources in the current period	$ 20,368,104	$ 20,371,538
30. Net Cost of Operations	$ 147,765,905	$ 125,617,966

Standard Disclosures

Beginning 4th Quarter, FY 2007, Department of Defense (DoD) reporting entities began presenting the Statement of Financing (SOF) as a note in accordance with the Office of Management and Budget Circular A-136. The SOF will no longer be considered a basic statement and is now referred to as "Reconciliation of Net Cost of Operations to Budget."

The SOF is designed to provide information about the total resources used by an entity, to explain how those resources were used to finance orders for goods and services not yet delivered, to acquire assets and liabilities, and to fund the entity's net cost of operations. It is designed to report the differences and facilitate the reconciliation of accrual based amounts used in the Statement of Net Cost (SNC) and obligation-based amounts used in the Statement of Budgetary Resources. The computations and presentation of items in the SOF demonstrate that the budgetary and proprietary information in an entity's financial management system agrees.

Due to DON financial system limitations, budgetary data is not in agreement with proprietary expenses and assets capitalized. Differences between budgetary and proprietary data are a previously identified deficiency. This causes a difference in net cost between the SNC and the SOF that requires an adjustment to the SOF. For 4th Quarter, FY 2007, an adjustment of $59.1 million was made to Resources that Finance the Acquisition of Assets of the SOF so that proprietary accounts reconcile with the budgetary accounts.

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

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

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

Description of Other Lines on the SOF
Resources Used to Finance Activities – Budgetary Resources Obligated:
The balance of $461.8 million reflects represents net gains and losses recorded in relation to the capitalization of assets such as Real Property, Construction in Progress, Operating Materiels and Supplies, and Military Equipment.

Resources Used to Finance Items not Part of the Net Cost of Operations:
The balance of $370.6 million reflects the value of donated fuel, and transfers of Construction-in-Progress and other assets without reimbursement from other DoD Components.

Components Requiring or Generating Resources in Future Periods:
The balance of $3.7 billion consists primarily of an estimate for potential legal liabilities, and employment related liabilities.

Components not Requiring or Generating Resources:
The balance of $47.3 million consists primarily of bad debt expense, the value of donated fuel, and the transfer of assets without reimbursement from other DoD Components. The fuel was donated by other nations to the United States military in support of the Global War on Terror.

Liabilities not covered by budgetary resources on the Balance Sheet totaling $28.9 billion, increased $3.1 billion and differs from the amount reported as Components Requiring or Generating Resources in Future Periods on the Statement of Financing, which totals $7.1 billion. The difference is primarily due to the differing perspectives between the two statements. Liabilities not covered by budgetary resources report the cumulative balance for Balance Sheet liabilities not yet funded whereas components requiring or generating resources in future periods reflects current period changes for unfunded environmental and disposal liabilities, annual leave, contingent liabilities, and other expenses not requiring budgetary resources.

Note 22. Disclosures Related to Incidental Custodial Collections

Not applicable.

Note 23. Earmarked Funds

BALANCE SHEET As of September 30 *(Amounts in Thousands)*	MRF	MERHCF	Other Earmarked Funds	Eliminations	Total
ASSETS					
Fund balance with Treasury	$ 0	$ 0	$ 15,568	$ 0	$ 15,568
Investments	0	0	9,756	0	9,756
Accounts and Interest Receivable	0	0	0	0	0
Other Assets	0	0	22	0	22
Total Assets	$ 0	$ 0	$ 25,346	$ 0	$ 25,346
LIABILITIES and NET POSITION *As of September 30*					
Military Retirement Benefits and Other Employment Related Actuarial Liabilities	$ 0	$ 0	$ 0	$ 0	$ 0
Other Liabilities	0	0	1,088	0	1,088
Total Liabilities	$ 0	$ 0	$ 1,088	$ 0	$ 1,088
Unexpended Appropriations	0	0	0	0	0
Cumulative Results of Operations	0	0	24,258	0	24,258
Total Liabilities and Net Position	$ 0	$ 0	$ 25,346	$ 0	$ 25,346
STATEMENT OF NET COST *As of September 30*					
Program Costs	$ 0	$ 0	$ 18,958	$ 0	$ 18,958
Less Earned Revenue	0	0	0	0	0
Net Program Costs	$ 0	$ 0	$ 18,958	$ 0	$ 18,958
Less Earned Revenues Not Attributable to Programs	0	0	0	0	0
Net Cost of Operations	$ 0	$ 0	$ 18,958	$ 0	$ 18,958
STATEMENT OF CHANGES IN NET POSITION *As of September 30*					
Net Position Beginning of the Period	$ 0	$ 0	$ 20,393	$ 0	$ 20,393
Net Cost of Operations	0	0	18,958	0	18,958
Budgetary Financing Sources	0	0	22,823	0	22,823
Other Financing Sources	0	0	0	0	0
Change in Net Position	$ 0	$ 0	$ 3,865	$ 0	$ 3,865
Net Position End of Period	$ 0	$ 0	$ 24,258	$ 0	$ 24,258

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

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

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

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

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

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

Ships Stores Profit, Navy:
This trust fund is authorized by 10 United States Code 7220. Deposits to this fund are derived from

profits realized through the operation of ships' stores and from the acceptance of gifts accepted for providing recreation, amusement, and contentment for enlisted members of the Navy and Marine Corps.

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

Note 24. Other Disclosures

As of September 30	2007 Asset Category			
	Land and Buildings	Equipment	Other	Total
(Amounts in Thousands)				
1. ENTITY AS LESSEE-				
Operating Leases				
Future Payments Due				
Fiscal Year				
2008	$ 50,483	$ 572	$ 0	$ 51,055
2009	44,916	81	0	44,997
2010	45,818	83	0	45,901
2011	46,858	85	0	46,943
2012	47,922	87	0	48,009
After 5 Years	48,210	89	0	48,299
Total Future Lease Payments Due	$ 284,207	$ 997	$ 0	$ 285,204

Note 25. Restatements

For FY 2007, Department of the Navy General Fund does not have any restatements.

General Fund

Required Supplementary Stewardship Information

Investments in Research and Development
Yearly Investment in Research and Development
For Fiscal Years 2003 through 2007
($ in Millions)

Categories	FY03	FY04	FY05	FY06	FY07
Basic Research	$ 399	$ 431	$ 437	$ 449	$ 448
Applied Research	743	686	692	739	781
Development					
Advanced Technology Development	836	967	951	912	801
Advanced Component Development and Prototypes	2,536	2,361	3,030	3,223	3,229
System Development and Demonstration	4,200	6,115	7,094	7,819	8,731
Research, Development, Test, and Evaluation Management Support	797	906	955	1,022	1,034
Operational Systems Development	2,385	1,820	3,775	3,399	3,810
Total	**$11,896**	**$13,286**	**$16,934**	**$17,563**	**$18,834**

Narrative Statement:

Investments in Research and Development
Investment values are based on Research and Development outlays (expenditures). Outlays are used because current Department of the Navy (DON) systems are unable to fully capture and summarize costs in accordance with standards promulgated by the Federal Accounting Standards Advisory Board.

A. Basic Research
Basic Research is the systematic study to gain knowledge or understanding of the fundamental aspects of phenomena and of observable facts without specific applications, processes, or products in mind. Basic Research involves the gathering of more knowledge or a better understanding of the subject under study. Major outputs are scientific studies and research papers.

The following are two representative program examples for the Basic Research category.

Prototype for Long Wavelength Array Sees "First Light"
Astronomers at the Naval Research Laboratory (NRL) have produced the first images of the sky from a prototype of the Long Wavelength Array (LWA), a revolutionary new radio telescope to be constructed in southwestern New Mexico. The images show emissions from the center of our galaxy, a supermassive black hole, and the remnant of a star that exploded in a supernova more than 300 years ago. The images represent not only a milestone in the development of the LWA, but also the first glimpse through a new window on the cosmos. "First light" is an astronomical term for the first image produced with a telescope. It is a key milestone for any telescope because it indicates that all of the individual components are working in unison as planned.

Once completed, the LWA will provide an entirely novel view of the sky in the radio frequency range of 20-80 MHz, currently one of the most poorly explored regions of the electromagnetic spectrum in astronomy. The LWA will be able to make sensitive high resolution images and scan the sky rapidly for new and transient sources of radio waves, which might represent the explosion of distant, massive stars, or the emissions from planets outside of our own solar system or even previously unknown objects or phenomena.

When completed, the LWA will operate like the current prototype, the Long Wavelength Development Array (LWDA), but on a much larger scale. While the LWDA telescope consists of 16 antennas connected to a suite of electronics that combine the signals from each antenna, plans for the LWA call for more than 13,000 individual antennas, divided into 50 stations. These stations will be spread over a 250-mile area across New Mexico, and possibly beyond.

Aristotle's First Mover Principle: "Tornadoes" are Transferred from Light to Sodium Atoms
For the first time, tornado-like rotational motions have been transferred from light to atoms in a controlled experiment at the National Institute of Standards and Technology (NIST). The new quantum physics technique can be used to manipulate Bose Einstein condensates, a state of matter potentially useful in quantum information systems that is the subject of worldwide research interest. Quantum information systems are an emerging computing and communications technology with potentially unlimited applications.

The NIST research team transferred orbital angular momentum—essentially the same motion as air molecules in a tornado or a planet revolving around a star—from laser light to sodium atoms.

The NIST experiment completes the scientific toolkit for complete control of the state of an atom, which now includes the internal, translational, and rotational behavior. The rotational motion of light previously has been used to rotate particles, but this new work marks the first time the motion has been transferred to atoms in discrete, measurable units, or quanta. Other researchers, as well as the NIST group, previously have transferred linear momentum and spin angular momentum (an internal magnetic state) from light to atoms.

The experiments were performed with more than a million sodium atoms confined in a magnetic trap. The atoms were chilled to near absolute zero and in identical quantum states, a condition known as a Bose Einstein condensate (BEC) in which they behave like a single "super-atom" with a jelly-like consistency. The BEC was illuminated from opposite sides by two laser beams, one of them with a rotating doughnut shape. Each atom absorbed one photon (the fundamental particle of light) from the doughnut laser beam and emitted one photon in the path of the other laser beam, picking up the difference in orbital angular momentum between the two photons. The interaction of the two opposing lasers created a corkscrew-like interference pattern, inducing the BEC to rotate—picture a rotating doughnut or a vortex similar to a hurricane.

The researchers demonstrated control over the process by inducing the cloud of atoms to simultaneously rotate and stand still, or to rotate simultaneously in opposite directions with varying amounts of momentum—a mind-bending peculiarity of quantum physics known as superposition.

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

The following are two representative program examples for the Applied Research category.

Electromagnetic Railgun
Railgun research in the United States has been ongoing for more than two decades. A significant milestone in the advancement of naval gun technology was achieved with the successful test and standup

of an electromagnetic (EM) railgun facility at the Naval Surface Warfare Center Dahlgren Division Laboratory.

Working for the Office of Naval Research (ONR), engineers at the laboratory fired a low energy shot, the first in a series of tests required to bring the facility online. The researchers are one step closer to the future of naval weaponry with the standup of this, the largest operational EM facility in the Navy. The recent advances in science and technology have made this technology feasible, as well as collaboration of scientists and engineers across government agencies, industry, and the branches of service. With the potential to deliver lethal, hypersonic projectiles at ranges in excess of 200 nautical miles within six minutes, a naval railgun offers a transformational solution for volume fires and time-critical strike. The range for five-inch guns on Navy ships is currently less than 15 miles.

Railguns provide a capability for sustained, offensive power projection, complementary to missiles and tactical aircraft. They may be a cost-effective solution to the Marine Corps Naval Surface Fire Support requirements because of their unique capability to simultaneously satisfy three key war-fighting objectives: extremely long ranges, short time-of-flight, and high lethality (energy-on-target).

Detection and Identification of Bacterial Agents

Researchers have used a new technique to rapidly detect and precisely identify bacteria, including dangerous E. coli, without time-consuming treatments that are usually required. The technique, called desorption electrospray ionization (DESI), could be used to create a new class of fast, accurate detectors for applications ranging from food safety to homeland security.

Using a mass spectrometer to analyze bacteria and other microorganisms ordinarily takes several hours and requires that samples be specially treated and prepared in a lengthy series of steps. The DESI eliminates the pretreatment steps, enabling researchers to take “fingerprints” of bacteria in less than a minute using a mass spectrometer.

Mass spectrometry works by turning molecules into ions, or electrically charged versions of itself, inside the instrument’s vacuum chamber. Once ionized, the molecules can be more easily manipulated, detected, and analyzed based on their masses. The key DESI innovation is performing the ionization step in the air or directly on surfaces outside of the mass spectrometer’s vacuum chamber. When combined with portable mass spectrometers, which are also under development, DESI promises to provide a new class of compact detectors.

Researchers are focusing on three potential applications for detecting and identifying pathogens: food safety, medical analysis, and homeland security. Such a detector could quickly analyze foods, medical cultures, and the air in hospitals, subway stations, and airports. Such a system could alert employees in the food and healthcare industries to the presence of pathogens and could provide security personnel with a new tool for screening suspicious suitcases or packages.

C. Development

Development takes what has been discovered or learned from basic and applied research and uses it to establish technological feasibility, assessment of operability, and production capability. Development is comprised of five stages, as defined below.

1. Advanced Technology Development is the systematic use of the knowledge or understanding gained from research directed toward proof of technological feasibility and assessment of operational and production rather than the development of hardware for service use. It employs demonstration activities intended to prove or test a technology or method.

2. Advanced Component Development and Prototypes evaluates integrated technologies in an operating environment that is as realistic as possible to assess the performance or

cost reduction potential of advanced technology. Programs in this phase are generally system specific. Major outputs of Advanced Component Development and Prototypes are hardware and software components or complete weapon systems ready for operational and developmental testing and field use.

3. System Development and Demonstration concludes the program or project and prepares it for production. It consists primarily of preproduction efforts, such as logistics and repair studies. Major outputs are weapons systems finalized for complete operational and development testing.

4. Research, Development, Test, and Evaluation Management Support is support for installations and operations for general research and development use. This category includes costs associated with test ranges, military construction maintenance support for laboratories, operation and maintenance of test aircraft and ships, and studies and analyses in support of the Research and Development program.

5. Operational Systems Development is concerned with development projects in support of programs or upgrades that are still in engineering and manufacturing development. These projects have received approval for production, for which production funds have been budgeted in subsequent fiscal years.

The following are two representative program examples for the Development category.

United States Marine Corps Increases Efforts to Modernize Truck Fleets
The United States Marine Corps General Fund has several initiatives to restore and upgrade its aging and combat-battered fleets of tactical trucks from relatively lightweight Humvees to heavy-duty cargo haulers. One of the first initiatives, for which contracts have been awarded, involves conceptual designs for a family of Joint Light Tactical Vehicles (JLTV) that the Marines and the Army need to replace the thin-skinned, 20-year-old Humvee. The Humvee, more formally known as the High Mobility Multipurpose Wheeled Vehicle, is the agile, all terrain military truck that the Military Services chose in the mid-1980s to supplant the World War II-era jeep.

The JLTV will be designed with factory-built armor but will accommodate additional protection that can be installed and removed in the field as needed. Each of the variants will be equipped with a compatible trailer and able to tow up to 10,000 pounds both on roads and cross country. The JLTV is being developed separately from the Marine Corps planned Internally Transportable Vehicle (ITV) and the Reconnaissance, Surveillance, and Targeting Vehicle (RST-V).

The ITV, a second initiative and part of the new expeditionary fire support system, is intended to transport up to four Marines, mount heavy machine guns, and tow a 120 mm mortar. It is being designed to fit inside the CH-53 Sea Stallion heavy transport helicopter and the MV-22 Osprey tilt-rotor aircraft, which neither the Humvee nor the JLTV can do.

The Marines are testing the latest version of the RST-V at Aberdeen Proving Ground, Maryland. It has a mission similar to the reconnaissance variant of the JLTV, and like the ITV, it is to be transported in the Osprey. However, unlike the JLTV and the ITV, the RST-V is to be powered by a hybrid electric-drive system that will allow it to be propelled by diesel, batteries, or a combination of the two. The idea is for the RST-V to be able to operate frequently with a mixture of diesel, electric, and battery power in order to conserve fuel and, for brief periods, to function using only stored battery energy, enabling it to move stealthily behind enemy lines.

Another Marine Corps initiative is the upgrading of its heavier trucks. A seven-ton transport, known as the Medium Tactical Vehicle Replacement (MTVR), has replaced the former five ton M-809 and M-939 series trucks. The MTVR can negotiate terrain twice as rough as its predecessors, which were based on a pre-Korean war design. It has been designed to operate 70 percent off road and 30 percent on road, just the reverse of the five-ton models.

The MTVR can carry 7.1 tons of payload cross-country and 15 tons on pavement. It can carry cargo, personnel, bulk fuel, and virtually anything required on the battlefield. The MTVR can traverse grades of 60 percent and side slopes of 30 percent, and it can ford five feet of water. On primary and secondary roads, it can cruise at 65 mph. It has an aluminum cab that folds down under the hood to make it easier to ship.

The Logistics Vehicle System Replacement (LVSR) is another initiative to update the Marine Corps' fleet of tactical trucks. The LVSR is a trailer-pulling variant of the Logistics Vehicle System (LVS), which is two decades old. Like the LVS, the LVSR will be used primarily for moving large amounts of supplies, such as ammunition, fuel, water, and heavy equipment. It can carry 33,000 pounds of off-road payload, more than twice that of its predecessor.

The LVSR offers improved survivability. It is the first vehicle that the Marine Corps has required to have armor as part of its design. The vehicle will be built with mounting points and hardware for add-on armor to reduce the time required to increase protection when needed.

Heat Induction Coatings Removal

A United States Navy aircraft carrier's flight deck experiences thousands of landings and takeoffs when deployed. Parts of the non-skid surface on the flight deck have worn away or are damaged from high temperature jet exhaust, hydrocarbon build-up, and the natural environment. The current processes for removing corrosion control coatings on ship decks are time-consuming, dangerous, noisy, and can generate significant volumes of hazardous waste.

A new technology funded by ONR's Technology Insertion Program for Savings (TIPS) and provided by engineers at NRL's Center for Corrosion Science and Engineering uses heat induction to instantaneously heat the ferrous based metal underneath a coating—be it non-skid, paint, or other hull material, bulkheads, or shaft treatments—without heating the coating itself. The heat breaks the chemical bonds between the coating and the steel deck. During the rework, all that has to be done is simply peel off the coating from the deck rather than hydro or sand blasting.

This new heat induction technology generates removed paint waste only and does it silently with components that fit in the back of a standard eight-foot pick-up truck bed making it relatively easy to move from one location to another.

The TIPS aims to significantly reduce operational and support costs through "technology insertion"—getting the right technology to the right users at the right time by using existing commercial or government technologies that need only minor additional development or certification. The goal is to use a modest amount of initial capital to create significant reductions in operations and support costs.

NON-FEDERAL PHYSICAL PROPERTY

The DON does not fund this type of Activity.

2007

General Fund

Required Supplementary Information

2007 Annual Financial Report

General Fund Required Supplementary Information

Department of the Navy
General Property, Plant, and Equipment
Real Property Deferred Maintenance
For Fiscal Year Ended September 30, 2007
($ in Thousands)

Property Type	1. Plant Replacement Value	2. Required Work (Deferred Maintenance)	3. Percentage
Category 1: Buildings, Structures, and Utilities			
Navy	$ 126,817,336	$ 19,405,486	15.3%
Marine Corps	$ 36,131,046	$ 1,065,134	2.95%
Category 2: Buildings, Structures, and Utilities			
Navy	$ 2,133,459	$ 326,419	15.3%
Marine Corps	$ 1,046,487	$ -	0.00%
Category 3: Buildings, Structures, and Utilities (Heritage Assets)			
Navy	$ 1,053,955	$ 161,255	15.3%
Marine Corps	$ 1,113,001	$ 32,811	2.95%

NOTE: In the table above, Navy real property deferred maintenance data represent both Department of the Navy (DON) General Fund and Navy Working Capital Fund (NWCF). Similarly, Marine Corps real property deferred maintenance data represent both the United States Marine Corps (USMC) General Fund and NWCF-MC.

Narrative Statement:

1. The method used to assess facilities conditions is a facilities inspection, which categorizes buildings as Adequate, Substandard or Inadequate. Those ratings are converted to Q-ratings of 100%-90% Q1; 90%-80% Q2; 80%-60% Q3; and less than 60% Q4 by assessing facilities that are rated as Adequate and less than 25 years old as Q1; facilities that are over 25 years old and rated as Adequate as Q2; facilities rated as Substandard as Q3; and Inadequate facilities as Q4.

2. There is no change since this is the first submission.

3. The Department of the Navy (DON) follows the Office of the Secretary of Defense installation strategic plan goal of having facilities at a Q2 level on average as an acceptable rating. This represents an average level of 15% of Plant Replacement Value (PRV) as an acceptable level of deferred maintenance. The table above shows that DON is approximately 15.3% below PRV. The PRV and deferred maintenance estimates are reported for the following Maintenance Fund Sources: Operation and Maintenance, Navy (O&M,N); O&M,N Reserve; Research, Development, Test, and Evaluation; Other Department of Defense; Defense Logistics Agency; NWCF; and Nonappropriated Fund. The deferred maintenance estimates are based on the facility Q-ratings found in the Navy's real property inventory. The Fiscal Year (FY) 2007 Q-ratings were set to be the lower of the Restoration Rating or Functionality Rating for each facility. The Restoration Rating assesses facility physical condition and the Functionality Rating assesses functionality or modernization deficiencies. The percentage for categories 1, 2, and 3 facilities are the same because DON cannot break out the deferred maintenance between those categories at this time.

The table above also shows that USMC is approximately 2.95% below PRV. The percentage for categories 1 and 3 facilities are the same because USMC cannot break out the deferred maintenance between those categories at this time. Category 2 is zero because USMC does not hold deferred maintenance backlogs on facilities to be demolished.

Facility Categories are as follows:

- Category 1: Buildings, Structures, and Utilities that are enduring and required to support an ongoing mission including multi-Heritage Assets.
- Category 2: Buildings, Structures, and Utilities that are excess to requirements or planned for replacement or disposal including multi-use Heritage Assets.
- Category 3: Buildings, Structures, and Utilities that are Heritage Assets.

Military Equipment
Deferred Maintenance Amounts
As of September 30, 2007
($ in Thousands)

Major Type	Amount
Aircraft	$ 47,497
Ships	26,039
Missiles	63,463
Combat Vehicles	359,739
Other Weapons Systems	269,641
Total	**$ 766,379**

Narrative Statement:

Aircraft Deferred Maintenance
Four subcategories comprise aircraft deferred maintenance: airframe rework and maintenance (active and reserve); engine rework and maintenance (active and reserve); component repair; and software maintenance. The airframe rework deferred maintenance calculation reflects unfunded requirements, which represent aircraft that failed Aircraft Service Period Adjustment inspections or reached fixed Period End Date at year-end. The engine rework deferred maintenance calculation reflects year-end actual requirements less actual funded units. Component repair deferred maintenance represents the difference between validated requirements and corresponding funding.

Airframe rework and maintenance (active and reserve) are performed under the Standard Depot Level Maintenance and Integrated Maintenance Concept (IMC) programs. Currently, the AV-8B, C-130, C-2, E-2, E-6, EA-6B, F-5, F/A-18, H-1, H-46, H-53, H-60, P-3, and S-3 aircraft programs have been incorporated under the IMC. The IMC uses Planned Maintenance Intervals, which allow for more frequent depot maintenance but with smaller work packages, thereby reducing out of service time. The goal of this program is to improve readiness while reducing operating and support costs. The Naval Air Systems Command's (NAVAIR) Industrial Strategy is to maintain the minimum level of organic capacity, consistent with force levels, which are necessary to sustain peacetime readiness and maintain fighting surge capability. The NAVAIR works in partnership with private industry to make maximum use of industry's production capabilities and for non-core related aviation depot maintenance.

Ship Deferred Maintenance
Fleet Type Commanders provide deferred ship maintenance data. Data is collected from the Current Ships Maintenance Plan database, which captures maintenance actions at all levels (organizational, intermediate, and depot) for active and reserve ships. Only depot level deferred maintenance is provided in the calculation of ship deferred maintenance. This includes maintenance actions deferred from actual depot maintenance work packages as well as maintenance deferred before inclusion in a work package due to fiscal, operational, or capacity constraints. Although there are some deferred maintenance actions,

no ships fall into the category of "unacceptable operating condition." Any ship that would be at risk of being in unacceptable operating condition would receive priority for maintenance funding to maintain acceptable operating condition.

Missile Maintenance
Four categories are used to determine missile maintenance: missiles, tactical missiles, software maintenance, and other. Deferred maintenance is defined as the difference between the total weapon maintenance requirement as determined by requirements modeling processes and the weapon maintenance that is funded in accordance with the annual budget controls for the missile maintenance program. The maintenance requirements model projects the quantity of missiles and missile components per weapon system that are required to be maintained or reworked annually.

Combat Vehicles
The combat vehicles category refers to deferred vehicle maintenance for the active and reserve Marine Corps assets. The combat vehicle category consists of weapons systems, such as the M1A1 Tank, the Amphibious Assault Vehicle, the Hercules Recovery Vehicle, and the Light Armored Vehicle. The total requirement is the planned quantity of combat vehicles that require depot level maintenance in a year as determined by program managers and the operating forces with requirements validated by a modeling process. The deferred maintenance is the difference between the validated requirements and funding received for that fiscal year.

Other Weapons Systems
The Other Weapons Systems category is comprised of ordnance, end item maintenance for support equipment, camera equipment, landing aids, calibration equipment, air traffic control equipment, target systems, expeditionary airfield equipment, special weapons, target maintenance, and repair of repairable components. Three categories define ordnance maintenance: ordnance maintenance, software maintenance, and other. Although the various programs differ in the methodology in defining requirements, all programs define deferred maintenance as the difference between validated requirements and funding.

Software Maintenance
Software maintenance requirements and deferred maintenance for aircraft, missiles, and other equipment are determined using the same methodology and therefore will not be addressed separately for each Military Equipment Deferred Maintenance reporting categories. Software maintenance includes the operational and system test software that runs in the airborne avionics systems (e.g., mission computer, display computer, and radar) and the software that runs the ground-based support labs used to perform software sustainment (e.g., compilers, editors, simulation, and configuration management).

Heritage Assets
For Fiscal Year Ended September 30, 2007

	Measurement Quantity	As of Oct 1, 2006	Additions	Deletions	As of Sep 30, 2007
Museums	Each	27	-	1	26
Monuments and Memorials	Each	552	11	44	519
Cemeteries	Sites	61	1	-	62
Archeological Sites	Sites	17,788	508	-	18,296
Buildings and Structures	Each	9,092	-	5,928	3,164
Major Collections	See table, "*Major Collections*"				

Narrative Statement:

The DON is required to report Heritage Assets in accordance with the following public laws and regulations:

- Antiquities Act of 1906
- Historic Sites Act of 1935
- USC 470 National Historic Preservation Act of 1966
- National Environmental Policy Act of 1969
- American Indian Religious Freedom Act of 1978
- Archeological Resources Protection Act of 1979
- Native American Graves Protection & Repatriation Act of 1990
- Presidential Memorandum for Heads of Executive Departments and Agencies: Government to Government Relations with Native American Tribal Governments Act of 1994
- 36 CFR 79 – Curation of Federally Owned and Administered Archeological Collections
- 36 CFR 60.4 – National Register of Historic Places
- Federal Accounting Standards Advisory Board (FASAB) Standard 29, "Heritage Assets and Stewardship Land"
- Executive Order 13287 – Preserve America – of 2003
- Executive Order 13327 – Federal Real Property Asset Management – of 2004
- SECNAVINST 5755.1A – Navy Museums – of 1992

In general, the DON defines Heritage Assets as items that are unique for one or more of the following reasons: historical or natural significance; cultural, educational, or artistic importance; or significant architectural characteristics. Monetary values are not required for Heritage Asset reporting; only physical units of measure are reported.

<u>Explanation for adjustments, additions, and deletions</u>
In FY 2007, adjustments to Archeological Sites were made after a reconciliation to the DON Federal Archeology Report was performed.

Accurate inventories of archeological artifacts, archaeological sites, and buildings and structures are dependent upon full implementation of tracking systems, notably the Internet Naval Facilities Asset Database Store (iNFADS) and the Department of the Navy Heritage Asset Management System, and related use of historic property data elements for buildings and structures.

<u>Process used to define assets as Heritage Assets</u>
The processes used to define items as having heritage significance vary among categories and type of assets being evaluated. Subject matter experts, including historians and curators, play a significant role in the definition process in addition to other criteria, such as a listing in the National Register of Historic Places. In all cases, a myriad of federal statutes, service regulations, and other guidelines mandate heritage significance or provide guidance in its determination.

<u>Multi-Use Heritage Assets</u>
Per DoD FMR Volume 6B, "Form and Content of the Department of Defense Audited Financial

Statements," Multi-Use Heritage Assets are reported as Heritage Assets in the Required Supplementary Stewardship Information and on the Balance Sheet as Real Property.

Information Pertaining to the Condition of DON Heritage Assets
The methodology used to report the condition of the heritage assets was a combination of visual assessment of the objects, historic value to the DON collection, and general display and storage standards for historic collections. The overall condition of the collection objects is good.

Museums
Museums are buildings, places, or institutions devoted to the acquisition, conservation, study, exhibition, and educational interpretation of objects having scientific, historical, or artistic value. Secretary of the Navy Instruction 5755.1A, "Navy Museums," defines the scope of the Navy Museum program.

The FY 2006 ending balance for museums was overstated by one, due to the U.S. Marine Corps museum at the Washington Navy Yard being reported in error. The museum was closed during FY 2006.

Monuments and Memorials
Monuments and Memorials have significant monetary and/or historical value to the DON.

Cemeteries
Cemeteries are government-owned burial grounds on which gravesites of prominent historical figures may be located in addition to other gravesites.

Archeological Sites
Archeological Sites are lands on which items of significance are located.

Buildings and Structures
Buildings and Structures are listed as or determined eligible for listing in the National Register of Historic Places, including Multi-Use Heritage Assets. Criteria for evaluating National Register eligibility of these sites may be referenced at 36 CFR 60.4.

Supplemental Reporting. In addition to the data presented in the table, "Heritage Assets," above, the following supplemental information on Major Collections was reported as of September 30, 2007:

Major Collections

Category	Measurement Quantity	As of Oct 1, 2006	Additions	Deletions	As of Sep 30, 2007
Archeological Artifacts	Cubic Feet	35,174	23	13	35,184
Archival	Linear Feet	98,148	164	-	98,312
Artwork	Item	38,540	188	-	38,728
Historical Artifacts	Item	1,141,747	797	-	1,142,544

Archeological Artifacts
The FY 2006 ending balance was adjusted upward by 17,124 Archeological Artifacts resulting in an FY 2007 beginning balance of 35,174. This adjustment reflects the correction of an error in the prior reporting period.

Archival
The FY 2007 net increase of 164 Artwork items reflects normal acquisitions and donations.

Artwork
The FY 2006 ending balance was adjusted downward by 262 items resulting in an FY 2007 beginning balance of 38,540. This adjustment reflects the correction of an error in the prior reporting period.

Historical Artifacts
The FY 2006 ending balance was adjusted downward by 3,988 items resulting in an FY 2007 beginning balance of 1,141,747. This adjustment reflects the correction of an error in the prior reporting period.

STEWARDSHIP LAND
For Fiscal Year Ended September 30, 2007
(Acres in Thousands)

Land Use	As of Oct 1, 2006	Additions	Deletions	As of Sep 30, 2007
Mission	2,026	76	9	2,093
Parks and Historic Sites	0	0	0	0
Totals	**2,026**	**76**	**9**	**2,093**

Narrative Statement

The DON followed the definition of Stewardship Land per the DoD FMR to include Public Domain, Land Set Aside, and Donated Land. The iNFADS was used to derive acres for Stewardship Land. Within the definition of Stewardship Land, land can be further categorized as Improved, Semi-Improved, or Other.

Department of Defense
Department of the Navy

DISAGGREGATED STATEMENT OF BUDGETARY RESOURCES

For the Years Ended September 30, 2007 and 2006
($ in Thousands)

	Other	Research, Development, Test & Evaluation	Operation and Maintenance	Procurement
BUDGETARY FINANCING ACCOUNTS				
BUDGETARY RESOURCES				
Unobligated balance, brought forward, October 1	$ 19,276	$ 2,127,404	$ 1,207,826	$ 15,831,434
Recoveries of prior year unpaid obligations	508	306,387	2,940,236	12,509,699
Budget authority				
Appropriation	324,489	19,203,722	46,986,844	41,570,580
Borrowing authority	0	0	0	0
Contract authority	0	0	0	0
Spending authority from offsetting collections				
Earned				
Collected	1,186	432,800	5,462,685	839,295
Change in receivables from Federal sources	(1,186)	24,306	268,023	(61,903)
Change in unfilled customer orders				
Advance received	0	15,228	(3,223)	0
Without advance from Federal sources	0	(56,946)	(312,127)	137,976
Anticipated for rest of year, without advances	0	0	0	0
Previously unavailable	0	0	0	0
Expenditure transfers from trust funds	0	0	0	0
Subtotal	324,489	19,619,110	52,402,202	42,485,948
Nonexpenditure transfers, net, anticipated and actual	(301,520)	628,976	155,370	(87,547)
Temporarily not available pursuant to Public Law	0	0	0	0
Permanently not available	0	(167,658)	(628,853)	(475,462)
Total Budgetary Resources	$ 42,753	$ 22,514,219	$ 56,076,781	$ 70,264,072
Status of Budgetary Resources:				
Obligations incurred:				
Direct	$ 32,631	$ 19,586,274	$ 48,637,839	$ 51,861,905
Reimbursable	0	394,907	5,945,858	279,536
Subtotal	32,631	19,981,181	54,583,697	52,141,441
Unobligated balance:				
Apportioned	10,121	2,338,485	166,702	17,801,245
Exempt from apportionment	0	0	0	0
Subtotal	10,121	2,338,485	166,702	17,801,245
Unobligated balance not available	0	194,553	1,326,383	321,386
Total Status of Budgetary Resources	$ 42,752	$ 22,514,219	$ 56,076,782	$ 70,264,072
Change in Obligated Balance:				
Obligated balance, net				
Unpaid obligations, brought forward, October 1	$ 59,227	$ 8,858,576	$ 19,110,166	$ 46,879,702
Less: Uncollected customer payments from Federal sources, brought forward, October 1	0	(373,196)	(1,700,757)	(105,891)
Total unpaid obligated balance	59,227	8,485,380	17,409,409	46,773,811
Obligations incurred net (+/-)	32,631	19,981,181	54,583,697	52,141,441
Less: Gross outlays	(19,468)	(19,200,372)	(49,712,310)	(35,457,000)
Obligated balance transferred, net				
Actual transfers, unpaid obligations (+/-)	0	0	0	0
Actual transfers, uncollected customer payments from Federal sources (+/-)	0	0	0	0
Total Unpaid obligated balance transferred, net	0	0	0	0
Less: Recoveries of prior year unpaid obligations, actual	(508)	(306,387)	(2,940,236)	(12,509,699)
Change in uncollected customer payments from Federal sources (+/-)	1,186	32,641	44,103	(76,073)
Obligated balance, net, end of period				
Unpaid obligations	71,882	9,332,998	21,041,317	51,054,445
Less: Uncollected customer payments (+/-) from Federal sources (-)	1,186	(340,556)	(1,656,654)	(181,964)
Total, unpaid obligated balance, net, end of period	73,068	8,992,442	19,384,663	50,872,481
Net Outlays:				
Gross outlays	19,468	19,200,372	49,712,310	35,457,000
Less: Offsetting collections	(1,186)	(448,029)	(5,459,462)	(839,295)
Less: Distributed Offsetting receipts	(268,762)	0	(1,810)	0
Net Outlays	$ (250,480)	$ 18,752,343	$ 44,251,038	$ 34,617,705

Department of Defense
Department of the Navy

DISAGGREGATED STATEMENT OF BUDGETARY RESOURCES

For the Years Ended September 30, 2007 and 2006
($ in Thousands)

	Military Personnel	Military Construction/ Family Housing	2007 Combined	2006 Combined
BUDGETARY FINANCING ACCOUNTS				
BUDGETARY RESOURCES				
Unobligated balance, brought forward, October 1	$ 199,479	$ 1,450,555	$ 20,835,975	$ 17,128,479
Recoveries of prior year unpaid obligations	753,197	(1,727)	16,508,300	5,261,990
Budget authority				
Appropriation	40,821,621	1,849,811	150,757,067	145,511,602
Borrowing authority	0	0	0	0
Contract authority	0	0	0	0
Spending authority from offsetting collections				
Earned				
Collected	368,213	586,082	7,690,260	7,767,620
Change in receivables from Federal sources	(2,851)	91,231	317,620	(948,730)
Change in unfilled customer orders				
Advance received	0	38,486	50,491	54,329
Without advance from Federal sources	17,560	220,855	7,319	519,073
Anticipated for rest of year, without advances	0	0	0	0
Previously unavailable	0	0	0	0
Expenditure transfers from trust funds	0	0	0	0
Subtotal	41,204,543	2,786,465	158,822,757	152,903,894
Nonexpenditure transfers, net, anticipated and actual	29,262	(280,367)	144,174	667,410
Temporarily not available pursuant to Public Law	0	0	0	0
Permanently not available	(20,469)	(35,681)	(1,328,122)	(3,253,303)
Total Budgetary Resources	$ 42,166,012	$ 3,919,245	$ 194,983,084	$ 172,708,470
Status of Budgetary Resources:				
Obligations incurred:				
Direct	$ 41,508,547	$ 1,670,610	$ 163,297,807	$ 146,006,781
Reimbursable	382,592	747,837	7,750,730	5,865,715
Subtotal	41,891,139	2,418,447	171,048,537	151,872,496
Unobligated balance:				
Apportioned	25,757	1,423,515	21,765,826	19,197,595
Exempt from apportionment	0	0	0	0
Subtotal	25,757	1,423,515	21,765,826	19,197,595
Unobligated balance not available	249,116	77,283	2,168,721	1,638,379
Total Status of Budgetary Resources	$ 42,166,012	$ 3,919,245	$ 194,983,084	$ 172,708,470
Change in Obligated Balance:				
Obligated balance, net				
Unpaid obligations, brought forward, October 1	$ 910,097	$ 2,270,253	$ 78,088,020	$ 72,093,186
Less: Uncollected customer payments from Federal sources, brought forward, October 1	(27,105)	(764,208)	(2,971,157)	(3,400,814)
Total unpaid obligated balance	882,992	1,506,045	75,116,863	68,692,372
Obligations incurred net (+/-)	41,891,139	2,418,447	171,048,537	151,872,496
Less: Gross outlays	(40,079,628)	(1,968,402)	(146,437,179)	(140,615,673)
Obligated balance transferred, net				
Actual transfers, unpaid obligations (+/-)	0	0	0	0
Actual transfers, uncollected customer payments from Federal sources (+/-)	0	0	0	0
Total Unpaid obligated balance transferred, net	0	0	0	0
Less: Recoveries of prior year unpaid obligations, actual	(753,197)	1,727	(16,508,300)	(5,261,990)
Change in uncollected customer payments from Federal sources (+/-)	(14,709)	(312,086)	(324,938)	429,657
Obligated balance, net, end of period				
Unpaid obligations	1,968,411	2,722,024	86,191,077	78,088,020
Less: Uncollected customer payments (+/-) from Federal sources (-)	(41,814)	(1,076,294)	(3,296,095)	(2,971,157)
Total, unpaid obligated balance, net, end of period	1,926,597	1,645,730	82,894,982	75,116,863
Net Outlays:				
Gross outlays	40,079,628	1,968,402	146,437,179	140,615,673
Less: Offsetting collections	(368,213)	(624,568)	(7,740,753)	(7,821,950)
Less: Distributed Offsetting receipts	0	0	(270,572)	(149,284)
Net Outlays	$ 39,711,415	$ 1,343,834	$ 138,425,854	$ 132,644,439

Schedule, Part A DoD Intra-governmental Asset Balances. *($ in Thousands)*	**Treasury Index:**	**Fund Balance with Treasury**	**Accounts Receivable**	**Loans Receivable**	**Investments**	**Other**
Government Printing Office	4	$0	$1	$0	$0	$0
Executive Office of the President	11	0	3,240	0	0	0
Department of Agriculture	12	0	316	0	0	0
Department of Commerce	13	0	638	0	0	2,316
Department of the Interior	14	0	16	0	0	23,638
Department of Justice	15	0	2,536	0	0	4,329
United States Postal Service	18	0	60	0	0	0
Department of State	19	0	3,956	0	0	0
Department of the Treasury	20	107,344,401	228	0	9,756	59
Army General Fund	21	0	30,716	0	0	1,265
Resolution Trust Corporation	22	0	6	0	0	0
Office of Personnel Management	24	0	1	0	0	36,911
Nuclear Regulatory Commission	31	0	91	0	0	0
Department of Veterans Affairs	36	0	818	0	0	0
General Service Administration	47	0	0	0	0	6,810
National Science Foundation	49	0	582	0	0	66
Air Force General Fund	57	0	5,280	0	0	234,131
Environmental Protection Agency	68	0	0	0	0	2,391
Department of Transportation	69	0	204	0	0	78,519
Homeland Security	70	0	15,797	0	0	717
Small Business Administration	73	0	0	0	0	68
Department of Health and Human Services	75	0	478	0	0	24
National Aeronautics and Space Administration	80	0	2,854	0	0	5,975
Department of Housing and Urban Development	86	0	6	0	0	0
Department of Energy	89	0	1,107	0	0	306
Selective Service System	90	0	0	0	0	0
Department of Education	91	0	15	0	0	0
US Army Corps of Engineers	96	0	2,394	0	0	0
Other Defense Organizations General Funds	97	0	33,375	0	0	4,255
Other Defense Organizations Working Capital Funds	97-4930	0	19,074	0	0	4,197
Army Working Capital Fund	97-4930.001	0	756	0	0	0
Navy Working Capital Fund	97-4930.002	0	81,232	0	0	(5,715)
Air Force Working Capital Fund	97-4930.003	0	310	0	0	0
Totals might not match to the Principal Statements	**TOTALS**	**$107,344,401**	**$206,087**	**$0**	**$9,756**	**$400,262**

Schedule, Part B DoD Intra-governmental entity liabilities. ***($ in Thousands)***	**Treasury Index:**	**Accounts Payable**	**Debts/Borrowings From Other Agencies**	**Other**
Department of Agriculture	12	$1,077	$0	$0
Department of Commerce	13	1,633	0	0
Department of the Interior	14	5,841	0	0
Department of Justice	15	2,782	0	0
Department of Labor	16	0	0	635,714
United States Postal Service	18	14,464	0	0
Department of State	19	14,590	0	0
Department of the Treasury	20	26,827	0	0
Army General Fund	21	61,726	0	0
Office of Personnel Management	24	691	0	42,452
Federal Communications Commission	27	755	0	0
Nuclear Regulatory Commission	31	23	0	0
Department of Veterans Affairs	36	2,798	0	0
General Service Administration	47	96,999	0	0
National Science Foundation	49	672	0	0
Air Force General Fund	57	42,101	0	0
Tennessee Valley Authority	64	446	0	0
Environmental Protection Agency	68	408	0	0
Department of Transportation	69	37,335	0	0
Homeland Security	70	14,418	0	0
Small Business Administration	73	38	0	0
Department of Health and Human Services	75	88	0	0
National Aeronautics and Space Administration	80	26,829	0	0
Department of Energy	89	128,038	0	0
US Army Corps of Engineers	96	(63)	0	0
Other Defense Organizations General Funds	97	44,587	0	1,960
The General Fund of the Treasury	99	0	0	3,962,692
Other Defense Organizations Working Capital Funds	97-4930	264,487	0	0
Army Working Capital Fund	97-4930.001	12,925	0	0
Navy Working Capital Fund	97-4930.002	569,352	0	0
Air Force Working Capital Fund	97-4930.003	4,701	0	0
Military Retirement Fund	97-8097	118,949	0	0
Totals might not match to the Principal Statements	**TOTALS**	**$1,495,517**	**$0**	**$4,642,818**

Schedule, Part C DoD Intra-governmental revenue and related costs. ***($ in Thousands)***	**Treasury Index:**	**Earned Revenue**
Government Printing Office	4	$118
Executive Office of the President	11	32,279
Department of Agriculture	12	59,321
Department of Commerce	13	11,521
Department of the Interior	14	143
Department of Justice	15	12,107
United States Postal Service	18	87
Department of State	19	8,679
Department of the Treasury	20	1,901
Army General Fund	21	637,053
Resolution Trust Corporation	22	19
Office of Personnel Management	24	29
Nuclear Regulatory Commission	31	759
Department of Veterans Affairs	36	3,380
General Service Administration	47	12
National Science Foundation	49	4,266
Air Force General Fund	57	219,191
Environmental Protection Agency	68	150
Department of Transportation	69	4,345
Homeland Security	70	72,618
Department of Health and Human Services	75	3,894
National Aeronautics and Space Administration	80	5,493
Department of Housing and Urban Development	86	126
Department of Energy	89	5,254
Selective Service System	90	9
Department of Education	91	1,843
Independent Agencies	95	154
US Army Corps of Engineers	96	11,780
Other Defense Organizations General Funds	97	617,481
Other Defense Organizations Working Capital Funds	97-4930	220,297
Army Working Capital Fund	97-4930.001	21,825
Navy Working Capital Fund	97-4930.002	1,376,637
Air Force Working Capital Fund	97-4930.003	4,955
DoD Medicare-Eligible Retiree Health Care Fund		115,961
Totals might not match to the Principal Statements	**TOTALS**	**$3,453,687**

Schedule, Part E DoD Intra-governmental non-exchange revenues. *($ in Thousands)*	**Treasury Index:**	**Transfers In**	**Transfers Out**
Department of the Treasury	20	$189	$0
Air Force General Fund	57	12,648	0
Other Defense Organizations General Funds	97	45,923	0
Other Defense Organizations Working Capital Funds	97-4930	32,712	0
Army Working Capital Fund	97-4930.001	66,000	0
Air Force Working Capital Fund	97-4930.003	100,000	0
Totals might not match to the Principal Statements	**TOTALS**	**$257,472**	**$0**

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General Fund

Other Accompanying Information

Appropriations, Funds, and Accounts Included in the Principal Statements

Entity Accounts

General Funds

17X0380	Coastal Defense Augmentation, Navy
17 0703	Family Housing, Navy and Marine Corps
17 0730	Family Housing Construction, Navy and Marine Corps
17 0735	Family Housing Operation and Maintenance, Navy and Marine Corps
17X0810	Environmental Restoration, Navy
17 1000	Medicare Eligible Retiree Health Care Fund, Military Personnel Navy
17 1001	Medicare Eligible Retiree Health Care Fund, Military Personnel Marine Corps
17 1002	Medicare Eligible Retiree Health Care Fund, Reserve Personnel Navy
17 1003	Medicare Eligible Retiree Health Care Fund, Reserve Personnel Marine Corps
17 1105	Military Personnel, Marine Corps
17 1106	Operation and Maintenance, Marine Corps
17 1107	Operation and Maintenance, Marine Corps Reserve
17 1108	Reserve Personnel, Marine Corps
17 1109	Procurement, Marine Corps
17 1205	Military Construction, Navy and Marine Corps
17 1235	Military Construction, Naval Reserve
17 1236	Payments to Kaho Olawe Island Conveyance, Remediation and Environmental Restoration Fund, Navy
17 1319	Research, Development, Test and Evaluation, Navy
17 1405	Reserve Personnel, Navy
17 1453	Military Personnel, Navy
17 1506	Aircraft Procurement, Navy
17 1507	Weapons Procurement, Navy
17 1508	Procurement of Ammunition, Navy and Marine Corps
17 1611	Shipbuilding and Conversion
17 1804	Operation and Maintenance, Navy
17 1806	Operation and Maintenance, Navy Reserve
17 1810	Other Procurement, Navy

Revolving Funds

17X4557	National Defense Sealift Fund, Navy

Earmarked Trust Funds

17X8716	Department of the Navy General Gift Fund
17X8723	Ships Stores Profits, Navy
17X8733	United States Naval Academy General Gift Fund

Earmarked Special Funds

17X5095	Wildlife Conservation, Military Reservations, Navy
17X5185	Kaho Olawe Island Conveyance, Remediation and Environmental Restoration Fund, Navy
17X5429	Rossmoor Liquidating Trust Settlement Account
17X5562	Ford Island Improvement Account

General Fund Non- Entity Accounts

17 1XXX	Receipt Accounts
17 3XXX	Receipt Accounts
17X6XXX	Deposit Funds

Parent-Child (Allocation) Transfer Accounts

17 11 1081	International Military Education and Training Funds, appropriated to the President
17 11X1081	International Military Education and Training Funds, appropriated to the President
17 11 1082	Foreign Military Financing Program, Funds appropriated to the President
17 12X1105B	State and Private Forestry, Forest Service
17 69X8083	Federal-Aid Highways (Liquidation of Contract Authorization), Federal Highway Administration

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Navy Working Capital Fund
Principal Statements

2007 Annual Financial Report

Limitations to the Financial Statements

The principal financial statements have been prepared to report the financial position and results of operations of the entity, pursuant to the requirements of 31 United States Code 3515 (b). While the statements have been prepared from the books and records of the entity in accordance with Generally Accepted Accounting Principles for Federal entities and 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.

Principal Statements

The Fiscal Year 2007 Navy Working Capital Fund Principal Statements and related notes are presented in the format prescribed by the Department of Defense Financial Management Regulation 7000.14, Volume 6B. The statements and related notes summarize financial information for individual activity groups and activities within the Navy Working Capital Fund for the fiscal year ending September 30, 2007, and are presented on a comparative basis with information previously reported for the fiscal year ending September 30, 2006.

The following statements comprise the Navy Working Capital Fund Principal Statements:

- Consolidated Balance Sheet
- Consolidated Statement of Net Cost
- Consolidated Statement of Changes in Net Position
- Combined Statement of Budgetary Resources

The Principal Statements and related notes have been prepared to report financial position pursuant to the requirements of the Chief Financial Officers Act of 1990, as amended by the Government Management Reform Act of 1994. The accompanying notes should be considered an integral part of the Principal Statements.

Department of Defense
Navy Working Capital Fund

CONSOLIDATED BALANCE SHEET

As of September 30, 2007 and 2006
($ in Thousands)

		2007 Consolidated		2006 Consolidated
ASSETS (Note 2)				
Intragovernmental:				
Fund Balance with Treasury (Note 3)				
Entity	$	1,156,401	$	1,244,509
Non-Entity Seized Iraqi Cash		0		0
Non-Entity - Other		0		0
Investments (Note 4)		0		0
Accounts Receivable (Note 5)		698,039		444,251
Other Assets (Note 6)		3,886		1,941
Total Intragovernmental Assets		1,858,326		1,690,701
Cash and Other Monetary Assets (Note 7)		0		0
Accounts Receivable, Net (Note 5)		86,078		69,356
Loans Receivable (Note 8)		0		0
Inventory and Related Property, Net (Note 9)		12,671,057		13,806,149
General Property, Plant and Equipment, Net (Note 10)		3,404,310		3,769,854
Investments (Note 4)		0		0
Other Assets (Note 6)		294,072		363,465
TOTAL ASSETS		18,313,843		19,699,525
LIABILITIES (Note 11)				
Intragovernmental:				
Accounts Payable (Note 12)		207,232		143,723
Debt (Note 13)		70,697		173,224
Other Liabilities (Note 15 & Note 16)		179,553		230,190
Total Intragovernmental Liabilities		457,482		547,137
Accounts Payable (Note 12)		3,381,559		1,485,833
Military Retirement and Other Federal Employment Benefits (Note 17)		1,047,589		1,185,039
Environmental and Disposal Liabilities (Note 14)		0		0
Loan Guarantee Liability (Note 8)		0		0
Other Liabilities (Note 15 & Note 16)		1,445,842		3,549,935
TOTAL LIABILITIES		6,332,472		6,767,944
NET POSITION				
Unexpended Appropriations - Earmarked Funds (Note 23)		0		0
Unexpended Appropriations - Other Funds		33,595		2,896
Cumulative Results of Operations - Earmarked Funds		0		0
Cumulative Results of Operations - Other Funds		11,947,776		12,928,685
TOTAL NET POSITION		11,981,371		12,931,581
TOTAL LIABILITIES AND NET POSITION	$	18,313,843	$	19,699,525

The accompanying notes are an integral part of the statements.

Department of Defense

Navy Working Capital Fund

CONSOLIDATED STATEMENT OF NET COST

For the Years Ended September 30, 2007 and 2006

($ in Thousands)

	2007 Consolidated	2006 Consolidated
Program Costs		
Gross Costs	$ 23,582,179	$ 24,097,994
Less: Earned Revenue	(22,257,566)	(22,373,405)
Net Costs	1,324,613	1,724,589
Costs Not Assigned to Programs	0	0
Less: Earned Revenue Not Attributable to Programs	0	0
Net Cost of Operations	$ 1,324,613	$ 1,724,589

The accompanying notes are an integral part of the statements.

Department of Defense

Navy Working Capital Fund

CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION

For the Years Ended September 30, 2007 and 2006

($ in Thousands)

	2007 Consolidated	2006 Consolidated
CUMULATIVE RESULTS OF OPERATIONS		
Beginning Balances	$ 12,928,685	$ 13,540,239
Prior Period Adjustments:		
Changes in accounting principles (+/-)	0	0
Correction of errors (+/-)	0	0
Beginning Balances, as adjusted	12,928,685	13,540,239
Budgetary Financing Sources:		
Other adjustments (rescissions, etc) (+/-)	0	0
Appropriations used	85,166	121,857
Nonexchange revenue	0	0
Donations and forfeitures of cash and cash equivalents	0	0
Transfers in/out without reimbursement (+/-)	112,504	(46,097)
Other budgetary financing sources (+/-)	0	0
Other Financing Sources:		
Donations and forfeitures of property	0	0
Transfers in/out without reimbursement (+/-)	17,242	(89,398)
Imputed financing from costs absorbed by others	475,066	559,297
Other (+/-)	(346,274)	567,376
Total Financing Sources	343,704	1,113,035
Net Cost of Operations (+/-)	1,324,613	1,724,589
Net Change	(980,909)	(611,554)
Cumulative Results of Operations	$ 11,947,776	$ 12,928,685
UNEXPENDED APPROPRIATIONS		
Beginning Balances	$ 2,896	$ 6,286
Prior Period Adjustments (+/-)		
Changes in accounting principles (+/-)	0	0
Correction of errors (+/-)	0	0
Beginning Balances, as adjusted	2,896	6,286
Budgetary Financing Sources:		
Appropriations received	116,192	118,467
Appropriations transferred-in/out (+/-)	0	0
Other adjustments (rescissions, etc) (+/-)	(327)	0
Appropriations used	(85,166)	(121,857)
Total Budgetary Financing Sources	30,699	(3,390)
Unexpended Appropriations	33,595	2,896
Net Position	$ 11,981,371	$ 12,931,581

The accompanying notes are an integral part of the statements.

Department of Defense
Navy Working Capital Fund

COMBINED STATEMENT OF BUDGETARY RESOURCES

For the Years Ended September 30, 2007 and 2006
($ in Thousands)

	2007 Combined	2006 Combined
BUDGETARY FINANCING ACCOUNTS		
Budgetary Resources:		
Unobligated balance, brought forward, October 1	$ 2,547,953	$ 2,816,660
Recoveries of prior year unpaid obligations	31,229	0
Budget Authority:		
Appropriations received	116,192	118,467
Borrowing authority	0	0
Contract authority	5,673,309	4,903,708
Spending authority from offsetting collections:		
Earned		
Collected	23,784,389	24,056,575
Change in receivables from Federal sources	263,324	108,975
Change in unfilled customer orders		
Advances received	(4,720)	(159,907)
Without advance from Federal sources	(357,667)	(371,044)
Anticipated for rest of year, without advances	0	0
Previously unavailable	0	0
Expenditure Transfers from trust funds	0	0
Subtotal	29,474,827	28,656,774
Nonexpenditure Transfers, net, anticipated and actual	112,504	(46,097)
Temporarily not available pursuant to Public Law	0	0
Permanently not available	(6,597,645)	(5,936,931)
Total Budgetary Resources	25,568,868	25,490,406
Status of Budgetary Resources:		
Obligations incurred:		
Direct	599	39,985
Reimbursable	24,043,103	22,902,470
Subtotal	24,043,702	22,942,455
Unobligated balance:		
Apportioned	1,525,168	2,796,842
Exempt from apportionment	(60,183)	(441,211)
Subtotal	1,464,985	2,355,631
Unobligated balances not available	60,181	192,320
Total Status of Budgetary Resources	$ 25,568,868	$ 25,490,406

The accompanying notes are an integral part of the statements.

Department of Defense
Navy Working Capital Fund

COMBINED STATEMENT OF BUDGETARY RESOURCES

For the Years Ended September 30, 2007 and 2006
($ in Thousands)

	2007 Combined	2006 Combined
RELATIONSHIP OF OBLIGATIONS TO OUTLAYS		
Change in Obligated Balance:		
Obligated balance, net		
Unpaid obligations, brought forward, October 1	$ 12,112,506	$ 12,667,320
Less: Uncollected customer payments from Federal sources, brought forward, October 1	(7,376,260)	(7,638,329)
Total Unpaid Obligated Balance	4,736,246	5,028,991
Obligations incurred, net (+/-)	24,043,702	22,942,454
Less: Gross outlays	(23,995,180)	(23,497,266)
Obligated balance transferred, net		
Actual transfers, unpaid obligations (+/-)	0	0
Actual transfers, uncollected customer payments from Federal sources (+/-)	0	(1)
Total Unpaid Obligated Balance Transferred, net	0	0
Less: Recoveries of prior year unpaid obligations, actual	(31,229)	0
Change in uncollected customer payments from Federal sources (+/-)	94,343	262,068
Obligated balance, net, end of period		
Unpaid obligations	12,129,800	12,112,506
Less: Uncollected customer payments from Federal sources	(7,281,919)	(7,376,260)
Total Unpaid Obligated Balance, net, end of period	4,847,881	4,736,246
Net Outlays:		
Gross Outlays	23,995,180	23,497,266
Less: Offsetting collections	(23,779,670)	(23,896,668)
Less: Distributed Offsetting receipts	0	0
Net Outlays	$ 215,510	$ (399,402)

The accompanying notes are an integral part of the statements.

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Navy Working Capital Fund

Notes to the Principal Statements

2007 Annual Financial Report

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Note 1. Significant Accounting Policies

1.A. Basis of Presentation

These financial statements have been prepared to report the financial position and results of operations of the Navy Working Capital Fund (NWCF), as required by the Chief Financial Officers (CFO) Act of 1990, expanded by the Government Management Reform Act of 1994, and other appropriate legislation. The financial statements have been prepared from the books and records of NWCF in accordance with the Department of Defense (DoD) Financial Management Regulation, the Office of Management and Budget (OMB) Circular A-136, Financial Reporting Requirements, and to the extent possible Generally Accepted Accounting Principles (GAAP). Effective 4th Quarter, Fiscal Year (FY) 2006, DoD no longer publishes consolidating/combining financial statements. The accompanying financial statements account for all resources for which NWCF is responsible unless otherwise noted. Information relative to classified assets, programs, and operations is excluded from the statements or otherwise aggregated and reported in such a manner that it is not discernable.

The NWCF is unable to fully implement all elements of GAAP and OMB Circular A-136 due to limitations of its financial and nonfinancial management processes and systems that feed into the financial statements. The NWCF derives its reported values and information for major asset and liability categories largely from nonfinancial systems, such as inventory and logistic systems. These systems were designed to support reporting requirements for maintaining accountability over assets and reporting the status of federal appropriations rather than preparing financial statements in accordance with GAAP. The NWCF continues to implement processes and system improvements addressing these limitations. The DoD currently has several auditor identified financial statement material weaknesses. Of these, NWCF has the following: Fund Balance with Treasury; General Property, Plant, and Equipment; Inventory; and Accounts Payable.

1.B. Mission of the Reporting Entity

The Department of the Navy (DON) was created on April 30, 1798 by an act of Congress (I Stat.533; 5 U.S.C. 411-12). The overall mission of DON is to maintain, train, and equip combat-ready Navy and Marine Corps forces capable of winning wars, deterring aggression and maintaining freedom of the seas. The NWCF provides goods, services, and infrastructure to DON and other DoD customers to help ensure our military forces are mobile, ready, and have the most advanced technology.

1.C. Appropriations and Funds

The NWCF receives its appropriations and funds as working capital (revolving) funds. The NWCF uses these appropriations and funds to execute its missions and subsequently report on resource usage.

Working capital funds (WCF) received funding to establish an initial corpus through an appropriation or a transfer of resources from existing appropriations or funds. The corpus finances operations and transactions that flow through the fund. The WCF resources the goods and services sold to customers on a reimbursable basis and maintains the corpus.

Reimbursable receipts fund future ongoing operations and generally are available in their entirety for use without further congressional action. At various times, the Congress provides additional appropriations to supplement WCF as an infusion of cash when revenues are inadequate to cover costs within the corpus.

1.D. Basis of Accounting

For FY 2007, NWCF's financial management systems are unable to meet all of the requirements for full accrual accounting. Many of NWCF's financial and nonfinancial feeder systems and processes were designed and implemented prior to the issuance of GAAP for federal agencies. These systems were not designed to collect and record financial information on the full accrual accounting basis as required by GAAP. Some NWCF budgetary accounts are not transaction driven. In certain cases, proprietary and statistical accounts are used to generate the budgetary accounts required to produce the Report on Budget Execution (SF 133) and Statement of Budgetary Resources. Therefore, amounts between the two will not necessarily align. The NWCF is working to correct this weakness.

The DoD has undertaken efforts to determine the actions required to bring its financial and nonfinancial feeder systems and processes into compliance with GAAP. One such action is the current revision of its accounting systems to record transactions based on the U.S. Standard General Ledger (USSGL). Until all of NWCF's financial and nonfinancial feeder systems and processes are updated to collect and report financial information as required by GAAP, NWCF's financial data will be derived from transactions from nonfinancial feeder systems, and accruals are made for major items such as payroll expenses and accounts payable.

In addition, DoD identifies program costs based upon the major appropriation groups provided by the Congress. Current processes and systems do not capture and report accumulated costs for major programs based upon the performance measures as required by the Government Performance and Results Act. The DoD is working towards a cost reporting methodology that meets the need for cost information required by the Statement of Federal Financial Accounting Standards (SFFAS) No. 4, "Managerial Cost Accounting Concepts and Standards for the Federal Government".

1.E. Revenues and Other Financing Sources

Depot Maintenance WCF activities recognize revenue according to the percentage of completion method. Research and Development activities recognize revenue according to the percentage of completion method or as actual costs are incurred and billed. Supply Management WCF activities recognize revenue from the sale of inventory items. Revenue is recognized at the time service is rendered for Base Support WCF activities. The Transportation WCF activity recognizes revenue on either a reimbursable or per diem basis.

The NWCF does not include nonmonetary support provided by U.S. allies for common defense and mutual security in amounts reported in the Statement of Net Cost and the Note 21, Reconciliation of Net Cost of Operations to Budget. The U.S. has cost sharing agreements with other countries. Examples include countries where there is a mutual or reciprocal defense agreement, where U.S. troops are stationed, or where the U.S. Fleet is in a port.

1.F. Recognition of Expenses

For financial reporting purposes, DoD policy requires the recognition of operating expenses in the period incurred. However, because NWCF's financial and nonfinancial feeder systems were not designed to collect and record financial information on the full accrual accounting basis, accruals are made for major items such as payroll expenses, accounts payable, and unbilled revenue. In the case of Operating Materiels and Supplies (OM&S), operating expenses are generally recognized when the items are purchased. Efforts are underway to transition towards the consumption method for recognizing OM&S expenses.

1.G. Accounting for Intragovernmental Activities

Preparation of reliable financial statements requires the elimination of transactions occurring among entities within DoD or between two or more federal agencies. However, NWCF cannot accurately match buyer and seller transactions by customer because NWCF's systems do not track at the transaction level. Generally, seller entities within DoD provide summary seller-side balances for revenue, accounts receivable, and unearned revenue to the buyer-side internal DoD accounting offices. In most cases, where the numbers do not match, buyer-side records are adjusted to agree with DoD seller-side balances. IntraDoD intragovernmental balances are then eliminated. The volume of intragovernmental transactions is so large that after-the-fact reconciliation cannot be accomplished effectively with existing or foreseeable resources. The DoD is developing long-term system improvements to ensure intragovernmental information, to include sufficient up-front edits and controls eliminating the need for after-the-fact reconciliations.

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

The DoD's proportionate share of public debt and related expenses of the Federal Government is not included. The Federal Government does not apportion debt and its related costs to federal agencies. The DoD's financial statements, therefore, do not report any portion of the public debt or interest thereon, nor do the statements report the source of public financing whether from issuance of debt or tax revenues.

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

1.H. Transactions with Foreign Governments and International Organizations

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

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

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

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

1.J. Foreign Currency

Not Applicable.

1.K. Accounts Receivable

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

1.L. Direct Loans and Loan Guarantees

Not Applicable.

1.M. Inventories and Related Property

All of NWCF's inventories are currently reported at an approximation of historical cost using latest acquisition cost adjusted for holding gains and losses. The latest acquisition cost method is used because legacy inventory systems were designed for materiel management rather than accounting. Although these systems provide visibility and accountability over inventory items, they do not maintain historical cost data necessary to comply with SFFAS No. 3, Accounting for Inventory and Related Property. Additionally, these systems cannot produce financial transactions using USSGL, as required by the Federal Financial Management Improvement Act of 1996 (P.L. 104-208). At the current time, NWCF does not report any inventory using the moving average cost method. However, by utilizing new system development processes, NWCF will be transitioning to the moving average cost method with the implementation of the Navy Enterprise Resource Planning (ERP).

The NWCF manages only military or government specific materiel under normal conditions. Materiel is a unique term that relates to military force management, and includes items such as weapons systems, spare parts and repair parts necessary to equip, operate, maintain, and support military activities without distinction as to its application for administrative or combat purposes. Items commonly used in and available from the commercial sector are not managed in NWCF materiel management activities. Operational cycles are irregular and the military risks associated with stock-out positions have no commercial parallel. The NWCF holds materiel based on military need and support for contingencies. The DoD does not attempt to account separately for "inventory held for sale" and "inventory held in reserve for future sale" based on SFFAS No. 3 definitions, unless otherwise noted.

Related property includes OM&S and stockpile materiels. The OM&S, including munitions not held for sale, are valued at standard purchase price. The NWCF uses both the consumption method and the purchase method of accounting for OM&S. Items that are centrally managed and stored, such as ammunition and engines, are generally recorded using the consumption method and are reported on the Balance Sheet as OM&S. When current systems cannot fully support the consumption method, NWCF uses the purchase method. Under this method, materiels and supplies are expensed when purchased. During FY 2007, NWCF expensed significant amounts using the purchase method because the systems could not support the consumption method or management deemed that the item was in the hands of the end user. This is a material weakness for DoD and long-term system corrections are in process. Once the proper systems are in place, these items will be accounted for under the consumption method of accounting.

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

The NWCF recognizes condemned materiel as "excess, obsolete, or unserviceable." The cost of disposal is greater than the potential scrap value; therefore, the net value of condemned materiel is zero. Potentially redistributed materiel, presented in previous years as "excess, obsolete, and unserviceable," is included in the "held for use" or "held for repair" categories according to its condition.

Inventory available and purchased for resale includes consumable spare and repair parts and repairable items owned and managed by NWCF. This inventory is retained to support military or national contingencies. Inventory held for repair is damaged inventory that requires repair to make suitable for sale or re-use. Often, it is more economical to repair these inventory items than to procure them. The NWCF often relies on weapon systems and machinery no longer in production. As a result, NWCF supports a process that encourages the repair and rebuilding of certain items. This repair cycle is essential to maintaining a ready, mobile, and armed military force.

Work in process balances include costs related to the production or servicing of items, including direct material, direct labor, applied overhead and other direct costs. Work in process also includes the value of finished products or completed services pending the submission of bills to the customer. The work in process designation may also be used to accumulate the amount paid to a contractor under cost reimbursable contract, to include amounts withheld from payment to ensure performance, and amounts paid to other government plants for accrued costs of end items of materiel ordered, but not delivered. Work in process includes munitions in production and depot maintenance work with its associated labor, applied overhead, and supplies used in the delivery of maintenance services.

1.N. Investments

Not Applicable.

1.O. General Property, Plant and Equipment

In FY 2006, DoD revised the real property capitalization threshold from $100 thousand to $20 thousand. The current $100 thousand capitalization threshold remains unchanged for the remaining General PP&E categories. The NWCF has not implemented this revised policy due to system and process limitations.

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

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

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

1.P. Advances and Prepayments

The DoD's policy is to record advances and prepayments in accordance with GAAP. As such, payments made in advance of the receipt of goods and services are reported as an asset on the Balance Sheet. The DoD's policy is to expense and/or properly classify assets when the related goods and services are received. Not all DoD entities have implemented this policy primarily due to system limitations.

1.Q. Leases

The NWCF does not have any leases to disclose for this reporting period.

1.R. Other Assets

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

The NWCF conducts business with commercial contractors under two primary types of contracts: fixed price and cost reimbursable. To alleviate the potential financial burden on the contractor that long-term contracts can cause, NWCF may provide financing payments. Contract financing payments are defined in the Federal Acquisition Regulations (FAR), Part 32, as authorized disbursements of monies to a contractor prior to acceptance of supplies or services by the Federal Government. Contract financing payments clauses are incorporated in the contract terms and conditions and may include advance payments, performance-based payments, commercial advance and interim payments, progress payments based on cost, and interim payments under certain cost-reimbursement contracts. Contract financing payments do not include invoice payments, payments for partial deliveries, lease and rental payments, or progress payments based on a percentage or stage of completion, which the Defense Federal Acquisition Regulation Supplement authorizes only for construction of real property, shipbuilding, and ship conversion, alteration, or repair. Progress payments for real property are reported as construction in progress. It is DoD policy to record certain contract financing payments as Other Assets.

1.S. Contingencies and Other Liabilities

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

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

1.T. Accrued Leave

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

1.U. Net Position

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

Unexpended appropriations represent the amounts of authority that are unobligated and have not been rescinded or withdrawn. Unexpended appropriations also represent amounts obligated for which legal liabilities for payments have not been incurred. Cumulative results of operations represent the net difference, since inception of an activity, between expenses and losses and financing sources (including appropriations, revenue, and gains). Beginning with FY 1998, the cumulative results also include donations and transfers in and out of assets that were not reimbursed.

1.V. Treaties for Use of Foreign Bases

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

1.W. Comparative Data

Not Applicable.

1.X. Unexpended Obligations

The NWCF obligates funds to provide goods and services for outstanding orders not yet delivered. The financial statements do not reflect this liability for payment for goods and services not yet delivered, unless title passes.

1.Y. Undistributed Disbursements and Collection

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

The DoD policy is to allocate supported undistributed disbursements and collections between federal and nonfederal categories based on the percentage of distributed federal and nonfederal accounts payable and accounts receivable. Unsupported undistributed disbursements are recorded in accounts payable. Unsupported undistributed collections are recorded in other liabilities.

1.Z. Significant Events

Beginning 4th Quarter, FY 2007, DoD began presenting the Statement of Financing (SOF) as a note in accordance with OMB Circular A-136. The SOF will no longer be considered a basic statement and is now referred to as "Reconciliation of Net Cost of Operations to Budget."

Note 2. Nonentity Assets

As of September 30	2007	2006
(Amounts in Thousands)		
1. Intragovernmental Assets		
A. Fund Balance with Treasury	$ 0	$ 0
B. Accounts Receivable	0	0
C. Total Intragovernmental Assets	$ 0	$ 0
2. Nonfederal Assets		
A. Cash and Other Monetary Assets	$ 0	$ 0
B. Accounts Receivable	3,031	2,822
C. Other Assets	0	0
D. Total Nonfederal Assets	$ 3,031	$ 2,822
3. Total Nonentity Assets	$ 3,031	$ 2,822
4. Total Entity Assets	$ 18,310,812	$ 19,696,703
5. Total Assets	$ 18,313,843	$ 19,699,525

Standard Disclosures
Nonentity assets are assets for which the Navy Working Capital Fund (NWCF) maintains stewardship accountability and responsibility to report, but are not available for NWCF operations.

The Nonentity Accounts Receivable amount represents interest, penalties, fines, and administrative fees. These fees do not belong to NWCF and will be distributed directly to the U.S. Treasury.

Note 3. Fund Balance with Treasury

As of September 30	2007	2006
(Amounts in Thousands)		
1. Fund Balances		
A. Appropriated Funds	$ 0	$ 0
B. Revolving Funds	1,156,401	1,244,509
C. Trust Funds	0	0
D. Special Funds	0	0
E. Other Fund Types	0	0
F. Total Fund Balances	$ 1,156,401	$ 1,244,509
2. Fund Balances Per Treasury Versus Agency		
A. Fund Balance per Treasury	$ 1,156,401	$ 1,244,509
B. Fund Balance per NWCF	1,156,401	1,244,509
3. Reconciling Amount	$ 0	$ 0

Status of Fund Balance with Treasury

As of September 30		2007		2006
(Amounts in Thousands)				
1. Unobligated Balance				
A. Available	$	1,464,986	$	2,355,631
B. Unavailable		60,181		192,321
2. Obligated Balance not yet Disbursed	$	12,129,800	$	12,112,507
3. Nonbudgetary FBWT	$	0	$	0
4. NonFBWT Budgetary Accounts	$	(12,498,566)	$	(13,415,951)
5. Total	$	1,156,401	$	1,244,508

Standard Disclosures
The Status of Fund Balance with Treasury (FBWT) reflects the budgetary resources to support FBWT.

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

Obligated Balance not yet Disbursed represents funds that have been obligated for goods not yet received or services not yet performed and goods and services that have been delivered/received but not yet paid.

Nonbudgetary FBWT includes entity and nonentity FBWT accounts which represent adjustments that do not have budgetary authority, such as unavailable receipt accounts or clearing accounts.

NonFBWT Budgetary Accounts represent adjustments to budgetary accounts that do not affect FBWT. This amount is comprised of contract authority, accounts receivable, and unfilled orders without advance from customers for Navy Working Capital Fund (NWCF). This category reduces the Status of FBWT.

All unobligated unavailable balances are restricted to future use and are not apportioned for current use. The unavailable balance consists of contract and budgetary authority from closed NWCF activities as a result of the financial closure process.

Disclosures Related to Suspense/Budget Clearing Accounts

Per Office of Under Secretary of Defense (Comptroller) direction, NWCF Suspense/Budget Clearing Accounts are being reported under Department of the Navy General Fund, Index 17.

Disclosures Related to Problem Disbursements

As of September 30		2005		2006		2007		(Decrease)/ Increase from FY 2006 to 2007
(Amounts in Thousands)								
1. Total Problem Disbursements, Absolute Value								
A. Unmatched Disbursements (UMDs)	$	73,422	$	54,269	$	50,729	$	(3,540)
B. Negative Unliquidated Obligations (NULO)		0		14		30		16
C. In-Transit Disbursements		476,076		14,275		457,236		442,961
2. Total	$	549,498	$	68,558	$	507,995	$	439,437

Standard Disclosures
A portion of the amounts reported on the metric furnished by Defense Finance and Accounting Service (DFAS) Arlington is not supported by NWCF accounting systems. These discrepancies exist within DFAS Columbus reports. In the current period, discrepancies in In-transit Disbursements amount to $9.1 million.

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

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

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

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

Beginning with 2nd Quarter, FY 2007, in-transit disbursements have been reported as an absolute value as opposed to net amounts disclosed in prior years. This reporting change applies to amounts in the note schedule for both the current and comparative years.

Note 4. Investments and Related Interest

Not applicable.

Note 5. Accounts Receivable

As of September 30	2007			2006
	Gross Amount Due	Allowance For Estimated Uncollectibles	Accounts Receivable, Net	Accounts Receivable, Net
(Amounts in Thousands)				
1. Intragovernmental Receivables	$ 698,039	N/A	$ 698,039	$ 444,251
2. Nonfederal Receivables (From the Public)	$ 86,107	$ (29)	$ 86,078	$ 69,356
3. Total Accounts Receivable	$ 784,146	$ (29)	$ 784,117	$ 513,607

Aged Accounts Receivable

As of September 30	2007		2006	
	Intragovernmental	Nonfederal	Intragovernmental	Nonfederal
(Amounts in Thousands)				
CATEGORY				
Nondelinquent				
Current	$ 806,069	$ 37,056	$ 699,170	$ 40,407
Noncurrent	0	7,179	0	0
Delinquent				
1 to 30 days	$ 10,203	$ 7,682	$ 2,765	$ 2,419
31 to 60 days	1,693	4,578	1,220	3,792
61 to 90 days	1,921	6,171	3,095	953
91 to 180 days	1,742	6,468	2,118	2,135
181 days to 1 year	1,016	6,493	470	2,031
Greater than 1 year and less than or equal to 2 years	1,072	2,272	699	3,262
Greater than 2 years and less than or equal to 6 years	44	4,114	3	2,410
Greater than 6 years and less than or equal to 10 years	0	1,589	0	1,845
Greater than 10 years	0	4,737	0	4,597
Subtotal	$ 823,760	$ 88,339	$ 709,540	$ 63,851
Less Supported Undistributed Collections	(79,560)	(4,114)	(148,182)	(8,724)
Less Eliminations	(46,521)	0	(106,136)	0
Less Other	360	1,882	(10,971)	14,256
Total	$ 698,039	$ 86,107	$ 444,251	$ 69,383

Standard Disclosures
The nondelinquent noncurrent nonfederal accounts receivable represents the remaining balance of the Guam Water Authority (GWA) debt to Base Support, Navy. The Department of the Navy (DON) filed a civil suit against the Government of Guam and GWA for failure to pay for water from January 1995 to October 1999. The court ordered final settlement allowed the Government of Guam and GWA to pay the debt of $9 million plus interest by making 105 monthly payments beginning October 1, 2003. Base Support, Navy has received the scheduled monthly payments to date and the account is current.

The DON is taking various collection actions to eliminate intragovernmental and nonfederal receivables older than 30 days. The Navy Working Capital Fund (NWCF) and Defense Finance and Accounting Service (DFAS) are working together to ensure timely collection/resolution of delinquent receivables, as well as timely submission of receivables to debt collection in accordance with guidance. The NWCF commands are also actively contacting agencies by phone, email, or one-on-one visits to resolve disputed accounts receivable. The DFAS is setting up a Government Receivables Debt Collection Office to act as a liaison between government agencies, ensuring timely collection of government receivables.

In the aging schedule above, the Other consists of required adjustments to reconcile account totals with the Seller Elimination Report. The NWCF is working with DFAS as part of DON's Financial Improvement Program to correct this issue.

Note 6. Other Assets

As of September 30	2007	2006
(Amounts in Thousands)		
1. Intragovernmental Other Assets		
A. Advances and Prepayments	$ 3,886	$ 1,941
B. Other Assets	0	0
C. Total Intragovernmental Other Assets	$ 3,886	$ 1,941
2. Nonfederal Other Assets		
A. Outstanding Contract Financing Payments	$ 27,116	$ 27,898
B. Other Assets (With the Public)	266,956	335,567
C. Total Nonfederal Other Assets	$ 294,072	$ 363,465
3. Total Other Assets	$ 297,958	$ 365,406

Standard Disclosures
Other Assets (With the Public) consists of outstanding debt principal, prepayments made to vendors, and travel advances.

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

The Contract Financing Payment balance of $27.1 million is entirely comprised of estimated future funded payments that will be paid to the contractor upon future delivery and Federal Government acceptance of a satisfactory product. See additional discussion in Note 15, Other Liabilities.

Other Disclosures
The outstanding debt principal amount in Other Assets (With the Public) is reported in order to reconcile with the amount incorrectly reported by the Federal Financing Bank (FFB). As required by the Office of Under Secretary of Defense (Comptroller) memorandum of January 22, 1999, Transportation, Military Sealift Command is correctly recording payments to FFB as operating expense. The misclassification by FFB has generated this long-standing reporting problem. See additional discussion in Note 13, Debt.

Note 7. Cash and Other Monetary Assets

Not applicable.

Note 8. Direct Loan and/or Loan Guarantee Programs

Not applicable.

Note 9. Inventory and Related Property

As of September 30	2007	2006
(Amounts in Thousands)		
1. Inventory, Net	$ 12,313,482	$ 13,378,039
2. Operating Materiels & Supplies, Net	357,575	428,110
3. Stockpile Materiels, Net	0	0
4. Total	$ 12,671,057	$ 13,806,149

Inventory, Net

As of September 30	2007			2006	
	Inventory, Gross Value	Revaluation Allowance	Inventory, Net	Inventory, Net	Valuation Method
(Amounts in Thousands)					
1. Inventory Categories					
A. Available and Purchased for Resale	$ 21,379,136	$ (17,906,650)	3,472,486	$ (304,744)	LAC,MAC
B. Held for Repair	11,483,090	(2,950,029)	8,533,061	13,288,296	LAC,MAC
C. Excess, Obsolete, and Unserviceable	1,046,666	(1,046,666)	0	0	NRV
D. Raw Materiels	0	0	0	0	MAC, SP, LAC, AC
E. Work in Process	307,935	0	307,935	394,487	
F. Total	$ 34,216,827	$ (21,903,345)	12,313,482	$ 13,378,039	

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

Standard Disclosures
There are no restrictions on the use, sale, or disposition of inventory except in the following situations:

1) Distributions without reimbursement are made when authorized by Department of Defense (DoD) directives;

2) War reserve materiel in the amount of $80.2 million includes repair items that are considered restricted; and

3) Inventory, with the exception of safety stocks, may be sold to foreign, state, and local governments; private parties; and contractors in accordance with current policies and guidance or at the direction of the President.

There are no known restrictions on disposition of inventory as related to environmental or other liabilities.

Inventory available and purchased for resale includes consumable spare and repair parts as well as repairable items owned and managed by the Navy Working Capital Fund (NWCF) and includes all materiel available for customer purchase. Inventory held for repair consists of damaged material that requires repair to make it usable and includes all economically repairable materiel. Excess inventory includes scrap materiels or items that cannot be economically repaired and are awaiting disposal. Work in process includes costs related to the production or servicing of items, including direct materiel, direct labor, applied overhead, and other direct costs. Work in process also includes the value of finished products or completed services pending the submission of bills to the customer.

Federal Accounting Standards require disclosure of the amount of inventory held for "future sale." The NWCF currently has no inventory held for future sale reported for 4th Quarter, FY 2007 in Inventory Held for Sale, Net. All inventory is currently planned for sale next fiscal year.

Inventory is assigned to categories based on guidance in the DoD Financial Management Regulation (FMR), Volume 11B, Chapter 55.

Other Disclosures
The Supply Management, Navy's inventory is reported using the approximation of historical cost method as discussed in the FMR Volume 11B, Chapter 55. The approximation of historical cost is calculated by using the latest acquisition cost less the allowance for holding gains and losses. Legacy inventory systems were designed to capture materiel management information rather than accounting data. Although these systems provide visibility and accountability over inventory items, they do not maintain historical cost data necessary to comply with the Statement of Federal Financial Accounting Systems (SFFAS) No. 3, Accounting for Inventory and Related Property. Since the implementation of the Office of Under Secretary of Defense, Comptroller (OUSD(C)) Cost of Goods Sold Model, prior year values in equity, inventory, and inventory allowance accounts have been impacted and remain noncompliant with SFFAS No. 3 and generally accepted accounting practices. The Navy Enterprise Resource Planning will value inventory at moving average cost and will be compliant with necessary guidance.

Operating Materiel and Supplies, Net

As of September 30	2007 OM&S Gross Value	2007 Revaluation Allowance	2007 OM&S, Net	2006 OM&S, Net	Valuation Method
(Amounts in Thousands)					
1. OM&S Categories					
A. Held for Use	$ 357,575	$ 0	$ 357,575	$ 428,110	SP, LAC, MAC
B. Held for Repair	0	0	0	0	SP, LAC, MAC
C. Excess, Obsolete, and Unserviceable	0	0	0	0	NRV
D. Total	$ 357,575	$ 0	$ 357,575	$ 428,110	

Legend for Valuation Methods:

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

Standard Disclosures

Operating Materiel and Supplies (OM&S) held for use consists of property that is consumed during normal operations and includes consumable spare and repair parts for use on customer work by various activities.

Federal Accounting Standards require disclosure of the amount of OM&S held for "future use." The NWCF reports that $13.0 million of OM&S is held for future use and is included in the "held for use" category.

There are no restrictions with regard to the use, sale, or disposition of OM&S applicable to NWCF activities.

In order to standardize reporting of the categories held for use, held for repair, and excess, obsolete, unserviceable, the Department of the Navy implemented OUSD(C) condition code crosswalk as defined in the memorandum, Accounting for Excess, Unserviceable, and Obsolete Inventory and Operating Materials and Supplies, of August 12, 2002. In addition, the condition code crosswalk was amended to include code "V" in the excess, obsolete, unserviceable category in September 2002.

Stockpile Materiel, Net

Not applicable.

Note 10. General PP&E, Net

As of September 30	2007					2006
	Depreciation/ Amortization Method	Service Life	Acquisition Value	(Accumulated Depreciation/ Amortization)	Net Book Value	Prior FY Net Book Value
(Amounts in Thousands)						
1. Major Asset Classes						
A. Land	N/A	N/A	$ 41,681	N/A	$ 41,681	$ 45,822
B. Buildings, Structures, and Facilities	S/L	20 or 40	5,992,356	$ (4,036,263)	1,956,093	2,077,944
C. Leasehold Improvements	S/L	lease term	305	(254)	51	78
D. Software	S/L	2-5 or 10	492,208	(334,908)	157,300	196,144
E. General Equipment	S/L	5 or 10	2,845,027	(2,234,523)	610,504	728,552
F. Military Equipment	S/L	Various	0	0	0	0
G. Assets Under Capital Lease	S/L	lease term	0	0	0	0
H. Construction-in- Progress	N/A	N/A	635,879	N/A	635,879	718,491
I. Other			2,802	0	2,802	2,823
J. Total General PP&E			$ $10,010,258	$ (6,605,948)	$ 3,404,310	$ 3,769,854

Legend for Valuation Methods:

S/L = Straight Line

N/A = Not Applicable

Standard Disclosures

There are no known restrictions on the use or convertibility of General Property, Plant, and Equipment (PP&E), nor are there any adjustments resulting from changes in the accounting standards.

Military equipment is reported on the financial statements of the Department of the Navy (DON) General Fund.

General PP&E, Other consists of assets awaiting disposal.

Heritage assets and stewardship land are reported on the financial statements of DON General Fund.

Assets Under Capital Lease

Not applicable.

Note 11. Liabilities Not Covered by Budgetary Resources

As of September 30	2007	2006
(Amounts in Thousands)		
1. Intragovernmental Liabilities		
A. Accounts Payable	$ 0	$ 0
B. Debt	0	0
C. Other	3,031	2,822
D. Total Intragovernmental Liabilities	$ 3,031	$ 2,822
2. Nonfederal Liabilities		
A. Accounts Payable	$ 0	$ 0
B. Military Retirement Benefits and Other Employment-Related Actuarial Liabilities	1,047,588	1,185,040
C. Environmental Liabilities	0	0
D. Other Liabilities	0	0
E. Total Nonfederal Liabilities	$ 1,047,588	$ 1,185,040
3. Total Liabilities Not Covered by Budgetary Resources	$ 1,050,619	$ 1,187,862
4. Total Liabilities Covered by Budgetary Resources	$ 5,281,853	$ 5,580,082
5. Total Liabilities	$ 6,332,472	$ 6,767,944

Standard Disclosures
Liabilities not covered by budgetary resources are liabilities for which congressional action is needed before budgetary resources can be provided.

The amount in liabilities not covered by budgetary resources is comprised of an actuarial liability, which is an estimate of what may have to be paid out in future fiscal years. Therefore, this liability is not covered by current fiscal year budgetary resources.

Other Intragovernmental Liabilities consists of interest, penalties, fines, and administrative fees. These fees do not belong to Navy Working Capital Fund (NWCF), but are assessed to contracts and legal documents that cite NWCF lines of accounting. These fees will be distributed directly to the U.S. Treasury.

Military Retirement and Other Federal Employment Benefits not covered by budgetary resources are comprised of employee actuarial liability not due and payable during the current fiscal year. This liability is comprised of Federal Employees' Compensation Act actuarial liability of $1.0 billion. See Note 17, Military Retirement and Other Federal Employment Benefits, for additional disclosures.

Note 12. Accounts Payable

As of September 30	2007			2006
	Accounts Payable	Interest, Penalties, and Administrative Fees	Total	Total
(Amounts in Thousands)				
1. Intragovernmental Payables	$ 207,232	$ N/A	$ 207,232	$ 143,723
2. Nonfederal Payables (to the Public)	3,381,559	0	3,381,559	1,485,833
3. Total	$ 3,588,791	$ 0	$ 3,588,791	$ 1,629,556

Standard Disclosures
The Navy Working Capital Fund's systems do not track Intragovernmental transactions by customer at the transaction level. Therefore, internal Department of Defense buyer-side balances are adjusted to agree with internal seller-side balances for revenue, accounts receivable, and unearned revenue. Accounts payable were adjusted by reclassifying amounts between federal and nonfederal accounts payable.

Note 13. Debt

As of September 30	2007			2006	
	Beginning Balance	Net Borrowing	Ending Balance	Net Borrowing	Ending Balance
(Amounts in Thousands)					
1. Agency Debt (Intragovernmental)					
A. Debt to the Treasury	$ 0	$ 0	$ 0	$ 0	$ 0
B. Debt to the Federal Financing Bank	173,224	(102,527)	70,697	(208,294)	173,224
C. Total Agency Debt	$ 173,224	$ (102,527)	$ 70,697	$ (208,294)	$ 173,224
2. Total Debt	$ 173,224	$ (102,527)	$ 70,697	$ (208,294)	$ 173,224

Standard Disclosures
The Afloat Prepositioning Force program, with congressional approval, provides ships for time charter to meet requirements not available in the marketplace. These ships are built or converted by private interim vessel owners using private, nongovernment financing obtained from various banking institutions. There were no payments made by the government during the building/conversion phase. Afloat Prepositioning Force program 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, each ship returns to the vessel's owner.

The Federal Financing Bank (FFB) is one of the institutions that provided loans to the vessel owners. The FFB reports that Transportation, Military Sealift Command (MSC) has a debt in the amount of $70.7 million, which represents an outstanding principal balance of $69.6 million and accrued interest payable of $1.1 million. The MSC does not owe this debt to FFB. This debt is a public debt owed by the private vessel owners. In order to simplify the payments to FFB and to meet its requirements, FFB cross disburses the semi-annual principal and interest payments directly from NWCF. This is done instead of having MSC make capital hire payments to the vessel owners, who would in turn make loan obligation payments to FFB. It is common for the Federal Government to make payments directly to the bank (FFB) and mirrors other time charters where payment is assigned directly to a bank. However, when establishing the loan, FFB coded the loan as a government debt instead of a public debt.

As required by the Office of Under Secretary of Defense (Comptroller) memorandum of January 22, 1999, MSC is correctly recording these payments as an operating expense. The outstanding debt principal amount is reported on NWCF Balance Sheet as an Other Asset in order to reconcile with the amount incorrectly reported by FFB. The misclassification by FFB has generated this long-standing reporting problem. See Note 6, Other Assets, for additional disclosures.

As required by the Department of Defense Appropriations Act passed in December 1985, ten percent of the fifth year termination value of the vessels must be obligated from Operation and Maintenance, Navy funds. This was completed as each vessel was delivered.

Note 14. Environmental Liabilities and Disposal Liabilities

The Navy Working Capital Fund Environmental Liabilities are reported under the Department of the Navy General Fund.

Note 15. Other Liabilities

As of September 30	2007 Current Liability	2007 Noncurrent Liability	2007 Total	2006 Total
(Amounts in Thousands)				
1. Intragovernmental				
A. Advances from Others	$ 145,647	$ 0	$ 145,647	$ 190,427
B. Deposit Funds and Suspense Account Liabilities	0	0	0	0
C. Disbursing Officer Cash	0	0	0	0
D Judgment Fund Liabilities	0	0	0	0
E. FECA Reimbursement to the Department of Labor	0	0	0	0
F. Other Liabilities	33,906	0	33,906	39,763
G. Total Intragovernmental Other Liabilities	$ 179,553	$ 0	$ 179,553	$ 230,190
2. Nonfederal				
A. Accrued Funded Payroll and Benefits	$ 703,169	$ 0	$ 703,169	$ 843,552
B. Advances from Others	247,232	0	247,232	207,797
C. Deferred Credits	0	0	0	0
D. Deposit Funds and Suspense Accounts	(9,881)	0	(9,881)	95,694
E. Temporary Early Retirement Authority	0	0	0	0
F. Nonenvironmental Disposal Liabilities				
(1) Military Equipment (Nonnuclear)	0	0	0	0
(2) Excess/Obsolete Structures	0	0	0	0
(3) Conventional Munitions Disposal	0	0	0	0
G. Accrued Unfunded Annual Leave	0	0	0	0
H. Capital Lease Liability	0	0	0	0
I. Other Liabilities	478,421	26,901	505,322	2,402,892
J. Total Nonfederal Other Liabilities	$ 1,418,941	$ 26,901	$ 1,445,842	$ 3,549,935
3. Total Other Liabilities	$ 1,598,494	$ 26,901	$ 1,625,395	$ 3,780,125

Standard Disclosures
Deposit funds and suspense accounts consist of an abnormal unsupported undistributed collections balance of $11.9 million for this reporting period. During FY 2007, Navy Working Capital Fund (NWCF) and the Defense Finance and Accounting Service (DFAS) reconciled unsupported undistributed collections and disbursements, and per Office of Under Secretary of Defense (Comptroller) policy, 26 NWCF activities cleared stabilized unsupported undistributed collections and disbursements. However, Transportation, Military Sealift Command (MSC) did not complete reconciliation of their abnormal balance in unsupported undistributed collections during FY 2007. The reconciliation of unsupported undistributed collections at MSC will be completed during FY 2008.

Intragovernmental Other Liabilities consists of retirement benefits, health benefits, custodial liabilities, and life insurance.

Nonfederal Other Liabilities consists of liabilities for depot level repairable carcass returns and liability for future contract financing payments.

Contingent Liabilities includes $27.1 million in estimated future contract financing payments that will be paid to the contractors upon delivery and Federal Government acceptance. In accordance with contract terms, specific rights to the contractor's work vests with the Federal Government when a specific type of contract financing payments is made. This action protects taxpayer funds in the event of contract nonperformance. These rights should not be misconstrued as the rights of ownership. The NWCF is under no obligation to pay the contractor for amounts greater than the amounts authorized in the contract until delivery and Federal Government acceptance. Because it is probable that the contractor will complete its efforts and deliver a satisfactory product to NWCF and the amount of potential future payments is estimable; NWCF has recognized a contingent liability for estimated future payments, which are conditional pending delivery and Federal Government acceptance.

Capital Lease Liability

Not applicable.

Note 16. Commitments and Contingencies

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

For FY 2007 and FY 2006, NWCF materiality threshold for reporting litigation, claims, and assessments was $4.5 million and $5.0 million, respectively. The DON OGC conducts a review of litigation and claims threatened or asserted involving NWCF to which DON OGC's attorneys devoted substantial attention in the form of legal consultation or representation. The NWCF currently has five cases that meet the existing FY 2007 NWCF materiality threshold of $4.5 million. All five cases are against NWCF and none are against the Navy Working Capital Fund-Marine Corps. DON legal counsel was unable to express an opinion concerning the likely outcome of these cases. This declaration is fully supported by the preliminary and final Legal Representation letters and the subsidiary management summary schedule.

Due to the inherent uncertainties of litigation, lawyers generally refrain from expressing judgments as to outcomes except in those relatively few clear cases. In response to a Department of Defense, Inspector General Audit, DoD Process for Reporting Contingent Legal Liabilities, DON developed a methodology to determine an estimate for contingent legal liabilities. Beginning with 1st Quarter, FY 2007, DON GF recognized and disclosed an estimate for contingent legal liabilities. The methodology considers the likelihood of an unfavorable outcome or potential liability and is provided as an overall assessment of all cases currently pending and not on an individual case basis. The likelihood of an unfavorable or potential liability was determined by using an average of the data from the preceding four years and the current year. This average was calculated by taking the total dollar amount of closed cases and dividing it by the total dollar amount claimed in those closed cases for each of the last four years plus current year. This average represents the percentage that has historically been paid on claims. It is based entirely on historical data. The merits of each individual case have not been taken into consideration. Until sufficient historical data can be collected for NWCF, the estimate recorded on DON GF financial statements will consider all DON funding sources together.

The NWCF does not have obligations related to cancelled appropriations for which there is a contractual commitment for payment. The NWCF has contractual arrangements, which may require future financial obligations (i.e. undelivered orders). These undelivered orders are estimated at $7.9 billion as of September 30, 2007.

The NWCF is a party in numerous individual contracts that contain clauses, such as price escalation, award fee payments, or dispute resolution, that may or may not result in a future outflow of expenditures. Currently, NWCF does not have a systemic process by which it captures or assesses these potential contingent liabilities; therefore, the amounts reported may not fairly present NWCF's contingent liabilities.

Note 17. Military Retirement and Other Federal Employment Benefits

As of September 30	2007 Present Value of Benefits	2007 Assumed Interest Rate (%)	2007 (Less: Assets Available to Pay Benefits)	2007 Unfunded Liability	2006 Present Value of Benefits
(Amounts in Thousands)					
1. Pension and Health Actuarial Benefits					
A. Military Retirement Pensions	$ 0		$ 0	$ 0	$ 0
B. Military Retirement Health Benefits	0		0	0	0
C. Military Medicare-Eligible Retiree Benefits	0		0	0	0
D. Total Pension and Health Actuarial Benefits	$ 0		$ 0	$ 0	$ 0
2. Other Actuarial Benefits					
A. FECA	$ 1,047,589		$ 0	$ 1,047,589	$ 1,185,039
B. Voluntary Separation Incentive Programs	0		0	0	0
C. DoD Education Benefits Fund	0		0	0	0
D. Total Other Actuarial Benefits	$ 1,047,589		$ 0	$ 1,047,589	$ 1,185,039
3. Other Federal Employment Benefits	$ 0		$ 0	$ 0	$ 0
4. Total Military Retirement and Other Federal Employment Benefits:	$ 1,047,589		$ 0	$ 1,047,589	$ 1,185,039

Standard Disclosures

The Department of the Navy (DON) actuarial liability for workers' compensation benefits is developed by the Department of Labor and provided to DON at the end of each fiscal year. The liability is distributed between the Navy Working Capital Fund and DON General Fund based upon the number of civilian employees funded in each entity as reported in the Navy Budget Tracking System. The liability 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 to predict the ultimate payments.

The assumptions relate to Federal Employees' Compensation Act (FECA). The projected annual benefit payments are discounted to the present value using Office of Management and Budget's economic assumptions for ten year U.S. Treasury notes and bonds. Cost of living adjustments and medical inflation factors are also taken into consideration when calculating projected future benefits.

The interest rate assumptions utilized when discounting were as follows:

2007
4.930% in Year 1
5.078% in Year 2 and thereafter

To provide more specificity concerning the effects of inflation on the liability for future workers' compensation benefits, wage inflation factors (cost of living adjustments or COLAs) or medical inflation factors (consumer price index medical or CPIMs) were applied to the calculation of projected future benefits. The actual rates for these factors for the charge back year (CBY) 2007 were also used to adjust the methodology's historical payments to current year constant dollars.

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

CBY	COLA	CPIM
2007	2.63%	3.74%
2008	2.90%	4.04%
2009	2.47%	4.00%
2010	2.37%	3.94%
2011+	2.30%	3.94%

The model's resulting projections were analyzed to ensure that the estimates were reliable. The analysis was based on four tests: (1) a sensitivity analysis of the model to economic assumptions, (2) a comparison of the percentage change in the liability amount by agency to the percentage change in the actual incremental payments, (3) a comparison of the incremental paid losses per case (a measure of case-severity) in CBY 2007 to the average pattern observed during the most current three charge back years, and (4) a comparison of the estimated liability per case in the 2007 projection to the average pattern for the projections of the most recent three years.

There have been changes in the calculation of actuarial liability since the last reporting period. The interest rate assumptions utilized and the number of civilian employees reported in the Navy Budget Tracking System have decreased.

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

Intragovernmental Costs and Exchange Revenue				
As of September 30		2007		2006
(Amounts in Thousands)				
1. Intragovernmental Costs	$	4,803,661	$	4,523,181
2. Public Costs		18,778,518		19,574,813
3. Total Costs	$	23,582,179	$	24,097,994
4. Intragovernmental Earned Revenue	$	(20,966,636)	$	(21,367,634)
5. Public Earned Revenue		(1,290,930)		(1,005,772)
6. Total Earned Revenue	$	(22,257,566)	$	(22,373,406)
7. Net Cost of Operations	$	1,324,613	$	1,724,588

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

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

The Navy Working Capital Fund's (NWCF) financial systems do not track intragovernmental transactions by customer at the transaction level. Therefore, internal Department of Defense buyer-side balances are adjusted to agree with internal seller-side balances for revenue or by other means. Expenses were adjusted by reclassifying amounts between federal and nonfederal expenses.

The Statement of Net Cost is unique because its principles are driven by an understanding of net cost of programs and or organizations that the Federal Government supports through appropriations. This Statement provides gross and net cost information that can relate to the amount of output for a given program and/or organization administered by a responsible reporting entity.

The NWCF financial management systems are unable to meet all of the requirements for full accrual accounting. Many of NWCF's financial and nonfinancial feeder systems and processes were designed and implemented prior to the issuance of Generally Accepted Accounting Principles (GAAP) for federal agencies. These systems were not designed to collect and record financial information as required by GAAP. The NWCF has undertaken efforts to determine the actions required to bring its financial and nonfinancial feeder systems and processes into compliance. Until all of NWCF's financial and nonfinancial feeder systems and processes are corrected, NWCF's financial data will be based on transactions from nonfinancial feeder systems, and accruals are made for major items such as payroll expenses and accounts payable.

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

As of September 30	2007 Cumulative Results of Operations	2007 Unexpended Appropriations	2006 Cumulative Results of Operations	2006 Unexpended Appropriations
(Amounts in Thousands)				
1. Prior Period Adjustments Increases (Decreases) to Net Position Beginning Balance				
A. Changes in Accounting Standards	$ 0	$ 0	$ 0	$ 0
B. Errors and Omissions in Prior Year Accounting Reports	0	0	0	0
C. Total Prior Period Adjustments	$ 0	$ 0	$ 0	$ 0
2. Imputed Financing				
A. Civilian CSRS/FERS Retirement	$ 177,593	$ 0	$ 225,349	$ 0
B. Civilian Health	296,553	0	332,920	0
C. Civilian Life Insurance	920	0	1,028	0
D. Judgment Fund	0	0	0	0
E. IntraEntity	0	0	0	0
F. Total Imputed Financing	$ 475,066	$ 0	$ 559,297	$ 0

Standard Disclosures
The Cumulative Results of Operations, Other Financing Sources, Other consists of gains and losses associated with the financial closure of Navy Working Capital Fund activities.

The Cumulative Results of Operations, Budgetary Financing Sources, Other adjustments (rescissions, etc.) consists of a rescission of an appropriation.

Note 20. Disclosures Related to the Statement of Budgetary Resources

As of September 30	2007		2006	
(Amounts in Thousands)				
1. Net Amount of Budgetary Resources Obligated for Undelivered Orders at the End of the Period	$	7,875,259	$	7,699,219
2. Available Borrowing and Contract Authority at the End of the Period		0		6,039,690

Standard Disclosures
The Navy Working Capital Fund (NWCF) reports all amounts for obligations incurred under apportionment category B. Category B apportionments typically distribute budgetary resources by activities, projects, objects or a combination of these categories. The NWCF direct and reimbursable obligations incurred totaled $599 thousand and $24.0 billion, respectively.

The Statement of Budgetary Resources (SBR) includes intraentity transactions, which have not been eliminated because the statements are presented as combined.

The SBR is an image of the monthly Report on Budget Execution, Standard Form 133 (SF 133). The NWCF reports a difference of $11.8 million between the unobligated balance and the unobligated balance brought forward amounts reported on the SBR and SF 133. This difference is a result of a prior period employee benefit adjustment that is carried forward per guidance. This difference should be corrected in 1st Quarter, FY 2008.

This note has been modified to accurately report the remaining available balance of borrowing and contract authority. Previously, the NWCF reported the amount of the contract/borrowing authority that had initially been used and not subsequently replaced by reimbursement or appropriation.

Note 21. Reconciliation of Net Cost of Operations to Budget

As of September 30	2007	2006
(Amounts in Thousands)		
Resources Used to Finance Activities:		
Budgetary Resources Obligated:		
1. Obligations incurred	$ 24,043,702	$ 22,942,454
2. Less: Spending authority from offsetting collections and recoveries (-)	(23,716,555)	(23,634,600)
3. Obligations net of offsetting collections and recoveries	$ 327,147	$ (692,146)
4. Less: Offsetting receipts (-)	0	0
5. Net obligations	$ 327,147	$ (692,146)
Other Resources:		
6. Donations and forfeitures of property	0	0
7. Transfers in/out without reimbursement (+/-)	17,242	(89,397)
8. Imputed financing from costs absorbed by others	475,066	559,297
9. Other (+/-)	(346,274)	567,376
10. Net other resources used to finance activities	$ 146,034	$ 1,037,276
11. Total resources used to finance activities	$ 473,181	$ 345,130
Resources Used to Finance Items not Part of the Net Cost of Operations:		
12. Change in budgetary resources obligated for goods, services and benefits ordered but not yet provided:		
12a. Undelivered Orders (-)	$ (176,039)	$ (113,368)
12b. Unfilled Customer Orders	(362,387)	(530,951)
13. Resources that fund expenses recognized in prior Periods (-)	(137,451)	(10,441)
14. Budgetary offsetting collections and receipts that do not affect Net Cost of Operations	0	0
15. Resources that finance the acquisition of assets (-)	(4,263,853)	(3,154,696)
16. Other resources or adjustments to net obligated resources that do not affect Net Cost of Operations:		
16a. Less: Trust or Special Fund Receipts Related to exchange in the Entity's Budget (-)	0	0
16b. Other (+/-)	329,032	(477,979)
17. Total resources used to finance items not part of the Net Cost of Operations	$ (4,610,698)	$ (4,287,435)
18. Total resources used to finance the Net Cost of Operations	$ (4,137,517)	$ (3,942,305)

As of September 30	2007	2006
(Amounts in Thousands)		
Components of the Net Cost of Operations that will not Require or Generate Resources in the Current Period:		
Components Requiring or Generating Resources in Future Period:		
19. Increase in annual leave liability	$ 0	$ 0
20. Increase in environmental and disposal liability	0	0
21. Upward/Downward reestimates of credit subsidy expense (+/-)	0	0
22. Increase in exchange revenue receivable from the public (-)	0	0
23. Other (+/-)	0	2,928
24. Total components of Net Cost of Operations that will Require or Generate Resources in future periods	$ 0	$ 2,928
Components not Requiring or Generating Resources:		
25. Depreciation and amortization	$ 228,829	$ 221,880
26. Revaluation of assets or liabilities (+/-)	1,930,023	1,583,686
27. Other (+/-)		
27a. Trust Fund Exchange Revenue	0	0
27b. Cost of Goods Sold	11,566,742	3,858,204
27c. Operating Material and Supplies Used	0	0
27d. Other	(8,263,464)	194
28. Total Components of Net Cost of Operations that will not Require or Generate Resources	$ 5,462,130	$ 5,663,964
29. Total components of Net Cost of Operations that will not Require or Generate Resources in the current period	$ 5,462,130	$ 5,666,892
30. Net Cost of Operations	$ 1,324,613	$ 1,724,587

Standard Disclosures

Due to Navy Working Capital Fund (NWCF) financial system limitations, budgetary data is not in agreement with proprietary expenses and assets capitalized. The difference between budgetary and proprietary data is a previously identified deficiency. As a result of these system limitations, resources that finance the acquisition of assets on the Reconciliation of Net Cost of Operations to Budget was adjusted upward by $17.7 billion (absolute amount) at the end of FY 2007 to bring it into balance with the Statement of Net Cost.

The following Reconciliation of Net Cost of Operations to Budget lines are presented as combined instead of consolidated due to interagency budgetary transactions not being eliminated:

- Obligations Incurred
- Less: Spending Authority from Offsetting Collections and Recoveries
- Obligations Net of Offsetting Collections and Recoveries
- Less: Offsetting Receipts

- Net Obligations
- Undelivered Orders
- Unfilled Customer Orders

Other Resources Used to Finance Activities consists of gains and losses associated with the financial closure of NWCF activities.

Other Resources Used to Finance Items not Part of the Net Cost of Operations consist of transfers of assets out of NWCF.

Other Components not Requiring or Generating Resources consist of overhead costs distributed to work in process, as well as costs originally recorded into another expense account that are transferred to one of three accounts: inventory work in process, internal use software in development, or completed assets.

There is a difference of $137.2 million between the amounts reported as Liabilities not Covered by Budgetary Resources and amounts reported as Components Requiring or Generating Resources in Future Periods on the Reconciliation of Net Cost of Operations to Budget. This difference is attributable to a decrease in the interest rate assumptions utilized and the number of civilian employees registered in the Navy Budget Tracking System this reporting period in the calculation of actuarial liability. This decrease was offset by an increase in nonentity receivables through FY 2007, as the collection of nonentity receivables will not require or generate resources for NWCF. These balances are deposited to U.S. Treasury and belong to the general cash balances of the Federal Government.

Note 22. Disclosures Related to Incidental Custodial Collections

Not applicable.

Note 23. Earmarked Funds

Not applicable.

Note 24. Other Disclosures

Not applicable.

Note 25. Restatements

For Fiscal Year 2007, the Navy Working Capital Fund does not have any restatements.

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Navy Working Capital Fund

Required Supplementary Information

2007 Annual Financial Report

Navy Working Capital Fund
General Property, Plant, and Equipment
Real Property Deferred Maintenance
For Fiscal Year Ended September 30, 2007

The Navy Working Capital Fund real property deferred maintenance for fiscal year ended September 30, 2007 is being reported with the Department of the Navy General Fund real property deferred maintenance. See Department of the Navy General Fund Required Supplementary Information.

Schedule, Part A DoD Intra-governmental Asset Balances. *($ Amounts in Thousands)*	Treasury Index:	Fund Balance with Treasury	Accounts Receivable	Loans Receivable	Investments	Other
Department of Agriculture	12	$0	$110	$0	$0	$0
Department of Commerce	13	0	374	0	0	0
Department of the Interior	14	0	36	0	0	0
Department of Justice	15	0	130	0	0	0
Navy General Fund	17	0	569,352	0	0	0
United States Postal Service	18	0	209	0	0	0
Department of State	19	0	9	0	0	0
Department of the Treasury	20	1,156,401	30	0	0	0
Army General Fund	21	0	15,411	0	0	0
Office of Personnel Management	24	0	13	0	0	0
National Credit Union Administration	25	0	4	0	0	0
Federal Communications Commission	27	0	7	0	0	0
Federal Trade Commission	29	0	(23)	0	0	0
John F. Kennedy Center	33	0	51	0	0	0
Department of Veterans Affairs	36	0	52	0	0	0
General Service Administration	47	0	299	0	0	0
Independent Agencies	48	0	728	0	0	0
National Science Foundation	49	0	71	0	0	0
Air Force General Fund	57	0	26,312	0	0	0
Tennessee Valley Authority	64	0	35	0	0	0
Environmental Protection Agency	68	0	1,553	0	0	0
Department of Transportation	69	0	442	0	0	0
Homeland Security	70	0	9,827	0	0	0
Department of Health and Human Services	75	0	89	0	0	0
National Aeronautics and Space Administration	80	0	1,743	0	0	0
National Archives and Records Administration	88	0	90	0	0	0
Department of Energy	89	0	874	0	0	0
Selective Service System	90	0	10	0	0	0
Department of Education	91	0	0	0	0	0
Independent Agencies	95	0	3,956	0	0	0
US Army Corps of Engineers	96	0	269	0	0	0
Other Defense Organizations General Funds	97	0	53,613	0	0	0
Other Defense Organizations Working Capital Funds	97-4930	0	6,440	0	0	3,886
Army Working Capital Fund	97-4930.001	0	3,901	0	0	0
Air Force Working Capital Fund	97-4930.003	0	2,021	0	0	0
Totals might not match to the Principal Statements	**TOTALS**	**$1,156,401**	**$698,038**	**$0**	**$0**	**$3,886**

Schedule, Part B DoD Intra-governmental entity liabilities. ***($ Amounts in Thousands)***	**Treasury Index:**	**Accounts Payable**	**Debts/Borrowings From Other Agencies**	**Other**
Library of Congress	3	$0	$0	$673
Government Printing Office	4	1	0	0
Executive Office of the President	11	1	0	19,656
Department of Agriculture	12	0	0	164
Department of Commerce	13	0	0	126
Department of the Interior	14	0	0	(92)
Department of Justice	15	0	0	48,215
Department of Labor	16	0	0	411
Navy General Fund	17	81,232	0	(5,715)
United States Postal Service	18	4,016	0	0
Department of State	19	0	0	7,458
Department of the Treasury	20	(1,078)	70,697	1,379
Army General Fund	21	5,862	0	1
Office of Personnel Management	24	40,339	0	30,875
Social Security Administration	28	0	0	479
Nuclear Regulatory Commission	31	0	0	1,480
John F. Kennedy Center	33	0	0	2
Department of Veterans Affairs	36	0	0	252
Pennsylvania Avenue Development Corp	42	0	0	21
General Service Administration	47	934	0	(424)
National Science Foundation	49	468	0	9,634
Air Force General Fund	57	944	0	7
Environmental Protection Agency	68	0	0	138
Department of Transportation	69	0	0	588
Homeland Security	70	0	0	48,423
Agency for International Development	72	0	0	50
Department of Health and Human Services	75	38	0	825
National Aeronautics and Space Administration	80	505	0	209
Department of Housing and Urban Development	86	0	0	0
Department of Energy	89	64	0	1,265
Other Defense Organizations General Funds	97	7,607	0	10,421
The General Fund of the Treasury	99	0	0	3,031
Other Defense Organizations Working Capital Funds	97-4930	61,406	0	0
Air Force Working Capital Fund	97-4930.003	4,892	0	0
Architect of the Capitol		0	0	0
Totals might not match to the Principal Statements	**TOTALS**	**$207,231**	**$70,697**	**$179,552**

Schedule, Part C DoD Intra-governmental revenue and related costs.(*$ Amounts in Thousands)*	Treasury Index:	Earned Revenue
Library of Congress	3	8,733
Congressional Budget Office	8	0
Executive Office of the President	11	328
Department of Agriculture	12	665
Department of Commerce	13	6,993
Department of the Interior	14	4,534
Department of Justice	15	117,277
Department of Labor	16	46
Navy General Fund	17	18,299,621
United States Postal Service	18	643
Department of State	19	16,002
Department of the Treasury	20	9,742
Army General Fund	21	297,095
Resolution Trust Corporation	22	0
Office of Personnel Management	24	122
Federal Communications Commission	27	37
Social Security Administration	28	445
Federal Trade Commission	29	(23)
Nuclear Regulatory Commission	31	1,005
John F. Kennedy Center	33	71
International Trade Commission	34	412
Department of Veterans Affairs	36	591
Pennsylvania Avenue Development Corp	42	1
General Service Administration	47	864
National Science Foundation	49	12,753
Air Force General Fund	57	398,097
Consumer Product Safety Commission	61	43
Environmental Protection Agency	68	4,011
Department of Transportation	69	4,086
Homeland Security	70	205,772
Agency for International Development	72	(84)
Department of Health and Human Services	75	3,100
National Aeronautics and Space Administration	80	89,091
Department of Housing and Urban Development	86	4
National Archives and Records Administration	88	412
Department of Energy	89	28,465
Selective Service System	90	573
Independent Agencies	95	70
US Army Corps of Engineers	96	5,399
Other Defense Organizations General Funds	97	1,171,623
The General Fund of the Treasury	99	37
Other Defense Organizations Working Capital Funds	97-4930	88,134
Army Working Capital Fund	97-4930.001	78,835
Air Force Working Capital Fund	97-4930.003	108,146
Architect of the Capitol		0
Totals might not match to the Principal Statements	**TOTALS**	**$20,963,771**

Schedule, Part E DoD Intra-governmental non-exchange revenues. *($Amounts in Thousands)*	**Treasury Index:**	**Transfers In**	**Transfers Out**
Other Defense Organizations Working Capital Funds	97-4930	$129,746	$0
Totals might not match to the Principal Statements	**TOTALS**	**$129,746**	**$0**

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Navy Working Capital Fund

Other Accompanying Information

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Appropriations, Funds, and Accounts Included in the Financial Statements

Reporting Entity

Navy Working Capital Fund (NWCF)

Fund/Account Treasury Symbol and Title:

97X4930.002

Navy Working Capital Fund Activity Group Treasury Symbol and Title:

97X4930.NA1*	Depot Maintenance-Shipyards[a]
97X4930.NA2*	Depot Maintenance-Aviation
97X4930.NA4A*	Depot Maintenance- Other, Marine Corps
97X4930.NA3*	Ordnance[b]
97X4930.ND*	Transportation
97X4930.NE*	Base Support
97X4930.NH*	Research and Development
97X4930.NC*	Supply Management
97X4930.NC2A*	Supply Management, Marine Corps

Notes

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

[a] Depot Maintenance, Shipyards became a part of the DON General Fund in FY 2007. The Depot Maintenance, Shipyards information included in this report represents residual NWCF accounting.

[b] The Ordnance activity group became a part of the DON General Fund in FY 2000. The Ordnance information included in this report represents residual NWCF accounting for this group.

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United States Marine Corps General Fund

Principal Statements

Department of the Navy Subsidiary Financial Statements

2007 Annual Financial Report

Limitations to the Financial Statements

The principal financial statements have been prepared to report the financial position and results of operations of the entity, pursuant to the requirements of 31 United States Code 3515 (b). While the statements have been prepared from the books and records of the entity in accordance with Generally Accepted Accounting Principles for Federal entities and 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.

In Fiscal Year (FY) 2006, the Office of the Under Secretary of Defense (Comptroller), with support from the Department of the Navy, designated the U.S. Marine Corps a financial reporting entity. This designation allowed the Marine Corps to prepare comprehensive subsidiary financial statements and related notes beginning in FY 2006.

The Marine Corps shares appropriations with the U.S. Navy and in addition maintains accountability for its own appropriations. The Marine Corps has specific funds and budget execution unto itself that are managed by Marine Corps program sponsors. Given this fiduciary responsibility, the Marine Corps is able to fully comply with Statement of Federal Financial Accounting Concepts Number 2, *Entity and Display.*

Principal Statements

The FY 2007 U.S. Marine Corps General Fund Principal Statements and related notes are subsidiary financial statements and related notes of the Department of the Navy General Fund, and are presented in the format prescribed by the Department of Defense Financial Management Regulation 7000.14, Volume 6B. The statements and related notes summarize financial information for individual funds and accounts within the U.S. Marine Corps General Fund for the fiscal year ending September 30, 2007, and are presented on a comparative basis with information previously reported for the fiscal year ending September 30, 2006.

The following statements comprise the U.S. Marine Corps General Fund Principal Statements:

- Consolidated Balance Sheet
- Consolidated Statement of Net Cost
- Consolidated Statement of Changes in Net Position
- Combined Statement of Budgetary Resources

The Principal Statements and related notes have been prepared to report financial position pursuant to the requirements of the Chief Financial Officers Act of 1990, as amended by the Government Management Reform Act of 1994. The accompanying notes should be considered an integral part of the Principal Statements.

Department of Defense
United States Marine Corps General Fund

CONSOLIDATED BALANCE SHEET

As of September 30, 2007 and 2006
($ in Thousands)

		2007 Consolidated		2006 Consolidated
ASSETS (Note 2)				
Intragovernmental:				
Fund Balance with Treasury (Note 3)				
Entity	$	17,067,669	$	12,774,224
Non-Entity Seized Iraqi Cash		0		0
Non-Entity - Other		204,152		118,017
Investments (Note 4)		0		0
Accounts Receivable (Note 5)		57,516		37,837
Other Assets (Note 6)		3,083		5,774
Total Intragovernmental Assets		17,332,420		12,935,852
Cash and Other Monetary Assets (Note 7)		37,783		59,649
Accounts Receivable, Net (Note 5)		32,735		21,282
Loans Receivable (Note 8)		0		0
Inventory and Related Property, Net (Note 9)		5,694,867		5,121,038
General Property, Plant and Equipment, Net (Note 10)		9,209,256		8,497,885
Investments (Note 4)		0		0
Other Assets (Note 6)		760,944		519,651
TOTAL ASSETS		33,068,005		27,155,357
LIABILITIES (Note 11)				
Intragovernmental:				
Accounts Payable (Note 12)		282,256		111,464
Debt (Note 13)		0		0
Other Liabilities (Note 15 & Note 16)		307,231		243,876
Total Intragovernmental Liabilities		589,487		355,340
Accounts Payable (Note 12)		1,302,211		520,609
Military Retirement and Other Federal Employment Benefits (Note 17)		216,869		214,433
Environmental and Disposal Liabilities (Note 14)		224,645		226,470
Loan Guarantee Liability (Note 8)		0		0
Other Liabilities (Note 15 & Note 16)		1,224,741		938,012
TOTAL LIABILITIES		3,557,953		2,254,864
NET POSITION				
Unexpended Appropriations - Earmarked Funds (Note 23)		0		0
Unexpended Appropriations - Other Funds		15,749,077		12,443,304
Cumulative Results of Operations - Earmarked Funds		475		383
Cumulative Results of Operations - Other Funds		13,760,500		12,456,806
TOTAL NET POSITION		29,510,052		24,900,493
TOTAL LIABILITIES AND NET POSITION	$	33,068,005	$	27,155,357

The accompanying notes are an integral part of the statements.

Department of Defense

United States Marine Corps General Fund

CONSOLIDATED STATEMENT OF NET COST

For the Years Ended September 30, 2007 and 2006

($ in Thousands)

		2007 Consolidated		2006 Consolidated
Program Costs				
Gross Costs	$	24,859,117	$	20,496,639
Less: Earned Revenue		(647,068)		(414,698)
Net Costs		24,212,049		20,081,941
Costs Not Assigned to Programs		0		0
Less: Earned Revenue Not Attributable to Programs		0		0
Net Cost of Operations	$	24,212,049	$	20,081,941

The accompanying notes are an integral part of the statements.

Department of Defense
United States Marine Corps General Fund

CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION

For the Years Ended September 30, 2007 and 2006
($ in Thousands)

	Earmarked Funds	Other Funds
CUMULATIVE RESULTS OF OPERATIONS		
Beginning Balances	$ 383	$ 12,456,806
Prior Period Adjustments:		
Changes in accounting principles (+/-)	0	0
Correction of errors (+/-)	0	0
Beginning Balances, as adjusted	383	12,456,806
Budgetary Financing Sources:		
Other adjustments (rescissions, etc) (+/-)	0	0
Appropriations used	0	25,400,443
Nonexchange revenue	0	0
Donations and forfeitures of cash and cash equivalents	0	0
Transfers in/out without reimbursement (+/-)	134	0
Other budgetary financing sources (+/-)	0	0
Other Financing Sources:		
Donations and forfeitures of property	0	0
Transfers in/out without reimbursement (+/-)	0	3,535
Imputed financing from costs absorbed by others	0	71,325
Other (+/-)	0	40,398
Total Financing Sources	134	25,515,701
Net Cost of Operations (+/-)	42	24,212,007
Net Change	92	1,303,694
Cumulative Results of Operations	$ 475	$ 13,760,500
UNEXPENDED APPROPRIATIONS		
Beginning Balances	$ 0	$ 12,443,304
Prior Period Adjustments (+/-)		
Changes in accounting principles (+/-)	0	0
Correction of errors (+/-)	0	0
Beginning Balances, as adjusted	0	12,443,304
Budgetary Financing Sources:		
Appropriations received	0	28,863,583
Appropriations transferred-in/out (+/-)	0	(86,118)
Other adjustments (rescissions, etc) (+/-)	0	(71,249)
Appropriations used	0	(25,400,443)
Total Budgetary Financing Sources	0	3,305,773
Unexpended Appropriations	0	15,749,077
Net Position	$ 475	$ 29,509,577

The accompanying notes are an integral part of the statements.

Department of Defense
United States Marine Corps General Fund

CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION

For the Years Ended September 30, 2007 and 2006
($ in Thousands)

	2007 Consolidated	2006 Consolidated
CUMULATIVE RESULTS OF OPERATIONS		
Beginning Balances	$ 12,457,189	$ 7,758,562
Prior Period Adjustments:		
Changes in accounting principles (+/-)	0	0
Correction of errors (+/-)	0	3,158,868
Beginning Balances, as adjusted	12,457,189	10,917,430
Budgetary Financing Sources:		
Other adjustments (rescissions, etc) (+/-)	0	0
Appropriations used	25,400,443	21,463,922
Nonexchange revenue	0	0
Donations and forfeitures of cash and cash equivalents	0	0
Transfers in/out without reimbursement (+/-)	134	158
Other budgetary financing sources (+/-)	0	0
Other Financing Sources:		
Donations and forfeitures of property	0	0
Transfers in/out without reimbursement (+/-)	3,535	90,379
Imputed financing from costs absorbed by others	71,325	67,241
Other (+/-)	40,398	0
Total Financing Sources	25,515,835	21,621,700
Net Cost of Operations (+/-)	24,212,049	20,081,941
Net Change	1,303,786	1,539,759
Cumulative Results of Operations	$ 13,760,975	$ 12,457,189
UNEXPENDED APPROPRIATIONS		
Beginning Balances	$ 12,443,304	$ 8,857,933
Prior Period Adjustments (+/-)		
Changes in accounting principles (+/-)	0	0
Correction of errors (+/-)	0	0
Beginning Balances, as adjusted	12,443,304	8,857,933
Budgetary Financing Sources:		
Appropriations received	28,863,583	25,417,616
Appropriations transferred-in/out (+/-)	(86,118)	(106,906)
Other adjustments (rescissions, etc) (+/-)	(71,249)	(261,417)
Appropriations used	(25,400,443)	(21,463,922)
Total Budgetary Financing Sources	3,305,773	3,585,371
Unexpended Appropriations	15,749,077	12,443,304
Net Position	$ 29,510,052	$ 24,900,493

Department of Defense
United States Marine Corps General Fund

COMBINED STATEMENT OF BUDGETARY RESOURCES

For the Years Ended September 30, 2007 and 2006
($ in Thousands)

	2007 Combined	2006 Combined
BUDGETARY FINANCING ACCOUNTS		
Budgetary Resources:		
Unobligated balance, brought forward, October 1	$ 2,582,128	$ 2,111,332
Recoveries of prior year unpaid obligations	1,796,992	1,569,189
Budget Authority:		
Earned	28,863,717	25,417,774
Borrowing authority	0	0
Contract authority	0	0
Spending authority from offsetting collections:		
Other adjustments (rescissions, etc) (+/-)		
Collected	617,575	580,388
Change in receivables from Federal sources	18,097	(61,287)
Change in unfilled customer orders		
Advances received	0	0
Without advance from Federal sources	(71,500)	(47,838)
Anticipated for rest of year, without advances	0	0
Previously unavailable	0	0
Expenditure Transfers from trust funds	0	0
Subtotal	29,427,889	25,889,037
Nonexpenditure Transfers, net, anticipated and actual	(86,118)	(106,906)
Temporarily not available pursuant to Public Law	0	0
Permanently not available	(71,249)	(261,418)
Total Budgetary Resources	33,649,642	29,201,234
Status of Budgetary Resources:		
Obligations incurred:		
Direct	29,635,288	25,801,864
Reimbursable	613,479	817,242
Subtotal	30,248,767	26,619,106
Unobligated balance:		
Apportioned	2,953,053	2,298,754
Exempt from apportionment	0	0
Subtotal	2,953,053	2,298,754
Unobligated balances not available	447,822	283,374
Total Status of Budgetary Resources	$ 33,649,642	$ 29,201,234

The accompanying notes are an integral part of the statements.

Department of Defense
United States Marine Corps General Fund
COMBINED STATEMENT OF BUDGETARY RESOURCES
For the Years Ended September 30, 2007 and 2006
($ in Thousands)

	2007 Combined	2006 Combined
RELATIONSHIP OF OBLIGATIONS TO OUTLAYS		
Change in Obligated Balance:		
Obligated balance, net		
Unpaid obligations, brought forward, October 1	$ 10,418,539	$ 7,499,117
Less: Uncollected customer payments from		
Federal sources, brought forward, October 1	(207,650)	(316,775)
Total Unpaid Obligated Balance	10,210,889	7,182,342
Obligations incurred, net (+/-)	30,248,767	26,619,106
Less: Gross outlays	(25,029,079)	(22,130,495)
Obligated balance transferred, net		
Actual transfers, unpaid obligations (+/-)	0	0
Actual transfers, uncollected customer		
payments from Federal sources (+/-)	0	0
Total Unpaid Obligated Balance Transferred, net	0	0
Less: Recoveries of prior year unpaid obligations, actual	(1,796,992)	(1,569,189)
Change in uncollected customer		
payments from Federal sources (+/-)	53,403	109,126
Obligated balance, net, end of period		
Unpaid obligations	13,841,236	10,418,539
Less: Uncollected customer payments from		
Federal sources	(154,247)	(207,650)
Total Unpaid Obligated Balance, net, end of period	13,686,989	10,210,889
Net Outlays:		
Gross Outlays	25,029,079	22,130,495
Less: Offsetting collections	(617,574)	(580,388)
Less: Distributed Offsetting receipts	20,195	3,296
Net Outlays	$ 24,431,700	$ 21,553,403

The accompanying notes are an integral part of the statements.

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United States Marine Corps General Fund

Notes to the Principal Statements

Department of the Navy Subsidiary Financial Statements

2007 Annual Financial Report

Note 1. Significant Accounting Policies

1.A. Basis of Presentation

The United States Marine Corps (USMC), a component of the Department of the Navy (DON), has prepared these financial statements to report the financial position and results of operations, as required by the Chief Financial Officers (CFO) Act of 1990, expanded by the Government Management Reform Act of 1994, and other appropriate legislation. Though USMC produces General Fund (GF) financial statements as a stand alone entity, USMC remains a subsidiary of DON for financial reporting purposes. The financial statements have been prepared from the books and records of USMC GF in accordance with the Department of Defense (DoD), Financial Management Regulation, the Office of Management and Budget (OMB) Circular No. A-136, Financial Reporting Requirements, and to the extent possible, generally accepted accounting principles (GAAP). Effective 4th Quarter, Fiscal Year (FY) 2006, DoD no longer publishes consolidating/combining financial statements. The accompanying financial statements account for all resources for which USMC GF is responsible unless otherwise noted. Information relative to classified assets, programs, and operations is aggregated and reported in such a manner that it is not discernable. In addition to the financial statements, and pursuant to OMB directives, USMC GF also prepares financial reports that are used to monitor and control the use of budgetary resources.

The USMC GF is unable to fully implement all elements of GAAP and OMB Circular A-136, due to limitations of its financial and nonfinancial management processes and systems that feed into the financial statements. The USMC GF derives its reported values and information for major asset and liability categories largely from nonfinancial systems, such as inventory systems and logistic systems. These systems were designed to support reporting requirements for maintaining accountability over assets and reporting the status of federal appropriations rather than preparing financial statements in accordance with GAAP. The USMC GF continues to implement process and system improvements addressing these limitations.

The USMC GF has no auditor identified financial statements material weaknesses, other than as part of the DON Financial Statements. The USMC GF continues to strengthen its financial management and financial reporting processes. The USMC GF has required the implementation of standard financial processes throughout the Marine Corps enterprise. Standardization improves transaction processing, management controls and information accuracy. The USMC Financial Improvement Initiative program has completed an in-depth assessment, evaluation and has implemented several remediation action efforts, in progress of completing self evaluation of management controls in compliance with Appendix A sections of OMB A-123 requirements. The USMC GF self assessment indicates the existence of the following material, or significant, financial statements weaknesses: (1) Financial Management Systems, (2) Environmental Liabilities, (3) General Property, Plant, and Equipment, (4) Operating Materiel and Supplies, and (5) Accounts Payable. The USMC GF does not have other identified financial management weaknesses that are considered material in USMC GF's financial management and reporting.

1.B. Mission of the Reporting Entity

The USMC was created on November 10, 1775 by an act of the 2nd Continental Congress. The overall mission of USMC is to provide trained and equipped forces to Combatant Commanders in support of the President's National Security Strategy. As set forth in the National Security Act of 1947, USMC missions are: to seize and defend advanced naval bases and to conduct such land operations as may be essential to the prosecution of a naval campaign; to provide detachments and organizations for service in armed vessels of the Navy or for protection of naval property on naval stations and bases; to develop, with the other Armed Forces, the tactics, techniques, and equipment employed by landing forces in amphibious operations; to train and equip, as required, Marine forces for airborne operations; to develop, with the other Armed Forces, doctrine, procedures, and equipment of interest to USMC for airborne operations which are not provided for by the Army; and to be able to expand from a peacetime posture to meet the needs of war in accordance with mobilization plans.

1.C. Appropriations and Funds

The USMC GF receives its appropriations and funds as general, special, and deposit funds. These appropriations and funds may be either provided solely to USMC GF or shared with other DON activities. The USMC GF uses these appropriations and funds to execute its mission and subsequently report on resource usage.

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

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

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

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

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

The USMC GF is a party to allocation transfers to and from other federal agencies receiving entity assets. Allocation transfers are legal delegations by one department of its authority to obligate budget authority and outlay funds for another department. Generally, all financial activity related to these allocation transfers (e.g., authority, obligation, outlays) is reported in the financial statements of the parent entity. The USMC GF receives allocation transfers, from DON and DoD.

1.D. Basis of Accounting

The USMC operates a single general fund accounting system – the Standard Accounting, Budgeting, and Reporting System (SABRS). Through this system USMC GF records the majority of the financial transactions reflected in these financial statements. The SABRS is a transaction driven general ledger accounting system that utilizes standardized transactions for processing. General ledger postings are derived from centralized posting logic maintained in a table within the accounting system and applied against detail transactions. The posting logic on this table is maintained in accordance with all applicable guidance and attempts to meet the standards of GAAP. Both budgetary and proprietary general ledgers are maintained and utilized for reporting. Transactions are entered into the accounting system via interfaces with financial feeder systems, electronically or manually.

The SABRS is interfaced with DoD approved business enterprise systems, such as the Defense Travel System, Standard Procurement System, Defense Civilian Personnel System, and Wide Area Work Flow. These interfaces improve financial reporting and eliminate manual recording by capturing data from the source systems. The SABRS is also Standard Financial Information Structure (SFIS) Phase 1 compliant. The USMC was the first and currently only agency to implement SFIS Phase 1. The SFIS will provide DoD a solution for identifying financial events in a like manner for all DoD components.

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

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

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

1.E. Revenues and Other Financing Sources

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

The USMC GF does not include nonmonetary support provided by U.S. allies for common defense and mutual security in the Statement of Net Cost and the Note 21, Reconciliation of Net Cost of Operations to Budget. The U.S. has cost sharing agreements with other countries that include both direct and indirect sharing of costs that each country incurs in support of the same general purpose. Examples include countries where there is a mutual or reciprocal defense agreement, where U.S. troops are stationed, or where the U.S. Fleet is in port.

1.F. Recognition of Expenses

For financial reporting purposes, DoD policy requires the recognition of operating expenses in the period incurred. However, because USMC GF's financial and nonfinancial feeder systems were not designed to collect and record financial information on the full accrual accounting basis, accruals are made for major items such as payroll expenses, accounts payable, environmental liabilities, and unbilled revenue. In the case of Operating Materiels and Supplies (OM&S), operating expenses are generally recognized when the items are purchased. Efforts are underway to transition toward the consumption method for recognizing OM&S expenses. Operating expenses are adjusted as a result of the elimination of trading partner balances between DoD components. Net increases or decreases in unexpended appropriations are recognized as a change in the net position. Certain expenses, such as annual and military leave earned but not taken, are financed in the period in which payment is made.

1.G. Accounting for Intragovernmental Activities

Preparation of reliable financial statements requires the elimination of transactions occurring among entities within DoD or between two or more federal agencies. However, USMC GF, as well as the majority of the Federal Government, cannot consistently and accurately eliminate intragovernmental transactions by customer because USMC GF's and many other federal agencies' systems do not track buyer and seller data at the transaction level. In an effort to more efficiently identify intragovernmental transactions by customer, USMC GF has implemented a field in its accounting system to capture trading partner data. Generally, seller entities within DoD provide summary seller side balances for revenue, accounts receivable, and unearned revenue to the buyer side internal DoD accounting offices. In most cases, the buyer side records are adjusted to agree with DoD seller side balances. IntraDoD intragovernmental balances are then eliminated. The volume of intragovernmental transactions is so large that after the fact reconciliation cannot be accomplished effectively with existing or foreseeable resources. The DoD is developing long term system improvements that will include sufficient up front edits and controls eliminating the need for after the fact reconciliations.

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

The DoD's proportionate share of public debt and related expenses of the Federal Government is not included. The Federal Government does not apportion debt and its related costs to federal agencies. The DoD's financial statements, therefore, do not report any portion of the public debt or interest thereon, nor do the statements report the source of public financing whether from issuance of debt or tax revenues.

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

1.H. Transactions with Foreign Governments and International Organizations

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

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

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

In addition, DFAS sites and USACE Finance Center submit reports to the U.S. Treasury by appropriation on interagency transfers, collections received, and disbursements issued. The U.S. Treasury records this information to the applicable fund balance with treasury account. Differences between USMC GF/DON GF's recorded balance in the fund balance with treasury accounts and U.S. Treasury's fund balance with treasury accounts sometimes result and are subsequently reconciled.

1.J. Foreign Currency

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

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

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

1.K. Accounts Receivable

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

1.L. Direct Loans and Loan Guarantees

Not applicable.

1.M. Inventories and Related Property

The USMC GF reports its inventory of repair parts, munitions, and ammunition in related property as OM&S. The USMC GF manages only military or government specific materiel under normal conditions. Items commonly used in and available from the commercial sector are not managed in USMC GF OM&S management activities. The USMC GF holds material based on military need and support for contingencies. Most of USMC GF's OM&S inventories are currently reported at an approximation of historical cost using latest acquisition cost adjusted for holding gains and losses. The USMC GF uses the latest acquisition cost method because legacy inventory systems were designed for materiel management rather than accounting. Although the legacy systems provide visibility and accountability over items, they do not maintain historical cost data necessary to comply with SFFAS No. 3, "Accounting for Inventory and Related Property." Additionally, these systems cannot produce financial transactions using the USSGL, as required by the Federal Financial Management Improvement Act of 1996 (Public Law 104 208). Implementation of moving average cost valuation would be both cost prohibitive as well as burdensome for USMC GF. In addition, historical cost information is not readily available to implement the moving average cost methodology. Consequently, USMC GF has elected to value its OM&S using latest acquisition cost for financial statements reporting and presentation purpose, as appropriated in accordance with SFFAS No. 3. The USMC GF has established an interface between the Operating Materials Supply Inventory System and its accounting system, SABRS.

Other OM&S, including munitions not held for sale, are valued at standard purchase price. The USMC GF uses both the consumption method and the purchase method of accounting for OM&S. Items that are centrally managed and stored, such as ammunition, tactical missiles, and engines are generally recorded using the consumption method and reported on the Balance Sheet as OM&S. When current systems cannot fully support the consumption method, USMC GF uses the purchase method. Under this method materiels and supplies are expensed when purchased. During FY 2007, USMC GF expensed significant amounts using the purchase method because the systems could not support the consumption method or management deemed that the item was in the hands of the end user. This is a material weakness for the DoD and long term system corrections are in process. Once the proper systems are in place, these items will be accounted for under the consumption method of accounting.

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

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

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

The USMC GF investments in U.S. Treasury securities are reported in the DON General Fund Financial Statements.

1.O. General Property, Plant, and Equipment

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

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

The DoD is moving away from a standard capitalization threshold for all categories (e.g., real property, military equipment, etc.) of General Property Plant and Equipment (PP&E) to one that is specific for each individual category. In FY 2006, DoD revised the real property capitalization threshold from $100 thousand to $20 thousand. The current $100 thousand capitalization threshold remains unchanged for the remaining General PP&E categories. Although DoD revised the real property capitalization threshold to $20 thousand, USMC GF real property capitalization threshold remains $100 thousand due to system and process limitations.

General PP&E, exclusive of military equipment, is capitalized at historical acquisition cost plus capitalized improvements when an asset has a useful life of two or more years, and the acquisition cost equals or exceeds DoD's capitalization threshold of $100 thousand. The DoD also requires capitalization of improvement costs over the DoD capitalization threshold of $100 thousand for General PP&E. The DoD depreciates all General PP&E, other than land, on a straight-line basis. Land is not depreciated. General PP&E previously capitalized at amounts below $100 thousand were written off General Fund financial statements in FY 1998.

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

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

The USMC GF has established an interface between its accounting system, SABRS, and the Defense Property Accountability System in order to decrease the amount of manual journal vouchers and data calls and increase the efficiency of reported data.

1.P. Advances and Prepayments

The DoD's policy is to record advances and prepayments in accordance with GAAP. As such, payments in advance of the receipt of goods and services are reported as an asset on the Balance Sheet. The DoD's policy is to expense and/or properly classify assets when the related goods and services are received. Not all DoD entities have implemented this policy primarily due to system limitations.

1.Q. Leases

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

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

1.R. Other Assets

Other Assets includes those assets, such as military and civil service employee pay advances, travel advances, and certain contracting financing payments that are not reported elsewhere on USMC GF's Balance Sheet.

The USMC GF conducts business with commercial contractors under two primary types of contracts: fixed price and cost reimbursable. To alleviate the potential financial burden on the contractor that long-term contracts can cause, USMC GF may provide financing payments. The USMC GF does not make financing payment for real property construction; USMC GF construction projects are managed by the Navy and reported in DON Balance Sheet and related notes. Contract financing payments are defined in the Federal Acquisition Regulations (FAR), Part 32, as authorized disbursements of monies to a contractor prior to acceptance of supplies or services by the Federal Government. Contract financing payment clauses are incorporated in the contract terms and conditions and may include advance payments, performance-based payments, commercial advance and interim payments, progress payments based on cost, and interim payments under certain cost-reimbursement contracts.

Contract financing payments do not include invoice payments, payments for partial deliveries, lease and rental payments, or progress payments based on a percentage or stage of completion, which the Defense Federal Acquisition Regulation Supplement authorizes only for construction of real property, shipbuilding, and ship conversion, alteration, or repair. It is DoD policy to record contract financing payments as Other Assets.

In addition, based on FAR, USMC GF makes financing payments under fixed price contracts that are not based on a percentage of completion. The USMC GF reports these financing payments as “Other Assets.” The USMC GF treats these payments as advances or prepayment because USMC GF becomes liable only after the contractor delivers the goods in conformance with the contract terms. If the contractor does not deliver a satisfactory product, USMC GF is not obligated to reimburse the contractor for its costs and the contractor is liable to repay USMC GF for the full amount of the advance.

1.S. Contingencies and Other Liabilities

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

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

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

1.T. Accrued Leave

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

1.U. Net Position

Net Position consists of unexpended appropriations and cumulative results of operations. Unexpended appropriations represent the amounts of authority that are unobligated and have not been rescinded or withdrawn. Unexpended appropriations also represent amounts obligated for which legal liabilities for payments have not been incurred. Cumulative results of operations represent the net difference, since inception of an activity, between expenses and losses and financing sources (including appropriations, revenue, and gains). Beginning with FY 1998, the cumulative results also include donations and transfers in and out of assets that were not reimbursement.

1.V. Treaties for Use of Foreign Bases

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

1.W. Comparative Data

Not applicable.

1.X. Unexpended Obligations

The USMC GF obligates funds to provide goods and services for outstanding orders not yet delivered. The financial statements do not reflect this liability for payment for goods and services not yet delivered unless title passes.

1.Y. Undistributed Disbursements and Collection

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

The DoD policy is to allocate supported undistributed disbursements and collections between federal and nonfederal categories based on the percentage of distributed federal and nonfederal accounts payable and accounts receivable. Unsupported undistributed disbursements are recorded in accounts payable. Unsupported undistributed collections are recorded in other liabilities. The USMC GF does not follow this procedure. For USMC GF, undistributed collections are allocated and recorded against federal and nonfederal accounts receivable based on the percentage of reimbursable receivables in each category. Undistributed collections are not recorded as other liabilities since the majority of time they remain USMC GF collections that were not processed due to timing difference. Undistributed disbursements are recorded against nonfederal accounts payable. Undistributed disbursements are not allocated to federal accounts payable as federal accounts payable must agree with trading partner eliminations.

1.Z. Significant Events

Beginning 4th Quarter, FY 2007, DoD began presenting the Statement of Financing (SOF) as a note in accordance with OMB Circular A-136. The SOF will no longer be considered a basic statement; but is now referred to as "Reconciliation of Net Cost of Operations to Budget."

Note 2. Nonentity Assets

As of September 30	2007	2006
(Amounts in Thousands)		
1. Intragovernmental Assets		
A. Fund Balance with Treasury	$ 204,152	$ 118,017
B. Accounts Receivable	0	0
C. Total Intragovernmental Assets	$ 204,152	$ 118,017
2. Nonfederal Assets		
A. Cash and Other Monetary Assets	$ 37,783	$ 59,649
B. Accounts Receivable	278	199
C. Other Assets	0	0
D. Total Nonfederal Assets	$ 38,061	$ 59,848
3. Total Nonentity Assets	$ 242,213	$ 177,865
4. Total Entity Assets	$ 32,825,792	$ 26,977,492
5. Total Assets	$ 33,068,005	$ 27,155,357

Standard Disclosures

Nonentity assets are assets for which the United States Marine Corps General Fund (USMC GF) maintains stewardship accountability and responsibility to report, but are not available for USMC's operations.

The nonentity fund balance with treasury represents amounts in USMC GF deposit fund accounts. The deposit fund accounts contain various withholdings from Marines' pay such as taxes, allotments, and garnishments held until the appropriate disbursement date. The USMC GF maintains stewardship accountability and reporting responsibility for these assets, but the assets are not available for use in operations.

Nonentity cash and other monetary assets represent disbursing officers' cash and foreign currency as reported on the Statement of Accountability. These assets are held by USMC disbursing officers, as agents of the U.S. Treasury, and are not available for use in USMC's operations.

The nonentity nonfederal accounts receivable represents interest, fines, and penalties receivable on aged delinquent debt. Once collected, nonentity receivables are deposited to the U.S. Treasury as miscellaneous receipts.

Note 3. Fund Balance with Treasury

As of September 30		2007		2006
(Amounts in Thousands)				
1. Fund Balances				
A. Appropriated Funds	$	17,067,169	$	12,773,794
B. Revolving Funds		0		0
C. Trust Funds		0		0
D. Special Funds		500		430
E. Other Fund Types		204,152		118,017
F. Total Fund Balances	$	17,271,821	$	12,892,241
2. Fund Balances Per Treasury Versus Agency				
A. Fund Balance per Treasury	$	15,543,476	$	11,573,192
B. Fund Balance per Marine Corps		17,271,821		12,892,241
3. Reconciling Amount	$	(1,728,345)	$	(1,319,049)

Standard Disclosures

Explanation of Reconciliation Amount	
(In Thousands)	
Shared Appropriations per United States Marine Corps General Fund (USMC GF)*	$1,792,444
Suspense and Deposit Accounts per USMC GF**	(20,628)
Canceling Year Appropriations***	(43,471)
Total Reconciling Amount	**$1,728,345**

*This amount is the Fund Balance With Treasury (FBWT) for USMC GF portion of appropriations shared with the U.S. Navy: Research and Development, Test and Evaluation; Procurement of Ammunition; Wildlife Conservation on Military Reservations, Navy; and Family Housing Operation and Maintenance, Navy and Marine Corps. The U.S. Treasury maintains and reports fund balances at the Treasury Index appropriation level. As a result, the U.S. Treasury does not separately identify USMC GF portion of fund balance with treasury for the shared appropriations.

**This amount is the FBWT for suspense and deposit accounts shared with the Department of the Navy: Disbursing Officer Suspense Account; Lost or Cancelled Treasury Checks Suspense Account; Interfund/ Intragovernmental Payment and Collection (IPAC) Suspense Account; and Small Escrow Amounts Deposit Account. The U.S. Treasury does not separately identify USMC GF portion of fund balance with treasury for the shared suspense and deposit accounts.

***This amount is the total FBWT for the appropriations that are canceling in FY 2007. This amount is not included in the final reports per applicable guidance.

Other Information

Other fund types represent USMC GF deposit fund accounts. The deposit fund accounts contain various withholdings from Marines' pay such as taxes, allotments, and garnishments held until the appropriate disbursement date. The USMC GF maintains stewardship accountability and reporting responsibility for these assets, but the assets are not available for use in USMC GF operations.

Status of Fund Balance with Treasury

As of September 30	2007		2006	
(Amounts in Thousands)				
1. Unobligated Balance				
A. Available	$	2,953,053	$	2,298,754
B. Unavailable		447,822		283,374
2. Obligated Balance not yet Disbursed	$	13,841,236	$	10,418,539
3. Nonbudgetary FBWT	$	183,957	$	99,224
4. NonFBWT Budgetary Accounts	$	(154,247)	$	(207,650)
5. Total	$	17,271,821	$	12,892,241

Standard Disclosures
The Status of FBWT reflects the budgetary resources to support the FBWT.

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

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

Nonbudgetary FBWT includes entity and nonentity FBWT accounts which represent adjustments that do not have budgetary authority, such as unavailable receipt accounts or clearing accounts. Nonbudgetary FBWT is comprised of the FBWT for the Disbursing Officer Suspense Account, Lost or Cancelled Treasury Checks Suspense Account, Interfund/IPAC Suspense Account, Small Escrow Accounts Deposit Account, and the Pay of the Marine Corps Deposit Account.

NonFBWT Budgetary Accounts represent adjustments to budgetary accounts that do not affect FBWT. NonFBWT budgetary accounts are comprised of unfilled customer orders without advance and reimbursements and other income earned-receivable. This category reduces the Status of FBWT.

Unobligated balances are segregated to show available and unavailable amounts in the note schedule. Certain unobligated balances may be restricted to future use and are not apportioned for current use. The USMC GF has no restrictions on unavailable/unobligated balances.

Disclosures Related to Suspense/Budget Clearing Accounts

As of September 30	2005	2006	2007	(Decrease)/ Increase from FY 2006 - 2007
(Amounts in Thousands)				
Account				
F3845 – Personal Property Proceeds	$ 0	$ 0	$ 0	$ 0
F3875 – Disbursing Officer Suspense	(15,167)	(18,771)	(20,452)	(1,681)
F3880 – Lost or Cancelled Treasury Checks	(43)	(32)	257	289
F3882 – Uniformed Services Thrift Savings Plan Suspense	0	0	0	0
F3885 – Interfund/IPAC Suspense	(287)	9	0	(9)
F3886 – Thrift Savings Plan Suspense	0	0	0	0
Total	$ (15,497)	$ (18,794)	$ (20,195)	$ (1,401)

Standard Disclosures
The F3875 suspense clearing represents the disbursing officer's suspense. Account F3885 represents the Interfund/IPAC suspense. These suspense accounts temporarily hold collections or disbursements until they can be assigned or identified to a valid appropriation.

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

Disclosures Related to Problem Disbursements and In-Transit Disbursements

As of September 30	2005	2006	2007	(Decrease)/ Increase from FY 2006 to 2007
(Amounts in Thousands)				
1. Total Problem Disbursements, Absolute Value				
A. Unmatched Disbursements (UMDs)	$ 36,589	$ 34,640	$ 14,108	$ (20,532)
B. Negative Unliquidated Obligations (NULO)	5,633	2,905	3,556	651
C. In-Transit Disbursements	524,623	324,330	134,408	(189,922)
Total	$ 566,845	$ 361,875	$ 152,072	$ (209,803)

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

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

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

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

Beginning with 2nd Quarter, FY 2007, in-transit disbursements are reported as an absolute value as opposed to net amounts disclosed in prior years. This reporting change applies to amounts in the note schedule for both the current and comparative years.

Note 4. Investments and Related Interest

The United States Marine Corps General Fund investments and related interest are reported under the Department of the Navy General Fund.

Note 5. Accounts Receivable

As of September 30	2007			2006
	Gross Amount Due	Allowance For Estimated Uncollectibles	Accounts Receivable, Net	Accounts Receivable, Net
(Amounts in Thousands)				
1. Intragovernmental Receivables	$ 57,516	N/A	$ 57,516	$ 37,837
2. Nonfederal Receivables (From the Public)	$ 40,556	$ (7,821)	$ 32,735	$ 21,282
3. Total Accounts Receivable	$ 98,072	$ (7,821)	$ 90,251	$ 59,119

Aged Accounts Receivable

As of September 30	2007				2006			
	Intragovernmental		Nonfederal		Intragovernmental		Nonfederal	
(Amounts in Thousands)								
CATEGORY								
Nondelinquent								
Current	$	62,067	$	36,123	$	46,286	$	12,684
Noncurrent		0		0		0		0
Delinquent								
1 to 30 days	$	320	$	6,672	$	743	$	2,034
31 to 60 days		46		860		8		537
61 to 90 days		12		1,244		135		1,659
91 to 180 days		114		1,424		85		1,574
181 days to 1 year		36		1,686		22		2,096
Greater than 1 year and less than or equal to 2 years		0		2,216		35		798
Greater than 2 years and less than or equal to 6 years		0		524		0		691
Greater than 6 years and less than or equal to 10 years		0		206		0		59
Greater than 10 years		0		60		0		36
Subtotal	$	62,595	$	51,015	$	47,314	$	22,168
Less Supported Undistributed Collections		(15,436)		(10,459)		(2,130)		0
Less Eliminations		10,357		0		(7,347)		0
Less Other		0		0		0		0
Total	$	57,516	$	40,556	$	37,837	$	22,168

Information Related to Aged Accounts Receivable
The total delinquent balance for FY 2007 is $15.4 million, of which $8.1 million of the balance are outstanding receivables in the United States Marine Corps General Fund reimbursable program. The remaining $7.3 million of the delinquent balance are refunds receivable that are managed by Defense Finance and Accounting Services Debt Management Office (DMO). The DMO is working these amounts by referring them to the U.S. Treasury for offset or due process.

Note 6. Other Assets

As of September 30	2007		2006	
(Amounts in Thousands)				
1. Intragovernmental Other Assets				
A. Advances and Prepayments	$	3,083	$	5,774
B. Other Assets		0		0
C. Total Intragovernmental Other Assets	$	3,083	$	5,774
2. Nonfederal Other Assets				
A. Outstanding Contract Financing Payments	$	740,207	$	505,172
B. Other Assets (With the Public)		20,737		14,479
C. Total Nonfederal Other Assets	$	760,944	$	519,651
3. Total Other Assets	$	764,027	$	525,425

Standard Disclosures
Other Assets (With the Public) is comprised of travel advances made to Marines and civilian personnel.

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

The Contract Financing Payment balance of $740.2 million is comprised of $688.5 million in contract financing payments and an additional $51.7 million in estimated future payments that will be paid to the contractor upon future delivery and Government acceptance of a satisfactory product. (See additional discussion in Note 15, Other Liabilities).

Note 7. Cash and Other Monetary Assets

As of September 30	2007		2006	
(Amounts in Thousands)				
1. Cash	$	37,768	$	59,639
2. Foreign Currency		15		10
3. Other Monetary Assets		0		0
4. Total Cash, Foreign Currency, & Other Monetary Assets	$	37,783	$	59,649

Standard Disclosures
Cash and foreign currency are nonentity assets and, as such, are considered restricted assets that are held by the United States Marine Corps General Fund (USMC GF) but not available to use in its operations.

Cash of $37.8 million and foreign currency of $15.0 thousand are restricted. These assets are held by USMC disbursing officers as agents of the U.S. Treasury.

The amounts reported as cash and foreign currency consist primarily of cash held by disbursing officers to carry out their payment, collection, and foreign currency accommodation exchange mission. The primary source of the amounts reported is the Statement of Accountability, a DoD disbursing officer's report.

The amount of foreign currency reported was valued using U.S. Treasury prevailing rate of exchange, the most favorable rate available to U.S. Government when acquiring foreign currency. Foreign currency is used to make official disbursements and to provide foreign currency for the exchange of U.S. dollars for military personnel.

Note 8. Direct Loan and/or Loan Guarantee Programs

Not applicable.

Note 9. Inventory and Related Property

As of September 30	2007	2006
(Amounts in Thousands)		
1. Inventory, Net	$ 0	$ 0
2. Operating Materiel & Supplies, Net	5,694,867	5,121,038
3. Stockpile Materiel, Net	0	0
4. Total	$ 5,694,867	$ 5,121,038

Inventory, Net

Not applicable.

Operating Materiel and Supplies, Net

As of September 30	2007			2006	
	OM&S Gross Value	Revaluation Allowance	OM&S, Net	OM&S, Net	Valuation Method
(Amounts in Thousands)					
1. OM&S Categories					
A. Held for Use	$ 5,179,630	$ 0	$ 5,179,630	$ 4,553,141	SP, LAC
B. Held for Repair	515,237	0	515,237	567,897	SP, LAC
C. Excess, Obsolete, and Unserviceable	42,099	(42,099)	0	0	NRV
D. Total	$ 5,736,966	$ (42,099)	$ 5,694,867	$ 5,121,038	

Legend for Valuation Methods:

Adjusted LAC = Latest Acquisition Cost, adjusted for holding gains and losses
NRV = Net Realizable Value
SP = Standard Price

Standard Disclosures

General Composition of Operating Materiels and Supplies (OM&S)

The OM&S includes (1) ammunition and munitions that consists of spare and repair parts and conventional missiles, and (2) Appropriation Purchase Account (APA) Secondary Inventory that consists of spare and repair parts, clothing and textiles, medical and dental supplies, and fuel.

Restrictions on Operating Materiels and Supplies

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

Decision Criteria for Identifying the Category to which Operating Materiels and Supplies are Assigned

In order to standardize reporting of the categories held for use, held for repair, and excess, obsolete, unserviceable, United States Marine Corps General Fund (USMC GF) implemented the Office of the Under Secretary of Defense (Comptroller) (OUSD(C)) condition code criterion as defined in the memorandum, "Accounting for Excess, Unserviceable, and Obsolete Inventory and Operating Materials and Supplies" dated, August 12, 2002. In addition, the condition code criterion was amended to include code "V" in the excess, obsolete, unserviceable category in September 2002.

The OM&S was reported as follows:

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

In addition to the account balances, the Statement of Federal Financial Accounting Standards No. 3, Accounting for Inventory and Related Property requires disclosure of the amount of OM&S held for "future use." This information is not captured by current OM&S systems which were designed for material management rather than accounting purposes.

Valuation Method for OM&S.

The USMC GF continues to value its OM&S using both standard price and latest acquisition cost adjusted for gains and losses. The USMC GF values certain aged ammunition and munitions, using the standard purchase price. The USMC GF values other OM&S, including ammunition and munitions using latest acquisition cost, adjusted for gains and losses. The USMC GF does not include a revaluation allowance for OM&S held for use or held for repair, but transfers items from these categories to excess, obsolete, and unserviceable where the revaluation allowance is reported. Of the gross $5.7 billion OM&S, $4.9 billion is valued using latest acquisition cost adjusted for gains and losses, the remaining, $817.3 million is valued at standard price.

Stockpile Materiel, Net

Not applicable.

Note 10. General PP&E, Net

As of September 30	2007					2006
	Depreciation/ Amortization Method	Service Life	Acquisition Value	(Accumulated Depreciation/ Amortization)	Net Book Value	Prior FY Net Book Value
(Amounts in Thousands)						
1.Major Asset Classes						
A. Land	N/A	N/A	$ 164,118	N/A	$ 164,118	$ 155,378
B. Buildings, Structures, and Facilities	S/L	20 or 40	7,775,077	$ (4,207,596)	3,567,481	3,529,432
C. Leasehold Improvements	S/L	lease term	0	0	0	0
D. Software	S/L	2-5 or 10	0	0	0	0
E. General Equipment	S/L	5 or 10	187,795	(145,041)	42,754	34,324
F. Military Equipment	S/L	Various	7,345,876	(1,910,973)	5,434,903	4,778,751
G. Assets Under Capital Lease	S/L	lease term	0	0	0	0
H. Construction-in-Progress	N/A	N/A	0	N/A	0	0
I. Other			0	0	0	0
J. Total General PP&E			$ 15,472,866	$ (6,263,610)	$ 9,209,256	$ 8,497,885

Standard Disclosures

Restrictions on the use or convertibility of General Property, Plant, and Equipment (PP&E), Net

For United States Marine Corps General Fund (USMC GF) sites outside of the continental U.S., there are no restrictions on the use or convertibility of General PP&E in accordance with international agreements.

Heritage Assets

The processes used to define items as having heritage significance vary between categories and type of assets being evaluated. Subject matter experts, including historians and curators, play a significant role in the definition process in addition to other criteria such as being listed on the National Register of Historic Places. In all cases, a myriad of federal statutes, service regulations, and other guidelines mandate heritage significance or provide guidance in its determination.

The methodology used to report the condition of the heritage assets was a combination of visual assessment of the objects, historic value to USMC GF collection, and general display and storage standards for historic collections. The overall condition of the collection objects is good.

Any additional information regarding heritage assets, multi-use heritage assets, and stewardship land is reported in Required Supplementary Information.

Museums

Museums are buildings, places, or institutions devoted to the acquisition, conservation, study, exhibition, and educational interpretation of objects having scientific, historical, or artistic value. The Secretary of the

Navy Instruction 5755.1A, Navy Museums, defines the scope of the Navy Museum program.

Stewardship Land
The USMC GF follows Department of Defense (DoD) Financial Management Regulation definition of stewardship land to include public domain, land set aside, and donated land. Within the definition of stewardship land, land can be further categorized as improved, semi-improved or in the other category of land.

Military Equipment
In accordance with the requirements of Statement of Federal Financial Accounting Standards (SFFAS) No. 23, Eliminating the Category National Defense Property, Plant, and Equipment, beginning in FY 2003, the DoD capitalized military equipment into General PP&E at estimated historical cost using information and methodology obtained from the Bureau of Economic Analysis (BEA). Effective 3rd Quarter, FY 2006, DoD replaced the BEA estimation methodology with one that is based on internal records for military equipment.

Assets Under Capital Lease

Not applicable.

Note 11. Liabilities Not Covered by Budgetary Resources

As of September 30	2007	2006
(Amounts in Thousands)		
1. Intragovernmental Liabilities		
A. Accounts Payable	$ 606	$ 0
B. Debt	0	0
C. Other	79,885	79,677
D. Total Intragovernmental Liabilities	$ 80,491	$ 79,677
2. Nonfederal Liabilities		
A. Accounts Payable	$ 3,230	$ 2,186
B. Military Retirement and Other Federal Employment Benefits	215,229	214,433
C. Environmental Liabilities	224,645	226,470
D. Other Liabilities	627,458	651,450
E. Total Nonfederal Liabilities	$ 1,070,562	$ 1,094,539
3. Total Liabilities Not Covered by Budgetary Resources	$ 1,151,053	$ 1,174,216
4. Total Liabilities Covered by Budgetary Resources	$ 2,406,900	$ 1,080,648
5. Total Liabilities	$ 3,557,953	$ 2,254,864

Standard Disclosures
Liabilities not covered by budgetary resources are liabilities for which congressional action is needed before budgetary resources can be provided.

Material Amounts Not Covered by Budgetary Resources
The Military Retirement and Other Federal Employment Benefits nonfederal liabilities (Federal Employees Compensation Act (FECA) Actuarial), $215.2 million; Environmental Liabilities, $224.6 million; and accounts payable from cancelling years –nonfederal liabilities, $3.2 million, are liabilities not covered by budgetary resources. These liabilities are not covered by realized budgetary resources as of the Balance Sheet date. Budgetary authority to satisfy these liabilities is expected to be provided in a future Defense Appropriations Act. The environmental liabilities are not funded by budgetary resources because they are estimates that may be cleaned up in future years. When that future budgetary authority is provided, these respective liabilities will be recorded as covered by budgetary resources with an associated funded expense.

Intragovernmental liabilities – other, not covered by budgetary resources includes FECA, $51.0 million and unemployment compensation, $28.6 million.

Nonfederal liabilities - other liabilities (not covered by budgetary resources) includes civilian and military annual leave liability, $586.7 million.

Military Retirement and Other Federal Employment Benefits not covered by budgetary resources are comprised of various employee actuarial liabilities not due and payable during the current fiscal year. These liabilities are primarily comprised of FECA, $215.2 million. Refer to Note 17, Military Retirement and Other Federal Employment Benefits, for additional details and disclosures.

Note 12. Accounts Payable

As of September 30	2007			2006
	Accounts Payable	Interest, Penalties, and Administrative Fees	Total	Total
(Amounts in Thousands)				
1. Intragovernmental Payables	$ 282,256	$ N/A	$ 282,256	$ 111,464
2. Nonfederal Payables (to the Public)	1,302,211	0	1,302,211	520,609
3. Total	$ 1,584,467	$ 0	$ 1,584,467	$ 632,073

Standard Disclosures
The United States Marine Corps General Fund systems do not track intragovernmental transactions by customer at the transaction level. Therefore, internal Department of Defense buyer-side balances are adjusted to agree with internal seller-side balances for revenue, accounts receivable, and unearned revenue. Accounts payable were adjusted by reclassifying amounts between federal and nonfederal accounts payable.

Note 13. Debt

Not applicable.

Note 14. Environmental Liabilities and Disposal Liabilities

As of September 30	2007 Current Liability	2007 Noncurrent Liability	2007 Total	2006 Total
(Amounts in Thousands)				
1. Environmental Liabilities--Nonfederal				
A. Accrued Environmental Restoration Liabilities				
1. Active Installations—Installation Restoration Program (IRP) and Building Demolition and Debris Removal (BD/DR)	$ 0	$ 0	$ 0	$ 0
2. Active Installations—Military Munitions Response Program (MMRP)	0	0	0	0
3. Formerly Used Defense Sites—IRP and BD/DR	0	0	0	0
4. Formerly Used Defense Sites—MMRP	0	0	0	0
B. Other Accrued Environmental Liabilities—Active Installations				
1. Environmental Corrective Action	198	30,758	30,956	40,637
2. Environmental Closure Requirements	179	193,510	193,689	185,833
3. Environmental Response at Operational Ranges	0	0	0	0
4. Other	0	0	0	0
C. Base Realignment and Closure (BRAC)				
1. Installation Restoration Program	0	0	0	0
2. Military Munitions Response Program	0	0	0	0
3. Environmental Corrective Action / Closure Requirements	0	0	0	0
4. Other	0	0	0	0
D. Environmental Disposal for Weapons Systems Programs				
1. Nuclear Powered Aircraft Carriers	0	0	0	0
2. Nuclear Powered Submarines	0	0	0	0
3. Other Nuclear Powered Ships	0	0	0	0
4. Other National Defense Weapons Systems	0	0	0	0
5. Chemical Weapons Disposal Program	0	0	0	0
6. Other	0	0	0	0
2. Total Environmental Liabilities	$ 377	$ 224,268	$ 224,645	$ 226,470

Standard Disclosures

Environmental Liabilities Nonfederal Other Accrued Environmental Liabilities – Active Installations

In the 4th Quarter, FY 2007, the United States Marine Corps General Fund (USMC GF) reported $31.0 million in Environmental Corrective Action and $193.7 million in Environmental Closure Requirements. The USMC GF is continuing efforts to complete their survey and estimations of USMC GF environmental liabilities of closure/decommissioning requirements for ongoing operations.

Applicable Laws and Regulations for Cleanup Requirements

The following is a summary of significant laws that affect USMC GF's conduct of environmental policy and regulations for cleanup requirements:

The Resource Conservation and Recovery Act (RCRA) of 1976 as amended by the Hazardous and Solid Waste Amendments of 1984, was the first comprehensive federal effort to deal with safe disposal of all types of hazardous wastes, and provides for "cradle to grave" tracking of hazardous wastes. The RCRA addresses and requires permits for solid waste and hazardous waste closure and corrective action, including solid waste landfill and hazardous waste permitted storage facility closures. Permits are required for treatment, storage or disposal. Requirements for underground storage tanks are also contained in RCRA.

The Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA), commonly referred to as the Superfund legislation, provided for Federal agencies authority to respond to the release or the substantial threat of release of hazardous substances into the environment. The CERCLA was amended several times; one of the amendments was the Superfund Amendment and Reauthorization Act of 1986. This amendment established procedures to ensure that actual or threatened hazardous substance releases have proper responses. The procedures address reporting, investigating, remedy selection, and responsive provisions.

The Clean Water Act (CWA) of 1977, Section 405 Disposal of Sewage Sludge, amended the Federal Water Pollution Control Act. The purpose of CWA is to restore and maintain the integrity of the nation's waters. Facilities may dispose of sewage sludge on site from the operation of a treatment works. The CWA implementing regulations established closure and post closure requirements for sewage sludge disposal. To help protect the nation's drinking water supply, including underground injections through a permitting scheme implemented by the states is the purpose of the Safe Drinking Water Act (SDWA) of 1974, amended in 1986 to include Wellhead Protection Areas. The SDWA regulates the underground disposal of wastes in deep wells and establishes a program to protect public water supply wells. One requirement to protect public water supply wells addresses closure of Class I injection wells used for industrial hazardous, industrial nonhazardous and municipal (nonhazardous) waste.

Methodology Used to Estimate NonDefense Environmental Restoration Program (Non-DERP) Environmental Liabilities

The Non-DERP environmental liability estimates are based on the following:

- Execution/payment amounts,
- Historical references (e.g., prior projects, investigations, monitoring),
- Current projects of comparable scope (similar sites),
- Estimates from vendors/contractors,
- Estimates from Military Construction Data Project form,
- Program Objectives Memorandum Guidebook, and
- Professional experience.

Description of the Types of Environmental Liabilities and Disposal Liabilities
Other Accrued Environmental Costs (Non-DERP), Cost, Base Realignment and Closure (BRAC), and Environmental Disposal for Weapons systems Programs
The USMC GF defines Non-DERP environmental sites/units as those sites/units associated with on-going operations such as solid waste management unit cleanup, landfill closure, permitted facilities, removal, replacement, retro fill, and/or disposal of the Polychlorinated Biphenyls (PCB) transformers, underground storage tank remedial investigation and closure. The USMC GF has reported NonDERP environmental liabilities for USMC GF installations totaled 225 projects and covered approximately 3,290 sites. The projects span the following Non-DERP reporting categories: (1) closure for units or sites put into service prior to September 30, 1997, (2) closure for units or sites put into service after September 30, 1997, and (3) corrective actions. There are no projects that are categorized as NonDERP environmental liability for "response at active ranges" and other reporting categories. For units or sites put into service after September 30, 1997, the number of years of service was used to allocate the liability for the current fiscal year and the accumulated liability to date.

Accrued Environmental Restoration Defense Environmental Restoration Program (DERP) Funded
The U.S. Navy centrally manages and executes DERP and BRAC portion at Department of the Navy (DON) level. Therefore, USMC GF does not report DERP or BRAC environmental liabilities.

Nature of Estimates and the Disclosure of Information Regarding Possible Changes due to Inflation, Deflation, Technology, or Applicable Laws and Regulations
NonDERP environmental liabilities can change in the future because of changes in laws/regulations and regulatory agencies agreements, and technology advances.

Description of the Level of Uncertainty Regarding the Accounting Estimates used to Calculate the Reported Environmental Liabilities
The environmental liabilities for USMC GF are based on accounting estimates that require certain judgments and assumptions that we believe are reasonable based upon information available to us at the time of calculating the estimates. The actual results may vary materially from the accounting estimates if laws/regulations change requiring a different closure method, or if agreements with regulatory agencies require remediation to a different degree than anticipated when calculating the estimates. The liabilities can be further impacted if further investigation of the environmental sites discloses contamination different than known at the time of the estimates.

Environmental Disclosures

Line A. The USMC GF reported an estimate for Other Environmental Liabilities (OEL). The USMC GF is determining what portion of OEL relates to units put into service after October 1, 1997. Therefore, detailed data is not available at this time.

Lines B and C. The USMC GF does not have any changes in the environmental liability estimates due to changes in laws, regulations, and technology.

Note 15. Other Liabilities

As of September 30	2007			2006
	Current Liability	Noncurrent Liability	Total	Total
(Amounts in Thousands)				
1. Intragovernmental				
A. Advances from Others	$ 0	$ 0	$ 0	$ 0
B. Deposit Funds and Suspense Account Liabilities	183,957	0	183,957	99,224
C. Disbursing Officer Cash	37,783	0	37,783	59,649
D. Judgment Fund Liabilities	0	0	0	0
E. FECA Reimbursement to the Department of Labor	22,421	28,537	50,958	50,081
F. Other Liabilities	34,533	0	34,533	34,922
G. Total Intragovernmental Other Liabilities	$ 278,694	$ 28,537	$ 307,231	$ 243,876
2. Nonfederal				
A. Accrued Funded Payroll and Benefits	$ 539,303	$ 0	$ 539,303	$ 173,846
B. Advances from Others	0	0	0	0
C. Deferred Credits	0	0	0	0
D. Deposit Funds and Suspense Accounts	0	0	0	0
E. Temporary Early Retirement Authority	0	0	0	0
F. Nonenvironmental Disposal Liabilities				
(1) Military Equipment (Nonnuclear)	0	0	0	0
(2) Excess/Obsolete Structures	5,282	34,110	39,392	39,392
(3) Conventional Munitions Disposal	0	0	0	0
G. Accrued Unfunded Annual Leave	586,677	0	586,677	608,058
H. Capital Lease Liability	0	0	0	0
I. Other Liabilities	4,348	55,021	59,369	116,716
J. Total Nonfederal Other Liabilities	$ 1,135,610	$ 89,131	$ 1,224,741	$ 938,012
3. Total Other Liabilities	$ 1,414,304	$ 117,668	$ 1,531,972	$ 1,181,888

Standard Disclosures

Intragovernmental other liabilities-others includes liabilities for unemployment and employee benefits.

Nonfederal other liabilities-other includes future contract financing payments.

Contingent liabilities balance includes $51.7 million in estimated future contract financing payments that will be paid to the contractor upon delivery and Government acceptance. In accordance with contract terms, specific rights to the contractor's work vests with the Government when a specific type of contract financing payments is made. This action protects taxpayer funds in the event of the contract nonperformance. These rights should not be misconstrued as the right of ownership. The United States Marine Corps General Fund (USMC GF) is under no obligation to pay the contractor for amounts greater than the amounts authorized in the contract until delivery and Government acceptance. Because it is probable that the contractor will complete its efforts and deliver a satisfactory product to USMC GF and the amount of potential future payments are estimable; USMC GF has recognized a contingent liability for estimated future payments, which are conditional pending delivery and Government acceptance.

Contingent liabilities balance, also, includes $1.4 million in estimated legal liabilities. The 1st Quarter, FY 2007, Department of Navy GF and USMC GF began recognizing and disclosing an estimate for contingent legal liabilities. The methodology to determine an estimate for contingent legal liabilities considers the likelihood of an unfavorable outcome or potential liability is provided as an overall assessment of all cases currently pending and not on an individual case basis. For more details, see Note 16, Commitments and Contingencies.

Capital Lease Liability

Not applicable.

Note 16. Commitments and Contingencies

Standard Disclosures

The United States Marine Corps General Fund (USMC GF), a sub-entity of the Department of the Navy (DON) General Fund (GF), is a party in various administrative proceedings and legal actions, with claims including environmental damage claims, equal opportunity matters, and contractual bid protests which may ultimately result in settlements or decisions adverse to the Federal Government. These proceedings and actions arise in the normal course of operations and their ultimate disposition is unknown. The USMC GF has accrued contingent liabilities for legal actions where Office of Navy General Counsel considers an adverse decision probable and the amount of the loss is measurable. In the event of an adverse judgment against the Government, some of the liabilities may be payable from the Judgment Fund. Others may be payable from DON resources, either directly or by reimbursement to the Judgment Fund. The USMC GF records Judgment Fund liabilities in Note 12, "Accounts Payable," or Note 15, "Other Liabilities."

The Office of Navy General Counsel completed a review of litigation and claims threatened or asserted involving the USMC GF to which DON attorneys devoted substantial attention in the form of legal consultation or representation. This review reflects a threshold of materiality of $3.6 million applied to individual and aggregate claims, litigation, and assessments arising out of a single event or series of events, and includes matters that existed on October 1, 2006 through September 30, 2007. The USMC GF has two cases that meet the existing FY 2007 USMC GF materiality threshold of $3.6 million. The DON legal counsel was unable to express an opinion concerning the likely outcome of these cases. Based on information contained in the FY 2007 Preliminary and Final Legal Representation Letters, management does not have sufficient reason to believe that it is likely that the Government will be liable for the amounts claimed in individual or aggregated cases.

Due to the inherent uncertainties of litigation, lawyers generally refrain from expressing judgments as to outcomes except in those relatively few clear cases. In response to a Department of Defense, Inspector General Audit, "DoD Process for Reporting Contingent Legal Liabilities," DON developed a methodology to determine an estimate for contingent legal liabilities. The DON/USMC began recognizing and disclosing an estimate for contingent legal liabilities beginning 1st Quarter, FY 2007. The methodology considers the likelihood of an unfavorable outcome or potential liability is provided as an overall assessment of all cases currently pending and not on an individual case basis. The likelihood of an unfavorable or potential liability was determined by using an average of the data from the preceding four years and the current year. The total dollar amount of the cases closed was divided by the total dollar amount claimed in those closed cases for each of the last four years plus current year which were then used to calculate the average. This average represents the percentage that has historically been paid on claims. It is based entirely on historical data. The merits of each individual case have not been taken into consideration. Until sufficient historical data can be collected for the Navy Working Capital Fund—Marine Corps, this estimate will consider all USMC funding sources together.

The estimate for those aggregate of cases considered reasonably possible to result in an adverse judgment against USMC is $17.6 million. Also, in Note 15, Other Liabilities, nonfederal other liabilities, USMC GF recognized an estimate for contingent legal liabilities that probably may result in an adverse judgment.

Other Commitments and Contingencies

The USMC GF is a party in numerous individual contracts that contain clauses, such as price escalation, award fee payments, or dispute resolution, that may or may mot result in a future outflow of expenditures. Currently, USMC GF does not have a systemic process by which it captures or assesses these potential contingent liabilities; therefore, the amounts reported may not fairly present USMC GF's contingent liabilities. The USMC GF contingent liabilities for obligations related to undelivered orders for open contracts citing canceled appropriations, which remain unfilled or unreconciled, and for contractual arrangements are reported at DON level.

Note 17. Military Retirement and Other Federal Employment Related Benefits

As of September 30	2007					2006
	Present Value of Benefits	Assumed Interest Rate (%)	(Less: Assets Available to Pay Benefits)	Unfunded Liability		Present Value of Benefits
(Amounts in Thousands)						
1. Pension and Health Actuarial Benefits						
A. Military Retirement Pensions	$ 0		$ 0	$ 0		$ 0
B. Military Retirement Health Benefits	0		0	0		0
C. Military Medicare-Eligible Retiree Benefits	0		0	0		0
D. Total Pension and Health Actuarial Benefits	$ 0		$ 0	$ 0		$ 0
2. Other Actuarial Benefits						
A. FECA	$ 215,229		$ 0	$ 215,229		$ 214,433
B. Voluntary Separation Incentive Programs	0		0	0		0
C. DoD Education Benefits Fund	0		0	0		0
D. Total Other Actuarial Benefits	$ 215,229		$ 0	$ 215,229		$ 214,433
3. Other Federal Employment Benefits	$ 1,640		$ (1,640)	$ 0		$ 0
4. Total Military Retirement and Other Federal Employment Benefits:	$ 216,869		$ (1,640)	$ 215,229		$ 214,433

Standard Disclosures

Military Retirement Pensions

The portion of the military retirement benefits actuarial liability applicable to the United States Marine Corps General Fund (USMC GF) is reported on the financial statements of the Military Retirement Fund.

Military Retirement Health Benefits.

Health benefits are funded centrally at the Department of Defense (DoD) level. As such, the portion of the health benefits actuarial liability that is applicable to USMC GF is reported only on DoD Agency wide

Financial Statements and the Medicare-Eligible Retiree Health Care Fund Financial Statements.

Federal Employees Compensation Act (FECA)
Actuarial Cost Method Used and Assumptions: The USMC GF actuarial liability for workers' compensation benefits is developed by Department of Labor and provided to USMC GF at the end of each fiscal year. The future workers' compensation benefits include the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases, plus a component for incurred but not reported claims. The liability is determined using a method that utilizes historical benefit payment patterns related to a specific incurred period to predict the ultimate payments related to that period. Consistent with past practice, these projected annual benefit payments have been discounted to present value using the Office of Management and Budget's economic assumptions for 10 year U.S. Treasury notes and bonds. Interest rate assumptions utilized for discounting were as follows:

Fiscal Year 2007
4.930% in Year 1
5.078% in Year 2 and thereafter

To provide more specifically for the effects of inflation on the liability for future workers' compensation benefits, wage inflation factors (cost of living adjustments or COLAs) and medical inflation factors (consumer price index medical or CPIMs) were applied to the calculation of projected future benefits. The actual rates for these factors for the charge back year (CBY) 2007 were also used to adjust the methodology's historical payments to current year constant dollars.

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

CBY	COLA	CPIM
2007	2.63%	3.74%
2008	2.90%	4.04%
2009	2.47%	4.00%
2010	2.37%	3.94%
2011+	2.30%	3.94%

The model's resulting projections were analyzed to ensure that the estimates were reliable. The analysis was based on four tests: (1) a sensitivity analysis of the model to economic assumptions, (2) a comparison of the percentage change in the liability amount by agency to the percentage change in the actual incremental payments, (3) a comparison of the incremental paid losses per case (a measure of case severity) in CBY 2007 to the average pattern observed during the most current three charge back years, and (4) a comparison of the estimated liability per case in the 2007 projection to the average pattern for the projections of the most recent three years. The estimated actuarial liability is updated only at the end of each fiscal year. The change in actuarial liability for fiscal year 2007 is an increase of $796.2 thousand.

The estimate was allocated between USMC GF and Navy Working Capital Fund-Marine Corps based on the number of civilian employees from the Navy Budget Tracking System.

Other Federal Employment Benefits
Other federal employment benefits consist primarily of voluntary separation incentive pay for former employees.

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

As of September 30		2007		2006
(Amounts in Thousands)				
1. Intragovernmental Costs	$	6,192,075	$	5,829,850
2. Public Costs		18,667,042		14,666,789
3. Total Costs	$	24,859,117	$	20,496,639
4. Intragovernmental Earned Revenue	$	(457,705)	$	(304,356)
5. Public Earned Revenue		(189,363)		(110,342)
6. Total Earned Revenue	$	(647,068)	$	(414,698)
7. Net Cost of Operations	$	24,212,049	$	20,081,941

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

Public costs and revenues are exchange transactions made between the United States Marine Corps General Fund (USMC GF) and a nonfederal entity.

The USMC GF systems do not track intragovernmental transactions by customer at the transaction level. Therefore, internal DOD buyer-side balances are adjusted to agree with internal seller-side balances for revenue. Expenses were adjusted by reclassifying amounts between federal and nonfederal expenses.

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

The USMC GF accounting system meets accounting standards and records transactions based on the U.S. Standard General Ledger. The information presented is not based on budgetary obligations, disbursements, and collection transactions.

The USMC GF accounting system does not capture information relative to heritage assets separately and distinctly from normal operations. The USMC GF does not report any amounts for the costs of acquiring, constructing, improving, reconstructing, or renovating heritage assets (other than multi use heritage assets); nor costs for acquiring stewardship land and preparing stewardship for its intended use.

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

As of September 30	2007		2006	
	Cumulative Results of Operations	Unexpended Appropriations	Cumulative Results of Operations	Unexpended Appropriations
(Amounts in Thousands)				
1. Prior Period Adjustments Increases (Decreases) to Net Position Beginning Balance				
A. Changes in Accounting Standards	$ 0	$ 0	$ 0	$ 0
B. Errors and Omissions in Prior Year Accounting Reports	0	0	3,158,868	0
C. Total Prior Period Adjustments	$ 0	$ 0	$ 3,158,868	$ 0
2. Imputed Financing				
A. Civilian CSRS/FERS Retirement	$ 23,214	$ 0	$ 23,303	$ 0
B. Civilian Health	47,493	0	42,640	0
C. Civilian Life Insurance	157	0	141	0
D. Judgment Fund	461	0	1,157	0
E. IntraEntity	0	0	0	0
				0
F. Total Imputed Financing	$ 71,325	$ 0	$ 67,241	$ 0

Standard Disclosures
The difference of $134.0 thousand between appropriations received on the Statement of Budgetary Resources (SBR) and appropriations received on the Statement of Change of Net Position (SCNP) is the amount of special receipts from the United States Marine Corps General Fund (USMC GF) portion of the Wildlife Conservation on Military Reservations appropriation. This amount is included as appropriations received on the SBR, but not on the SCNP. Refer to Note 20 for additional details.

Note 20. Disclosures Related to the Statement of Budgetary Resources

As of September 30		2007		2006
(Amounts in Thousands)				
1. Net Amount of Budgetary Resources Obligated for Undelivered Orders at the End of the Period	$	12,430,461	$	10,014,842
2. Available Borrowing and Contract Authority at the End of the Period		0		0

Standard Disclosures

The United States Marine Corps General Fund (USMC GF) Report on Budget Execution accurately reflects $20.7 billion direct obligations in category A, amounts apportioned quarterly; $8.9 billion direct obligations in category B, amounts apportioned on a basis other than quarterly; and $613.5 million reimbursable obligations in category B.

The Statement of Budgetary Resources (SBR) reflects total direct obligations of $29.6 billion and $613.5 million in reimbursable obligations.

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

Appropriations Received on SBR does not agree with Appropriations Received on the Statement of Changes in Net Position (SCNP) because of differences between proprietary and budgetary accounting concepts and reporting concepts. The difference of $134.0 thousand is the amount of special receipts from USMC GF portion of the Wildlife Conservation on Military Reservations appropriation. This amount is included on the SBR, but not on SCNP.

Note 21. Reconciliation of Net Cost of Operations to Budget

As of September 30		2007		2006
(Amounts in Thousands)				
Resources Used to Finance Activities:				
Budgetary Resources Obligated:				
1. Obligations incurred	$	30,248,767	$	26,619,106
2. Less: Spending authority from offsetting collections and recoveries (-)		(2,361,164)		(2,040,452)
3. Obligations net of offsetting collections and recoveries	$	27,887,603	$	24,578,654
4. Less: Offsetting receipts (-)		20,195		3,296
5. Net obligations	$	27,907,798	$	24,581,950
Other Resources:				
6. Donations and forfeitures of property		0		0
7. Transfers in/out without reimbursement (+/-)		3,535		90,379
8. Imputed financing from costs absorbed by others		71,325		67,241
9. Other (+/-)		40,398		0
10. Net other resources used to finance activities	$	115,258	$	157,620
11. Total resources used to finance activities	$	28,023,056	$	24,739,570
Resources Used to Finance Items not Part of the Net Cost of Operations:				
12. Change in budgetary resources obligated for goods, services and benefits ordered but not yet provided:				
12a. Undelivered Orders (-)	$	(2,415,619)	$	(3,066,878)
12b. Unfilled Customer Orders		(71,500)		(47,838)
13. Resources that fund expenses recognized in prior Periods (-)		(33,592)		(27)
14. Budgetary offsetting collections and receipts that do not affect Net Cost of Operations		(20,194)		(3,296)
15. Resources that finance the acquisition of assets (-)		(2,068,268)		(2,875,425)
16. Other resources or adjustments to net obligated resources that do not affect Net Cost of Operations:				
16a. Less: Trust or Special Fund Receipts Related to exchange in the Entity's Budget (-)		0		0
16b. Other (+/-)		(43,934)		(90,379)
17. Total resources used to finance items not part of the Net Cost of Operations	$	(4,653,107)	$	(6,083,843)
18. Total resources used to finance the Net Cost of Operations	$	23,369,949	$	18,655,727

As of September 30		2007		2006
(Amounts in Thousands)				
Components of the Net Cost of Operations that will not Require or Generate Resources in the Current Period:				
Components Requiring or Generating Resources in Future Period:				
19. Increase in annual leave liability	$	8,003	$	0
20. Increase in environmental and disposal liability		0		226,470
21. Upward/Downward re-estimates of credit subsidy expense (+/-)		0		0
22. Increase in exchange revenue receivable from the public (-)		0		0
23. Other (+/-)		2,345		106,134
24. Total components of Net Cost of Operations that will Require or Generate Resources in future periods	$	10,348	$	332,604
Components not Requiring or Generating Resources:				
25. Depreciation and amortization	$	770,514	$	1,458,802
26. Revaluation of assets or liabilities (+/-)		26,298		(25,176)
27. Other (+/-)				
27a. Trust Fund Exchange Revenue		0		0
27b. Cost of Goods Sold		0		0
27c. Operating Materiel and Supplies Used		28,429		(338,188)
27d. Other		6,511		(1,828)
28. Total Components of Net Cost of Operations that will not Require or Generate Resources	$	831,752	$	1,093,610
29. Total components of Net Cost of Operations that will not Require or Generate Resources in the current period	$	842,100	$	1,426,214
30. Net Cost of Operations	$	24,212,049	$	20,081,941

Standard Disclosures

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

Obligations incurred
Less: Spending authority from offsetting collections and recoveries
Obligations Net of Offsetting Collections and Recoveries
Less: Offsetting Receipts
Net Obligations
Undelivered Orders
Unfilled Customer Orders

The SOF line, "Resources Used to Finance Activities, Other" is primarily comprised of a gain on real property and a loss on ammunition.

The SOF line, “Other Resources or Adjustments to Net Obligated Resources That Do Not Affect Net Cost of Operations, Other” is comprised of the transfer-in of donated fuel from Defense Logistics Agency (DLA) and the transfer-in of equipment from the Department of Air Force. In 1st Quarter, FY 2007, DLA received a donation of fuel from foreign countries with no requirement for reimbursement. The DLA then transferred a portion of the donated fuel to USMC GF.

The SOF line, “Components not Requiring or Generating Resources, Other” is primarily comprised of the bad debt expense for public accounts receivables.

The SOF line, “Components Requiring or Generating Resources Future Period, Other” is comprised of the year-to-date change in Federal Employee Compensation Act (FECA) actuarial liability, the year-to-date change in accrued FECA liability, year-to-date change in unemployment unfunded liability, accrual of a contingent liability for legal liabilities for 4th Quarter, FY 2007 and payables from cancelled years.

The SOF line, “Components Requiring or Generating Resources in Future Period” are costs not funded in the period the costs are incurred. The expense and the corresponding liability are recognized in the current period but the budgetary resource will not be provided until a subsequent period. In general, the changes in liabilities not covered by budgetary resources as shown on the Balance Sheet are reflected on the SOF. Differences are a result of $10.3 million in components of the net cost of operations that will require or generate resources in the future period, $33.6 million in resources that fund expenses recognized in prior periods, and $81 thousand in custodial liabilities covered by current unobligated budgetary resources.

Note 22. Disclosures Related to the Statement of Custodial Activity

Not applicable.

Note 23. Earmarked Funds

BALANCE SHEET As of September 30 *(Amounts in Thousands)*	MRF	MERHCF	Other Earmarked Funds	Eliminations	Total
ASSETS					
Fund balance with Treasury	$ 0	$ 0	$ 501	$ 0	$ 501
Investments	0	0	0	0	0
Accounts and Interest Receivable	0	0	0	0	0
Other Assets	0	0	0	0	0
Total Assets	$ 0	$ 0	$ 501	$ 0	$ 501
LIABILITIES and NET POSITION *As of September 30*					
Military Retirement Benefits and Other Employment Related Actuarial Liabilities	$ 0	$ 0	$ 0	$ 0	$ 0
Other Liabilities	0	0	26	0	26
Total Liabilities	$ 0	$ 0	$ 26	$ 0	$ 26
Unexpended Appropriations	0	0	0	0	0
Cumulative Results of Operations	0	0	475	0	475
Total Liabilities and Net Position	$ 0	$ 0	$ 501	$ 0	$ 501
STATEMENT OF NET COST *As of September 30*					
Program Costs	$ 0	$ 0	$ 42	$ 0	$ 42
Less Earned Revenue	0	0	0	0	0
Net Program Costs	$ 0	$ 0	$ 42	$ 0	$ 42
Less Earned Revenues Not Attributable to Programs	0	0	0	0	0
Net Cost of Operations	$ 0	$ 0	$ 42	$ 0	$ 42
STATEMENT OF CHANGES IN NET POSITION *As of September 30*					
Net Position Beginning of the Period	$ 0	$ 0	$ 383	$ 0	$ 383
Net Cost of Operations	0	0	42	0	42
Budgetary Financing Sources	0	0	134	0	134
Other Financing Sources	0	0	0	0	0
Change in Net Position	$ 0	$ 0	$ 92	$ 0	$ 92
Net Position End of Period	$ 0	$ 0	$ 475	$ 0	$ 475

Wildlife Conservation, Military Reservations, 16 USC 670
This fund provides for the development and conservation of fish and wildlife and recreational facilities on military installations. Proceeds from the sale of fishing and hunting permits are used for these programs at Navy and Marine Corps installations charging such user fees. These programs are carried out through cooperative plans agreed upon by the local representatives of the Secretary of Defense, the Secretary of the Interior, and the appropriate agency of the state in which the installation is located. During this reporting period, legislation regarding the purpose and use of the Wildlife Conservation, Military Reservation has not changed.

The nonexchange revenue in the amount of $134.0 thousand for 4th Quarter, FY 2007 is from the proceeds of the sale of fishing and hunting permits.

Note 24. Other Disclosures

Other Information
Currently, the United States Marine Corps General Fund (USMC GF) does not record or report operating leases; however, under its Financial Improvement Initiative program, USMC GF has began to implement a strategy to identify operating leases and to develop a process to report operating leases in the USMC GF financial statements. The development of our process is in its early stages, therefore, at this time, a completion date has not been established.

Note 25. Restatements

For FY 2007, the United States Marine Corps General Fund does not have any restatements.

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United States Marine Corps General Fund

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Investments in Research and Development
Yearly Investment in Research and Development
For Fiscal Years 2006 and 2007
($ in Millions)

Categories	FY07	FY06
Development		
Advanced Technology Development	$ 5	$ 36
Advanced Component Development and Prototypes	64	302
System Development and Demonstration	8	13
Research, Development, Test, and Evaluation Management Support	48	48
Operational Systems Development	359	284
Total	**$ 494**	**$ 683**

Narrative Statement:

Investments in Research and Development
Fiscal Year (FY) 2007 is the second year that the United States Marine Corps (USMC) General Fund (GF) is reporting as a separate entity and therefore only is reporting one comparative year for the Investment in Research and Development schedule. The USMC GF Research, Development, Test, and Evaluation (RDT&E) investments are all in Development; there are no basic and applied research investments. The values included in the table above are based on Development outlays (expenditures). Outlays are used because current USMC GF systems are unable to fully capture and summarize costs in accordance with standards promulgated by the Federal Accounting Standards Advisory Board.

Development
Development takes what has been discovered or learned from basic and applied research and uses it to establish technological feasibility, assessment of operability, and production capability. Development is comprised of five stages, as defined below.

1. Advanced Technology Development is the systematic use of the knowledge or understanding gained from research directed toward proof of technological feasibility and assessment of operational and production rather than the development of hardware for service use. It employs demonstration activities intended to prove or test a technology or method.

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

3. System Development and Demonstration concludes the program or project and prepares it for production. It consists primarily of preproduction efforts, such as logistics and repair studies. Major outputs are weapons systems finalized for complete operational and development testing.

4. RDT&E Management Support is support for installations and operations for general research and development use. This category includes costs associated with test ranges, military construction maintenance support for laboratories, operation and maintenance of test aircraft and ships, and studies and analyses in support of the Research and Development program.

5. Operational Systems Development is concerned with development projects in support of programs or upgrades that are still in engineering and manufacturing development. These projects have received approval for production, for which production funds have been budgeted in subsequent fiscal years.

The following are two representative program examples for the Development category.

United States Marine Corps Increases Efforts to Modernize Truck Fleets

The United States Marine Corps General Fund has several initiatives to restore and upgrade its aging and combat-battered fleets of tactical trucks from relatively lightweight Humvees to heavy-duty cargo haulers. One of the first initiatives, for which contracts have been awarded, involves conceptual designs for a family of Joint Light Tactical Vehicles (JLTV) that the Marines and the Army need to replace the thin-skinned, 20-year-old Humvee. The Humvee, more formally known as the High Mobility Multipurpose Wheeled Vehicle, is the agile, all terrain military truck that the Military Services chose in the mid-1980s to supplant the World War II-era jeep.

The JLTV will be designed with factory-built armor but will accommodate additional protection that can be installed and removed in the field as needed. Each of the variants will be equipped with a compatible trailer and able to tow up to 10,000 pounds both on roads and cross country. The JLTV is being developed separately from the Marine Corps planned Internally Transportable Vehicle (ITV) and the Reconnaissance, Surveillance, and Targeting Vehicle (RST-V).

The ITV, a second initiative and part of the new expeditionary fire support system, is intended to transport up to four Marines, mount heavy machine guns, and tow a 120 mm mortar. It is being designed to fit inside the CH-53 Sea Stallion heavy transport helicopter and the MV-22 Osprey tilt-rotor aircraft, which neither the Humvee nor the JLTV can do.

The Marines are testing the latest version of the RST-V at Aberdeen Proving Ground, Maryland. It has a mission similar to the reconnaissance variant of the JLTV, and like the ITV, it is to be transported in the Osprey. However, unlike the JLTV and the ITV, the RST-V is to be powered by a hybrid electric-drive system that will allow it to be propelled by diesel, batteries, or a combination of the two. The idea is for the RST-V to be able to operate frequently with a mixture of diesel, electric, and battery power in order to conserve fuel and, for brief periods, to function using only stored battery energy, enabling it to move stealthily behind enemy lines.

Another Marine Corps initiative is the upgrading of its heavier trucks. A seven-ton transport, known as the Medium Tactical Vehicle Replacement (MTVR), has replaced the former five ton M-809 and M-939 series trucks. The MTVR can negotiate terrain twice as rough as its predecessors, which were based on a pre-Korean war design. It has been designed to operate 70 percent off road and 30 percent on road, just the reverse of the five-ton models.

The MTVR can carry 7.1 tons of payload cross-country and 15 tons on pavement. It can carry cargo, personnel, bulk fuel, and virtually anything required on the battlefield. The MTVR can traverse grades of 60 percent and side slopes of 30 percent, and it can ford five feet of water. On primary and secondary roads, it can cruise at 65 mph. It has an aluminum cab that folds down under the hood to make it easier to ship.

The Logistics Vehicle System Replacement (LVSR) is another initiative to update the Marine Corps' fleet of tactical trucks. The LVSR is a trailer-pulling variant of the Logistics Vehicle System (LVS), which is two decades old. Like the LVS, the LVSR will be used primarily for moving large amounts of supplies, such as ammunition, fuel, water, and heavy equipment. It can carry 33,000 pounds of off-road payload, more than twice that of its predecessor.

The LVSR offers improved survivability. It is the first vehicle that the Marine Corps has required to have armor as part of its design. The vehicle will be built with mounting points and hardware for add-on armor to reduce the time required to increase protection when needed.

Heliplane and the XHawk
The Heliplane and the XHawk are two vertical takeoff and landing (VTOL) aircraft under development. Like the MV 22 Osprey, which the Marine Corps currently uses, the VTOL aircraft combine the vertical takeoff and landing capabilities of a helicopter. Both the Heliplane and the XHawk are based on concepts that originated decades ago, but technological breakthroughs and modern warfare requirements have spawned development.

The Heliplane, a proof of concept for combat search and rescue roles, has both helicopter style rotor blades that produce lift and fixed wing style turbofan engines that produce thrust. It is slower than an airplane but much faster than a helicopter. It can hover and take off and land vertically without a runway. It will be potentially easier to operate and less expensive to maintain than a helicopter. It will also be safer, having the capability to land in the event of a power failure.

The Heliplane builds upon the Fairey Rotodyne, an experimental aircraft with a similar rotor system that first flew in 1957 and reached a speed of 191 mph. The Heliplane will be designed to fly twice as fast as the Rotodyne. If the Heliplane is successful, it has the potential to revolutionize VTOL systems. Not every mission performed by a helicopter today can be performed better by a Heliplane, but many of today's helicopters, both military and commercial, could be replaced by Heliplanes.

The XHawk is based on fancraft technology, which incorporates an enclosed rotor or "fan" at both ends of the aircraft. Though the concept has been around for a half century, two principal technological breakthroughs have facilitated revival of the concept. Adaptable ducts permit high speed operations of up to 140 knots, and a vane control system provides lateral stability and control. One of the great innovations of this configuration is to place control vanes on the intake side of the duct. That innovation almost doubles the lateral control power of the vehicle. This semi autonomous automatic flight control system, or stabilization system, allows the pilot independent access to all six degrees of freedom. Developers are exploring the potential of adding wings that fold out from underneath the body of the aircraft in forward flight, thus offloading the main lift fans further. Such wings could potentially enable speeds of 160 to 180 knots.

Unlike conventional helicopters, which can be heard from long distances, the XHawk is expected to be relatively quiet, thereby improving survivability. Quiet operation coupled with a small footprint increase flexibility. Specifically, the XHawk will be able to fly alongside buildings and among other structures to assist in confronting insurgents.

NON-Federal PHYSICAL PROPERTY
The USMC GF does not fund this type of Activity.

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United States Marine Corps General Fund

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United States Marine Corps
General Property, Plant, and Equipment
Real Property Deferred Maintenance
For Fiscal Year Ended September 30, 2007
($ in Thousands)

Property Type	1. Plant Replacement Value	2. Required Work (Deferred Maintenance)	3. Percentage
Category 1: Buildings, Structures, and Utilities	$ 36,131,046	$ 1,065,134	2.95%
Category 2: Buildings, Structures, and Utilities	$ 1,046,487	$ -	0.00%
Category 3: Buildings, Structures, and Utilities (Heritage Assets)	$ 1,113,001	$ 32,811	2.95%

NOTE: The table above presents real property deferred maintenance data for both U.S. Marine Corps (USMC) General Fund and Navy Working Capital Fund-Marine Corps.

Narrative Statement:

1. The method used to assess facilities conditions is a facilities inspection, which categorizes buildings as Adequate, Substandard or Inadequate. Those ratings are converted to Q-ratings of 100%-90% Q1; 90%-80% Q2; 80%-60% Q3; and less than 60% Q4 by assessing facilities that are rated as Adequate and less than 25 years old as Q1; facilities that are over 25 years old and rated as Adequate as Q2; facilities rated as Substandard as Q3; and Inadequate facilities as Q4.

2. There is no change since this is the first submission.

3. The USMC follows the Office of the Secretary of Defense installation strategic plan goal of having facilities at a Q2 level on average as an acceptable rating. This represents an average level of 15% of Plant Replacement Value (PRV) as an acceptable level of deferred maintenance. The table above shows that USMC is approximately 2.95% of below PRV. The percentage for categories 1 and 3 facilities are the same because USMC cannot break out the deferred maintenance between those categories at this time. Category 2 is zero because USMC does not hold deferred maintenance backlogs on facilities to be demolished.

Facility Categories are as follows:

- Category 1: Buildings, Structures, and Utilities that are enduring and required to support an ongoing mission including multi-Heritage Assets.
- Category 2: Buildings, Structures, and Utilities that are excess to requirements or planned for replacement or disposal including multi-use Heritage Assets.
- Category 3: Buildings, Structures, and Utilities that are Heritage Assets.

Military Equipment
Deferred Maintenance Amounts
As of September 30, 2007
($ in Thousands)

Major Type	Amount
Missiles	$ 750
Combat Vehicles	359,725
Other Weapons Systems	82,937
Total	**$ 443,412**

Narrative Statement:

Missile Maintenance
Four categories are used to determine missile maintenance: missiles, tactical missiles, software maintenance, and other. Deferred maintenance is defined as the difference between the total weapon maintenance requirement as determined by requirements modeling processes and the weapon maintenance that is funded in accordance with the annual budget controls for the missile maintenance program. The maintenance requirements model projects the quantity of missiles and missile components per weapon system that are required to be maintained or reworked annually.

Combat Vehicles
The combat vehicles category refers to deferred vehicle maintenance for the active and reserve Marine Corps assets. The combat vehicle category consists of weapons systems, such as the M1A1 Tank, the Amphibious Assault Vehicle, the Hercules Recovery Vehicle, and the Light Armored Vehicle. The total requirement is the planned quantity of combat vehicles that require depot level maintenance in a year as determined by program managers and the operating forces with requirements validated by a modeling process. The deferred maintenance is the difference between the validated requirements and funding received for that fiscal year.

Other Weapons Systems
The Other Weapons Systems category is comprised of ordnance, end item maintenance for support equipment, camera equipment, landing aids, calibration equipment, air traffic control equipment, target systems, expeditionary airfield equipment, special weapons, target maintenance, and repair of repairable components. Three categories define ordnance maintenance: ordnance maintenance, software maintenance, and other. Although the various programs differ in the methodology in defining requirements, all programs define deferred maintenance as the difference between validated requirements and funding.

Heritage Assets
For Fiscal Year Ended September 30, 2007

	Measurement Quantity	As of Oct 1, 2006	Additions	Deletions	As of Sep 30, 2007
Museums	Each	6	-	(1)	5
Monuments and Memorials	Each	0	-	-	-
Cemeteries	Sites	0	-	-	-
Archeological Sites	Sites	0	-	-	-
Buildings and Structures	Each	0	-	-	-
Major Collections	See table, "*Major Collections*"				

Narrative Statement:

Fiscal Year (FY) 2007 is the second year that the USMC GF is reporting as a separate entity. The USMC GF is required to report Heritage Assets in accordance with the following public laws and regulations:

- Antiquities Act of 1906
- Historic Sites Act of 1935
- USC 470 National Historic Preservation Act of 1966
- National Environmental Policy Act of 1969
- American Indian Religious Freedom Act of 1978
- Archaeological Resources Protection Act of 1979
- Native American Graves Protection & Repatriation Act of 1990
- Presidential Memorandum for Heads of Executive Departments and Agencies: Government Relations with Native American Tribal Governments Act of 1994
- 36 CFR 79 – Curation of Federally Owned and Administered Archaeological Collections
- 36 CFR 60.4 – National Register of Historic Places
- Federal Accounting standards Advisory Board (FASAB) Standard 29, "Heritage Assets and Stewardship Land"
- Executive Order 13237 – Preserve America – of 2003
- Executive Order 13327 – Federal Real Property Asset Management – of 2004

Heritage Assets are defined as items that are unique for one or more of the following reasons: historical or natural significance; cultural, educational, or artistic importance; or significant architectural characteristics. Monetary values are not required for Heritage Asset reporting; only physical units of measure are reported.

<u>Process used to define assets as Heritage Assets</u>
The processes used to define items as having heritage significance vary among categories and type of assets being evaluated. Subject matter experts, including historians and curators, play a significant role in the definition process in addition to other criteria, such as a listing in the National Register of Historic Places. In all cases, a myriad of Federal statutes, service regulations, and other guidelines mandate heritage significance or provide guidance in its determination.

<u>Multi-Use Heritage Assets</u>. Per DoD FMR Volume 6B, "Form and Content of the Department of Defense Audited Financial Statements," Multi-Use Heritage Assets are reported both as Heritage Assets in the Required Supplementary Stewardship Information and on the Balance Sheet as Real Property.

<u>Information Pertaining to the Condition of USMC Heritage Assets</u>. The methodology used to report the condition of the heritage assets was a combination of a visual assessment of the objects, historic value to the USMC collection, and general display and storage standards for historic collections. The overall condition of the collection objects is good.

Museums
Museums are buildings, places, or institutions devoted to the acquisition, conservation, study, exhibition, and educational interpretation of objects having scientific, historical, or artistic value. Secretary of the Navy Instruction 5755.1A, “Navy Museums,” defines the scope of the Navy Museum program.

The FY 2006 ending balance for museums was overstated by one, due to the USMC museum at the Washington Navy Yard being reported in error. The museum was closed during FY 2006.

Supplemental Reporting
In addition to the data presented in the table, “Heritage Assets,” above, the following supplemental information on Major Collections was reported as of September 30, 2007:

Major Collections

Category	Measurement Quantity	As of Oct 1, 2006	Additions	Deletions	As of Sep 30, 2007
Archeological Artifacts	Cubic Feet	915	22.5	0	937.5
Archival	Linear Feet	25,726	617.74	453	25,890.74
Artwork	Item	8,946	158	0	9,104
Historical Artifacts	Item	53,432	767	9	54,190

STEWARDSHIP LAND
For Fiscal Year Ended September 30, 2007
(Acres in Thousands)

Land Use	As of Oct 1, 2006	Additions	Deletions	As of Sep 30, 2007
Mission	680	0	0	680
Parks and Historic Sites	0	0	0	0
Totals	**680**	**0**	**0**	**680**

Narrative Statement:
Per the DoD FMR, USMC GF Stewardship Land includes Public Domain, Land Set Aside, and Donated Land. Within the definition of Stewardship Land, land can be further categorized as Improved, Semi-Improved or Other.

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United States Marine Corps General Fund

Other Accompanying Information

Department of the Navy Subsidiary Financial Statements

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Appropriations, Funds, and Accounts Included in the Principal Statements

Entity Accounts

General Accounts

17 1001	Medicare Eligible Retiree Health Care Fund, Military Personnel Marine Corps
17 1003	Medicare Eligible Retiree Health Care Fund, Reserve Personnel Marine Corps
17 1105	Military Personnel, Marine Corps
17 1106	Operation and Maintenance, Marine Corps
17 1107	Operation and Maintenance, Marine Corps Reserve
17 1108	Reserve Personnel, Marine Corps
17 1109	Procurement, Marine Corps

Shared Appropriations (Appropriations from which US Marine Corps receives allocations)

17 0703	Family Housing, Navy and Marine Corps
17 1319	Research and Development, Test and Evaluation, Navy
17 1508	Procurement of Ammunition, Navy and Marine Corps

Shared Earmarked Funds

17X5095	Wildlife Conservation

Non-Entity Accounts

17X6026	Pay of the Marine Corps, Deposit Fund Receipts

Shared Non-Entity Accounts

17 3XXX	Receipt Accounts
17X6XXX	Deposit Funds

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Navy Working Capital Fund – Marine Corps

Principal Statements

Department of the Navy Subsidiary Financial Statements

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Limitations to the Financial Statements

The principal financial statements have been prepared to report the financial position and results of operations of the entity, pursuant to the requirements of 31 United States Code 3515 (b). While the statements have been prepared from the books and records of the entity in accordance with Generally Accepted Accounting Principles for Federal entities and 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.

In Fiscal Year (FY) 2006, the Office of the Under Secretary of Defense (Comptroller), with support from the Department of the Navy, designated the U.S. Marine Corps a financial reporting entity. This designation allowed the Marine Corps to prepare comprehensive subsidiary financial statements and related notes beginning in FY 2006.

The Marine Corps shares appropriations with the U.S. Navy and in addition maintains accountability for its own appropriations. The Marine Corps has specific funds and budget execution unto itself that are managed by Marine Corps program sponsors, maintained in a single core integrated Working Capital Fund accounting and budgeting reporting system, and supported by Marine Corps managerial accountants and the Defense Finance and Accounting Service-Kansas City. Given this fiduciary responsibility, the Marine Corps is able to fully comply with Statement of Federal Financial Accounting Concepts Number 2, *Entity and Display.*

Principal Statements

The FY 2007 Navy Working Capital Fund – Marine Corps Principal Statements and related notes are subsidiary financial statements and related notes of the Navy Working Capital Fund, and are presented in the format prescribed by the Department of Defense Financial Management Regulation 7000.14, Volume 6B. The statements and related notes summarize financial information for individual activity groups and activities within the Navy Working Capital Fund – Marine Corps for the fiscal year ending September 30, 2007, and are presented on a comparative basis with information previously reported for the fiscal year ending September 30, 2006.

The following statements comprise the Navy Working Capital Fund – Marine Corps Principal Statements:

- Consolidated Balance Sheet
- Consolidated Statement of Net Cost
- Consolidated Statement of Changes in Net Position
- Combined Statement of Budgetary Resources

The Principal Statements and related notes have been prepared to report financial position pursuant to the requirements of the Chief Financial Officers Act of 1990, as amended by the Government Management Reform Act of 1994. The accompanying notes should be considered an integral part of the Principal Statements.

Department of Defense
Navy Working Capital Fund - Marine Corps
CONSOLIDATED BALANCE SHEET
As of September 30, 2007 and 2006
($ in Thousands)

	2007 Consolidated	2006 Consolidated
ASSETS (Note 2)		
Intragovernmental:		
Fund Balance with Treasury (Note 3)		
Entity	$ 67,119	$ 30,193
Non-Entity Seized Iraqi Cash	0	0
Non-Entity - Other	0	0
Investments (Note 4)	0	0
Accounts Receivable (Note 5)	24,848	33,906
Other Assets (Note 6)	684	0
Total Intragovernmental Assets	92,651	64,099
Cash and Other Monetary Assets (Note 7)	0	0
Accounts Receivable, Net (Note 5)	74	327
Loans Receivable (Note 8)	0	0
Inventory and Related Property, Net (Note 9)	475,126	558,068
General Property, Plant and Equipment, Net (Note 10)	45,925	48,275
Investments (Note 4)	0	0
Other Assets (Note 6)	127	519
TOTAL ASSETS	613,903	671,288
LIABILITIES (Note 11)		
Intragovernmental:		
Accounts Payable (Note 12)	5,768	6,382
Debt (Note 13)	0	0
Other Liabilities (Note 15 & Note 16)	858	917
Total Intragovernmental Liabilities	6,626	7,299
Accounts Payable (Note 12)	79,541	67,846
Military Retirement and Other Federal Employment Benefits (Note 17)	27,624	29,595
Environmental and Disposal Liabilities (Note 14)	0	0
Loan Guarantee Liability (Note 8)	0	0
Other Liabilities (Note 15 & Note 16)	9,141	30,673
TOTAL LIABILITIES	122,932	135,413
NET POSITION		
Unexpended Appropriations - Earmarked Funds (Note 23)	0	0
Unexpended Appropriations - Other Funds	32,400	0
Cumulative Results of Operations - Earmarked Funds	0	0
Cumulative Results of Operations - Other Funds	458,571	535,875
TOTAL NET POSITION	490,971	535,875
TOTAL LIABILITIES AND NET POSITION	$ 613,903	$ 671,288

The accompanying notes are an integral part of the statements.

Department of Defense

Navy Working Capital Fund - Marine Corps

CONSOLIDATED STATEMENT OF NET COST

For the Years Ended September 30, 2007 and 2006

($ in Thousands)

	2007 Consolidated	2006 Consolidated
Program Costs		
Gross Costs	$ 665,405	$ 730,863
Less: Earned Revenue	(608,572)	(708,962)
Net Costs	56,833	21,901
Costs Not Assigned to Programs	0	0
Less: Earned Revenue Not Attributable to Programs	0	0
Net Cost of Operations	$ 56,833	$ 21,901

The accompanying notes are an integral part of the statements.

Department of Defense

Navy Working Capital Fund - Marine Corps

CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION

For the Years Ended September 30, 2007 and 2006

($ in Thousands)

	2007 Consolidated	2006 Consolidated
CUMULATIVE RESULTS OF OPERATIONS		
Beginning Balances	$ 535,875	$ 635,690
Prior Period Adjustments:		
Changes in accounting principles (+/-)	0	0
Correction of errors (+/-)	0	0
Beginning Balances, as adjusted	535,875	635,690
Budgetary Financing Sources:		
Other adjustments (rescissions, etc) (+/-)	0	0
Appropriations used	0	0
Nonexchange revenue	0	0
Donations and forfeitures of cash and cash equivalents	0	0
Transfers in/out without reimbursement (+/-)	63,393	0
Other budgetary financing sources (+/-)	0	0
Other Financing Sources:		
Donations and forfeitures of property	0	0
Transfers in/out without reimbursement (+/-)	0	(90,240)
Imputed financing from costs absorbed by others	12,325	12,327
Other (+/-)	(96,189)	0
Total Financing Sources	(20,471)	(77,913)
Net Cost of Operations (+/-)	56,833	21,901
Net Change	(77,304)	(99,814)
Cumulative Results of Operations	$ 458,571	$ 535,876
UNEXPENDED APPROPRIATIONS		
Beginning Balances	$ 0	$ 0
Prior Period Adjustments (+/-)		
Changes in accounting principles (+/-)	0	0
Correction of errors (+/-)	0	0
Beginning Balances, as adjusted	0	0
Budgetary Financing Sources:		
Appropriations received	32,400	0
Appropriations transferred-in/out (+/-)	0	0
Other adjustments (rescissions, etc) (+/-)	0	0
Appropriations used	0	0
Total Budgetary Financing Sources	32,400	0
Unexpended Appropriations	32,400	0
Net Position	$ 490,971	$ 0

The accompanying notes are an integral part of the statements.

Department of Defense
Navy Working Capital Fund - Marine Corps

COMBINED STATEMENT OF BUDGETARY RESOURCES

For the Years Ended September 30, 2007 and 2006
($ in Thousands)

	2007 Combined	2006 Combined
BUDGETARY FINANCING ACCOUNTS		
Budgetary Resources:		
Unobligated balance, brought forward, October 1	$ 177,371	$ 227,700
Recoveries of prior year unpaid obligations	0	0
Budget Authority:		
Appropriations received	32,400	0
Borrowing authority	0	0
Contract authority	(49,945)	16,540
Spending authority from offsetting collections:		
Earned		
Collected	626,041	621,225
Change in receivables from Federal sources	(21,618)	17,585
Change in unfilled customer orders		
Advances received	520	(110)
Without advance from Federal sources	(20,741)	(11,164)
Anticipated for rest of year, without advances	0	0
Previously unavailable	0	0
Expenditure Transfers from trust funds	0	0
Subtotal	566,657	644,076
Nonexpenditure Transfers, net, anticipated and actual	63,393	0
Temporarily not available pursuant to Public Law	0	0
Permanently not available	(32,400)	0
Total Budgetary Resources	775,021	871,776
Status of Budgetary Resources:		
Obligations incurred:		
Direct	0	0
Reimbursable	595,206	694,405
Subtotal	595,206	694,405
Unobligated balance:		
Apportioned	116,422	177,371
Exempt from apportionment	63,393	0
Subtotal	179,815	177,371
Unobligated balances not available	0	0
Total Status of Budgetary Resources	$ 775,021	$ 871,776

The accompanying notes are an integral part of the statements.

Department of Defense
Navy Working Capital Fund - Marine Corps

COMBINED STATEMENT OF BUDGETARY RESOURCES

For the Years Ended September 30, 2007 and 2006
($ in Thousands)

	2007 Combined	2006 Combined
RELATIONSHIP OF OBLIGATIONS TO OUTLAYS		
Change in Obligated Balance:		
Obligated balance, net		
Unpaid obligations, brought forward, October 1	$ 333,699	$ 292,725
Less: Uncollected customer payments from Federal sources, brought forward, October 1	(340,071)	(333,650)
Total Unpaid Obligated Balance	(6,372)	(40,925)
Obligations incurred, net (+/-)	595,206	694,405
Less: Gross outlays	(685,430)	(653,431)
Obligated balance transferred, net		
Actual transfers, unpaid obligations (+/-)	0	0
Actual transfers, uncollected customer payments from Federal sources (+/-)	0	0
Total Unpaid Obligated Balance Transferred, net	0	0
Less: Recoveries of prior year unpaid obligations, actual	0	0
Change in uncollected customer payments from Federal sources (+/-)	42,360	(6,421)
Obligated balance, net, end of period		
Unpaid obligations	243,475	333,699
Less: Uncollected customer payments from Federal sources	(297,712)	(340,071)
Total Unpaid Obligated Balance, net, end of period	(54,237)	(6,372)
Net Outlays:		
Gross Outlays	685,430	653,431
Less: Offsetting collections	(626,562)	(621,115)
Less: Distributed Offsetting receipts	0	0
Net Outlays	$ 58,868	$ 32,316

The accompanying notes are an integral part of the statements.

2007

Navy Working Capital Fund–MC

Notes to the Principal Statements

Department of the Navy Subsidiary Financial Statements

Note 1. Significant Accounting Policies

1.A. Basis of Presentation

These financial statements have been prepared to report the financial position and results of operations of the Navy Working Capital Fund-Marine Corps (NWCF-MC), as required by the "Chief Financial Officers Act of 1990," expanded by the "Government Management Reform Act of 1994," and other appropriate legislation. The financial statements have been prepared from the books and records of NWCF-MC in accordance with the "Department of Defense (DoD), Financial Management Regulation," the Office of Management and Budget (OMB) Circular A-136, Financial Reporting Requirements, and to the extent possible generally accepted accounting principles (GAAP). Effective 4th Quarter, Fiscal Year (FY) 2006, DoD no longer publishes consolidating/combining financial statements. The accompanying financial statements account for all resources for which NWCF-MC is responsible unless otherwise noted.

The NWCF-MC is unable to fully implement all elements of GAAP and OMB Circular A-136, due to limitations of its financial and nonfinancial management processes and systems that feed into the financial statements. The NWCF-MC derives its reported values and information for major asset and liability categories largely from nonfinancial systems, such as inventory systems and logistic systems. These systems were designed to support reporting requirements for maintaining accountability over assets and reporting the status of federal appropriations rather than preparing financial statements in accordance with GAAP. The DoD currently has several auditor identified financial statement material weaknesses. Of these, the Department of the Navy-NWCF (DON-NWCF) has the following material weaknesses: Fund Balance with Treasury, General Property, Plant, and Equipment, Inventory, and Accounts Payable. The NWCF-MC has no material weaknesses identified other than as part of DON-NWCF. However, NWCF-MC continues to implement business processes and system improvements addressing known limitations.

1.B. Mission of the Reporting Entity

The United States Marine Corps (USMC) was created on November 10, 1775 as an act of the 2nd Continental Congress. The overall mission of USMC is to defend advanced naval bases and to conduct such land operations as may be essential to the prosecution of a naval campaign. The NWCF-MC provides goods and quality products, responsive maintenance support services required to support mobilization, surge and reconstitution requirements to DON and other DoD customers to ensure the operating forces are equipped for war in accordance with mobilization plans. In addition, NWCF-MC supports other government and non-governmental customers.

1.C. Appropriations and Funds

The NWCF-MC receives its appropriations and funds as working capital (revolving) funds. The NWCF-MC uses these appropriations and funds to execute its missions and subsequently report on resource usage. Working capital funds (WCF) received funding to establish an initial corpus through an appropriation or a transfer of resources from existing appropriations or funds. The corpus finances operations and transactions that flow through the fund. The WCF resources the goods and services sold to customers on a reimbursable basis and maintains the corpus. Reimbursable receipts fund future operations and generally are available in their entirety for use without further congressional action. At various times, Congress provides additional appropriations to supplement the WCF as an infusion of cash when revenues are inadequate to cover costs within the corpus.

1.D. Basis of Accounting

For FY 2007, NWCF-MC financial management systems are unable to meet all of the requirements for full accrual accounting. Many of NWCF-MC's financial and nonfinancial feeder systems and processes were designed and implemented prior to the issuance of GAAP for federal agencies. These systems were not designed to collect and record financial information on the full accrual accounting basis as required by GAAP. The NWCF-MC and the Defense Finance and Accounting Service (DFAS) continue with the implementation of new accounting systems designed to produce both proprietary and budgetary reports and use the United States Standard General Ledger (USSGL). Until the implementation is completed, the amounts recorded are primarily proprietary.

The DoD has undertaken efforts to determine the actions required to bring its financial and nonfinancial feeder systems and processes into compliance with GAAP. One such action is the current revision of its accounting systems to record transactions based on USSGL. Until all of NWCF-MC's financial and nonfinancial feeder systems and processes are updated to collect and report financial information as required by GAAP, NWCF-MC financial data will be derived from transactions from nonfinancial feeder systems, and accruals made for major items such as payroll expenses, and accounts payable.

In addition, DoD identifies program costs based upon the major appropriation groups provided by the Congress. Current processes and systems do not capture and report accumulated costs for major programs based upon the performance measures as required by the Government Performance and Results Act. The DoD is working towards a cost reporting methodology that meets the need for cost information required by the Statement of Federal Financial Accounting Standards (SFFAS) No. 4, "Managerial Cost Accounting Concepts and Standards for the Federal Government."

1.E. Revenues and Other Financing Sources

Depot Maintenance WCF activities recognize revenue according to the percentage of completion method. Supply Management WCF activities recognize revenue from the sale of inventory items.

1.F. Recognition of Expenses

For financial reporting purposes, DoD policy requires the recognition of operating expenses in the period incurred. However, because NWCF-MC's financial and nonfinancial feeder systems were not designed to collect and record financial information on the full accrual accounting basis, accruals are made for major items such as payroll expenses, accounts payable, and unbilled revenue. In the case of Operating Materiels and Supplies (OM&S), operating expenses are generally recognized when the items are purchased. Efforts are underway to transition towards the consumption method for recognizing OM&S expenses.

1.G. Accounting for Intragovernmental Activities

Preparation of reliable financial statements requires the elimination of transactions occurring among entities within DoD or between two or more federal agencies. However, NWCF-MC cannot accurately eliminate intragovernmental transactions by customer because NWCF-MC's systems do not track at the transaction level. Generally, seller entities within DoD provide summary seller-side balances for revenue, accounts receivable, and unearned revenue to the buyer-side internal DoD accounting offices. In most cases, the buyer-side records are adjusted to agree with DoD seller-side balances. IntraDoD intragovernmental balances are then eliminated. The volume of intragovernmental transactions is so large that after-the-fact reconciliation cannot be accomplished effectively with existing or foreseeable resources. The DoD is developing long-term system improvements to ensure accurate intragovernmental information, to include sufficient up-front edits and controls eliminating the need for after-the-fact reconciliations.

The U.S. Treasury Financial Management Service is responsible for eliminating transactions between DoD and other federal agencies. The Treasury Financial Manual, Part 2 – Chapter 4700, "Agency Reporting Requirements for the Financial Report of the United States Government" and U.S. Treasury's "Federal Intra-governmental Transactions Accounting Policy Guide" provide guidance for reporting and reconciling intragovernmental balances. While NWCF-MC is unable to fully reconcile intragovernmental transactions with all federal partners, NWCF-MC is able to reconcile balances pertaining to investments in federal securities, borrowings from U.S. Treasury and the Federal Financing Bank, Federal Employees' Compensation Act transactions with the Department of Labor, and benefit program transactions with the Office of Personnel Management. The DoD's proportionate share of public debt and related expenses to the Federal Government are not included. The Federal Government does not apportion debt and its related costs to federal agencies. The DoD's financial statements, therefore, do not report any portion of the public debt or interest thereon, nor do the statements report the source of public financing whether from issuance of debt or tax revenues.

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

1.H. Transactions with Foreign Governments and International Organizations

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

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

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

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

1.J. Foreign Currency

Not applicable.

1.K. Accounts Receivable

As presented in the Balance Sheet, accounts receivable includes accounts, claims, and refunds receivable from other federal entities or from the public. Allowances for uncollectible accounts due from the public are based upon an estimate of uncollectible accounts receivable. This estimate is a percentage of the billed amount after the total project cost has been adjusted to reflect the advance deposit. The NWCF-MC requires an advance deposit from all public entities prior to the commencement of work. Therefore, an assumption is made that the amount of uncollectible accounts should be negligible. The DoD does not recognize an allowance for estimated uncollectible amounts from other federal agencies. Claims against other federal agencies are to be resolved between the agencies in accordance with dispute resolution procedures defined in the Intragovernmental Business Rules published in the Treasury Financial Manual at *http://www.fms.treas.gov/tfm/vol1/07-03.pdf*.

1.L. Direct Loans and Loan Guarantees

Not applicable.

1.M. Inventories and Related Property

The NWCF-MC values and reports its resale inventories at an approximation of historical cost using Latest Acquisition Cost (LAC) adjusted for holding gains and losses. The LAC method is used because legacy inventory systems were designed for materiel management rather than accounting. Although these systems provide visibility and accountability over inventory items, they do not maintain historical cost data necessary to comply with the SFFAS No. 3, "Accounting for Inventory and Related Property." Additionally, these systems cannot produce financial transactions using USSGL as required by the "Federal Financial Management Improvement Act of 1996 (P.L. 104-208)." By utilizing new systems development processes, NWCF-MC is continuing to transition the balance of the inventories to the moving average cost method. However, since the on-hand balances which transitioned were not, for the most part, baselined to auditable historical cost, the reported values remain non-compliant with SFFAS No. 3 and GAAP.

The NWCF-MC manages only military or government specific materiel under normal conditions. Materiel is a unique term that relates to military force management, and includes all items (including tanks, self-propelled weapons, etc., and related spares, repair parts, and support equipment, but excluding real property, installations, and utilities) necessary to equip, operate, maintain, and support military activities without distinction as to its application for administrative or combat purposes. Items commonly used in and available from the commercial sector are not managed in NWCF-MC materiel management activities. Operational cycles are irregular, and the military risks associated with stock-out positions have no commercial parallel. The NWCF-MC holds materiel based on military need and support for contingencies. Materiel held in reserve for future sale is included in inventories and related materiel property line item on the financial statements with a separate disclosure in the footnotes based on SFFAS No. 3 definitions.

Related property includes OM&S and stockpile materials. The OM&S, including munitions not held for sale, are valued at standard purchase price. The NWCF-MC uses both the consumption method and the purchase method of accounting for OM&S. Items that are centrally managed and stored, such as ammunition and engines, are generally recorded using the consumption method and are reported on the Balance Sheet as OM&S. When current systems cannot fully support the consumption method, NWCF-MC uses the purchase method. Under this method, materials and supplies are expensed when purchased. During FY 2007, NWCF-MC expensed significant amounts using the purchase method because the systems could not support the consumption method or management deemed that the item was in the hands of the end user. This is a material weakness for DoD and long-term system corrections are in process. Once the proper systems are in place, these items will be accounted for under the consumption method of accounting.

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

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

1.N. Investments
Not applicable.

1.O. General Property, Plant and Equipment
In FY 2006, DoD revised the real property capitalization threshold from $100 thousand to $20 thousand. The current $100 thousand capitalization threshold remains unchanged for the remaining General Property, Plant, and Equipment (PP&E) categories. Not all Military Departments have implemented this revised policy due to system and process limitations.

General PP&E assets are capitalized at historical acquisition cost plus capitalized improvements when an asset has a useful life of two or more years and the acquisition cost equals or exceeds DoD capitalization threshold of $100 thousand. The DoD also requires capitalization of improvement costs over DoD capitalization threshold of $100 thousand for General PP&E. The DoD depreciates all General PP&E, other than land, on a straight-line basis.

Prior to FY 1996, General PP&E was capitalized if it had an acquisition cost of $15 thousand, $25 thousand, and $50 thousand for FYs 1993, 1994, and 1995, respectively, and an estimated useful life of two or more years. General PP&E previously capitalized at amounts below $100 thousand were written off General Fund financial statements in FY 1998. No adjustment was made for WCF assets that remain capitalized and reported on WCF financial statements. For WCF activities, all General PP&E used in the performance of their mission is categorized as General PP&E, whether or not it meets the definition of any other General PP&E categories.

1.P. Advances and Prepayments
The DoD's policy is to record advances and prepayments in accordance with GAAP. As such, payments made in advance of the receipt of goods and services are reported as an asset on the Balance Sheet. The DoD's policy is to expense and/or properly classify assets when the related goods and services are received. Not all DoD entities have implemented this policy primarily due to system limitations.

1.Q. Leases
Not applicable.

1.R. Other Assets
Other assets include those assets, such as military and civil service employee pay advances, travel advances, and certain contract financing payments that are not reported elsewhere on NWCF-MC's Balance Sheet.

The NWCF-MC conducts business with commercial contractors under two primary types of contracts: fixed price and cost reimbursable. To alleviate the potential financial burden on the contractor that long-term contracts can cause, NWCF-MC may provide financing payments. Contract financing payments are defined in the Federal Acquisition Regulations, Part 32, as authorized disbursements of monies to a contractor prior to acceptance of supplies or services by the Government. Contract financing payments clauses are incorporated in the contract terms and conditions and may include advance payments, performance-based payments, commercial advance and interim payments, progress payments based on cost, and interim payments under certain cost-reimbursement contracts. Contract financing payments do not include invoice payments, payments for partial deliveries, lease and rental payments, or progress payments based on a percentage or stage of completion, which the Defense Federal Acquisition Regulation Supplement authorizes only for construction of real property. Progress payments for real property are reported as Construction in Progress. It is DoD policy to record certain contract financing payments as Other Assets.

1.S. Contingencies and Other Liabilities

The SFFAS No. 5, "Accounting for Liabilities of the Federal Government," as amended by SFFAS No. 12, "Recognition of Contingent Liabilities Arising from Litigation," defines a contingency as an existing condition, situation, or set of circumstances that involves an uncertainty as to possible gain or loss. The uncertainty will be resolved when one or more future events occur or fail to occur.

The NWCF-MC is unable to identify specify legal contingencies primarily due to uncertainties of litigation and difficulty identifying data and method of computation. During 1st Quarter, FY 2007, DON worked with the Office of General Counsel and the Office of the Under Secretary of Defense (Comptroller) to develop and implement a methodology to produce an estimate for Contingent Legal Liabilities. This methodology was able to recognize contingent legal liabilities at DON and corporate Marine Corps levels only; but not at NWCF-MC level.

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

1.T. Accrued Leave

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

1.U. Net Position

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

1.V. Treaties for Use of Foreign Bases

Not applicable.

1.W. Comparative Data

Not applicable.

1.X. Unexpended Obligations

The NWCF-MC obligates funds to provide goods and services for outstanding orders not yet delivered. The financial statements do not reflect this liability for payment for goods and services not yet delivered, unless title passes.

1.Y. Undistributed Disbursements and Collections

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

The DoD policy is to allocate supported undistributed disbursements and collections between federal and nonfederal categories based on the percentage distributed federal and nonfederal accounts payable and accounts receivable. Unsupported undistributed disbursements are recorded in accounts payable. Unsupported undistributed collections are recorded in other liabilities. The NWCF-MC does not follow this procedure. Unsupported collections are allocated to federal accounts receivable and unsupported disbursements to nonfederal accounts payable.

1.Z. Significant Events

Beginning 4th Quarter, FY 2007, DoD began presenting Statement of Financing (SOF) as a note in accordance with OMB Circular A-136. The SOF will no longer be considered a basic statement and is now referred to as "Reconciliation of Net Cost of Operations to Budget."

Note 2. Nonentity Assets

As of September 30	2007	2006
(Amounts in Thousands)		
1. Intragovernmental Assets		
A. Fund Balance with Treasury	$ 0	$ 0
B. Accounts Receivable	0	0
C. Total Intragovernmental Assets	$ 0	$ 0
2. Nonfederal Assets		
A. Cash and Other Monetary Assets	$ 0	$ 0
B. Accounts Receivable	0	0
C. Other Assets	0	0
D. Total Nonfederal Assets	$ 0	$ 0
3. Total Nonentity Assets	$ 0	$ 0
4. Total Entity Assets	$ 613,903	$ 671,288
5. Total Assets	$ 613,903	$ 671,288

Information Related to Nonentity Assets

The Navy Working Capital Fund-Marine Corps does not have nonentity assets.

Note 3. Fund Balance with Treasury

As of September 30	2007	2006
(Amounts in Thousands)		
1. Fund Balances		
A. Appropriated Funds	$ 0	$ 0
B. Revolving Funds	67,119	30,193
C. Trust Funds	0	0
D. Special Funds	0	0
E. Other Fund Types	0	0
F. Total Fund Balances	$ 67,119	$ 30,193
2. Fund Balances Per Treasury Versus Agency		
A. Fund Balance per Treasury	$ 67,119	$ 30,193
B. Fund Balance per United States Marine Corps (USMC)	67,119	30,193
3. Reconciling Amount	$ 0	$ 0

The Navy Working Capital Fund-Marine Corps (NWCF-MC) has no reconciling amount to report this period.

Status of Fund Balance with Treasury

As of September 30	2007	2006
(Amounts in Thousands)		
1. Unobligated Balance		
A. Available	$ 179,815	$ 177,371
B. Unavailable	0	0
2. Obligated Balance not yet Disbursed	$ 243,475	$ 333,699
3. Nonbudgetary FBWT	$ 0	$ 0
4. NonFBWT Budgetary Accounts	$ (356,172)	$ (1,572,615)
5. Total	$ 67,119	$ (1,061,545)

Standard Disclosures
The Status of Fund Balance with Treasury (FBWT) reflects the budgetary resources to support FBWT.

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

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

NonBudgetary FBWT includes entity and nonentity FBWT accounts which represent adjustments that do not have budgetary authority, such as unavailable receipt accounts or clearing accounts. There is no NonBudgetary FBWT reported this period.

NonFBWT Budgetary Accounts represent adjustments to budgetary accounts that do not affect FBWT. For NWCF-MC, NonFBWT budgetary accounts are comprised of contract authority for capital assets in depot maintenance and operating expenses in supply management, accounts receivable, and unfilled orders from customers. This category reduces the Status of FBWT.

Unobligated balances are segregated to show available and unavailable amounts in the note schedule. For this reporting period, there are no unobligated unavailable balances for NWCF-MC. Unobligated available balances are not restricted to future use and are not apportioned for current use.

Disclosures Related to Suspense/Budget Clearing Accounts

Information Related to Suspense/Budget Clearing Accounts
The NWCF-MC Suspense/Budget Clearing Accounts are being reported under United States Marine Corps-General Fund.

Disclosures Related to Problem Disbursements

As of September 30	2005	2006	2007	(Decrease)/ Increase from FY 2006 to 2007
(Amounts in Thousands)				
1. Total Problem Disbursements, Absolute Value				
A. Unmatched Disbursements (UMDs)	$ 5,719	$ 4,088	$ 1,316	$ (2,772)
B. Negative Unliquidated Obligations (NULO)	0	2	0	(2)
C. In-Transit Disbursements	(6,565)	6,346	11,431	5,085
2. Total	$ (846)	$ 10,436	$ 12,747	$ 2,311

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

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

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

In-transits
The In-transits represent the absolute value of disbursements and collections made by NWCF-MC disbursing activity on behalf of an accountable activity and have not been posted to the accounting system.

Other Disclosures
The NWCF-MC does not have any discrepancies between amounts reported in the problem disbursement metric furnished to DFAS Arlington and the Note 3 schedule. Beginning with 2nd Quarter, FY 2007, in-transit disbursements are reported as an absolute value as opposed to net amounts disclosed in prior years. This reporting change applies to amounts in the note schedule for both the current and comparative years.

Note 4. Investments and Related Interest

Not applicable.

Note 5. Accounts Receivable

As of September 30	2007			2006
	Gross Amount Due	Allowance For Estimated Uncollectibles	Accounts Receivable, Net	Accounts Receivable, Net
(Amounts in Thousands)				
1. Intragovernmental Receivables	$ 24,848	N/A	$ 24,848	$ 33,906
2. Nonfederal Receivables (From the Public)	$ 74	$ 0	$ 74	$ 327
3. Total Accounts Receivable	$ 24,922	$ 0	$ 24,922	$ 34,233

Aged Accounts Receivable

As of September 30	2007		2006	
	Intragovernmental	Nonfederal	Intragovernmental	Nonfederal
(Amounts in Thousands)				
CATEGORY				
Nondelinquent				
Current	$ 24,064	$ 83	$ 33,633	$ 320
Noncurrent	0	0	0	0
Delinquent				
1 to 30 days	$ 446	$ 0	$ 9	$ 0
31 to 60 days	342	(0)	322	(0)
61 to 90 days	394	0	254	0
91 to 180 days	976	0	131	2
181 days to 1 year	318	(9)	89	2
Greater than 1 year and less than or equal to 2 years	416	(0)	163	3
Greater than 2 years and less than or equal to 6 years	0	0	0	0
Greater than 6 years and less than or equal to 10 years	0	0	0	0
Greater than 10 years	0	0	0	0
Subtotal	$ 26,956	$ 74	$ 34,601	$ 327
Less Supported Undistributed Collections	(13,721)	0	0	0
Less Eliminations	11,613	0	(695)	0
Less Other	0	0	0	0
Total	$ 24,848	$ 74	$ 33,906	$ 327

Standard Disclosures
Current systems do not allow for the identification of the aging of any undistributed amounts. Aging information is not automatically generated and is not readily available in all feeder financial systems and must be manually reported.

A monthly aged accounts receivable report, which is manually produced by Defense Finance and Accounting Service (DFAS) and Navy Working Capital Fund-Marine Corps (NWCF-MC), is used to complete the various categories shown in the above chart. The bottom portion of the chart is derived from the accounting adjustments required in the preparation of the financial statements to account for trading partner reported data and to reconcile delinquent and nondelinquent data with the total accounts receivables recorded in NWCF-MC accounting records. To complete the chart, unallocated adjustments, if any, are made to the "other" line and DFAS will work with the various field sites to identify the correct category for this amount and subsequently post in the proper category as necessary.

The $11.6 million identified in the eliminations line in the chart represents the amount identified by Department of Defense (DoD) trading partners, including internal NWCF-MC accounting records as accounts payable to NWCF-MC Depot Maintenance Activity Group and Supply Management Activity Group accounts.

Other Disclosures
On an ongoing basis, NWCF-MC and DFAS utilize several processes, including automated DoD inventory management system inquiry as well as written and verbal communication tools to request payment of delinquent accounts receivables. After several collection attempts have been exhausted, the aged accounts receivable are written off as required. Information received as to why payment has not been made is directly related to either cash posture or data reconciliation requiring labor intensive processes to be completed by the sources of supply.

Note 6. Other Assets

As of September 30	2007	2006
(Amounts in Thousands)		
1. Intragovernmental Other Assets		
A. Advances and Prepayments	$ 684	$ 0
B. Other Assets	0	0
C. Total Intragovernmental Other Assets	$ 684	$ 0
2. Nonfederal Other Assets		
A. Outstanding Contract Financing Payments	$ 81	$ 501
B. Other Assets (With the Public)	46	18
C. Total Nonfederal Other Assets	$ 127	$ 519
3. Total Other Assets	$ 811	$ 519

Standard Disclosures
Contract terms and conditions for certain types of contract financing payments convey certain rights to the Navy Working Capital Fund-Marine Corps (NWCF-MC) that protect the contract work from state or local taxation, liens or attachment by the contractor's creditors, transfer of property, or disposition in bankruptcy; however, these rights should not be misconstrued to mean that ownership of the contractor's work has transferred to the Government. The Government does not have the right to take the work, except as provided in contract clauses related to termination or acceptance, and NWCF-MC is not obligated to make payment to the contractor until delivery and acceptance.

The Contract Financing Payment balance of $81.0 thousand is the estimated future payments that will be paid to the contractor upon future delivery and Government acceptance of a satisfactory product. (See additional discussion in Note 15, Other Liabilities).

<u>Composition of Other Assets (With the Public)</u>
The composition of Other Assets (With the Public) includes travel advances. This represents the value of unliquidated advances of funds made to civilian employees for the payment of meals and incidental expenses, mileage, other expenses, and relocation expenses for official government travel.

Note 7. Cash and Other Monetary Assets

Not applicable.

Note 8. Direct Loan and/or Loan Guarantee Programs

Not applicable.

Note 9. Inventory and Related Property

As of September 30	2007	2006
(Amounts in Thousands)		
1. Inventory, Net	$ 318,682	$ 431,512
2. Operating Materiel & Supplies, Net	156,444	126,556
3. Stockpile Materiel, Net	0	0
4. Total	$ 475,126	$ 558,068

Inventory, Net

As of September 30	2007			2006	
	Inventory, Gross Value	Revaluation Allowance	Inventory, Net	Inventory, Net	Valuation Method
(Amounts in Thousands)					
1. Inventory Categories					
A. Available and Purchased for Resale	$ 413,928	$ (330,162)	$ 83,766	$ 236,253	LAC, MAC
B. Held for Repair	234,792	0	234,792	194,387	LAC, MAC
C. Excess, Obsolete, and Unserviceable	0	0	0	0	NRV
D. Raw Materiel	0	0	0	0	MAC, SP, LAC
E. Work in Process	124	0	124	872	AC
F. Total	$ 648,844	$ (330,162)	$ 318,682	$ 431,512	

Legend for Valuation Methods:

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

Standard Disclosures

Restrictions of Inventory Use, Sale, or Disposition

Generally, there are no restrictions with regard to the use, sale, or disposition of inventory to applicable Department of Defense (DoD) activities and personnel. Other than specified safety and war reserve levels, established as a result of DoD and Marine Corps (MC) regulatory operations, inventory may be sold to foreign countries, state and local governments, private parties and contractors in accordance with DoD and MC policies and guidance or at the direction of the President.

Composition of Inventory
Except for the work in process, all inventory categories shown in the table above apply to the Supply Management Activities.

Inventory Categories
Inventory represents property that is held for (a) sale to customers, (b) in the process of supporting production for eventual sale to customers, (c) to be consumed in the production of goods for sale, or (d) in the provision of providing services for a fee.

Inventory Available and Purchased for Resale includes consumable spare and repair parts and repairable items owned and managed by Navy Working Capital Fund-Marine Corps (NWCF-MC) as well as consumable and repairable items that are managed by other Military Services, such as the Defense Logistics Agency or the General Services Administration where the Marine Corps has permission to stock, store and sale. Materiel available and purchased for resale includes materiel held, due to various managerial decisions to support military or national contingencies.

Included in “Inventory Available and Purchased for Resale,” is an amount of $80.2 million for War Reserve Material for Supply Management, Marine Corps.

Federal Accounting Standards requires disclosure of the amount of Inventory Held for “Future Sale.” The NWCF-MC currently has no Inventory included in this reporting period, which is being held for future sale. All inventory, included in Inventory Net through 4th Quarter, FY 2007 is currently planned for sale to customers or retained for military or national contingencies. There is no management or valuation difference between the two categories.

Inventory Held for Repair is inventory that is in less than “ready for issue/sale” condition and requires repair to make suitable for sale. Some of the inventory items are more economical to repair than to procure. For warfighting readiness, since many weapon systems and machinery are no longer in commercial production, this leaves relatively no ready and economical sources of replenishment via new purchase. The MC supports its customers’ requests for purchase of certain items by repairing or rebuilding these items vice new acquisitions. The repair/rebuild process is an essential part of the Marine Corps’ commitment as a “Force in Readiness” as well as supporting our other DoD customers in maintaining a ready, mobile, and armed military force.

Work in Process balances include costs related to the production or servicing of items, including direct materiel, direct labor, applied overhead and other direct costs. Work in Process also includes the value of finished products or completed services pending billing to the customer. Work in Process designation may also be used to accumulate the amount paid to a contractor under cost reimbursable contracts, including the amount withheld from payment to ensure performance, and the amount paid to other Government plants for accrued costs of end items of materiel ordered but not delivered.

Inventory Work in Process
Work in Process at MC Depot Maintenance activities is $124.0 thousand and is included as inventory. This amount represents work that has been completed, expenses incurred, and waiting to be billed to the customer.

Operating Materiel and Supplies, Net

As of September 30	2007			2006	
	OM&S Gross Value	Revaluation Allowance	OM&S, Net	OM&S, Net	Valuation Method
(Amounts in Thousands)					
1. OM&S Categories					
A. Held for Use	$ 156,444	$ 0	$ 156,444	$ 126,556	SP, LAC
B. Held for Repair	0	0	0	0	SP, LAC
C. Excess, Obsolete, and Unserviceable	0	0	0	0	NRV
D. Total	$ 156,444	$ 0	$ 156,444	$ 126,556	

Legend for Valuation Methods:

Adjusted LAC = Latest Acquisition Cost, adjusted for holding gains and losses
NRV = Net Realizable Value
SP = Standard Price

Standard Disclosures

Restrictions on OM&S

Generally, there are no restrictions with regard to the use, sale, or disposition of OM&S applicable to DoD activities.

Composition of Operating Materiels and Supplies (OM&S)

OM&S Held for Use represents property that is consumed during normal operations and includes consumable spare and repair parts for use on customer work by various activities. The items are recorded using different methodologies including actual, weighted-average and historical cost.

Federal Accounting Standards requires disclosure of the amount of OM&S Held for "Future Use." The NWCF-MC reports that $156.4 million of OM&S is categorized as Held for Future Use. All OM&S categories shown in the table above apply to the Depot Maintenance Activity Group, Marine Corps only.

Government Furnished Materiel (GFM) and Contractor Acquired Materiel (CAM)

Generally, the values of the NWCF-MC's GFM and CAM in the hands of contractors are not included in the OM&S values reported above. The DoD is presently reviewing its process for reporting these amounts in an effort to determine the appropriate accounting treatment and the best method to annually collect and report required information without duplicating information already in other existing logistics systems in accordance with Volume 6B, Chapter 10 of DoD Financial Management Regulation.

Stockpile Materiel, Net

Not applicable.

Note 10. General PP&E, Net

As of September 30	2007					2006
	Depreciation/ Amortization Method	Service Life	Acquisition Value	(Accumulated Depreciation/ Amortization)	Net Book Value	Prior FY Net Book Value
(Amounts in Thousands)						
1. Major Asset Classes						
A. Land	N/A	N/A	$ 0	N/A	$ 0	$ 0
B. Buildings, Structures, and Facilities		20 or 40	71,843	$ (41,770)	30,073	31,532
C. Leasehold Improvements	S/L	lease term	0	0	0	0
D. Software	S/L	2-5 or 10	0	0	0	0
E. General Equipment	S/L	5 or 10	69,813	(58,120)	11,693	11,146
F. Military Equipment	S/L	Various	0	0	0	0
G. Assets Under Capital Lease	S/L	lease term	0	0	0	0
H. Construction- in- Progress	N/A	N/A	4,159	N/A	4,159	5,597
I. Other			0	0	0	0
J. Total General PP&E			$ 145,815	$ (99,890)	$ 45,925	$ 48,275

Legend for Valuation Methods:

S/L = Straight Line

N/A = Not Applicable

Standard Disclosures

Military Equipment

Military equipment is reported on the financial statements of the United States Marine Corps General Fund (USMC GF).

Heritage Assets and Stewardship Land

Heritage assets and stewardship land are reported on the financial statements of USMC GF.

Other Disclosures

Generally, for Navy Working Capital Fund-Marine Corps (NWCF-MC), there are no restrictions on General Property, Plant and Equipment (PP&E).

Assets Under Capital Lease

Not applicable.

Note 11. Liabilities Not Covered by Budgetary Resources

As of September 30	2007	2006
(Amounts in Thousands)		
1. Intragovernmental Liabilities		
A. Accounts Payable	$ 0	$ 0
B. Debt	0	0
C. Other	0	0
D. Total Intragovernmental Liabilities	$ 0	$ 0
2. Nonfederal Liabilities		
A. Accounts Payable	$ 0	$ 0
B. Military Retirement Benefits and Other Employment-Related Actuarial Liabilities	27,624	29,595
C. Environmental Liabilities	0	0
D. Other Liabilities	0	0
E. Total Nonfederal Liabilities	$ 27,624	$ 29,595
3. Total Liabilities Not Covered by Budgetary Resources	$ 27,624	$ 29,595
4. Total Liabilities Covered by Budgetary Resources	$ 95,308	$ 105,818
5. Total Liabilities	$ 122,932	$ 135,413

Standard Disclosures
Liabilities Not Covered by Budgetary Resources are liabilities for which congressional action is needed before budgetary resources can be provided.

<u>Composition of Intragovernmental Other Liabilities</u>
Intragovernmental Other Liabilities is made up of interest, penalties, and administrative fees owed to the U.S. Treasury for services of the Debt Management Office to handle and recover delinquent accounts receivable from public customers.

<u>Other Disclosures Related to Liabilities Not Covered by Budgetary Resources</u>
The $27.6 million included for Military Retirement Benefits and Other Federal Employment Benefits are related to the Department of Labor's Office of Inspector General estimated liability for future Navy Working Capital Fund-Marine Corps workers' compensation benefits. This liability is recorded as actuarial since it is based on guidelines issued by the Office of Management and Budget and represents estimated values, which may or may not materialize.

Military Retirement and Other Federal Employment Benefits not covered by budgetary resources are comprised of various employee actuarial liabilities not due and payable during the current fiscal year. This liability is primarily comprised of $27.6 million, which represent the benefits described. Refer to Note 17, Military Retirement and Other Federal Employment Benefits, for additional details and disclosures.

Note 12. Accounts Payable

As of September 30	2007 Accounts Payable	2007 Interest, Penalties, and Administrative Fees	2007 Total	2006 Total
(Amounts in Thousands)				
1. Intragovernmental Payables	$ 5,768	$ N/A	$ 5,768	$ 6,382
2. Nonfederal Payables (to the Public)	79,541	0	79,541	67,846
3. Total	$ 85,309	$ 0	$ 85,309	$ 74,228

Standard Disclosures

The Navy Working Capital Fund-Marine Corps' systems do not track intragovernmental transactions by customer at the transaction level. Therefore, internal Department of Defense buyer-side balances are adjusted to agree with internal seller-side balances for revenue, accounts receivable, and unearned revenue. Accounts payable were adjusted by reclassifying amounts between federal and nonfederal accounts payable.

Note 13. Debt

Not applicable.

Note 14. Environmental Liabilities and Disposal Liabilities

Standard Disclosures

Environmental Liabilities are reported under the United States Marine Corps General Fund.

Environmental Disclosures

Not applicable.

Note 15. Other Liabilities

As of September 30	2007 Current Liability	2007 Noncurrent Liability	2007 Total	2006 Total
(Amounts in Thousands)				
1. Intragovernmental				
A. Advances from Others	$ 0	$ 0	$ 0	$ 0
B. Deposit Funds and Suspense Account Liabilities	0			0
C. Disbursing Officer Cash	0	0	0	0
D. Judgment Fund Liabilities	0	0	0	0
E. FECA Reimbursement to the Department of Labor	0	0	0	0
F. Other Liabilities	858	0	858	917
G. Total Intragovernmental Other Liabilities	$ 858	$ 0	$ 858	$ 917
2. Nonfederal				
A. Accrued Funded Payroll and Benefits	$ 8,720	$ 0	$ 8,720	$ 10,236
B. Advances from Others	555	0	555	35
C. Deferred Credits	0	0	0	0
D. Deposit Funds and Suspense Accounts	0	0	0	0
E. Temporary Early Retirement Authority	0	0	0	0
F. Nonenvironmental Disposal Liabilities	0	0	0	
(1) Military Equipment (Nonnuclear)	0	0	0	0
(2) Excess/Obsolete Structures	0	0	0	0
(3) Conventional Munitions Disposal	0	0	0	0
G. Accrued Unfunded Annual Leave	0	0	0	0
H. Capital Lease Liability	0	0	0	0
I. Other Liabilities	0	(134)	(134)	20,402
J. Total Nonfederal Other Liabilities	$ 9,275	$ (134)	$ 9,141	$ 30,673
3. Total Other Liabilities	$ 10,133	$ (134)	$ 9,999	$ 31,590

Standard Disclosures

Composition of Intragovernmental Other Liabilities (Line 1.F)

Intragovernmental other liabilities include amounts presented in Navy Working Capital Fund-Marine Corps (NWCF-MC) balance sheet. A breakout of the major components of intragovernmental other liabilities are as follows:

a. Liabilities for Health and Life Insurance, Retirement and other employee benefits and entitlements representing government contributions.

b. Liabilities owed to the United States Treasury, Debt Management Office for interest, penalties, and administrative fees related to services for collection of accounts receivable from public customers.

Composition of Nonfederal Other Liabilities (Line 2.I)

Nonfederal other liabilities include amounts that are significant portions of the total liabilities presented in NWCF-MC balance sheet. A breakout of the major components of nonfederal other liabilities are as follows:

a. Accrued cost for travel advances, base support, and contracts for work performed by civilian personnel, contractors and other agencies in which a request for payment has not been received.

b. Estimated future payments for contract financing balances payments that will be paid to contractors upon future delivery and government acceptance of a satisfactory product.

Disclosures Related to Other Liabilities

Contingent Liabilities includes $81.0 thousand in estimated future contract financing payments that will be paid to the contractors upon delivery and Government acceptance. In accordance with contract terms, specific rights to the contractor's work vests with the Government when a specific type of contract financing payments is made. This action protects taxpayer funds in the event of contract nonperformance. These rights should not be misconstrued as the rights of ownership. The NWCF-MC is under no obligation to pay the contractor for amounts greater than the amounts authorized in the contract until delivery and Government acceptance. Because it is probable that the contractor will complete its efforts and deliver a satisfactory product to NWCF-MC and the amount of potential future payments is estimable; NWCF-MC has recognized a contingent liability for estimated future payments, which are conditional pending delivery and Government acceptance.

Abnormalities Related to Other Liabilities

Other Liabilities has an abnormal balance in the amount of $134.0 thousand. This is due to the net effect of a $215.0 thousand debit posting to contract holdbacks and a $81.0 thousand credit posting to contingent liabilities resulting from data calls generated by Mechanization of Contract Administration Services (MOCAS) processes. The abnormal balance was created by the debit posting, in the month of September 2007, which was identified as a Department of the Navy (DON) contract with a private entity. The contract included multiple contract line item numbers as well as multiple Marine Corps and DON appropriations. Based on current reviews, the debit posting appear to be erroneously identified for NWCF-MC, Supply Management Activity Group appropriations and not recorded as a liability prior to MOCAS debit posting. The Marine Corps is currently working with the Defense Contract Management Agency and Defense Finance and Accounting Service to identify the correct line of appropriations for proper posting and expects to resolve this issue.

Capital Lease Liability

Not applicable.

Note 16. Commitments and Contingencies

Standard Disclosures

The Navy Working Capital Fund-Marine Corps (NWCF-MC) is a party in various administrative proceedings and legal actions, with claims including equal opportunity matters, and contractual bid protests. The NWCF-MC is not aware of any contingent liabilities for legal actions. However, primarily due to uncertainties of litigation, difficulty identifying data and method of computation, NWCF-MC is unable to identify specific legal contingencies. During 1st Quarter, Fiscal Year (FY) 2007, the Department of the Navy (DON) worked with the Office of General Counsel and the Office of the Under Secretary of Defense (Comptroller) to develop and implement a methodology to produce an estimate for contingent legal liabilities. This methodology was able to recognize contingent legal liabilities at DON and United States Marine Corps General Fund levels only; but not at NWCF-MC level. As such, legal contingencies for MC are identified in the General Fund's financial records. The MC will continue to work to identify a methodology to identify legal contingencies, if any, at the various reporting entity level but has difficulty to anticipate the timeframe of implementation.

The NWCF-MC does not have obligations related to cancelled appropriations for which a contractual commitment for payment exists. In addition, NWCF-MC is not involved in any legal action or claims where DON Office of General Counsel considers an adverse decision is probable and the amount of loss measurable.

The NWCF-MC has contractual arrangements (i.e. undelivered orders) which may require financial obligations based on contractor claims under the "disputes" clause contained in contracts. As of the end of the 4th Quarter, FY 2007, undelivered orders are estimated at $161 million.

The NWCF-MC has contingencies that are considered both measurable and probable have been recognized as liabilities. Refer to Note 15 for further details.

The NWCF-MC is a party in numerous individual contracts that contain clauses, such as price escalation, award fee payments of dispute resolution that may or may not result in a future outflow of expenditures. Currently, NWCF-MC does not have a systemic process by which it captures or assesses these potential contingent liabilities; therefore, the amounts reported may not fairly present NWCF-MC contingent liabilities.

Note 17. Military Retirement and Other Federal Employment Benefits

As of September 30	2007								2006	
	Present Value of Benefits		Assumed Interest Rate (%)	(Less: Assets Available to Pay Benefits)		Unfunded Liability			Present Value of Benefits	
(Amounts in Thousands)										
1. Pension and Health Actuarial Benefits										
A. Military Retirement Pensions	$	0		$	0	$	0		$	0
B. Military Retirement Health Benefits		0			0		0			0
C. Military Medicare-Eligible Retiree Benefits		0			0		0			0
D. Total Pension and Health Actuarial Benefits	$	0		$	0	$	0		$	0
2. Other Actuarial Benefits										
A. FECA	$	27,624		$	0	$	27,624		$	29,595
B. Voluntary Separation Incentive Programs		0					0			0
C. DoD Education Benefits Fund		0			0		0			0
D. Total Other Actuarial Benefits	$	27,624		$	0	$	27,624		$	29,595
3. Other Federal Employment Benefits	$	0		$	0	$	0		$	0
4. Total Military Retirement and Other Federal Employment Benefits:	$	27,624		$	0	$	27,624		$	29,595

Standard Disclosures

Actuarial Cost Method Used

The Department of the Navy (DON) actuarial liability for workers' compensation benefits is developed by the Department of Labor and provided to DON at the end of each fiscal year. The liability is distributed between the Navy Working Capital Fund (NWCF) and General Fund for DON and the Marine Corps, which is based upon the number of civilian employees funded in each entity, as reported in the Navy Budget Tracking System. The liability 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 to predict the ultimate payments. The NWCF-MC's estimated actuarial liability is updated only at the end of each fiscal year.

The projected annual benefit payments are discounted to the present value using Office of Management and Budget's economic assumptions for ten year United States Treasury notes and bonds. Cost-of-living adjustments and medical inflation factors are also applied to the calculation of projected future benefits. The interest rate assumptions used in the discount calculations are as follows for September 30, 2007:

2007
4.930% in Year 1
5.078% in Year 2 and thereafter

To provide more specifically for the effects of inflation on the liability for future workers' compensations benefits, wage inflation factors (cost of living adjustments or COLAs) and medical inflation factors (consumer price index medical or CPIMs) were applied to the calculation of projected future benefits. The actual rates for these factors for the charge back year (CBY) 2007 were also used to adjust the methodology's historical payments to current year constant dollars.

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

CBY	COLA	CPIM
2007	2.63%	3.74%
2008	2.90%	4.04%
2009	2.47%	4.00%
2010	2.37%	3.94%
2011+	2.30%	3.94%

The model's resulting projections were analyzed to ensure that the estimates were reliable. The analysis was based on four tests:

(1) a sensitivity analysis of the model to economic assumptions,

(2) a comparison of the percentage change in the liability amount by agency to the percentage change in the actual incremental payments,

(3) a comparison of the incremental paid losses per case (a measure of case-severity) in CBY 2007 to the average pattern observed during the most current three charge back years,

(4) a comparison of the estimated liability per case in the 2007 projection to the average pattern for the projections of the most recent three years.

Other Disclosures Related to Liabilities Not Covered by Budgetary Resources
The $27.6 million included in Military Retirement Benefits and Other Federal Employment Benefits are related to entitlements outlined in the Federal Employee Compensation Act liabilities.

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

As of September 30		2007		2006
(Amounts in Thousands)				
1. Intragovernmental Costs	$	264,758	$	255,735
2. Public Costs		400,647		475,129
3. Total Costs	$	665,405	$	730,864
4. Intragovernmental Earned Revenue	$	(595,965)	$	(617,997)
5. Public Earned Revenue		(12,607)		(90,965)
6. Total Earned Revenue	$	(608,572)	$	(708,962)
7. Net Cost of Operations	$	56,833	$	21,902

Standard Disclosures
<u>Composition of Statement of Net Cost</u>
The Navy Working Capital Fund-Marine Corps (NWCF-MC) generally records transactions on an accrual basis as required by federal generally accepted accounting principles (GAAP). Information presented on the statement of net cost represents the net result of post-closing adjustments and eliminating entries made in compiling and consolidating NWCF-MC financial statements. These entries significantly affected the reported amounts of intragovernmental program cost, program cost with the public, earned revenue and net program cost. The post-closing adjustments were made in order to increase or decrease certain NWCF-MC account balances reported as of September 30, 2007 to ensure agreement with related balances reported by other Department of Defense (DoD) and other federal reporting entities. Eliminating entries are required adjustments made as part of the financial process. This process enables the matching of trading partner data recorded at each financial statement consolidation level: NWCF, DoD, and Federal Government levels.

Other Disclosures Related to the Statement of Net Cost
Statement of Net Cost is unique because its principles are driven by an understanding of net cost of programs and/or organizations that the Federal Government supports through appropriations or other means. This statement provides gross and net cost information that can be related to the amount of output or outcome for a given program and/or organization administered by a responsible reporting entity.

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

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

The NWCF-MC's systems do not track intragovernmental transactions by customer at the transaction level. Therefore, internal DoD buyer-side balances are adjusted to agree with internal seller-side balances for revenue. Expenses were adjusted by reclassifying amounts between federal and nonfederal expenses or accruing additional accounts payable and expenses.

The NWCF-MC does not report any heritage assets or stewardship land, as these entities are reported on the financial statements of the Department of the Navy General Fund.

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

As of September 30	2007		2006	
	Cumulative Results of Operations	Unexpended Appropriations	Cumulative Results of Operations	Unexpended Appropriations
(Amounts in Thousands)				
1. Prior Period Adjustments Increases (Decreases) to Net Position Beginning Balance				
A. Changes in Accounting Standards	$ 0	$ 0	$ 0	$ 0
B. Errors and Omissions in Prior Year Accounting Reports	0	0	0	0
C. Total Prior Period Adjustments	$ 0	$ 0	$ 0	$ 0
2. Imputed Financing				
A. Civilian CSRS/FERS Retirement	$ 2,957	$ 0	$ 3,426	$ 0
B. Civilian Health	9,347	0	8,879	0
C. Civilian Life Insurance	21	0	22	0
D. Judgment Fund		0	0	0
E. IntraEntity		0	0	0
F. Total Imputed Financing	$ 12,325	$ 0	$ 12,327	$ 0

Standard Disclosures
The eliminations column on the Statement of Net Position (SCNP) reflect zero dollars. In the SCNP, all offsetting balances (i.e. transfers-in and transfers out, revenues, and expenses) for intra-Department of Defense activity between other (nonearmarked) funds are reported on the same lines. This results in an eliminations column, which appears to contain no balance. In reality, the column contains all appropriate elimination entries, but all net to zero within each respective line, except for intraentity imputed financing costs.

Note 20. Disclosures Related to the Statement of Budgetary Resources

As of September 30	2007	2006
(Amounts in Thousands)		
1. Net Amount of Budgetary Resources Obligated for Undelivered Orders at the End of the Period	$ 161,145	$ 227,740
2. Available Borrowing and Contract Authority at the End of the Period	0	1,232,543

Standard Disclosures

The Statement of Budgetary Resources (SBR) is an image of the monthly Report on Budget Execution. These reports should be produced using budgetary accounts. However, many of the Navy Working Capital Fund-Marine Corps (NWCF-MC) financial and nonfinancial feeder systems and processes were designed and implemented prior to the issuance of Generally Accepted Accounting Principles (GAAP) for Federal agencies. These systems were not designed to collect and record financial information on the budgetary accounting basis as required by GAAP. The NWCF-MC and the Defense Finance and Accounting Service (DFAS) continue to implement new accounting systems designed to produce both proprietary and budgetary reports and use the United States Standard General Ledger. Until the implementations are completed, the amounts recorded are primarily proprietary.

Change in Receivables from Federal Sources includes amounts reported as reimbursements and other income earned-receivable. The amount presented on this line is the ending balance less the beginning balance for the current fiscal year. The net negative value change is a reflection of NWCF-MC aggressive efforts to collect on reimbursable operations and the continuing efforts between DFAS, partnering with NWCF-MC, to reduce accounts receivable.

For SBR, Supply Management revenue is defined as gross sales less credit returns. For the Balance Sheet, credit returns are posted as inventory allowance and are reclassified as contra to the revenue accounts. The difference in "meanings" causes variances in the reports.

As of September 30, 2007, the difference between U.S. Treasury and NWCF-MC activity ledgers is minimal. The principal cause of the difference is related to timing issues or type of transactions. The differences are recorded as undistributed disbursements and collections on the departmental reports. While there may be no impact upon U.S. Treasury balance, the above differences have created minor distortions in the accounts receivable and accounts payable on SBR. Accounting relationship issues involving the treatment of undistributed collections and disbursements have also created minor abnormal balances for accounts receivable and accounts payable on SBR.

Intraentity Transactions

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

Apportionment Categories

The Office of Management and Budget (OMB) Circular A-136 requires disclosure of the amount of direct and reimbursable obligations incurred against amounts apportioned under categories A, B, and exempt from apportionment. All of the $595.2 million in NWCF-MC obligations fall into category B (reimbursable).

Spending Authority from Offsetting Collections

Adjustments in funds that are temporarily not available pursuant to Public Law, and those that are permanently not available, are not included in the Spending Authority from Offsetting Collections and Adjustments line on SBR or the Spending Authority for Offsetting Collections and Adjustments line on the Reconciliation of Net Cost of Operations to Budget.

Disclosure Related to Abnormal Account Balance

The NWCF-MC has an abnormal balance of $49.9 million in Contract Authority Realized. During the month of September 2007, journal vouchers were processed in an effort to reconcile the Status of Funds with the Fund Balance with Treasury. A beginning balance adjustment of $93.3 million was made to Contract Authority Carried Forward, along with a current period credit adjustment of $62.6 million to Contract Authority Realized, causing the abnormal balance. The entries were made to facilitate correcting cash and Contract Authority Carried Forward. The abnormal balance was offset by current period closing balance of $12.6 million to Contract Authority Realized. The abnormal balance of Contract Authority Realized will close to Contract Authority Carried Forward, resulting in the correct balance in budgetary cash and Contract Authority Carried Forward.

This adjustment is the result of reconciliation to balance NWCF-MC budgetary with proprietary accounts. The original unreconciled balance between NWCF-MC budgetary and proprietary was the result of missed budgetary entries during the manual processes of reporting the SF 133, Report on Budget Execution and Budgetary Resources. Since the introduction of the Defense Departmental Reporting System (DDRS)-Budgetary and DDRS-Audited Financial Statements reconciliation, recognition of these types of issues is more readily identifiable.

Other Disclosures Related to the Statement of Budgetary Resources
The information contained in this note represents a subset of the information portrayed in Unpaid Obligations and Gross Outlays of the Statement of Budgetary Resources and is reconcilable back to the applicable general ledger accounts.

The NWCF-MC does not have any legal arrangements affecting the use of unobligated balances of budget authority such as time limits, purpose, and obligation limitations.

The NWCF-MC has no borrowing authority and available contract authority at the end of the period.

The NWCF-MC received $32.4 million in a direct appropriation from the fiscal year (FY) 2007 U.S. Troop Readiness, Veterans' Care, Katrina Recovery, and Iraq Accountability Appropriations Act. This funding was received in June of 3rd Quarter, FY 2007 as a part of the emergency supplemental funding to finance the cost of War Reserve Material procurements.

The NWCF-MC received $63.4 million in July 2007 due to a transfer-in of cash to realign cash balances within NWCF activities, which resulted in an internal net zero realignment for the Department of the Navy. The cash realignment effort was done in order to comply with the Management Initiative Decision 903 dated December 2002, which proposed an initiative to realign cash balances at the activity groups for all of the Defense Working Capital Funds to improve cash management.

The NWCF-MC has no material differences between amounts reported on SBR and SF 133, Report on Budget Execution and Budgetary Resources.

This note has been modified to accurately report the remaining available balance of borrowing and contract authority. Previously, NWCF-MC reported the amount of the contract/borrowing authority that had initially been used and not subsequently replaced by reimbursement or apportionment.

Note 21. Reconciliation of Net Cost of Operations to Budget

As of September 30	2007	2006
(Amounts in Thousands)		
Resources Used to Finance Activities:		
Budgetary Resources Obligated:		
1. Obligations incurred	$ 595,206	$ 694,405
2. Less: Spending authority from offsetting collections and recoveries (-)	(584,202)	(627,536)
3. Obligations net of offsetting collections and recoveries	$ 11,004	$ 66,869
4. Less: Offsetting receipts (-)	0	0
5. Net obligations	$ 11,004	$ 66,869
Other Resources:		
6. Donations and forfeitures of property	0	0
7. Transfers in/out without reimbursement (+/-)	0	(90,240)
8. Imputed financing from costs absorbed by others	12,325	12,327
9. Other (+/-)	(96,189)	0
10. Net other resources used to finance activities	$ (83,864)	$ (77,913)
11. Total resources used to finance activities	$ (72,860)	$ (11,044)
Resources Used to Finance Items not Part of the Net Cost of Operations:		
12. Change in budgetary resources obligated for goods, services and benefits ordered but not yet provided:		
12a. Undelivered Orders (-)	$ 66,595	$ (27,627)
12b. Unfilled Customer Orders	(20,222)	(11,274)
13. Resources that fund expenses recognized in prior Periods (-)	(1,972)	0
14. Budgetary offsetting collections and receipts that do not affect Net Cost of Operations	0	0
15. Resources that finance the acquisition of assets (-)	(164,323)	(177,220)
16. Other resources or adjustments to net obligated resources that do not affect Net Cost of Operations:		
16a. Less: Trust or Special Fund Receipts Related to exchange in the Entity's Budget (-)	0	0
16b. Other (+/-)	96,189	90,240
17. Total resources used to finance items not part of the Net Cost of Operations	$ (23,733)	$ (125,881)
18. Total resources used to finance the Net Cost of Operations	$ (96,593)	$ (136,925)

As of September 30	2007	2006
(Amounts in Thousands)		
Components of the Net Cost of Operations that will not Require or Generate Resources in the Current Period:		
Components Requiring or Generating Resources in Future Period:		
19. Increase in annual leave liability	$ 0	$ 0
20. Increase in environmental and disposal liability	0	0
21. Upward/Downward reestimates of credit subsidy expense (+/-)	0	0
22. Increase in exchange revenue receivable from the public (-)	0	0
23. Other (+/-)	0	2,928
24. Total components of Net Cost of Operations that will Require or Generate Resources in future periods	$ 0	$ 2,928
Components not Requiring or Generating Resources:		
25. Depreciation and amortization	$ 5,461	$ 3,560
26. Revaluation of assets or liabilities (+/-)	67,449	(38,835)
27. Other (+/-)		
27a. Trust Fund Exchange Revenue	0	0
27b. Cost of Goods Sold	80,516	191,173
27c. Operating Materiel and Supplies Used	0	0
27d. Other	0	0
28. Total Components of Net Cost of Operations that will not Require or Generate Resources	$ 153,426	$ 155,898
29. Total components of Net Cost of Operations that will not Require or Generate Resources in the current period	$ 153,426	$ 158,826
30. Net Cost of Operations	$ 56,833	$ 21,901

Standard Disclosures

The Reconciliation of Net Cost of Operations to Budget is designed to provide information about the total resources used by an entity to explain how those resources were used to finance orders for goods and services not yet delivered, to acquire assets and liabilities, and to fund the entity's net cost of operations. It is designed to report the differences and facilitate the reconciliation of accrual based amounts used in the Statement of Net Cost and obligation-based amounts used in the Statement of Budgetary Resources (SBR). The computations and presentation of items in the Reconciliation of Net Cost of Operations to Budget demonstrate that the budgetary and proprietary information in an entity's financial management system agree.

Due to the Navy Working Capital Fund-Marine Corps (NWCF-MC) financial system limitations, budgetary data is not in agreement with proprietary expenses and assets capitalized. The difference between budgetary and proprietary data has been previously identified as a system deficiency. To bring the Reconciliation of Net Cost of Operations to Budget into balance with the Statement of Net Cost, the following adjustment (absolute value) was made:

Resources That Finance the Acquisition of Assets: $168.1 million.

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

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

Resources That Finance the Acquisition of Assets
For NWCF-MC, the various automated and manual financial management and feeder systems do not record transfers of material purchases to the various fixed asset categories at the time of receipt. The current financial process produces the proprietary general ledger account transactions that result in amounts equating to the value of inventory received, recorded as an asset prior to being expensed and thereafter, during the month, applied to cost of goods sold depending on time of sale and financial system updates.

Composition of Other on the Reconciliation of Net Cost of Operations to Budget
The NWCF-MC has three "Other" lines on the Reconciliation of Net Cost of Operations to Budget during Fiscal Year 2007. The composition of these lines is described below:

Resources Used to Finance Activities, Other Resources, Other
The amount reported as "other" on this line consists of net results of NWCF-MC gains and losses generated from reconciling transfers in and out.

Resources Used to Finance Items not Part of the Net Cost of Operations, Other Resources or Adjustments to Net Obligated Resources
The amount reported as "other" on this line consists of net results of NWCF-MC gains and losses generated from reconciling transfers in and out.

Components Not Requiring or Generating Resources from Cost of Goods Sold
The amount reported as other consists of NWCF-MC cost of goods sold.

Other Disclosures
The NWCF-MC has a $2.0 million difference between the amount reported as liabilities not covered by budgetary resources on the balance sheet and the amounts reported as components requiring or generating resources in future periods on the Reconciliation of Net Cost of Operations to Budget. The differences are due to the following:

- NWCF-MC recognizing the liabilities owed to the U.S. Treasury, Debt Management Office for interest, penalties, and administrative fees related to services for collection of accounts receivables from public customers.

- A decrease in future funded liabilities for Military Retirement Benefits and Other Federal Employment Benefits resulting from a decline in civilian personnel endstrength levels.

Note 22. Disclosures Related to Incidental Custodial Collections

Information Related to Incidental Custodial Collections:
The Navy Working Capital Fund-Marine Corps has no Disclosures Related to Incidental Custodial Collections.

Note 23. Earmarked Funds

Information Related to Earmarked Funds:
The Navy Working Capital Fund-Marine Corps has no Earmarked Funds.

Note 24. Other Disclosures

Information Related to Other Disclosures:
The Navy Working Capital Fund-Marine Corps has no Other Disclosures.

Note 25. Restatements

Information Related to Restatements:
For FY 2007, the Navy Working Capital Fund-Marine Corps has no restatements.

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Navy Working Capital Fund – Marine Corps

Required Supplementary Information

Department of the Navy Subsidiary Financial Statements

2007 Annual Financial Report

Navy Working Capital Fund-Marine Corps
General Property, Plant, and Equipment
Real Property Deferred Maintenance
For Fiscal Year Ended September 30, 2007

The Navy Working Capital Fund-Marine Corps real property deferred maintenance for fiscal year ended September 30, 2007 is being reported with the U.S. Marine Corps General Fund real property deferred maintenance. See United States Marine Corps General Fund Required Supplementary Information.

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Navy Working Capital Fund – Marine Corps

Other Accompanying Information

Department of the Navy Subsidiary Financial Statements

2007 Annual Financial Report

Appropriations, Funds, and Accounts Included in the Financial Statements

Reporting Entity

Navy Working Capital Fund (NWCF)

Fund/Account Treasury Symbol and Title:

97X4930.002

Navy Working Capital Fund Activity Group Treasury Symbol and Title:

97X4930.NA4A	Depot Maintenance - Other, Marine Corps
97X4930.NC2A	Supply Management, Marine Corps

Audit Opinions

2007

2007 Annual Financial Report

INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
ARLINGTON, VIRGINIA 22202-4704

November 8, 2007

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

SUBJECT: Independent Auditor's Report on the FY 2007 Department of the Navy General Fund Financial Statements (Report No. D-2008-014)

The Chief Financial Officers Act of 1990, as amended, requires the Department of Defense Inspector General to audit the accompanying Department of the Navy General Fund Consolidated Balance Sheet as of September 30, 2007 and 2006, and the Consolidated Statement of Net Cost, the Consolidated Statement of Changes in Net Position, the Combined Statement of Budgetary Resources, and related notes for the FYs then ended.[1] The basic financial statements are the responsibility of Department of the Navy management. The Navy is also responsible for implementing effective internal control and for complying with laws and regulations. We are unable to express an opinion on the Navy General Fund FY 2007 Financial Statements because of limitations on the scope of our work. Thus, the financial statements may be unreliable. In addition to our disclaimer of opinion on the financial statements, we are including the required Report on Internal Control and Compliance with Laws and Regulations. The Report on Internal Control and Compliance with Laws and Regulations is an integral part of our disclaimer of opinion on the financial statements and should be considered in assessing the results of our work.

Disclaimer of Opinion on the Financial Statements

The Assistant Secretary of the Navy (Financial Management and Comptroller) acknowledged to us that the Navy General Fund FY 2007 Financial Statements would not substantially conform to accounting principles generally accepted in the United States of America (GAAP), and that Navy financial management and feeder systems were unable to adequately support material amounts on the financial statements as of September 30, 2007. Section 1008(d) of the FY 2002 National Defense Authorization Act limits the Department of Defense Inspector General to performing only those audit procedures required by generally accepted government auditing standards that are consistent with the representations made by management. Therefore, we did not perform auditing procedures required by U.S. Government auditing standards and Office of Management and Budget Bulletin No. 07-04 (OMB Bulletin 07-04) to determine whether material amounts on the financial statements were fairly presented. Prior audits have identified, and the Navy has also acknowledged, the long-standing material internal control weaknesses identified in the Summary of Internal Control. These pervasive material weaknesses affect the reliability of certain information contained in the annual financial statements—much of which is taken from the same data sources as the basic financial statements.[2] Therefore, we are unable to express, and we do not express, an opinion on the basic financial statements. Further, the purpose of the audit was not to express an opinion on Management Discussion and Analysis, Required Supplementary

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[1] Beginning in FY 2007, OMB Circular A-136 requires entities to present the Statement of Financing as a note. It is no longer considered a basic statement.

[2] The annual financial statements include the basic statements, Management Discussion and Analysis, Required Supplementary Stewardship Information, Required Supplementary Information, and Other Accompanying Information.

Stewardship Information, Required Supplementary Information, Other Accompanying Information, and Performance Measures accompanying the basic financial statements. Accordingly, we express no opinion on that information.

Summary of Internal Control

In planning our work, we considered Navy internal controls over financial reporting and compliance with applicable laws and regulations. We did this to determine our procedures for auditing the financial statements and to comply with OMB guidance, but our purpose was not to express an opinion on internal control. Accordingly, we do not express an opinion on internal control over financial reporting and compliance with applicable laws and regulations. However, previously identified significant deficiencies, all of which are material, continued to exist in the following areas:

- **Financial Management Systems**
- **Fund Balance with Treasury**
- **Accounts Receivable**
- **Other Assets**
- **Inventory and Related Property, Net**
- **General Property, Plant and Equipment**
- **Accounts Payable**
- **Environmental Liabilities**
- **Statement of Net Cost**
- **Problem Disbursements**
- **Unobligated Balances**

The Navy General Fund reported all of the above weaknesses in its 2007 Statement of Assurance except for the Statement of Net Cost Unobligated Balances. We identified additional material weaknesses in Inventory and Related Property, Net that were not reported by Navy management in FY 2007.

A material weakness is a significant deficiency, or a combination of significant deficiencies, resulting in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected.[3, 4]

[3] The term "remote" is defined as "the chance of the future event or events occurring is slight." Therefore, the likelihood of an event is "more than remote" when it is at least reasonably possible.

[4] A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or a combination of control deficiencies, adversely affecting the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles. Significant deficiencies result in more than a remote likelihood that a misstatement of an entity's financial statements that is more than inconsequential will not be prevented or detected.

Our internal control work (conducted as part of prior audits) would not necessarily disclose all significant deficiencies. The Attachment offers additional details on significant deficiencies, all of which we consider to be material internal control weaknesses.

Summary of Compliance with Laws and Regulations

Our work to determine compliance with selected provisions of applicable laws and regulations related to financial reporting was limited because management acknowledged that instances of noncompliance identified in prior audits continue to exist. The Assistant Secretary of the Navy (Financial Management and Comptroller) acknowledged to us that Navy financial management systems do not substantially comply with Federal financial management system requirements, GAAP, and the U.S. Government Standard General Ledger at the transaction level. Therefore, we did not determine whether the Navy was in compliance with all applicable laws and regulations related to financial reporting. Providing an opinion on compliance with certain provisions of laws and regulations was not an objective of our audit and, accordingly, we do not express such an opinion. See the Attachment for additional details on compliance with laws and regulations.

Management's Responsibilities

Management is responsible for:

- preparing the financial statements in conformity with GAAP;
- establishing, maintaining, and assessing internal controls to provide reasonable assurance that the broad control objectives of the Federal Managers' Financial Integrity Act are met; and
- complying with applicable laws and regulations.

We provided a draft of this report to the Assistant Secretary of the Navy (Financial Management and Comptroller) who then provided us technical comments, which we incorporated as appropriate. Navy officials expressed their continuing commitment to address the problems this report outlines.

Paul J. Granetto

Paul J. Granetto, CPA
Assistant Inspector General and Director
Defense Financial Auditing
Service

Attachment:
As stated

Report on Internal Control and Compliance with Laws and Regulations

Internal Control

Management is responsible for implementing and maintaining effective internal control and for providing reasonable assurance that accounting data are accumulated, recorded, and reported properly; that the requirements of applicable laws and regulations are met; and that assets are safeguarded against misappropriation and abuse. Our purpose was not to, and we do not, express an opinion on internal control over financial reporting. However, we have identified the following material weaknesses that could adversely affect the Navy financial management operations.

Previously Identified Material Weaknesses. Management acknowledged that previously identified significant deficiencies, all of which are material, continued to exist in the following areas.

Financial Management Systems. Navy financial system deficiencies include the inability to fully implement GAAP and the U.S. Government Standard General Ledger at the transaction level.

Fund Balance with Treasnry. Deficiencies associated with Fund Balance with Treasury include: unmatched disbursements and collections; undistributed disbursements, collections, and abnormal balances; and inability to reconcile Navy records with the Department of Treasury records and to the Statement of Budgetary Resources.

Accounts Receivable. The audit trails for accounts receivable are inadequate. In addition, the accounts receivable subledgers do not reconcile with the general ledger.

Other Assets. The Navy Enterprise Resource Planning pilot system is unable to capture outstanding finance payments as required. In addition, contract progress payment transactions are not reported accurately in the Enterprise Resource Planning pilot system. Furthermore, controls over the contract financing payment process may not be operating effectively. The Navy did not maintain written procedures for compiling its contract financing balance, excluded valid contracting financing amounts, and included contract financing amounts that were not supported by source documentation.

Inventory and Related Property, Net. The legacy systems currently used do not maintain the historical cost data necessary to comply with Statement of Federal Financial Accounting Standards No. 3, "Accounting for Inventory and Related Property." In addition, completeness issues exist because these legacy systems were not designed to ensure that all of the inventory items are included in the values reported on the Balance Sheet. Some Navy commands have not used the consumption method for expensing Operating Materials and Supplies as specified in Statement of Federal Financial Standards No. 3. Also, some commands are unable to provide Operating Materials and Supplies at the detail-transaction level and only maintain beginning and ending balances.

General Property, Plant, and Eqnipment. Completeness issues still exist associated with recognizing internal use software and leasehold improvements. Trading partner data for capitalized assets are not always recorded. The Navy is currently working with the Office of the Under Secretary of Defense for Acquisition, Technology, and Logistics and Navy major commands to fully implement Statement of Federal Financial Accounting Standards No. 23, "Eliminating the Category National Defense Property, Plant, and Equipment." In addition, the Navy is working with the Office of the Under Secretary of Defense (Comptroller) to ensure that documentation for real property is available beginning with FY 1999 and that Form DD 1354, "Transfer and Acceptance of Military Real Property" is properly used throughout the Department of the Navy.

Accounts Payable. Intragovernmental Accounts Payable transactions and Accounts Payable with the Public are not being recorded timely, completely, or accurately. Lack of sufficient systems, processes, and data to support reconciliation of buyer-side trading partner information continue to be issues.

Environmental Liabilities. The Navy cannot be assured that it complies with recent modifications to the DoD Financial Management Regulation regarding the reporting of site-level current and non-current liabilities. In addition, deficiencies exist over the justification of data used to estimate the cost of an environmental project. The Navy does not have effective controls over Environmental Liabilities to ensure that adequate audit trails and supporting documentation for estimates exist and that the estimates comply with established guidance.

Statement of Net Cost. The Navy currently derives the information on the Statement of Net Cost from budgetary accounts instead of using an accrual basis. In addition, the costs are aligned to the major appropriations instead of being aligned with major programs and goals, as required in Statement of Federal Financial Accounting Standards No. 4, "Managerial Cost Accounting Concepts and Standards." Furthermore, the Navy costs are not broken out and reported by the responsible components, as required by Statement of Federal Financial Accounting Standards No. 4.

Problem Disbursements. On the Statement of Budgetary Resources, inaccurate or missing fund accounting codes have resulted in unmatched disbursements and collections requiring the use of suspense accounts. The suspense accounts cause difficulty in reconciling Navy General Fund records with the Department of Treasury's records.

Unobligated Balances. On the Statement of Budgetary Resources, deficiencies exist in recorded unobligated amounts because financial systems are not fully integrated, and not all commands sufficiently reviewed unliquidated obligations. Additionally, reimbursable transactions were not properly documented or reported on the Disbursing Officer Statement of Accountability.

Material Weakness Identified During FY 2007

Our financial-related work during FY 2007 identified an additional material weakness. The Navy reported Inventory and Related Property, Net as a deficiency, and our audits, "Report on Navy Sponsor Owned Material Stored at the Space and Naval Warfare Systems Centers," Report No. D-2007-048, and "Reporting of Navy Sponsor Owned Material Stored at the Naval Air Systems Command Activities," Report No. D-2007-085, described additional deficiencies related to Operating Materials and Supplies that were not identified by the Navy. Specifically, the Navy did not accurately report its Sponsor Owned Material. The Navy included Sponsor Owned Material as Operating Materials and Supplies instead of reporting it as Inventory or Property, Plant, and Equipment. This resulted in a misstatement of the financial statements. In addition, the Navy did not maintain audit trails or adequately validate the data on Sponsor Owned Material before submitting the data to the Assistant Secretary of the Navy (Financial Management and Comptroller) for inclusion in the financial statements.

These financial management deficiencies may cause inaccurate management information. As a result, Navy management decisions based in whole or in part on this information may be adversely affected. Financial information reported by the Navy may also contain misstatements resulting from these deficiencies.

Attachment

Compliance with Laws and Regulations

Management is responsible for compliance with existing laws and regulations related to financial reporting. We limited our work to determine compliance with selected provisions of the applicable laws and regulations because management acknowledged instances of noncompliance, and previously reported instances of noncompliance continue to exist. Therefore, we did not determine whether the Navy was in compliance with selected provisions of all applicable laws and regulations related to financial reporting. Our objective was not to, and we do not, express an opinion on compliance with applicable laws and regulations.

Federal Financial Management Improvement Act of 1996. The Federal Financial Management Improvement Act (FFMIA) of 1996 requires the Navy to establish and maintain financial management systems that comply substantially with Federal financial management systems requirements, applicable Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level. For FY 2007, the Navy did not fully comply with FFMIA. The Navy acknowledged that many of its critical financial management and feeder systems did not substantially comply with Federal financial management systems requirements, Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level as of September 30, 2007.

Audit Disclosures

The Assistant Secretary of the Navy (Financial Management and Comptroller) acknowledged to us on March 15, 2007, that the Navy financial management and feeder systems cannot provide adequate evidence supporting various material amounts on the financial statements, and previously identified material weaknesses continue to exist. Therefore, we did not perform detailed testing related to previously identified material weaknesses. In addition, we did not perform audit work related to the following selected provisions of laws and regulations: Anti-Deficiency Act, Federal Credit Reform Act, Pay and Allowance System for Civilian Employees, and Prompt Payment Act.

This report does not include recommendations to correct the material internal control weaknesses and instances of noncompliance with laws and regulations because either previous audit reports contained recommendations for corrective actions or audit projects currently in process will include appropriate recommendations.

INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
ARLINGTON, VIRGINIA 22202-4704

November 8, 2007

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

SUBJECT: Independent Auditor's Report on the Department of the Navy Working Capital Fund FY 2007 Financial Statements (Report No. D-2008-015)

The Chief Financial Officers Act of 1990, as amended, requires the Department of Defense Inspector General to audit the accompanying Department of the Navy Working Capital Fund Consolidated Balance Sheet as of September 30, 2007 and 2006, and the Consolidated Statement of Net Cost, the Consolidated Statement of Changes in Net Position, the Combined Statement of Budgetary Resources, and the related notes for the FYs then ended.[1] The financial statements are the responsibility of Department of the Navy management. The Department of the Navy is also responsible for implementing effective internal control and for complying with laws and regulations. We are unable to express an opinion on the Department of the Navy Working Capital Fund FY 2007 Financial Statements because of limitations on the scope of our work. Thus, the financial statements may be unreliable. In addition to our disclaimer of opinion on the financial statements, we are including the required Report on Internal Control and Compliance with Laws and Regulations. The Report on Internal Control and Compliance with Laws and Regulations is an integral part of our disclaimer of opinion on the financial statements and should be considered in assessing the results of our work.

Disclaimer of Opinion on the Financial Statements

The Assistant Secretary of the Navy (Financial Management and Comptroller) acknowledged to us that the Department of the Navy Working Capital Fund FY 2007 Financial Statements would not substantially conform to accounting principles generally accepted in the United States of America (GAAP), and that financial management and feeder systems were unable to adequately support material amounts on the financial statements as of September 30, 2007. Section 1008(d) of the FY 2002 National Defense Authorization Act limits the Department of Defense Inspector General to performing only those audit procedures required by generally accepted government auditing standards that are consistent with the representations made by management. Therefore, we did not perform auditing procedures required by U.S. Government auditing standards and Office of Management and Budget Bulletin No. 07-04 (OMB Bulletin 07-04) to determine whether material amounts on the financial statements were fairly presented. Prior audits have identified, and the Department of the Navy has also acknowledged, the long-standing material internal control weaknesses identified in the Summary of Internal Control. These pervasive material weaknesses affect the reliability of certain information contained in the annual financial statements—much of which is taken from the same data sources as the basic financial statements.[2] Therefore, we are unable to express, and we do not express, an opinion on the basic financial statements. Further, the purpose of the audit was not to express an opinion on Management Discussion and Analysis, Required Supplementary Information, Other

[1] Beginning in FY 2007, OMB Circular A-136 requires entities to present the Statement of Financing as a note. It is no longer considered a basic statement.

[2] The annual financial statements include the basic statements, Management Discussion and Analysis, Required Supplementary Information, and Other Accompanying Information.

Accompanying Information, and Performance Measures accompanying the basic financial statements. Accordingly, we express no opinion on that information.

Summary of Internal Control

In planning our work, we considered the Department of the Navy internal controls over financial reporting and compliance with applicable laws and regulations. We did this to determine our procedures for auditing the financial statements and to comply with OMB guidance, but our purpose was not to express an opinion on internal control. Accordingly, we do not express an opinion on internal control over financial reporting and compliance with applicable laws and regulations. However, previously identified significant deficiencies, all of which are material, continued to exist in the following areas:

- **Financial Management Systems**
- **Fund Balance with Treasury**
- **Accounts Receivable**
- **Inventory and Related Property, Net**
- **General Equipment**
- **Accounts Payable**
- **Other Liabilities**

A material weakness is a significant deficiency, or a combination of significant deficiencies,[3] resulting in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected.[4] The Department of the Navy reported the above weaknesses in their 2007 Statement of Assurance.

Our internal control work (conducted as part of prior audits) would not necessarily disclose all significant deficiencies. The Attachment offers additional details on significant deficiencies, all of which we consider to be material internal control weaknesses.

Summary of Compliance with Laws and Regulations

We limited our work to determine compliance with selected provisions of applicable laws and regulations related to financial reporting because management acknowledged that instances of noncompliance identified in prior audits continue to exist. The Assistant Secretary of the Navy (Financial Management and Comptroller) acknowledged to us that Department of the Navy

[3] A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or a combination of control deficiencies, adversely affecting the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles. Significant deficiencies result in more than a remote likelihood that a misstatement of an entity's financial statements that is more than inconsequential will not be prevented or detected.

[4] The term "remote" is defined as "the chance of the future event or events occurring is slight." Therefore, the likelihood of an event is "more than remote" when it is at least reasonably possible.

financial management systems do not substantially comply with Federal financial management system requirements, GAAP, and the U.S. Government Standard General Ledger at the transaction level. Therefore, we did not determine whether the Department of the Navy was in compliance with all applicable laws and regulations related to financial reporting. Providing an opinion on compliance with certain provisions of laws and regulations was not an objective of our audit and, accordingly, we do not express such an opinion. See the Attachment for additional details on compliance with laws and regulations.

Management's Responsibilities

Management is responsible for:

- preparing the financial statements in conformity with GAAP;
- establishing, maintaining, and assessing internal controls to provide reasonable assurance that the broad control objectives of the Federal Managers' Financial Integrity Act are met; and
- complying with applicable laws and regulations.

We discussed a draft of this report with the Department of the Navy Assistant Secretary of the Navy (Financial Management and Comptroller) personnel, who then provided us technical comments, which we incorporated as appropriate. The Department of the Navy officials expressed their continuing commitment to address the problems this report outlines.

Paul J. Granetto

Paul J. Granetto, CPA
Assistant Inspector General and Director
Defense Financial Auditing Service

Attachment:
As stated

Report on Internal Control and Compliance with Laws and Regulations

Internal Control

Management is responsible for implementing and maintaining effective internal control and for providing reasonable assurance that accounting data are accumulated, recorded, and reported properly; that the requirements of applicable laws and regulations are met; and that assets are safeguarded against misappropriation and abuse. Our purpose was not to, and we do not, express an opinion on internal control over financial reporting. However, we have identified the following material weaknesses that could adversely affect the Department of the Navy financial management operations.

Previously Identified Material Weaknesses. Management acknowledged that previously identified significant deficiencies, all of which are material, continued to exist in the following areas.

Financial Management Systems. The Department of the Navy financial systems do not comply with GAAP and the U.S. Government Standard General Ledger at the transaction level. As a result, the Department of the Navy financial management and feeder systems cannot provide adequate evidence supporting various material amounts on the financial statements.

Fund Balance with Treasury. The Department of the Navy Working Capital Fund activities do not reconcile cash accounts to the Department of the Treasury cash account balance on a consistent basis. In addition, system interfaces do not exist between the financial reporting systems, which results in unmatched disbursement and collections.

Accounts Receivable. The Department of the Navy does not reconcile subsidiary records to corresponding general ledger accounts on a regular basis, resulting in control weakness and loss of an audit trail. They also post unmatched collections to accounts receivable using journal vouchers, leaving no audit trail. Trading partner adjustments posted to intragovernmental accounts receivable are not always supported by transactions. The Department of the Navy does not always record and post collection of public accounts such as contract overpayments, travel advances, and employee debt.

Inventory and Related Property, Net. The Department of the Navy Working Capital Fund supply management activities record inventory at latest acquisition cost. To comply with GAAP, latest acquisition cost must be converted to approximations of historical costs. However, the Department of the Navy does not have adequate data, processes, and methodologies to make accurate conversions which would enable auditors to verify resulting inventory balances.

General Property, Plant, and Equipment. Completeness issues associated with financial reporting of General Equipment still exist. Trading partner data for capitalizing assets may not always be recorded.

Accounts Payable. The Accounts Payable line item is adversely affected by insufficient and/or inconsistent reconciliations and supporting documentation, lack of direct system interfaces that result in matching difficulties, undistributed disbursements, and the inability to capture trading partner information. Unmatched disbursements are transferred to accounts payable using journal vouchers, leaving no audit trail and often causing an abnormal balance.

Other Liabilities. Unsupported, undistributed disbursements need to be resolved. The Office of the Under Secretary of Defense (Comptroller)/Chief Financial Officer, the Defense Finance and Accounting Service Cleveland, and the Department of the Navy staff are working cooperatively to resolved this deficiency. Contract accruals need to be analyzed to determine whether these amounts are posted properly to Other Liabilities.

These financial management deficiencies may cause inaccurate management information. As a result, the Department of the Navy management decisions based in whole or in part on this information may be adversely affected. Financial information reported by DoD may also contain misstatements resulting from these deficiencies.

Attachment

Compliance with Laws and Regulations

Management is responsible for compliance with existing laws and regulations related to financial reporting. We limited our work to determine compliance with selected provisions of the applicable laws and regulations because management acknowledged instances of noncompliance, and previously reported instances of noncompliance continue to exist. Therefore, we did not determine whether the Department of the Navy was in compliance with selected provisions of all applicable laws and regulations related to financial reporting. Our objective was not to, and we do not, express an opinion on compliance with applicable laws and regulations.

Federal Financial Management Improvement Act of 1996. The Federal Financial Management Improvement Act of 1996 requires DoD to establish and maintain financial management systems that comply substantially with Federal financial management systems requirements, applicable Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level. For FY 2007, the Department of the Navy did not fully comply with the Federal Financial Management Improvement Act. The Assistant Secretary of the Navy (Financial Management and Comptroller) acknowledged that many of its critical financial management and feeder systems did not substantially comply with Federal financial management system requirements, Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level as of September 30, 2007.

Audit Disclosures

The Assistant Secretary of the Navy (Financial Management and Comptroller) acknowledged to us on March 15, 2007, that the Department of the Navy financial management and feeder systems cannot provide adequate evidence supporting various material amounts on the financial statements, and previously identified material weaknesses continue to exist. Therefore, we did not perform detailed testing related to previously identified material weaknesses. In addition, we did not perform audit work related to the following selected provisions of laws and regulations: Provisions Governing Claims of the United States Government, Pay and Allowance System for Civilian Employees, the Antideficiency Act, the Federal Credit Reform Act, and the Prompt Payment Act.

This report does not include recommendations to correct the material internal control weaknesses and instances of noncompliance with laws and regulations because either previous audit reports contained recommendations for corrective actions or audit projects currently in process may include appropriate recommendations.

INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
ARLINGTON, VIRGINIA 22202-4704

November 8, 2007

MEMORANDUM FOR ASSISTANT DEPUTY COMMANDANT FOR PROGRAMS AND RESOURCES (FISCAL), OF THE UNITED STATES MARINE CORPS

SUBJECT: Independent Auditor's Report on the FY 2007 United States Marine Corps General Fund Financial Statements (Report No. D-2008-016)

Under Secretary of Defense (Comptroller) guidance implementing the Chief Financial Officers Act of 1990, as amended, requires the Department of Defense Office of Inspector General to audit the accompanying United States Marine Corps General Fund Consolidated Balance Sheet as of September 30, 2007 and 2006, and the Consolidated Statement of Net Cost, the Consolidated Statement of Changes in Net Position, the Combined Statement of Budgetary Resources and related notes for the FYs then ended.[1] The basic financial statements are the responsibility of United States Marine Corps management. The United States Marine Corps is also responsible for implementing effective internal control and for complying with laws and regulations. We are unable to express an opinion on the United States Marine Corps FY 2007 Financial Statements because of limitations on the scope of our work. Thus, the basic financial statements may be unreliable. In addition to our disclaimer of opinion on the basic financial statements, we are including the required Report on Internal Control and Compliance with Laws and Regulations. The Report on Internal Control and Compliance with Laws and Regulations is an integral part of our disclaimer of opinion on the basic financial statements and should be considered in assessing the results of our work.

Disclaimer of Opinion on the Financial Statements

The United States Marine Corps Director, Fiscal Division acknowledged to us that the United States Marine Corps FY 2007 Financial Statements would not substantially conform to accounting principles generally accepted in the United States of America (GAAP). In addition, the United States Marine Corps Director, Fiscal Division deferred to the Under Secretary of Defense (Comptroller) regarding financial management and feeder systems. The Under Secretary of Defense (Comptroller) acknowledged that DoD financial management and feeder systems were unable to adequately support material amounts on the financial statements as of September 30, 2007. Section 1008(d) of the FY 2002 National Defense Authorization Act limits the Department of Defense Inspector General to performing only those audit procedures required by generally accepted government auditing standards that are consistent with the representations made by management. Therefore, we did not perform auditing procedures required by U.S. Government auditing standards and Office of Management and Budget (OMB) Bulletin No. 07-04 to determine whether material amounts on the financial statements were fairly presented. The United States Marine Corps is a Component of the Department of the Navy. The United States Marine Corps Director, Fiscal Division and the Assistant Secretary of the Navy (Financial Management and Comptroller) have acknowledged the material internal control weaknesses identified in the Summary of Internal Controls. These pervasive material weaknesses may affect the reliability of certain information contained in the annual financial

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[1] Beginning in FY 2007, OMB Circular A-136 requires entities to present the Statement of Financing as a note. It is no longer considered a basic statement.

statements—much of which is taken from the same data sources as the basic financial statements.[2] Therefore, we are unable to express, and we do not express, an opinion on the basic financial statements. Further, the purpose of the audit was not to express an opinion on Management Discussion and Analysis, Required Supplementary Stewardship Information, Required Supplementary Information, Other Accompanying Information, and Performance Measures accompanying the basic financial statements. Accordingly, we express no opinion on that information.

Summary of Internal Control

In planning our work, we considered the United States Marine Corps internal controls over financial reporting and compliance with applicable laws and regulations. We did this to determine our procedures for auditing the financial statements and to comply with OMB guidance, but our purpose was not to express an opinion on internal control. Accordingly, we do not express an opinion on internal control over financial reporting and compliance with applicable laws and regulations.

A material weakness is a significant deficiency, or a combination of significant deficiencies, resulting in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected.[3]

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or a combination of control deficiencies, adversely affecting the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with GAAP. The following list identifies significant deficiencies, all of which are material.

- **Financial Management Feeder Systems**
- **Fund Balance with Treasury**
- **Inventory and Related Property, Net**
- **General Property, Plant, and Equipment**
- **Environmental Liabilities**
- **Statement of Net Cost**
- **Accounts Payable**

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[2] The annual financial statements include the basic statements, Management Discussion and Analysis, Required Supplementary Stewardship Information, Required Supplementary Information, and Other Accompanying Information.

[3] The term "remote" is defined as "the chance of the future event or events occurring is slight." Therefore, the likelihood of an event is "more than remote" when it is at least reasonably possible.

- **Accounts Receivable**
- **Other Assets**
- **Other Liabilities**
- **Problem Disbursements**
- **Unobligated Balances**
- **Data Collection Process**

Our internal control work (conducted as part of prior audits) would not necessarily disclose all significant deficiencies. The Attachment offers additional details on these significant deficiencies, all of which we consider to be material internal control weaknesses.

Summary of Compliance with Laws and Regulations

We limited our work to determine compliance with selected provisions of applicable laws and regulations related to financial reporting because management acknowledged that instances of noncompliance identified in prior audits continue to exist. The Assistant Secretary of the Navy (Financial Management and Comptroller) acknowledged to us that Department of Navy financial management systems do not substantially comply with Federal financial management system requirements, GAAP, and the U.S. Government Standard General Ledger at the transaction level. Although the United States Marine Corps, Director, Fiscal Division did not make assertions relating to compliance with laws and regulations, it is a Component of the Department of the Navy, which has identified weaknesses regarding compliance with laws and regulations. Therefore, we did not determine whether United States Marine Corps was in compliance with all applicable laws and regulations related to financial reporting. Providing an opinion on compliance with certain provisions of laws and regulations was not an objective of our audit and, accordingly, we do not express such an opinion. See the Attachment for additional details on compliance with laws and regulations.

Management's Responsibilities.

Management is responsible for:

- preparing the financial statements in conformity with GAAP;
- establishing, maintaining, and assessing internal controls to provide reasonable assurance that the broad control objectives of the Federal Managers' Financial Integrity Act are met; and
- complying with applicable laws and regulations.

We provided a draft copy of this report to personnel at the Office of the Assistant Deputy Commandant for Programs and Resources (Fiscal) of the United States Marine Corps, who provided no comments, but expressed a continuing commitment to address the problems this report outlines.

Paul J. Granetto, CPA
Assistant Inspector General and Director
Defense Financial Auditing
Service

Attachment:
As stated

Report on Internal Control and Compliance with Laws and Regulations

Internal Control

Management is responsible for implementing and maintaining effective internal control and for providing reasonable assurance that accounting data are accumulated, recorded, and reported properly; that the requirements of applicable laws and regulations are met; and that assets are safeguarded against misappropriation and abuse. Our purpose was not to, and we do not, express an opinion on internal control over financial reporting. However, we have identified the following material weaknesses and significant deficiencies that could adversely affect the United States Marine Corps financial management operations.

Material Weaknesses Identified During FY 2007. As a result of our financial-related work during FY 2007, we identified the following significant deficiencies, all of which are material.

Financial Management Feeder Systems. DoD financial management systems do not comply fully with GAAP and the U.S. Government Standard General Ledger at the transaction level. As a result, DoD financial management and feeder systems cannot provide adequate evidence supporting various material amounts on the financial statements.

Fund Balance with Treasury. Deficiencies associated with Fund Balance With Treasury include: unmatched disbursements and collections; undistributed dishursements, collections, and abnormal balances; and the Marine Corps' inability to reconcile Department of the Navy's fund records with Treasury's records and with the Statement of Budgetary Resources.

Inventory and Related Property, Net. The data transfer capability currently does not allow for transaction-to-transaction issues. Financial management and accountability efforts are in the design state for Ammunition Inventory to properly comply with Statement of Federal Financial Accounting Standards No. 3, "Accounting for Inventory and Related Property."

General Property, Plant, and Equipment. Issues related to documentation and support of valuation of Real Property, Personal Property, and Military Equipment, have not yet been resolved. The United States Marine Corps also acknowledged its limitations in effectively accounting for Military Equipment. The Marine Corps is unable to verify the existence and condition of equipment assets that are currently deployed.

Statement of Net Cost. Statement of Federal Financial Accounting Standards No.4, "Managerial Cost Accounting Concepts and Standards," requires that Federal agencies provide reliable and timely information on the full cost of Federal programs, activities and outputs. Currently, the Department of Navy derives the following balances from budgetary accounts, and not on an accrual basis; Intragovernmental Gross Costs, Gross Costs with the Public, Intragovernmental Earned Revenue, and Earned Revenue from the Public. In addition, the costs are not aligned with major programs and goals, as required in Statement of Federal Financial Accounting Standards No.4, but are aligned to the major appropriations. Also Department of Navy costs are not broken out and reported by the responsible Components, as required by Statement of Federal Financial Accounting Standards No 4.

Environmental Liabilities. The processes, procedures, and documents supporting environmental liabilities have not been fully implemented to resolve weaknesses. The United States Marine Corps consultants for audit readiness identified inconsistent calculations of Non-

Defense Environmental Restoration Program current liabilities, a lack of clear and consistent thresholds for recognizing liabilities, and a lack of documentation.

Accounts Payable. The United States Marine Corps has not evaluated the implementation of the Defense Finance and Accounting Service-supported estimation process. In addition, the United States Marine Corps does not currently have a supportable estimation process for all material vendor payment systems. These systems include estimations of major contracts, "level spend," and other contract estimates based on historical cost analysis and contract projections.

Accounts Receivable. The audit trails for accounts receivable are inadequate. In addition, the universe of accounts receivable transactions does not support the balance sheet amount.

Other Assets. Two material deficiencies have been identified relative to contract financing payments: inability to capture required outstanding finance payments within Sigma, an Enterprise Resource Planning pilot system, and inaccuracies in reporting contract progress payment transactions in the same pilot.

Other Liabilities. The Department of the Navy has identified this area as a material weakness and has begun its discovery process for this line. In addition, the United States Marine Corps consultants for audit readiness identified a lack of source documentation for non-environmental disposal liabilities, a lack of reconciliations between source documents and journal vouchers, and a lack of standard data call procedures.

Problem Disbursements. Inaccurate and missing fund accounting codes have resulted in unmatched disbursements and collections requiring use of suspense accounts and an inability to reconcile Department of the Navy's fund records with Treasury's records. Because of a change in scope in classifying transactions as unmatched disbursements during FY 2005, the value of problem disbursements changed significantly. During the fiscal year, aggressive efforts to identify and correct erroneous data have resulted in a dramatic decrease in problem disbursements. The Department of the Navy and the Defense Finance and Accounting Service are working together to reduce problem disbursements to an immaterial amount prior to submitting Department of Navy's assertion package for Fund Balance With Treasury.

Unobligated Balances. Deficiencies noted in recorded unobligated amounts are caused by financial systems that are not fully integrated and the fact that sufficient reviews of unliquidated obligations were not performed by all commands. Additionally, reimbursable transactions were not properly documented or reported on the Disbursing Officer Statement of Accountability.

Data Collection Process. Approximately 60 percent of the data for the Balance Sheet are derived from information resident in feeder systems. The Office of Financial Operations collects this data through a quarterly data call. At the end of 4th Quarter, FY 2006, the Office of Financial Operations completed migrating the data collection process from the Department of the Navy Data Collection Instrument to the Defense Departmental Reporting System-Data Collection Module. Though controls have been established in collecting the data via a web-based data collection module, there may still be internal control weaknesses at the source of the data.

These financial management deficiencies may cause inaccurate management information. As a result, United States Marine Corps management decisions based in whole or in part on this information may be adversely affected. Financial information reported by DoD may also contain misstatements resulting from these deficiencies.

Compliance with Laws and Regulations

Management is responsible for compliance with existing laws and regulations related to financial reporting. We limited our work to determine compliance with selected provisions of the applicable laws and regulations because management acknowledged instances of noncompliance, and previously reported instances of noncompliance continue to exist. Therefore, we did not determine whether the United States Marine Corps was in compliance with selected provisions of all applicable laws and regulations related to financial reporting. Our objective was not to, and we do not, express an opinion on compliance with applicable laws and regulations.

Federal Financial Management Improvement Act of 1996. The Federal Financial Management Improvement Act of 1996 requires DoD to establish and maintain financial management systems that comply substantially with Federal financial management system requirements, applicable Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level. The Assistant Secretary of the Navy (Financial Management and Comptroller) acknowledged that many of its critical financial management and feeder systems did not substantially comply with Federal financial management system requirements, Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level as of September 30, 2007.

Audit Disclosures

The United States Marine Corps Director, Fiscal Division, did not make assertions regarding all financial management and feeder systems, therefore, we relied on the assertions made by the Department of Navy, of which the United States Marine Corps is a Component. The Department of Navy, Assistant Secretary of the Navy, Financial Management and Comptroller acknowledged to us on March 15, 2007, that the Department of Navy financial management and feeder systems cannot provide adequate evidence supporting various material amounts on the financial statements, and previously identified material weaknesses continue to exist. Therefore, we did not perform detailed testing related to previously identified material weaknesses. In addition, we did not perform audit work related to the following selected provisions of laws and regulations: Provisions Governing Claims of the United States Government (including provisions of the Debt Collection Improvement Act), Federal Credit Reform Act, the Pay and Allowance System for Civilian Employees, Prompt Payment Act, and the Antideficiency Act.

This report does not include recommendations to correct the material internal control weaknesses and instances of noncompliance with laws and regulations because either previous audit reports contained recommendations for corrective actions or audit projects currently in process will include appropriate recommendations.

INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
ARLINGTON, VIRGINIA 22202-4704

November 8, 2007

MEMORANDUM FOR ASSISTANT DEPUTY COMMANDANT FOR PROGRAMS AND RESOURCES (FISCAL) OF THE UNITED STATES MARINE CORPS

SUBJECT: Independent Auditor's Report on the FY 2007 Department of the Navy Working Capital Fund-Marine Corps Financial Statements (Report No. D-2008-017)

Under Secretary of Defense (Comptroller) guidance implementing the Chief Financial Officers Act of 1990, as amended, requires the Department of Defense Office of Inspector General to audit the accompanying Department of the Navy Working Capital Fund-Marine Corps Consolidated Balance Sheet as of September 30, 2007 and 2006, and the Consolidated Statement of Net Cost, the Consolidated Statement of Changes in Net Position, the Combined Statement of Budgetary Resources and related notes for the FYs then ended.[1] The basic financial statements are the responsibility of Marine Corps management. The Marine Corps is also responsible for implementing effective internal control and for complying with laws and regulations. We are unable to express an opinion on the Department of the Navy Working Capital Fund-Marine Corps FY 2007 Financial Statements because of limitations on the scope of our work. Thus, the basic financial statements may be unreliable. In addition to our disclaimer of opinion on the basic financial statements, we are including the required Report on Internal Control and Compliance with Laws and Regulations. The Report on Internal Control and Compliance with Laws and Regulations is an integral part of our disclaimer of opinion on the financial statements and should be considered in assessing the results of our work.

Disclaimer of Opinion on the Financial Statements

The United States Marine Corps Director, Fiscal Division acknowledged to us that the Department of the Navy Working Capital Fund-Marine Corps FY 2007 Financial Statements would not substantially conform to accounting principles generally accepted in the United States of America (GAAP), and that the Department of the Navy Working Capital Fund-Marine Corps financial management and feeder systems were unable to adequately support material amounts on the financial statements as of September 30, 2007. Section 1008(d) of the FY 2002 National Defense Authorization Act limits the Department of Defense Inspector General to performing only those audit procedures required by generally accepted government auditing standards that are consistent with the representations made by management. Therefore, we did not perform auditing procedures required by U.S. Government auditing standards and Office of Management and Budget (OMB) Bulletin No. 07-04 to determine whether material amounts on the financial statements were fairly presented. The United States Marine Corps Director, Fiscal Division, has acknowledged material internal control weaknesses identified in the Summary of Internal Control. These pervasive material weaknesses may affect the reliability of certain information contained in the annual financial statements --much of which is taken from the same data sources

[1] Beginning in FY 2007, OMB Circular A-136 requires entities to present the Statement of Financing as a note. It is no longer considered a basic statement.

as the basic financial statements.[2] Therefore, we are unable to express, and we do not express, an opinion on the basic financial statements. Further, the purpose of the audit was not to express an opinion on Management Discussion and Analysis, Required Supplementary Information, Other Accompanying Information, and Performance Measures accompanying the basic financial statements. Accordingly, we express no opinion on that information.

Summary of Internal Control

In planning our work, we considered Department of the Navy Working Capital Fund-Marine Corps internal controls over financial reporting and compliance with applicable laws and regulations. We did this to determine our procedures for auditing the financial statements and to comply with OMB guidance, but our purpose was not to express an opinion on internal control. Further, we do not express an opinion on internal control over financial reporting and compliance with applicable laws and regulations.

A material weakness is a significant deficiency, or a combination of significant deficiencies, resulting in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected.[3]

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or a combination of control deficiencies, adversely affecting the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with GAAP. The following list identifies significant deficiencies, all of which are material.

- **Financial Management Systems**
- **Fund Balance with Treasury**
- **Inventory and Related Property, Net**
- **General Property, Plant, and Equipment**
- **Statement of Net Cost**
- **Accounts Receivable**
- **Other Assets**
- **Accounts Payable**
- **Other Liabilities**
- **Statement of Budgetary Resources**
- **Statement of Changes in Net Position**
- **Consolidation Procedures**

[2] The annual financial statements include the basic financial statements, Management Discussion and Analysis, Required Supplementary Information, and Other Accompanying Information.

[3] The term "remote" is defined as "the chance of the future event or events occurring is slight." Therefore, the likelihood of an event is "more than remote" when it is at least reasonably possible.

Our internal control work would not necessarily disclose all significant deficiencies. The Attachment offers additional details on significant deficiencies, all of which we consider to be material internal control weaknesses.

Summary of Compliance with Laws and Regulations

Our work to determine compliance with selected provisions of applicable laws and regulations related to financial reporting was limited because management acknowledged that instances of noncompliance identified in prior audits continue to exist. The United States Marine Corps Director, Fiscal Division acknowledged to us that the Department of the Navy Working Capital Fund-Marine Corps financial management systems do not substantially comply with Federal financial management system requirements, GAAP, and the U.S. Government Standard General Ledger at the transaction level. Therefore, we did not determine whether Marine Corps was in compliance with all applicable laws and regulations related to financial reporting. Providing an opinion on compliance with certain provisions of laws and regulations was not an objective of our audit and, accordingly, we do not express such an opinion. See the Attachment for additional details on compliance with laws and regulations.

Management's Responsibilities

Management is responsible for:

- preparing the financial statements in conformity with GAAP;
- establishing, maintaining, and assessing internal controls to provide reasonable assurance that the broad control objectives of the Federal Managers' Financial Integrity Act are met; and
- complying with applicable laws and regulations.

We provided a draft copy of this report to personnel at the Office of the Assistant Deputy Commandant for Programs and Resources (Fiscal) of the United States Marine Corps, who provided no comments, but expressed their continuing commitment to address the problems this report outlines.

Paul J. Granetto, CPA
Assistant Inspector General and Director
Defense Financial Auditing
Service

Attachment:
As stated

Report on Internal Control and Compliance with Laws and Regulations

Internal Control

Management is responsible for implementing and maintaining effective internal control and for providing reasonable assurance that accounting data are accumulated, recorded, and reported properly; that the requirements of applicable laws and regulations are met; and that assets are safeguarded against misappropriation and abuse. Our purpose was not to, and we do not, express an opinion on internal control over financial reporting. However, we have identified the following material weaknesses and significant deficiencies that could adversely affect the Marine Corps financial management operations.

Material Weaknesses Identified During FY 2007. As a result of our financial-related work during FY 2007, we identified significant deficiencies, all of which are material.

Financial Management Systems. The legacy financial management systems and feeder systems are not fully compliant with the Federal financial management system requirements, GAAP, and the U.S. Government Standard General Ledger at the transaction level.

Fund Balance with Treasury. The Navy Working Capital Fund-Marine Corps cash account balance is not reconciled to the Treasury cash account balance on a consistent basis to include rationale and verification of posting accounts. The lack of direct automated information system interfaces between the official financial reporting system and one or more feeder systems causes difficulties in the reconciliation process. As a result, accounting personnel must use unmatched disbursements, abnormal balances, and unsupported journal voucher entries to reconcile Treasury records.

Inventory and Related Property, Net. Legacy and migratory feeder systems supporting the Navy Working Capital Fund-Marine Corps financial management systems were not designed with all requirements to meet the historical cost data outlined in the Statement of Federal Financial Accounting Standards No. 3, "Accounting for Inventory and Related Property." In addition, while these systems provide controls to ensure accountability and visibility of inventory, they were designed to record issue and receipt of inventory at standard unit price/latest acquisition cost instead of moving average cost. In order to comply with Statement of Federal Financial Accounting Standards, latest acquisition cost should be converted to moving average cost. Adequate data, processes and methodologies do not exist to make these conversions accurately and in a manner allowing auditors to verify the resulting inventory balances.

General Property, Plant, and Equipment. The Marine Corps has identified this area as a material deficiency and has begun its discovery process for this line.

Statement of Net Cost. The Marine Corps has identified this area as a material deficiency and has begun its discovery process for this line.

Accounts Receivable. Subsidiary records are not reconciled to their corresponding general ledger accounts on a regular basis, thus resulting in an internal control weakness and the loss of the audit trail. In addition, difficulties exist with trading partner adjustments being posted to intergovernmental accounts receivable primarily because of communication problems with trading partners and the lack of a process to ensure that the Marine Corps, instead of the Department of the Navy, is identified as the payee of record for services rendered.

Other Assets. The Marine Corps has identified this area as a material deficiency and has begun its discovery process for this line.

Accounts Payable. This line has been adversely affected by inconsistent reconciliations and insufficient supporting documentation, lack of directly interfaced information systems, and erroneous trading partner information. The results of this are unmatched or unreconciled records (including at the Treasury level), mandated journal voucher posting, and unsupported validation of transactions. Unmatched disbursements are transferred to accounts payable using a journal voucher manual document which is not substantiated with supporting documentation, thus leaving no audit trail and causing abnormal balances. During the 2nd Quarter of FY 2007, DoD and the Defense Finance and Accounting Service identified debt related to suspended revenue owed to other departments. Defense Finance and Accounting Service is currently posting a manual journal voucher for this debt on a quarterly basis. The Marine Corps cannot validate the debt for payment since insufficient information has been provided.

Other Liabilities. Unsupported, undistributed disbursements need to be resolved.

Statement of Budgetary Resources. Multiple deficiencies exist within the Statement of Budgetary Resources. For example, the implementation of automated information systems such as the Defense Travel System, Purchase Request Builder and the Standard Procurement System has identified problems with electronic data feeds to the various accounting systems. The Marine Corps continues to work with Defense Finance and Accounting Service and other stakeholders to employ direct-feed transactions from the various feeder systems to the Defense Industrial Financial Management System, as well as the Standard Accounting, Budgeting, and Reporting System.

Statement of Changes in Net Position. Prior period adjustments in the automated financial systems and updated guidance need to be reflected in this line. In addition, material weaknesses associated with the proper recording of accounts receivable and accounts payable have a direct impact on recording of revenues and expenses on the Statement of Net Cost and the Statement of Changes in Net Position.

Consolidation Procedures. The accuracy and reliability of the Navy Working Capital Fund-Marine Corps annual financial statements is adversely affected by journal vouchers prepared by Defense Finance and Accounting Service to adjust financial statement balances recording trading partner information provided on behalf of the Navy Working Capital Fund-Marine Corps. Specifically, journal vouchers for accounts payable, accounts receivable, prepayments, advances, earned revenue, transfers-in or transfers-out, operating expenses, net operating results, and cumulative operating results lack documentation and potentially are incomplete, inaccurate, or arbitrarily adjusted to agree with balances reported by other DoD and Federal civilian agencies.

These financial management deficiencies may cause inaccurate management information. As a result, United States Marine Corps management decisions based in whole or in part on this information may be adversely affected. Financial information reported by DoD may also contain misstatements resulting from these deficiencies.

Compliance with Laws and Regulations

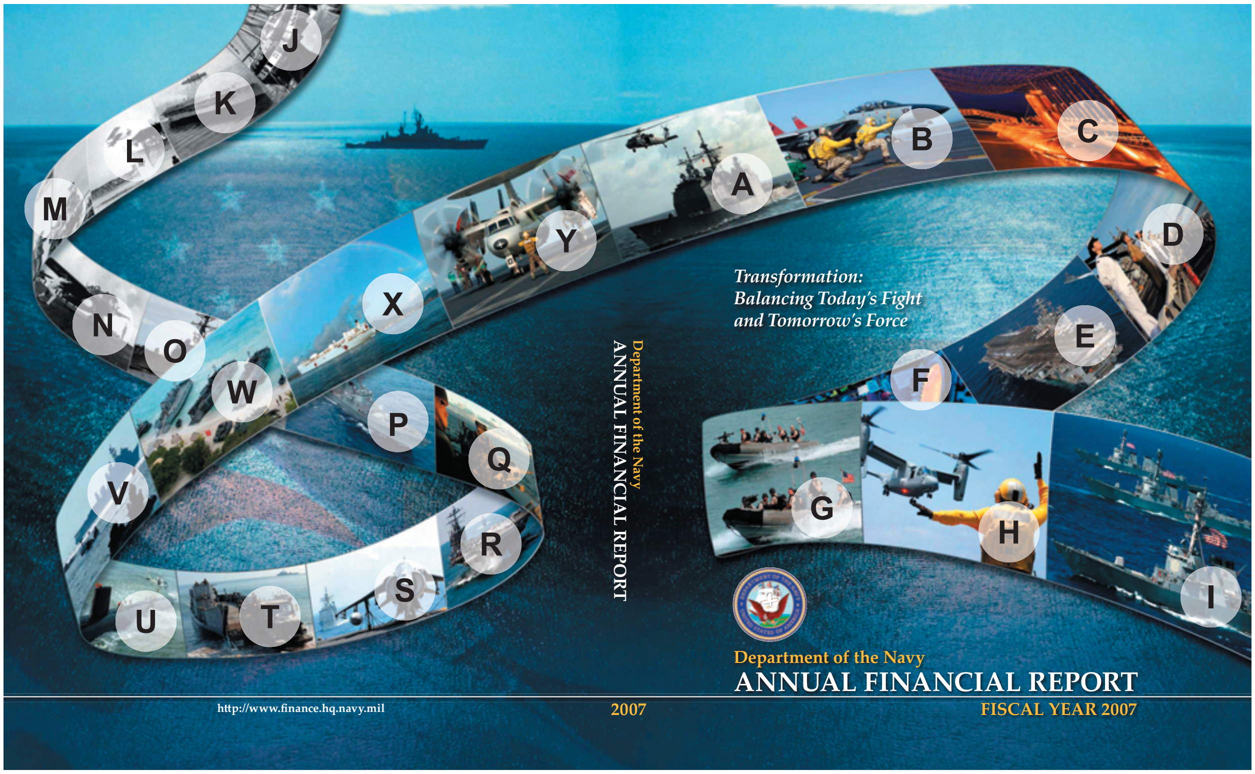
Management is responsible for compliance with existing laws and regulations related to financial reporting. Our work to determine compliance with selected provisions of the applicable laws and regulations was limited because management acknowledged instances of noncompliance, and previously reported instances of noncompliance continue to exist. Therefore, we did not determine whether the United States Marine Corps was in compliance with selected provisions of all applicable laws and regulations related to financial reporting. Our objective was not to, and we do not, express an opinion on compliance with applicable laws and regulations.

Federal Financial Management Improvement Act of 1996. The Federal Financial Management Improvement Act of 1996 requires DoD to establish and maintain financial management systems that comply substantially with Federal financial management system requirements, applicable Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level. For FY 2007, Marine Corps did not fully comply with Federal Financial Management Improvement Act of 1996. The Marine Corps acknowledged that many of its critical financial management and feeder systems did not substantially comply with Federal financial management system requirements, Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level as of September 30, 2007.

Audit Disclosures

The United States Marine Corps Director, Fiscal Division acknowledged to us on October 1, 2007, that the Department of the Navy Working Capital Fund-Marine Corps financial management and feeder systems cannot provide adequate evidence supporting various material amounts on the financial statements, and previously identified material weaknesses continue to exist. Therefore, we did not perform detailed testing related to previously identified material weaknesses. In addition, we did not perform audit work related to the following selected provisions of laws and regulations: Provisions Governing Claims of the United States Government (including provisions of the Debt Collection Improvement Act), Federal Credit Reform Act, the Pay and Allowance System for Civilian Employees, Prompt Payment Act, and the Antideficiency Act.

This report does not include recommendations to correct the material internal control weaknesses and instances of noncompliance with laws and regulations because either previous audit reports contained recommendations for corrective actions or audit projects currently in process will include appropriate recommendations.



The cover of the FY 2007 Department of the Navy Annual Financial Report depicts the transformation of the U.S. Navy and the U.S. Marine Corps over the last 152 years.

FRONT COVER

Images from top to bottom, left to right:

A: Arabian Sea (May 15, 2007) – USS Antietam (CG 54) and an MH-60S Seahawk from Helicopter Sea Combat Squadron (HSC) 23 are headed to the USNS Bridge (T-AOE 10) for a replenishment at sea. *U.S. Navy photo by Mass Communication Specialist 3rd Class Paul J. Perkins*

B: Persian Gulf (Feb. 7, 2006) – An F-14D Tomcat assigned to Fighter Squadron Three One (VF-31) is launched off the flight deck of the Nimitz-class aircraft carrier USS Theodore Roosevelt (CVN 71). *U.S. Navy photo by Photographer's Mate 3rd Class Michael D. Cole*

C: Silverdale, Washington (Aug. 16, 2006) – The Sea Wolf-class attack submarine USS Jimmy Carter (SSN 23) sits moored in the Magnetic Silencing Facility at Naval Base Kitsap Bangor. *U.S. Navy photo by Master Chief Mass Communication Specialist Jerry McLain*

D: Townsville, Australia (July 4, 2007) – Sailors and Marines man the rails aboard amphibious assault ship USS Essex (LHD 2). *U.S. Navy photo by Mass Communication Specialist 2nd Class Corey Truax*

E: Caribbean Sea (May 11, 2006) – Two F/A 18 Super Hornets launch simultaneously from the flight deck of the Nimitz-class aircraft carrier USS George Washington (CVN 73). *U.S. Navy photo by Photographer's Mate 3rd Class Michael D. Blackwell II*

F: Philippine Sea (June 21, 2006) – Shown is the Combat Information Center aboard the Ticonderoga-class guided missile cruiser USS Mobile Bay (CG 53). *U.S. Navy photo by Photographer's Mate Airman James R. Evans*

G: Persian Gulf (May 15, 2007) – Sailors approach the guided-missile destroyer USS Preble (DDG 88) in rigid hull inflatable boats. *U.S. Navy photo by Mass Communication Specialist 3rd Class Ron Reeves*

H: Atlantic Ocean (May 22, 2007) – An Aviation Boatswain's Mate Handling 2nd Class guides an MV-22 Osprey onto the flight deck of amphibious assault USS Kearsarge (LHD 3). *U.S. Navy photo by Mass Communication Specialist 2nd Class Oscar Espinoza*

I: Pacific Ocean (June 18, 2006) – Three Arleigh Burke-class guided-missile destroyers, the USS McCampbell (DDG 85), USS Lassen (DDG 82), and USS Shoup (DDG 86), steam in formation. *U.S. Navy photo by Chief Photographer's Mate Todd P. Cichonowicz*

BACK COVER

Images from top to bottom, left to right:

J: Annapolis, Maryland (Oct. 28, 2004) – The Civil War era warship Constellation is shown moored at the U.S. Naval Academy. The Constellation was commissioned on July 28, 1855 and is undergoing restoration. *U.S. Navy photo by Don S. Montgomery*

K: San Diego, California (1928) – USS Langley (CV-1) is shown underway with Vought VE-7 aircraft on her flight deck. Collection of Lieutenant Gustave J. Freret, USN (Retired), 1972. *U.S. Naval Historical Center photograph*

L: San Diego, California (1925) – A Douglas DT-2 airplane takes off from the flight deck of the USS Langley (CV-1) at Naval Air Station, North Island. *U.S. Naval Historical Center photograph*

M: Mount Suribachi, Iwo Jima (Feb. 23, 1945) – Marines of the 28th Regiment, Fifth Marine Division, hoist the U.S. flag at the summit of Mount Suribachi. This photo was taken by Staff Sergeant Louis R. Lowery, USMC staff photographer for *Leatherneck* magazine seventeen minutes before the famous flag-raising was immortalized by Associated Press photographer Joe Rosenthal. *Official U.S. Marine Corps photograph from the collections of the Naval Historical Center*

N: (1945) – An FM-2 "Wildcat" fighter prepares to launch from the USS Makin Island (CVE-93). Courtesy of PHC John Highfill, USN (Retired). *U.S. Naval Historical Center photograph*

O: Atlantic Ocean (April 14, 2007) – Guided missile destroyer USS Laboon (DDG 58) is shown in transit. *U.S. Navy photo by Mass Communication Specialist Seaman Coleman Thompson*

P: Pacific Ocean (May 1, 2007) – Guided missile destroyer USS Milius (DDG 69) steams in formation. *U.S. Navy photo by Mass Communication Specialist Seaman Mark Patterson II*

Q: Pacific Ocean (Jan. 15, 2006) – An Aviation Ordnanceman 3rd Class mans a MK-38 25mm machine gun aboard the amphibious assault ship USS Peleliu (LHA 5). *U.S. Navy photo by Journalist 2nd Class Zack Baddorf*

R: Atlantic Ocean (April 6, 2007) – Nimitz-class aircraft carrier USS Harry S. Truman (CVN 75) transits the Atlantic. *U.S. Navy photo by Mass Communication Specialist 2nd Class Jay C. Pugh*

S: Atlantic Ocean (June 20, 2007) – An AV-8B Harrier rests on the flight deck of amphibious assault ship USS Kearsarge (LHD 3). *U.S. Navy photo by Mass Communication Specialist Seaman Derek Poole*

T: Cifuncho, Chile (May 29, 2007) – The 24th Marine Regiment arrives on land to conduct live fire exercises with their Chilean counterparts. *U.S. Navy photo by Mass Communication Specialist 2nd Class Lenny M. Francioni*

U: Atlantic Coast (Jan. 17, 2005) – A SEAL delivery vehicle team performs a fast-roping exercise from an MH-60S Seahawk helicopter to the topside of Los Angeles-class fast attack submarine USS Toledo (SSN 769). *U.S. Navy photo by Journalist 3rd Class Davis J. Anderson*

V: Philippine Sea (March 8, 2006) – U.S. Marine Corps armored amphibious vehicles from the 2nd Battalion, 5th Marine Regiment, Battalion Landing Team leave the beach on the island of Iwo Jima to return to the amphibious dock landing ship USS Harpers Ferry (LSD 49). *U.S. Navy photo by Journalist 2nd Class Brian P. Biller*

W: Curacao, Netherlands Antilles (June 6, 2006) – Amphibious Craft Unit Two (ACU-2) rehearse storming the beach. *U.S. Navy photo by Photgrapher's Mate 3rd Class Jeremy L. Grisham*

X: Jolo, Philippines (June 8, 2006) – Military Sealift Command Hospital ship USNS Mercy (T-AH 19) is shown anchored off the coast of Jolo City. *U.S. Navy photo by Chief Photographer's Mate Edward G. Martens*

Y: Persian Gulf (May 24, 2007) – An Aviation Boatswain's Mate 3rd Class taxies an E-2C Hawkeye aboard nuclear-powered aircraft carrier USS Nimitz (CVN 68). *U.S. Navy photo by Mass Communication Specialist Seaman Apprentice John Scorza*

*Special thanks to **Rear Admiral Frank Thorp IV**, Chief of Naval Information; **Mr. Christopher Madden**, Director of the Navy Visual News Service; **Lieutenant Christopher Bishop**, Deputy Director of the Navy Visual News Service; and the **staff of the Office of the Chief of Naval Information** for providing the Department of the Navy photographs.*

Many thanks also to the Financial Operations Team at the Department of the Navy (DON) Office of Financial Operations, the extended financial community at the DON major commands, and our accounting partners at the Defense Finance and Accounting Service for their dedicated time and effort in producing the Fiscal Year 2007 Department of the Navy Annual Financial Report. The Fiscal Year 2007 Department of the Navy Annual Financial Report is dedicated once again to the men and women of our Navy and Marine Corps war-fighting team.