GAO

United States General Accounting Office

Report to the Congress

August 1992

FINANCIAL AUDIT

Examination of the Army's Financial Statements for Fiscal Year 1991

147238

GAO/AFMD-92-83

GAO

United States
General Accounting Office
Washington, D.C. 20548

Comptroller General
of the United States

B-249197

August 7, 1992

To the President of the Senate and the
Speaker of the House of Representatives

Pursuant to the Chief Financial Officers Act of 1990 (Public Law 101-576), the Army is required to prepare agencywide financial statements for fiscal years 1991 and 1992 and have them audited. The purpose of this report is to present the results of our audit of the Army's Principal Statements for fiscal year 1991. The report, delivered to the Army on July 2, 1992, provides our opinion, which includes our reports on internal controls and compliance with laws and regulations.

We were unable to express an overall opinion on the Principal Statements primarily for two reasons. First, with respect to the report on financial position, there are material uncertainties regarding the reasonableness of amounts reported for most of the Army's assets. Second, the accounting systems' inadequacies and failure to adhere to Department of Defense and Army policies made an audit of the consolidated reports of operations, cash flows, and reconciliation impractical. Problems such as the lack of an integrated general ledger system and weak internal controls prevented us from assessing the reliability of these reports for the year ended September 30, 1991. Therefore, we caution users that the Principal Statements may not be reliable.

In addition to weak internal controls which limit the Army's ability to prepare reliable financial statements and other reports, our audit found that the internal controls cannot be relied upon to safeguard the Army's assets or ensure material compliance with budget authority and various laws and regulations. Our audit did not identify material instances of noncompliance with provisions of laws and regulations selected for testing. However, we are continuing to address the legal implications of (1) the Corps of Engineers not recording obligations for its Civil Works Revolving Fund equipment contracts and (2) a potential violation of the Anti-Deficiency Act at the Aviation Systems Command and will report on them if necessary. The overall results of our review of the Army's financial management operations are discussed in greater detail in a separate comprehensive report.

We are sending copies of this report to the Secretaries of Defense and the Army, the Director of the Office of Management and Budget, interested congressional committees, and other interested parties. Copies will be made available on request.

Charles A. Bowsher

Charles A. Bowsher
Comptroller General
of the United States

Contents

Abbreviations

CFO	Chief Financial Officer
DOD	Department of Defense
FMFIA	Federal Managers' Financial Integrity Act
OMB	Office of Management and Budget

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To the Secretary of the Army

Pursuant to the Chief Financial Officers (CFO) Act of 1990 (Public Law 101-576), we initiated an audit of the Army's Principal Statements consisting of the consolidated report on financial position as of September 30, 1991, and the related consolidated reports on operations, cash flow, and reconciliation for the fiscal year then ended. The Army is 1 of 10 pilot agencies required to prepare such statements and their first time preparation required a great deal of effort on the part of Army managers. The difficulty of the task was compounded by the Army's participation in the Desert Shield/Desert Storm operations which were carried out during fiscal year 1991.

We are unable to express an overall opinion on the Principal Statements primarily for two reasons. First, with respect to the report on financial position, there are material uncertainties regarding the reasonableness of amounts reported for most of the Army's assets. These include military equipment of $151 billion, inventories of $17 billion, real property of $61 billion, and construction in progress of $34 billion. These amounts were assembled from a variety of separate information systems of questionable reliability, and we were unable to satisfactorily verify or adjust the amounts.

Second, the accounting systems' inadequacies and failure to adhere to Department of Defense (DOD) and Army policies made an audit of the consolidated reports of operations, cash flow, and reconciliation impractical. Problems similar to those cited above with respect to the financial position as of October 1, 1990, the lack of an integrated general ledger system, and weak internal controls prevented us from assessing the reliability of reports showing transactions during the fiscal year ended September 30, 1991.

Therefore, we caution users that the Principal Statements may not be reliable. In addition to weak internal controls which limit the Army's ability to prepare reliable financial statements and other reports, our audit found that internal controls cannot be relied upon to safeguard the Army's assets or ensure material compliance with budget authority and various laws and regulations.

These results were not entirely unexpected because of known problems acknowledged by the Army at the outset of our audit. Before we completed our audit work, the Army had initiated actions to address the problems we are reporting, which will be more fully discussed in separate detailed reports. DOD has ongoing but longer range programs to improve accounting systems. Until the problems we are reporting are corrected, the Army will not have effective financial control over the assets entrusted to it, nor will it have reliable information from its financial systems to economically and efficiently control its operations or adapt them to the changing national defense environment.

Described briefly below are the significant findings precluding an opinion on the consolidated report on financial position and leading to an adverse opinion on the related internal controls as of September 30, 1991. This report also discusses the results of our tests of compliance with selected laws and regulations; our conclusions on the Overview of the Army, the Combining Statements, and other supplemental financial information; and the scope of our audit and the methodology we used.

Significant Findings Precluding an Opinion on the Report on Financial Position

On May 19, 1992, we proposed about $95 billion of adjustments to improve the accuracy and presentation of the Army's report on financial position.[1] The Army made about $55 billion of the adjustments to reclassify account balances and another $20.7 billion to correct account balances. The remaining adjustments of $19.3 billion relating to division-level inventories and ammunition at installations were not made because DOD's established accounting policies permitted the treatment given to these assets.

Even if all the proposed adjustments had been made, sufficient uncertainties regarding other amounts reported would have prevented us from expressing an opinion on the report on financial position. The following sections discuss these uncertainties.

Cash on Hand Is Not Reported

As of September 30, 1991, Army disbursing officers had $400 million of cash on hand which was not included in the financial statements because DOD policy required that cash held by disbursing officers not be recorded as an asset for external reports. Since the Army is responsible for cash it holds, we believe this stewardship responsibility should be reported in its financial statements.

[1] Management letter to the Assistant Secretary of the Army for Financial Management and the Director, Defense Finance and Accounting Service, (GAO/AFMD-92-68ML).

Unreliable and Incomplete Accounting for Inventories

The Army's inventory records and accounts did not accurately record either the quantities or the values of the reported $17 billion in inventories of spare parts and supplies as of September 30, 1991. The Army has acknowledged that inventory accuracy has been adversely affected by the failure to perform physical inventories required by Army policy. Also, inventory records did not report reliable information because other accounting polices were not followed or were inadequate. Examples include the following.

- About 35 percent of the logistics records were inaccurate by more than 10 percent for the $12 billion of inventory stored at Army depots, and about 7,400 items had been improperly valued.
- Over $18.4 billion of ammunition inventory held in central storage areas at installations were not recorded in accounting records and there were no accounting or logistics records for about $0.8 billion of ammunition inventories either in transit or in production.
- About $0.9 billion in inventories held by combat and support divisions was not recorded in accounting records.
- Custodial records were inaccurate for the $2.3 billion in inventories stored at installations.

As a result of these deficiencies, we could not determine the value of the Army's inventories.

Military Equipment Not Reported at Actual Cost

The Army's financial statements reported military equipment valued at $151 billion. DOD accounting policy requires that such equipment be valued at the actual costs incurred to acquire the equipment and put it into operation. Instead, the Army accounted for its equipment at a standard price intended to reflect the most recent acquisition cost.

Other Equipment Not Recorded Accurately

Accountable property officers maintain property books for capital equipment and sensitive items. However, we found that the property books were often not periodically updated or reconciled with general ledger records. For example, Corps of Engineers managers were unable to substantiate the locations or the value of the estimated $1.3 billion equipment reported in the Corps' general ledger. Furthermore, at the 10 installations we visited, 22 of 123 property books for nontactical units were not reported to the accounting office, and $134 million of property was, in turn, not included in the financial statements.

Real Property Accounts Are Not Accurately Reported

The Army reported $61 billion of real property in its September 30, 1991, report on financial position. Of this amount, the Corps of Engineers reported almost $28 billion in real property, but records were not maintained to show the cost of its real property assets; accordingly, we were unable to substantiate this amount. For the balance of $33 billion, we found discrepancies between the amounts reported on the Army installations' general ledgers and the subsidiary property records, as well as other weaknesses in recording real property transactions. For example, at six installations, the general ledger property accounts were approximately $461 million less than the subsidiary property records.

Some of the costs of completed military construction projects were included in both the Corps of Engineers' construction-in-progress accounts and Army installations' property records, thus causing the financial statements to double count the value of this property. The Corps was unable to determine the extent of the overstatement in the construction-in-progress account balance of $34 billion as of September 30, 1991.

Not All Liabilities Reported

Contrary to established policy, the Army did not record all estimable liabilities or disclose in the footnotes to the financial statements billions of dollars of potential liabilities for chemical weapons destruction, environmental pollution claims, and cleanup of hazardous waste sites.

Internal Controls Are Not Satisfactory

Our tests of the internal controls affecting or potentially affecting the Army's Principal Statements showed they could not be relied upon to achieve their intended objectives. The internal controls we evaluated were those designed to

- safeguard assets against loss from unauthorized use or disposition;
- assure the execution of transactions in accordance with budgetary authority and applicable laws and regulations; and
- properly record, process, and summarize transactions to permit the preparation of financial statements and to maintain accountability for assets.

Our work disclosed material weaknesses in internal controls that, in our opinion, result in more than a relatively low risk that (1) unauthorized use or disposition of assets could lead to losses considered to be material in relation to the Principal Statements and (2) instances of noncompliance and misstatements material in relation to the Principal Statements could occur and not be detected within a timely period. A number of these weaknesses are root causes preventing us from expressing an overall opinion on the Principal Statements. Some specific weaknesses in internal controls not already mentioned are discussed below.

Inventory Systems Do Not Provide Financial Accountability and Control

Serious problems were noted in the manner in which the Army manages and controls its inventories.

- The Army has unrequired inventories of $2 billion, or 12 percent of its reported total inventory. An additional $2 billion in unrequired inventory had been written down to a $50 million scrap value.
- Obvious errors in inventory reports and records, such as negative inventory account balances, were not investigated.
- Large amounts of military equipment and related inventories awaiting repair were unsecured and unprotected, and security over depot warehouses was lax.

As a result of these and other deficiencies, the Army's inventories are highly susceptible to mismanagement and loss.

Unsupported Adjustments Made to Financial Statements

The Defense Finance and Accounting Service initiated and processed adjustments and corrections valued at $250 billion after the end of fiscal year 1991. However, officials were unable to provide records or documentation to support many of the adjustments and, in those cases where documentation did exist, there was no evidence of supervisory review or approval of the adjustments.

Controls Over Contractor-Held Property Are Not in Place

The Army does not have a system or procedure to track and monitor property owned by the Army but held by contractors. Once property is given to contractors, it is dropped from the Army's records, leaving the contractor to account for the property in its possession. As of September 30, 1991, contractors reported that they had almost $11.3 billion of inventory, equipment, and real property that was owned by the government.

Army Did Not Report All Material Control Weaknesses

The additional material internal control and systems weaknesses noted in our audit and our evaluation of the overall magnitude of other known weaknesses lead us to disagree with the Army's fiscal year 1991 report to the Secretary of Defense on internal controls. The Army reports annually to the Secretary of Defense as part of DOD's evaluation of controls under the Federal Managers' Financial Integrity Act of 1982 (FMFIA) (31 U.S.C. 3512). In the 1991 report, the Secretary stated that the Army's internal control structure, except for 12 material weaknesses, provided reasonable assurance that control objectives were achieved.

Compliance With Certain Laws and Regulations

We tested the Army's compliance with the provisions of selected laws and regulations listed on page 13. We are continuing to address the legal implications of the following two matters and, if necessary, we will report separately on them:

- The Corps of Engineers awards its Civil Works Revolving Fund equipment contracts if it is estimated that the required payments can be made out of the Fund's projected revenue. However, the Corps does not record these contracts as obligations when the contracts are awarded. This practice raises the issue of whether the Corps is violating the general requirements to record contracts as obligations and ensure that contracts are supported by available budget authority.
- The Aviation Systems Command made unsupported adjustments of its recorded obligations. This action raises the issue of whether the adjustments obscured potential violations of the Anti-Deficiency Act and whether the Command violated an Army regulation that requires reports and follow-up on potential violations.

Subject to the resolution of these two matters, our tests disclosed no specific instances of material noncompliance with the selected laws and regulations. However, as discussed above, we disagree with the Army's 1991 report to the Secretary of Defense on internal controls. Office of Management and Budget (OMB) Bulletin 91-14 (September 10, 1991) characterizes a conflict between an agency's FMFIA report and the auditor's evaluation of the agency's internal control system as a condition of noncompliance with FMFIA.

Other Information Reported

The Overview of the Army, the Combining Statements providing financial information by program and activity, and other supplemental information contain a wide range of data, some of which are not directly related to the Principal Statements. Our limited tests of this information and the other problems identified in our audit prevent us from expressing an opinion on this information. We have expressed concerns to DOD and Army officials about how the Overview and Combining Statements are presented.

The Overview does not adequately describe the Army's mission and goals and its progress in attaining its goals. It discusses several programs that are relatively minor in comparison to the Army's overall mission and goals and that represent a small percent of its appropriations and assets. These programs include counternarcotics, disaster relief and emergency assistance, and security assistance. Likewise, the performance measures presented do not address the Army's primary mission and goals and do not show the costs of the various programs. A discussion of the Army's overall mission and major programs, such as new weapons procurement and inventory management, would be much more informative and useful.

The Combining Statements do not consist of like functions for which meaningful performance measures could be identified. For example, the Conventional Ammunition Working Capital Fund, which finances the production of conventional ammunition, was consolidated with the Corps of Engineers' Revolving Fund, which finances Corps activities and equipment.

Objectives, Scope, and Methodology

Army's management is responsible for

- preparing the annual financial statements in conformity with applicable accounting principles,
- establishing and maintaining internal controls and systems to provide reasonable assurance that the broad control objectives of FMFIA are met, and
- complying with applicable laws and regulations.

Our responsibility is to perform tests to obtain reasonable assurance about whether the Principal Statements are reliable and whether relevant internal controls are in place and operating effectively. We are also responsible for testing compliance with provisions of selected laws and regulations and for performing limited procedures with respect to certain other information appearing in these annual financial statements.

In carrying out these responsibilities, we

- examined, on a test basis, evidence supporting the amounts and disclosures in the Principal Statements;

- assessed the accounting standards used and significant estimates made by management; and
- evaluated the overall presentation of the Principal Statements.

We also evaluated and tested relevant internal controls which encompassed the following areas:

- financial reporting,
- stock fund inventories,
- ammunition inventory,
- facilities,
- military equipment,
- civilian pay,
- military pay,
- depot maintenance,
- equipment,
- construction, and
- treasury.

We tested compliance with selected provisions of the following laws and regulations:

- Prompt Payment Act (31 U.S.C. 3901-3906) and Office of Management and Budget implementing regulations (OMB Circular A-125);
- Anti-Deficiency Act (31 U.S.C. 1341, 1342, and 1511-1519);
- Federal Managers' Financial Integrity Act of 1982 (31 U.S.C. 3512(b) and (c));
- Chief Financial Officers Act of 1990 (Public Law 101-576) and OMB implementing regulations (OMB Bulletins 91-14 and 91-15); and
- Department of Defense appropriation acts.

We also considered compliance with the process required by FMFIA for evaluating and reporting on internal control and accounting systems. We did not evaluate all internal controls relevant to operating objectives as broadly defined by FMFIA and implementing guidance, such as those controls relevant to preparing statistical reports and ensuring efficient operations. We limited our work to accounting and other controls necessary to support amounts and disclosures in the Principal Statements and to achieve the objectives outlined in our opinion on internal controls.

Our work was also limited in the following respects:

Classified Programs Not Audited. The Army directs certain programs and maintains assets which are classified for national security reasons. According to an Army official, the consolidated statement of financial position does not contain information about classified assets. While at other times we have reviewed specific aspects of classified programs at the request of the Congress, we performed no auditing procedures related to classified programs and assets during this audit.

Certain Disbursements of Army Funds Not Audited. During fiscal year 1991, approximately $12.6 billion of disbursements were made from Army funds by non-Army entities. These entities—primarily the Defense Logistics Agency; the General Services Administration; and the Departments of State, Air Force, and Navy—are responsible through interservice and interagency agreements for administering contracts for the Army. We did not perform auditing procedures at non-Army entities concerning disbursements of Army funds; however, we did review the Army's procedures related to these disbursements.

Army National Guard and Army Reserves Not Audited. The consolidated statement of financial position includes assets for which the Army National Guard or Army Reserves are accountable. These entities are operating units of the Army and receive their funding through Army appropriations. As of September 30, 1991, the Army National Guard and Army Reserves reported assets of $24.4 billion and $5 billion and expenses of $5 billion and $3 billion, respectively. Together, Army National Guard and Army Reserve assets comprise 8 percent of total Army assets, while their expenses comprise 8 percent of total Army expenses for fiscal year 1991. We did not audit these entities.

In all other respects, our work was done in accordance with Government Auditing Standards and OMB Bulletin 91-14, "Audit Requirements for Federal Financial Statements."

Other Reports

Our audit work has enabled us to make important and comprehensive recommendations for improving financial management and accounting for both the Army and DOD. These recommendations will be included in separate detailed reports.

Charles A. Bowsher

Charles A. Bowsher
Comptroller General
of the United States

June 24, 1992

Principal Statements

Report on Financial Position

as of September 30, 1991

Identification:
Department/Agency: **Department of the Army**
Bureau/Organizational Unit: **Principal Statements**
OMB Identification Code:
Basis Used:

ASSETS		Total
1. Fund Balance with Treasury **(Note 1.C)** and Cash		
a. Fund Balance	47,999,675,569	
b. Cash		
c. Foreign Currency, Net		
d. Subtotal		47,999,675,569
2. Accounts Receivable **(Note 1.E)**		
a. Federal Agencies		
1. Current	1,080,679,884	
2. Noncurrent		
b. Public		
1. Current	177,006,231	
2. Noncurrent	916,796,297	
c. Less: Allowances	-61,970,691	
d. Subtotal		2,112,511,721
3. Advances and Prepayments **(Note 1.F)**		
a. Federal Agencies	-75,231,401	
b. Public	966,032,313	
c. Subtotal		890,800,912
4. Inventories **(Note 1.G)**		
a. Operating consumables	10,236,898,509	
b. Product or Service Components	4,734,466,157	
c. Stockpiled materials	2,474,303,000	
d. Other		
e. Subtotal		17,445,667,666
5. Investments, Net		
a. Federal Securities	224,858,484	
b. Non-Federal Securities		
c. Other-Public Securities		
d. Subtotal		224,858,484
6. Loans Receivables		
a. Federal Agencies		
1. Current		
2. Noncurrent		
b. Public		
1. Current		
2. Noncurrent	550,000	
c. Less: Allowances		
d. Subtotal		550,000

as of September 30, 1991

Bureau/Organizational Unit:

ASSETS Continued		**Total**
7. Property, Plant, and Equipment, Net **(Note 1.H)**		
a. Structures, Facilities, and Leasehold Improvements	60,727,183,580	
b. Military Equipment	150,808,676,040	
c. ADP Software	12,876,319	
d. Equipment	1,266,870,382	
e. Assets Under Capital Lease	92,796,219	
f. Other	62,036,727	
g. Construction-in-Progress	33,832,242,022	
h. Land	3,883,870,697	
i. Allowances	-4,190,494,641	
j. Subtotal		246,496,057,345
8. Other Assets **(Note 1. I)**		
a. Acquired Collateral	7,438,504	
b. Deferred Exp from Cap Lease	54,584,638	
c. Inventories-Other (Ammunition)	25,207,141,000	
d. Other	5,367,108,232	
e. Subtotal		30,636,272,374
9. TOTAL ASSETS		345,806,394,071
LIABILITIES		
10. Accounts Payable **(Note 1.J)**		
a. Federal Agencies	5,566,822,250	
b. Public	5,092,374,731	
c. Subtotal		10,659,196,981
11. Interest Payable		
a. Federal Agencies		
b. Public		
c. Subtotal		
12. Accrued Payroll and Benefits **(Note 1.K)**		2,510,862,214
13. Accrued Unfunded Annual Leave **(Note 1.L)**		1,617,840,348
14. Unearned Revenue (Advances)		
a. Federal Agencies	1,500,689,575	
b. Public	416,019,540	
c. Subtotal		1,916,709,115
15. Deposit Funds		26,034,520
16. Debt Issued Under Borrowing		
a. Gross Federal Debt		
b. Intragovernmental Debt		
c. Other Debt	662,560	
d. Subtotal		662,560
17. Actuarial Liabilities		
a. Pension Plans		
b. Insurance and Annuity Programs		
c. Subtotal		

as of September 30, 1991

Liabilities Continued		**Total**
18. Other Liabilities **(Note 1.M)**		
a. Property Furnished by Others	76,045,529	
b. Insurance Reserve, Civil Works	44,172,789	
c. Capital Lease, Civil Works	22,992,346	
d. Unearned Income	481,988,113	
e. Other	-232,098	
f. Subtotal		624,966,679
19. TOTAL LIABILITIES		17,356,272,417
EQUITY		
Appropriated Fund Equity		
20. Unexpended Financed Budget Authority		
a. Unexpended Appropriations	38,087,369,827	
b. Less: Unfilled Customer Orders		
c. Subtotal		38,087,369,827
21. Invested Capital		268,275,309,251
Revolving Fund Equity		
22. Revolving Fund Balance(s)		
a. Appropriated Capital	3,311,898,557	
b. Cumulative Results	16,918,428,078	
c. Donations		
d. Subtotal		20,230,326,635
Trust Fund Equity		
23. Trust Fund Balances		1,857,115,941
24. TOTAL EQUITY **(Note 1.N)**		328,450,121,654
25. TOTAL LIABILITIES AND EQUITY		345,806,394,071

Report on Operations

for the year ended September 30, 1991

Bureau/Organizational Unit: **Principal Statements**
OMB Identification Code:

REVENUES AND FINANCING SOURCES		
1. Appropriated Capital Used		79,998,735,628
2. Revenue		
a. Federal Sources	10,961,308,573	
b. Public Sources	472,404,769	
c. Subtotal		11,433,713,342
3. Government receipts		82,944,041
4. Other		
a. Interest Revenue Approp/Fund & Govt	21,243,295	
b. Interest Revenue Approp/Fund & NonGovt		
c. Gains	75,051,200	
d. Other	6,909,558,387	
e. Subtotal		7,005,852,882
5. Less: Receipts Returned to Treasury		-97,673,264
6. Total Financing Sources **(Note 1.B)**		98,423,572,629
OPERATING EXPENSES		
7. Cost of Goods Sold		8,450,927,415
8. Operating/Program Expenses, Funded **(Note 1.O)**		82,343,441,372
9. Interest Expense, Funded		
a. Federal Financing Bank/ Treasury Borrowings		
b. Federal Securities		
c. Other	2,373,910	
d. Subtotal		2,373,910
10. Other Funded Expenses **(Note 1.P)**		
a. Loss on Disposition of Assets	3,383,139	
b. Inventory Losses	151,570,702	
c. Investment Losses		
d. Other Losses	-32,126,023	
e. Subtotal		122,827,818

for the year ended September 30, 1991

Bureau/Organizational Unit:

NET RESULTS		Total
11. Unfunded Expenses		5,268,746,589
12. Total Operating Expenses		96,188,317,104
13. Net Results Before Adjustments		2,235,255,525
14. Less: Capital Expenditures		107,915,913
15. Less Extraordinary Items		
16. Net Results		2,127,339,612

Report on Cash Flows

for the year ended September 30, 1991

Bureau/Organizational Unit: **Principal Statements**
OMB Identification Code:
Basis Used:

Description		Total
1. Fund balance with Treasury and cash, beginning of period (PY SF 220)		46,992,419,807
2. Sources of funds:		
a. Increase in debt	-123,072	
b. Appropriations	96,066,923,907	
c. Revenue	11,394,356,342	
d. Sale of assets		
e. Increase in payables	-1,234,034,725	
f. Decrease in receivables and advances	2,183,795,275	
g. Other	-482,475,845	
h. Total		107,928,441,882
3. Application of funds:		
a. Operating expenses (SF 221)	96,188,317,103	
b. Less: Expenses not requiring outlays (SF 221)	-5,268,746,589	
c. Increase in investments	-66,471,824	
d. Increase in inventory	-2,088,495,886	
e. Purchase of property, plant and equipment	18,279,976,788	
f. Other	-123,393,47[illegible]	
g. Total		106,921,186,120
4. Fund balance with Treasury and cash, end of period (SF 220)		47,999,675,569

Report on Reconciliation to the Budget

for the year ended September 30, 1991

Bureau/Organizational Unit: **Principal Statements**
OMB Identification Code:
Basis Used:

Description	Total
1. Total operating expenses (SF 221)	96,188,317,103
2. Adjustments:	
Add:	
a. Capital expenditures	18,280,128,788
b. Increase(decrease) in inventories	-2,088,495,886
Deduct:	
a. Increase(decrease) in accounts payable	2,455,636,065
b. Accrued expenses not requiring outlays	5,268,746,589
3. Total gross disbursements	104,655,567,351
4. Less: Offsetting collections credited	-10,330,745,456
5. Net disbursements	94,324,821,895

Disbursements/Collections were reduced by $17,456,981,388.52 to reflect the effect of intra-agency eliminations. (See Footnote 2.)

NOTE 1: Summary of Significant Accounting Policies

A. Entity and Basis of Consolidation

Department of the Army is the largest component under the Department of Defense. The Army's principal mission involves preserving peace and security for the United States and its allies. These financial statements are based upon a consolidation of data by several systems at the accounts office (major command) level and at the departmental level by the Program, Budget, and Accounting System (PBAS). Due to delays encountered in upgrading reporting systems for subordinate commands, the departmental system will not achieve full compliance with prescribed general ledger standards before October 1, 1992. Consequently, general ledger account balances have been used in the financial statements only when they have proven to be accurate and reliable. The Consolidated Financial Statements have been prepared in accordance with the Department of Defense Accounting Manual (7220.9-M). This DoD guidance incorporates GAO's Title 2 requirements. Any deviations from Title 2 have been separately disclosed.

B. Recognition of Earnings and Financing Sources

The Army is financed primarily through appropriations provided by Congress for annual and multi-year purposes. The following Treasury accounts are used to fund, execute, and report on total financial activity for Army and Corps of Engineers (Civil Works).

1) General funds. This grouping contains the bulk of congressional appropriations, including operations, research and development, and investment/construction accounts. Mission (operations and pay) accounts represent those monies used for the payment of operating forces. These funds finance the functional and administrative support needed to operate and maintain Army installations. The Research, Development, Test & Evaluation (RDTE) facilities located throughout the world are operated and maintained by RDTE funds to perform ongoing test and evaluation as well as basic and applied research. Investment/construction accounts are used for specific purposes approved by and reportable to Congress. These accounts are used for the acquisition or construction of technology, property, and infrastructures.

2) Revolving funds. These accounts operate under the direction of 10 U.S.C. 2208. They are designed to provide an effective means of financing, budgeting, accounting for, and controlling inventory, as well as the costs of providing goods and services used to support both peacetime and wartime operations. Revolving funds support the operating and investment accounts by providing a coordinated focus, efficiencies of operations, and economies of scale. The Army operates four revolving funds (stock fund, industrial fund, conventional ammunition working capital fund, and a Corps of Engineers revolving fund). Revenue recognition varies by fund. Stock Fund activities recognize revenue at the point of sale. For industrial fund and Corps of Engineers revolving fund activities, revenue accrues at the point the service is completed or on a cost incurred basis. The ammunition fund recognizes revenues at the point of delivery.

The Army is financed primarily through appropriations provided by Congress for annual and multi-year purposes.

The Army Stock Fund (ASF) has both wholesale and retail divisions. Sales revenues are used to replenish inventory to meet future customer needs. It should operate on a break-even basis while maintaining a five-day cash standard as directed by Congress. The Stock Fund recorded an operating gain of $990 million for FY 91, attributable primarily to sales of war reserves and customer returns without credit for Desert Shield/Storm materiel.

The Army Industrial Fund (AIF) has four major activity groups (military traffic management, depot maintenance, logistics support activities, and arsenals) which provide products and services to customers. AIF operates on a buyer-seller concept. Costs (labor, material, other direct costs, production overhead expense, and general/administrative expense) are initially paid from working capital. Customers are billed based upon the terms of the reimbursable order (e.g., fixed cost or cost incurred). AIF recorded an operating gain of $145 million in FY 91.

As the single manager of conventional ammunition, the Army is responsible for procurement, production, storage, distribution, maintenance, and demilitarization of conventional ammunition for all services (on a reimbursable basis). In FY 91, the ammunition fund recorded an operating deficit of $16 million.

The revolving fund for the Corps of Engineers (COE) is used for the acquisition and maintenance of plant and equipment used in civil works functions that will ultimately be charged to other appropriations. The fund is reimbursed for the cost of equipment, facilities, and services furnished at a rate that includes overhead, depreciation, plant and equipment, and accrued leave.

3) Trust funds. These accounts are used to record the receipt and outlay of funds held in trust by the government for use in carrying out specific purposes or programs in accordance with the terms of a trust agreement or statute. Trust accounts include monies collected through gifts and bequests (as well as interest earned on the investments of some of these gifts) and assets held for particular purposes. The Army Revolving Trust Fund, Commissary Stores Surcharge Collections, is the most significant of the trust funds. Effective October 1, 1991, commissary sales functions were consolidated under DoD and will transfer to the new Defense Commissary Agency. As a result, FY 91 is the last year surcharge revenues from commissary sales will accrue to the Army.

Annual and multi-year congressional appropriations, when authorized, are supplemented by revenues generated by sales of goods or services through a reimbursable order process.

Civil Works trust funds include Inland Waterways Trust Fund (IWWTF) and Rivers and Harbors, Contributed Funds. Revenue for IWWTF is derived from taxes imposed on fuel in vessels engaged in commercial waterway transportation and is used for one half of the construction and rehabilitation costs of specified inland waterways projects. Administrative data for Inland Waterways Trust Fund reflects September 30, 1990 data. Fiscal year 1991 data was not available from the Department of the Treasury at the time this report was prepared. IWWTF funds transferred to the Corps of Engineers in FY 1991 was $148.5 million. Funds for Rivers and Harbors, Contributed Funds are derived from contributions by non-Federal interests for expenditures on improvements of rivers and harbors. This includes cash contributions by terms of agreements with non-Federal interests for study, design, construction and maintenance of authorized Federal projects as well as other non-federal contributions. Total contributions in FY 1991 were $121 million. Rivers and Harbors, Contributed Funds is an uninvested trust fund.

4) Special funds. These funds are comprised of receipt and expenditure accounts that can only be used in accordance with specific provisions of law. The Army manages several such funds: Wildlife Conservation Fund; Restoration, Rocky Mountain Arsenal; and the DoD Forest Products Reserve Account. The Corps of Engineers (Civil Works) manages several special funds including Payments to States-Flood Control Act of 1954; Special Recreation Use Fees; Hydraulic Mining in California-Debris Fund; and Maintenance and Operation of Dams and Other Improvements of Navigable Waters.

5) Deposit funds. These generally are used to hold assets that are awaiting legal determination or for which the Army acts as agent or custodian. Additionally, these accounts may be used for unidentified remittances. The Army expressly requires all check collections to pass under the immediate control of one of these deposit funds upon receipt, regardless of source, if the ultimate recipient is unknown. The Army maintains 24 deposit accounts and COE (Civil Works) maintains ten deposit accounts.

• Annual and multi-year congressional appropriations, when authorized, are supplemented by revenues generated by sales of goods or services through a reimbursable order process. This process allows the seller to increase funds available by the cost of the supplies and/or services ordered by the customer. For financial reporting purposes under accrual accounting, revenue is recognized when earned (i.e., when the customer receives supplies or services). The cost of goods sold or services provided is recognized when expenses are incurred. Funds received prior to delivery of the goods or services are treated as unearned revenue and recorded as a liability of the Army.

• Donations to the Army are recognized as a financial source upon acceptance of the donated asset, and a revenue is recorded for the value of the increase to the asset account.

•During FY 90 and 91, DoD increased Army's funds available, on an emergency basis, for Desert Shield/Storm prior to funds being provided by Congress, by invoking R.S. 3732, the Feed and Forage Act (P.L. 41 U.S.C. 11). This Act allows DoD to exceed congressionally issued funds if necessary to maintain the armed forces during military actions. Additional congressional funding was received prior to the close of FY 90 and 91 to cover costs incurred under authority of the Feed and Forage Act.

•Certain expenses, such as civilian and military annual leave earned but not taken, are not funded when accrued in appropriated funds. They are financed in the period in which payment is required. The unfunded liability is reported in the Statement of Financial Position, and the offset is a reduction to the equity balances.

C. Funds with U. S. Treasury

The Treasury maintains Army appropriations in separate accounts for recording warrants, receipts, and disbursements. During the fiscal year, Army also has the use of various suspense accounts to record collections/disbursements that have either been rejected during the edit phase of the reporting process or require additional processing (Deposits in Transit and Recertified Check transactions) before final disposition can be made. These accounts are aged and reviewed on a regular basis to ensure suspended transactions are cleared in a timely manner.

Prior to passage of P.L. 101-510 unobligated balances in expired, expiring or merged accounts were withdrawn by Treasury and not recorded on Army's books; the Treasury would restore funds to Army from the surplus (restoration) accounts as required. Basically, the new law extends the expired life of an appropriation by three years, and eliminates all merged accounts by the end of FY 93. Funds are no longer withdrawn by Treasury and therefore remain part of Army's assets during the funds' expired period. Cancellation of unobligated balances in Treasury restoration accounts and of all obligations which had resided in merged accounts for more than five years significantly reduced Army's assets. During FY 91, the Army cancelled $10.5 billion in unobligated merged account balances which were previously available to cover obligation adjustments. Additionally, $400 million of unliquidated obligations that had been in a merged status for at least 5 years were cancelled. Army requested that $484.5 million of the unobligated restoration balance be restored before cancellation to cover valid upward obligation adjustments, including foreign currency requirements. DoD approved restoration of $415.7 million. Some portion of the shortfall could require use of current unexpired accounts for obligation payment purposes.

While P.L. 101-510 provides for the cancellation of funds, it doesn't cancel any corresponding legal liability and imposes certain limitations. Controls are in place to ensure that disbursements for cancelled prior year obligations don't exceed the imposed limitations. These limitations state that the disbursement of funds for previously cancelled obligations does not exceed: 1) 1% of current funds; and 2) the value of original appropriation (for merged accounts, the value of the cancelled funds). The Army anticipates that approximately $310 million of current unexpired funds will be required to cover valid merged account obligations which have been cancelled.

Department of the Army acts as an agent for the Department of the Treasury for cash on hand. Therefore, cash in the accounts of Army officials is excluded from Army financial statements.

D. Fund Control

Program authority and funds are distributed to Army activities through an on-line, real-time system. Fund control at the performing activity is divided into installation segments. Reporting and report certification processes follow the same path as fund distribution, in reverse, with each successive level maintaining control and reviewing operating results. Statutory and administrative limitations on fund use are printed on system generated fund distribution documents to aid in preventing Anti-Deficiency Act violations (31 U.S.C. 1341a). Army reported only one anti-deficiency violation to DoD in FY 91.

Anti-Deficiency Act

Amount	Command/Activity	Cause
$11,200,000	AMC / Department of the Army Receipt, Issue, Storage and Support Activity	Minor Construction costs exceeded the $200,000 Operation & Maintenance, Army statutory funding limitation.

Other alleged violations have been reported to the Assistant Secretary of the Army (Financial Management) and are being reviewed.

E. Accounts Receivable

Accounts receivable are recognized upon delivery of the goods or services (recognition of earnings) and reduced upon receipt of payment.

As presented in the Consolidated Statement of Financial Position, accounts receivable include reimbursements receivable, out-of-service debts (amounts owed by former service members), contractor debt and unused travel tickets. Allowances for doubtful accounts are based upon analyses of collection experience. During FY 91, the Army wrote off approximately $50.5 million in uncollectable receivables. Of this amount, $36.3 million were for debts owed by former military members whose whereabouts are unknown or who are unable to pay. Mobilizing reserve units, many of whose members were unfamiliar with the pay and benefits of active duty military, resulted in a large amount of overpayments during Operation Desert Storm. These overpayments are identified when soldiers are separated from the active Army pay system. At the end of FY 91, there was a backlog of over 59,000 personnel in separation status. An average of 6,000 debts is being passed to the out-of-service debt system each month; the average individual debt is $400. There is a current moratorium on collecting debts stemming from the mobilization of personnel for Operation Desert Storm. A waiver of these debts (approximately $40 million) is possible, and would cause the FY 91 Military Personnel Appropriation to absorb the unplanned disbursements.

> ***Waiver of Desert Shield/Storm debts could cause the FY 91 military pay appropriation to absorb $40 million in unplanned disbursements.***

In accordance with P.L. 101-510, the Army transferred receivables of $386.5 thousand to miscellaneous receipts of the Treasury. Debts residing in this account aren't reported in the Army's Financial Statements. However, the Army remains responsible for ensuring collection. The Army assesses interest and administrative fees on all delinquent non-Federal receivables (i.e., those more than 30 days overdue).

GAO found over $328 million in negative unliquidated obligations on Army's books in September 1989 for one of the Army's major commands. These negative amounts represent erroneous accounting entries and overpayments to contractors resulting in an understatement of accounts payable. As of September 1991, the balance for that major command was $259 million, a $112 million increase over the balance reflected in FY 90 footnotes. The increase is attributed primarily to staffing cuts within that command, erroneous records processed by entities outside the Army's control, and changes in priorities due to Desert Shield/Storm. Forty-one million dollars of the September 1991 balance represents actual contractor overpayments. However, $8 million of this amount is in jeopardy of not being recouped due to contractor bankruptcy, litigation, and similar matters. The remaining $218 million represent accounting errors and processing delays. There is an additional $80 million of negative unliquidated obligation balances spread throughout the rest of the Army commands with an additional $5 million in contractor overpayments.

The noncurrent accounts receivable for general funds include $411.9 million for long-term water storage contracts at Corps of Engineers (Civil Works) reservoirs. The receivables are recorded as current in the year they become due.

F. Advances and Prepayments

Advances and prepayments are classified as assets in the Standard General Ledger and the Army's accounting subsystems. Accounting policy requires offset of these assets against recorded liabilities upon fulfillment of the contractual action which gave rise to them.

G. Inventories

Inventory is designated by DoD as the aggregate of tangible personal property items categorized as either consumable items or as depot level repairable items. Inventory items are either (a) held for sale to DoD users (or to other authorized customers including U.S. allies) in the ordinary course of Defense operations, (b) are in the process of repair or production for resale, or (c) are to be currently consumed directly or indirectly in the production of goods or services to be available for sale. Inventories are carried at standard prices (established by Army or Defense Logistics Agency) throughout the year, as required by DoD accounting directives. Generally, prices on inventory held for resale are based on the cost of the most recently acquired items plus appropriate surcharges.

Army Stock Fund (ASF) inventory (wholesale and retail) was revalued for these financial statements using DoD's latest acquisition cost inventory method. The ASF inventory values in the financial statements were derived by applying percentage adjustment factors to ending inventory balances to remove surcharges, reduce excess inventory to scrap value, and reduce "unserviceable" inventory to carcass value (i.e., the value of items which are still repairable). The total reduction as a result of this action was $9.7 billion. Total inventory value includes $2.474 billion held in the event of a military conflict (War Reserves).

The Corps of Engineers (Civil Works) does not maintain separate accounts for inventories. Generally, since supplies are purchased as needed, COE does not have material levels of items that would be considered inventory. Consequently, the items are expensed instead of capitalized at the time of purchase.

H. Property, Plant and Equipment

Capitalization rules are applied and used for all property, plant, and equipment in accordance with GAO's Title 2 criteria (i.e., $5,000 or more for an individual item with a useful life of two years or more). The Army also capitalizes the costs of additions, improvements, leasehold improvements, rehabilitations, alterations, betterments, and replacements that extend the service life of the asset. The costs of engineering changes and other modifications to existing weapon systems and equipment aren't capitalized unless the changes enhance the item's performance.

All fixed assets, including land held in public domain, are valued at acquisition cost. Acquisition cost includes such costs as purchase price; broker's commissions; fees for examining and recording the title; and other related costs of obtaining the property. When the acquisition cost cannot be determined, fair market value at the time of acquisition is used.

Military equipment which includes weapons systems is currently valued at standard cost which represents "latest acquisition" cost. Generally accepted accounting principles and the DoD Accounting Manual require that it be valued at actual historical cost. Accordingly, for FY 1991 a test to determine actual historical costs was made of four large weapons systems which comprised approximately 17 percent of the 30 September 1991 Military Equipment balance. The actual historical costs were obtained from the Selected Acquisition Reports (SAR) which contained the best data available from a single source. Each individual Weapons System Program Manager reports the SAR data based on installation accounting records. From the calculated actual historical costs obtained from the SARs of the four weapons systems reviewed, an adjusting entry was made to the 30 September 1991 balance. Use of costs obtained from the SAR was an interim, expeditious method. Not all costs are contained in the SAR. For example, some modification costs and simulator/training device costs are not contained in the SAR. Some GFM/GFE costs are not included, e.g., where those GFM/GFE costs are included in SARs of other systems. In addition, there are issues associated with standard data definition and data collection processes as related to accumulation of historical costs. Review of all these cost issues will be incorporated into the expanded sample being planned for the FY 1992 statements.

The Army Financial Statements include depreciation for the Army Industrial Fund and the Corps of Engineers Civil Works. This depreciation is computed on a straight line basis in conformance with DoD policy and GAO's Title 2 which does not specifically require the depreciation of general fund assets. Property ownership is recognized in the carrier (appropriated fund) account. According to current DFAS-IN legal interpretation, DoD accounts (including the new Defense Business Operations Fund) are prohibited from owning real property. Consequently, when Army depots were consolidated under DLA, the Army retained ownership of the property.

Previously, the Army treated ADP software development and acquisition costs as operating expenses. Using guidelines prescribed in GAO's Title 2, Army stations are now required to develop cumulative capitalization values for software with a cost in excess of $5,000 and a minimum remaining life of 2 years. Cumulative capitalization values (SF 220-line 7c) included software maintenance costs incurred during the current year when they extended the life of the software. Based on this information, the Army incorporated the cost of these assets into its departmental ledgers along with the corresponding adjustment to invested capital. Corps of Engineers (Civil Works) does not capitalize software costs.

The Army maintains accountability for equipment issued to operating forces in central logistics systems which are subsidiary to the General Ledger. Valuation of this equipment is consistent throughout the system. No gains or losses are recognized in the Statement of Operations for revaluation changes and/or the loss of equipment. However, the assets and related investment accounts do reflect both pricing and value changes based on a monthly update to the General Ledger.

As of September 30, 1991, the Army was committed to numerous operating leases and rental agreements. Generally, these leases and agreements were for the rental of equipment, space, and operating facilities.

> ***Base closures will result in $400 to $900 million in property being removed from Army's records.***

The Army owns substantially all of the facilities and real property used in its domestic operations, and overseas assets are capitalized in a manner similar to domestic assets. Most of the leases Army has entered into are believed to be operating rather than capital in nature. Consequently, analysis is underway to ensure proper classification of the account in the financial statements.

Construction-in-progress is updated as costs are incurred. An installation capitalizes the value of buildings when they are transferred to its control. The value is based on construction cost plus engineering, design, and inspection costs. Gains or losses from transfer of assets or liabilities between agencies aren't recognized, except when assets are transferred to the Base Realignment and Closure Account. This account is not allowed to accumulate gains or losses on disposal. Any gain or loss must be transferred back to the original/losing command. Base closures from the 1988 Base Realignment Commission (BRAC) could result in approximately $400 to $900 million in real property being removed from the Army's accounting records between FYs 93 and 95. We've specified a projected range because we cannot identify, at this level, the specific impact of partial base closures. Another projected $850 million could be removed as a result of the 1991 BRAC decisions.

The U.S. Army, Europe drawdown plan could affect military equipment accounts in the future. The plan calls for transfer of Conventional Armed Forces in Europe treaty limited weapons to U.S. allies. Several NATO allies have verbally committed to accept the excess treaty-limited equipment.

I. Other Assets

Acquired Collateral: Represents the value of collateral acquired upon mortgage default. The asset will be carried in the accounts as the amount of the mortgage underwritten by the Department of the Army plus any other unsettled, outstanding mortgages in place against the collateral. This account is restricted for use by the U.S. Corps of Engineers.

Other - Other assets: The "Other - Other Assets" account is primarily comprised of $4.2 billion in government property held by contractors and $1.082 billion in Inventory-Raw Materials and Supplies.

J. Accounts Payable

Accounts payable for goods and services are recognized based upon receipt of a receiving report providing notification of delivery of goods or services. In accordance with Army policy, fiscal stations record an obligation, accrual, and expense simultaneously when preparing obligation documents for travel, transportation, or for documents with small amounts (i.e., $1,000 or less).

Centrally managed allotments use the cash basis for accounting. Obligations are established monthly based on a combination of the disbursement values reported by installations compared to the budgeted value developed from trend analysis/projections prepared by Army budget officers. Centrally managed allotments are used when it is not cost effective or is cost prohibitive to issue funds to all possible disbursing offices, and there is an inability to project usage of the funds at that level. Some examples are permanent change of station travel for military personnel and long term training funds.

The Army owes interest to vendors if invoices aren't paid on time. For fiscal year 1991, the Army paid only $2.8 million in interest and penalties on 4.6 million vouchers totalling $17.1 billion.

K. Accrued Payroll and Benefits

All military and civilian payroll earned but not paid as of September 30, 1991 is accrued in the financial statements. Due to the small dollar values for all appropriations except OMA (2020), all accrued payroll was recorded as non-Federal. Nineteen percent of the OMA expenses were determined to be within the federal government and have been reflected as such in the financial statements. Accruals for military pay reflect $1.097 billion for undisbursed military pay and benefits for the month of September 1991.

L. Accrued Leave

Civilian annual leave and military leave are accrued as earned. The military pay system computes the balance for military leave at the end of the fiscal year based on current pay rates for the leave that is earned but not taken. The balance for civilian annual leave represents the value of the unused accrued leave hours reported as of September 30, 1991 as computed by installation civilian pay systems. This balance excludes the government's share of approximately $18 million of social security taxes that may be paid to the Social Security Administration when the employee departs government service. A majority of the leave liability that is reflected in the unfunded liability lines was incurred in prior years and carried forward to the current statements. This balance is understated because some installations omitted this reporting requirement. Sick and other types of leave are expensed as taken.

No current liability exists in the Army for sick leave; however, a future liability exists in the pension funds managed by the Office of Personnel Management (OPM) for those employees under the Civil Service Retirement System (CSRS). Unused sick leave is credited toward years of service when computing pension benefits.

M. Other Liabilities

The Army's FY 1991 financial statements (SF 220 - Line 7a) include $148 million of structures and facilities which are located overseas and have been obtained through various international treaties and agreements negotiated by Department of State. These assets under the control of Army are expected to be returned to the source from which acquired in "reasonably close to original condition." This liability is recognized in the SF 220 - Line 18(a), "Other Liabilities, Property Furnished by Others" account as shown below:

OTHER LIABILITIES - PROPERTY FURNISHED BY OTHERS:

	(Millions)
Property Furnished by Others (Foreign)	$148
less Army Stock Fund balance	$72*
SF 220 - Line 18(a) balance	$76

* During Desert Shield / Storm, requisitions at the Army National Inventory Control Points exceeded the withdrawal authorization limits established by Army Material Command for issues of non-reimbursable Depot Level Repairables. This created an abnormal balance in the Army Stock Fund "Property Furnished by Others" account.

Generally, treaty terms allow the Army continued investments in building and other facilities located on the overseas bases. These buildings and other facilities are capitalized as stipulated in Note 1(H).

Corps of Engineers (Civil Works) maintains an insurance reserve in the Revolving Fund ($44.2 million) for replacement of assets due to casualty loss or damage. The reserve is funded by a surcharge against the book value of assets.

N. Equity

The Army's equity consists of invested capital, cumulative results of operations, and unexpended appropriations. Invested capital, as presented in the Consolidated Statement of Financial Position, represents the value of the Army's capital assets at cost less any applicable depreciation and amortization.

Changes in invested capital are recorded when capital assets are acquired, constructed, or transferred without reimbursement. Decreases occur as capital assets are depreciated or consumed in operations.

Cumulative Results of Operations for revolving funds represent the excess of net revenues over expenses since fund inception, less returns to the Treasury.

Unexpended appropriations represent amounts of funding authority which have not been obligated, rescinded or withheld pending withdrawal, and amounts obligated that have not been paid.

O. Operating/Program Expenses, Funded

The account represents cumulative fiscal year-to-date expenses reported in Army's General Ledger for the subsidiary accounts identified. A schedule of funded operating/program expenses by subsidiary account is presented on the following page. Corps of Engineers (Civil Works) is displayed by fund type because their expenses are not reported through Army's General Ledger.

Operating Program/Expenses Funded

Account	(Millions)
Personnel Services and Benefits	$ 2,443
Civ Pay, FT Perm and Mil Pay	38,982
Transportation of Persons	1,459
Travel/Transportation of Things	2,530
Rents, Communications and Utilities	1,699
Printing/Reproduction	59
Other Contract Services	24,843
Supplies/Materials	8,785
Equipment	236
Grants, Subsidies and Contributions	18
Insurance Claims and Indemnities	2
Applied Overhead	(1,326)
Total Military	$ 79,730
Corps of Engineers - Civil	
General Fund	$ 2,544
Special Fund	14
Deposit Fund	2
Trust Fund	29
Total Civil	$ 2,589
Total Military/Civil	$ 82,319
Summary - GAO Adjustment	24
Total Operating/Program Expenses, Funded	$ 82,343

P. Other Funded Expenses

Inventory Losses: The "Inventory Losses" found on SF 221-line 10b, resulted from a cancelled project. The inventory control point was unable to give full credit to the Army Industrial Fund when the materials were returned because of either obsolescence or price and surcharge adjustments.

Other Losses: The abnormal balance on SF 221-line 10d, is due to the Army Stock Fund's accounting treatment of Depot Level Repairables issued without reimbursement during Desert Shield/Storm.

NOTE 2: Accounting for Inter/Intra-government Activities

The Department of the Army, as an agency of the DoD and the federal government, interacts with and is dependent on the financial activities of the federal government as a whole. Therefore, these Financial Statements do not reflect the results of all financial decisions applicable to the Army which would otherwise be recorded if the agency was a stand-alone entity.

The Army's proportionate share of public debt and related expenses of the federal government are not included in the Financial Statements. Debt incurred by the federal government and the related interest are not apportioned to federal agencies. Consequently, the Army's Financial Statements do not reflect any portion of the public debt or interest thereon, nor do the Statements reflect the source of public financing (e.g. debt issuance, tax revenues).

All identifiable inter/intra-agency transactions and balances have been eliminated in the Principle Statements through the use of data elements resident in the departmental accounting system. No eliminations are reflected in the Combining Statements for inter-agency transactions.

The following table shows the amount (in millions) of eliminated intra-agency balances by account and fund type.

Fund Type	Accts Rec/ Accts Pay	Rev/ Exp	Unearned Rev/ Advances	Disb/ Coll
Commercial	$226.	$9,796.	-	$9,570.
Revolving	$206.	$1,723.	$1,633.	$3,151.
Trust	$1.	$1.	-	-
Other	$798.	$5,486.	$48.	$4,736.
Cemeterial	-	-	-	-
Total	$1,231.	$17,006.	$1,681.	$17,457.

NOTE 3: Foreign Sales

In FY 91, the Army sold assets to foreign governments under the provisions of the Arms Export Control Act of 1976. The Act authorizes DoD to sell defense articles and services to foreign countries, generally at no profit or loss to the U. S. Government. Customers are required to make payments in advance to a trust fund maintained by the Treasury. The trust fund is used to reimburse the DoD components for the cost of administering and executing sales. The Army processed $6.165 billion representing sales of assets and services under the Foreign Military Sales Program in FY 91.

NOTE 4: Desert Shield/Storm

The Army's FY 90 and 91 cost of the operation includes obligations of nearly $20 billion, assistance in kind of $3.6 billion, and accrued costs of $2.6 billion for a combined incremental cost of $26.2 billion. The costs are based on reports provided by the DoD Comptroller to the Army Budget Office. Major end item losses as of September 30, 1991 amounted to

$412.9 million. Losses were reported regardless of whether replacement is currently anticipated. Costs were based on current procurement or last procurement inflated to FY 91 values. Army received $19.2 billion from the Defense Cooperation Account to offset Desert Shield/Storm costs.

NOTE 5: Obligations and Contingencies

The Army is obligated to pay for undelivered orders (goods and services which have been ordered but not yet received) as of September 30, 1991. Aggregate undelivered orders amounted to $43.3 billion at fiscal year-end. This includes $843 million for the Corps of Engineers (Civil Works), $178 million of which is for the Civil Works Revolving Fund. Undelivered orders are not recorded in the Civil Works Revolving Fund but are provided as a footnote by Corps accounting offices. Equity values in the Financial Statements are reduced by the value of unfilled orders (reimbursable orders received for which supplies or services have not been delivered to the ordering agency).

The Army is a party to various legal and administrative claims brought against it. Most are tort claims resulting from aircraft and vehicle accidents, medical malpractice, contract disputes, and property and environmental damages resulting from Army activities.

The Army is a party to various legal and administrative claims brought against it.

The accounts receivable value excludes estimated third party claims for carrier recovery, medical care, and property damage. The following chart was provided by the U. S. Army Claims Service.

Report of Claims Assessed and Collected[1]

	($ millions)
Estimated Carrier Recovery Assessed (July-June 91)	$ 16.736
Estimated Carrier Recovery Collected (July--June 91)	$9.178
Estimated Medical Care Assessed (July—June 91)	$2.602
Estimated Medical Care Collected (July—June 91)	$1.325
Estimated Property Damage Assessed (FY 91)	$21.940
Estimated Property Damage Collected (FY 91)	$13.428

[1]Amounts include collections of previously assessed claims. The reported figures are estimates and subject to future adjustment.

An updated DoD estimate indicates that the projected funding needed to complete the Installation Restoration Program for the Army is $11.6 billion. This is a long term contingent liability for the Army.

The Army recognized a contingent liability at departmental level to cover claims stemming from a procedural error in recording night differential pay due civilian employees. The error caused an underpayment of approximately $6 million. To date, Army has paid $500,000 in validated claims. Because of the low demand on these funds during FY 91, the obligation will be reviewed along with the adequacy of the error notification provided potential claimants.

A significant amount of the Army's overseas operations is conducted in the currency of the host nation. However, the obligation amounts representing this activity are in U.S. dollars, and the exchange rate of the U.S. dollar can affect the cost of liquidating these obligations. The impact of this process is displayed as a contingent liability against the following appropriations: Operations and Maintenance, Army; Military Construction; Family Housing Operations and Maintenance; and Family Housing Construction. The current estimate of this liability as of September 30, 1991 is $533 million. The Army recognizes the cost of these transactions during the period in which they occur. Current unexpired funds will be used for any requirements in excess of this amount.

A $156.5 million contingent liability exists for Department of Labor Workers' Compensation payments for current and former Army employees. The liability covers the periods July 1, 1989 through June 30, 1991. Payment will be made from the FY 92 and FY 93 appropriations, as applicable.

Other contingent liabilities not recorded include Army's portion of the Rocky Mountain Arsenal environmental restoration project ($1.5 billion) and $1 million in contingent liabilities for uncleared deposits in transit that have not been charged back to Army.

As of September 30, 1991, the Army was a party to 771 appeals (246 of which involve the Corps of Engineers (COE)) pending before the Armed Services Board of Contract Appeals (ASBCA). The appeals involve an estimated $604.6 million ($527 non-COE, $77.6 COE). None of the claims involves an amount in excess of $100 million. Approximately 85% of the dollars in dispute involve contractor claims against the government; the other 15% involve government claims against contractors. We have no means of estimating the eventual or probable dollar recovery on pending claims. The majority of claims normally involve negotiated settlements with partial payment of the claim. The average length of time it takes to process an ASBCA case is about two years (from date of filing). We estimate that cases pending at the end of FY91 will be resolved within an average of 18 months. There were 563 (406 non-COE, 157 COE) ASBCA appeals actually docketed in FY91, and 79 appeals (46 non-COE, 33 COE) were successfully defended (i.e., found fully in the government's favor with no partial settlement). The dollar amount of these successfully defended appeals in FY91 was $18.1 million ($16.6 non-COE, $1.5 COE). Unadjudicated claims in the amount of $379 million were outstanding as of September 30, 1991 for the Corps of Engineers (Civil Works).

Army payments during FY 91 for awards, compromises, and settlements resulting from legal actions amounted to $4.445 million. The Department of Justice (DOJ) Judgement Fund was cited for $25.413 million. The Army's Judge Advocate General estimates that payments arising from legal and administrative claims outstanding at September 30, 1991, will approximate $700 thousand in FY 92 for Army funds, and $28.345 million for the DOJ Judgement Fund.

In the opinion of Army management and its legal counsel, the ultimate resolution of legal actions still pending will not materially affect the agency's operations or financial position. Accordingly, the Army doesn't recognize a contingent liability for these actions in its Consolidated Statement of Financial Position. The chart below provides a detailed breakout of judgements and settlements for FY 91 and 92.

JUDGEMENTS & SETTLEMENTS

Subject of Litigation:	FY 91 [1]	FY 92 [2]	Paying Agency:
Medical Malpractice	$13,947,500.	$15,000,000.	DOJ Judgment Fund
Vehicle Accidents	1,785,994.	2,000,000.	DOJ Judgment Fund
Other Tort Cases	4,044,014.	5,000,000.	DOJ Judgment Fund
Military Personnel Cases	378,899.	500,000.	DOJ Judgment Fund
Civilian Personnel Cases	125,000.	200,000.	DOJ Judgment Fund
Transportation Claims	132,000.	645,000.	DOJ Judgment Fund
Environmental Cases	$5,000,000.	$5,000,000.	DOJ Judgment Fund
TOTAL:	**$25,413,407.**	**$28,345,000.**	**DOJ Judgment Fund**
Contract Dispute Cases in U.S. Claims Court or District Court	$466,544.	$550,000.	Army Funds
Privacy/Freedom of Information Act	164,000.	$150,000.	Army Funds
Lease Dispute	12,674.		Army Funds
Student Loan Case	2,200.		Army Funds
Environmental Case	$3,700,000.		Army Materiel Command
TOTAL:	**$4,345,418.**	**$700,000.**	**Army Funds**
Environmental Cases	$1,000,000.	$5,000,000.	Army Defense Environmental Restoration Account

1 Represents disbursements made during FY 91

2 Represents estimated disbursements to be made during FY 92

NOTE 6: Pensions and Retirement Expenses

The Army's civilian employees participate in the Civil Service Retirement System (CSRS) and Federal Employees' Retirement System (FERS); military personnel are covered by the Military Retirement System (MRS). Personnel covered by FERS and MRS are also covered by Social Security, and all personnel are subject to mandatory Medicare contributions. These Financial Statements don't reflect MRS, CSRS, or FERS assets, accumulated plan benefits, or unfunded liabilities applicable to Army employees. Reporting such amounts is the responsibility of OPM for CSRS and FERS, and the DoD for MRS.

In FY 91, the Army contributed the following amounts to retirement plans and Social Security.

CSRS	$	418.8 million
FERS		371.1 million
MRS		6,694.0 million
Social Security		362.1 million
Total	$	7,846.0 million

Contributions of $365.3 million were made to the FERS Thrift Savings Plan during FY 91.

NOTE 7: Changes in Accounting Methods

The Army did not report inventory for appropriated (non-revolving) funds in prior years. Army policy required expensing all operating inventories for consumer appropriations at the time of purchase. For FY 91, Army is reporting on hand procurement and RDTE funded items, obtained to support procurement funded DoD systems, as "Other Assets." The Army previously reported this hardware as Military Equipment subject to depreciation. Since these items aren't currently in use, depreciation should not be applied. Reclassifying this equipment as Other Assets on the Balance Sheet allows the Army to recognize these (otherwise depreciable) assets without accumulating depreciation until the items are put in use.

Secondary inventory items (spare parts) were previously sold from the procurement accounts. These items were transferred to the FY 91 ASF account at no charge. Until March 1992, the Defense Business Operations Fund will issue these items free of charge to Army installations. Defense Business Operations Fund replaces the ASF as the revolving fund activity responsible for providing logistics support, effective October 1, 1991.

In previous years, a prepayment to a contractor or a progress payment for an inventory item was recorded as an increase to inventory. In FY 91, all progress payments are recorded under Prepaid Assets, in accordance with revised DoD policy. The specific policy changes with regard to inventory are listed on the following page.

- Procurement/RDTE (investment accounts) assets are not inventory or equipment, but are recorded as "Other Assets." Included in these values are:

• •Work-in-Process GFM	$2,192 million
• •Construction-in-Process GFM	$4,318 million
• •Equipment with Contractors	$3,381 million

- ASF Inventory revalued in accordance with guidance from OSD ($9.7 billion decrease in recorded value).

Effective October 1, 1991, assets, liabilities and equity of the ASF, AIF and the commissary trust fund were transferred to the Defense Business Operations Fund; (See Overview for additional information.)

NOTE 8: Supplemental Information

- These financial statements don't reflect the resources of the Army's Morale, Welfare, and Recreation (MWR) programs or the Army Air Force Exchange Service (AAFES). The latter prepares separate financial statements and is audited by an independent certified public accounting firm. The MWR programs and AAFES receive direct and indirect appropriated fund support from the Army and generate their own non-appropriated funds from user fees or the sale of goods and services. The Army and DoD receive financial reports on MWR programs, and the programs are subject to audit by AAA, the DoDIG, and GAO. Due to different reporting cycles, non-appropriated fund MWR data won't be available until the end of December 1991. Therefore, MWR data aren't incorporated in these footnotes. The chart on the following page displays a partial balance sheet for the Army/Air Force Exchange Service (AAFES) organization.

Army Air Force Exchange Service ($ millions)	
Assets at 7/28/91	$ 2,964.0
Liabilities at 7/28/91	$ 904.5
Net Worth at 7/28/91	$ 2,059.5
Liabilities & Net Worth	$ 2,964.0
Rev for year ended 9/30/91	$ 4,970.0

• Corps of Engineers - Civil Works did not always classify and capitalize property plant and equipment transactions in accordance with Federal accounting standards. Actions are ongoing to ensure the following transactions are properly recorded:

• Design and engineering costs are recorded as completed construction costs.

• All completed project costs are properly classified.

• Personal property is consistently capitalized.

• The following adjustments have been included in the principal statements based on observations by the General Accounting Office (GAO). These adjustments were statistically derived by the GAO based on their audit. Since GAO based these adjustments on statistical samples, there is no supporting documentation to warrant adjusting installation level accounting records. Therefore, these adjustments are included solely in the principal statements.

Report on Financial Position:

Inventories, Operating Consumables	$ 8,846,465
Property, Plant & Equipment,	
Structures, Facilities, &	
Leasehold Improvements	-167,424,869
Military Equipment	-1,448,725,193
Land	-3,139,743
Accrued Unfunded A/L	656,652,410
Invested Capital	953,790,930

Report on Operations:

Appropriated Capital Used	$ 656,652,410
Unfunded Expenses	-656,652,410

• The following additional adjustments were included in the principal statements based on actual physical observations by the GAO. Sufficient supporting documentation was not available to adjust the various funds presented in the combining statements. Therefore, all GAO adjustments were only included in the principal statements.

Report on Financial Position:

Accounts Receivable:	
Federal, Current	10,748,891
Public, Current	-369,624
Public, Noncurrent	476,404,400
Less: Allowances	-50,000
Inventories:	
Operating Consumables	-2,566,464,258
Product or Service	1,342,845,177
Loans Receivable:	
Public, Noncurrent	550,000
Prop, Plant & Equipment,	
Structures, Facilities &	
Leasehold Improvements	4,080,335,962
Military Equipment	17,143,744,784
Equipment	-8,572,482
Const-in-Prog	-889,007,762
Land	86,583,696
Allowances	-6,783,095
Other Assets:	
Ammunition	25,207,141,000
Other	-20,446,206,770
Accounts Payable:	
Federal	-10,044
Public	-54,256,501
Accrued Pay & Benefits	689,055
Accrued Unfunded A/L	-1,537,963
Unearned Revenue(Advs):	
Federal	-7,900,016
Other Liabilities:	
Prop Furnished by Others	7,157
Unearned Income	-481,756,015
Invested Capital	-23,886,135,591

Report on Operations:

Appropriated Capital Used	-14,504,093
Revenue:	
Federal	-11,684,926
Public	356,034

Report on Operations (Continued)

Other:	
Other	-26,904
Operating/Prog Exp, Funded	24,321,926
Unfunded Expenses	1,537,963

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