

2012

Fiscal Year 2012 United States Air Force Agency Financial Report





THE AIRMAN'S CREED

I AM AN AMERICAN AIRMAN.

I AM A WARRIOR.

I HAVE ANSWERED MY NATION'S CALL.

I AM AN AMERICAN AIRMAN.

MY MISSION IS TO FLY, FIGHT, AND WIN.

I AM FAITHFUL TO A PROUD HERITAGE,

A TRADITION OF HONOR, AND A LEGACY OF VALOR.

I AM AN AMERICAN AIRMAN,

GUARDIAN OF FREEDOM AND JUSTICE,

MY NATION'S SWORD AND SHIELD,

ITS SENTRY AND AVENGER.

I DEFEND MY COUNTRY WITH MY LIFE.

I AM AN AMERICAN AIRMAN:

WINGMAN, LEADER, WARRIOR.

I WILL NEVER LEAVE AN AIRMAN BEHIND,

I WILL NEVER FALTER, AND I WILL NOT FAIL.

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November 2012

Message from the Secretary of the Air Force

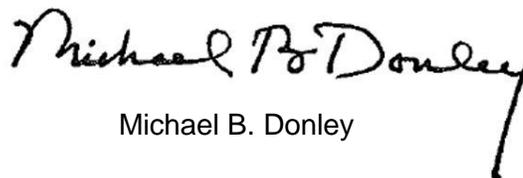


I am pleased to present the Air Force Annual Financial Report for Fiscal Year 2012 (FY 12). The Annual Financial Report details how the Air Force is using budgeted resources to deliver our Nation's air, space, and cyber defense capability. It also provides an overview of the Air Force's achievements, objectives, and challenges.

The Air Force is striving to reach audit readiness and is fully committed to meeting Secretary Panetta's directive to produce an auditable Statement of Budgetary Resources by FY14 and to have all financial statements auditable by FY17. Improving the accuracy, reliability, and timeliness of financial information promotes better decision making at every level. Submitting financial statements that have passed the scrutiny of an independent audit will demonstrate to Congress, the President, and the American people that the funds entrusted to us are spent prudently.

As our Nation continues its focus on economic recovery, the Air Force is placing emphasis on achieving internal efficiencies within our budget. We must continue to provide the essential force structure and capabilities on which our Nation depends, and be ready to respond to a challenging and dynamic security environment. Making far-sighted decisions now on how to best utilize our resources will position the Air Force for success in the future. As we make these difficult budget decisions, taking care of our Airmen will remain a top priority.

We are mindful of the current fiscal situation that our Nation faces and recognize that the Air Force must do its part to support getting our economic house in order. Whatever the future brings, we know that the members of our Total Force are up to the challenge and that *Integrity, Service, and Excellence* will continue to be our guiding principles.


Michael B. Donley



November 2012

**Message from the Principal Deputy Assistant Secretary
of the Air Force for Financial Management and Comptroller
(Performing as SAF/FM)**



The Air Force Annual Financial Statement for Fiscal Year 2012 reports the Air Force's financial position and results of operations. It provides Congress, Department of Defense (DoD) leadership, and the American taxpayers with information on the financial status of the Air Force. The Air Force financial management staff is working diligently to improve financial management processes and systems to reach our goal of producing financial statements which are auditable by an independent public audit firm in accordance with the priorities identified by the Department of Defense.

In October 2011, Secretary Panetta accelerated the deadline for having an auditable Statement of Budgetary Resources (SBR) to FY 2014. The Air Force has made considerable progress towards achieving this goal. As a test of our ability to audit a major acquisition program, we asserted audit readiness for the Space Based Infrared System, an advanced missile warning satellite constellation, two months ahead of schedule. The Air Force also asserted Budgetary Funds Distribution to base level.

The accelerated deadline requires the Air Force to assert the SBR before our new enterprise resource planning system, the Defense Enterprise Accounting and Management System (DEAMS), is fully implemented. While we will continue to rely on DEAMS for achieving sustainable auditability and financial system modernization over the medium-term, we are simultaneously working to advance audit readiness within the current legacy system environment by improving internal controls and financial processes.

Secretary Panetta has also directed the department to increase its emphasis on accountability of mission critical assets. In June, the DoD Inspector General (IG) issued a clean examination opinion on Air Force aircraft, intercontinental ballistic missiles, satellites, cruise missiles, and aerial targets and drones. The combined value of these assets is approximately \$86 billion, which represents 41 percent of the Air Force's mission critical assets and 14 percent of DoD mission critical assets. The DoD IG is currently examining the Air Force assertion of spare engines and uninstalled missile motors and initial testing was completed for Real Property.

Auditable financial statements will provide the transparency necessary to demonstrate good stewardship of the funds entrusted to us. We remain committed to providing the war fighter with the resources needed to fly, fight, and win in air, space and cyberspace while maintaining excellence in fiscal accountability.

A handwritten signature in cursive script that reads "Marilyn M. Thomas".

Marilyn M. Thomas



Air Force Vision

“The United States Air Force will be a trusted, reliable joint partner with our sister services known for integrity in all of our activities, including supporting the joint mission first and foremost. We will provide compelling air, space, and cyber capabilities for use by the Combatant Commanders. We will excel as stewards of all Air Force resources in service to the American people, while providing precise and reliable Global Vigilance, Reach and Power for the nation.”

Air Force Mission

The mission of the United States Air Force is to
fly, fight and win...in air, space and cyberspace.



Air Force in Action--FY 2012

Since the first clash of battle, warriors have relied on breaking through the lines to achieve victory. However, once the airplane was used over the battlefields of World War I, the battle itself was forever revolutionized. In the 65 years since the establishment of the United States Air Force as a separate Service, our technological, strategic, and tactical innovations have played an important role in shaping the way the United States engages in war, deters aggression, and maintains peace. The Air Force has pioneered advancements that have been essential in ensuring our nation's security while reducing combat casualties. As the Department of Defense faces fiscal pressures and an evolving strategic environment, America will continue to depend on the Air Force to contribute innovative strategies and systems to conduct our most important military missions.

During the past decade, the United States has engaged in a prolonged war aimed at disrupting, dismantling and defeating al-Qa'ida and its network. A major part of this effort involved a long-term and large-scale presence on the ground. The withdrawal of combat forces from Iraq and the drawdown in Afghanistan signal the beginning of a new chapter for America in which we will rely more heavily on airpower to complement innovative, lower-cost, lighter footprint approaches around the world. As the Nation sustains its global presence with a renewed emphasis on the Asia-Pacific region, in addition to continued focus on the Middle East, we must maintain the best military in the world—a force capable of deterring conflict, a force capable of projecting power, and a force capable of winning wars. We will preserve the capability and expertise in irregular warfare that we developed over the past decade and we will invest in fielding appropriate amounts of new and existing military capabilities in order to meet the national security challenges of today and the future.

In June 2010, the Secretary of Defense challenged the Services to increase funding for mission activities by identifying efficiencies in overhead, support and other less mission-essential areas. The efficiency target for the Air Force was \$28.3 billion across the Future Years Defense Program (FYDP). The Air Force is committed to enhancing capabilities by reducing expenses allocated to overhead and support functions, while shifting resources to modernization and readiness programs.

As part of the FY12 budget, the Air Force exceeded our efficiency target by \$5 billion and identified \$33.3 billion in efficiencies in an effort to make resources available to better support warfighter and readiness programs across the FYDP. Examples of these efficiencies include:

- Consolidating installation support management to improve Air Force-wide standardization and prioritization;
- Reducing fuel consumption by leveraging proven commercial aviation practices for flight planning and weight reduction;
- Reducing acquisition costs by consolidating services, scrutinizing contracts, and reducing contract support;
- Improving our procurement of satellites with a new acquisition strategy which will lower procurement costs and stabilize the defense industrial base.

The realization of these efficiencies allowed the Air Force to reallocate funding to modernize and recapitalize weapons systems, improve capabilities and enhance warfighter operations. Examples include:

- Investing in the Long-Range Strike Family of Systems, including a new penetrating bomber as a key component of the Joint portfolio;
- Repurposing 5,600 active duty billets to support ISR capability, including the U-2 continuation
- Procuring an additional 16 simulators for F-35 aircrew training;
- Recapitalizing aging aircraft;
- Improving aircraft computer infrastructure;

All of this is possible with the multi-talented Total Force. The overall programmed Air Force end strength for FY 2012 is more than 693,540 personnel. This includes 328,800 active duty, 75,840 Reserve, 106,700 Air National Guard, and 182,200 civilian personnel. The Secretary of Defense has limited our civilian workforce to FY 2010 levels, with limited growth allowed for specific priorities like the acquisition workforce. The Air Force conducted an enterprise-wide review of civilian personnel end strength and, to facilitate DoD's efforts for efficiencies and reinvestment possibilities, offered early retirement to those eligible civilian personnel. At the completion of this effort, the Air Force anticipates meeting its manning restrictions without adverse displacement of the civilian workforce.

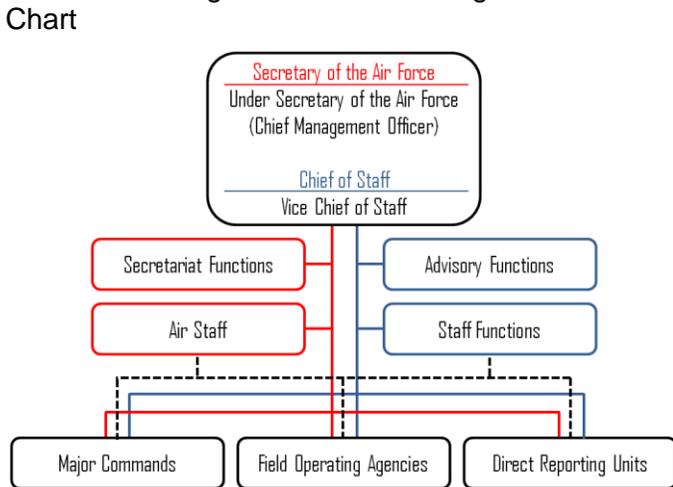
“Although we will be smaller and leaner, we will not sacrifice readiness.”

Secretary of the Air Force Michael B. Donley

Air Force Structure

The command line of the Air Force flows from the President and the National Command Authority to the Secretary of Defense and the Department of the Air Force. The Air Force is headed by the Secretary of the Air Force (SECAF), with the Chief of Staff reporting to the Secretary (see Figure 1). Immediately subordinate to the departmental headquarters are the Major Commands (MAJCOMs), Field Operating Agencies (FOAs), Direct Reporting Units (DRUs), and the Auxiliary.

Figure 1: Air Force Organization Chart



Major Command Structure

Most units of the Air Force are assigned to a specific major command (MAJCOM), led by a general officer. MAJCOMs have extensive functional responsibilities as will be shown on the following pages. They may be subdivided into Numbered Air Forces (NAF) with each responsible for one or more wings or independent groups.

Wings are the primary units of the working Air Force and are responsible for maintaining an Air Force base or carrying out a specific mission. Wings may be commanded by a general officer or a colonel. A wing may have several squadrons in more than one dependent group. Wings typically contain an operations group, a maintenance group, a support group and a medical group.

The majority of individual officers and Airmen are assigned to a squadron, which may be composed

of several flights. Additionally, there are other types of organizations in the Air Force structure such as centers, field operating agencies and direct reporting units.

Air Combat Command (ACC)



Mission: Air Combat Command is the primary force provider of combat airpower to America’s warfighting commands.

Responsibilities: To support global implementation of national security strategy, ACC operates fighter, bomber, reconnaissance, battle-management, and electronic-combat aircraft. It also provides command, control, communications and intelligence systems, and conducts global information operations.

As a force provider, ACC organizes, trains, equips and maintains combat-ready forces for rapid deployment and employment while ensuring strategic air defense forces are ready to meet the challenges of peacetime air sovereignty and wartime air defense. ACC numbered air forces provide the air component to the Central, Southern and Northern Combatant Commands. ACC also augments forces to the European, Pacific, and Strategic Combatant Commands.

Command Personnel: 153,000



Air Force Thunderbirds (F-16) perform above Turku Airport, Finland



Air Education and Training Command (AETC)



Mission: Develop America’s Airmen today.....for tomorrow.

Responsibilities: With a vision to deliver unrivaled air, space and cyberspace education and training, the command recruits Airmen and provides basic military training, initial and advanced technical training, flying training, medical training, space and missile training, cyber training, and professional military and degree-granting professional education. The command also conducts joint, readiness and Air Force security assistance training. AETC’s role makes it the first command to touch the life of nearly every Airman.

Command Personnel: 65,960

Air Force Global Strike Command (AFGSC)



Mission: Develop and provide combat-ready forces for nuclear deterrence and global strike operations ... *Safe, Secure, Effective*, to support the President of the United States and combatant commanders.

Responsibilities: Organize, train and equip the Air Force’s three intercontinental ballistic missile wings, two B-52 Stratofortress wings and the single B-2 Spirit wing. The three weapons systems make up two-thirds of the nation’s strategic nuclear triad by providing the land-based and airborne nuclear deterrent forces.

Command Personnel: 24,983

Air Force Materiel Command (AFMC)



Mission: Deliver technology, acquisition, test, sustainment and expeditionary capabilities to the warfighter.

Responsibilities: AFMC delivers war-winning expeditionary capabilities to the warfighter through development and transition of technology, professional acquisition management, exacting test and evaluation, and world-class sustainment of all Air Force weapon systems. From cradle-to-grave, AFMC provides the work force and infrastructure necessary to ensure the United States remains the world’s most respected Air and Space Force.

Command Personnel: 81,956

Air Force Reserve Command (AFRC)



Mission: To provide combat ready forces to fly, fight, and win in air, space, and cyberspace.

Responsibilities: The AFRC augments the active component. The AFRC is extremely cost effective and retains valuable military expertise and mission continuity on a ready-now, but called-up as needed basis. Reserve units are staffed and trained to meet the same training standards and readiness levels as the active component forces, and are supplied with the same equipment on an equal priority. Because Reservists are community neighbors and civilian employees in society, many Americans who interact with them have a better understanding of the Armed Forces and military service.

Command Personnel: 75,747



Air Force Space Command (AFSPC)

Mission: Provide resilient and cost-effective space and cyberspace capabilities for the joint force and the nation.

Responsibilities: Organizing, equipping, training and maintaining mission-ready space and cyberspace forces and capabilities for North American Aerospace Defense Command, U.S. Strategic Command and other combatant commands world-wide. AFSPC oversees Air Force network operations to provide capabilities in, through, and from cyberspace; manages a global network of satellites, and is responsible for space system development and acquisition. It executes spacelift to launch satellites with a variety of expendable launch systems and operates them to provide space capabilities in support of combatant commanders around the clock. It provides positioning, navigation, timing, communications, missile warning, weather and intelligence warfighting support.

AFSPC operates sensors that provide direct attack warning and assessment to U.S. Strategic Command and North American Aerospace Defense Command. The command develops, acquires, fields, operates and sustains space systems and fields and sustains cyber systems.

Command Personnel: 42,000

Air Mobility Command (AMC)



Mission: Provide global air mobility ... right effects, right place, right time.

Responsibilities: AMC Airmen — active duty, Air National Guard, Air Force Reserve and civilians — provide airlift and aerial refueling for all of America’s armed forces. They also provide aeromedical evacuation and Global Reach laydown. The command has many special duty and operational support aircraft and plays a crucial role in providing humanitarian support at home and around the world.

Command Personnel: 133,975



C-5M Super Galaxy transports two M-1 Abrams tanks.



Air National Guard (ANG)

Mission: The Air National Guard has both a federal and state mission. The dual mission, a provision of the U. S.

Constitution, results in each guardsman holding membership in the National Guard of his or her state and in the National Guard of the United States.

Federal Mission: Maintain well-trained, well-equipped units available for prompt mobilization during war and provide assistance during national emergencies, such as natural disasters or civil disturbances. During peace, the combat-ready units and support units are assigned to Air Force major commands to carry out missions compatible with training, mobilization readiness, humanitarian and contingency operations. ANG provides almost half of the Air Force’s tactical airlift support, combat communications functions, aeromedical evacuation and aerial refueling. In addition, ANG has total responsibility for air defense of the entire United States.

State Mission: When ANG units are not mobilized or under federal control, they report to the governor of their respective state, territory or the commanding general of the District of Columbia National Guard. Under state law, ANG provides protection of life and property, and preserves peace, order and public safety through emergency relief support during natural disasters, search and rescue operations, support to civil defense authorities, maintenance of vital public services and counterdrug operations.

Responsibilities: The Air National Guard provides tactical airlift, air refueling tankers, general purpose fighters, rescue and recovery capabilities, tactical air support, weather flights, strategic airlift, special operations capabilities and aeromedical evacuation units.

Command Personnel: 106,700



Pacific Air Forces (PACAF)

Mission: Provide Pacific Command integrated expeditionary Air Force capabilities to defend the homeland, promise stability, dissuade/deter aggression, and swiftly defeat enemies.

Responsibilities: PACAF’s area of responsibility extends from the west coast of the United States to the east coast of Africa and from the Arctic to the Antarctic, covering more than 100 million square miles. The area is home to 50 percent of the world’s population in 36 nations and over one-third of the global economic output. The unique location of the strategic triangle (Hawaii-Guam-Alaska) gives our nation persistent presence and options to project U.S. airpower from sovereign territory.

Command Personnel: 43,623

U.S. Air Forces in Europe (USAFE)



Mission: As the air component for both U.S. European Command (USEUCOM), and U.S. Africa Command (USAFRICOM), USAFE

directs air operations in a theater spanning three continents, covering more than 19 million square miles, containing 105 independent states, and possessing more than a quarter of the world’s population and more than a quarter of the world’s Gross Domestic Product.

Responsibilities: USAFE is an Air Expeditionary Force with a mobile and deployable mix of people and resources that can simultaneously operate in multiple locations. Its role in Europe and Africa has



expanded from warfighting to include humanitarian and peacekeeping operations, as well as other non-traditional contingencies throughout its area of responsibility. In peacetime, USAFE trains and equips U.S. Air Force units pledged to the North Atlantic Treaty Organization (NATO).

Command Personnel: 36,763



Air Force Special Operations Command (AFSOC)

Mission: America’s specialized air power — a step ahead in a changing world, delivering special operations power anytime, anywhere.

Responsibilities: Air Force Special Operations Command provides Air Force special operations forces (SOF) for worldwide deployment and assignment to combatant commands. The command’s SOF are composed of highly trained, rapidly deployable airmen, conducting global special operations missions ranging from precision application of firepower, to infiltration, exfiltration, resupply, and refueling of SOF operational elements.

The command’s core missions include battlefield air operations; agile combat support; aviation foreign internal defense; information operations; precision aerospace fires; psychological operations; specialized air mobility; specialized refueling; and intelligence, surveillance and reconnaissance.

Command Personnel: 17,820



CV-22 Osprey, Hurlbert Field, Fla. (Search & Rescue)

Direct Reporting Unit (DRU)

A DRU is a subdivision of the Air Force that is directly subordinate to Headquarters Air Force, separate from any MAJCOM or FOA because of a unique mission, legal requirements, or other factors. DRUs have the same administrative and

organizational responsibilities as MAJCOMs. The DRUs are the Air Force Academy, Air Force District of Washington, and Air Force Operational Test and Evaluation Center.

Civil Air Patrol (CAP)



Mission: Support America’s communities with emergency response, diverse aviation and ground service, youth development and promotion of air and space power.

Responsibilities: Civil Air Patrol provides operational capabilities in support of aerial and ground search and rescue disaster relief and counterdrug and homeland security missions. It conducts 90 percent of all inland search-and-rescue missions tasked by the Air Force Rescue Coordination Center. It builds strong citizens for the future by providing leadership training, technical education, scholarships and career education to young men and women, ages 12 to 21, in the CAP cadet program. It promotes and supports aerospace education, both for its members and the general public, and conducts a national school enrichment program from K-12.

Personnel: 61,451

Field Operating Agency (FOA)

A FOA is a subdivision of the Air Force that carries out field activities under the operational control of a Headquarters U.S. Air Force functional manager. FOAs perform field activities beyond the scope of any of the MAJCOMs. Examples of FOAs include the Air Force Audit Agency, Air Force Center for Engineering and the Environment, Air Force Financial Services Center, Air Force Services Agency, and Air Force Weather Agency, among others.

Air Force Resources

The three vital resources to successful accomplishment of the Air Force mission are:

Places: A network of bases that reflect the Air Force’s global competencies. The Air Force is a global force, spanning facilities both in the United States and around the world. The Air Force currently has 65 major bases in the continental United States and another 14 major bases outside the continental United States. The Air Force maintains an additional 79 minor bases, which are primarily used by the Air National Guard.

People: Trained, motivated, and dedicated. The Air Force consists of over 693,540 military and civilian personnel. Aerospace power is a proven necessity for victory on land, sea, air, space, and cyberspace. The foundation for this is our people. The reserve component (Air Force Reserve and Air National Guard) has become more important than ever in sustaining worldwide operations. These warriors make possible the successful accomplishment of Air Force missions.

Systems: Modern weapons platforms that integrate air, space, and cyber assets into an undefeatable force. Air Force “systems” no longer mean only “manned aircraft.” Systems also include space launch vehicles, satellites, intelligence, surveillance and reconnaissance assets, unmanned aerial systems, and the cohesive infrastructure to all Air Force systems. All Air Force systems are essential assets for Air Force people to accomplish the mission.

Management Assertions

We are mindful of the current fiscal situation and recognize that we must contribute to government-wide deficit reduction as a national security imperative. Our ability to make proper investments to modernize and sustain the capabilities of the Air Force is directly tied to the economic health of the United States. As stewards of the American taxpayer’s dollars, the Air Force is committed to achieving audit readiness and meeting Secretary Panetta’s accelerated goal to achieve auditability of the Statement of Budgetary Resources (SBR) by 2014.

Statutory Requirements

The Chief Financial Officers’ Act of 1990 requires the 24 largest federal agencies to prepare annual financial statements. The Government Management Reform Act of 1994 requires these financial statements to be audited. The DoD is striving to improve financial systems and processes so that it could undergo an audit without being disclaimed.

In a memorandum dated October 13, 2011, Secretary of Defense Panetta directed the DoD to accelerate audit readiness efforts. Specifically the Secretary called for the Department to:

- Achieve audit readiness of the SBR by the end of calendar year 2014.
- Increase emphasis on accountability of assets.

- Execute a full review of the Department’s financial controls over the next two years and establish interim goals against which to assess progress.
- Meet the legal requirements to achieve full audit readiness for all DoD financial statements by 2017.

Legal requirements in the National Defense Authorization Act of 2010 require the DoD to assert all financial statements as audit ready by September 30, 2017. The Department has developed an accelerated plan to asset the SBR as audit ready by 2014 and is committed to full audit readiness by 2017.

While these dates are a challenging deadline for a military organization as large and diverse as the Air Force, the strong engagement of senior leadership, additional financial resources provided in recent years, and a focus on fielding effective financial systems will help the Air Force achieve audit readiness. We are focusing our efforts on the information most relevant to decision makers, and the Air Force Financial Improvement Plan is closely aligned with the DoD strategy to achieve a clean audit opinion.

Progress Towards Auditability Statement of Budgetary Resources

During FY 2012, the Air Force continued to employ a strategy to achieve audit readiness of the SBR that focused on the lifecycle of appropriated funds. A methodology for achieving auditability of the SBR was developed by the Air Force with input and coordination from the Defense Finance and Accounting Service (DFAS). This methodology focused on assessable units that cover the fund receipt and distribution, obligation, outlay, reimbursement and reconciliation processes that impact the entire SBR.

In previous years the Air Force asserted audit readiness on Appropriations Received and Fund Balance with Treasury (FBWT) reconciliation process. An independent public accounting firm issued unqualified examination opinions in August 2011 and October 2011, respectively.

In April 2012, the Air Force released its *Statement of Budgetary Resources Audit Acceleration Plan*. Described within the plan is the Air Force’s resources and schedule to accomplish the Secretary of Defense’s goals of: (1) audit readiness of the SBR by the end of 2014. This plan revealed the collective expertise of functional leaders, key



stakeholder from Headquarters Air Force and Major Commands (MAJCOMs), representatives from the Office of the Under Secretary for Defense (Comptroller) and DFAS.

The Under Secretary of Defense (Comptroller) requested that each military service perform an assessment of a major acquisition program. For that reason, the Air Force asserted the Major Defense Acquisition Program (MDAP) as audit ready in 3rd quarter 2012, two months ahead of schedule. The Air Force selected the Space-Based Infrared System (SBIRS), an advanced space surveillance system. The objective of this assertion was to demonstrate financial stewardship of funds allotted for a major acquisition program and to determine that Appropriation Status by FY Program and Subaccount Report (the AR(M) 1002) serves as the basis for documenting and verifying the viability of the SBIRS's business processes. Funds distribution, obligations and expenditures were reviewed to determine that the amounts reported in the AR(M) 1002 were materially correct and were supported by the required documentation.

In the 4th quarter 2012, the Air Force asserted the funds distribution process from the MAJCOM level to base-level entities as audit ready.

Existence and Completeness (E&C)

The Air Force continues to execute a consistent strategy to achieve E&C audit readiness for mission-critical assets, with a specific focus on the validation of physical inventory documentation. The Air Force is also leveraging existing E&C field work performed by the Air Force Audit Agency (AFAA) to shorten the time required to draft primary assertion documentation and provide supporting physical inventory documentation and working papers.

Military equipment was asserted as audit ready in the 1st Quarter of FY 2011. Military equipment includes aircraft, inter-continental ballistic missiles, and satellites. This assertion was supported by physical inventory testing of selected aircraft assets in the Reliability and Maintainability Information System (REMIS). The test results indicate that the Air Force has highly effective internal controls over military equipment asset accountability.

Cruise missiles and aerial targets/drones, two sub-assessable units of Operating Materials and Supply, was asserted as audit ready in the 3rd quarter of FY 2011. AFAA performed physical inventory testing by selecting a representative sample of cruise missiles and aerial targets/drones

from REMIS. The test results indicate that the Air Force has effective internal controls over the accountability for cruise missiles and aerial target/drone assets.

In the 3rd quarter of FY 2012, the DoD Inspector General issued a clean examination opinion on military equipment, cruise missiles, and aerial targets/drones. The value of these assets is approximately \$86 billion, which represents 41 percent of Air Force mission critical assets and 14 percent of DoD mission critical assets.

During the 2nd quarter of FY 2012, the Air Force asserted spare engines and uninstalled missile motors as audit ready. These two assertions are undergoing DoD Inspector General examination and results are expected in November 2012.

Internal Controls

The Air Force operates a robust Managers' Internal Control Program in compliance with OMB Circular A-123 and the Government Accountability Office's standards for internal control. This program employs a comprehensive system of continuous evaluation of internal controls and is fully integrated with functional program control assessments used to help ensure that the goals of the Department of the Air Force are achieved each year. Under the guidance of the Office of the Under Secretary of Defense (Comptroller), the Secretary of the Air Force reports a level of assurance over its internal controls in three distinct areas: Internal Control over Nonfinancial Operations (ICONO), Internal Control over Financial Reporting (ICOFR), and Internal Control over Financial Systems (ICOFS).

Internal Control Over Financial Reporting

As directed in the Under Secretary of Defense (Comptroller) Memorandums dated August 2009, and the December 2011, Financial Improvement and Audit Readiness Guidance, the Air Force integrated FIAR methodology into ICOFR and focused on the strategic prioritization of the SBR and the existence and completeness (E&C) of mission critical assets. Under this plan, the Air Force completed ICOFR reviews as a part of existence and completeness audit ready assertions for elements of OM&S and the audit examination of military equipment. During FY 2012, the Air Force established sustainable valuation and reporting requirements for military equipment and validated the effectiveness of corrective actions to mitigate portions of the OM&S ICOFR material weakness. In addition, the Air Force evaluated the effectiveness of internal controls over the key

Procure to Pay and Order to Cash business processes utilizing the Department's newest financial management system, the Defense Enterprise Accounting Management System (DEAMS). This system will serve as the future enterprise core financial management solution enabling the Air Force to achieve financial statement audit readiness. This effort involved documenting key processes and internal controls, performing risk assessments, and testing and analyzing the effectiveness of the key controls consistent with OMB A-123, Appendix A. We continue to track and report on seven other previously identified ICofR material weaknesses that are included in the Secretary's Annual Statement of Assurance.

Continuous Improvement

The Air Force has issued a Commander's Checklist to assist commanders and directors in evaluating and reporting the organization's financial management effectiveness and audit readiness. Just as a command uses checklists to assess engineering, logistics, medical, and operational readiness before the next deployment, the Commander's Checklist assess an organization's financial readiness for upcoming financial audits. As the Air Force conducted the prescribed phases of discovery and evaluation for assessable units within the Air Force audit readiness strategy, there were several issues that surfaced, corrective actions were developed, and a way forward to audit readiness was identified. The continual evolution of the Air Force audit readiness strategy incorporates lessons learned, identifies best practices from past assertions and the other Services, leverages the knowledge of the personnel in the field that perform the current processes, and integrates with the ERP systems of the future to ensure audit readiness is sustained. The existing governance structure continued to monitor progress, address obstacles and work collectively as an enterprise to ensure audit readiness is a priority and remains one until complete Air Force audit readiness is achieved.

Current and Future Financial Systems - Defense Enterprise Accounting and Management System (DEAMS)

Our systems enable us to maintain stewardship over the resources entrusted to us. DEAMS is key to our current and future ability to manage the Air Force's resources. DEAMS was launched in August 2003 as a joint initiative between the Air Force, U.S. Transportation Command (USTRANSCOM) and the Defense Finance and Accounting Service

under what was the Defense Department's Business Transformation Agency. The DEAMS mission is to support the Nation's warfighters with timely, accurate, and reliable financial information, enabling more efficient and effective decision making by DoD managers. DEAMS is enabling reengineered financial management processes and activities through a unified system and business enterprise architecture, standardized business rules and processes, and the first implementation of the new Standard Financial Information Structure.

The Air Force is implementing DEAMS through a two-increment development approach with eight scheduled software releases. Increment 1, Release 1 supports a technology demonstration at Scott AFB, Illinois, involving USTRANSCOM; Headquarters, Air Mobility Command; and Air Force Active Duty, selected Air National Guard and Air Force Reserve tenant organizations on or associated with Scott AFB.

During FY 2007, the program successfully demonstrated the system's capability to support commitment accounting. In May of 2010 an operational version of Release 1 was deployed at Scott AFB, taking the full Oracle E-Business Suite to those same units.

Scheduled software Releases 1-2 under Increment 1 will expand DEAMS capability to the remaining AMC bases. Releases 3-4 will enable a major system upgrade and further deploy the system to the HQ's of the Surface Deployment and Distribution Command (SDDC) and Military Sealift Command (MSC). By FY 2017 DEAMS Increment 2, through a series of software support releases, is scheduled to have deployed DEAMS to the remaining Air Force MAJCOMs, their installations and supported tenant organizations providing full financial management and reporting capabilities to the Air Force.

When fully fielded, DEAMS will transform financial management and set a new standard for effective and efficient stewardship of our Nation's Defense resources.

Analysis of Financial Statements

As discussed in the accompanying independent auditor's report, long-standing financial management challenges prevent the Air Force from producing auditable financial statements for either the General Fund or the Working Capital Fund. The Air Force has made significant progress toward improving the quality and timeliness of our financial



information. However, we are currently unable to fully implement all elements of U.S. Generally Accepted Accounting Principles and Office of Management and Budget (OMB) Circular A-136, "Financial Reporting Requirements," due to limitations of our financial and non-financial management processes and systems.

Air Force General Fund

The General Fund is the fund into which most receipts of the United States Government are deposited. Exceptions include receipts from specific sources required by law to be deposited into other designated funds and receipts from appropriations made by Congress to carry on the general and ordinary operations of the Government. The Notes to the Principal Statements provide more detail on the appropriations. The major appropriations in the Air Force General Fund and their uses are introduced below.

Military Personnel (MILPERS)

This appropriation provides funding for the care and payroll of our Airmen. It includes all direct military compensation for active duty, reserve, guard, and retired personnel including regular pay, allowances, and bonuses. Additionally, this appropriation funds all Permanent Change of Station (PCS) moves and supports a total force (active, reserve and guard) of 511,340.

Operations & Maintenance (O&M)

This appropriation funds key readiness programs critical to prepare forces for combat operations and other peacetime missions. These include day-to-day operating costs such as flying hours, depot maintenance, training, spare parts, and base operations. The FY 2012 appropriation supported 79 major installations, including operations at two space lift ranges, and funded approximately 1.2 million flying hours.

Procurement

This appropriation provides for purchase of aircraft, missiles, vehicles, electronic and telecommunications equipment, satellite and launch equipment, base maintenance and support equipment, and investment-type spares. The FY 2012 program expanded, modified and upgraded weapons systems (ISR-Reaper procurement & RPA capabilities, Light Attack Armed Reconnaissance buys, Joint Strike Fighter, satellites).

Research, Development, Test and Evaluation (RDT&E)

This appropriation provides funding for the research and development of next generation weapons and platforms and for the testing and evaluation of current prototypes and upgrades. The FY 2012 initiatives include:

- Continue F-35 flight testing
- Invest in Long Range Strike Family of Systems, including a new penetrating bomber
- Continue development of four KC-X integration & capability demonstration aircraft
- Continue Defense Weather Satellite System development
- Continue development and integration of ISR enhancements to unmanned platforms

Military Construction (MILCON)

Typically this appropriation applies to any military construction project, either major or minor, than exceeds \$750,000, and for the planning and design for those projects.

Military Family Housing

The Military Family Housing Construction account funds new construction, construction improvements, planning and design and the Federal government costs for family housing privatization projects. The Air Force closed the Western Group privatization project in FY 2012. Also, the appropriation delivered 1,932 units at Japan, Europe, United Kingdom, and the United States in FY 2012. The Military Family Housing Operation and Maintenance accounts pays for maintenance and repair, furnishings, management, services, utilities, leasing, interest, mortgage insurance, and miscellaneous expenses. The FY 2012 Military Family Housing program was approximately \$499 million.

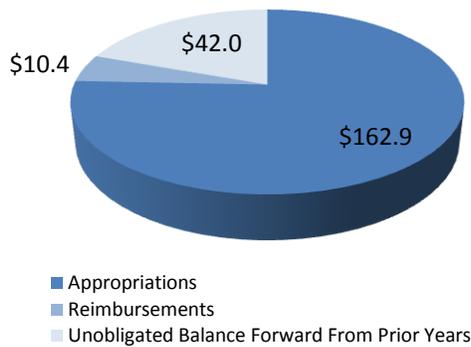
Base Realignment and Closure (BRAC)

The law authorizes the BRAC accounts to fund one-time, nonrecurring costs required to implement approved BRAC recommendations. Following the completion of the statutory implementation period, the accounts may only be used for environmental restoration and property management and to discharge legal obligations incurred. In addition, the law stipulates the accounts as the sole source of environmental restoration for base closures covered by the law. The FY 2012 BRAC program was approximately \$125 million.

Results of Operation

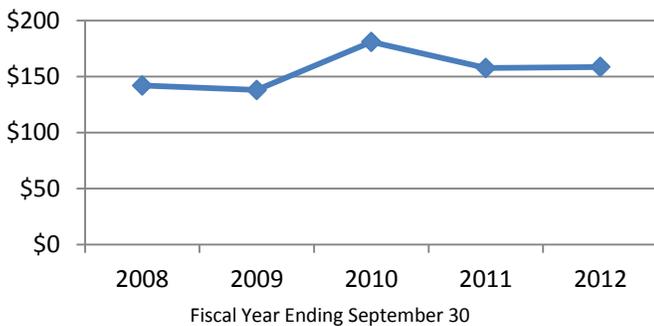
The Combined Statement of Budgetary Resources presents total budgetary resources of \$215.3 billion that were available to the AFGF during FY 2012. Total budgetary resources for FY 2011 were \$215.6 billion. Total obligations incurred in FY 2012 were \$182.3 billion compared to \$177.6 billion for FY 2011.

AFGF Sources of Funds, FY 2012
(\$ in Billions)



The Combined Statement of Net Cost presents net cost of operations of \$158.7 billion during FY 2012 compared to \$157.7 billion for FY 2011. Net cost of operations represents gross costs incurred by the AFGF less earned revenue.

AFGF Net Cost of Operation, FY 2008 - 2012
(\$ in Billions)

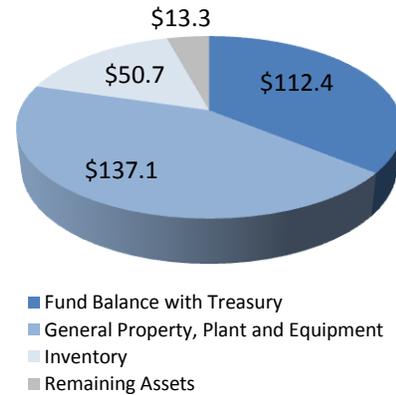


Financial Position

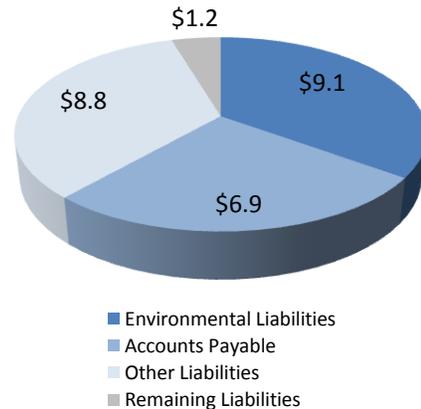
The AFGF continued to report a positive net position on its Consolidated Balance Sheet. Net position is the difference between total assets (what is owned) and total liabilities (what is owed). As of September 30, 2012, net position totaled \$287.6 billion. As of September 30, 2011 net position totaled \$282.0 billion.

Total assets were \$313.5 billion as of September 30, 2012, compared to \$306.8 billion as of September 30, 2011. Total liabilities were \$26.0 billion as of September 30, 2012, compared to \$24.8 billion as of September 30, 2011.

AFGF Total Assets, FY 2012
(\$ in Billions)



AFGF Total Liabilities, FY 2012
(\$ in Billions)



Air Force Working Capital Fund

The Air Force Working Capital Fund (AFWCF) conducts business in two primary areas: the Consolidated Sustainment Activity Group (CSAG) and the Supply Management Activity Group-Retail (SMAG-R). Air Force Materiel Command (AFMC) manages more than 90 percent of the AFWCF business activity for Supply Management and Depot Maintenance activities. These functions provide goods and services to the Air Force and DoD customers, as well as customers outside the DoD (e.g., local and foreign governments). Supply Management provides expedited repair, replenishment and inventory control for spare parts and associated logistics support services to fulfill Air Force needs during war and peacetime. Depot



Maintenance provides economical and responsive repair, overhaul and modification of aircraft, missiles, engines, other major end items and associated components.

In FY 1998 the Air Force was appointed the Executive Agent for Transportation Working Capital Fund (TWCF) cash. Even though AFWCF manages TWCF's cash, daily operations are managed by the United States Transportation Command. As a result, TWCF's financial statements are reported with other Defense Agencies.

The AFWCF allows the Air Force to accomplish the following: ensure readiness through reduced support costs, stabilized rates and responsive customer service; flexibility to respond to customer support needs in real-world situations; focus management attention on net operating results, including cost and performance; identify the total cost of providing support products and services; and establish strong customer/provider relationships.

Consolidated Sustainment Activity Group (CSAG)

CSAG is an AFWCF business activity chartered for operation in FY 2009. The CSAG consolidates the Depot Maintenance Activity Group (DMAG) and the previous Material Support Division (MSD) from the Supply Management Activity Group (SMAG) into a single business enterprise. This consolidation eliminates internal transactions between MSD and DMAG, resulting in a more efficient business enterprise and customer support improvements. The mission of CSAG is supply management of reparable and Air Force managed consumable items as well as maintenance services. Under CSAG, business operations formerly known as DMAG are now characterized as the Maintenance Division and business operations formerly known as MSD are now designated the Supply Division.

The **CSAG Maintenance Division** repairs systems and spare parts to ensure readiness in peacetime and to provide sustainment for combat forces in wartime. This division operates on the funds received from its customers through sales of its services. In peacetime, the Air Force enhances readiness by efficiently and economically repairing, overhauling and modifying aircraft, engines, missiles, components and software to meet customer demands. The Maintenance Division's depots have unique skills and equipment required to support and overhaul both new, complex components as well as aging weapon systems. During wartime or contingencies, the depots can

surge repair operations and realign capacity to support the war fighter's immediate needs.

CSAG Maintenance Division is managed by AFMC and employs over 24,000 personnel supporting four industrial locations:

- Ogden Air Logistics Center (OO-ALC), UT
- Oklahoma City Air Logistics Center (OC-ALC), OK
- Warner Robins Air Logistics Center (WR-ALC), GA
- Aerospace Maintenance and Regeneration Group (AMARG), Tucson, AZ

The **CSAG Supply Division** is primarily responsible for Air Force-managed, depot-level reparable spares and consumable spares unique to the Air Force. Spares are an individual part, subassembly, or assembly supplied for the maintenance or repair of systems or equipment. In addition to management of these inventories, the Supply Division provides a wide range of logistics support services including requirements forecasting, item introduction, cataloging, provisioning, procurement, repair, technical support, data management, item disposal, distribution management and transportation.

Supply Management Activity Group—Retail

The Air Force Supply Management Activity Group-Retail (SMAG-R) is comprised of three divisions: General Support, Medical-Dental, and the United States Air Force Academy.

The Air Force SMAG-R provides a wide range of logistics support services including requirements forecasting, item introduction, cataloging, provisioning, procurement, repair, technical support, data management, item disposal, distribution management and transportation. Consumable item inventories are an integral part of SMAG-R and are maintained by each of the divisions in support of customer requirements. The SMAG-R objective is to replenish inventories and provide supplies to customers in a timely manner within customer funding constraints, while maintaining fund solvency. The Air Force SMAG-R manages weapon system spare parts, medical-dental supplies and equipment, and other supply items used in non-weapon system applications.

The **General Support Division (GSD)** manages nearly 1.1 million items, which are procured from Defense Logistics Agency (DLA) and General Services Administration (GSA). GSD customers use the majority of these items to support field and

depot maintenance of aircraft, ground and airborne communication and electronic systems, as well as other sophisticated systems and equipment. The GSD also manages many items related to installation, maintenance, and administrative functions.

The **Medical-Dental Division (MDD)** manages nearly 76,000 different items for 74 Medical Treatment Facilities (MTF) worldwide. All supply and equipment requirements generated by Air Force MTFs are procured through this division. MDD also maintains a War Readiness Materiel (WRM) requirement. WRM provides initial war fighting capability until re-supply lines can sustain wartime demands for medical and dental supplies and equipment.

The **Air Force Academy Division** finances the purchase of uniforms and uniform accessories for sale to cadets in accordance with regulations of the Air Force Academy and related statutes. The customer base consists of approximately 4,000 cadets who receive distinctive uniforms procured from various manufacturing contractors.

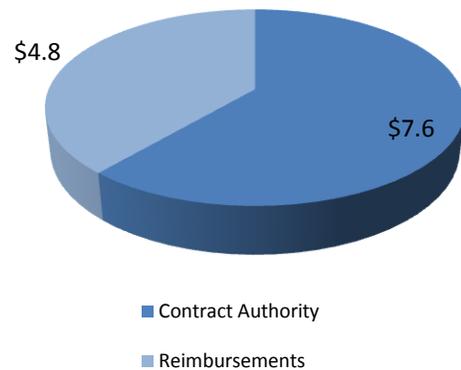
Air Force Working Capital Fund Customers

AFWCF provides support to a variety of customers: Air Force Major Commands (including the Air National Guard & Air Force Reserves), the Army, the Navy, other WCFs, other government agencies and foreign countries.

Results of Operation

The combined Statement of Budgetary Resources presents total budgetary resources of \$12.4 billion that were available to AFWCF during FY 2012 and the status of those resources at fiscal year-end. Total budgetary resources for FY 2011 were \$12.9 billion. Total obligations incurred during FY 2012 were \$12.3 billion, compared to \$12.4 billion during FY 2011.

AFWCF Sources of Funds, FY 2012
(\$ in Billions)



AFWCF assesses financial performance using the Statement of Net Costs. The Statement of Net Costs represents gross costs incurred by the AFWCF less earned revenue. For budget purposes, the Statement of Net Costs is adjusted by removing all non-recoverable activity to arrive at a bottom-line profit or loss indicator, also referred to as the recoverable Net Operating Result (NOR). The NOR objective of an activity group is to break even over a two year period. Prices are established to achieve this objective by recovering or returning all prior-year losses or gains.

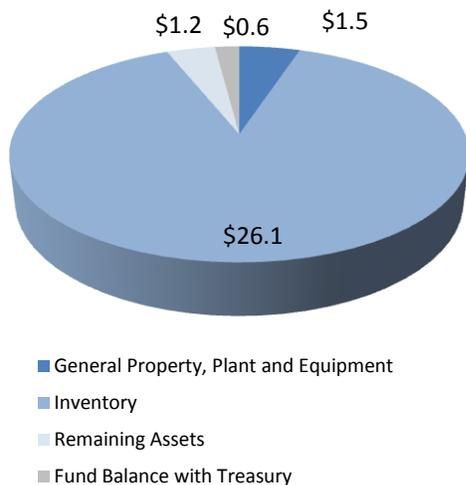
Financial Position

The AFWCF continued to report a positive net position on its Consolidated Balance Sheet. Net position is the difference between total assets (what is owned) and total liabilities (what is owed). As of September 30, 2012, net position totaled \$28.1 billion. As of September 30, 2011, net position totaled \$28.9 billion.



AFWCF Total Assets, FY 2012

(\$ in Billions)



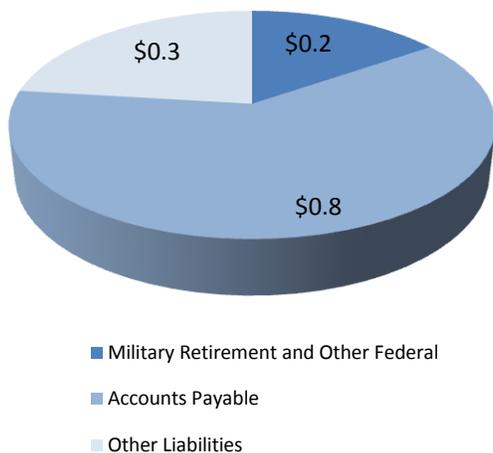
Cash Management

The AF manages working capital fund cash at the Department level. This cash is made up of both AFWCF and the USTRANSCOM cash balances and is reported by the U.S. Treasury as part of the AFWCF. However, for the purposes of Audited Financial Statements (AFS), USTRANSCOM is included with the Other Defense Organizations reporting which is separate from the AFWCF. AF targets to maintain cash levels at seven to ten days of operational costs plus sufficient cash reserves to meet six months of projected capital outlays, as required by the Department of Defense Financial Management Regulation. The AF WCF FY 2012 seven-day cash requirement was \$477.0 million and the ten-day requirement was \$628.0 million. AF WCF yearend cash balance, \$556.5 million, fell with the 7 to 10 day targets.

Total assets were \$29.4 billion as of September 30, 2012, compared to \$30.3 billion as of September 30, 2011. Total liabilities were \$1.3 billion as of September 30, 2012, compared to \$1.4 billion as of September 30, 2011.

AFWCF Total Liabilities, FY 2012

(\$ in Billions)



Financing the Fight

Despite new challenges and fiscal stress, America is and will unquestionably remain the global leader. As the Department of Defense’s recently released strategic guidance mentions, the Joint Force of the future must be smaller and leaner—but agile, flexible, ready, and technologically advanced. The Air Force will leverage the innovative ability and technological acumen of its Airmen as we conduct military missions that protect our core national interests. We have made the hard choices to closely align with the new strategic guidance by trading size for quality. We will be a smaller, but superb, force that maintains the agility, flexibility, and readiness to engage a full range of contingencies and threats. We will provide the necessary capability, capacity and versatility required to prevail today and in the future as we continue “Financing the Fight.”

References:

- Department of the Air Force. “2012 United States Air Force Posture Statement.” [United States Air Force](#). February 2012
- Department of the Air Force. “United States Air Force FY 2012 Budget Overview.” [United States Air Force](#). February 2011
- Department of the Air Force. “Air Force 101 Briefing.” [United States Air Force](#). April, 2012

Fiscal Year 2012

Annual Financial Statements

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 Title 31, United States Code, Section 3515 (b). While the statements have been prepared from the books and records of the entity, in accordance with U.S. generally accepted accounting principles promulgated by the Federal Accounting Standards Advisory Board, 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.



General Fund Principal Statements

Fiscal Year 2012

The FY 2012 Department of the Air Force General Fund Principal Statements and related notes are presented in the format prescribed by the Department of Defense Financial Management Regulation 7000.14-R, Volume 6B. The statements and related notes summarize financial information for individual activity groups and activities within the General Fund for the fiscal year ending September 30, 2012, and are presented on a comparative basis with information previously reported for the fiscal year ending September 30, 2011.

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

Consolidated Balance Sheet

The Consolidated Balance Sheet presents as of September 30, 2012 and 2011 those resources owned or managed by the Air Force which are available to provide future economic benefits (assets); amounts owed by the Air Force that will require payments from those resources or future resources (liabilities); and residual amounts retained by the Air Force, comprising the difference (net position)

Consolidated Statement of Net Cost

The Consolidated Statement of Net Cost presents the net cost of the Air Force's operations for the years ended September 30, 2012 and 2011. The Air Force's net cost of operations includes the gross costs incurred by the Air Force less any exchange revenue earned from Air Force activities.

Consolidated Statement of Changes in Net Position

The Consolidated Statement of Changes in Net Position presents the change in the Air Force's net position resulting from the net cost of Air Force's operations, budgetary financing sources other than exchange revenues, and other financing sources for the years ended September 30, 2012 and 2011.

Combined Statement of Budgetary Resources

The Combined Statement of Budgetary Resources presents the budgetary resources available to the Air Force during FY 2012 and 2011, the status of these resources at September 30, 2012 and 2011, and the outlay of budgetary resources for the years ended September 30, 2012 and 2011.

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, the Government Management Reform Act of 1994, and the Office of Management and Budget's Circular A-136, "Financial Reporting Requirements."

**Department of Defense
Department of the Air Force
CONSOLIDATED BALANCE SHEET
As of September 30, 2012 and 2011
(\$ in Thousands)**

	<u>2012 Consolidated</u>	<u>2011 Consolidated</u>
ASSETS (Note 2)		
Intragovernmental:		
Fund Balance with Treasury (Note 3)	\$ 112,402,627	\$ 110,088,325
Investments (Note 4)	1,072	1,077
Accounts Receivable (Note 5)	465,673	588,063
Other Assets (Note 6)	175,315	85,368
Total Intragovernmental Assets	<u>\$ 113,044,687</u>	<u>\$ 110,762,833</u>
Cash and Other Monetary Assets (Note 7)	\$ 80,838	\$ 95,583
Accounts Receivable, Net (Note 5)	422,316	366,409
Inventory and Related Property, Net (Note 9)	50,711,684	48,650,905
General Property, Plant and Equipment, Net (Note 10)	137,082,241	134,784,123
Other Assets (Note 6)	12,207,338	12,108,803
TOTAL ASSETS	<u><u>\$ 313,549,104</u></u>	<u><u>\$ 306,768,656</u></u>
STEWARDSHIP PROPERTY, PLANT & EQUIPMENT (Note 10)		
LIABILITIES (Note 11)		
Intragovernmental:		
Accounts Payable (Note 12)	\$ 2,493,311	\$ 2,553,974
Other Liabilities (Note 15 & 16)	2,193,658	2,029,335
Total Intragovernmental Liabilities	<u>\$ 4,686,969</u>	<u>\$ 4,583,309</u>
Accounts Payable (Note 12)	\$ 4,435,280	\$ 3,013,935
Military Retirement and Other Federal	1,150,353	1,126,143
Employment Benefits (Note 17)		
Environmental and Disposal Liabilities (Note 14)	9,084,414	10,564,623
Other Liabilities (Note 15 and Note 16)	6,606,541	5,478,873
TOTAL LIABILITIES	<u><u>\$ 25,963,557</u></u>	<u><u>\$ 24,766,883</u></u>
COMMITMENTS AND CONTINGENCIES (NOTE 16)		
NET POSITION		
Unexpended Appropriations - Other Funds	113,050,127	114,254,051
Cumulative Results of Operations - Earmarked Funds	19,479	12,425
Cumulative Results of Operations - Other Funds	174,515,941	167,735,297
TOTAL NET POSITION	<u><u>\$ 287,585,547</u></u>	<u><u>\$ 282,001,773</u></u>
TOTAL LIABILITIES AND NET POSITION	<u><u>\$ 313,549,104</u></u>	<u><u>\$ 306,768,656</u></u>



Department of Defense
Department of the Air Force
CONSOLIDATED STATEMENT OF NET COST
For the periods ended September 30, 2012 and 2011
(\$ in Thousands)

	<u>2012 Consolidated</u>	<u>2011 Consolidated</u>
Program Costs		
Gross Costs	\$ 168,983,383	\$ 166,451,900
Military Personnel	35,365,094	36,391,504
Operations, Readiness & Support	56,975,553	62,207,918
Procurement	44,410,025	38,706,085
Research, Development, Test & Evaluation	28,534,874	28,007,745
Family Housing & Military Construction	3,697,837	1,138,648
	<hr/>	<hr/>
(Less: Earned Revenue)	(10,325,178)	(8,751,985)
Net Cost before Losses/(Gains) from Actuarial Assumption for Military Retirement Benefits	<hr/> 158,658,205	<hr/> 157,699,915
Net Program Costs Including Assumption Changes	158,658,205	157,699,915
Net Cost of Operations	<u>\$ 158,658,205</u>	<u>\$ 157,699,915</u>

**Department of Defense
Department of the Air Force
CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION
For the periods ended September 30, 2012 and 2011
(\$ in Thousands)**

	<u>2012 Earmarked Funds</u>	<u>2012 All Other Funds</u>
CUMULATIVE RESULTS OF OPERATIONS		
Beginning Balances	\$ 12,425	\$ 167,735,297
Prior Period Adjustments:		
Corrections of errors (+/-)	0	0
Beginning balances, as adjusted	<u>12,425</u>	<u>167,735,297</u>
Budgetary Financing Sources:		
Appropriations used	0	162,287,754
Nonexchange revenue	898	0
Donations and forfeitures of cash and cash equivalents	1,762	0
Transfers-in/out without reimbursement	0	370,000
Other Financing Sources:		
Transfers-in/out without reimbursement (+/-)	(9)	(1,200,669)
Imputed financing from costs absorbed by others	0	763,656
Other (+/-)	0	3,222,511
Total Financing Sources	<u>2,651</u>	<u>165,443,252</u>
Net Cost of Operations (+/-)	<u>(4,394)</u>	<u>158,662,599</u>
Net Change	<u>7,045</u>	<u>6,780,653</u>
Cumulative Results of Operations	<u>19,470</u>	<u>174,515,950</u>
UNEXPENDED APPROPRIATIONS		
Beginning Balances	\$ 0	\$ 114,254,051
Beginning balances, as adjusted	<u>0</u>	<u>114,254,051</u>
Budgetary Financing Sources:		
Appropriations received	0	162,893,282
Appropriations transferred-in/out	0	1,659,029
Other adjustments (rescissions, etc)	0	(3,468,481)
Appropriations used	0	(162,287,754)
Total Budgetary Financing Sources	<u>0</u>	<u>(1,203,924)</u>
Unexpended Appropriations	<u>0</u>	<u>113,050,127</u>
Net Position	<u>19,470</u>	<u>287,566,077</u>



**Department of Defense
Department of the Air Force
CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION
For the periods ended September 30, 2012 and 2011
(\$ in Thousands)**

	<u>2012 Eliminations</u>	<u>2012 Consolidated</u>
CUMULATIVE RESULTS OF OPERATIONS		
Beginning Balances	\$ 0	\$ 167,747,722
Prior Period Adjustments:		
Corrections of errors (+/-)	0	0
Beginning balances, as adjusted	0	167,747,722
Budgetary Financing Sources:		
Appropriations used	0	162,287,754
Nonexchange revenue	0	898
Donations and forfeitures of cash and cash equivalents	0	1,762
Transfers-in/out without reimbursement	0	370,000
Other Financing Sources:		
Transfers-in/out without reimbursement (+/-)	0	(1,200,678)
Imputed financing from costs absorbed by others	0	763,656
Other (+/-)	0	3,222,511
Total Financing Sources	0	165,445,903
Net Cost of Operations (+/-)	0	158,658,205
Net Change	0	6,787,698
Cumulative Results of Operations	0	174,535,420
UNEXPENDED APPROPRIATIONS		
Beginning Balances	\$ 0	\$ 114,254,051
Beginning balances, as adjusted	0	114,254,051
Budgetary Financing Sources:		
Appropriations received	0	162,893,282
Appropriations transferred-in/out	0	1,659,029
Other adjustments (rescissions, etc)	0	(3,468,481)
Appropriations used	0	(162,287,754)
Total Budgetary Financing Sources	0	(1,203,924)
Unexpended Appropriations	0	113,050,127
Net Position	0	287,585,547

Department of Defense
Department of the Air Force
CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION
For the periods ended September 30, 2012 and 2011
(\$ in Thousands)

	2011 Earmarked Funds	2011 All Other Funds
CUMULATIVE RESULTS OF OPERATIONS		
Beginning Balances	\$ 18,568	\$ 179,970,391
Prior Period Adjustments:		
Corrections of errors (+/-)	0	(15,513,410)
Beginning balances, as adjusted	18,568	164,456,981
Budgetary Financing Sources:		
Appropriations used	0	159,703,254
Nonexchange revenue	913	0
Donations and forfeitures of cash and cash equivalents	4,728	0
Transfers-in/out without reimbursement	0	0
Other Financing Sources:		
Transfers-in/out without reimbursement (+/-)	0	867,507
Imputed financing from costs absorbed by others	0	855,639
Other (+/-)	1	(459,954)
Total Financing Sources	5,642	160,966,446
Net Cost of Operations (+/-)	11,785	157,688,130
Net Change	(6,143)	3,278,316
Cumulative Results of Operations	12,425	167,735,297
UNEXPENDED APPROPRIATIONS		
Beginning Balances	\$ 0	\$ 108,832,210
Beginning balances, as adjusted	0	108,832,210
Budgetary Financing Sources:		
Appropriations received	0	167,631,093
Appropriations transferred-in/out	0	772,813
Other adjustments (rescissions, etc)	0	(3,278,811)
Appropriations used	0	(159,703,254)
Total Budgetary Financing Sources	0	5,421,841
Unexpended Appropriations	0	114,254,051
Net Position	12,425	281,989,348



**Department of Defense
Department of the Air Force
CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION
For the periods ended September 30, 2012 and 2011
(\$ in Thousands)**

	<u>2011 Eliminations</u>	<u>2011 Consolidated</u>
CUMULATIVE RESULTS OF OPERATIONS		
Beginning Balances	\$ 0	\$ 179,988,959
Prior Period Adjustments:		
Corrections of errors (+/-)	0	(15,513,410)
Beginning balances, as adjusted	<u>0</u>	<u>164,475,549</u>
Budgetary Financing Sources:		
Appropriations used	0	159,703,254
Nonexchange revenue	0	913
Donations and forfeitures of cash and cash equivalents	0	4,728
Transfers-in/out without reimbursement	0	0
Other Financing Sources:		
Transfers-in/out without reimbursement (+/-)	0	867,507
Imputed financing from costs absorbed by others	0	855,639
Other (+/-)	0	(459,953)
Total Financing Sources	<u>0</u>	<u>160,972,088</u>
Net Cost of Operations (+/-)	<u>0</u>	<u>157,699,915</u>
Net Change	<u>0</u>	<u>3,272,173</u>
Cumulative Results of Operations	<u>0</u>	<u>167,747,722</u>
UNEXPENDED APPROPRIATIONS		
Beginning Balances	\$ 0	\$ 108,832,210
Beginning balances, as adjusted	<u>0</u>	<u>108,832,210</u>
Budgetary Financing Sources:		
Appropriations received	0	167,631,093
Appropriations transferred-in/out	0	772,813
Other adjustments (rescissions, etc)	0	(3,278,811)
Appropriations used	0	(159,703,254)
Total Budgetary Financing Sources	<u>0</u>	<u>5,421,841</u>
Unexpended Appropriations	<u>0</u>	<u>114,254,051</u>
Net Position	<u>0</u>	<u>282,001,773</u>

Department of Defense
Department of the Air Force
COMBINED STATEMENT OF BUDGETARY RESOURCES
For the periods ended September 30, 2012 and 2011
(\$ in Thousands)

	<u>2012 Combined</u>	<u>2011 Combined</u>
Budgetary Resources:		
Unobligated balance brought forward, Oct 1	38,007,021	36,090,271
Unobligated balance brought forward, Oct 1, as adjusted, as Adjusted	\$ 38,007,021	\$ 36,090,271
Recoveries of prior year unpaid obligations	5,451,702	4,488,152
Other changes in unobligated balance (+ or -)	(1,436,459)	(1,513,515)
Unobligated balance from prior year budget authority, net	42,022,264	39,064,908
Appropriations (discretionary and mandatory)	162,892,954	166,644,250
Spending Authority from offsetting collections	10,414,411	9,925,864
Total Budgetary Resources	<u>215,329,629</u>	<u>215,635,022</u>
Obligations Incurred	182,251,093	177,628,001
Unobligated balance, end of year		
Apportioned	28,142,256	33,990,184
Exempt from Apportionment	11,493	11,170
Unapportioned	4,924,787	4,005,667
Total unobligated balance, end of year	<u>33,078,536</u>	<u>38,007,021</u>
Total Budgetary Resources	<u>215,329,629</u>	<u>215,635,022</u>
Change in Obligated Balance:		
Unpaid obligations, brought forward, October 1 (gross)	74,701,468	74,007,637
Uncollected customer payments from Federal sources, brought forward, October 1 (-)	(3,032,491)	(2,968,685)
Obligated balance start of year (net), before adjustments (+ or -)	71,668,977	71,038,952
Obligated balance, start of year (net), as adjusted	71,668,977	71,038,952
Obligations incurred	182,251,093	177,628,001
Outlays (gross) (-)	(170,489,664)	(172,446,017)
Change in uncollected customer payments from Federal Sources (+ or-)	858,758	(63,806)
Recoveries of prior year unpaid obligations (-)	(5,451,701)	(4,488,153)
Obligated balance, end of year		
Unpaid Obligations, end of year (gross)	81,011,196	74,701,468
Uncollected customer payments from Federal sources, end of	(2,173,733)	(3,032,491)
Obligated balance, end of year	<u>78,837,463</u>	<u>71,668,977</u>



Department of Defense
Department of the Air Force
COMBINED STATEMENT OF BUDGETARY RESOURCES
For the periods ended September 30, 2012 and 2011
(\$ in Thousands)

	2012 Combined	2011 Combined
Budget Authority and Outlays, Net:		
Budget authority, gross (discretionary and mandatory)	173,307,365	176,570,114
Actual offsetting collections (discretionary and mandatory) (-)	(11,273,169)	(9,862,060)
Change in uncollected customer payments from Federal	858,758	(63,806)
Sources (discretionary and mandatory) (+ or -)		
Budget Authority, net (discretionary and mandatory)	162,892,954	166,644,248
Outlays, gross (discretionary and mandatory)	170,489,664	172,446,017
Actual offsetting collections (discretionary and mandatory) (-)	(11,273,169)	(9,862,060)
Outlays, net (discretionary and mandatory)	159,216,495	162,583,957
Distributed offsetting receipts (-)	(177,075)	(154,152)
Agency Outlays, net (discretionary and mandatory)	159,039,420	162,429,805

General Fund

Fiscal Year 2012

Notes to the Principal Statements

Notes to the financial statements communicate information essential for fair presentation of the financial statements that is not displayed on the face of the 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 Air Force, as required by the Chief Financial Officers Act of 1990, expanded by the Government Management Reform Act of 1994, and other appropriate legislation. The financial statements have been prepared from the books and records of the Air Force in accordance with, and to the extent possible, U.S. generally accepted accounting principles (USGAAP) promulgated by the Federal Accounting Standards Advisory Board; the Office of Management and Budget (OMB) Circular No. A-136, Financial Reporting Requirements; and the Department of Defense (DoD), Financial Management Regulation (FMR). The accompanying financial statements account for all resources for which the Air Force is responsible unless otherwise noted.

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

The Air Force is unable to implement fully all elements of USGAAP and the OMB Circular No. A-136, due to limitations of financial and nonfinancial management processes and systems that support the financial statements. The Air Force derives 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 USGAAP. The Air Force continues to implement process and system improvements addressing these limitations.

The DoD currently has 13 auditor identified material weaknesses. Of these the Air Force has the following: (1) Financial Management Systems; (2) Accounts Receivable; (3) Operating Materials and Supplies; (4) General Property, Plant, and Equipment; (5) Government-Furnished Material and Contractor-Acquired Material; (6) Accounts Payable; (7) Environmental Liabilities; (8) Statement of Net Cost; (9) Intragovernmental Eliminations; (10) Other Accounting Entries; and (11) Reconciliation of Net Cost of Operations to Budget.

1.B. Mission of the Reporting Entity

The United States Air Force was created on September 18, 1947, by the National Security Act of 1947 and operates under the direction, authority, and control of the Secretary of the Air Force. The Air Force's overall mission is to deliver sovereign options for the defense of the United States of America and its global interests to "Aim High...Fly, Fight, Win" in air, space, and cyberspace. The Air Force carries out its mission by adhering to a strategic framework of Core Values consisting of Integrity First, Service Before Self, and Excellence in All We Do. In addition, the Air Force is committed to providing Global Vigilance, Global Reach, and Global Power, while defending and protecting the United States.

1.C. Appropriations and Funds

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

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

These general funds also include supplemental funds enacted by the American Recovery and Reinvestment Act (Recovery Act) of 2009. Details relating to Recovery Act appropriated funds are available online at <http://www.defenselink.mil/recovery>.

Trust funds contain receipts and expenditures of funds held in trust by the government for use in carrying out specific purposes or programs in accordance with the terms of the donor, trust agreement, or statute. Special fund accounts are used to record government receipts reserved for a specific purpose. Certain trust and special funds may be designated as 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. The Air Force is required to separately

account for and report on the receipt, use and retention of revenues and other financing sources for earmarked funds.

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

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

The Air Force receives allocation transfers for EOP (Foreign Military Sales – Military Assistance Program) meeting the OMB exception; however, activities for this fund are reported separately from the DoD financial statements.

The accounts used to prepare the financial statements are categorized as either entity or nonentity. The Air Force accounts consist of resources that are available for use in the operations of the entity. The Air Force is authorized to decide how to use resources in entity accounts or may be legally obligated to use these resources to meet entity obligations. Nonentity accounts, on the other hand, consist of assets that are held by an entity but that are not available for use in the operations of the entity. The following is a list of the major Air Force account numbers and titles (all accounts are entity accounts unless otherwise noted):

AF Account Number	Title
57 * 0704	Military Family Housing, Operations and Maintenance (O&M) and Construction, Air Force
57 * 0740	Military Family Housing (Construction), Air Force
57 * 0743	Military Family Housing (Construction), Air Force, Recovery Act
57 * 0745	Military Family Housing, Operations and Maintenance (O&M), Air Force
57 * 0748	Military Family Housing, Operations and Maintenance (O&M), Air Force, Recovery Act
57 * 0810	Environmental Restoration, Air Force
57 * 1007	Medicare Eligible Retiree Health Fund Contributions, Air Force
57 * 1008	Medicare Eligible Retiree Health Fund Contributions, Air Force Reserve
57 * 1009	Medicare Eligible Retiree Health Fund Contributions, Air National Guard
57 * 3010	Aircraft Procurement, Air Force
57 * 3011	Procurement of Ammunition, Air Force
57 * 3020	Missile Procurement, Air Force
57 * 3080	Other Procurement, Air Force
57 * 3300	Military Construction, Air Force
57 * 3307	Military Construction, Air Force, Recovery Act
57 * 3400	Operations and Maintenance (O&M), Air Force
57 * 3404	Operations and Maintenance (O&M), Air Force, Recovery Act
57 * 3500	Military Personnel, Air Force
57 * 3600	Research, Development, Testing, and Evaluation (RDT&E), Air Force
57 * 3605	Research, Development, Testing, and Evaluation (RDT&E), Air Force, Recovery Act
57 * 3700	Personnel, Air Force Reserve
57 * 3730	Military Construction, Air Force Reserve
57 * 3740	Operations and Maintenance (O&M), Air Force Reserve
57 * 3744	Operations and Maintenance (O&M), Air Force Reserve, Recovery Act
57 * 3830	Military Construction, Air National Guard
57 * 3834	Military Construction, Air National Guard, Recovery Act
57 * 3840	Operations and Maintenance (O&M), Air National Guard
57 * 3844	Operations and Maintenance (O&M), Air National Guard, Recovery Act
57 * 3850	Personnel, Air National Guard
57 X 5095	Wildlife Conservation, etc., Military Reservations, Air Force
57 X 8418	Air Force Cadet Fund
57 X 8928	Air Force General Gift Fund
57 * 3XXX (Incl Nonentity)	Budget Clearing Accounts



57 * 6XXX (Nonentity)	Deposit Fund Accounts
57 **** (Nonentity)	Receipt Accounts

1.D. Basis of Accounting

The Air Force's financial management systems are unable to meet all full accrual accounting requirements. Many of the Air Force's financial and nonfinancial feeder systems and processes were designed and implemented prior to the issuance of USGAAP. These systems were not designed to collect and record financial information on the full accrual accounting basis as required by USGAAP. Most of Air Force's financial and nonfinancial legacy systems were designed to record information on a budgetary basis.

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

The DoD is determining the actions required to bring its financial and nonfinancial feeder systems and processes into compliance with USGAAP. One such action is the current revision of accounting systems to record transactions based on the U.S. Standard General Ledger (USSGL). Until all Air Force financial and nonfinancial feeder systems and processes are updated to collect and report financial information as required by USGAAP, Air Force's financial data will be derived from budgetary transactions, data from nonfinancial feeder systems, and accruals.

1.E. Revenues and Other Financing Sources

The Air Force receives congressional appropriations as financing sources for general funds that expire annually, on a multi-year basis, or do not expire. When authorized by legislation, these appropriations are supplemented by revenues generated by sales of goods or services. The Air Force recognizes revenue as a result of costs incurred for goods and services provided to other federal agencies and the public. Full-cost pricing is Air Force's standard policy for services provided as required by OMB Circular A-25, User Charges. The Air Force recognizes revenue when earned within the constraints of its current system capabilities. In some instances, revenue is recognized when bills are issued.

The Air Force 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 countries having 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. Current financial and nonfinancial feeder systems were not designed to collect and record financial information on the full accrual accounting basis. Estimates are made for major items such as payroll expenses, accounts payable, environmental liabilities, and unbilled revenue. Some accounts such as civilian pay, military pay, and accounts payable are presented on the accrual basis of accounting on the financial statements, as required by USGAAP.

In the case of Operating Materials & Supplies (OM&S), operating expenses are generally recognized when the items are purchased. Efforts are underway to transition to the consumption method for recognizing OM&S expenses. Under the consumption method, OM&S would be expensed when consumed.

Due to system limitations, in some instances expenditures for capital and other long-term assets may be recognized as operating expenses. The Air Force continues to implement process and system improvements to address these limitations.

1.G. Accounting for Intragovernmental Activities

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

The U.S. Treasury's Federal Intragovernmental Transactions Accounting Policy Guide and Treasury Financial Manual Part 2 – Chapter 4700, Agency Reporting Requirements for the Financial Report of the United States Government, provide guidance for reporting and reconciling intragovernmental balances. While Air Force is unable to fully reconcile intragovernmental transactions with all federal agencies, Air Force 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 do not report any public debt, interest, or source of public financing, whether from issuance of debt or tax revenues.

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

1.H. Transactions with Foreign Governments and International Organizations

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

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

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

In addition, DFAS 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 these transactions to the applicable Fund Balance with Treasury (FBWT) account. On a monthly basis, Air Force's FBWT is adjusted to agree with the U.S. Treasury accounts.

1.J. Cash and 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 deposit in banks and other financial institutions. Foreign currency consists of the total U.S. dollar equivalent of both purchased and nonpurchased foreign currencies held in foreign currency fund accounts. Foreign currency is valued using the U.S. Treasury prevailing rate of exchange.

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



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

1.K. Accounts Receivable

Accounts receivable from other federal entities or the public include: accounts receivable, claims receivable, and refunds receivable. Allowances for uncollectible accounts due from the public are based upon analysis of collection experience by fund type. The DoD does not recognize an allowance for estimated uncollectible amounts from other federal agencies. Claims against other federal agencies are to be resolved between the agencies in accordance with dispute resolution procedures defined in the Intragovernmental Business Rules published in the Treasury Financial Manual.

1.L. Direct Loans and Loan Guarantees

Not applicable.

1.M. Inventories and Related Property

The Air Force 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 self-propelled weapons, aircraft, etc., and related spares, repair parts, and support equipment. Items commonly used in and available from the commercial sector are not managed in Air Force's materiel management activities. Operational cycles are irregular and the military risks associated with stock-out positions have no commercial parallel. The Air Force holds materiel based on military need and support for contingencies. The DoD is currently developing a methodology to be used to account for "inventory held for sale" and "inventory held in reserve for future sale."

Related property includes OM&S and stockpile materiel. The majority of OM&S, with the exception of munitions not held for sale, are valued using the moving average cost method. Munitions not held for sale are valued at standard purchase price. The Air Force 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, Air Force uses the purchase method. Under this method, materiel and supplies are expensed when purchased. During FY 2012 and FY 2011, Air Force 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 Air Force 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 Air Force recognizes excess, obsolete, and unserviceable OM&S at a net realizable value of \$0 pending development of an effective means of valuing such materiel.

Inventory available and purchased for resale includes consumable spare and repair parts and repairable items owned and managed by Air Force. This inventory is retained to support military or national contingencies. Inventory held for repair is damaged inventory that requires repair to make it suitable for sale. Often, it is more economical to repair these items rather than to procure them. Air Force often relies on weapon systems and machinery no longer in production. As a result, Air Force supports a process that encourages the repair and rebuilding of certain items. This repair cycle is essential to maintaining a ready, mobile and armed military force. Work in process balances include (1) costs related to the production or servicing of items, including direct material, labor, overhead; (2) the value of finished products or completed services that are yet to be placed in service; and (3) munitions in production and depot maintenance work with its associated costs incurred in the delivery of maintenance services.

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

The Air Force reports investments in U.S. Treasury securities at cost, net of amortized premiums or discounts. Premiums or discounts are amortized over the term of the investments using the effective interest rate method or another method obtaining similar results. The Air Force's intent is to hold investments to maturity, unless they are needed to finance claims or otherwise sustain operations. Consequently, a provision is not made for unrealized gains or losses on these securities.

The Air Force invests in nonmarketable market-based U.S. Treasury securities, which are issued to federal agencies by the U.S. Treasury's Bureau of Public Debt. They are not traded on any securities exchange but mirror the prices of particular U.S. Treasury securities traded in the government securities market.

1.O. General Property, Plant and Equipment

The Air Force uses the estimated historical cost for valuing 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 establish a baseline. The military equipment baseline is updated using expenditure, acquisition, and disposal information.

The DoD's General Property, Plant, and Equipment (PP&E) capitalization threshold is \$100 thousand except for real property, which is \$20 thousand. The Air Force has not fully implemented the threshold for real property; therefore, DoD is primarily using the capitalization threshold of \$100 thousand for General PP&E, and most real property.

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

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

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

1.P. Advances and Prepayments

When advances are permitted by law, legislative action, or presidential authorization, DoD's policy is to record advances or prepayments in accordance with USGAAP. As such, payments made in advance of the receipt of goods and services should be reported as an asset on the Balance Sheet. The DoD's policy is to expense and/or properly classify assets when the related goods and services are received. The Air Force has not fully implemented this policy primarily due to system limitations.

1.Q. Leases

Lease payments for the rental of equipment and operating facilities are classified as either capital or operating leases. When a lease is essentially equivalent to an installment purchase of property (a capital lease), and the value equals or exceeds the current capitalization threshold, Air Force records the applicable asset as though purchased, with an offsetting liability, and depreciates it. The Air Force records the asset and the liability at the lesser of the present value of the rental and other lease payments during the lease term (excluding portions representing executory costs paid to the lessor) or the asset's fair market value. The discount rate for the present value calculation is either the lessor's implicit interest rate or the government's incremental borrowing rate at the inception of the lease. The Air Force, as the lessee, receives the use and possession of leased property, for example real estate or equipment, from a lessor in exchange for a



payment of funds. An operating lease does not substantially transfer all the benefits and risk of ownership. Payments for operating leases are expensed over the lease term as they become payable.

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

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 Air Force's Balance Sheet.

The Air Force 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, Air Force may provide financing payments. Contract financing payments are defined in the Federal Acquisition Regulations, Part 32, as authorized disbursements to a contractor prior to acceptance of supplies or services by the Government. Contract financing payments clauses are incorporated in the contract terms and conditions and may include advance payments, performance-based payments, commercial advances and interim payments, progress payments based on cost, and interim payments under certain cost-reimbursement contracts. It is DoD policy to record certain contract financing payments as other assets. The Air Force has fully implemented this policy.

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

1.S. Contingencies and Other Liabilities

The Statement of Federal Financial Accounting Standards (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 Air Force recognizes contingent liabilities when past events or exchange transactions occur, a future loss is probable, and the loss amount can be reasonably estimated.

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

Other liabilities also arise as a result of anticipated disposal costs for Air Force assets. Consistent with SFFAS No. 6, Accounting for Property, Plant, and Equipment, recognition of an anticipated environmental disposal liability begins when the asset is placed into service. Based on DoD's policy, which is consistent with SFFAS No. 5, Accounting for Liabilities of the Federal Government, nonenvironmental disposal liabilities are recognized when management decides to dispose of an asset. The DoD recognizes nonenvironmental disposal liabilities for military equipment nuclear-powered assets when placed into service. These amounts are not easily distinguishable and are developed in conjunction with environmental disposal costs. The Air Force does not recognize contingent liabilities associated with nonenvironmental disposals due to immateriality.

1.T. Accrued Leave

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

1.U. Net Position

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

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

Cumulative results of operations represent the net difference between expenses and losses, and financing sources (including appropriations, revenue, and gains), since inception. The cumulative results of operations also include donations and transfers in and out of assets that were not reimbursed.

1.V. Treaties for Use of Foreign Bases

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

1.W. Undistributed Disbursements and Collections

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

Supported disbursements and collections are evidenced by corroborating documentation. Unsupported disbursements and collections do not have supporting documentation for the transaction and most likely would not meet audit scrutiny. However, both supported and unsupported adjustments may have been made to the Air Force Accounts Payable and Receivable trial balances prior to validating underlying transactions required to establish the Accounts Payable/Receivable were previously made. As a result, misstatements of reported Accounts Payable and Receivables are likely present in the Air Force financial statements.

Due to noted material weaknesses in current accounting and financial feeder systems, the DoD is generally unable to determine whether undistributed disbursements and collections should be applied to federal or nonfederal accounts payable/receivable at the time accounting reports are prepared. Accordingly, the DoD policy is to allocate supported undistributed disbursements and collections between federal and nonfederal categories based on the percentage of distributed federal and nonfederal accounts payable and accounts receivable. Both supported and unsupported undistributed disbursements and collections are then applied to reduce accounts payable and receivable accordingly.

1.X. Fiduciary Activities

Fiduciary cash and other assets are not assets of the Air Force and are not recognized on the Balance Sheet. Fiduciary activities are reported on the financial statement note schedules.

1.Y. Military Retirements and Other Federal Employment Benefits

Not applicable.

1.Z. Significant Events

Not applicable.



Note 2. Nonentity Assets

As of September 30 (Amounts in thousands)	2012	2011
1. Intragovernmental Assets		
A. Fund Balance with Treasury	\$ 122,890	\$ 126,641
B. Accounts Receivable	0	0
C. Other Assets	0	0
D. Total Intragovernmental Assets	\$ 122,890	\$ 126,641
2. Nonfederal Assets		
A. Cash and Other Monetary Assets	\$ 80,838	\$ 95,583
B. Accounts Receivable	293,607	296,028
C. Other Assets	179,050	184,825
D. Total Nonfederal Assets	\$ 533,495	\$ 576,436
3. Total Nonentity Assets	\$ 676,385	\$ 703,077
4. Total Entity Assets	\$ 312,872,718	\$ 306,065,578
5. Total Assets	\$ 313,549,104	\$ 306,768,655

Relevant Information for Comprehension

Nonentity assets are assets for which the Air Force maintains stewardship accountability and reporting responsibility but are not available for the Air Force’s normal operations.

Intragovernmental Fund Balance with Treasury represents amounts in Air Force’s deposit fund and two suspense fund accounts (Uniformed Services Thrift Savings Plan Suspense and Thrift Savings Plan Suspense) that are not available for Air Force use.

Nonfederal Accounts Receivable include interest receivable that upon collection is remitted to the U.S. Treasury as miscellaneous receipts.

Nonfederal Cash and Other Monetary Assets represent disbursing officers’ cash and undeposited collections as reported on the Statement of Accountability (Standard Form 1219). These assets are held by the Air Force Disbursing Officers as agents of the U.S. Treasury. The Nonfederal Cash and Other Monetary assets represent a fiduciary capacity held by Air Force Disbursing Officers as agents for U.S. Treasury and are not available for use in operations.

Nonfederal Other Assets consist of advances to contractors as part of the advance payment pool agreements with the Massachusetts Institute of Technology and other nonprofit institutions. These agreements are used for the financing of cost-type contracts with nonprofit educational research institutions for experimental research and development work when several contracts or a series of contracts require financing by advance payments. These funds are not available for use in Air Force operations.

Note 3. Fund Balance with Treasury

As of September 30 (Amounts in thousands)	2012	2011
1. Fund Balances		
A. Appropriated Funds	\$ 112,266,178	\$ 109,948,002
B. Revolving Funds	0	0
C. Trust Funds	11,568	11,635
D. Special Funds	1,990	2,046
E. Other Fund Types	122,890	126,641
F. Total Fund Balances	\$ 112,402,626	\$ 110,088,324
2. Fund Balances Per Treasury Versus Agency		
A. Fund Balance per Treasury	\$ 114,557,011	\$ 111,739,128
B. Fund Balance per Agency	112,402,626	110,088,324
3. Reconciling Amount	\$ 2,154,385	\$ 1,650,804

Relevant Information for Comprehension

Other Fund Types include balances in deposit accounts which consist of taxes, small escrow accounts and other federal payroll withholding allotments.

The Air Force shows a reconciling amount of \$ 2.2 billion with U.S. Treasury, which is comprised of the net value of the following:

\$26.6 million in allocation transfers to Air Force from the Department of Agriculture and the Foreign Military Sales-Military Assistance Program (MAP). An allocation transfer occurs when the Treasury appropriates funds to one federal entity, which then transfers the authority to execute its funds to another federal entity. Treasury reports these funds as Air Force in the Fund Balance with Treasury (FBWT), but Air Force does not include in its FBWT because the Departments of Agriculture and MAP report these balances in their financial statements.

\$21.9 million in allocation transfers from Air force to the Department of Transportation (DoT). These funds are reported in FBWT by Air Force but are not included in FBWT at Treasury, because Treasury reports these balances under DoT.

\$1.8 million of unavailable receipt accounts due to fiduciary activity consisting of the Savings Deposit Program (SDP). The U.S. Treasury reported these funds as Air Force FBWT, but activity recorded within the SDP must be excluded form the Air Force FBWT.

\$2.0 billion in withdrawal of the FBWT in the cancelling appropriations at September 30, 2012. These funds are included in FBWT per Treasury but are not included in FBWT per Air Force.

\$98.7 million in withdrawal of the FBWT for unavailable receipt accounts at September 30, 2012. These funds are included in FBWT per Treasury but are not included in FBWT per Air Force.



Status of Fund Balance with Treasury

As of September 30	2012		2011	
(Amounts in thousands)				
1. Unobligated Balance				
A. Available	\$	28,153,750	\$	34,001,355
B. Unavailable		4,924,787		4,005,666
2. Obligated Balance not yet Disbursed	\$	81,011,195	\$	74,701,468
3. Nonbudgetary FBWT	\$	487,686	\$	413,385
4. NonFBWT Budgetary Accounts	\$	(2,174,792)	\$	(3,033,550)
5. Total	\$	112,402,626	\$	110,088,324

Relevant Information for Comprehension

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

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

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

Nonbudgetary FBWT includes accounts that do not have budgetary authority, such as deposit funds, unavailable receipt accounts, clearing accounts and nonentity FBWT. The items reported as Nonbudgetary FBWT account comprises the FBWT for suspense, deposit and receipt accounts.

NonFBWT Budgetary Accounts reduce the Status of FBWT. The items that comprise the amount reported as NonFBWT receipts are from investments and discounts in U.S. Treasury securities, and unfilled customer orders without advances.

Note 4. Investments and Related Interest

As of September 30	2012				
	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	1,072	Effective Interest	(5)	1,067	1,067
5. Total Nonmarketable, Market-Based	1,072		(5)	1,067	1,067
B. Accrued Interest	5			5	5
C. Total Intragovernmental Securities	\$ 1,077		\$ (5)	\$ 1,072	\$ 1,072

2. Other Investments

A. Total Other Investments	\$ 0		\$ 0	\$ 0	N/A
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As of September 30	2011				
	Cost	Amortization Method	Amortized (Premium) / Discount	Investments, Net	Market Value Disclosure
(Amounts in thousands)					
3. 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	1,077	Effective Interest	(5)	1,072	1,072
5. Total Nonmarketable, Market-Based	1,077		(5)	1,072	1,072
B. Accrued Interest	6			6	6
C. Total Intragovernmental Securities	\$ 1,083		\$ (5)	\$ 1,078	\$ 1,078

4. Other Investments

A. Total Other Investments	\$ 0		\$ 0	\$ 0	N/A
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Relevant Information for Comprehension

The U.S. Treasury securities are issued to the earmarked funds as evidence of its receipt and are an asset to the Air Force and a liability to the U.S. Treasury. The Federal Government does not set aside assets to pay future benefits or other expenditures associated with earmarked funds. The cash generated from earmarked funds are deposited in the U.S. Treasury, which uses the cash for general Government purposes. Since the Air Force and the U.S. Treasury are both part of the Federal Government, these assets and liabilities offset each other from the standpoint of the Federal Government as a whole. For this reason, they do not represent an asset or a liability in the U.S. Governmentwide financial statements.

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

Intragovernmental Securities (Other Funds) primarily represents the Air Force Gift Fund investment in U.S. Treasury Securities.

Note 5.	Accounts Receivable
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As of September 30	2012		
	Gross Amount Due	Allowance For Estimated Uncollectibles	Accounts Receivable, Net
(Amounts in thousands)			
1. Intragovernmental Receivables	\$ 465,674	N/A	\$ 465,674
2. Nonfederal Receivables (From the Public)	\$ 700,231	\$ (277,915)	\$ 422,316
3. Total Accounts Receivable	\$ 1,165,905	\$ (277,915)	\$ 887,990

As of September 30	2011		
	Gross Amount Due	Allowance For Estimated Uncollectibles	Accounts Receivable, Net
(Amounts in thousands)			
1. Intragovernmental Receivables	\$ 588,063	N/A	\$ 588,063
2. Nonfederal Receivables (From the Public)	\$ 672,052	\$ (305,644)	\$ 366,408
3. Total Accounts Receivable	\$ 1,260,115	\$ (305,644)	\$ 954,471

Relevant Information for Comprehension

The accounts receivable represent the Air Force’s claim for payment from other entities. The Air Force only recognizes an allowance for uncollectible amounts from the public. Claims with other federal agencies are resolved in accordance with the Intragovernmental Business Rules.



Note 6. Other Assets

As of September 30 (Amounts in thousands)	2012	2011
1. Intragovernmental Other Assets		
A. Advances and Prepayments	\$ 175,315	\$ 93,765
B. Other Assets	0	0
C. Total Intragovernmental Other Assets	\$ 175,315	\$ 93,765
2. Nonfederal Other Assets		
A. Outstanding Contract Financing Payments	\$ 11,999,840	\$ 11,288,053
B. Advances and Prepayments	28,449	92,343
C. Other Assets (With the Public)	179,050	184,825
D. Total Nonfederal Other Assets	\$ 12,207,339	\$ 11,565,221
3. Total Other Assets	\$ 12,382,654	\$ 11,658,986

Relevant Information for Comprehension

Nonfederal Other Assets (With the Public) is comprised exclusively of advance payment pool agreements with nonprofit educational institutions. These agreements are funded under cost-type contract procedures and are mainly for experimental research and development requirements.

Contract terms and conditions for certain types of contract financing payments convey certain rights to the Federal Government 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 Air Force is not obligated to make payment to the contractor until delivery and acceptance.

Note 7. Cash and Other Monetary Assets

As of September 30 (Amounts in thousands)	2012		2011	
1. Cash	\$	65,202	\$	77,946
2. Foreign Currency		15,636		17,638
3. Other Monetary Assets		0		0
4. Total Cash, Foreign Currency, & Other Monetary Assets	\$	80,838	\$	95,584

Relevant Information for Comprehension

The amount reported as cash and foreign currency consists primarily of cash held by Disbursing Officers. The foreign currency amount reported is valued at U.S. Treasury’s prevailing exchange rate, which is the most favorable rate available to the Government for foreign exchange transactions. Foreign currency is primarily used to make vendor disbursements and to exchange U.S. dollars for military personnel.

Cash and foreign currency are nonentity assets and, as such, considered restricted assets that are held by the Air Force but are not available for use in its operations. These assets are held by Air Force Disbursing Officers as agents of U.S. Treasury. The total balance of \$80.8 million is restricted.

Note 8. Direct Loans and Loan Guarantees

Not applicable



Note 9. Inventory and Related Property

As of September 30 (Amounts in thousands)	2012	2011
1. Inventory, Net	\$ 0	\$ 0
2. Operating Materials & Supplies, Net	50,711,683	48,650,905
3. Stockpile Materiel, Net	0	0
4. Total	\$ 50,711,683	\$ 48,650,905

Relevant Information for Comprehension

General Composition of OM&S

The Operating Materials and Supplies (OM&S) include weapon systems spares, ammunition, tactical missiles, aerial target drones, uninstalled aircraft and cruise missile engines, and uninstalled intercontinental ballistic missile motors.

In addition to the account balances shown in Note 9, the federal accounting standard requires disclosure of the amount of OM&S held for future use. Except for an immaterial amount of munitions, the Air Force is not holding any items for future use.

Restrictions on the Use of OM&S

The Air Force does not maintain any OM&S restricted assets.

Decision Criteria for Identifying the Category to Which OM&S Items Are Assigned

The category Held for Use includes all materiel available for issuance. OM&S classified as such is marked within each supply or inventory system.

The category Held for Repair generally includes all economically reparable materiel as defined by the Military Standard Transaction Reporting and Accounting Procedures Manual (DoD 4000.25-2-M). The category Held for Repair represents suspended, unserviceable (but reparable) items recorded at Moving Average Cost (MAC) or standard price.

The category Held as Excess, Obsolete, and Unserviceable includes all materiel that managers determine to be more costly to repair than to replace. Items retained for management purposes which are beyond economic repair are coded “condemned.” These items are held until proper disposal can be made. Excess, Obsolete, and Unserviceable are valued at zero. This allowance results in a zero value to the Air Force.

Changes in the Criteria for Identifying the Category to Which OM&S Items Are Assigned

Under current DoD policy, no allowance is made for serviceable, ready-to-issue items (Held for Use). An allowance equal to 100% of MAC or standard price, however, is made for the category Excess, Obsolete, and Unserviceable. This allowance results in a net book value of zero to the Air Force. Excess, Obsolete, and Unserviceable are valued at zero. This allowance results in a zero value to the Air Force. The category Held for Repair represents suspended, unserviceable (but reparable) items recorded at MAC or standard price.

Operating Materiel and Supplies (OM&S) Value

The OM&S data reported on the financial statements are derived from logistics systems designed for materiel management purposes. Some of these systems do not maintain the historical cost data necessary to comply with the valuation requirements of the Statement of Federal Financial Accounting Standards (SFFAS) No. 3, "Accounting for Inventory and Related Property."

In general, the Air Force uses the consumption method of accounting for OM&S, since OM&S is defined in SFFAS No. 3 as materiel that has not yet been issued to the end user. Once issued, the materiel is expensed. According to federal accounting standards, the consumption method of accounting should be used to account for OM&S unless: (1) the amount of OM&S is not significant, (2) OM&S are in the hands of the end user for use in normal operations, or (3) it is cost beneficial to expense OM&S when purchased (purchase method).

Other Air Force Disclosures

In the past, the Air Force provided only minimal OM&S accounting data that can be used to prepare the financial statements but has made considerable strides in improving the systems to provide actual transactions for completing the financial statements. However, in some cases, the data provided still consists of only beginning and ending balances for each of the asset accounts Held for Use; Excess, Obsolete, and Unserviceable; and Held for Repair. Without the required additional data (acquisitions, transfers in, amounts consumed, transfers out, trading partner data, etc.), DFAS can only report the net change between prior period ending balances and the values reported as current period ending balances.



Inventory, Net

Not applicable

Operating Materials and Supplies, Net

As of September 30	2012			Valuation Method
	OM&S Gross Value	Revaluation Allowance	OM&S, Net	

(Amounts in thousands)

1. OM&S Categories

A. Held for Use	\$ 39,196,024	\$ 0	\$ 39,196,024	SP, LAC, MAC
B. Held for Repair	11,515,659	0	11,515,659	SP, LAC, MAC
C. Excess, Obsolete, and Unserviceable	402,171	(402,171)	0	NRV
D. Total	\$ 51,113,854	\$ (402,171)	\$ 50,711,683	

As of September 30	2011			Valuation Method
	OM&S Gross Value	Revaluation Allowance	OM&S, Net	

(Amounts in thousands)

1. OM&S Categories

A. Held for Use	\$ 37,183,077	\$ 0	\$ 37,183,077	SP, LAC, MAC
B. Held for Repair	11,467,828	0	11,467,828	SP, LAC, MAC
C. Excess, Obsolete, and Unserviceable	551,424	(551,424)	0	NRV
D. Total	\$ 49,202,329	\$ (551,424)	\$ 48,650,905	

Legend for Valuation Methods:

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

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

MAC = Moving Average Cost

Stockpile Materiel, Net

Not applicable.

Note 10. General Property, Plant & Equipment, Net

As of September 30	2012				
	Depreciation/ Amortization Method	Service Life	Acquisition Value	(Accumulated Depreciation/ Amortization)	Net Book Value
(Amounts in thousands)					
1. Major Asset Classes					
A.Land	N/A	N/A	\$ 424,618	N/A \$	424,618
B.Buildings, Structures, and Facilities	S/L	20 Or 40	72,435,882 \$	(37,200,608)	35,235,274
C.Leasehold Improvements	S/L	Lease Term	63,510	(9,808)	53,702
D.Software	S/L	2-5 Or 10	626,824	(402,653)	224,171
E.General Equipment	S/L	5 Or 10	47,270,027	(35,597,256)	11,672,771
F. Military Equipment	S/L	Various	293,447,899	(209,292,723)	84,155,176
G.Shipbuilding (Construction-in-Progress)	N/A	N/A	0	0	0
H.Assets Under Capital Lease	S/L	Lease Term	106,923	(91,443)	15,480
I. Construction-in- Progress (Excludes Military Equipment)	N/A	N/A	5,301,049	N/A	5,301,049
J. Other			0	0	0
K.Total General PP&E			<u>\$ 419,676,732</u>	<u>\$ (282,594,491)</u>	<u>\$ 137,082,241</u>

1 Note 15 for additional information on Capital Leases

Legend for Valuation Methods:

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



As of September 30	2011				
	Depreciation/ Amortization Method	Service Life	Acquisition Value	(Accumulated Depreciation/ Amortization)	Net Book Value
(Amounts in thousands)					
1. Major Asset Classes					
A.Land	N/A	N/A	\$ 408,291	N/A \$	408,291
B.Buildings, Structures, and Facilities	S/L	20 Or 40	64,474,698 \$	(32,831,874)	31,642,825
C.Leasehold Improvements	S/L	Lease Term	18,460	(5,020)	13,440
D.Software	S/L	2-5 Or 10	620,744	(382,707)	238,037
E.General Equipment	S/L	5 or 10	45,957,562	(36,506,073)	9,451,489
F.Military Equipment	S/L	Various	296,659,522	(209,083,244)	87,576,277
G.Shipbuilding (Construction-in-Progress)	N/A	N/A	0	0	0
H.Assets Under Capital Lease	S/L	Lease Term	372,563	(338,806)	33,757
I. Construction-in- Progress (Excludes Military Equipment)	N/A	N/A	5,420,007	N/A	5,420,007
J. Other			0	0	0
K.Total General PP&E			<u>\$ 413,931,847</u>	<u>\$ (279,147,724)</u>	<u>\$ 134,784,123</u>

1 Note 15 for additional information on Capital Leases

Legend for Valuation Methods:

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

Heritage Assets and Stewardship Land

Categories	Measure Quantity	Beginning Balance	Additions	Deletions	Ending Balance
Buildings and Structures	Each	8,576	187	1,609	7,154
Archeological Sites	Each	2,414	235	0	2,649
Museum Collection Items (Objects, Not Including Fine Art)	Each	129,609	4,775	195	134,189
Museum Collection Items (Objects, Fine Art)	Each	11,139	1,441	0	12,580

(Acres in Thousands)

Facility Code	Facility Title	Beginning Balance	Additions	Deletions	Ending Balance
9110	Government Owned Land	1,569	0	3	1,566
9111	State Owned Land	0	0	0	0
9120	Withdrawn Public land	7,659	0	1,380	6,279
	Licensed and Permitted	248	461	0	709
9130	Land				
9140	Public Land	191	0	0	191
9210	Land Easement	160	0	0	160
9220	In-leased Land	93	10	0	103
9230	Foreign Land	296	0	0	296
Grand Total					9,304
TOTAL - All Other Lands					2,834
TOTAL – Stewardship Lands					6,470

Relevant Information for Comprehension

General Property, Plant and Equipment (PP&E)

There are restrictions on the Air Force’s ability to dispose of real property (land and buildings) located outside the continental United States.

Due to lack of historical data, in the past the Air Force estimated historical values for capitalized military equipment using current departmental internal records. Currently, the Air Force uses actual acquisition cost for capitalizing military equipment. The Air Force estimates historical values for capitalized military equipment using departmental internal records.

Other Air Force Disclosures

The value of the Air Force’s General PP&E real property in the possession of contractors is included in the values reported for the major asset classes of Land and Buildings, Structures, and Facilities. The value of General PP&E personal property major asset class of Software and Equipment does not include all of the General PP&E above the DoD capitalization threshold in the possession of contractors. The Air Force does not report the value of equipment purchased directly by the contractor. The Inspector General, DoD, and the Air Force are developing new policies and a contractor reporting process to capture General PP&E information for future reporting purposes in compliance with generally accepted accounting principles.



Heritage Assets and Stewardship Land

The Air Force's overall mission is to deliver sovereign options for the defense of the United States of America and its global interests to fly, fight, and win in air, space, and cyberspace. As this mission has been executed, Air Force has become a large-scale owner of historic buildings, structures, archeological sites and artifacts, aircraft, other cultural resources, and stewardship land. The protection of the nation's heritage assets and stewardship land is an important aspect of the Air Force's mission.

Heritage Assets are PP&E of historical, natural, cultural, educational or artistic significance (e.g. aesthetic); or with significant architectural characteristics. Heritage Assets and Stewardship Land are resources that protect, restore, enhance, modernize, preserve and sustain mission capability within the Air Force through effective planning and management of natural and cultural resources to guarantee access to air, land, and water. These assets are resources that are managed to provide multiple-use activities for the public benefit. This includes actions to comply with requirements such as federal laws, Executive Orders, policies, final governing standards, and other binding agreements. Air Force policy is to promote and preserve indefinitely the identifiable human, environmental or civic value of these assets.

Stewardship Land comprises land and land rights other than that acquired for or in connection with General PP&E, land acquired via the public domain, or land acquired at no cost. Air Force policy is to promote and preserve indefinitely the identifiable human, environmental or civic value of such land

The Air Force reported 6,470,000 acres of mission-essential land under its administration. Land purchased by the Air Force with the intent to construct buildings or facilities is considered General PP&E and is reported on the balance sheet. All Stewardship Land, as reported, is in acceptable condition based on designated use.

Heritage Assets within the Air Force consist of buildings and structures, archeological sites, museum collection items (objects, not including fine art), and museum collection items (fine art). The Air Force's accounting systems generally do not capture information relative to heritage assets separately and distinctly from normal operations. Although the underlying accounting and recordkeeping systems track the quantities of these assets, and, in some cases, their historical cost, information regarding their fair market value is not readily available.

Buildings and Structures: Buildings and Structures that are listed on, or eligible for listing on the National Register of Historic Places (NRHP), including multi-use facilities, are Heritage Assets. These buildings and structures are maintained in accordance with the National Historic Preservation Act (NHPA), and "The Secretary of Interior's Standards for The Treatment of Historic Properties" by each base's civil engineering group, as part of their overall responsibility. The Air Force reported 7,154 buildings and structures on Air Force installations and sites to be Heritage Assets as of Sep 2012. Installation Cultural Resource Managers (CRMs) reported that 187 Heritage Assets were added to the AF inventory in FY12, and that 1,609 were deleted. Those deleted comprise Heritage Assets covered by the 2008 Capehart-Wherry Era Housing, and the 2010 Cold War Era Ammunition Storage Facilities, and Cold War Era Unaccompanied Housing nation-wide programmatic agreements that completed NHPA Section 106 review for these abundant facilities. The 187 increase in Heritage Asset buildings and structures reflects the ongoing annual NHPA responsibility of Air Force to survey and evaluate the National Register of Historic Property (NRHP) eligibility of buildings and structures as they approach 50 years of age. The number of Heritage Asset buildings and structures is nearly 7% of the total built inventory, which equals 105,627 buildings and structures owned or controlled by the Air Force.

Heritage Asset buildings and structures are maintained by each base civil engineering group and are considered to be in good condition. These buildings and structures are subject to NHPA, Section 106 review and consultation requirements whenever Air Force undertakings might affect their historic characteristics.

Section 106 reviews ensure State Historic Preservation Officers, tribal leaders, and other party concerns are taken into account when Air Force decides to adversely affect Heritage Asset buildings and structures.

Archeological Sites: Prehistoric and historic archaeological sites that have been identified, evaluated, and determined to be eligible for or are listed on the National Register of Historic Places in accordance with NHPA Section 110. The Air Force reports 2,649 archeological sites on or eligible for listing on the National Register as of Sep 2012, up 235 from the 2,414 reported for FY2011. This cohort of archaeological Heritage Assets is a subset of over 19,000 archaeological sites recorded on Air Force controlled and owned lands in the USA and its Territories.

Museum Collection Items, Objects Not Including Fine Art: This represents the number of objects which meet the criteria for historical property as defined in Air Force Instruction 84-103 and that have been evaluated, accessioned, and catalogued in the Air Force national historical collection. The National Museum of the United States Air Force (NMUSAF) performs inherently governmental functions by fulfilling statutory requirements delegated by the Secretary of the Air Force for management of the Air Force's national historic collection. The NMUSAF is fully accredited by the American Association of Museums.

During the period 1 October 2011 – 30 September 2012 there have been 4,775 objects added to the collection. These additions are a result of private donations, transfers from Air Force or other federal entities, curatorial administrative actions, and the continued documentation of newly reported artifacts at Air Force activities worldwide. 195 objects were deaccessioned from the collection as having been determined not to meet historic property criteria, were in poor condition, or were transferred to other federal historical activities. As part of the NMUSAF's active collection management process, the accession and deaccession of objects is continuous.

The overall condition of the historic collection, which is primarily located at the NMUSAF, is very good as a result of both the professional care from trained conservators and ever improving exhibit/storage conditions. During FY2012 detailed restoration work continued on the B-17F "Memphis Belle" and the Douglas A-1H "Skyraider".

Museum Collection Items, Fine Art

The art collection contains original oils, drawing, sketches and sculptures. These paintings were in direct result of the artists visiting bases and operations throughout the Air Force. This represents 86 additions from the Air Force Art Program and 1,355 pieces of fine art from the National Museum of the United States Air Force for this FY. Included in the number above are fine art paintings inclusive of the National Museum of the United States Air Force holding. The collection is maintained and kept in good condition.



Assets Under Capital Lease

As of September 30	2012	2011
(Amounts in thousands)		
1. Entity as Lessee, Assets Under Capital Lease		
A. Land and Buildings	\$ 106,922	\$ 372,563
B. Equipment	0	0
C. Accumulated Amortization	(91,442)	(338,806)
D. Total Capital Leases	\$ 15,480	\$ 33,757

Note 11. Liabilities Not Covered by Budgetary Resources

As of September 30	2012	2011
(Amounts in thousands)		
1. Intragovernmental Liabilities		
A. Accounts Payable	\$ 0	\$ 0
B. Debt	0	0
C. Other	436,543	355,740
D. Total Intragovernmental Liabilities	\$ 436,543	\$ 355,740
2. Nonfederal Liabilities		
A. Accounts Payable	\$ (209,471)	\$ 410,321
B. Military Retirement and Other Federal Employment Benefits	1,148,192	1,118,609
C. Environmental Liabilities	8,022,732	9,596,842
D. Other Liabilities	3,080,304	3,000,313
E. Total Nonfederal Liabilities	\$ 12,041,757	\$ 14,126,085
3. Total Liabilities Not Covered by Budgetary Resources	\$ 12,478,300	\$ 14,481,826
4. Total Liabilities Covered by Budgetary Resources	\$ 13,485,258	\$ 10,285,058
5. Total Liabilities	\$ 25,963,558	\$ 24,766,884

Relevant Information for Comprehension

Liabilities Not Covered by Budgetary Resources includes liabilities for which congressional action is needed before budgetary resources can be provided.

The material amounts and sensitive areas included in Total Liabilities Not Covered by Budgetary Resources are categorized as not covered because there is no current or immediate appropriation available for liquidation. These

liabilities will require resources funded from future year appropriations. The Air Force fully expects to receive the necessary resources to cover these liabilities in future years.

Other Intragovernmental Liabilities are primarily comprised of Federal Employees' Compensation Act (FECA) liabilities to the Department of Labor and other unfunded employment related liabilities.

Other Nonfederal Liabilities are primarily comprised of the amounts recorded for unpaid leave earned to which an employee is entitled upon separation and for contingent liabilities which are probable and measurable and will require resources funded from future years' appropriations.

Military Retirement and Other Federal Employment Benefits consists of various employee actuarial liabilities not due and payable during the current fiscal year. These liabilities primarily consist of the amount recorded by employer agencies for the actuarial present value of future FECA benefits provided to federal employees or their beneficiaries as a result of work related deaths, disability, or occupational disease. Refer to Note 17, Military Retirement and Other Federal Employment Benefits, for additional details and disclosures.

The abnormal balance in Nonfederal Liabilities Accounts Payable of \$209.5 million can be attributed mainly to abnormal balances reported for accounts payable in cancelled appropriations for Operation and Maintenance, Aircraft Procurement, and Research, Development Test & Evaluation.

Note 12.	Accounts Payable
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As of September 30	2012		
	Accounts Payable	Interest, Penalties, and Administrative Fees	Total

(Amounts in thousands)

1. Intragovernmental Payables	\$ 2,493,312	\$ N/A	\$ 2,493,312
2. Nonfederal Payables (to the Public)	4,435,295	(15)	4,435,280
3. Total	\$ 6,928,607	\$ (15)	\$ 6,928,592

As of September 30	2011		
	Accounts Payable	Interest, Penalties, and Administrative Fees	Total

(Amounts in thousands)

1. Intragovernmental Payables	\$ 2,553,975	\$ N/A	\$ 2,553,975
2. Nonfederal Payables (to the Public)	3,013,900	35	3,013,935
3. Total	\$ 5,567,875	\$ 35	\$ 5,567,910



Relevant Information for Comprehension

Accounts Payable include amounts owed to federal and nonfederal entities for goods and services received by Air Force. The Air Force's systems do not track intragovernmental transactions by customer at the transaction level. Buyer-side accounts payable are adjusted to agree with intra-agency seller-side accounts receivable. Accounts Payable were adjusted by accruing additional accounts payable and expenses.

Note 13.	Debt
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Not applicable

Note 14. Environmental Liabilities and Disposal Liabilities

As of September 30	2012	2011
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(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)	\$ 5,427,336	\$ 6,246,261
2. Active Installations—Military Munitions Response Program (MMRP)	554,667	351,864
3. Formerly Used Defense Sites—IRP and BD/DR	0	0
4. Formerly Used Defense Sites--MMRP	0	0

B. Other Accrued Environmental Liabilities—Non-BRAC

1. Environmental Corrective Action	14,722	15,489
2. Environmental Closure Requirements	1,253,417	1,253,417
3. Environmental Response at Operational Ranges	0	0
4. Asbestos	467,582	888,960
5. Non-Military Equipment	34,175	34,175
6. Other	0	0

C. Base Realignment and Closure Installations

1. Installation Restoration Program	1,282,013	1,646,347
2. Military Munitions Response Program	14,018	13,073
3. Environmental Corrective Action / Closure Requirements	82	78,635
4. Asbestos	0	0
5. Non-Military Equipment	0	0
6. Other	0	0

D. Environmental Disposal for Military Equipment / Weapons Programs

1. Nuclear Powered Military Equipment / Spent Nuclear Fuel	0	0
2. Non-Nuclear Powered Military Equipment	36,402	36,402
3. Other Weapons Systems	0	0

E. Chemical Weapons Disposal Program

1. Chemical Demilitarization - Chemical Materials Agency (CMA)	0	0
2. Chemical Demilitarization - Assembled Chemical Weapons Alternatives (ACWA)	0	0
3. Other	0	0

2. Total Environmental Liabilities	\$ 9,084,414	\$ 10,564,623
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Relevant Information for Comprehension

Other Information Related to Environmental Liabilities

An environmental liability is a probable and measurable future outflow or expenditure of resources that exists as of the financial reporting date for environmental cleanup costs resulting from past transactions or events. The Air Force acknowledges that liabilities can change for environmental cleanup costs to include (1) costs associated with environmental restoration of sites funded under the Air Force portion of the Defense Environmental Restorations Program (DERP); (2) corrective actions funded with other than DERP, Base Realignment and Closure (BRAC); and (3) environmental costs associated with future closure or disposal of facilities, equipment, asbestos, and weapon systems. These costs include researching and determining the existence of hazardous waste; removing, containing, and/or disposing of hazardous waste from property; or material and property that consist of hazardous waste at the time of shutdown or disposal of the asset. Cleanup costs may include, but are not limited to, decontamination, decommissioning, site restoration, site monitoring, closure, and post closure costs related to Air Force operations that result in hazardous waste.

Applicable Laws and Regulations of Cleanup, Closure, and Disposal Requirements.

The Air Force is required to clean up contamination resulting from past waste disposal practices, leaks, spills and other past activity, which has created a public human health or environmental risk. Air Force does this in coordination with regulatory agencies and, if applicable, with other responsible parties. The Air Force is also required to recognize closure, post closure and disposal costs for its Property, Plant and Equipment (PP&E) and environmental corrective action costs for current operations. The Air Force is responsible for tracking and reporting all required environmental information related to environmental restoration and corrective action, closure and disposal costs of PP&E, and environmental costs related to BRAC actions that have taken place in prior years. Applicable laws and regulations for cleanup requirements are:

- Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA)
- Superfund Amendments and Reauthorization Act (SARA)
- Clean Water Act
- Safe Drinking Water Act
- Clean Air Act
- Resource Conservation and Recovery Act (RCRA)
- Toxic Substances Control Act (TSCA)
- Medical Waste Tracking Act
- Atomic Energy Act
- Nuclear Waste Policy Act
- Low Level Radioactive Waste Policy Amendments Act

Types of Environmental Liabilities Identified

The Air Force has environmental liabilities for clean-up requirements for active installations: Installation Restoration Program, Building Demolition and Debris Removal, Military Munitions Response Program, and Environmental Corrective Action. The Air Force also has environmental liabilities for cleanup requirements at installations closed under BRAC. Finally, the Air Force has identified environmental liabilities for closure and disposal of PP&E to include facilities, general equipment, asbestos, and weapon systems. All clean-up is done in coordination with regulatory agencies, other responsible parties, and current property owners.

The Air Force reports a \$0 balance for line items where another DoD Entity is designated as DoD Executive Agent. Executive agents are responsible for identifying funding requirements and disclosing financial information regarding the progress of this program. The United States Army Corps of Engineers is the Executive agent for Formerly Used Defense Sites. The Department of the Navy is the Executive Agent for environmental liabilities due to Nuclear Powered Military Equipment and Spent Nuclear Fuel, and the Department of the Army is the Executive Agent for environmental liabilities related to the chemical weapons program.

Method for Assigning Estimated Total Cleanup Costs to Current Operating Periods

The Air Force uses engineering estimates and independently validated models to estimate environmental cleanup costs. The models are either developed within the Remedial Action Cost Engineering Requirements application, or a historic comparable project, a specific bid, or an independent government cost estimate is referenced for the current project. The Air Force validates the models in accordance with DoD Instruction 5000.61 and uses the models to estimate environmental cleanup costs based on data received during a preliminary assessment and initial site investigation. The Air Force primarily uses engineering estimates after obtaining data during the remedial investigation/feasibility phase of the environmental project. The Air Force has already expensed the costs for cleanup associated with General PP&E placed into service prior to October 1, 1997, unless the costs are intended to be recovered through user charges. If the costs are recovered through user charges, the Air Force expenses cleanup costs associated with that portion of the asset life that has passed since the General PP&E was placed into service. The Air Force systematically recognizes the remaining cost over the life of the assets. The unrecognized portion of the estimated total cleanup costs associated with general property, plant, and equipment is \$373 million.

Once the environmental cleanup cost estimates are complete, Air Force will comply with accounting standards to assign costs to current operating periods. The Air Force Accrued Environmental Restoration Liability is accounted for as a totally self contained program. All direct and indirect costs of the program are captured and reported. The Air Force systematically recognizes the remaining cost over the life of the assets.

The accounting standards also require environmental liabilities recognized for closure and disposal requirements. Air Force has closure requirements or disposal liabilities at active installations. Closure and disposal liabilities for facilities (including landfills), asbestos, general equipment and weapon systems are estimated for the applicable inventory of real property, general equipment and weapon systems. Air Force uses a set of historical disposal factors to estimate the environmental disposal liability for each asset and the estimated closure and monitoring cost for landfills. The current liability for these classes of assets is determined from the related disposal programs including the resources expected to be expended in the next year from prior and future budgets.

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

The Air Force is not aware of any pending changes to reported values of Environmental Liabilities but recognizes that changes may occur in the future due to changes in laws and regulations, changes in agreements with regulatory agencies, and advances in technology.

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

The environmental liabilities for the Air Force are based on accounting estimates, which require certain judgments and assumptions that are reasonable based upon information available at the time the estimates are calculated. The actual results may materially vary from the accounting estimates if agreements with regulatory agencies require remediation to a different degree than anticipated when calculating the estimates. Liabilities can be further affected if investigation of the environmental sites reveals contamination levels that differ from the estimate parameters.

The Air Force has the potential to incur costs for restoration initiatives in conjunction with returning overseas Defense facilities to host nations. The Air Force is unable to provide a reasonable estimate at this time because the extent of required restoration necessary for returning an installation to a host nation is unknown.

Other Disclosures

The total Air Force Active Installations environmental liabilities decreased from FY11 to FY12 due to the following environmental restoration activities: the reduction in manpower due to further centralization of restoration personnel's roles and responsibilities, and the re-programming of the Department of Defense and State Memorandum of Agreement (DSMOA) to align with States' funding requests based on anticipated level of effort to support installation programs.

There was a liability variation from FY11 to FY12 of more than 10% in the Asbestos line of Other Accrued Environmental Liabilities – Active Installations. This variation was primarily due to the use of updated real property data, which included significant changes in the inventory through the recording additions and deletions of real property assets in the Air Force inventory.



The total Air Force BRAC environmental liabilities decreased from FY11 to FY12 due to the following environmental restoration activities: the application of Legacy BRAC funding towards accelerated site cleanup/closure at several installations; execution of Performance Based Remediation (PBR) contracts; and successful negotiations and signed Record of Decision (ROD) at the former McClellan AFB. There was a liability variation from FY11 to FY12 of more than 10% at 28 Legacy BRAC and 2 BRAC05 installations. This was primarily due to a site evaluation resulting in reallocation of site restoration costs that were directly attributable to environmental cleanup but previously captured under management. In addition, a variation from FY 11 to FY 12 in excess of 10% resulted from a re-assignment of liabilities in the BRAC program from the Environmental Corrective Action / Closure Requirements line to the Installation Restoration Program line. Although individual environmental liabilities increased at several installations, overall environmental liabilities decreased year over year.

Note 15. Other Liabilities

As of September 30

		2012		
		Current Liability	Noncurrent Liability	Total

(Amounts in thousands)

1. Intragovernmental

A. Advances from Others	\$	803,355	\$	0	\$	803,354
B. Deposit Funds and Suspense Account Liabilities		364,794		0		364,794
C. Disbursing Officer Cash		262,061		0		262,061
D. Judgment Fund Liabilities		133,841		0		133,841
E. FECA Reimbursement to the Department of Labor		112,446		141,686		254,132
F. Custodial Liabilities		0		291,434		291,434
G. Employer Contribution and Payroll Taxes Payable		35,263		0		35,263
H. Other Liabilities		48,777		0		48,777
I. Total Intragovernmental Other Liabilities	\$	1,760,537	\$	433,120	\$	2,193,657

2. Nonfederal

A. Accrued Funded Payroll and Benefits	\$	1,792,119	\$	0	\$	1,792,119
B. Advances from Others		65,755		0		65,755
C. Deferred Credits		0		0		0
D. Deposit Funds and Suspense Accounts		122,892		0		122,892
E. Temporary Early Retirement Authority		0		0		0
F. Nonenvironmental Disposal Liabilities						
(1) Military Equipment (Nonnuclear)		0		0		0
(2) Excess/Obsolete Structures		0		0		0
(3) Conventional Munitions Disposal		0		0		0
G. Accrued Unfunded Annual Leave		2,645,132		0		2,645,132
H. Capital Lease Liability		2,020		22,208		24,228
I. Contract Holdbacks		92,993		0		92,993
J. Employer Contribution and Payroll Taxes Payable		62,990		0		62,990
K. Contingent Liabilities		0		1,792,951		1,792,951
L. Other Liabilities		7,480		0		7,480
M. Total Nonfederal Other Liabilities	\$	4,791,381	\$	1,815,159	\$	6,606,540

3. Total Other Liabilities

	\$	6,551,918	\$	2,248,279	\$	8,800,197
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As of September 30

		2011		
		Current Liability	Noncurrent Liability	Total

(Amounts in thousands)

1. Intragovernmental

A. Advances from Others	\$	775,017	\$	0	\$	775,017
B. Deposit Funds and Suspense Account Liabilities		286,744		0		286,744
C. Disbursing Officer Cash		282,156		0		282,156
D. Judgment Fund Liabilities		46,328		0		46,328
E. FECA Reimbursement to the Department of Labor		107,062		145,379		252,441
F. Custodial Liabilities		0		294,281		294,281
G. Employer Contribution and Payroll Taxes Payable		35,059		0		35,059
H. Other Liabilities		57,309		0		57,309
I. Total Intragovernmental Other Liabilities	\$	1,589,675	\$	439,660	\$	2,029,335

2. Nonfederal

A. Accrued Funded Payroll and Benefits	\$	1,038,388	\$	0	\$	1,038,388
B. Advances from Others		43,375		0		43,375
C. Deferred Credits		0		0		0
D. Deposit Funds and Suspense Accounts		130,133		0		130,133
E. Temporary Early Retirement Authority		0		0		0
F. Nonenvironmental Disposal Liabilities						
(1) Military Equipment (Nonnuclear)		0		0		0
(2) Excess/Obsolete Structures		0		0		0
(3) Conventional Munitions Disposal		0		0		0
G. Accrued Unfunded Annual Leave		2,645,982		0		2,645,982
H. Capital Lease Liability		7,154		28,128		35,282
I. Contract Holdbacks		101,974		0		101,974
J. Employer Contribution and Payroll Taxes Payable		226,373		0		226,373
K. Contingent Liabilities		875,791		354,027		1,229,818
L. Other Liabilities		27,548		0		27,548
M. Total Nonfederal Other Liabilities	\$	5,096,718	\$	382,155	\$	5,478,873

3. Total Other Liabilities

	\$	6,686,393	\$	821,815	\$	7,508,207
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Relevant Information for Comprehension

Intragovernmental Other Liabilities represent government contributions for employee benefits and unemployment compensation.

Nonfederal Other Liabilities reflect accrued moving allowance and miscellaneous expenses to contractors.

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

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

Estimation Methodology

The Air Force General Counsel, through legal determination, assesses and categorizes all contingent legal liability cases that equal or exceed the materiality threshold set by Department of Defense Inspector General (DoDIG). For the remaining cases falling below the dollar materiality threshold set by DoDIG, they are considered in aggregate, if the total amount of the cases equal or exceed the established materiality threshold.

The Air Force General Counsel also solicits case data through quarterly data calls from the Air Force JAC (Judge Advocate Civil Lawsuits and Litigation Directorate). Air Force financial management personnel use the solicited case data, which include the current reporting year and each of the prior two years, to estimate the amounts of probable and reasonably possible contingent liabilities. See Note 16 for detailed disclosure of contingent liabilities.

Air Force financial management personnel use a three-year prior case analysis spreadsheet, which was developed by the Air Force Audit Agency, to calculate and estimate the amount of contingent liabilities (probable and reasonably possible) for reporting or disclosing in the quarterly financial statements. In cases where Air Force General Counsel discloses that a judgment has been awarded against the Air Force, these amounts will be reported on the Balance Sheet and within this note.



Capital Lease Liability

As of September 30

2012

Asset Category

Land and Buildings

Equipment

Other

Total

(Amounts in thousands)

1. Future Payments Due

A. 2013	\$	9,462	\$	0	\$	0	\$	9,462
B. 2014		8,688		0		0		8,688
C. 2015		8,688		0		0		8,688
D. 2016		0		0		0		0
E. 2017		0		0		0		0
F. After 5 Years		0		0		0		0
G. Total Future Lease Payments Due	\$	26,838	\$	0	\$	0	\$	26,838
H. Less: Imputed Interest Executory Costs		2,610		0		0		2,610
I. Net Capital Lease Liability	\$	24,228	\$	0	\$	0	\$	24,228

2. Capital Lease Liabilities Covered by Budgetary Resources

\$ 24,228

3. Capital Lease Liabilities Not Covered by Budgetary Resources

\$ 0

As of September 30

2011

Asset Category

Land and Buildings

Equipment

Other

Total

(Amounts in thousands)

1. Future Payments Due

A. 2012	\$	36,786	\$	0	\$	0	\$	36,786
B. 2013		13,088		0		0		13,088
C. 2014		9,462		0		0		9,462
D. 2015		8,688		0		0		8,688
E. 2016		8,688		0		0		8,688
F. After 5 Years		0		0		0		0
G. Total Future Lease Payments Due	\$	76,712	\$	0	\$	0	\$	76,712
H. Less: Imputed Interest Executory Costs		41,429		0		0		41,429
I. Net Capital Lease Liability	\$	35,283	\$	0	\$	0	\$	35,283

2. Capital Lease Liabilities Covered by Budgetary Resources

\$ 35,283

3. Capital Lease Liabilities Not Covered by Budgetary Resources

\$ 0

Note 16. Commitments and Contingencies

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

The Air Force has accrued contingent liabilities for legal actions where the Secretary of the Air Force General Counsel (SAF/GC) considers an adverse decision probable and the amount of loss measurable. In the event of an adverse judgment against the Government, some of the liabilities may be payable from the U.S. Treasury Judgment Fund. The Air Force records contingent liabilities in Note 15, Other Liabilities.

Claims and litigation from Civil Law having a reasonably possible liability are estimated at \$221.8 million. Neither past payments nor the current contingent liability estimate provides a basis for accurately projecting the results of any individual lawsuit or claim. Since monetary judgments paid to civil litigants come from a judgment fund administered by U.S. Treasury, it is uncertain that claims will become a liability to the Air Force.

The amounts disclosed for litigation claims and assessments are fully supportable and must agree with Force's legal representation letters and management summary schedule.

The amount of obligations related to cancelled appropriations for which the reporting entity has a contractual commitment for payment is \$826.6 million.

The Air Force is a party in numerous individual contracts that contain clauses, such as price escalation, award fee payments, or dispute resolution, that may result in a future outflow of budgetary resources. Currently, the Air Force has limited automated system processes by which it captures or assesses these potential liabilities; therefore, the amounts reported may not fairly present Air Force commitments and contingencies.

The estimated probable liability amount of \$1.8 billion was recognized in Note 15 as contingent liabilities.

In addition, Air Force recognized the total estimated probable liability for claims and litigation against the Air Force, handled by the Civil Law and Litigation Directorate, as of September 30, 2012, valued at \$434 million, included in Nonfederal Contingent Liabilities. As of June 30, 2011, the Air Force was party to 3,535 claims and litigation actions. This liability dollar amount recorded in the financial statements is an estimate based on the weighted average payout rate for the previous three years. There are only two types of cases where U.S. Treasury will seek reimbursements from the affected agency, the Contract Dispute Act cases and select Federal Government personnel disciplinary matters.

The SAF/GC developed the estimating methodology for the contingent liabilities recognized in Note 15.

In cases where SAF/GC disclosed that a judgment has been awarded against the Air Force, these amounts were reported on the Balance Sheet and within Note 15.



Note 17. Military Retirement and Other Federal Employment Benefits

As of September 30	2012		
	Liabilities	(Less: Assets Available to Pay Benefits)	Unfunded Liabilities
(Amounts in thousands)			
1. Pension and Health Benefits			
A. Military Retirement Pensions	\$ 0	\$ 0	\$ 0
B. Military Pre Medicare-Eligible Retiree Health Benefits	0	0	0
C. Military Medicare-Eligible Retiree Health Benefits	0	0	0
D. Total Pension and Health Benefits	\$ 0	\$ 0	\$ 0
2. Other Benefits			
A. FECA	\$ 1,148,192	\$ 0	\$ 1,148,192
B. Voluntary Separation Incentive Programs	0	0	0
C. DoD Education Benefits Fund	0	0	0
D. Other	2,161	(2,161)	0
E. Total Other Benefits	\$ 1,150,353	\$ (2,162)	\$ 1,148,192
3. Total Military Retirement and Other Federal Employment Benefits:			
	\$ 1,150,353	\$ (2,162)	\$ 1,148,192

As of September 30	2011		
	Liabilities	(Less: Assets Available to Pay Benefits)	Unfunded Liabilities
(Amounts in thousands)			
1. Pension and Health Benefits			
A. Military Retirement Pensions	\$ 0	\$ 0	\$ 0
B. Military Pre Medicare-Eligible Retiree Health Benefits	0	0	0
C. Military Medicare-Eligible Retiree Health Benefits	0	0	0
D. Total Pension and Health Benefits	\$ 0	\$ 0	\$ 0
2. Other Benefits			
A. FECA	\$ 1,118,609	\$ 0	\$ 1,118,609
B. Voluntary Separation Incentive Programs	0	0	0
C. DoD Education Benefits Fund	0	0	0
D. Other	7,533	(7,533)	0
E. Total Other Benefits	\$ 1,126,142	\$ (7,533)	\$ 1,118,609
3. Total Military Retirement and Other Federal Employment Benefits:			
	\$ 1,126,142	\$ (7,533)	\$ 1,118,609

Relevant Information for Comprehension

Programs for which actuarial benefits are computed include the Federal Employees' Compensation Act (FECA); the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases; and a component for incurred but not reported claims.

FECA liability is determined using a method that utilizes historical benefit payment patterns to predict the ultimate payments. The projected annual benefit payments are then 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:

Discount Rates

2.293% in Year 1
3.138% 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 Adjustment (COLA)] and medical inflation factors [Consumer Price Index Medical (CPIM)] were applied to the calculation of projected future benefits. The actual rates for these factors for the charge-back year (CBY) 2012 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:

<u>CBY</u>	<u>COLA</u>	<u>CPIM</u>
2012	N/A	N/A
2013	2.83%	3.65%
2014	2.03%	3.66%
2015	1.93%	3.72%
2016	2.00%	3.73%
2017	2.03%	3.80%
and thereafter		

The model's resulting projections were analyzed to ensure that the estimates were reliable. 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 2012 to the average pattern observed during the most current three charge-back years, and (4) a comparison of the estimated liability per case in FY 2012 projection to the average pattern for the projections of the most recent three years.

The Air Force's actuarial liability for workers' compensation benefits is developed and provided by Department of Labor at the end of each fiscal year. There is no change on a quarterly basis.

Other Federal Employment Benefits is comprised of additional post employment benefits due and payable to military personnel.



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

Intragovernmental Costs and Exchange Revenue

As of September 30	2012	2011
(Amounts in thousands)		
Military Retirement Benefits		
1. Gross Cost		
A. Intragovernmental Cost	\$ 0	\$ 0
B. Nonfederal Cost	0	0
C. Total Cost	<u>\$ 0</u>	<u>\$ 0</u>
2. Earned Revenue		
A. Intragovernmental Revenue	\$ 0	\$ 0
B. Nonfederal Revenue	0	0
C. Total Revenue	<u>\$ 0</u>	<u>\$ 0</u>
3. Losses/(Gains) from Actuarial Assumption Changes for Military Retirement Benefits	\$ 0	\$ 0
Total Net Cost	<u>\$ 0</u>	<u>\$ 0</u>
Civil Works		
1. Gross Cost		
A. Intragovernmental Cost	\$ 0	\$ 0
B. Nonfederal Cost	0	0
C. Total Cost	<u>\$ 0</u>	<u>\$ 0</u>
2. Earned Revenue		
A. Intragovernmental Revenue	\$ 0	\$ 0
B. Nonfederal Revenue	0	0
C. Total Revenue	<u>\$ 0</u>	<u>\$ 0</u>
3. Losses/(Gains) from Actuarial Assumption Changes for Military Retirement Benefits	\$ 0	\$ 0
Total Net Cost	<u>\$ 0</u>	<u>\$ 0</u>
Military Personnel		
1. Gross Cost		
A. Intragovernmental Cost	\$ 12,439,091	\$ 8,872,533
B. Nonfederal Cost	22,926,002	27,518,970
C. Total Cost	<u>\$ 35,365,093</u>	<u>\$ 36,391,503</u>
2. Earned Revenue		
A. Intragovernmental Revenue	\$ (431,674)	\$ (107,779)
B. Nonfederal Revenue	(332,535)	(68,734)
C. Total Revenue	<u>\$ (764,209)</u>	<u>\$ (176,513)</u>
3. Losses/(Gains) from Actuarial Assumption Changes for Military Retirement Benefits	\$ 0	\$ 0
Total Net Cost	<u>\$ 34,600,884</u>	<u>\$ 36,214,991</u>

Operations, Readiness & Support

1. Gross Cost			
A. Intragovernmental Cost	\$	(3,443,037)	\$ 761,642
B. Nonfederal Cost		60,418,590	61,446,276
C. Total Cost	\$	56,975,553	\$ 62,207,918
2. Earned Revenue			
A. Intragovernmental Revenue	\$	(540,912)	\$ (1,906,351)
B. Nonfederal Revenue		93,503	(375,944)
C. Total Revenue	\$	(447,409)	\$ (2,282,295)
3. Losses/(Gains) from Actuarial Assumption Changes for Military Retirement Benefits	\$	0	\$ 0
Total Net Cost	\$	56,528,144	\$ 59,925,623

Procurement

1. Gross Cost			
A. Intragovernmental Cost	\$	19,796,871	\$ 18,771,999
B. Nonfederal Cost		24,613,154	19,934,086
C. Total Cost	\$	44,410,025	\$ 38,706,085
2. Earned Revenue			
A. Intragovernmental Revenue	\$	(463,086)	\$ (430,430)
B. Nonfederal Revenue		(172,771)	(275,309)
C. Total Revenue	\$	(635,857)	\$ (705,739)
3. Losses/(Gains) from Actuarial Assumption Changes for Military Retirement Benefits	\$	0	\$ 0
Total Net Cost	\$	43,774,168	\$ 35,389,001

Research, Development, Test & Evaluation

1. Gross Cost			
A. Intragovernmental Cost	\$	11,745,005	\$ 11,292,973
B. Nonfederal Cost		16,789,869	16,714,772
C. Total Cost	\$	28,534,874	\$ 28,007,745
2. Earned Revenue			
A. Intragovernmental Revenue	\$	(2,908,316)	\$ (2,907,727)
B. Nonfederal Revenue		(1,459,292)	(53,283)
C. Total Revenue	\$	(4,367,608)	\$ (2,961,010)
3. Losses/(Gains) from Actuarial Assumption Changes for Military Retirement Benefits	\$	0	\$ 0
Total Net Cost	\$	24,167,266	\$ 25,046,735



Family Housing & Military Construction			
1. Gross Cost			
A. Intragovernmental Cost	\$	179,138	\$ 128,898
B. Nonfederal Cost		3,518,697	1,009,750
C. Total Cost	\$	3,697,835	\$ 1,138,648
2. Earned Revenue			
A. Intragovernmental Revenue	\$	(11,528)	\$ (15,082)
B. Nonfederal Revenue		(4,098,563)	0
C. Total Revenue	\$	(4,110,091)	\$ (15,082)
3. Losses/(Gains) from Actuarial Assumption Changes for Military Retirement Benefits	\$	0	\$ 0
Total Net Cost	\$	(412,257)	\$ 1,123,566
Consolidated			
1. Gross Cost			
A. Intragovernmental Cost	\$	40,717,069	\$ 39,828,047
B. Nonfederal Cost		128,266,311	126,623,853
C. Total Cost	\$	168,983,380	\$ 166,451,899
2. Earned Revenue			
A. Intragovernmental Revenue	\$	(4,355,517)	\$ (5,367,368)
B. Nonfederal Revenue		(5,969,659)	(3,384,616)
C. Total Revenue	\$	(10,325,176)	\$ (8,751,984)
3. Losses/(Gains) from Actuarial Assumption Changes for Military Retirement Benefits	\$	0	\$ 0
4. Costs Not Assigned to Programs	\$	0	\$ 0
5. (Less: Earned Revenues) Not Attributed to Programs	\$	0	\$ 0
Total Net Cost	\$	158,658,204	\$ 157,699,915

Relevant Information for Comprehension

In 2012 Operations, Readiness & Support reported an abnormal balances for Intragovernmental cost in the amount of \$3.4 billion. This is in relation to transfers to and from other government entities. Because of business practices, sometimes transfers from other Intergovernmental entities are recorded against program cost instead of revenue.

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

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

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

The Air Force's systems do not track intragovernmental transactions by customer at the transaction level. Buyer-side expenses are adjusted to agree with internal seller-side revenue. Expenses are generally adjusted by accruing additional accounts payable and expenses. Intradepartment revenues and expenses are then eliminated.

The Air Force does not meet accounting standards. Information presented is based on budgetary obligations, disbursements, and collection transactions, as well as nonfinancial feeder systems adjusted to record known accruals for major items such as payroll expenses, accounts payable and environmental liabilities.

The Air Force's accounting systems generally 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

Other Financing Sources, Other is comprised of unsupported adjustments to reconcile reported intragovernmental transfers, the majority of which are recorded at the Air Force Component level, as the respective federal partners could not be identified nor the transfers reconciled.

The Appropriations Received on the Statement of Changes in Net Position (SCNP) do not agree with Appropriations on the Statement of Budgetary Resources (SBR) in the amount of \$328 thousand. The difference is due to additional resources included in the Appropriations line item on the SBR. Refer to Note 20, Disclosures Related to the Statement of Budgetary Resources, for further information.

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



Note 20. Disclosures Related to the Statement of Budgetary Resources

As of September 30 (Amounts in thousands)	2012	2011
1. Net Amount of Budgetary Resources Obligated for Undelivered Orders at the End of the Period	\$ 83,077,686	\$ 79,038,813
2. Available Borrowing and Contract Authority at the End of the Period	0	0

Relevant Information for Comprehension

Apportionment Categories

Funds are apportioned by three categories: (1) Category A is apportioned quarterly, (2) Category B is apportioned by activity or project, and (3) Exempt is funds not subject to apportionment. The amounts of direct and reimbursable obligations incurred are stated in the table.

	Category A	Category B	Exempt
Direct	\$96.7 billion	\$75.0 billion	\$2.3 million
Reimbursable	\$6.9 billion	\$3.6 billion	\$ 0 million

Intraentity Transactions

The Statement of Budgetary Resources (SBR) includes intraentity transactions because the statements are presented as combined.

The Statement of Budgetary Resources (SBR) includes intraentity transactions because the statements are presented as combined.

Permanent Indefinite Appropriations

Permanent indefinite appropriations are as follows (reference Note 23 for additional information):

Department of the Air Force General Gift Fund [10 USC 2601(b)]

Wildlife Conservation Fund [16 USC 670(a)]

Air Force Cadet Fund [37 USC 725(s)]

Medicare-Eligible Retiree Health Fund Contribution, Air Force (10 USC 1116)

Medicare-Eligible Retiree Health Fund Contribution, Reserve Personnel, Air Force (10 USC 1116)

Medicare-Eligible Retiree Health Fund Contribution, National Guard Personnel, Air Force (10 USC 1116)

Legal limitations and time restrictions on the use of unobligated appropriation balances such as upward adjustments are provided under Public Law.

Appropriations Received

Appropriations on the SBR differ from those reported on the Statement of Changes in Net Position (SCNP) because (1) Appropriations on the SBR include transfers and permanent reductions to authority and (2) Appropriations Received on the SCNP do not include dedicated appropriations and earmarked receipts. Dedicated appropriations and earmarked receipts are accounted for as either nonexchange revenue or donations and forfeitures of cash and cash equivalents. This resulted in a \$328 thousand difference.



Note 21. Reconciliation of Net Cost of Operations to Budget

As of September 30	2012	2011
(Amounts in thousands)		
Resources Used to Finance Activities:		
Budgetary Resources Obligated:		
1. Obligations incurred	\$ 182,251,092	\$ 177,628,001
2. Less: Spending authority from offsetting collections and recoveries (-)	(15,865,741)	(14,414,018)
3. Obligations net of offsetting collections and recoveries	\$ 166,385,351	\$ 163,213,983
4. Less: Offsetting receipts (-)	(177,075)	(154,152)
5. Net obligations	\$ 166,208,276	\$ 163,059,831
Other Resources:		
6. Donations and forfeitures of property	0	0
7. Transfers in/out without reimbursement (+/-)	(1,200,677)	867,507
8. Imputed financing from costs absorbed by others	763,656	855,639
9. Other (+/-)	3,222,509	(459,953)
10. Net other resources used to finance activities	\$ 2,785,488	\$ 1,263,193
11. Total resources used to finance activities	\$ 168,993,764	\$ 164,323,024
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 (-)	\$ (4,038,873)	\$ (2,517,648)
12b. Unfilled Customer Orders	212,936	(619,759)
13. Resources that fund expenses recognized in prior Periods (-)	(2,115,190)	(416,750)
14. Budgetary offsetting collections and receipts that do not affect Net Cost of Operations	177,075	154,152
15. Resources that finance the acquisition of assets (-)	(11,185,716)	(15,963,606)
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 (+/-)	(2,022,203)	(407,554)
17. Total resources used to finance items not part of the Net Cost of Operations	\$ (18,971,971)	\$ (19,771,165)
18. Total resources used to finance the Net Cost of Operations	\$ 150,021,793	\$ 144,551,859

As of September 30

2012

2011

(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	\$	17,377	\$	73,728
20. Increase in environmental and disposal liability		0		1,725,271
21. Upward/Downward reestimates of credit subsidy expense (+/-)		0		0
22. Increase in exchange revenue receivable from the public (-)		(44,742)		0
23. Other (+/-)		188,189		307,815
24. Total components of Net Cost of Operations that will Require or Generate Resources in future periods	\$	160,824	\$	2,106,814

Components not Requiring or Generating Resources:

25. Depreciation and amortization	\$	11,802,239	\$	15,128,148
26. Revaluation of assets or liabilities (+/-)		2,676,242		(1,761,057)
27. Other (+/-)				
27a. Trust Fund Exchange Revenue		0		0
27b. Cost of Goods Sold		0		0
27c. Operating Material and Supplies Used		23,708,306		27,907,673
27d. Other		(29,711,199)		(30,233,522)
28. Total Components of Net Cost of Operations that will not Require or Generate Resources	\$	8,475,588	\$	11,041,242

29. Total components of Net Cost of Operations that will not Require or Generate Resources in the current period	\$	8,636,412	\$	13,148,056
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30. Net Cost of Operations	\$	158,658,205	\$	157,699,915
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Relevant Information for Comprehension

Due to Air Force financial system limitations, budgetary data do not agree with proprietary expenses and capitalized assets. The difference between budgetary and proprietary data is a previously identified deficiency. The amount of the adjustment to the note schedule to bring it into balance with the Statement of Net Cost is (\$32) million in the Other Components Not Requiring or Generating Resources category.

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
- Less: Offsetting Receipts
- Net Obligations
- Undelivered Orders
- Unfilled Customer Orders

Other Resources Used to Finance Activities consist of other gains to adjust intragovernmental transfers in.

Other Resources Used to Finance Items Not Part of the Net Cost of Operations include adjustments to net obligated resources that do not affect the Net Cost of Operation such as net transfers in and out without reimbursement, and other gains and losses to adjust intragovernmental transfers in.

Other Components of the Net Cost of Operations that will not Require or Generate Resources in the Current Period consist of expenses due to Air Force active military personnel.

Other Components not Requiring or Generating Resources include expenses for Operations and Maintenance, Procurement, Military Construction and Family Housing.

Note 22.	Disclosures Related to Incidental Custodial Collections
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The Air Force collected \$38.4 million of incidental custodial revenues generated primarily from collection of accounts receivable related to cancelled accounts. These funds are not available for use by Air Force. At the end of each fiscal year, the accounts are closed and the balances rendered to the U.S. Treasury.

Note 23. Earmarked Funds

BALANCE SHEET As of September 30 (Amounts in thousands)	2012				
	Military Retirement Fund	Medicare Eligible Retiree Health Care Fund	Other Earmarked Funds	Eliminations	Total
ASSETS					
Fund balance with Treasury	\$ 0	\$ 0	\$ 13,558	\$ 0	\$ 13,558
Investments	0	0	1,072	0	1,072
Accounts and Interest Receivable	0	0	1	0	1
Other Assets	0	0	5,042	0	5,042
Total Assets	\$ 0	\$ 0	\$ 19,672	\$ 0	\$ 19,672

LIABILITIES and NET POSITION

Military Retirement Benefits and Other Federal Employment Benefits	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
Other Liabilities	0	0	202	0	202
Total Liabilities	\$ 0	\$ 0	\$ 202	\$ 0	\$ 202
Unexpended Appropriations	0	0	0	0	0
Cumulative Results of Operations	0	0	19,470	9	19,479
Total Liabilities and Net Position	\$ 0	\$ 0	\$ 19,672	\$ 9	\$ 19,681

STATEMENT OF NET COST

For the period ended September 30 (Amounts in thousands)					
Program Costs	\$ 0	\$ 0	\$ 443	\$ 0	\$ 443
Less Earned Revenue	0	0	(4,837)	0	(4,837)
Net Program Costs	\$ 0	\$ 0	\$ (4,394)	\$ 0	\$ (4,394)
Less Earned Revenues Not Attributable to Programs	0	0	0	0	0
Net Cost of Operations	\$ 0	\$ 0	\$ (4,394)	\$ 0	\$ (4,394)



STATEMENT OF CHANGES IN NET POSITION For the period ended September 30 (Amounts in thousands)	2012				
	Military Retirement Fund	Medicare Eligible Retiree Health Care Fund	Other Earmarked Funds	Eliminations	Total
Net Position Beginning of the Period	\$ 0	\$ 0	\$ 12,425	\$ 0	\$ 12,425
Net Cost of Operations	0	0	(4,394)	0	(4,394)
Budgetary Financing Sources	0	0	2,660	0	2,660
Other Financing Sources	0	0	(9)	9	0
Change in Net Position	\$ 0	\$ 0	\$ 7,045	\$ 9	\$ 7,054
Net Position End of Period	\$ 0	\$ 0	\$ 19,470	\$ 9	\$ 19,479

BALANCE SHEET As of September 30 (Amounts in thousands)	2012				
	Military Retirement Fund	Medicare Eligible Retiree Health Care Fund	Other Earmarked Funds	Eliminations	Total

ASSETS

Fund balance with Treasury	\$ 0	\$ 0	\$ 13,681	\$ 0	\$ 13,681
Investments	0	0	1,077	0	1,077
Accounts and Interest Receivable	0	0	1	0	1
Other Assets	0	0	5	0	5
Total Assets	\$ 0	\$ 0	\$ 14,764	\$ 0	\$ 14,764

LIABILITIES and NET POSITION

Military Retirement Benefits and Other Federal Employment Benefits	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
Other Liabilities	0	0	2,339	0	2,339
Total Liabilities	\$ 0	\$ 0	\$ 2,339	\$ 0	\$ 2,339

Unexpended Appropriations	0	0	0	0	0
Cumulative Results of Operations	0	0	12,425	0	12,425
Total Liabilities and Net Position	\$ 0	\$ 0	\$ 14,764	\$ 0	\$ 14,764

STATEMENT OF NET COST

For the period ended September 30 (Amounts in thousands)					
Program Costs	\$ 0	\$ 0	\$ 12,001	\$ 0	\$ 12,001
Less Earned Revenue	0	0	(216)	0	(216)
Net Program Costs	\$ 0	\$ 0	\$ 11,785	\$ 0	\$ 11,785
Less Earned Revenues Not Attributable to Programs	0	0	0	0	0
Net Cost of Operations	\$ 0	\$ 0	\$ 11,785	\$ 0	\$ 11,785



STATEMENT OF CHANGES IN NET POSITION For the period ended September 30 (Amounts in thousands)	2011				
	Military Retirement Fund	Medicare Eligible Retiree Health Care Fund	Other Earmarked Funds	Eliminations	Total
Net Position Beginning of the Period	\$ 0	\$ 0	\$ 18,568	\$ 0	\$ 18,568
Net Cost of Operations	0	0	11,784	0	11,784
Budgetary Financing Sources	0	0	5,641	0	5,641
Other Financing Sources	0	0	0	0	0
Change in Net Position	\$ 0	\$ 0	\$ (6,143)	\$ 0	\$ (6,143)
Net Position End of Period	\$ 0	\$ 0	\$ 12,425	\$ 0	\$ 12,425

Relevant Information for Comprehension

Department of the Air Force General Gift Fund [10 USC 2601 (b)]

The Department of the Air Force General Gift Fund accepts, holds, and administers any gift, device, or bequest of real or personal property, made on the condition that it is used for the benefit (or in connection with the establishment, maintenance, or operation) of a school, hospital, library, museum, or cemetery under the Air Force’s jurisdiction. The fund is available to such institutions or organizations subject to the terms of the gift, device, or bequest.

Conditional gifts are invested in U.S. Treasury securities, and any interest earned on these securities is accumulated in the fund.

Wildlife Conservation Fund [16 USC 670 (a)]

The Wildlife Conservation Fund provides for (1) the conservation and rehabilitation of natural resources on military installations, (2) the sustainable multipurpose use of the resources which include hunting, fishing, trapping, and nonconsumptive uses, and (3) the public access to military installations to facilitate its use, subject to safety requirements and military security. The fund is available to carry out these programs and other such expenses that may be necessary for the purpose of the cited statute.

Consisting of both appropriated and nonappropriated funding, this fund gives installation commanders the authority to collect fees from the sale of hunting and fishing permits.

Air Force Cadet Fund [37 USC 725 (s)]

The Air Force Cadet Fund is maintained for the benefit of Air Force Academy cadets. Disbursements are made for the personal services of cadets such as laundry, arts, and athletics while collections are received from the same cadets at least equal to any disbursements made.

The Air Force General Gift Fund and Wildlife Conservation Fund are trust funds. The Air Force Cadet Fund is classified as a special fund. All three funds utilize receipt and expenditure accounts in accounting for and reporting the funds.

Note 24. Fiduciary Activities

Schedule of Fiduciary Activity

For the period ended September 30	2012	2011
(Amounts in thousands)		
1. Fiduciary net assets, beginning of year	\$ 37,353	\$ 30,624
2. Fiduciary revenues	0	0
3. Contributions	49,746	53,933
4. Investment earnings	3,047	3,434
5. Gain (Loss) on disposition of investments, net	0	0
6. Administrative and other expenses	0	0
7. Distributions to and on behalf of beneficiaries	(57,629)	(50,639)
8. Increase/(Decrease) in fiduciary net assets	\$ (4,836)	\$ 6,728
9. Fiduciary net assets, end of period	\$ 32,517	\$ 30,352

Schedule of Fiduciary Net Assets

For the period ended September 30	2012	2011
(Amounts in thousands)		
FIDUCIARY ASSETS		
1. Cash and cash equivalents	\$ 32,517	\$ 37,353
2. Investments	0	0
3. Other Assets	0	0
FIDUCIARY LIABILITIES		
4. Less: LIABILITIES	\$ 0	\$ 0
5. TOTAL FIDUCIARY NET ASSETS	\$ 32,517	\$ 37,353

Relevant Information for Comprehension

A fiduciary relationship may exist anytime a Federal Government entity collects or receives, and holds or makes disposition of assets in which a non-federal individual or entity has an ownership interest that the Federal Government must uphold. The relationship is based on statute or other legal authority and the fiduciary activity must be in furtherance of that relationship. The Air Force's fiduciary activities primarily consist of the Savings Deposit Program (SDP). SDP was established to provide members of the uniformed services serving in a designated combat zone the opportunity to build their financial savings.



Note 25. Other Disclosures

As of September 30	2012 Asset Category			
	Land and Buildings	Equipment	Other	Total
(Amounts in thousands)				
1. ENTITY AS LESSEE-Operating Leases				
Future Payments Due				
Fiscal Year				
2012	59,045	0	15,745	74,790
2013	40,594	0	15,903	56,497
2014	39,053	0	16,062	55,114
2015	37,589	0	16,222	53,811
2016	24,614	0	16,384	40,999
After 5 Years	22,738	0	16,125	38,864
Total Future Lease Payments Due	\$ 223,633	\$ 0	\$ 96,441	\$ 320,075

Relevant Information for Comprehension

Leases in the land and buildings category include costs for operating leased facilities for the active Air Force in the United States and overseas. Land and Buildings consist mostly of housing facilities as well as other mission critical assets.

Leases in the other category are made up of commercial leases. Commercial leases are leases made by the Air Force with the general public. These would include leases with dealerships, car rental companies, or any other such entity that provides car leasing services.

Note 26. Restatements

Not applicable for 2012.

General Fund

Fiscal Year 2012

Required Supplementary
Stewardship Information



STEWARDSHIP INVESTMENTS

Stewardship investments are substantial investments made by DoD for the benefit of the nation, but are not physical assets owned by DoD. Stewardship investments include expenses incurred for federally financed, but not federally owned, physical property (Nonfederal Physical Property) and federally financed research and development (Research and Development).

NONFEDERAL PHYSICAL PROPERTY

Nonfederal Physical Property investments are expenses included in calculating net cost incurred by the reporting entity for the purchase, construction or major renovation of physical property owned by state and local governments. The expenses include the costs identified for major additions, alterations and replacements, purchases of major equipment, and purchases or improvements of other nonfederal assets. In addition, Nonfederal Physical Property Investments include federally owned physical property transferred to state and local governments.

NONFEDERAL PHYSICAL PROPERTY					
Yearly Investment in State and Local Governments					
For the Current and Four Preceding Fiscal Years					
(\$ in millions)					
Categories	FY 2012	FY 2011	FY 2010	FY 2009	FY 2008
1. Transferred Assets:					
National Defense Mission Related	0	0	0	0	0
2. Funded Assets:					
National Defense Mission Related	\$ 7.6	\$ 12.0	\$ 11.5	\$ 19.6	\$ 2.8
Totals	\$ 7.6	\$ 12.0	\$ 11.5	\$ 19.6	\$ 2.8

The Air National Guard investments in Nonfederal Physical Property are strictly through the Military Construction Cooperative Agreements (MCCAs). These agreements involve the transfer of money only and allow joint participation with States, Counties, and Airport Authorities for construction or repair of airfield pavements and facilities required to support the flying mission assigned at these civilian airfields.

Investment values included in this report are based on Nonfederal Physical Property outlays (expenditures). Outlays are used because current DoD systems are unable to capture and summarize costs in accordance with the Federal GAAP requirements.

RESEARCH AND DEVELOPMENT

Research and Development investments are incurred in the search for new or refined knowledge and ideas, for the application or use of such knowledge and ideas for the development of new or improved products and processes with the expectation of maintaining or increasing national economic productive capacity or yielding other future benefits.

INVESTMENTS IN RESEARCH AND DEVELOPMENT					
Yearly Investment in Research and Development For the Current and Four Preceding Fiscal Years (\$ in millions)					
Categories	FY 2012	FY 2011	FY 2010	FY 2009	FY 2008
1. Basic Research	\$ 494	\$ 475	\$ 473	\$ 444	\$ 401
2. Applied Research	1,120	1,175	1,120	1,185	1,135
3. Development:					
Advanced Technology Development	598	546	598	709	665
Advanced Component Development and Prototypes	1,179	1,981	1,179	2,283	2,336
System Development and Demonstration	2,783	3,137	2,783	3,925	4,176
Research, Development, Test and Evaluation					
Management Support	1,270	1,440	1,270	1,480	1,521
Operational Systems Development	14,913	18,653	14,913	16,460	15,572
Totals	\$ 22,357	\$ 27,407	\$ 22,336	\$ 26,486	\$ 25,806

RESEARCH AND DEVELOPMENT

Research and Development investments are incurred in the search for new or refined knowledge and ideas, for the application or use of such knowledge and ideas for the development of new or improved products and processes with the expectation of maintaining or increasing national economic productive capacity or yielding other future benefits.

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 a fuller knowledge or understanding of the subject under study. Major outputs are scientific studies and research papers.

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 the practical application of such knowledge or understanding for the purpose of meeting a recognized need. This research points toward specific military needs with a view toward developing and evaluating the feasibility and practicality of proposed solutions and determining their parameters. Major outputs are scientific studies, investigations, research papers, hardware components, software codes, and limited construction of, or part of, a weapon system, to include nonsystem specific development efforts.

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 the following five stages:

1. Advanced Technology Development is the systematic uses of the knowledge or understanding gained from research directed towards proof of technological visibility and assessment of operational and productivity rather than the development of hardware for service use. 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 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 weapon systems finalized for complete operational and developmental 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, operations and maintenance of test aircraft and ships, and studies and analyses in support of the R&D program.

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

The following are representative program examples for each of the above major categories:

Basic Research

AFRL-funded researchers recently achieved several unique breakthroughs in atomic layer deposition, or ALD, a method that puts down a layer of "paint" one-atom thick. The ALD method offers a tremendous range of applications including coating aircraft canopies, particles and nano-particles; creating insulators in integrated circuits; and controlling catalysts and sensors. The ALD application process also offers the revolutionary ability to coat micro-electro-mechanical systems the size of a micron or smaller.

AFRL also funded research in laser light technology that will help the Military create new forms of metal that may guide, attract, and repel liquids and cool small electronic devices. The research team discovered a way to transform a shiny piece of metal into one that is pitch black, not by paint, but by using incredibly intense bursts of laser light. The resulting black metal absorbs all radiation that shines upon it. With the creation of this black metal, an entirely new class of material becomes available which may open up an entirely new horizon for various applications. Additional research has centered on creating technology that may enable the Air Force to create an additional kind of metal by using the femtosecond laser to alter the surface of metal and create unique nano - and micro-scale structures.

Applied Research

The Real-time Active Imaging in 3-D at Extended Range (RAIDER) system is a turreted, 3-D imaging lidar providing terrain mapping and high resolution imaging for combat identification. The system was completed, integrated in the flight turret and successfully conducted multiple missions in support of the CLEAN SWEEP program. RAIDER demonstrated high confidence identification of a wide variety of targets in diverse backgrounds completing the CLEAN SWEEP integrated capability for wide area detection, identification and prosecution of military vehicles.

Munitions scientists from the Air Force Research Laboratory (AFRL) and Lawrence Livermore National Laboratory (LLNL) aggressively designed and tested an advanced warhead to provide precision lethality with low collateral damage. AFRL's 5-month Precision Lethality Mk82 (PL82) Risk Reduction program accelerated Technology Readiness Level (TRL) growth from 5 to 6 through successful warhead blast and target

penetration demonstrations. This quickly provided the technical maturity needed for immediate transition to the BLU-129/B Quick Reaction Capability (QRC) program at the Air Armament Center (AAC), Eglin Air Force Base, Florida, and has been designated as the BLU-129/B warhead.

Advanced Technology Development

The Counter-Electronics High Power Microwave Advanced Missile Project (CHAMP) successfully executed the pointing demonstration during a flight test recently at the Utah Test and Training Range. A major milestone, the test demonstrated the navigational and pointing accuracy of CHAMP's aerial platform and integrated high power microwave (HPM) beam, which can disrupt or damage targeted electronic circuits and components, as well as its ability to correctly trigger the payload with great timing accuracy. CHAMP provides the warfighter a non-lethal, low collateral damage capability against targets and helps keep post-conflict reconstruction costs to a minimum.

Gotcha Radar Exploitation Program (GREP) Data Collect Demonstration: The main goal of the Gotcha Radar Exploitation Program (GREP) data collect demonstration that took place on 26 and 29 September 2011 was to generate real-time (1 second to generate a frame of each of the following) video synthetic aperture radar (SAR), coherent change detection (CCD), and non-coherent change detection (NCD) on a 1.25 km by 1.25 km spot at 1/3 m resolution. This goal was accomplished. It was also possible to generate real time (1 frame per second) video SAR on a 4 km by 4 km spot at 1/3 m resolution and display this video on a touchscreen display. By drawing a box on the screen it was possible (within 30-45 seconds) to do a three dimensional reconstruction using all of the available data up to that point in the demonstration (i.e., all 360 degrees or less). Data transmission from the radar to the Desch supercomputer was accomplished by using the AOptix (optical) datalink. All of this data was kept so further analysis could be done in the future. This system provides a step to the capability to use real-time SAR video to look at change detection and two and three dimensional imaging which could be very useful to the warfighter. Furthermore, by keeping the data, forensic analysis can be done if an incident happens and it is necessary to ascertain what, or who, caused the incident.

Demonstration and Validation (Advanced Component Development and Prototypes):

The Air Force's Advanced Component Development and Prototypes programs are comprised of system specific advanced technology integration efforts accomplished in an operational environment to help expedite transition from the effort. In FY 2004, the Air Force successfully demonstrated Fighter Aircraft Command and Control Enhancement (FACE). FACE provides an improved, beyond-line-of-sight (BLOS) command and control link with fighter aircraft by integrating Iridium telephone communications equipment with existing aircraft communications equipment. BLOS capability has traditionally been provided by low-density, high-demand airborne platforms acting as communications relays. FACE provides relief for these overworked assets, while allowing combatant commanders to maintain positive control of the battle space. FACE has been approved for deployment to Afghanistan through the Air Force's Rapid Response Process, and has the potential for extensive use in virtually any area of responsibility, including Homeland Defense.

System Development and Demonstration:

The F-35 Joint Strike Fighter (JSF) program is developing a family of strike fighter aircraft for the Air Force, Navy, Marine Corps and our allies, with maximum commonality among the variants to minimize life cycle costs. The F-35A Conventional Takeoff and Landing (CTOL) variant will be a multi-role, primary air-to-ground aircraft to replace the F-16 and A-10, and complement the F-22. While the F-22 will establish air dominance, the F-35 with its combination of stealth, large internal payloads and multi-spectral avionics will provide persistent stealth and precision engagement to future battle space. The F-35 is in the 11th year of a 17-year Engineering and Manufacturing Development (EMD) effort. The President's Budget for FY 2012 decreased procurement by 124 aircraft in order to reduce the impacts of concurrent development and production. Significant program accomplishments in FY 2012 include:



- 19 of 20 flight and ground test aircraft have been produced and delivered
- Milestone B was approved on March 28, 2012. The original Milestone B, approved in October 2001, was rescinded in June 2010 due to a critical Nunn McCurdy breach.
- Nine production CTOLs and ten production Short Takeoff and Vertical Landing (STOVL) aircraft have been delivered to Eglin AFB to form the beginning of the training fleet
- Local area operations at Eglin AFB commenced for the CTOL on March 6, 2012 and for the STOVL on May 22, 2012. Over 300 sorties have been flown as of September 30, 2012.
- Low Rate Initial Production (LRIP) Lot 5 airframe and engine contracts were initiated via Unfinalized Contract Actions (UCAs) in December 2011. Negotiations for full contract award are ongoing.
- The CTOL test variants have accomplished the first night flight, first night aerial refueling, and first flight with external weapons
- The first airborne weapon separation test occurred on August 8, 2012. A STOVL variant, traveling at 400 knots at an altitude of 4,200 feet, released a 1,000 lb GBU-32 Joint Direct Attack Munition (JDAM).

The Advanced Extremely High Frequency (AEHF) System is a joint service satellite communications system that will provide survivable, global, secure, protected, and jam-resistant communications for high-priority military ground, sea and air assets. AEHF will allow the National Security Council and Unified Combatant Commanders to control their tactical and strategic forces at all levels of conflict through general nuclear war and supports the attainment of information superiority. The AEHF System is the follow-on to the Milstar system, augmenting and improving on the capabilities of Milstar, and expanding the MILSATCOM architecture.

FY 2012 marked the beginning of operational capability for the constellation. The first satellite, AEHF-1, was launched in August 2010 from Cape Canaveral Air Force Station, Florida. Shortly after launch, an anomaly in the spacecraft's bi-propellant propulsion system (the Liquid Apogee Engine) disrupted its flight. A team of military and civilian engineers devised a sophisticated orbit-raising plan utilizing hydrazine thrusters and Hall Current Thrusters to safely deliver the vehicle to its intended orbit 14 months later. The satellite was transferred to operations in March 2012 without diminishing its designed mission life. AEHF-2 was successfully launched on May 4, 2012 and is expected to complete on-orbit testing in FY 2013.

Research, Development, Test and Evaluation Management Support:

The Air Force's Research, Development, Test and Evaluation (RDT&E) Management Support efforts include projects directed toward support of installations and operations required for testing at the Air Force Major Range and Test Facility Base (MRTFB) Activities.

In FY2012 multiple EW improvement efforts were on going. Per the Air Force Electronic Warfare Evaluation Simulator (AFEWES) transition plan, IR threat simulator hardware and RF threat simulator hardware was moved from the AFEWES facility to the Guided Weapons Evaluation Facility (GWEF) and 412 EWG-OL_HN at Edwards AFB and capability reconstitution planning was initiated. Digital Integrated Air Defense System (DIADS) developed and validated upgrades to simulate evolving threats in support of F-22 and MALD-J. The Advanced Warfare Test and Evaluation Capability (AWTEC) continued Benefield Anechoic Chamber (BAF) upgrades by completing EMI/EMC power upgrades and fielding new products for improved test management and new real-time displays and controls. The National Radar Cross Section Test Facility (NRTF) at Holloman AFB continued efforts to enhance efficiency operations and accuracy for measuring Radar Cross Section (RCS) of low observable platforms and antennas, including design and fabrication of a new operational control center and adaptive signal processing and antenna development.

Other significant improvement and modernization efforts at the AF test facilities in 2012 were focused on Airframe, Propulsion, and Avionics (APA) or Armament/Munitions (A/M). The Advanced Range Systems Upgrade (ARSU) fielded critical infrastructure upgrades to the operational control center, digital handling systems, and data display and analysis systems at the 412TW range at Edwards AFB to manage obsolescence. The Von Karmen Facility (VFK) plant modernization project completed additional rewinds and control room modifications improving efficiency, performance, reliability, and maintainability of the VKF compressor facility that supplies high pressure air to all AEDC test cells. Lastly, the Advanced Command Destruct System (ACDS) project completed procurement and continued integration efforts to upgrade the command destruct systems supporting test missions at Eglin AFB and Edwards AFB. The Next Generation Munitions Test Environment (NGMTE) project began design, development, and procurement efforts to upgrade aging guns and munitions test capabilities to support advent of modern, smarter weapon systems requiring more precise data.

Operational Systems Development:

The Air Force's operational system efforts include projects in support of development acquisition programs or upgrades. The F-22 Raptor program concluded assembly and delivery of all 178 operational fleet aircraft in May of 2012. As outstanding a capability the Raptor currently provides, the program will continue to maintain its role as enabler of joint air dominance for years to come through a series of Operational Systems Development activities. Increment 2 is resident in delivered aircraft and represents the first upgrade over initial operational capability. The modernization program will enhance the air vehicle, engine, and training systems to improve F-22A weapons, communications, and Intelligence Surveillance Reconnaissance (ISR) capabilities to further enhance Global Strike capabilities. FY 2012 activities included the initial fielding of the Increment 3.1 suite and the Critical Design review in February 2012 of Increment 3.2A, a software only upgrade to significantly improve electronic protection and combat identification capabilities of the F-22. In addition, the Increment 3.2B Preliminary Design Review was completed in June 2012 and this upgrade will dramatically improve the F-22A Raptor's Air-to-Air and Air-to-Ground attack capabilities with AIM-9X, AIM-120D, improved geolocation capabilities and electronic protection enhancements.

Shrinking force structure, increased tasking, evolving threats, and collateral damage avoidance will drive a demand for a precision strike capability with a mission planned datalink equipped weapon. SDB II will provide strike aircraft with a capability to attack stationary and mobile targets through the weather with standoff capability while retaining miniature munition type weapon attributes (effective day/night, adverse weather, increased load-out, focused logistics, etc.) plus the capability to attack a range of stationary targets across the combat arena. The 42-month Risk Reduction competition between two contractors that commenced in May 2006 to mature critical technologies for an all-up-round design completed in October 2009. Following the Risk Reduction Phase, a single contractor was selected to complete an approximately 59 month EMD contract with production options. The Milestone B review occurred 27 Jul 2010, with Critical Design Review taking place the first half of FY11. Production for SDB II is scheduled to start FY 2014 and continue through FY2023. Required Assets Available on the F-15E is planned for FY2016.

Reaper (MQ-9) UAV Program

Completed Block 30 Ground Control Station (GCS) development that provides new STORM cockpit with touch screen interfaces, adjustable rudder pedals, ergonomic seat, improved High Definition displays, and Human Machine Interface (HMI) improvements for safety of flight. Fielding begins in FY12. The MQ-9 Reaper UAV program is continuing development of the capability to instantaneously derive and disseminate JDAM-quality coordinates from the aimpoint of its electro-optical/infra-red (EO/IR) full motion video sensor. Sensor improvements include development of a precise attitude reference system coupled with an off-the-shelf two color eye-safe laser rangefinder/designator plus development of an accurately timed metadata system. Aircraft will be modified with a new guidance system incorporating differential GPS. Fielding is scheduled to begin in



FY13. Follow-on development will provide a capability for instantaneous JDAM-quality data for all pixels within the EO/IR image.

Global Hawk (RQ-4) Test program

The Global Hawk program completed Block 30 Force Development Evaluation (FDE) test in 2nd quarter FY 2012. The program completed developmental and operational testing of Airborne Signals Intelligence Payload (ASIP) 2.0.3.1. ASIP software updates to enable operational imagery intelligence missions at forward operating locations.

Seven Block 40 aircraft have been delivered as of October 2012; the remaining four will be delivered in FY13-14. . . In July 2012, Block 40 completed AN/ZPY-2 Radar System Level Performance Verification (RSLPV), meeting all Capabilities Production Document (CPD) requirements. In September 2012, the first flight testing with sensor software KD2.2 started. AN/ZPY-2 sensor performance baseline flight tests with KD2.2 configuration will be conducted in Oct-Dec of 2012.

In support of JUON 336, the Battlefield Airborne Communications Node (BACN) development and flight testing was completed in 2011 and two BACN-equipped Global Hawks were deployed to CENTCOM.

Airborne Warning and Control System (AWACS)

The Airborne Warning and Control System (AWACS) aircraft continues to modernize its mission capabilities to remain an effective airborne battle management and surveillance system for command and control of combat forces. The Block 40/45 Upgrade improves the quality and timeliness of sensor data for shooters, improves combat identification, supports a common tactical picture through multi-sensor integration, improves the AWACS contribution to Time Critical Targeting via Data Link Infrastructure, improves electronic support measures processing, and enables more effective, faster upgrades via an open system, Ethernet-based architecture. FY12 RDT&E activities for Block 40/45 included the development of maintenance and crew training systems, as well as development of a Secure Iridium Communication capability. The Next Generation Identification Friend or Foe (NGIFF) effort provides AWACS with a secure Mode 5 capability. NGIFF completed Milestone C and awarded a production contract for the Block 30/35 NGIFF in 2012. The Block 40/45 NGIFF variant continued software development and Mode S. The AWACS program continued EMD for the Diminishing Manufacturing Sources (DMS) Replacement of Avionics for Global Operations and Navigation (DRAGON) modification and completed a system preliminary design review. DRAGON's EMD effort is a cooperative development effort with the NATO AWACS program, which will provide aircraft that satisfy international airspace and air traffic control mandates. The Phase 1 Flight Performance Software was fielded, automating aircrew calculations for Take Off and Landings. The AWACS program is also continuing risk reduction efforts on multiple fronts to satisfy the high bandwidth and Beyond Line of Sight (BLOS) requirements of the battle space. These efforts will assure that AWACS remains a relevant combat partner on the joint battlefield.

B-2 EHF SATCOM and Computer, Increment 1

The B-2 EHF Increment 1 program replaces the aircraft flight management computers, upgrades and expands digital storage and installs fiber optic buses. The EHF Increment 1 effort is the foundation for all subsequent B-2 avionics upgrades to include updated stores management software for additional mission flexibility and an upgrade to the Defensive Management System to address emerging / proliferating electronic threats to ensure the B-2's continued ability to penetrate adversary defenses in AA/AD environments. The program completed a successful initial operational test and evaluation (IOT&E) in June 2012, with Director, Operational Test and Evaluation (DOT&E) expected to submit the Beyond LRIP report (BLRIP) later this year. The program earned

approval for low rate initial production in November 2011 and signed a production contract for five systems in September 2012.

B-2 Defensive Management System Modernization (DMS-M)

In Fiscal Year 2012 the Air Force continued technology development for the DMS-M program. DMS-M modernizes the original defensive management system to address emerging / proliferating electronic threats, ensuring the B-2 Spirit's continued ability to penetrate adversary defenses in AA/AD environments. DMS-M replaces the electronic support measures (ESM), the avionics graphics processor (AGP) and develops new antennas to expand the frequency coverage and capabilities of the B-2 defensive system. The prime contractor for the effort, Northrop-Grumman Aerospace Systems (NGAS), completed a source selection for the ESM in November 2010, awarding a supplier contract to BAE Nashua in October 2011. Northrop-Grumman completed source selection for the avionics graphics processor sub vendor in March 2012, awarding a supplier contract to Lockheed-Martin Owego in April 2012. The competition for the antenna subsystem is underway, with a supplier down select anticipated in early CY-2013 after competing antenna prototypes are evaluated. Technology development includes rapid acquisition initiatives (RAI) intended to accelerate the overall program and reduce costs. A successful technology development phase will culminate in entry into engineering and manufacturing development in 2014.



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General Fund

Fiscal Year 2012

Required Supplementary Information



Department of Defense
Department of the Air Force
STATEMENT OF DISAGGREGATED BUDGETARY RESOURCES
For the periods ended September 30, 2012 and 2011
(\$ in Thousands)

	Research, Development, Test & Evaluation	Procurement	Military Personnel
BUDGETARY RESOURCES:			
Unobligated balance brought forward, Oct. 1	\$ 5,988,752	26,888,580	290,384
Unobligated balance brought forward, Oct. 1, as adjusted	5,988,752	26,888,580	290,384
Recoveries of prior year unpaid obligations	626,084	801,673	825,639
Other changes in unobligated balance (+ or -)	(132,673)	(213,951)	(457,234)
Unobligated balance from prior year budget authority	6,482,163	27,476,302	658,789
Appropriations (discretionary and mandatory)	26,372,749	40,492,337	36,623,898
Spending Authority from offsetting collections (discretionary and mandatory)	3,219,867	632,379	470,798
Total Budgetary Resources	\$ 36,074,779	68,601,018	37,753,485
Obligations Incurred	31,037,871	45,674,457	37,118,973
Unobligated balance, end of year			
Apportioned	4,597,627	21,431,020	184,375
Exempt from Apportionment	0	0	0
Unapportioned	439,281	1,495,542	450,138
Total unobligated balance, end of year	5,036,908	22,926,562	634,513
Total Budgetary Resources	\$ 36,074,779	68,601,019	37,753,486
Change in Obligated Balance:			
Unpaid obligations, brought forward, October 1 (gross)	11,525,163	31,026,233	1,995,442
Uncollected customer payments from Federal sources, brought forward, October 1 (-)	(423,182)	19,500	(101,194)
Obligated balance start of year (net), before adjustments (+or-)	11,101,981	31,045,733	1,894,248
Obligated balance, start of year (net), as adjusted	11,101,981	31,045,733	1,894,248
Obligated incurred	31,037,871	45,674,457	37,118,973
Outlays (gross) (-)	(27,984,332)	(40,080,867)	(35,528,019)
Change in uncollected customer payments from Federal Sources (+ or -)	(266,513)	(63,259)	39,150
Recoveries of prior year unpaid obligations (-)	(626,084)	(801,673)	(825,639)
Obligated balance, end of year			
Unpaid Obligations, end of year (gross)	13,952,619	35,818,150	2,760,757
Uncollected customer payments from Federal sources, end of year (-)	(689,696)	(43,759)	(62,044)
Obligated balance, end of year	\$ 13,262,923	35,774,391	2,698,713
Budget Authority and Outlays, Net:			
Budget authority, gross (discretionary and mandatory)	29,592,616	41,124,716	37,094,696
Actual offering collections (discretionary and mandatory) (-)	(2,953,353)	(569,120)	(509,948)
Change in uncollected customer payments from Federal Sources (discretionary and mandatory) (+ or -)	(266,513)	(63,259)	39,150
Budget Authority, net (discretionary and mandatory)	\$ 26,372,750	40,492,337	36,623,898
Outlays, gross (discretionary and mandatory)	27,984,332	40,080,867	35,528,019
Actual offsetting collections (discretionary and mandatory) (-)	(2,953,353)	(569,120)	(509,948)
Outlays, net (discretionary and mandatory)	25,030,979	39,511,747	35,018,071
Distributed offsetting receipts (-)	0	0	0
Agency Outlays, net (discretionary and mandatory)	\$ 25,030,979	39,511,747	35,018,071

Family Housing & Military Construction	Operations, Readiness & Support	2012 Combined	2011 Combined
2,322,596	2,516,709	38,007,021	36,090,271
2,322,596	2,516,709	38,007,021	36,090,271
81,554	3,116,752	5,451,702	4,488,152
(6,355)	(626,245)	(1,436,459)	(1,513,515)
2,397,795	5,007,216	42,022,264	39,064,908
1,369,787	58,034,183	162,892,954	166,644,250
15,811	6,075,556	10,414,411	9,925,864
<u>\$ 3,783,393</u>	<u>69,116,955</u>	<u>215,329,629</u>	<u>215,635,022</u>
1,954,802	66,464,990	182,251,093	177,628,001
1,676,355	252,881	28,142,256	33,990,184
0	11,493	11,493	11,170
<u>152,236</u>	<u>2,387,591</u>	<u>4,924,787</u>	<u>4,005,667</u>
<u>1,828,591</u>	<u>2,651,965</u>	<u>33,078,536</u>	<u>38,007,021</u>
<u>3,783,393</u>	<u>69,116,955</u>	<u>215,329,629</u>	<u>215,635,022</u>
2,842,271	27,312,359	74,701,468	74,007,637
2,450	(2,530,064)	(3,032,491)	(2,968,685)
2,844,721	24,782,295	71,668,977	71,038,952
2,844,721	24,782,295	71,668,977	71,038,952
1,954,802	66,464,990	182,251,093	177,628,001
(1,913,249)	(64,983,196)	(170,489,664)	(172,446,017)
(2,450)	1,151,830	858,758	(63,806)
(81,554)	(3,116,752)	(5,451,701)	(4,488,153)
2,802,270	25,677,400	81,011,196	74,701,468
0	(1,378,234)	(2,173,733)	(3,032,491)
<u>2,802,270</u>	<u>24,299,167</u>	<u>78,837,463</u>	<u>71,668,977</u>
1,385,598	64,109,739	173,307,365	176,570,114
(13,362)	(7,227,386)	(11,273,169)	(9,862,060)
(2,450)	1,151,830	858,758	(63,806)
<u>1,369,786</u>	<u>58,034,183</u>	<u>162,892,954</u>	<u>166,644,248</u>
1,913,249	64,983,196	170,489,664	172,446,017
(13,362)	(7,227,386)	(11,273,169)	(9,862,060)
1,899,887	57,755,810	159,216,495	162,583,957
0	(177,075)	(177,075)	(154,152)
<u>1,899,887</u>	<u>57,578,735</u>	<u>159,039,420</u>	<u>162,429,805</u>



DISAGGREGATED STATEMENT OF BUDGETARY RESOURCES

The Air Force has performance measures based on missions and outputs. The Air Force is unable to accumulate costs for major programs based on those performance measures because its financial processes and systems were not designed to collect and report this type of cost information. Until the processes and systems are upgraded, the Air Force will break out programs by major appropriation groupings.

STEWARDSHIP PLANT, PROPERTY, AND EQUIPMENT (PP&E)

HERITAGE ASSETS For Fiscal Year Ended September 30, 2012					
Heritage Asset Categories	Measurement Quantity	As of 9/30/11	Additions	Deletions	As of 9/30/12
Buildings and Structures	Each	8,576	187	1,235	7,154
Archaeological Sites	Sites	2,414	235	0	2,649
Museum Collection Items (Objects, Not Including Fine Art)	Each	129,609	4,775	195	134,189
Museum Collection Items (Fine Art)	Each	11,139	1,441	0	12,580

Heritage Assets are items of historical, natural, cultural, educational, or artistic significance (e.g., aesthetic), or items with significant architectural characteristics.

1. Buildings and Structures

Buildings and Structures that are listed on, or eligible for, listing on the National Register of Historic Places (NRHP), including multi-use facilities, are Heritage Assets. These buildings and structures are maintained in accordance with the National Historic Preservation Act (NHPA), and “The Secretary of Interior’s Standards for The Treatment of Historic Properties” by each base’s civil engineering group, as part of their overall responsibility. The Air Force reported 7,154 buildings and structures on Air Force installations and sites to be Heritage Assets as of Sep 2012. Installation Cultural Resource Manager (CRMs) reported that 187 Heritage Assets were added to the AF inventory in FY12, and that 1,235 were deleted. Those deleted comprise Heritage Assets covered by the 2008 Capehart-Wherry Era Housing, and the 2010 Cold War Era Ammunition Storage Facilities, and Cold War Era Unaccompanied Housing nation-wide programmatic agreements that completed NHPA Section 106 review for these abundant facilities. The 187 increase in Heritage Asset buildings and structures reflects the ongoing annual NHPA responsibility of Air Force to survey and evaluate the National Register of Historic Property (NRHP) eligibility of buildings and structures as they approach 50 years of age. The number of Heritage Asset buildings and structures is nearly 7% of the total built inventory, which equals 105,627 buildings and structures owned or controlled by the Air Force.

Heritage Asset buildings and structures are maintained by each base civil engineering group and are considered to be in good condition. These buildings and structures are subject to NHPA, Section 106 review and consultation requirements whenever Air Force undertakings might affect their historic characteristics. Section 106 reviews ensure State Historic Preservation Officers, tribal leaders, and other party concerns are taken into account when Air Force decides to adversely affect Heritage Asset buildings and structures.

2. Archaeological Sites

Prehistoric and historic archaeological sites that have been identified, evaluated, and determined to be eligible for or are listed on the National Register of Historic Places in accordance with NHPA Section 110. The Air Force reports 2,649 archeological sites on or eligible for listing on the National Register as of Sep 2012, up 235 from the 2,414 reported for FY2011. This cohort of archaeological Heritage Assets is a subset of over 19,000 archaeological sites recorded on Air Force controlled and owned lands in the USA and its Territories.

3. Museum Collection Items, Objects

This represents the number of objects which meet the criteria for historical property as defined in Air Force Instruction 84-103 and that have been evaluated, accessioned, and catalogued in the Air Force national historical collection. The National Museum of the United States Air Force (NMUSAF) performs inherently governmental functions by fulfilling statutory requirements delegated by the Secretary of the Air Force for management of the Air Force's national historic collection. The NMUSAF is fully accredited by the American Association of Museums.

During the period 1 October 2011 – 30 September 2012 there have been 4,775 objects added to the collection. These additions are a result of private donations, transfers from Air Force or other federal entities, curatorial administrative actions, and the continued documentation of newly reported artifacts at Air Force activities worldwide. 195 objects were deaccessioned from the collection as having been determined not to meet historic property criteria, were in poor condition, or were transferred to other federal historical activities. As part of the NMUSAF's active collection management process, the accession and deaccession of objects is continuous.

The overall condition of the historic collection, which is primarily located at the NMUSAF, is very good as a result of both the professional care from trained conservators and ever improving exhibit/storage conditions. During FY2012 detailed restoration work continued on the B-17F "Memphis Belle" and the Douglas A-1H "Skyraider".

Museum Collection Items, Fine Art

The art collection contains original oils, drawing, sketches and sculptures. These paintings were in direct result of the artists visiting bases and operations throughout the Air Force. This represents 86 additions from the Air Force Art Program and 1,355 pieces of fine art from the National Museum of the United States Air Force for this FY. Included in the number above are fine art paintings inclusive of the National Museum of the United States Air Force holding.

The collection is maintained and kept in good condition. Each year during the annual inventory, Air Force Art requests the condition of the paintings as well. Maintenance continues to be a constant.



Stewardship Land

STEWARDSHIP LAND					
For Fiscal Year Ended September 30, 2012					
(Acres in Thousands)					
Facility Code	Facility Title	As of 9/30/11	Additions	Deletions	As of 9/30/12
9110	Government Owned Land	1,570	0	4	1,566
9111	State Owned Land	0	0	0	0
9120	Withdrawn Public land	7,660	0	1,380	6,280
9130	Licensed and Permitted Land	248	461	0	709
9140	Public Land	0	0	0	0
9210	Land Easement	160	0	0	160
9220	In-leased Land	93	10	0	103
9230	Foreign Land	296	0	0	296
Grand Total					9,114
Total - All Lands					
Total - Stewardship Lands					

Stewardship Land represents land rights owned by the Federal Government but not acquired for, or in connection with, items of General Property, Plant, and Equipment (PP&E). “Acquired for or in connection with” is defined as including land acquired with the intent to construct general PP&E and land acquired in combination with general PP&E. Without exception, all land provided to the Air Force from the public domain, or at no cost, shall be classified as Stewardship Land, regardless of its use.

The Air Force has 9,114,013 acres of mission-essential Stewardship Land under its administration. Land purchased by the Air Force with the intent to construct buildings or facilities is considered PP&E and is reported on the balance sheet. All stewardship land, as reported, is in acceptable condition, based on designated use.

REAL PROPERTY DEFERRED MAINTENANCE

Real Property Deferred Maintenance For Fiscal Year Ended September 30, 2012 (\$ in Millions)			
Property Type	Plant Replacement Value	Required Work (Deferred Maintenance)	Percentage
Category 1: Buildings, Structures, and Utilities (Enduring Facilities)	\$211,521	\$23,293	11%
Category 2: Buildings, Structures, and Utilities (Excess Facilities or Planned for Replacement)	\$11,235	\$196	1.7%
Category 3: Buildings, Structures, and Utilities (Heritage Assets)	\$9,362	\$1,567	16.7%

The figures in column 1 were calculated based off of an estimate of the current aggregate PRV of all facilities (buildings, structures, and utilities) in the Air Force Real Property inventory of which the DoD has ownership interest broken down by enduring, excess, and heritage. The deferred maintenance figures in column 2 consist of the current known maintenance and repair requirements needed to correct facility deficiencies in our inventory.

Ownership interest is defined as those assets that USAF holds title to, as opposed to those assets owned by foreign governments, leased facilities, out-grants, or other federal and non-federal entities.



Military Equipment Deferred Maintenance For Fiscal Year Ended September 30, 2012 (\$ in Thousands)			
Major Categories	OP30 Amounts	Adjustments	Total
1. Aircraft	\$ 1,234,879	\$961,525	\$273,354
2. Automotive Equipment	46,958	(24,600)	71,558
3. Combat Vehicles	0	0	0
4. Construction Equipment	0	0	0
5. Electronic and Communications Systems	203,916	138,727	65,189
6. Missiles	32,015	26,680	5,335
7. Ships	0	0	0
8. Ordnance Weapons and Munitions	14,833	(450)	15,283
9. General Purpose Equipment	9,872	9,242	630
10. All Other Items Not Identified to Above Categories	26,336	(6,890)	33,226
Total	\$ 1,568,809	\$1,104,234	\$464,575

The figures presented are projected deferred maintenance amounts for FY 2012 based on the original position as reported in the FY2013 President's Budget. FY2012 Overseas Contingency Operations (OCO) supplemental funding is included in the Adjustments column, along with other adjustments for requirements that did not generate or were otherwise reduced due to efficiencies realized or fact of life changes. Adjusted totals do not include Deferred Funding for Contract Logistics Support (CLS) which contains depot maintenance, but do include Deferred Funding for Depot Purchased Equipment Maintenance (DPEM).

General Fund

Fiscal Year 2012

Audit Opinion



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

November 8, 2012

MEMORANDUM FOR ASSISTANT SECRETARY OF THE AIR FORCE
(FINANACIAL MANAGEMENT AND COMPTROLLER)

SUBJECT: Independent Auditor's Report on the Air Force General Fund FY 2012 and
FY 2011 Financial Statements (Report No. DODIG-2013-009)

The Chief Financial Officers Act of 1990, as amended, requires the Department of Defense Inspector General to audit the accompanying Air Force General Fund Consolidated Balance Sheet as of September 30, 2012 and 2011, and the Consolidated Statement of Net Cost, Consolidated Statement of Changes in Net Position, and Combined Statement of Budgetary Resources and related notes for the fiscal years then ended. The financial statements are the responsibility of Air Force management. Management is also responsible for implementing effective internal control and for complying with laws and regulations. In addition, management is responsible for implementing and maintaining financial management systems that comply with the requirements of the Federal Financial Management Improvement Act of 1996 (FFMIA). Our responsibility is to express an opinion on the financial statements based on our audit.

We are unable to express an opinion on the Air Force General Fund FY 2012 and FY 2011 Basic Financial Statements because of limitations on the scope of our work. Thus, the financial statements may be unreliable. In addition to our disclaimer on the financial statements, we are including the required Report on Internal Control and Compliance with Laws and Regulations. The report is an integral part of our auditor's report 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 Air Force (Financial Management and Comptroller) represented to us that the Air Force General Fund FY 2012 and FY 2011 Basic Financial Statements would not substantially conform to accounting principles generally accepted in the United States of America (U.S. GAAP) and that Air Force financial management and feeder systems were unable to adequately support material amounts on the financial statements as of September 30, 2012. 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 auditing standards that are consistent with the management representations made to us. Accordingly, we did not perform all the auditing procedures required by generally accepted government auditing standards and Office of Management and Budget (OMB) Bulletin 07-04, "Audit Requirements for Federal Financial Statements," as amended,¹ to determine whether material amounts on the financial statements were presented fairly.

¹ OMB Memorandum M-09-33, Technical Amendments to OMB Bulletin No. 07-04, "Audit Requirements for Federal Financial Statements," September 23, 2009.

Prior audits have identified, and the Air Force has acknowledged, the long-standing material internal control weaknesses identified in the Summary of Internal Control. These material internal control weaknesses may affect the reliability of certain information contained in the annual financial statements—much of which is taken from the same data sources.² Therefore, we are unable to express, and we do not express, an opinion on the Basic Financial Statements.

Summary of Internal Control

In planning our work, we considered Air Force internal control over financial reporting and compliance with applicable laws and regulations. We did this to determine our audit procedures 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 material weaknesses continue to exist in the following areas.

- Financial Management Systems
- Operating Materials and Supplies
- General Property, Plant, and Equipment
- Government-Furnished Material and Contractor-Acquired Material
- Statement of Net Cost
- Intragovernmental Eliminations
- Other Accounting Entries
- Reconciliation of Net Cost of Operations to Budget Reporting

A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the financial statements will not be prevented, or detected and corrected on a timely basis.

In our report on the FY 2011 financial statements, we identified Fund Balance with Treasury Reconciliation as a material weakness. During FY 2012, Air Force completed improvements to address control deficiencies and financial reporting risks related to the reconciliation and reduced the material weakness to a significant deficiency.

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

- Accounts Receivable Financial Reporting
- Accounts Payable Financial Reporting
- Reimbursable Programs

² The annual financial statements include the Basic Financial Statements, Management Discussion and Analysis, Required Supplementary Stewardship Information, Required Supplementary Information, and Other Accompanying Information.



Internal control work we conducted as part of our prior audits would not necessarily disclose all deficiencies. The Attachment offers additional details on the material weaknesses and significant deficiencies reported.

The Air Force reported the above weaknesses in its FY 2012 Statement of Assurance, except for:

Material Weaknesses:

- General Property, Plant, and Equipment
- Statement of Net Cost
- Intragovernmental Eliminations
- Other Accounting Entries
- Reconciliation of Net Cost of Operations to Budget Reporting

Significant Deficiency:

- Reimbursable Programs

Compliance With Laws and Regulations

We limited our work to determining compliance with selected provisions of applicable laws and regulations related to financial reporting because management represented that instances of noncompliance identified in prior audits continue to exist. The Assistant Secretary of the Air Force (Financial Management and Comptroller) represented to us that Air Force financial management systems do not substantially comply with Federal financial management systems requirements, U.S. GAAP, and the U.S. Government Standard General Ledger at the transaction level. Therefore, we did not determine whether Air Force complied 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.

Other Information in the Annual Financial Statements

The Management Discussion and Analysis, Required Supplementary Information, and Other Accompanying Information in the annual financial statements include a wide range and detailed information and do not affect our opinion on the financial statements. The information is presented for use by management and those charged with governance and should not be used for other purposes. We did not audit and do not express an opinion on the information. We compared the information with the Air Force basic financial statements for consistency. Based on our limited work, we did not find any material inconsistencies between the information and the financial statements and applicable sections of OMB Circular No. A-136 (Revised), "Financial Reporting Requirements," August 3, 2012.

Scope and Methodology

Management is responsible for:

- preparing financial statements that conform with U.S. GAAP;
- establishing, maintaining, and assessing internal control to provide reasonable assurance that the broad control objectives of the Federal Managers' Financial Integrity Act of 1982 (FMFIA) are met;

- ensuring that Air Force financial management systems substantially comply with FFMIA requirements, and
- complying with applicable laws and regulations.

We are responsible for planning and performing the audit to obtain reasonable assurance and to provide an opinion on whether the Air Force basic financial statements are presented fairly, in all material respects, in conformity with U.S. GAAP. We are also responsible for (1) testing whether Air Force financial management systems substantially comply with the three FFMIA requirements, (2) testing compliance with selected provisions of laws and regulations that have a direct and material effect on the financial statements and laws for which OMB audit guidance requires testing, and (3) performing limited procedures with respect to certain other information appearing in the Annual Financial Statements.

We did not evaluate all internal controls relevant to operating objectives as broadly defined by FMFIA, such as those controls relevant to preparing statistical reports and ensuring efficient operations. We limited our internal control testing over financial reporting and compliance to previously identified material weaknesses and significant deficiencies that continue to exist. Because of inherent limitations in internal controls, misstatements due to error or fraud, losses, or noncompliance may nevertheless occur and not be detected.

Because of the significance of the limitations on the scope of our work, we were unable to and did not perform our audit of internal control in accordance with U.S. GAAP and OMB audit guidance. We considered the limitation on the scope of our work in forming conclusions and in testing the financial statements.

We performed our audit in accordance with U.S. generally accepted government auditing standards. We believe our audit provides a reasonable basis for our opinions and other conclusions.

Agency Comments and Our Evaluation

We provided a draft of this report to Air Force officials, who provided technical comments that we have incorporated as appropriate. Air Force officials expressed their continuing commitment to address the problems this report outlines.

This report is intended solely for the information and use of the Department's management, DoD Office of Inspector General, Office of Management and Budget, Government Accountability Office, and Congress and is not intended to be used by anyone other than these specified parties.



Lorin T. Venable, CPA
Acting Assistant Inspector General
DoD Payments and Accounting Operations

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 to include providing reasonable assurance that Air Force personnel accumulated, recorded, and reported accounting data properly; met the requirements of applicable laws and regulations; and safeguarded assets against misappropriation and abuse. Our purpose was not to, and we do not, express an opinion on internal control over financial reporting. The following material weaknesses and significant deficiencies exist that could adversely affect Air Force financial reporting.

Previously Identified Material Weaknesses

Management acknowledged that it is unable to comply with applicable reporting requirements and has identified the following material weaknesses that continued to exist in the following areas.

Financial Management Systems

Statement of Federal Financial Accounting Concepts No. 1, “Objectives of Federal Financial Reporting,” requires that financial management system controls be adequate to ensure that transactions are executed in accordance with budgetary and financial laws and other requirements, are consistent with the purposes authorized, and are recorded in accordance with Federal accounting standards. This statement also requires that financial management system controls ensure the proper safeguarding of assets to deter fraud, waste, and abuse and provide adequate support for performance measurement information. The Assistant Secretary of the Air Force (Financial Management and Comptroller) acknowledged that many Air Force financial management systems did not substantially comply with Federal financial management system requirements. The design of the Air Force financial management and feeder systems did not allow them to collect and record financial information based on a full-accrual accounting basis. Until these systems are able to collect and report financial information in compliance with U.S. GAAP, the Air Force proprietary financial reporting will be largely based on budgetary transactions and nonfinancial feeder systems.

Operating Materials and Supplies

The Air Force is required by Statement of Federal Financial Accounting Standards No. 3, “Accounting for Inventory and Related Property,” to use the historical cost to value its Operating Materials and Supplies inventory. This statement also requires that an expense be recorded for Operating Materials and Supplies when the user consumes such items. The Air Force has acknowledged that significant amounts of Operating Materials and Supplies were valued using standard prices, and it did not always use the consumption method to recognize the related expense. Accordingly, management was not certain that the Operating Materials and Supplies balances reported in its Basic Financial Statements were accurate.

General Property, Plant, and Equipment

Statement of Federal Financial Accounting Standards No. 6, "Accounting for Property, Plant, and Equipment," requires the Air Force to record General Property, Plant, and Equipment using acquisition cost, capitalized improvement costs, and depreciation expense. However, the Air Force has acknowledged that despite its implementation of a new system to improve its controls over recording real property, construction-in-progress, and related expenses, additional corrective actions, including improving supporting documentation, were required before the validation of real property financial reporting. This validation was required to ensure real property reporting did not materially misstate General Property, Plant, and Equipment.

Government-Furnished Material and Contractor-Acquired Material

Statement of Federal Financial Accounting Standards No. 6, "Accounting for Property, Plant, and Equipment," requires that the Government report on its Balance Sheet the property and equipment in the possession of a contractor for use in accomplishing a contract. Government property should be accounted for based on the nature of the item, regardless of who has possession. The Air Force has acknowledged that its balance did not include the cost of all Government-furnished material in the hands of contractors where such value exceeds the capitalization threshold. As a result, the Air Force did not reliably report the value of its property and material in the possession of contractors.

Environmental Liabilities

The Air Force was not currently able to support its environmental cleanup cost estimates as recorded in the Air Force Real Property Agency management information system. This system provides unsupported cost information for reporting in the annual financial statements.

Statement of Net Cost

Statement of Federal Financial Accounting Concepts No. 2, "Entity and Display," requires that that Statement of Net Cost present gross and net cost information for major organization and programs and data related to their outputs and outcomes. The Air Force acknowledged that it accumulates the amounts reported in its Statement of Net Cost by major appropriation groups funded by Congress and not by major organization and programs, as required. In addition, the Air Force did not accumulate cost information in accordance with U.S. GAAP. It presented the amounts for the General Fund based on budgetary obligations, disbursements, and collections, with adjustments made for only major items of known accruals and imputed expenses. Thus, the Statement of Net Cost may not report all actual costs or may report costs not actually incurred.

Intragovernmental Eliminations

Air Force accountants could not always identify intragovernmental trading partners when recording transactions. Thus, the Air Force could not properly eliminate all transactions among its internal organizational elements. In addition, the Air Force could not reconcile intragovernmental accounts receivable, accounts payable, and revenues for transactions between its DoD and other Federal trading partners. This may prevent the Air Force from properly eliminating all of its intragovernmental transactions.



Other Accounting Entries

The Air Force acknowledged that it continued to enter material amounts of accounting adjustments without adequate detailed transaction support. Additionally, there were material transactions that the Air Force has not properly recorded in the accounting records underlying the Basic Financial Statements or the disclosed notes to the Basic Financial Statements. The lack of adequate supporting documentation for material adjustments prevents an audit of the related financial statement amounts.

Reconciliation of Net Cost of Operations to Budget

Statement of Federal Financial Accounting Standards No. 7, “Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting,” states that the Reconciliation of Net Costs of Operations to Budget (in the footnotes to the Basic Financial Statements) should reconcile resources obligated during the accounting period to the net cost of operations for that period. However, as stated in preceding paragraphs, the amounts presented in the Consolidated Statement of Net Costs and assets and liabilities reported in the Balance Sheet may be inaccurate. The Air Force did not reconcile budgetary amounts to actual proprietary expenses and assets and liabilities.

Current and Previously Identified Significant Deficiencies

As part of our financial-related audits, we noted the following significant deficiencies. Fund Balance with Treasury, previously identified as a material weakness, is now identified as a significant deficiency, and the remaining significant deficiencies continued to exist.

Fund Balance With Treasury

Previously, we reported a material weakness related to the Air Force Fund Balance with Treasury reconciliation process. Air Force did not have assurance that it could reconcile its reported balance of Fund Balance with Treasury (FBWT) to the balance the Treasury maintains because it did not receive transaction-level data from other DoD Components processing collections and disbursements on its behalf. Air Force now receives the necessary data and identifies, monitors, and resolves reconciling amounts between these balances.

Specifically, DFAS accountants obtain the FBWT transactions monthly from the Air Force and the other originators of the transactions and store those transactions in a specialized reconciliation software package. The monthly and cumulative totals of those detail transactions are reconciled to the summary totals reported to the Treasury by all DoD components disbursing and collecting Air Force appropriated funds. To complete the reconciliation process, the reconciliation software compares each of those detail transactions to the FBWT transactions reported in the Air Force general ledger. From this process, DFAS accountants identify transactions that resulted in a difference between the balances maintained by Treasury and the balances in the Air Force general ledger and report those transactions to the Air Force for resolution.

However, management has acknowledged and our audit procedures have confirmed that further improvements are required to enable the reconciliation process to include certain appropriation accounts that Air Force does not reconcile to Treasury and to reduce the amount of unresolved reconciling items that have been outstanding in excess of Treasury guidelines of 60 days.

These matters are significant deficiencies that require the current attention of management to ensure its corrective action plans result in improvements in these control weaknesses.

We made our review of the current-year FBWT reconciliation for the express purpose of determining whether the previously identified material weakness was reduced to a significant deficiency and not for the purpose of determining whether FBWT was presented fairly, in accordance with U.S. GAAP. The scope of our current-year tests of internal controls focused solely on the Air Force assertion that it had reduced the previously reported material weakness to a significant deficiency and did not include tests of any other internal controls for Air Force's FBWT activity. The Air Force implementation of an internal control to reconcile the Air Force balances to the Treasury balances by itself does not ensure that the Air Force Fund Balance with Treasury reported on its balance sheet is ready for audit or presented fairly, in accordance with U.S. generally accepted accounting principles.

Accounts Receivable Financial Reporting

The Air Force could not ensure the accuracy of its Accounts Receivable financial statement line item because of weaknesses in the intragovernmental trading partner eliminations supporting documentation. These deficiencies resulted in the inability to properly reconcile and support the validity of Accounts Receivable.

Accounts Payable Financial Reporting

The Air Force could not ensure the accuracy of the amount of Accounts Payable reported in the Basic Financial Statements because of the financial system internal control weaknesses. Because of these weaknesses, the Air Force could not support entries to Accounts Payable or reconcile the reported balance to transaction detail.

Reimbursable Programs

Statement of Federal Financial Accounting Concepts No. 1, "Objectives of Federal Financial Reporting," requires the Air Force to track the cost of performing work reimbursed by other Government entities or by non-Federal customers. Statement of Federal Financial Accounting Concepts No. 1 defines costs as a measure of resources (personnel, material, and equipment) used to accomplish the work. The Air Force has acknowledged that its reimbursable programs may not recover all billable costs incurred in the fulfillment of reimbursable orders. Specifically, the Air Force was not always able to identify logistical, contractual, or labor costs incurred in support of reimbursable orders; therefore, such costs were not properly billed to the customer.

These financial management deficiencies may cause inaccurate management information. As a result, Air Force management decisions based in whole or in part on this information may be adversely affected. Air Force reported that financial information 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 determining 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 Air Force 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

FFMIA requires Air Force to establish and maintain financial management systems that comply substantially with the Federal financial management systems requirements, applicable Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level. For FY 2012, Air Force did not fully comply with FFMIA. The Air Force acknowledged that many of its critical financial management and feeder systems did not substantially comply with the Federal financial management systems requirements, Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level as of September 30, 2012.

Antideficiency Act

Section 1341, title 31, United States Code (31 U.S.C. § 1341) limits the Air Force and its agents to making or authorizing expenditures or obligations that do not exceed the available appropriations or funds. Additionally, the Air Force or its agents may not contract or obligate for the payment of money before an appropriation is made available for that contract or obligation unless otherwise authorized by law. According to 31 U.S.C. § 1351, if an officer or employee of an executive agency violates the Antideficiency Act (ADA), the head of the agency must report immediately to the President and Congress all relevant facts and a statement of actions taken. During FY 2012, the Air Force reported two ADA cases.

DoD Regulation 7000.14-R, “Financial Management Regulation,” Volume 14, Chapter 7, “Antideficiency Act Report,” November 2010, limits the time from identification to reporting of ADA violations to 15 months. Our review of the Air Force ADA violations showed that the Air Force General Fund did not process the two ADA violations cases within 15 months.

Audit Disclosures

The Assistant Secretary of the Air Force (Financial Management and Comptroller) acknowledged to us on June 28, 2012, that the Air Force financial management and feeder systems could not provide adequate evidence supporting various material amounts on the financial statements and that previously identified material weaknesses continued 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, and the Pay and Allowance System for Civilian Employees.

Recommendations

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

Working Capital Fund

Principal Statements

Fiscal Year 2012

The FY 2012 Department of the Air Force Working Capital Fund Principal Statements and related notes are presented in the format prescribed by the Department of Defense Financial Management Regulation 7000.14-R, Volume 6B. The statements and related notes summarize financial information for individual activity groups and activities within the Working Capital Fund for the fiscal year ending September 30, 2012, and are presented on a comparative basis with information previously reported for the fiscal year ending September 30, 2011.

The following statements comprise the Department of the Air Force Working Capital Fund Principal Statements:

Consolidated Balance Sheet

The Consolidated Balance Sheet presents as of September 30, 2012 and 2011 those resources owned or managed by the Air Force which are available to provide future economic benefits (assets); amounts owed by the Air Force that will require payments from those resources or future resources (liabilities); and residual amounts retained by the Air Force, comprising the difference (net position)

Consolidated Statement of Net Cost

The Consolidated Statement of Net Cost presents the net cost of the Air Force's operations for the years ended September 30, 2012 and 2011. The Air Force's net cost of operations includes the gross costs incurred by the Air Force less any exchange revenue earned from Air Force activities.

Consolidated Statement of Changes in Net Position

The Consolidated Statement of Changes in Net Position presents the change in the Air Force's net position resulting from the net cost of Air Force's operations, budgetary financing sources other than exchange revenues, and other financing sources for the years ended September 30, 2012 and 2011.

Combined Statement of Budgetary Resources

The Combined Statement of Budgetary Resources presents the budgetary resources available to the Air Force during FY 2012 and 2011, the status of these resources at September 30, 2012 and 2011, and the outlay of budgetary resources for the years ended September 30, 2012 and 2011.

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, the Government Management Reform Act of 1994, and the Office of Management and Budget's Circular A-136, "Financial Reporting Requirements."



**Department of Defense
Air Force Working Capital Fund
CONSOLIDATED BALANCE SHEET
As of September 30, 2012 and 2011
(\$ in Thousands)**

	<u>2012 Consolidated</u>	<u>2011 Consolidated</u>
ASSETS (Note 2)		
Intragovernmental:		
Fund Balance with Treasury (Note 3)	\$ 556,537	\$ 670,929
Accounts Receivable (Note 5)	778,172	933,040
Other Assets (Note 6)	167,739	111,126
Total Intragovernmental Assets	<u>\$ 1,502,448</u>	<u>\$ 1,715,095</u>
Accounts Receivable, Net (Note 5)	4,792	3,710
Inventory and Related Property, Net (Note 9)	26,099,598	26,813,221
General Property, Plant and Equipment, Net (Note 10)	1,509,820	1,458,929
Other Assets (Note 6)	239,991	336,601
TOTAL ASSETS	<u><u>\$ 29,356,649</u></u>	<u><u>\$ 30,327,556</u></u>
STEWARDSHIP PROPERTY, PLANT & EQUIPMENT (Note 10)		
LIABILITIES (Note 11)		
Intragovernmental:		
Accounts Payable (Note 12)	\$ 180,355	\$ 226,029
Other Liabilities (Note 15 & 16)	55,304	55,730
Total Intragovernmental Liabilities	<u>\$ 235,659</u>	<u>\$ 281,759</u>
Accounts Payable (Note 12)	\$ 577,905	\$ 694,713
Military Retirement and Other Federal Employment Benefits (Note 17)	217,518	214,927
Other Liabilities (Note 15 and Note 16)	251,517	239,258
TOTAL LIABILITIES	<u>\$ 1,282,599</u>	<u>\$ 1,430,657</u>
COMMITMENTS AND CONTINGENCIES (NOTE 16)		
NET POSITION		
Unexpended Appropriations - Other Funds	20,380	36,975
Cumulative Results of Operations - Other Funds	28,053,670	28,859,924
TOTAL NET POSITION	<u>\$ 28,074,050</u>	<u>\$ 28,896,899</u>
TOTAL LIABILITIES AND NET POSITION	<u><u>\$ 29,356,649</u></u>	<u><u>\$ 30,327,556</u></u>

Department of Defense
Air Force Working Capital Fund
CONSOLIDATED STATEMENT OF NET COST
For the periods ended September 30, 2012 and 2011
(\$ in Thousands)

	<u>2012 Consolidated</u>	<u>2011 Consolidated</u>
Program Costs		
Gross Costs	\$ 12,456,829	\$ 13,099,620
Operations, Readiness & Support	12,456,829	13,099,620
	<hr/>	<hr/>
(Less: Earned Revenue)	(11,403,352)	(11,852,895)
Net Cost before Losses/(Gains) from Actuarial Assumption for Military Retirement Benefits	<hr/> 1,053,477	<hr/> 1,246,725
Net Program Costs Including Assumption Changes	1,053,477	1,246,725
Net Cost of Operations	<hr/> <u>\$ 1,053,477</u>	<hr/> <u>\$ 1,246,725</u>



**Department of Defense
Air Force Working Capital Fund
CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION
For the periods ended September 30, 2012 and 2011
(\$ in Thousands)**

	2012 Earmarked Funds	2012 All Other Funds
CUMULATIVE RESULTS OF OPERATIONS		
Beginning Balances	\$ 0	\$ 28,859,924
Beginning balances, as adjusted	0	28,859,924
Budgetary Financing Sources:		
Appropriations used	0	81,967
Transfers-in/out without reimbursement	0	(514,850)
Other Financing Sources:		
Transfers-in/out without reimbursement (+/-)	0	34,967
Imputed financing from costs absorbed by others	0	180,027
Other (+/-)	0	465,112
Total Financing Sources	0	247,223
Net Cost of Operations (+/-)	0	1,053,477
Net Change	0	(806,254)
Cumulative Results of Operations	0	28,053,670
UNEXPENDED APPROPRIATIONS		
Beginning Balances	\$ 0	\$ 36,975
Beginning balances, as adjusted	0	36,975
Budgetary Financing Sources:		
Appropriations received	0	65,372
Appropriations used	0	(81,967)
Total Budgetary Financing Sources	0	(16,595)
Unexpended Appropriations	0	20,380
Net Position	0	28,074,050

Department of Defense
Air Force Working Capital Fund
CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION
For the periods ended September 30, 2012 and 2011
(\$ in Thousands)

	2012 Eliminations	2012 Consolidated
CUMULATIVE RESULTS OF OPERATIONS		
Beginning Balances	\$ 0	\$ 28,859,924
Beginning balances, as adjusted	0	28,859,924
Budgetary Financing Sources:		
Appropriations used	0	81,967
Transfers-in/out without reimbursement	0	(514,850)
Other Financing Sources:		
Transfers-in/out without reimbursement (+/-)	0	34,967
Imputed financing from costs absorbed by others	0	180,027
Other (+/-)	0	465,112
Total Financing Sources	0	247,223
Net Cost of Operations (+/-)	0	1,053,477
Net Change	0	(806,254)
Cumulative Results of Operations	0	28,053,670
UNEXPENDED APPROPRIATIONS		
Beginning Balances	\$ 0	\$ 36,975
Beginning balances, as adjusted	0	36,975
Budgetary Financing Sources:		
Appropriations received	0	65,372
Appropriations used	0	(81,967)
Total Budgetary Financing Sources	0	(16,595)
Unexpended Appropriations	0	20,380
Net Position	0	28,074,050



**Department of Defense
Air Force Working Capital Fund
CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION
For the periods ended September 30, 2012 and 2011
(\$ in Thousands)**

	2011 Earmarked Funds	2011 All Other Funds
CUMULATIVE RESULTS OF OPERATIONS		
Beginning Balances	\$ 0	\$ 29,786,340
Beginning balances, as adjusted	0	29,786,340
Budgetary Financing Sources:		
Appropriations used	0	54,059
Transfers-in/out without reimbursement	0	0
Other Financing Sources:		
Transfers-in/out without reimbursement (+/-)	0	(10,561)
Imputed financing from costs absorbed by others	0	191,388
Other (+/-)	0	85,423
Total Financing Sources	0	320,309
Net Cost of Operations (+/-)	0	1,246,725
Net Change	0	(926,416)
Cumulative Results of Operations	0	28,859,924
UNEXPENDED APPROPRIATIONS		
Beginning Balances	\$ 0	\$ 24,173
Beginning balances, as adjusted	0	24,173
Budgetary Financing Sources:		
Appropriations received	0	66,861
Appropriations used	0	(54,059)
Total Budgetary Financing Sources	0	12,802
Unexpended Appropriations	0	36,975
Net Position	0	28,896,899

Department of Defense
Air Force Working Capital Fund
CONSOLIDATED STATEMENT OF CHANGES IN NET POSITION
For the periods ended September 30, 2012 and 2011
(\$ in Thousands)

	2011 Eliminations	2011 Consolidated
CUMULATIVE RESULTS OF OPERATIONS		
Beginning Balances	0	29,786,340
Beginning balances, as adjusted	0	29,786,340
Budgetary Financing Sources:		
Appropriations used	0	54,059
Transfers-in/out without reimbursement	0	0
Other Financing Sources:		
Transfers-in/out without reimbursement (+/-)	0	(10,561)
Imputed financing from costs absorbed by others	0	191,388
Other (+/-)	0	85,423
Total Financing Sources	0	320,309
Net Cost of Operations (+/-)	0	1,246,725
Net Change	0	(926,416)
Cumulative Results of Operations	0	28,859,924
UNEXPENDED APPROPRIATIONS		
Beginning Balances	0	24,173
Beginning balances, as adjusted	0	24,173
Budgetary Financing Sources:		
Appropriations received	0	66,861
Appropriations used	0	(54,059)
Total Budgetary Financing Sources	0	12,802
Unexpended Appropriations	0	36,975
Net Position	0	28,896,899



**Department of Defense
Air Force Working Capital Fund
COMBINED STATEMENT OF BUDGETARY RESOURCES
For the periods ended September 30, 2012 and 2011
(\$ in Thousands)**

	<u>2012 Combined</u>	<u>2011 Combined</u>
Budgetary Resources:		
Unobligated balance brought forward, Oct 1	555,328	532,408
Unobligated balance brought forward, Oct 1, as adjusted, as Adjusted	\$ 555,328	\$ 532,408
Recoveries of prior year unpaid obligations	38,915	103,939
Other changes in unobligated balance (+ or -)	(553,765)	(19,801)
Unobligated balance from prior year budget authority, net	40,478	616,546
Appropriations (discretionary and mandatory)	0	66,861
Contract Authority (discretionary and mandatory)	7,559,690	7,989,074
Spending Authority from offsetting collections	4,842,419	4,258,403
Total Budgetary Resources	<u>12,442,587</u>	<u>12,930,884</u>
Status of Budgetary Resources:		
Obligations Incurred	12,336,028	12,375,556
Unobligated balance, end of year		
Apportioned	106,559	555,328
Total unobligated balance, end of year	<u>106,559</u>	<u>555,328</u>
Total Budgetary Resources	<u>12,442,587</u>	<u>12,930,884</u>
Change in Obligated Balance:		
Unpaid obligations, brought forward, October 1 (gross)	7,364,314	7,824,540
Uncollected customer payments from Federal sources, brought forward, October 1 (-)	(3,619,244)	(3,893,169)
Obligated balance start of year (net), before adjustments (+ or -)	3,745,070	3,931,371
Obligated balance, start of year (net), as adjusted	3,745,070	3,931,371
Obligations incurred	12,336,028	12,375,556
Outlays (gross) (-)	(12,601,195)	(12,731,843)
Change in uncollected customer payments from Federal Sources (+ or-)	505,811	273,922
Recoveries of prior year unpaid obligations (-)	(38,915)	(103,939)
Obligated balance, end of year		
Unpaid Obligations, end of year (gross)	7,060,232	7,364,314
Uncollected customer payments from Federal sources, end of	(3,113,433)	(3,619,247)
Obligated balance, end of year	<u>3,946,799</u>	<u>3,745,067</u>

**Department of Defense
Air Force Working Capital Fund
COMBINED STATEMENT OF BUDGETARY RESOURCES
For the periods ended September 30, 2012 and 2011
(\$ in Thousands)**

	<u>2012 Combined</u>	<u>2011 Combined</u>
Budget Authority and Outlays, Net:		
Budget authority, gross (discretionary and mandatory)	12,402,109	12,314,338
Actual offsetting collections (discretionary and mandatory) (-)	(12,936,282)	(13,024,352)
Change in uncollected customer payments from Federal	505,811	273,922
Sources (discretionary and mandatory) (+ or -)		
Budget Authority, net (discretionary and mandatory)	<u>(28,362)</u>	<u>(436,092)</u>
Outlays, gross (discretionary and mandatory)	12,601,195	12,731,843
Actual offsetting collections (discretionary and mandatory) (-)	(12,936,282)	(13,024,352)
Outlays, net (discretionary and mandatory)	<u>(335,087)</u>	<u>(292,509)</u>
Agency Outlays, net (discretionary and mandatory)	<u>(335,087)</u>	<u>(292,509)</u>



Working Capital Fund

Fiscal Year 2012

Notes to the Principal Statements

Notes to the financial statements communicate information essential for fair presentation of the financial statements that is not displayed on the face of the 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 Air Force Working Capital Fund (AFWCF), as required by the Chief Financial Officers Act of 1990, expanded by the Government Management Reform Act of 1994, and other appropriate legislation. The financial statements have been prepared from the books and records of the AFWCF in accordance with, and to the extent possible, U.S. generally accepted accounting principles (USGAAP) promulgated by the Federal Accounting Standards Advisory Board; the Office of Management and Budget (OMB) Circular No. A-136, Financial Reporting Requirements; and the Department of Defense (DoD), Financial Management Regulation (FMR). The accompanying financial statements account for all resources for which the AFWCF is responsible unless otherwise noted.

The AFWCF is unable to fully implement all elements of USGAAP and the OMB Circular No. A-136, due to limitations of financial and nonfinancial management processes and systems that support the financial statements. The AFWCF derives 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 USGAAP. The AFWCF continues to implement process and system improvements addressing these limitations.

The AFWCF currently has eight auditor identified financial statement material weaknesses: (1) financial and nonfinancial feeder systems do not contain an adequate audit trail for the proprietary and budgetary accounts, (2) AFWCF may have material amounts of account adjustments that are not adequately supported, (3) AFWCF cannot accurately identify all intragovernmental transactions by customer, which is required for eliminations when preparing consolidated financial statements, (4) the value of the AFWCF government furnished and contractor acquired materiel and equipment may not be accurately reported, (5) AFWCF General Property, Plant, and Equipment (PP&E) may not be accurately valued, (6) Operating Materiel and Supplies (OM&S) are not reflected at historical cost, (7) cost of goods sold and work in progress are not recorded in accordance with the Statement of Federal Financial Accounting Standards (SFFAS) No. 3, "Accounting for Inventory and Related Property", and (8) supply management systems do not provide sufficient audit trails to confirm and value the in transit inventory reported as part of inventory held for sale on the Consolidated Balance Sheet.

1.B. Mission of the Reporting Entity

The United States Air Force was created on September 18, 1947, by the National Security Act of 1947. The National Security Act Amendments of 1949 established the DoD and made the Air Force a department within DoD. The overall mission of the United States Air Force is to fly, fight and win...in air, space and cyberspace. Our priorities are: (1) continue to strengthen the nuclear enterprise, (2) partner with Joint and Coalition team to win today's fight, (3) develop and care for Airmen and their families, (4) modernize our air and space inventories, organizations, and training, and (5) recapture acquisition excellence.

The stock and industrial revolving fund accounts were created by the National Security Act of 1947, as amended in 1949 and codified in United States Code 10 Section 2208. The revolving funds were established as a means to more effectively control the cost of work performed by DoD. The DoD began operating under the revolving fund concept on July 1, 1951.

Effective FY 2009, AFWCF operations consist of two major activity groups: Consolidated Sustainment Activity Group (CSAG) and the Supply Management Activity Group - Retail (SMAG-R). All AFWCF CSAG and SMAG-R activities establish rates based on full cost recovery. If an operating loss or gain is incurred, the activity will make the appropriate adjustment in following years' prices to recoup the loss or return the gain to their customers.

The mission of CSAG is supply management of reparable and consumable items, and maintenance activities. The CSAG combines the activities of the previous Material Support Division (MSD) of the Supply Management Activity Group and the Depot Maintenance Activity Group (DMAG). Under CSAG, business operations formerly known as DMAG are now related to the Maintenance Division. Likewise, business operations formerly known as MSD are now referred to as the Supply Division.



Supply Division activities of CSAG are authorized to procure and manage reparable and consumable items for which the Air Force is the Inventory Control Point. The Supply Division manages more than 106 thousand items that are generally related to weapon systems and ground support, and include both depot level reparables and non-depot level reparables.

Maintenance Division activities of CSAG are authorized to perform: (a) overhaul, conversion, reclamation, progressive maintenance, modernization, software development, storage, modification, and repair of aircraft, missiles, engines, accessories, components, and equipment; (b) the manufacture of parts and assemblies required to support the foregoing; and (c) the furnishing of other authorized services or products for the Air Force and other agencies of the DoD. As directed by the Air Force Materiel Command or higher authority, the Maintenance Division may furnish the above mentioned products or services to agencies of other departments or instrumentalities of the U.S. Government, and to private parties and other agencies, as authorized by law.

The SMAG-R consists of three business divisions: General Support Division (GSD), Medical-Dental Division, and Air Force Academy Division. GSD procures and manages nearly 1.1 million consumable supply items related to maintenance, flying hour program, and installation functions. The majority are used in support of field and depot maintenance of aircraft, ground and airborne communication systems, and other support systems and equipment. The Medical-Dental Division procures and manages nearly 9 thousand different medical supply items and equipment necessary to maintain an effective Air Force Health Care system for the active military, retirees and their dependents. The Air Force Academy Division procures and manages a retail inventory of uniforms, academic supplies and other recurring issue requirements for the Cadet Wing of the United States Air Force Academy. Inventory procurement is only for mandatory items as determined by the Cadet Uniform Board.

1.C. Appropriations and Funds

The AFWCF receives appropriations and funds as general and working capital (revolving) funds. The AFWCF 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 WCF as an infusion of cash when revenues are inadequate to cover costs within the corpus.

1.D. Basis of Accounting

The AFWCF financial management systems are unable to meet all full accrual accounting requirements. Many of the AFWCF financial and nonfinancial feeder systems and processes were designed and implemented prior to the issuance of USGAAP. These systems were not designed to collect and record financial information on the full accrual accounting basis as required by USGAAP. Most of AFWCF's financial and nonfinancial legacy systems were designed to record information on a budgetary basis.

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

The DoD is determining the actions required to bring its financial and nonfinancial feeder systems and processes into compliance with USGAAP. One such action is the current revision of accounting systems to record transactions based on the U.S. Standard General Ledger (USSGL). Until all AFWCF's financial and nonfinancial feeder systems and processes are updated to collect and report financial information as required by USGAAP, AFWCF's financial data will be derived from budgetary transactions, data from nonfinancial feeder systems, and accruals.

1.E. Revenues and Other Financing Sources

The CSAG Maintenance Division recognizes revenue according to the percentage of completion method. The CSAG Supply Division and SMAG-R recognize revenue based on flying hours executed and 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. Current financial and nonfinancial feeder systems were not designed to collect and record financial information on the full accrual accounting basis. Estimates are made for major items such as payroll expenses, accounts payable and unbilled revenue. In the case of OM&S, the consumption method is used. Under the consumption method, OM&S would be expensed when consumed. Due to system limitations, in some instances expenditures for capital and other long-term assets may be recognized as operating expenses. The AFWCF continues to implement process and system improvements to address these limitations.

1.G. Accounting for Intragovernmental Activities

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

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

The DoD's proportionate share of public debt and related expenses of the Federal Government is not included. The Federal Government does not apportion debt and its related costs to federal agencies. The DoD's financial statements do not report any public debt, interest or source of public financing, whether from issuance of debt or tax revenues.

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

1.H. Transactions with Foreign Governments and International Organizations

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

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

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

In addition, DFAS 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 these transactions to the applicable



Fund Balance with Treasury (FBWT) account. On a monthly basis, AFWCF's FBWT is adjusted to agree with the U.S. Treasury accounts.

1.J. Cash and Other Monetary Assets

Not applicable.

1.K. Accounts Receivable

Accounts receivable from other federal entities or the public include: accounts receivable, claims receivable, and refunds receivable. Allowances for uncollectible accounts due from the public are based upon analysis of collection experience by fund type. The DoD does not recognize an allowance for estimated uncollectible amounts from other federal agencies. Claims against other federal agencies are to be resolved between the agencies in accordance with dispute resolution procedures defined in the Intragovernmental Business Rules published in the Treasury Financial Manual.

1.L. Direct Loans and Loan Guarantees

Not applicable.

1.M. Inventories and Related Property

The AFWCF values approximately 99% of its resale inventory using the moving average cost method and reports the remaining 1% of resale inventories 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 the USSGL, as required by the Federal Financial Management Improvement Act of 1996 (PL 104-208). The AFWCF is continuing to transition the balance of the inventories to the moving average cost method through the use of new inventory systems. Most transitioned balances, however, were not baselined to auditable historical cost and remain noncompliant with SFFAS No. 3.

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

Related property includes OM&S which is valued at purchase price. The AFWCF uses the consumption method of accounting for OM&S.

The AFWCF recognizes excess, obsolete, and unserviceable inventory and OM&S at a net realizable value of \$0 pending development of an effective means of valuing such materiel.

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

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

Not applicable.

1.O. General Property, Plant and Equipment

The DoD's General Property, Plant, and Equipment (PP&E) capitalization threshold is \$100 thousand except for real property, which is \$20 thousand. The AFWCF has not fully implemented the threshold for real property; therefore, DoD is primarily using the capitalization threshold of \$100 thousand for General PP&E, and most real property.

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

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

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

1.P. Advances and Prepayments

When advances are permitted by law, legislative action, or presidential authorization, DoD's policy is to record advances or prepayments in accordance with USGAAP. As such, payments made in advance of the receipt of goods and services should be reported as an asset on the Balance Sheet. The DoD's policy is to expense and/or properly classify assets when the related goods and services are received. The AFWCF has implemented this policy.

1.Q. Leases

Not applicable.

1.R. Other Assets

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

The AFWCF 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, AFWCF may provide financing payments. Contract financing payments are defined in the Federal Acquisition Regulations, Part 32, as authorized disbursements to a contractor prior to acceptance of supplies or services by the Government. Contract financing payments clauses are incorporated in the contract terms and conditions and may include advance payments, performance-based payments, commercial advances and interim payments, progress payments based on cost, and interim payments under certain cost-reimbursement contracts. It is DoD policy to record certain contract financing payments as other assets. The AFWCF has not fully implemented this policy primarily due to system limitations.

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

1.S. Contingencies and Other Liabilities

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

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

1.T. Accrued Leave

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

1.U. Net Position

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

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

Cumulative results of operations represent the net difference between expenses and losses, and financing sources (including appropriations, revenue, and gains), since inception. The cumulative results of operations also include donations and transfers in and out of assets that were not reimbursed.

1.V. Treaties for Use of Foreign Bases

Not applicable.

1.W. Undistributed Disbursements and Collections

Undistributed disbursements and collections represent the difference between disbursements and collections matched at the transaction level to specific obligations, payables, or receivables in the source systems and those reported by the U.S. Treasury. Supported disbursements and collections may be evidenced by the availability of corroborating documentation that would generally support the summary level adjustments made to accounts payable and receivable. Unsupported disbursements and collections do not have supporting documentation for the transactions and most likely would not meet audit scrutiny. However, both supported and unsupported adjustments may have been made to the [Component/Department] Accounts Payable and Receivable trial balances prior to validating underlying transactions required to establish the Accounts Payable/Receivable were previously made. As a result, misstatements of reported Accounts Payable and Receivables are likely present in the [Component/Department] financial statements.

Due to noted material weaknesses in current accounting and financial feeder systems, the DoD is generally unable to determine whether undistributed disbursements and collections should be applied to federal or nonfederal accounts payables/receivable at the time accounting reports are prepared. Accordingly, the DoD policy is to allocate supported undistributed disbursements and collections between federal and nonfederal categories based on the percentage of distributed federal and nonfederal accounts payable and accounts receivable. Both supported and unsupported undistributed disbursements and collections are then applied to reduce accounts payable and receivable accordingly.

1.X. Fiduciary Activities

Not Applicable.

1.Y. Military Retirement and Other Federal Employment Benefits

Not Applicable.

1.Z. Significant Events

Not Applicable.

Note 2. Nonentity Assets

As of September 30 (Amounts in thousands)	2012		2011	
1. Intragovernmental Assets				
A. Fund Balance with Treasury	\$	0	\$	0
B. Accounts Receivable		0		0
C. Other Assets		0		0
D. Total Intragovernmental Assets	\$	0	\$	0
2. Nonfederal Assets				
A. Cash and Other Monetary Assets	\$	0	\$	0
B. Accounts Receivable		155		296
C. Other Assets		0		0
D. Total Nonfederal Assets	\$	155	\$	296
3. Total Nonentity Assets	\$	155	\$	296
4. Total Entity Assets	\$	29,356,494	\$	30,327,260
5. Total Assets	\$	29,356,649	\$	30,327,556

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

Nonentity assets are assets for which the AFWCF maintains stewardship accountability and reporting responsibility, but are not available for the AFWCF's normal operations.

These nonentity assets are interest, penalties and administrative fees that will be forwarded to the General Fund of the U.S. Treasury upon collection.



Note 3. Fund Balance with Treasury

As of September 30 (Amounts in thousands)	2012	2011
1. Fund Balances		
A. Appropriated Funds	\$ 0	\$ 0
B. Revolving Funds	556,537	670,929
C. Trust Funds	0	0
D. Special Funds	0	0
E. Other Fund Types	0	0
F. Total Fund Balances	<u>\$ 556,537</u>	<u>\$ 670,929</u>
2. Fund Balances Per Treasury Versus Agency		
A. Fund Balance per Treasury	\$ 811,253	\$ 1,026,251
B. Fund Balance per AFWCF	556,537	670,929
3. Reconciling Amount	<u>\$ 254,716</u>	<u>\$ 355,322</u>

The reconciling amount represents \$254.7 million for the United States Transportation Command (USTC), which is reported by the U.S. Treasury as part of the AFWCF. However, for the purposes of Audited Financial Statements (AFS), USTC is included with the Other Defense Organizations reporting which is separate from the AFWCF. Therefore, USTC funds are not included in the AFWCF AFS.

Status of Fund Balance with Treasury

As of September 30	2012		2011	
(Amounts in thousands)				
1. Unobligated Balance				
A. Available	\$	106,559	\$	555,328
B. Unavailable		0		0
2. Obligated Balance not yet Disbursed	\$	7,060,232	\$	7,364,315
3. Nonbudgetary FBWT	\$	0	\$	0
4. NonFBWT Budgetary Accounts	\$	(6,610,254)	\$	(7,248,714)
5. Total	\$	556,537	\$	670,929

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

Unobligated Balance is classified as available or unavailable and represents the cumulative amount of budgetary authority that has not been set aside to cover outstanding obligations. The unavailable balance consists of funds temporarily precluded from obligation by law. Certain unobligated balances may be restricted to future use and are not apportioned for current use. The AFWCF has no restrictions on unobligated balances.

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

Nonbudgetary FBWT includes accounts that do not have budgetary authority, such as deposit funds, unavailable receipt accounts, clearing accounts, and nonentity FBWT. The AFWCF currently does not have a Nonbudgetary FBWT.

NonFBWT Budgetary Accounts reduces the Status of FBWT. The amount reported as NonFBWT Budgetary Accounts is comprised of contract authority, unfilled orders without advance from customers, and accounts receivable.

Note 4. Investments and Related Interest

The AFWCF has no Investments and Related Interest.



Note 5. Accounts Receivable

As of September 30	2012		
	Gross Amount Due	Allowance For Estimated Uncollectibles	Accounts Receivable, Net
(Amounts in thousands)			
1. Intragovernmental Receivables	\$ 778,172	N/A	\$ 778,172
2. Nonfederal Receivables (From the Public)	\$ 12,452	\$ (7,660)	\$ 4,792
3. Total Accounts Receivable	\$ 790,624	\$ (7,660)	\$ 782,964

As of September 30	2011		
	Gross Amount Due	Allowance For Estimated Uncollectibles	Accounts Receivable, Net
(Amounts in thousands)			
1. Intragovernmental Receivables	\$ 933,040	N/A	\$ 933,040
2. Nonfederal Receivables (From the Public)	\$ 12,405	\$ (8,695)	\$ 3,710
3. Total Accounts Receivable	\$ 945,445	\$ (8,695)	\$ 936,750

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

Note 6. Other Assets

As of September 30 (Amounts in thousands)	2012	2011
1. Intragovernmental Other Assets		
A. Advances and Prepayments	\$ 28	\$ 4
B. Other Assets	167,711	111,122
C. Total Intragovernmental Other Assets	<u>\$ 167,739</u>	<u>\$ 111,126</u>
2. Nonfederal Other Assets		
A. Outstanding Contract Financing Payments	\$ 121,079	\$ 164,286
B. Advances and Prepayments	118,754	172,083
C. Other Assets (With the Public)	158	232
D. Total Nonfederal Other Assets	<u>\$ 239,991</u>	<u>\$ 336,601</u>
3. Total Other Assets	<u>\$ 407,730</u>	<u>\$ 447,727</u>

Contract terms and conditions for certain types of contract financing payments convey certain rights to the Government 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 AFWCF is not obligated to make payment to the contractor until delivery and acceptance.

The balance in Outstanding Contract Financing Payments includes \$102.6 million in contract financing payments and an additional \$18.5 million in estimated future payments to contractors upon delivery and government acceptance of a satisfactory product. See additional discussion in Note 15, Other Liabilities.

The \$167.7 million in Intragovernmental Other Assets - Other Assets and the \$157.5 thousand balance in Nonfederal Other Assets – Other Assets (With the Public) are comprised of Supply Management Activity Group's assets returned to vendors for which credit is pending. There will be no dollar payments received for this credit but vendor billings will be offset.



Note 7. Cash and Other Monetary Assets

The AFWCF has no Cash and Other Monetary Assets.

Note 8. Direct Loan and Loan Guarantees

The AFWCF has no Direct Loan and/or Loan Guarantee Programs.

Note 9. Inventory and Related Property

As of September 30	2012		2011	
(Amounts in thousands)				
1. Inventory, Net	\$	25,957,956	\$	26,675,393
2. Operating Materiel & Supplies, Net		141,642		137,828
3. Stockpile Materiel, Net		0		0
4. Total	\$	26,099,598	\$	26,813,221

Inventory, Net

As of September 30	2012			Valuation Method
	Inventory, Gross Value	Revaluation Allowance	Inventory, Net	
(Amounts in thousands)				
1. Inventory Categories				
A. Available and Purchased for Resale	\$ 15,907,341	\$ (23,689)	15,883,652	MAC,FIFO,LAC
B. Held for Repair	13,994,240	(3,964,574)	10,029,666	LAC,MAC
C. Excess, Obsolete, and Unserviceable	53,822	(53,822)	0	NRV
D. Raw Materiel	0	0	0	MAC,SP,LAC
E. Work in Process	44,638	0	44,638	AC
F. Total	\$ 30,000,041	\$ (4,042,085)	25,957,956	

As of September 30	2011			Valuation Method
	Inventory, Gross Value	Revaluation Allowance	Inventory, Net	
(Amounts in thousands)				
1. Inventory Categories				
A. Available and Purchased for Resale	\$ 16,726,636	\$ (17,269)	16,709,367	LAC,MAC
B. Held for Repair	13,916,093	(3,987,787)	9,928,306	LAC,MAC
C. Excess, Obsolete, and Unserviceable	171,099	(171,099)	0	NRV
D. Raw Materiel	0	0	0	MAC,SP,LAC
E. Work in Process	37,720	0	37,720	AC
F. Total	\$ 30,851,548	\$ (4,176,155)	26,675,393	

Legend for Valuation Methods:		
LAC = Latest Acquisition Cost	NRV = Net Realizable Value	MAC = Moving Average Cost
SP = Standard Price	LCM = Lower of Cost or Market	
AC = Actual Cost	O = Other	

Restrictions

There are no restrictions on the use, sale, or disposition of inventory except for War Reserve Materiel and nuclear related spare parts.

General Composition of Inventory

Inventory includes weapon system consumable and reparable parts, base supply items, and medical-dental supplies. Inventory is tangible personal property that is held for sale or held for repair for eventual sale, in the process of production for sale, or to be consumed in the production of goods for sale or in the provision of services for a fee.

Definitions

Inventory Available and Purchased for Resale includes consumable and reparable parts owned and managed by AFWCF.

Inventory Held for Repair is damaged inventory that requires repair to make it suitable for sale. Many of the inventory items are more economical to repair than to procure. In addition, because AFWCF often relies on weapon systems and machinery no longer in production, AFWCF 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.

Excess, Obsolete, and Unserviceable inventory consists of obsolete, excess to requirements, or items that cannot be economically repaired and are awaiting disposal.

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.



Operating Materiel and Supplies, Net

As of September 30	2012			Valuation Method
	OM&S Gross Value	Revaluation Allowance	OM&S, Net	
(Amounts in thousands)				
1. OM&S Categories				
A. Held for Use	\$ 141,642	\$ 0	\$ 141,642	SP, LAC, MAC
B. Held for Repair	0	0	0	SP, LAC, MAC
C. Excess, Obsolete, and Unserviceable	0	0	0	NRV
D. Total	\$ 141,642	\$ 0	\$ 141,642	

As of September 30	2011			Valuation Method
	OM&S Gross Value	Revaluation Allowance	OM&S, Net	
(Amounts in thousands)				
1. OM&S Categories				
A. Held for Use	\$ 137,828	\$ 0	\$ 137,828	SP, LAC, MAC
B. Held for Repair	0	0	0	SP, LAC, MAC
C. Excess, Obsolete, and Unserviceable	0	0	0	NRV
D. Total	\$ 137,828	\$ 0	\$ 137,828	

Legend for Valuation Methods:

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

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

MAC = Moving Average Cost

General Composition of Operating Materiel and Supplies

Operating Materiel and Supplies (OM&S) includes consumable parts and supplies used to remanufacture spare parts and repair weapons systems.

Restrictions

There are no restrictions on the use, sale, or disposition of OM&S.

Definition

Held for Use includes consumable parts and supplies.

Stockpile Materiel, Net

As of September 30	2012			Valuation Method
	Stockpile Materiel Amount	Allowance for Gains (Losses)	Stockpile Materiel, Net	

(Amounts in thousands)

1. Stockpile Materiel Categories

A. Held for Sale	\$	0	\$	0	\$	0	AC, LCM
B. Held in Reserve for Future Sale		0		0		0	AC, LCM
C. Total	\$	0	\$	0	\$	0	

As of September 30	2011			Valuation Method
	Stockpile Materiel Amount	Allowance for Gains (Losses)	Stockpile Materiel, Net	

(Amounts in thousands)

1. Stockpile Materiel Categories

A. Held for Sale	\$	0	\$	0	\$	0	AC, LCM
B. Held in Reserve for Future Sale		0		0		0	AC, LCM
C. Total	\$	0	\$	0	\$	0	

Legend for Valuation Methods:

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

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

MAC = Moving Average Cost

The AFWCF has no Stockpile Materiels.



Note 10. General PP&E, Net

As of September 30	2012				
	Depreciation/ Amortization Method	Service Life	Acquisition Value	(Accumulated Depreciation/ Amortization)	Net Book Value
(Amounts in thousands)					
1. Major Asset Classes					
A.Land	N/A	N/A	\$ 0	N/A	\$ 0
B.Buildings, Structures, and Facilities	S/L	20 Or 40	1,241,503	\$ (726,062)	515,441
C.Leasehold Improvements	S/L	lease term	0	0	0
D.Software	S/L	2-5 Or 10	1,160,024	(1,055,863)	104,161
E.General Equipment	S/L	5 or 10	2,946,622	(2,067,332)	879,290
F.Military Equipment	S/L	Various	0	0	0
G. Shipbuilding (Construction-in- Progress)	N/A	N/A	0	0	0
H.Assets Under Capital Lease	S/L	lease term	0	0	0
I. Construction-in- Progress (Excludes Military Equipment)	N/A	N/A	10,928	N/A	10,928
J. Other			0	0	0
K.Total General PP&E			\$ 5,359,077	\$ (3,849,257)	\$ 1,509,820

As of September 30	2011				
	Depreciation/ Amortization Method	Service Life	Acquisition Value	(Accumulated Depreciation/ Amortization)	Net Book Value
(Amounts in thousands)					
1. Major Asset Classes					
A.Land	N/A	N/A	\$ 0	N/A	\$ 0
B.Buildings, Structures, and Facilities	S/L	20 Or 40	1,195,805	\$ (707,649)	488,156
C.Leasehold Improvements	S/L	lease term	0	0	0
D.Software	S/L	2-5 Or 10	1,150,082	(1,010,668)	139,414
E.General Equipment	S/L	5 or 10	2,819,068	(2,012,299)	806,769
F.Military Equipment	S/L	Various	0	0	0
G. Shipbuilding (Construction-in- Progress)	N/A	N/A	0	0	0
H.Assets Under Capital Lease	S/L	lease term	0	0	0
I. Construction-in- Progress (Excludes Military Equipment)	N/A	N/A	24,590	N/A	24,590
J. Other			0	0	0
K.Total General PP&E			\$ 5,189,545	\$ (3,730,616)	\$ 1,458,929

Working Capital Fund
Notes to the Principal Statements

Note 15 for additional information on Capital Leases

Legend for Valuation Methods:

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

Air Force Working Capital Fund

Categories	Measure Quantity	Beginning Balance	Additions	Deletions	Ending Balance
Buildings and Structures	Each	0	0	0	0
Archeological Sites	Each	0	0	0	0
Museum Collection Items (Objects, Not Including Fine Art)	Each	0	0	0	0
Museum Collection Items (Objects, Fine Art)	Each	0	0	0	0

(Acres in Thousands)

Facility Code	Facility Title	Beginning Balance	Additions	Deletions	Ending Balance
9110	Government Owned Land	0	0	0	0
9111	State Owned Land	0	0	0	0
9120	Withdrawn Public land	0	0	0	0
9130	Licensed and Permitted Land	0	0	0	0
9140	Public Land	0	0	0	0
9210	Land Easement	0	0	0	0
9220	In-leased Land	0	0	0	0
9230	Foreign Land	0	0	0	0
Grand Total					0
TOTAL - All Other Lands					0
TOTAL – Stewardship Lands					0

AFWCF does not have any restrictions on the use or convertibility of General PP&E.

Assets Under Capital Lease

As of September 30	2012	2011
(Amounts in thousands)		
1. Entity as Lessee, Assets Under Capital Lease		
A. Land and Buildings	\$ 0	\$ 0
B. Equipment	0	0
C. Accumulated Amortization	0	0
D. Total Capital Leases	\$ 0	\$ 0



Note 11. Liabilities Not Covered by Budgetary Resources

As of September 30 (Amounts in thousands)	2012	2011
1. Intragovernmental Liabilities		
A. Accounts Payable	\$ 0	\$ 0
B. Debt	0	0
C. Other	48,144	48,504
D. Total Intragovernmental Liabilities	\$ 48,144	\$ 48,504
2. Nonfederal Liabilities		
A. Accounts Payable	\$ 0	\$ 0
B. Military Retirement and Other Federal Employment Benefits	217,518	214,927
C. Environmental Liabilities	0	0
D. Other Liabilities	0	0
E. Total Nonfederal Liabilities	\$ 217,518	\$ 214,927
3. Total Liabilities Not Covered by Budgetary Resources	\$ 265,662	\$ 263,431
4. Total Liabilities Covered by Budgetary Resources	\$ 1,016,937	\$ 1,167,226
5. Total Liabilities	\$ 1,282,599	\$ 1,430,657

Liabilities Not Covered by Budgetary Resources includes liabilities for which congressional action is needed before budgetary resources can be provided.

The \$48.1 million in Intragovernmental Liabilities - Other Liabilities is comprised of the portion of the total Air Force Federal Employee's Compensation Act (FECA) liability allocated to the AFWCF.

Military Retirement and Other Federal Employment Benefits consists of FECA actuarial liabilities not due and payable during the current fiscal year. Refer to Note 17, Military Retirement and Other Federal Employment Benefits, for additional details and disclosures.

Note 12. Accounts Payable

As of September 30	2012		
	Accounts Payable	Interest, Penalties, and Administrative Fees	Total
(Amounts in thousands)			
1. Intragovernmental Payables	\$ 180,355	\$ N/A	\$ 180,355
2. Nonfederal Payables (to the Public)	577,905	0	577,905
3. Total	\$ 758,260	\$ 0	\$ 758,260

As of September 30	2011		
	Accounts Payable	Interest, Penalties, and Administrative Fees	Total
(Amounts in thousands)			
1. Intragovernmental Payables	\$ 226,029	\$ N/A	\$ 226,029
2. Nonfederal Payables (to the Public)	694,713	0	694,713
3. Total	\$ 920,742	\$ 0	\$ 920,742

Accounts Payable include amounts owed to federal and nonfederal entities for goods and services received by AFWCF. The AFWCF's systems do not track intragovernmental transactions by customer at the transaction level. Buyer-side accounts payable are adjusted to agree with interagency seller-side accounts receivable. Accounts payable was adjusted by reclassifying amounts between federal and nonfederal accounts payable and applying both supported and unsupported undistributed disbursements at the reporting entity level.

Note 13. Debt

The AFWCF has no Debt.

Note 14. Environmental Liabilities and Disposal Liabilities

The AFWCF has no Environmental Liabilities and Disposal Liabilities.



Note 15. Other Liabilities

As of September 30

2012 (Amounts in Thousands)

Current Liability	Noncurrent Liability	Total
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1. Intragovernmental

A. Advances from Others	\$ 0	\$ 0	\$ 0
B. Deposit Funds and Suspense Account Liabilities	0	0	0
C. Disbursing Officer Cash	0	0	0
D. Judgment Fund Liabilities	0	0	0
E. FECA Reimbursement to the Department of Labor	21,301	26,842	48,143
F. Custodial Liabilities	155	0	155
G. Employer Contribution and Payroll Taxes Payable	7,006	0	7,006
H. Other Liabilities	0	0	0
I. Total Intragovernmental Other Liabilities	\$ 28,462	\$ 26,842	\$ 55,304

2. Nonfederal

A. Accrued Funded Payroll and Benefits	\$ 137,450	\$ 0	\$ 137,450
B. Advances from Others	46,753	0	46,753
C. Deferred Credits	0	0	0
D. Deposit Funds and Suspense Accounts	0	0	0
E. Temporary Early Retirement Authority	0	0	0
F. Nonenvironmental Disposal Liabilities			
(1) Military Equipment (Nonnuclear)	0	0	0
(2) Excess/Obsolete Structures	0	0	0
G. Accrued Unfunded Annual Leave	0	0	0
H. Capital Lease Liability	0	0	0
I. Contract Holdbacks	827	0	827
J. Employer Contribution and Payroll Taxes Payable	0	0	0
K. Contingent Liabilities	0	18,510	18,510
L. Other Liabilities	47,977	0	47,977
M. Total Nonfederal Other Liabilities	\$ 233,007	\$ 18,510	\$ 251,517

3. Total Other Liabilities

	\$ 261,469	\$ 45,352	\$ 306,821
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Working Capital Fund
Notes to the Principal Statements

As of September 30	2011		
	Current Liability	Noncurrent Liability	Total
(Amounts in thousands)			
1. Intragovernmental			
A. Advances from Others	\$ 0	\$ 0	\$ 0
B. Deposit Funds and Suspense			
Account Liabilities	0	0	0
C. Disbursing Officer Cash	0	0	0
D. Judgment Fund Liabilities	0	0	0
E. FECA Reimbursement to the Department of Labor	20,571	27,932	48,503
F. Custodial Liabilities	296	0	296
G. Employer Contribution and Payroll Taxes Payable	6,931	0	6,931
H. Other Liabilities	0	0	0
I. Total Intragovernmental Other Liabilities	\$ 27,798	\$ 27,932	\$ 55,730
(Amounts in thousands)			
2. Nonfederal			
A. Accrued Funded Payroll and Benefits	\$ 139,025	\$ 0	\$ 139,025
B. Advances from Others	25,022	0	25,022
C. Deferred Credits	0	0	0
D. Deposit Funds and Suspense Accounts	0	0	0
E. Temporary Early Retirement Authority	0	0	0
F. Nonenvironmental Disposal Liabilities			
(1) Military Equipment (Nonnuclear)	0	0	0
(2) Excess/Obsolete Structures	0	0	0
(3) Conventional Munitions Disposal	0	0	0
G. Accrued Unfunded Annual Leave	0	0	0
H. Capital Lease Liability	0	0	0
I. Contract Holdbacks	1,199	0	1,199
J. Employer Contribution and Payroll Taxes Payable	0	0	0
K. Contingent Liabilities	0	24,605	24,605
L. Other Liabilities	49,407	0	49,407
M. Total Nonfederal Other Liabilities	\$ 214,653	\$ 24,605	\$ 239,258
3. Total Other Liabilities	\$ 242,451	\$ 52,537	\$ 294,988



The \$48.0 million balance in the Nonfederal Other Liabilities – Other Liabilities primarily consist of accrued liabilities established in the Consolidated Sustainment Activity Group (CSAG) Supply as an offset to the asset established when foreign governments provide funds to buy their respective share of inventory that is owned and managed by the Air Force under a Cooperative Logistics Supply Support Agreement (CLSSA).

Contingent liabilities include \$18.5 million related to contracts authorizing progress payments based on cost as defined in the Federal Acquisition Regulation (FAR). In accordance with contract terms, specific rights to the contractors' work vests with the Federal Government when a specific type of contract financing payment is made. This action protects taxpayer funds in the event of contract nonperformance. It is DoD policy that these rights should not be misconstrued as rights of ownership. The AFWCF is under no obligation to pay contractors for amounts greater than the amounts of progress payments authorized in contracts until delivery and government acceptance. Due to the probability the contractors will complete their efforts and deliver satisfactory products, and because the amount of contractor costs incurred but yet unpaid are estimable, the AFWCF has recognized a contingent liability for the estimated unpaid costs that are considered conditional for payment pending delivery and government acceptance.

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

Capital Lease Liability

As of September 30	2012			
	Asset Category			
	Land and Buildings	Equipment	Other	Total
(Amounts in thousands)				
1. Future Payments Due				
A. 2013	\$ 0	\$ 0	\$ 0	\$ 0
B. 2014	0	0	0	0
C. 2015	0	0	0	0
D. 2016	0	0	0	0
E. 2017	0	0	0	0
F. After 5 Years	0	0	0	0
G. Total Future Lease Payments Due	\$ 0	\$ 0	\$ 0	\$ 0
H. Less: Imputed Interest Executory Costs	0	0	0	0
I. Net Capital Lease Liability	\$ 0	\$ 0	\$ 0	\$ 0
2. Capital Lease Liabilities Covered by Budgetary Resources			\$	0
3. Capital Lease Liabilities Not Covered by Budgetary Resources			\$	0

As of September 30	2011			
	Asset Category			
	Land and Buildings	Equipment	Other	Total
(Amounts in thousands)				
1. Future Payments Due				
A. 2012	\$ 0	\$ 0	\$ 0	\$ 0
B. 2013	0	0	0	0
C. 2014	0	0	0	0
D. 2015	0	0	0	0
E. 2016	0	0	0	0
F. After 5 Years	0	0	0	0
G. Total Future Lease Payments Due	\$ 0	\$ 0	\$ 0	\$ 0
H. Less: Imputed Interest Executory Costs	0	0	0	0
I. Net Capital Lease Liability	\$ 0	\$ 0	\$ 0	\$ 0
2. Capital Lease Liabilities Covered by Budgetary Resources			\$	0
3. Capital Lease Liabilities Not Covered by Budgetary Resources			\$	0



Note 16.	Commitments and Contingencies
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The AFWCF is a party in various administrative proceedings and legal actions, related to claims for environmental damage, equal opportunity matters, and contractual bid protests. The AFWCF's Office of the General Counsel considers the possibility of the AFWCF sustaining any losses on these legal actions to be remote.

The AFWCF is a party in numerous individual contracts that contain clauses, such as price escalation, award fee payments, or dispute resolution, that may result in a future outflow of budgetary resources. Currently, AFWCF has limited automated system processes by which it captures or assesses these potential liabilities; therefore, no associated liabilities are recognized or disclosed.

Note 17. Military Retirement and Other Federal Employment Benefits

As of September 30	2012				
	Liabilities		(Less: Assets Available to Pay Benefits)		Unfunded Liabilities
(Amounts in thousands)					
1. Pension and Health Benefits					
A. Military Retirement Pensions	\$	0	\$	0	0
B. Military Pre Medicare-Eligible Retiree Health Benefits		0		0	0
C. Military Medicare-Eligible Retiree Health Benefits		0		0	0
D. Total Pension and Health Benefits	\$	0	\$	0	0
2. Other Benefits					
A. FECA	\$	217,518	\$	0	217,518
B. Voluntary Separation Incentive Programs		0		0	0
C. DoD Education Benefits Fund		0		0	0
D. Other		0		0	0
E. Total Other Benefits	\$	217,518	\$	0	217,518
3. Total Military Retirement and Other Federal Employment Benefits:					
	\$	217,518	\$	0	217,518

Federal Employees Compensation Act (FECA)

The AFWCF actuarial liability for workers' compensation benefits is developed by the Department of Labor and is updated at the end of each fiscal year. The liability includes the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases, plus a component for incurred but not reported claims. The 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 (OMB's) economic assumptions for 10-year Treasury notes and bonds. Interest rate assumptions utilized for discounting were as follows:

- 2012
- 2.29% in Year 1
- 3.14% 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 CPIs) were applied to the calculation of projected future benefits. The actual rates for these factors for the charge back year (CBY) 2012 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
 2012 N/A N/A
 2013 2.83% 3.65%
 2014 2.03% 3.66%
 2015 1.93% 3.72%
 2016 2.00% 3.73%
 2017+ 2.03% 3.80%
 and thereafter

The model's resulting projections were analyzed to insure 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 2012 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 2012 projection to the average pattern for the projections of the most recent three years.

As of September 30	2011		
	Liabilities	(Less: Assets Available to Pay Benefits)	Unfunded Liabilities
(Amounts in thousands)(Amounts in thousands)			
1. Pension and Health Benefits			
A. Military Retirement Pensions	\$ 0	\$ 0	0
B. Military Pre Medicare-Eligible Retiree Health Benefits	0	0	0
C. Military Medicare-Eligible Retiree Health Benefits	0	0	0
D. Total Pension and Health Benefits	\$ 0	\$ 0	0
2. Other Benefits			
A. FECA	\$ 214,927	\$ 0	214,927
B. Voluntary Separation Incentive Programs	0	0	0
C. DoD Education Benefits Fund	0	0	0
D. Other	0	0	0
E. Total Other Benefits	\$ 214,927	\$ 0	214,927
3. Total Military Retirement and Other Federal Employment Benefits:	\$ 214,927	\$ 0	214,927

Working Capital Fund
Notes to the Principal Statements

As of September 30	2012				
	Military Retirement Pensions	Military Pre Medicare-Eligible Retiree Health Benefits	Military Medicare-Eligible Retiree Health Benefits	Voluntary Separation Incentive Programs	DoD Education Benefits Fund
(Amounts in thousands)					
Beginning Actuarial Liability	\$ 0	0	0	0	0
Plus Expenses:					
Normal Cost	0	0	0	0	0
Interest Cost	0	0	0	0	0
Plan Amendments	0	0	0	0	0
Experience Losses (Gains)	0	0	0	0	0
Other factors	0	0	0	0	0
Subtotal: Expenses before Losses (Gains) from Actuarial Assumption Changes	0	0	0	0	0
Actuarial losses/ (gains) due to:					
Changes in trend assumptions	0	0	0	0	0
Changes in assumptions other than trend	0	0	0	0	0
Subtotal: Losses (Gains) from Actuarial Assumption Changes	0	0	0	0	0
Total Expenses	\$ 0	0	0	0	0
Less Benefit Outlays	0	0	0	0	0
Total Changes in Actuarial Liability	\$ 0	0	0	0	0
Ending Actuarial Liability	\$ 0	0	0	0	0



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

Intragovernmental Costs and Exchange Revenue

As of September 30

(Amounts in thousands)

Military Retirement Benefits

1. Gross Cost

	2012	2011
A. Intragovernmental Cost	\$ 0	\$ 0
B. Nonfederal Cost	0	0
C. Total Cost	\$ 0	\$ 0

2. Earned Revenue

A. Intragovernmental Revenue	\$ 0	\$ 0
B. Nonfederal Revenue	0	0
C. Total Revenue	\$ 0	\$ 0

3. Losses/(Gains) from Actuarial Assumption Changes for Military Retirement Benefits

	\$ 0	\$ 0
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Total Net Cost

Civil Works

1. Gross Cost

A. Intragovernmental Cost	\$ 0	\$ 0
B. Nonfederal Cost	0	0
C. Total Cost	\$ 0	\$ 0

2. Earned Revenue

A. Intragovernmental Revenue	\$ 0	\$ 0
B. Nonfederal Revenue	0	0
C. Total Revenue	\$ 0	\$ 0

3. Losses/(Gains) from Actuarial Assumption Changes for Military Retirement Benefits

	\$ 0	\$ 0
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Total Net Cost

Military Personnel

1. Gross Cost

A. Intragovernmental Cost	\$ 0	\$ 0
B. Nonfederal Cost	0	0
C. Total Cost	\$ 0	\$ 0

2. Earned Revenue

A. Intragovernmental Revenue	\$ 0	\$ 0
B. Nonfederal Revenue	0	0
C. Total Revenue	\$ 0	\$ 0

3. Losses/(Gains) from Actuarial Assumption Changes for Military Retirement Benefits

	\$ 0	\$ 0
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Total Net Cost

Working Capital Fund
Notes to the Principal Statements

Operations, Readiness & Support

1. Gross Cost			
A. Intragovernmental Cost	\$	1,395,194	\$ 1,711,508
B. Nonfederal Cost		11,061,635	11,388,112
C. Total Cost	\$	12,456,829	\$ 13,099,620
2. Earned Revenue			
A. Intragovernmental Revenue	\$	(11,096,564)	\$ (11,501,527)
B. Nonfederal Revenue		(306,788)	(351,368)
C. Total Revenue	\$	(11,403,352)	\$ (11,852,895)
3. Losses/(Gains) from Actuarial Assumption Changes for Military Retirement Benefits	\$	0	\$ 0
Total Net Cost	\$	1,053,477	\$ 1,246,725

Procurement

1. Gross Cost			
A. Intragovernmental Cost	\$	0	\$ 0
B. Nonfederal Cost		0	0
C. Total Cost	\$	0	\$ 0
2. Earned Revenue			
A. Intragovernmental Revenue	\$	0	\$ 0
B. Nonfederal Revenue		0	0
C. Total Revenue	\$	0	\$ 0
3. Losses/(Gains) from Actuarial Assumption Changes for Military Retirement Benefits	\$	0	\$ 0
Total Net Cost	\$	0	\$ 0

Research, Development, Test & Evaluation

1. Gross Cost			
A. Intragovernmental Cost	\$	0	\$ 0
B. Nonfederal Cost		0	0
C. Total Cost	\$	0	\$ 0
2. Earned Revenue			
A. Intragovernmental Revenue	\$	0	\$ 0
B. Nonfederal Revenue		0	0
C. Total Revenue	\$	0	\$ 0
3. Losses/(Gains) from Actuarial Assumption Changes for Military Retirement Benefits	\$	0	\$ 0
Total Net Cost	\$	0	\$ 0

Family Housing & Military Construction

1. Gross Cost			
A. Intragovernmental Cost	\$	0	\$ 0
B. Nonfederal Cost		0	0
C. Total Cost	\$	0	\$ 0



2. Earned Revenue			
A. Intragovernmental Revenue	\$	0	\$ 0
B. Nonfederal Revenue		0	0
C. Total Revenue	\$	0	\$ 0
3. Losses/(Gains) from Actuarial Assumption Changes for Military Retirement Benefits	\$	0	\$ 0
Total Net Cost	\$	0	\$ 0
Consolidated			
1. Gross Cost			
A. Intragovernmental Cost	\$	1,395,194	\$ 1,711,508
B. Nonfederal Cost		11,061,635	11,388,112
C. Total Cost	\$	12,456,829	\$ 13,099,620
2. Earned Revenue			
A. Intragovernmental Revenue	\$	(11,096,564)	\$ (11,501,527)
B. Nonfederal Revenue		(306,788)	(351,368)
C. Total Revenue	\$	(11,403,352)	\$ (11,852,895)
3. Losses/(Gains) from Actuarial Assumption Changes for Military Retirement Benefits	\$	0	\$ 0
4. Costs Not Assigned to Programs	\$	0	\$ 0
5. (Less: Earned Revenues) Not Attributed to Programs	\$	0	\$ 0
Total Net Cost	\$	1,053,477	\$ 1,246,725

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

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

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

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

The AFWCF records transactions on an accrual basis. The AFWCF may not have all the actual costs and revenues input into the system in time for reporting. Accrual estimates based upon budget information and historical data are made as required by generally accepted accounting principles. These estimates reverse as actual costs or revenues are recorded.

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

The \$465.1 million in Other Financing Sources, Other consists primarily of other gains and losses due to the reclassification of intragovernmental transfers in or out without reimbursement for which Air Force could not determine the trading partners.

Appropriations Received on the Statement of Changes in Net Position (SCNP) does not agree with Appropriations on the Statement of Budgetary Resources (SBR). The difference is due to the inclusion of the liquidation of contract authority for the receipt of the appropriation, being recorded on the same line as the appropriation received, thus reducing the Appropriations (Discretionary and Mandatory) line on the SBR to zero. Refer to Note 20, Disclosures Related to the Statement of Budgetary Resources for further information.



Note 20. Disclosures Related to the Statement of Budgetary Resources

As of September 30 (Amounts in thousands)	2012	2011
1. Net Amount of Budgetary Resources Obligated for Undelivered Orders at the End of the Period	\$ 6,216,080	\$ 6,429,727
2. Available Borrowing and Contract Authority at the End of the Period	0	0

There is an (\$83.7) million abnormal balance on the AFWCF summary level trial balance within USSGLA 4610 that is not visible on the Unobligated Balance, end of year, Apportioned line on the Statement of Budgetary Resources (SBR). This abnormality occurred during 4th Quarter, FY 2012 and is caused by the \$190.3 million in open commitments recorded in USSGLA 4700. USSGLA 4610 and 4700 combined, make up the Unobligated Balance, end of year, Apportioned line, which closed the year with a positive \$106.6 million balance.

The abnormal balance in USSGLA 4610 will be cleared upon completion of the year end closing transaction when the \$106.6 million Unobligated Balance, end of year, is closed into USSGLA 4450. The \$106.6 million that closed into USSGLA 4450 will then be re-opened in USSGLA 4610 to begin FY 2013.

The AFWCF reported reimbursable obligations of \$12.3 billion in category B.

The SBR includes intraentity transactions because the statements are presented as combined.

Appropriations on the SBR, does not agree with Appropriations Received on the Statement of Changes in Net Position (SCNP). The difference is due to the inclusion of the liquidation of contract authority for the receipt of the appropriation, being recorded on the same line as the appropriation received, thus reducing the Appropriations (Discretionary and Mandatory) line on the SBR to zero.

Note 21. Reconciliation of Net Cost of Operations to Budget

As of September 30

2012

2011

(Amounts in thousands)

Resources Used to Finance Activities:

Budgetary Resources Obligated:

1. Obligations incurred	\$	12,336,028	\$	12,375,556
2. Less: Spending authority from offsetting collections and recoveries (-)		(12,469,386)		(12,854,369)
3. Obligations net of offsetting collections and recoveries	\$	(133,358)	\$	(478,813)
4. Less: Offsetting receipts (-)		0		0
5. Net obligations	\$	(133,358)	\$	(478,813)

Other Resources:

6. Donations and forfeitures of property		0		0
7. Transfers in/out without reimbursement (+/-)		34,967		(10,561)
8. Imputed financing from costs absorbed by others		180,027		191,388
9. Other (+/-)		465,112		85,423
10. Net other resources used to finance activities	\$	680,106	\$	266,250
11. Total resources used to finance activities	\$	546,748	\$	(212,563)

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 (-)	\$	213,648	\$	329,160
12b. Unfilled Customer Orders		(308,865)		(399,773)
13. Resources that fund expenses recognized in prior Periods (-)		(8,934)		(1,731)
14. Budgetary offsetting collections and receipts that do not affect Net Cost of Operations		0		0
15. Resources that finance the acquisition of assets (-)		(5,696,852)		(5,907,746)
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 (+/-)		(500,080)		(74,862)
17. Total resources used to finance items not part of the Net Cost of Operations	\$	(6,301,083)	\$	(6,054,952)
18. Total resources used to finance the Net Cost of Operations	\$	(5,754,335)	\$	(6,267,515)

- Unfilled Customer Orders

The \$465.1 million in Resources Used to Finance Activities, Other, consists primarily of other gains and losses due to the reclassification of intragovernmental transfers in or out without reimbursement for which Air Force could not determine the trading partners.

Resources Used to Finance Items not Part of the Net Cost of Operations, Other, is comprised of:

1. Other gains and losses totaling \$465.1 million due to the reclassification of intragovernmental transfers in or out without reimbursement for which Air Force could not determine the trading partners.
2. Property transfers in from DoD agencies totaling \$35.0 million.

Components Requiring or Generating Resources in Future Period, Other, in the prior year column, represents the change in the Federal Employees Compensation Act (FECA) unfunded liability.

Components not Requiring or Generating Resources, Other, is comprised of \$4.8 billion for Consolidated Sustainment Activity Group - Maintenance Division work-in-process offsets.



Note 21. Reconciliation of Net Cost of Operations to Budget

As of September 30

2012

2011

(Amounts in thousands)

Resources Used to Finance Activities:			
Budgetary Resources Obligated:			
1. Obligations incurred	\$	12,336,028	\$ 12,375,556
2. Less: Spending authority from offsetting collections and recoveries (-)		(12,469,386)	(12,854,369)
3. Obligations net of offsetting collections and recoveries	\$	(133,358)	\$ (478,813)
4. Less: Offsetting receipts (-)		0	0
5. Net obligations	\$	(133,358)	\$ (478,813)
Other Resources:			
6. Donations and forfeitures of property		0	0
7. Transfers in/out without reimbursement (+/-)		34,967	(10,561)
8. Imputed financing from costs absorbed by others		180,027	191,388
9. Other (+/-)		465,112	85,423
10. Net other resources used to finance activities	\$	680,106	\$ 266,250
11. Total resources used to finance activities	\$	546,748	\$ (212,563)
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 (-)	\$	213,648	\$ 329,160
12b. Unfilled Customer Orders		(308,865)	(399,773)
13. Resources that fund expenses recognized in prior Periods (-)		(8,934)	(1,731)
14. Budgetary offsetting collections and receipts that do not affect Net Cost of Operations		0	0
15. Resources that finance the acquisition of assets (-)		(5,696,852)	(5,907,746)
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 (+/-)		(500,080)	(74,862)
17. Total resources used to finance items not part of the Net Cost of Operations	\$	(6,301,083)	\$ (6,054,952)
18. Total resources used to finance the Net Cost of Operations	\$	(5,754,335)	\$ (6,267,515)

Working Capital Fund
Notes to the Principal Statements

As of September 30		
	2012	2011

(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 (-)		7,840		259
23. Other (+/-)		3,137		66,258
24. Total components of Net Cost of Operations that will Require or Generate Resources in future periods	\$	10,977	\$	66,517

Components not Requiring or Generating Resources:

25. Depreciation and amortization	\$	168,796	\$	179,031
26. Revaluation of assets or liabilities (+/-)		2,184,928		2,732,182
27. Other (+/-)				
27a. Trust Fund Exchange Revenue		0		0
27b. Cost of Goods Sold		9,190,484		9,261,101
27c. Operating Material and Supplies Used		2,708		7,531
27d. Other		(4,750,081)		(4,732,122)
28. Total Components of Net Cost of Operations that will not Require or Generate Resources	\$	6,796,835	\$	7,447,723
29. Total components of Net Cost of Operations that will not Require or Generate Resources in the current period	\$	6,807,812	\$	7,514,240
30. Net Cost of Operations	\$	1,053,477	\$	1,246,725

Due to the AFWCF's financial system limitations, budgetary data does not agree with proprietary expenses and capitalized assets. The difference between budgetary and proprietary data is a previously identified deficiency.

A \$2.0 million adjustment was made to the Resources That Finance the Acquisition of Assets in order to align the note schedule with the amount reported on 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 intraagency 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 \$465.1 million in Resources Used to Finance Activities, Other, consists primarily of other gains and losses due to the reclassification of intragovernmental transfers in or out without reimbursement for which Air Force could not determine the trading partners.

Resources Used to Finance Items not Part of the Net Cost of Operations, Other, is comprised of:

1. Other gains and losses totaling \$465.1 million due to the reclassification of intragovernmental transfers in or out without reimbursement for which Air Force could not determine the trading partners.
2. Property transfers in from DoD agencies totaling \$35.0 million.

Components Requiring or Generating Resources in Future Period, Other, in the prior year column, represents the change in the Federal Employees Compensation Act (FECA) unfunded liability.

Components not Requiring or Generating Resources, Other, is comprised of \$4.8 billion for Consolidated Sustainment Activity Group - Maintenance Division work-in-process offsets.

Note 23. Earmarked Funds

AFWCF has no Earmarked Funds.

Note 24. Fiduciary Activities

AFWCF has no Fiduciary Activities.

Note 25. Other Disclosures

AFWCF has no other disclosures.

Note 26. Restatements

AFWCF has no Restatements.



Working Capital Fund

Fiscal Year 2012

Required Supplementary Information

Department of Defense
Air Force Working Capital Fund
STATEMENT OF DISAGGREGATED BUDGETARY RESOURCES
For the periods ended September 30, 2012 and 2011
(\$ in Thousands)

	<u>Operations, Readiness & Support</u>	<u>2012 Combined</u>	<u>2011 Combined</u>
Budgetary Resources:			
Unobligated balance brought for, October 1	555,328	555,328	532,408
Unobligated balance brought forward,			
October 1, as adjusted	555,328	555,328	532,408
Recoveries of prior year unpaid obligations	38,915		
Other changes in unobligated balance (+ or -)	(553,765)	(553,765)	(19,801)
Unobligated balance from prior year budget authority, net	40,478	40,478	616,546
Appropriations (discretionary and mandatory)	0	0	66,861
Contract Authority (discretionary and mandatory)	7,559,690	7,559,690	7,989,074
Spending Authority from offsetting collections (discretionary and mandatory)	<u>4,842,419</u>	<u>4,842,419</u>	<u>4,258,403</u>
Total Budgetary Resources	<u>12,442,587</u>	<u>12,442,587</u>	<u>12,930,884</u>
Status of Budgetary Resources:			
Obligations Incurred	12,336,028	12,336,028	12,375,556
Unobligated balance, end of year, Apportioned	<u>106,559</u>	<u>106,559</u>	<u>555,328</u>
Total unobligated balance, end of year	<u>106,559</u>	<u>106,559</u>	<u>555,328</u>
Total Budgetary Resources	<u>12,442,587</u>	<u>12,442,587</u>	<u>12,930,884</u>
Change in Obligated Balance:			
Unpaid obligations, brought forward, October 1 (gross)	7,364,314	7,364,314	7,824,540
Uncollected customer payments from Federal sources, Brought forward, October 1 (-)	(3,619,244)	(3,619,244)	(3,893,169)
Obligated balance start of year (net), before adjustments (+ or -)	3,745,070	3,745,070	3,931,371
Obligated balance, start of year (net), as adjusted	3,745,070	3,745,070	3,931,371
Obligations incurred	12,336,028	12,336,028	12,375,556
Outlays (gross) (-)	(12,601,195)	(12,601,195)	(12,731,843)
Change in uncollected customer payments from Federal Sources (+ or -)	505,812	505,812	273,922
Recoveries of prior year unpaid obligations (-)	(38,915)	(38,915)	(103,939)
Obligated balance, end of year			
Unpaid Obligations, end of year (gross)	7,060,232	7,060,232	7,364,314
Uncollected customer payments from Federal sources, end of year (-)	<u>(3,113,433)</u>	<u>(3,113,433)</u>	<u>(3,619,247)</u>
Obligated balance, end of year	<u>3,946,800</u>	<u>3,946,799</u>	<u>3,745,067</u>
Budget Authority and Outlays, Net:			
Budget authority, gross (discretionary and mandatory)	12,402,109	12,402,109	12,314,338
Actual offsetting collections (discretionary and mandatory) (-)	(12,936,282)	(12,936,282)	(13,024,352)
Change in uncollected customer payments from Federal Sources (discretionary and mandatory) (+ or -)	<u>505,812</u>	<u>505,812</u>	<u>273,922</u>
Budget Authority, net (discretionary and mandatory)	<u>(28,361)</u>	<u>28,361</u>	<u>(436,092)</u>
Outlays, gross (discretionary and mandatory)	12,601,195	12,601,195	12,731,843
Actual offsetting collections (discretionary and mandatory) (-)	(12,936,282)	(12,936,282)	(13,024,352)
Outlays, net (discretionary and mandatory)	<u>335,087</u>	<u>(335,087)</u>	<u>(292,509)</u>
Agency Outlays, net (discretionary and mandatory)	<u>(335,087)</u>	<u>(335,087)</u>	<u>(292,509)</u>



Working Capital Fund

Fiscal Year 2012

Audit Opinion



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

November 8, 2012

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

SUBJECT: Independent Auditor's Report on the Air Force Working Capital Fund FY 2012 and FY 2011 Financial Statements (Report No. DODIG-2013-010)

The Chief Financial Officers Act of 1990, as amended, requires the Department of Defense Inspector General to audit the accompanying Air Force Working Capital Fund Consolidated Balance Sheet as of September 30, 2012 and 2011, and the Consolidated Statement of Net Cost, Consolidated Statement of Changes in Net Position, and Combined Statement of Budgetary Resources and related notes for the fiscal years then ended. The financial statements are the responsibility of Air Force management. Management is also responsible for implementing effective internal control and for complying with laws and regulations. In addition, management is responsible for implementing and maintaining financial management systems that comply with the requirements of the Federal Financial Management Improvement Act of 1996 (FFMIA). Our responsibility is to express an opinion on the financial statements based on our audit.

We are unable to express an opinion on the Air Force Working Capital Fund FY 2012 and FY 2011 Basic Financial Statements because of limitations on the scope of our work. Thus, the financial statements may be unreliable. In addition to our disclaimer, we are including the required Report on Internal Control and Compliance with Laws and Regulations. The report is an integral part of our auditor's report 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 Air Force (Financial Management and Comptroller) represented to us that the Air Force Working Capital Fund FY 2012 and FY 2011 Basic Financial Statements would not substantially conform to accounting principles generally accepted in the United States of America (U.S. GAAP) and that Air Force financial management and feeder systems were unable to adequately support material amounts on the financial statements as of September 30, 2012. 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 auditing standards that are consistent with the management representations made to us. Accordingly, we did not perform all the auditing procedures required by generally accepted government auditing standards and Office of Management and Budget (OMB) Bulletin 07-04, "Audit Requirements for Federal Financial Statements," as amended,¹ to determine whether material amounts on the financial statements were presented fairly.

¹ OMB Memorandum M-09-33, Technical Amendments to OMB Bulletin No. 07-04, "Audit Requirements for Federal Financial Statements," September 23, 2009.



Prior audits have identified, and the Air Force has acknowledged, the long-standing material internal control weaknesses identified in the Summary of Internal Control. These material internal control weaknesses may affect the reliability of certain information contained in the annual financial statements—much of which is taken from the same data sources.² Therefore, we are unable to express, and we do not express, an opinion on the Basic Financial Statements.

Summary of Internal Control

In planning our work, we considered Air Force internal control over financial reporting and compliance with applicable laws and regulations. We did this to determine our audit procedures 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 material weaknesses continue to exist in the following areas.

- Financial Management Systems
- In-Transit Inventory
- Operating Materials and Supplies
- General Property, Plant, and Equipment
- Subsidiary Ledgers and Special Journals
- Intragovernmental Eliminations
- Other Accounting Entries

A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

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

- Accounts Receivable Financial Reporting
- Accounts Payable Financial Reporting

Internal control work we conducted as part of our prior audits would not necessarily disclose all deficiencies. The Attachment offers additional details on the material weaknesses and significant deficiencies reported.

The Air Force reported the above weaknesses in its FY 2012 Statement of Assurance, except for the Operating Materials and Supplies; General Property, Plant, and Equipment; Subsidiary Ledgers and Special Journals; Intergovernmental Eliminations; and Other Accounting Entries.

² The annual financial statements include the Basic Financial Statements, Management Discussion and Analysis, Required Supplementary Stewardship Information, Required Supplementary Information, and Other Accompanying Information.

Compliance With Laws and Regulations

We limited our work to determining compliance with selected provisions of applicable laws and regulations related to financial reporting because management represented that instances of noncompliance identified in prior audits continue to exist. The Assistant Secretary of the Air Force (Financial Management and Comptroller) represented to us that Air Force financial management systems do not substantially comply with Federal financial management systems requirements, U.S. GAAP, and the U.S. Government Standard General Ledger at the transaction level. Therefore, we did not determine whether Air Force complied 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.

Other Information in the Annual Financial Statements

The Management Discussion and Analysis, Required Supplementary Information, and Other Accompanying Information in the annual financial statements include a wide range and detailed information and do not affect our opinion on the financial statements. The information is presented for use by management and those charged with governance and should not be used for other purposes. We did not audit and do not express an opinion on the information. We compared the information with the Air Force basic financial statements for consistency. Based on our limited work, we did not find any material inconsistencies between the information and the financial statements and applicable sections of OMB Circular No. A-136 (Revised), "Financial Reporting Requirements," August 3, 2012.

Scope and Methodology

Management is responsible for:

- preparing financial statements that conform with U.S. GAAP;
- establishing, maintaining, and assessing internal control to provide reasonable assurance that the broad control objectives of the Federal Managers' Financial Integrity Act of 1982 (FMFIA) are met;
- ensuring that Air Force financial management systems substantially comply with FMFIA requirements, and
- complying with applicable laws and regulations.

We are responsible for planning and performing the audit to obtain reasonable assurance and to provide an opinion on whether the Air Force basic financial statements are presented fairly, in all material respects, in conformity with U.S. GAAP. We are also responsible for (1) testing whether Air Force financial management systems substantially comply with the three FMFIA requirements, (2) testing compliance with selected provisions of laws and regulations that have a direct and material effect on the financial statements and laws for which OMB audit guidance requires testing, and (3) performing limited procedures with respect to certain other information appearing in the Annual Financial Statements.



We did not evaluate all internal controls relevant to operating objectives as broadly defined by FMFIA, such as those controls relevant to preparing statistical reports and ensuring efficient operations. We limited our internal control testing over financial reporting and compliance to previously identified material weaknesses and significant deficiencies that continue to exist. Because of inherent limitations in internal controls, misstatements due to error or fraud, losses, or noncompliance may nevertheless occur and not be detected.

Because of the significance of the limitations on the scope of our work, we were unable to and did not perform our audit of internal control in accordance with U.S. GAAP and OMB audit guidance. We considered the limitation on the scope of our work in forming conclusions and in testing the financial statements.

We performed our audit in accordance with U.S. generally accepted government auditing standards. We believe our audit provides a reasonable basis for our opinions and other conclusions.

Agency Comments and Our Evaluation

We provided a draft of this report to Air Force officials, who provided technical comments that we have incorporated as appropriate. Air Force officials expressed their continuing commitment to address the problems this report outlines.

This report is intended solely for the information and use of the Department's management, DoD Office of Inspector General, Office of Management and Budget, Government Accountability Office, and Congress and is not intended to be used by anyone other than these specified parties.

A handwritten signature in cursive script that reads "Lorin T. Venable".

Lorin T. Venable, CPA
Acting Assistant Inspector General
DoD Payments and Accounting Operations

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 to include providing reasonable assurance that Air Force personnel accumulated, recorded, and reported accounting data properly; met the requirements of applicable laws and regulations; and safeguarded assets against misappropriation and abuse. Our purpose was not to, and we do not, express an opinion on internal control over financial reporting. However, the following material weaknesses and significant deficiencies exist that could adversely affect Air Force financial reporting.

Previously Identified Material Weaknesses

Management acknowledged that it is unable to comply with applicable reporting requirements and has identified the following material weaknesses that continued to exist in the following areas.

Financial Management Systems

Statement of Federal Financial Accounting Concepts No. 1, "Objectives of Federal Financial Reporting," requires that financial management system controls be adequate to ensure that transactions are executed in accordance with budgetary and financial law and other requirements, are consistent with the purpose authorized, and are recorded in accordance with Federal accounting standards. Statement of Federal Financial Accounting Concepts No. 1 also requires that financial management system controls ensure proper safeguards for assets to deter fraud, waste, and abuse and provide adequate support for performance measurement information. The Assistant Secretary of the Air Force (Financial Management and Comptroller) acknowledged that many Air Force financial management systems did not substantially comply with Federal financial management system requirements. The design of the Air Force financial management and feeder systems did not allow them to collect and record financial information based on a full-accrual accounting basis. Until these systems are able to collect and report financial information in compliance with U.S. GAAP, the Air Force proprietary financial reporting will be largely based on budgetary transactions and nonfinancial feeder systems.

In-Transit Inventory

The Air Force supply management systems did not provide sufficient audit trails to confirm and value the in-transit inventory included as part of inventory held for sale on the Consolidated Balance Sheet.

Operating Materials and Supplies

The Air Force is required by Statement of Federal Financial Accounting Standards No. 3, "Accounting for Inventory and Related Property," to record an expense at the time a user consumes Operating Materials and Supplies. The Air Force did not record cost of goods sold and work-in-process in accordance with this statement. Additionally, uncertainties existed



regarding the existence and completeness of the quantities used to derive the balances reported in the financial statements for Operating Materials and Supplies inventory.

General Property, Plant, and Equipment

Statement of Federal Financial Accounting Standards No. 6, “Accounting for Property, Plant, and Equipment,” requires the Air Force to record General Property, Plant, and Equipment using acquisition cost, capitalized improvement costs, and depreciation expense. However, the Air Force could not verify General Property, Plant, and Equipment values in accordance with this statement. In addition, the General Property, Plant, and Equipment line item on the Balance Sheet did not include all Government-furnished equipment, with values exceeding the capitalization threshold, in the hands of contractors.

Subsidiary Ledgers and Special Journals

Air Force Working Capital Fund resource managers did not always maintain adequate documentation or use transaction subsidiary ledgers and special journals to support recorded trial balance accounts. Air Force and Defense Finance and Accounting Service personnel did not perform reconciliations and system validations to verify the accuracy of accounts receivable from Foreign Military Sales, progress payments to contractors, and accounts payable from the Consolidated Sustainment Activity Group Supply Division.

Intragovernmental Eliminations

The Air Force could not accurately identify all intragovernmental transactions by customer. Seller entities within DoD provided summary balances for revenue, accounts receivable, and unearned revenue to the buyer-side internal DoD accounting offices. In most cases, the Air Force adjusted its buyer-side records to recognize unrecorded costs and accounts payable.

Other Accounting Entries

The Air Force acknowledges that it continued to make material adjustments for financial reporting that were not supported by detailed transactions because of its inability to properly identify intragovernmental trading partner transactions and the deficiencies described above.

Previously Identified Significant Deficiencies

Previously identified significant deficiencies continue to exist in the following areas.

Accounts Receivable

The Air Force could not ensure the validity of Accounts Receivable reported on its financial statements because of significant deficiencies in internal control. Specifically, the significant deficiencies included intragovernmental trading partner eliminations, Foreign Military Sales, undistributed collections, the completeness of the Triannual Review, and the lack of supporting documentation.

Accounts Payable

The Air Force could not ensure the accuracy of Accounts Payable reported in the Basic Financial Statements because of significant deficiencies in intragovernmental trading partner eliminations, accruals, supporting documentation, and the completeness of the Triannual Review. Because of

these weaknesses, the Air Force was unable to properly reconcile and support the validity of Accounts Payable.

These financial management deficiencies may cause inaccurate management information. As a result, Air Force 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 determining 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 Air Force 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

FFMIA requires Air Force to establish and maintain financial management systems that comply substantially with the Federal financial management systems requirements, applicable Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level.

For FY 2012, Air Force did not fully comply with FFMIA. The Air Force acknowledged that many of its critical financial management and feeder systems did not substantially comply with the Federal financial management systems requirements, Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level as of September 30, 2012.

Antideficiency Act

Section 1341, title 31, United States Code (31 U.S.C. § 1341) limits the Air Force and its agents to making or authorizing expenditures or obligations that do not exceed the available appropriations or funds. Additionally, the Air Force or its agents may not contract or obligate for the payment of money before an appropriation is made available for that contract or obligation unless otherwise authorized by law. According to 31 U.S.C. § 1351, if an officer or employee of an executive agency violates the Antideficiency Act (ADA), the head of the agency must report immediately to the President and Congress all relevant facts and a statement of actions taken. During FY 2012, the Air Force Working Capital Fund did not report any ADA violations.

Audit Disclosures

The Assistant Secretary of the Air Force (Financial Management and Comptroller) acknowledged to us on June 28, 2012, that the Air Force financial management and feeder systems could not provide adequate evidence supporting various material amounts on the financial statements and that previously identified material weaknesses continued 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: Federal Credit Reform Act, Government Performance and Results Act, Pay Provisions and Allowance System for Civilian Employees, Prompt Payment



Act, Improper Payments Information Act, and Provisions Governing Claims of the United States Government (including provisions of the Debt Collection Improvement Act).

Recommendations

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

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A blue-tinted circular image showing an F-35 fighter jet in flight. The jet is positioned horizontally across the middle of the frame, flying from left to right. On its tail fin, the markings "EG", "33 FW", and "60747" are visible. Below the jet, a coastal city with buildings and a harbor is visible, along with a large body of water. The sky is filled with light clouds.

"Aim High ...

fly-fight-win"

For more information or to contact us:

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