Defense Logistics Agency

Annual Financial Report

Fiscal Year 2008

(Unaudited)

THE WARFIGHTER'S LOGISTICS COMBAT SUPPORT AGENCY

DEFENSE LOGISTICS AGENCY
DEFENSE WORKING CAPITAL FUND and GENERAL FUND
Fiscal Year 2008 Annual Financial Report

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Message from the Director
October 2008

Since becoming the Director of the Defense Logistics Agency (DLA) in the fall of 2006, a primary focus has been alignment of DLA's operations and strategy with the needs of our Nation's warfighters. We made great strides in both extending our Enterprise forward to the point of demand and partnering with America's industrial base to seamlessly flow supplies and materiel directly to the Military Service customers.

While many of our customers are satisfied with the support we provide, they continually look to us to increase and leverage our capabilities so they can focus their resources on warfighting readiness and transformational efforts. Base Closure and Realignment 2005 reconfigures the supply, storage and distribution infrastructure under DLA as a single integrated provider. This realignment will go a long way toward meeting that expectation. Furthermore, our creative, energetic, and knowledgeable forward deployed civilian and military personnel will ensure that our supplier network is coherently linked to our warfighting customers' demand.

Even as we execute as the Department's logistics combat support Agency, we still have many obstacles that preclude the audit of our financial statements. Our stewardship of the resources entrusted to our care by the American people remains a top priority. DLA's leadership is committed to developing and implementing automated systems, business processes, and management controls that will comply with federal financial management requirements. By executing the DLA Financial Improvement and Audit Readiness plan, a transformational roadmap, we will address our deficiencies and achieve those commitments in a cost efficient and operationally effective manner.

The Nation's men and women who volunteer to serve in uniform require and deserve the finest support, supplies, and materiel. There is no other private or governmental organization in existence that can do what DLA does, and the dedication of our workforce ensures that America's warfighters receive what they rightfully deserve as military volunteers in a free republic. I am honored and proud to lead the DLA team to this end.

R. T. Dail

ROBERT T. DAIL
Lieutenant General, USA
Director

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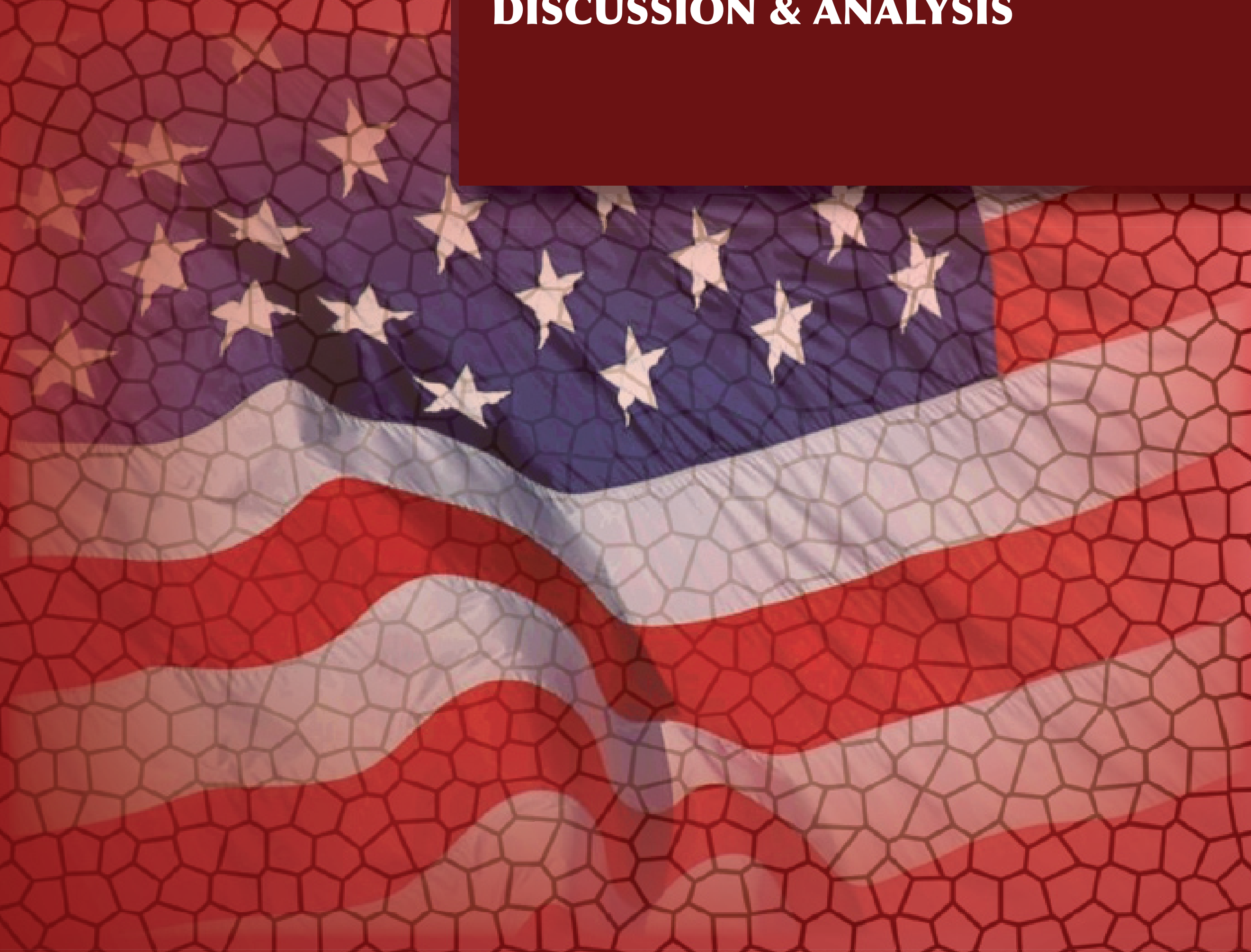
DEFENSE LOGISTICS AGENCY

CONSOLIDATED MANAGEMENT'S DISCUSSION & ANALYSIS



DESCRIPTION OF THE DEFENSE LOGISTICS AGENCY

The Defense Logistics Agency (DLA) is the Logistics Combat Support Agency of the Department of Defense (DoD) and reports to the Under Secretary of Defense for Acquisition, Technology and Logistics through the Deputy Under Secretary of Defense for Logistics and Materiel Readiness. DLA's primary mission is to provide best value logistics solutions to meet the needs of America's Armed Forces around-the-clock and around-the-world in times of peace, national emergency, and war. Execution of the United States (U.S.) national defense strategy depends on DLA support to feed, clothe, fuel, medicate and treat, and sustain our troops and many of our nation's allies. DLA supports DoD objectives and missions with involvement in the full range of military operations-from participation with multi-national forces engaged in large-scale combat operations, peacekeeping efforts, emergency support, and humanitarian assistance to the global war on terrorism.

DLA manages more than 5.2 million items and disseminates logistics cataloging information for most items managed by DLA that support the DoD, other Federal Agencies, and U.S. international partners. Among the materiel we manage are fuel and repair parts for weapon systems as well as food, clothing, and medical supplies needed to deploy and sustain U.S. Forces. DLA receives, issues, and distributes these items through a network of depots and commercial supplier relationships; and through the reutilization and marketing service, we manage DoD programs to reutilize, transfer, donate, or sell surplus and excess materiel and dispose of hazardous materiel. DLA also administers the DoD document automation and production services.

DLA missions have evolved and grown over the past four decades to an extent that if our forces fight with it, wear it, eat it, or burn it as fuel, we probably buy it; warehouse and distribute it; or arrange for its reuse, sale, or disposal after the owner no longer needs it.

AGENCY STRATEGIC GOALS AND STRATEGIES

DLA has a pivotal role in delivering the joint logistics capability that optimizes warfighter support; and the ability to deliver the right logistics solution to the warfighters on every transaction requires supply chain excellence. Consequently, the U.S. military's ability to generate and sustain global combat readiness depends on a supply chain that seamlessly moves DLA-managed materiel from the nation's industrial base to its ultimate user.

To fulfill this mission, DLA will build on its wholesaler excellence. We will leverage the operational efficiencies generated by the Agency's transformational initiatives, such as the efforts to implement the Base Realignment and Closure (BRAC) 2005 Supply and Storage recommendations and the recently completed Enterprise Business System (EBS) – an end-to-end Enterprise Resource Planning capability managing all of DLA's hardware and troop support items. NOTE: In prior annual financial reports, EBS was referred to as the Business System Modernization (BSM) program.

The Defense Logistics Agency FY 07 – FY 13 Strategic Plan, promulgated in February 2007, contains four strategic goals and clearly documents and commits DLA's resources and energy to the realization of three new strategic thrusts; each one is designed to move DLA beyond its traditional wholesaler responsibilities. Those strategic thrusts will:

1) Extend Enterprise resources to geographically align with supported activities and capitalize on best value opportunities that improve warfighter readiness.

2) Connect warfighter demand with supply by transforming the Department's demand planning capabilities and the processing of demand signals throughout the supply chain.

3) Deliver supply chain excellence by forging end-to-end logistics solutions that strike the targeted balance among effectiveness, agility, reliability, speed, visibility, and cost.

DLA's Mission:
To Provide Best Value Integrated Logistics Solutions to
America's Armed Forces and Other Designated Customers…
in Peace and in War…Around the Clock, Around the World

DLA's Vision:
Extending the Enterprise Forward to Meet the Needs of the Warfighter
DLA…Supporting Mission Success!

DLA's four strategic goals:

Strategic Goals:

- Maximize warfighter potential by extending the Enterprise to provide worldwide response and integrated, best value supplies and services consistently to our customers.
- Continuously improve DLA performance through the development of better processes and business arrangements that reduce cost, increase logistics capabilities, and link customer demands with our supply chains.
- Ensure a diverse, enabled, empowered, and motivated workforce that delivers and sustains supply chain excellence.
- Manage DLA resources for best customer value.

DLA will achieve these strategic goals through a series of integrated enterprise-wide strategies.

Goal 1. Maximize warfighter potential by *extending the Enterprise* to provide worldwide response and integrated, best value supplies and services consistently to our customers.

Strategy 1.1. Extend competencies and capabilities closer to the warfighters.

Strategy 1.2. Actively engage the warfighters to better understand their needs and meet their requirements.

Goal 2. Continuously improve DLA performance through the development of better processes and business arrangements that reduce cost, increase logistics capabilities, and *link customer demands with our supply chains.*

Strategy 2.1. Align demand and supply chain capabilities within the supply chain management model to better support the warfighters and their weapon systems.

Strategy 2.2. Leverage industry capabilities to provide world-class support to the warfighter at the lowest possible cost.

Strategy 2.3. Adopt, institutionalize, and continuously improve best business practices to improve quality and speed and to reduce cycle time and costs, while maintaining the integrity of the procurement process.

Strategy 2.4. Achieve world-class supply chain performance, completing DLA's transition from wholesale to end-to-end supply chain management excellence.

Strategy 2.5. Design, implement, and sustain a best value Enterprise Information Technology (IT) environment.

Goal 3. Ensure a diverse, enabled, empowered, and motivated workforce that delivers and sustains *supply chain excellence.*

Strategy 3.1. Acquire, develop, and retain, world-class supply chain expertise through a comprehensive talent management program.

Strategy 3.2. Attain and sustain a corporate culture that meets the needs of the warfighter through logistics excellence.

Strategy 3.3. Provide a quality work environment that optimizes employee performance.

Goal 4. Manage DLA resources for best customer value.

Strategy 4.1. Resource DLA's operational strategies.

Strategy 4.2. Minimize total supply chain costs.

Strategy 4.3. Demonstrate stewardship and foster stakeholder trust.

For any enterprise of DLA's size and scope, transformation and organizational evolution are complex processes that require an immense expenditure of capital, energy, and effort by all involved. In order to mitigate these challenges while maintaining its focus on its core missions, DLA organized its efforts into 14 transformational initiatives that support the three overarching strategic thrusts. The strategic thrusts provide the initiatives with a coherent focus, ensuring that individual initiatives do not lose sight of the strategic picture even as they remain fixed upon their unique missions. The transformational initiatives are individual programs for executing enterprise change: the quality of its services, the scope of its mission, and the efficiency with which it operates to meet the needs of the warfighter while providing the best value for the taxpayer. DLA's strategic thrusts and transformation initiatives are identified and summarized below:

Extend the Enterprise

- **Customer Facing** is a multi-phase effort to co-locate DLA personnel and Agency capabilities with the Military Services and Combatant Commanders (COCOMs). This initiative is delivering on DLA's strategy to provide DLA's customers with direct access to the Agency's competencies and capabilities.

- **Joint Regional Inventory Materiel Management (JRIMM)** is designed to improve warfighter support by: 1) establishing a single warehousing/distribution hub in each region; 2) minimizing all other storage sites within a region; 3) eliminating duplicate inventories; 4) maximizing utilization of the DLA Strategic Distribution Platforms (SDP); 5) reducing the number of times that materiel is handled; and 6) consolidating regional transportation management.

- **National Inventory Management Strategy (NIMS)** is an initiative that streamlines and improves consumable item management by affording the Military Services the opportunity to eliminate their unnecessary inventory investment in DLA-managed parts. This allows the merger of DLA wholesale and Military Service retail inventories into a single national inventory whose total cost is less than the sum of the individual stockpiles.

- **Global Stock Positioning (GSP)** is the strategy to position materiel around the globe in advance of customer requirements. It is designed to appropriately balance materiel availability with investment, storage, and distribution costs.

- **Forward Buying** is a global DLA capability to bring the contracting point of engagement closer to the customer - whereby buyers are deployed at the customers' sites to support customers' emergency and spot buys. Except for the Energy commodity, these forward buyers are authorized to procure DLA managed items regardless of supply chain or commodity; and they will also offer contracting support on three distinct levels - strategic, intermediate, and tactical. A forward buyer's performance is tracked the same as a supply chain buyer's performance at the home base.

Connect Warfighter Demand with Supply

- **Supplier Relationship Management (SRM)** is an initiative to build collaborative alliances with key suppliers in order to ensure materiel availability, quality, and value for those DLA-managed items vital to warfighter support. SRM also provides the capability to evaluate and manage supplier performance. Other long-term benefits of SRM include: 1) reduced vendor delivery times; 2) inventory savings; 3) collaborative communication between DLA, its customers, and suppliers; and 4) leveraged buying power for DoD.

- **Industrial Product-Support Vendor (IPV)**, formerly known as Integrated Prime Vendor, provides integrated supply chain management and logistics support of expendable items (i.e., consumable spare parts and industrial hardware) to support the customers' maintenance, repair, and overhaul operations. IPV is an initiative to migrate the management and requisitioning of consumable spare parts – industrial hardware, such as nuts, bolts, screws, and o-rings, used at Military Service maintenance facilities, from individual Service-managed programs to contractor-provided support. These parts are stored in bins at or near the point of use - at the industrial maintenance locations and on production lines. IPV is a push-pull concept whereby the vendor forecasts requirements and pushes the parts (bench stock) into the bins, and the customer pulls parts from the bins without a requisition. This strategy is aligned with DLA's strategic vision of linking supply and demand and extending the Enterprise forward to the customers' locations. In addition, the strategy provides command and control at the supply chain level (Aviation, Land, and Maritime); provides better program and acquisition accountability and visibility over each supply chain; aligns with the Enterprise Business System's (EBS) organizational structure; incorporates Supplier Relationship Management (SRM) involvement; includes headquarters oversight and support; and identifies alignment of future IPV support at the affected BRAC sites.

- **Integrated Data Environment (IDE)/Global Transportation Network (GTN) Convergence (IGC)** is a system-of-systems partnership initiative that will provide a single point of access to decision support related data and information within DLA and the United States Transportation Command (USTRANSCOM), and between DLA/USTRANSCOM and external systems. The convergence of these two programs will create a single face to DoD systems that require access to common and authoritative data, business standards, and information from DLA and USTRANSCOM.

- **DLA Fusion Center** is an initiative designed to enable our processes, empower our workforce, and facilitate our ability to measure and assess DLA's support to the warfighter. The DLA Fusion Center will combine people, processes, and technology in a net-centric distributed environment where operational and performance data from DLA and our mission partners will be integrated. Consequently, it will link supply availability to specific demand satisfaction (to specific customers, weapon systems, theaters, and items). It will provide access to information needed for decision making; help managers determine the importance and priority of issues; provide employees the ability to more quickly recognize and correct deficiencies; and provide analysts with tools needed to conduct root analysis and present alternatives for problem resolution.

- **Contract Administration** is a Post-Award activity that required renewed management attention. Consequently, DLA designated 2008 as "The Year of Contract Administration" whereby Contract Administration received equal emphasis with Pre-Award activities in terms of skill recognition, technology development, and performance metrics standardization. The Contract Administration Plan of Action and Milestones tracks 13 major action items to support this initiative.

- **Public/Private Competitions and High Performing Organizations (HPOs):** In FY 1998, DLA began competing with private industry for the distribution operations at its depots; the distribution functions at its reutilization and marketing offices; and the document automation and support functions at the Document Automation & Production Service (DAPS). During FY 2006 and FY 2007, DLA expanded this initiative by competing for its installation services support functions at two strategic distribution platforms. The goals of these competitions are to reduce operating costs either by reengineering existing business processes or by inserting the market forces of competition into these service functions while maintaining equal or better mission performance. Consequently, eighteen competitions were completed with DLA retaining in-house operations from nine competitions, while the other nine were contracted with private industry. In addition, both the DAPS Most Efficient Organization and the DLA Human Resources Center were designated by the Office of the Secretary of Defense as HPOs, where reengineering driven efficiencies have yielded savings comparable to those obtained through public-private competitions. Net savings for FY 1998 – 2008 from these eighteen competitions and two HPOs are $656 million and the projected additional net savings for FY 2009 – 2013 is about $600 million.

Deliver Supply Chain Excellence

- **Enterprise Business System (EBS)** is an on-going initiative to establish a DLA-wide Enterprise Resource Planning (ERP) environment that integrates nearly every Agency system and process into a single system that combines software programs for many diverse activities, such as materiel management, order fulfillment, and procurement. EBS is the key enabler for DLA's new business model, allowing the Agency to reengineer its business processes quickly and efficiently to improve overall effectiveness.

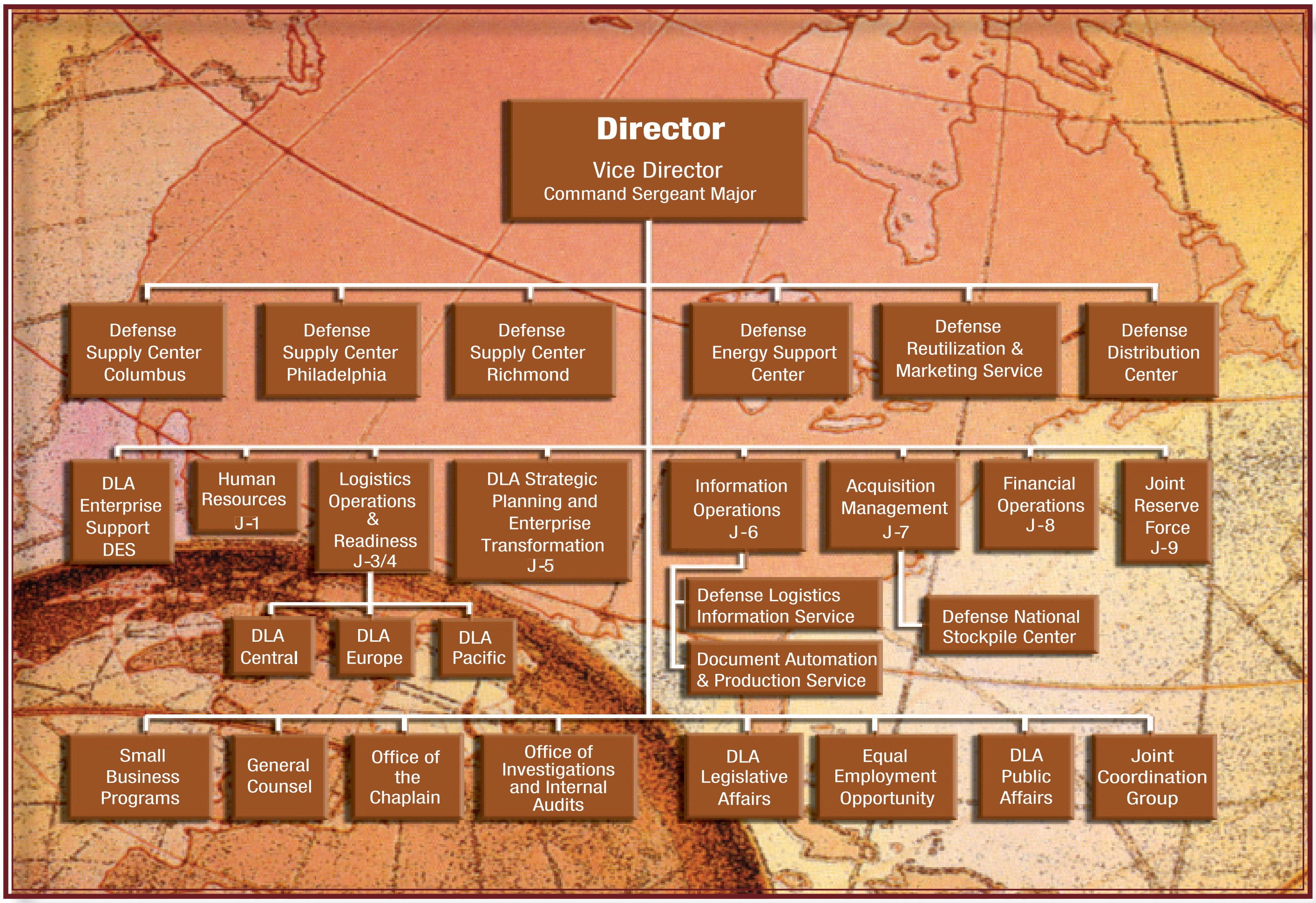
- **Common Food Management System (CFMS)** is a joint initiative between DLA and the Military Services to replace the Military Services' individual food management systems with a single, cross-service system that also allows service members to purchase food at any of the Military Services' dining facilities and will result in an end-to-end logistics solution for the worldwide DoD subsistence supply chain.

- **Reutilization Business Integration (RBI)**, formerly known as the Reutilization Modernization Program (RPM), is a DLA initiative to update its disposal business processes and replace the current Defense Reutilization and Marketing Service (DRMS) inventory management information technology (IT) systems. RBI will integrate the DLA Enterprise Business System (EBS), Distribution Standard System, and other Commercial-Off-the-Shelf (COTS) / Government Off-the-Shelf (GOTS) programs into a single IT system, while re-engineering the DRMS business processes.

ORGANIZATION

DLA maintains a global presence and accomplishes its mission with approximately 21,800 civilian personnel, 475 active duty personnel, and 735 reserve personnel. Despite our significant mission expansion over the past 47 years, the DLA workforce is now at the smallest level since 1963. Agency leaders are committed to the continuous assessment and transformation of the organizational culture, size, structure, and alignment through enterprise integration and partnering with the private sector. These efforts will enable the implementation of an enterprise business model that develops, deploys, and executes an improved set of corporate business processes and strategies. By organizing as a single, integrated business enterprise, DLA will be in a position to focus more efficiently and effectively on supporting the DoD's supply chain, enhancing the Armed Forces' readiness, and providing for the warfighter during contingency operations. DLA is proactive in serving warfighter mission needs and constantly meets face-to-face with customers to determine requirements and how best to fulfill them.

Our organizational structure is depicted below:



DLA's core functions are directed or supported by:

- **DLA Enterprise Support (DES)** provides Enterprise-wide agency policy, program, and world-wide operational support in Environment; Safety and Occupational Health; Installation Management; Public Safety; Management Internal Controls; Forms and Policy Management; Defense Travel System; and Morale, Welfare, and Recreation for DLA. DES directs the administration of policy for centralized management and support service functions of the Agency; serves as a key enabler of logistics and information operations initiatives; and serves as the principal support service advisor to the Director, DLA for the DES Headquarters and Site Missions and Functions.

- **Human Resources (J-1**) provides a full range of civilian human resources services for the DLA civilian and military workforce. J-1 conducts these services from its customer support offices located in Columbus, OH and New Cumberland, PA; a centralized military personnel support organization located at HQ DLA in Fort Belvoir, VA; and the DLA Training Center, which provides training support to DLA's workforce, located in Columbus, OH.

- **Logistics Operations and Readiness (J-3/4)** is responsible for the end-to-end supply chain management of DLA's eight supply chains, providing logistics and materiel process management policy, guidance, oversight, and monitoring of supply chain performance. J-3/4 is the principal strategic, operational, and tactical planner for DLA business operations, championing best business practices, and value-added logistics solutions for the warfighter. It serves as the Agency's focal point for customer support, engaging customers around the world, understanding their needs, and translating those needs back to the rest of DLA to maximize the Agency's logistics capability. J-3/4 oversees the daily operation of the DLA Logistics Field Activities and has primary responsibility for DLA's Research and Development (R&D) program. In collaboration with the Military Services, J-3/4 is responsible for operational planning and execution oversight for the DLA BRAC implementation.

- **Strategic Planning and Enterprise Transformation (J-5)** is DLA's strategy management office, responsible for Agency strategic planning, strategic communications, and overall management of enterprise transformation programs. The Director, J-5, communicates and executes the DLA Director's vision and senior leadership's strategies and objectives through the DLA Strategic Plan and the strategic measures portfolio. J-5 ensures horizontal integration and execution of strategy by sponsoring cross-functional processes and collaboration forums for enterprise decision-making. J-5 develops the strategy, concept of operations, and policy for agency-wide deployment of Continuous Process Improvement (CPI).

- **Information Operations (J-6)** is DLA's knowledge broker, and is responsible for providing comprehensive, best practice technological support to the DoD/DLA logistics community, resulting in the highest quality of information systems, efficient and economical computing, data management, electronic commerce, and telecommunication services. The Director, J-6, is responsible for the development and compliance of information technology (IT) policy; the development of IT plans and strategies; and the establishment of IT standards, processes, and measurements. The Director, J-6, also serves as the Agency's Chief Information Officer. Information Operations includes oversight of two field activities: the Defense Logistics Information Service and the Document Automation & Production Service.

- **Acquisition Management (J-7)**, DLA's full life-cycle contracting process owner, is responsible for planning, organizing, directing, and managing the procurement and contract administration functions for DLA acquisition in support of both internal operations and other supported activities. The Director, J-7, also serves as the Agency's Component Acquisition Executive. Acquisition Management includes oversight of the DLA Contracting Services Office Center of Excellence; the acquisition of major Information Technology (IT) systems/programs; and the oversight of the Defense National Stockpile Center (DNSC), which is a DLA field activity responsible for the administration and execution of the Department's Strategic and Critical Materials management policies and operations.

- **Financial Operations (J-8)** is led by the Agency's Chief Financial Officer and - as the financial management process owner - is the single spokesperson on financial management matters with external organizations. J-8 is responsible for designing, implementing, and executing standard financial processes across the Agency; determining financial services' resource requirements and performance targets; and establishing financial core competency requirements.

- **Joint Reserve Forces (JRF) (J-9)** supports DLA with trained, ready, and available reservists, of all reserve components, for contingency operations, peacetime contributory support, wartime surge support, and planning support. Further, J-9 advises the Director, DLA, on the planning and application of JRF support in accordance with DoD and Military Service readiness and activation policies.

DEFENSE WORKING CAPITAL FUND

The primary source of financing for DLA operations is its revolving fund, the Defense-wide Working Capital Fund (DWCF). By design the DWCF fosters a demand-driven cost-based relationship between customers (primarily the military operating forces) and suppliers (the DoD's business-driven support organizations). In this capacity, the operations of a DWCF activity are financed with the funded orders placed by its customers and satisfied by that activity. The expected outcome of this relationship is the effective and efficient delivery of goods and services. Since the financial structure of the DWCF allows for the identification of the cost to produce goods and services and subsequently set prices, the customer can use both pricing and delivery information in its decision-making process. This visibility also enables DLA managers to use performance measures to ensure that the activities operate consistent with budget execution targets, address program requirements, and foster productivity improvements. Each year, DLA either obtains or returns funds to the DWCF and other DoD appropriations.

During FY 2008, DLA executed a total budget program of almost $49.0 billion and finished the year with total assets valued at approximately $25.1 billion and liabilities of $3.8 billion from the Consolidated Balance Sheet and a net operating gain of almost $1.8 billion on program costs of approximately $41.0 billion and revenues of approximately $42.8 billion from the Consolidated Statement of Net Cost.

The following activity groups are financed by customer orders and direct appropriations through the DWCF:

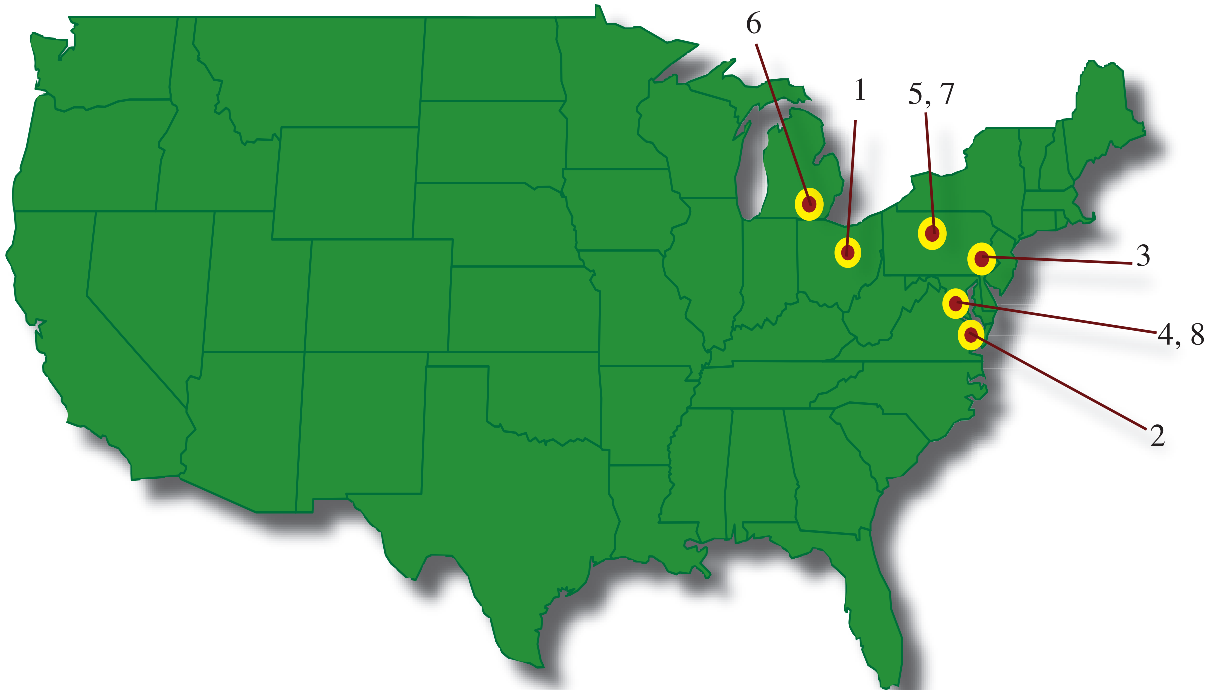
- **Supply Management:** The Supply Management activity group provides customer support through its management of logistics processes. This includes centralized management of logistics catalog information, energy, repair parts, operating supply items, food, pharmaceuticals, medical and surgical supplies, construction materiel and equipment, and clothing and textiles. Supply Management operates through three supply centers located in Columbus, OH; Richmond, VA; and Philadelphia, PA; and the Defense Energy Support Center located at Fort Belvoir, VA. The Supply Management activity group is the largest of our business areas. It makes up about 97% of the assets, 85% of the liabilities, and more than 94% of revenue and costs on the financial statements.

- **Distribution:** The Distribution activity group provides a single, unified materiel distribution system for DoD. In addition to its primary mission of receiving, storing, and issuing materiel worldwide, distribution depots perform other functions that include - but are not limited to - providing refrigerated storage, cylinder refurbishment, tent repair, medical unit assemblies, kitting, and set assembly or disassembly. The Distribution activity group is under the control of the Defense Distribution Center in New Cumberland, PA, and includes 26 subordinate distribution centers located throughout the United States, Europe, Southwest Asia, and the Pacific region.

- **Reutilization and Marketing:** The Reutilization and Marketing activity group supports and coordinates the disposal of excess and surplus property within DoD. Property not reutilized within DoD is available for transfer to other Federal agencies or for donation to authorized non-profit organizations, state governments, and local governments. Property not reused, transferred, or donated is either sold to the public on a competitive basis or disposed of in an environmentally safe manner. A critical part of the Reutilization and Marketing mission is to arrange for the worldwide disposal of hazardous waste in compliance with laws and regulations. The activity group accomplishes its mission from a headquarters in Battle Creek, MI, and 104 Defense Reutilization and Marketing Offices located on military installations around the world.

- **Document Automation & Production:** The Document Automation & Production activity group provides printing, duplicating, and document automation services within DoD. This mission encompasses the full range of automated services to include: document workflow conversion, electronic storage and output, and distribution of hard copy and digital information. The focus is on enabling customers to transition from hardcopy to digital/electronic-based document management. The worldwide mission of the activity group is managed through a headquarters in Mechanicsburg, PA, and a network of 185 production facilities.

DEFENSE LOGISTICS AGENCY ACTIVITY GROUP PRINCIPAL LOCATIONS



1. Defense Supply Center Columbus (DSCC)
2. Defense Supply Center Richmond (DSCR)
3. Defense Supply Center Philadelphia (DSCP)
4. Defense Energy Support Center (DESC)
5. Defense Distribution Center (DDC)
6. Defense Reutilization and Marketing Service (DRMS)
7. Document Automation & Production Service (DAPS)
8. Defense Logistics Agency Headquarters (DLA HQ)

GENERAL FUND AND TRANSACTION FUND

The General Fund is appropriated by Congress which also grants authority to the Office of the Secretary of Defense (OSD) and its components to obligate funds and pay for goods and services from their annual budgets. After funds are appropriated, apportioned by the Office of Management & Budget (OMB), and allotted by the OSD, the funds may be used to acquire goods and services. Both detail and summary level financial reports are available to provide the information necessary to make suitable management decisions pertaining to the allocation and use of the General Fund.

In FY 2008 DLA received approximately $699.4 million in General Funds direct appropriations, which accounted for less than 2% of DLA's total budget program. These appropriations included: Operation and Maintenance (O&M); Research, Development, Test and Evaluation (RDT&E); Military Construction (MILCON); Procurement, Family Housing Construction; Family Housing O&M; and Family Housing Improvement Fund.

The DLA O&M appropriation, approximately $402.2 million, funded two distinct groups: Other Logistics Services (OLS), $325.6 million, and Other Logistics Programs (OLP), $76.6 million. The OLS group included approximately 30 programs that were associated with the DLA logistics mission, such as: Price Comparability, Warstoppers, Hard Copy Map Function, Unemployment, Morale Welfare & Recreation, and Disaster Relief Blankets. In addition, OLS included programs added by either the DoD or Congress, such as Logistics Transformation. The OLP group consisted of approximately eight program offices for which DLA either provided administrative support or had program oversight, such as the Defense Property Accountability System and the Continuity of Operations Program.

The DLA RDT&E appropriation, $181.5 million, primarily supported two types of efforts: Advanced Technology Development (Logistics Research and Development

Technology Demonstration and Defense Microelectronics Equipment) and Operational System Development (Industrial Preparedness/Manufactured Technology and Logistics Support Activities).

The DLA MILCON appropriation, $105.4 million, funded major construction projects to replace, renovate, or build new facilities. The Army Corps of Engineers and Naval Facilities Engineering Command are the primary design and construction agents for this program.

The DLA Procurement appropriation, $8.9 million, funded the purchase of mission essential equipment, including passenger carrying motor vehicles, telecommunications equipment, automated data processing, and microelectronics equipment.

The DLA Family Housing O&M appropriation, $1.3 million, supported an inventory of 201 units located at the Defense Supply Center, Richmond, VA (31), the Distribution Depot Susquehanna, PA (140), and the Distribution Depot San Joaquin, CA (30). DLA's Family Housing program consisted of routine operation requirements including management and utility costs, carpet and linoleum replacement, painting, and replacement of appliances.

The DLA General Funds finished FY 2008 with total assets valued at approximately $1.0 billion and liabilities of approximately $300 million from the Consolidated Balance Sheet.

DLA also manages the National Defense Stockpile Transaction Fund, a separate $207 million revolving fund that strives to provide safe, secure, and environmentally sound stewardship for strategic and critical materiel in the National Defense Stockpile. The Transaction Fund is not accounted for in these financial statements, but is embedded in the DoD Agency-wide financial statements.

LIMITATIONS OF THE FINANCIAL STATEMENTS

The financial statements have been prepared to report the financial position and results of operations for DLA, pursuant to the requirements of Title 31, United States Code, Section 3515(b).

While the statements were prepared from the books and records of DLA in accordance with the formats prescribed by the Office of Management and Budget (OMB), 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.

To the extent possible, the financial statements were prepared in accordance with federal accounting standards. At times, the Department is unable to implement all elements of the standards due to financial management systems limitations. The Department continues to implement system improvements to address these limitations. There are other instances when the Department's application of the accounting standards differs from the auditor's application of the standards. In those situations, the DoD has reviewed the intent of the standard and applied it in a manner that management believes fulfills that intent. The statements should be read with the realization that they are for a component of the United States Government, a sovereign entity. One implication of this is that the liabilities cannot be liquidated without legislation that provides resources to do so.

SYSTEMS, CONTROLS, AND AUDIT READINESS

Internal controls are safeguards designed by management to provide reasonable assurance that the Agency will achieve its mission, goals, and objectives. They are designed to protect assets, ensure compliance with laws and regulations, operate efficiently and effectively, and maintain the accuracy of financial and business data.

The Defense Logistics Agency (DLA) senior management evaluated the system of internal accounting and administrative controls in effect during fiscal year 2008 (FY 2008) as of the reporting period of July 1, 2007 through June 30, 2008. This evaluation was done in accordance with OMB Circular A-123, "Management's Responsibility for Internal Control," dated August 5, 2005, as implemented by DoD Instruction 5010.40, "Managers' Internal Control Program Procedures," dated January 4, 2006, and DoD Comptroller guidance, "FY 2008 Guidance for the Preparation of the Statement of Assurance (SOA)," dated November 2007. The OMB guidelines were issued in conjunction with the Comptroller General of the United States, as required by the "Federal Managers' Financial Integrity Act of 1982." Included was an evaluation of whether the system of internal accounting and administrative controls for DLA complies with standards prescribed by the Comptroller General.

Based on its evaluation, DLA provided a qualified statement of assurance that DLA's system of internal controls, as of June 30, 2008, was operating effectively with the exception of 18 material weaknesses. In FY 2008, DLA closed one weakness, "Other Liabilities," and identified three new weaknesses: "Storage, Supply, and Distribution"; "Accounts Payable (Business Systems Modernization – Energy (BSM-E))"; and "Accounts Receivable (BSM-E)". The Accounts Payable (BSM-E) and Accounts Receivable (BSM-E) weaknesses are extracts of previously reported weaknesses that address the unique challenges inherent in the information system to support DLA's Energy Supply Chain.

DLA remains vigilant in assessing its internal controls, continues to address all of its weaknesses efficiently and effectively, and is committed to resolving them in a timely manner.

Systems

DLA has a multitude of short and long-term efforts designed to fully assess its financial operations and to develop integrated systems and processes that are compliant with Federal system and accounting requirements. Three of our major strategies:

- The improvements to Enterprise Business System (EBS) is a "technical-plus" upgrade for DLA, which will introduce only limited new functionality for all process areas with the majority occurring in finance. This upgrade also provides the foundation for future DLA initiatives (including eProcurement and BRAC) and resolves longer term software maintenance issues. The upgrade also offers Section 508 compliance improvements; provides performance improvement tools; and is required to support the future Enterprise Operating Accounting System (EOAS) initiative. The new financial functionality is primarily based on the introduction of the:

    o Budgetary Control System;
    o Budgetary Ledger;
    o Streamlined year-end close processing;
    o Improved payment update program; and
    o Funds Management - limited to Goods Receipt, not Goods Receipt/Invoice Receipt.

- The Enterprise Operational Accounting System (EOAS) project will migrate the DLA business areas that remain on two DLA legacy systems – the Defense Business Management System and the Defense Working Capital Accounting System (DWAS) onto EBS. The project mainly focuses on the operational accounting functionality performed in the legacy systems; however, the Document Automation & Production Service and the Defense National Stockpile Center will design and build key sales functionality, which is currently performed in the DWAS. While many new interfaces between feeder systems and EBS will be created, all DLA financials residing in legacy accounting systems will instead reside in the DLA EBS.

- The legacy Energy Supply Chain management was replaced by BSM-Energy (formerly, the Fuel Automated System (FAS)). FAS was an automated information system designed to support the Defense Energy Support Center (DESC) and the Military Services in performing their respective responsibilities in fuels supply chain management. In December 2003, DLA was directed to converge FAS with the DLA core architecture (introduced via the BSM program). This Energy Convergence Program will fully assess all of DESC's supply chain operations and will develop integrated systems and processes that comply with Federal system and accounting requirements.

The Defense Finance and Accounting Service (DFAS) prepared the FY 2008 DLA financial statements from available automated finance, accounting, and feeder systems (such as acquisition, logistics, and personnel systems) and manual processes. Due to system deficiencies, there are limitations in collecting the data needed to prepare financial statements that comply with Federal standards. To prepare the financial statements, DFAS made numerous adjustments during the compilation process in an attempt to overcome these deficiencies. DLA has corrective actions underway that are intended to improve the underlying systems, business processes, and internal controls.

Management Controls

DLA is institutionally committed to fostering a climate supportive of internal controls. The information contained in the DLA FY 2008 Statement of Assurance (SOA) is a result of audits, inspection reports, and self-reporting of control deficiencies by its Assessable Units, along with accomplishments toward preventing control deficiencies. The SOA demonstrates progress in addressing difficult management issues while emphasizing a strategy of continuous improvement. DLA's rigorous internal control process methodology; Lean Six Sigma; and Enterprise Risk Management initiatives all play important roles in strengthening the Agency's understanding of its key business processes, as well as in the identification, validation, and testing of internal controls.

A pre-condition to assessing DLA's internal controls is for Agency Assessable Units to ensure that their mission, goals, and objectives align with the Agency's mission, goals, and objectives to assure proper configuration, support, and focus. Assessable unit managers then review and analyze their organizational alignment, policies, processes, and procedures that they employ to uncover areas of risk that could prevent them from meeting their objectives and to identify internal controls in place that are necessary to mitigate these risks. Once the internal controls are identified, managers then test them to ensure that they are designed properly and are working as intended. The results of these tests support the assessable unit's statement of assurance.

Under the oversight of DLA's Senior Assessment Team (SAT), which maintains complete records of the assessment documentation, DLA conducted assessments in strict compliance with OMB Circular A-123, Appendix A, "Internal Control over Financial Reporting (ICOFR)." Based on the results of this evaluation, DLA was able to provide a qualified statement of assurance that DLA's ICOFR implementation areas, as of June 30, 2008, were operating effectively with the exception of the material weaknesses described in the SOA. These included one corrected weakness, two new material weaknesses, and one material weakness that moved from Part I to Part II of OMB Circular A-123, Appendix A. Corrective Action Plans are developed to document and fix ICOFR material weaknesses. Progress in executing Corrective Action Plans are reported to the SAT and the DLA Corporate Board (through Balanced Scorecard Metrics at least quarterly). In addition, Corrective Action Plans are reported to the DoD Financial Improvement and Audit Readiness (FIAR) Directorate through its web-based FIAR tool.

The Financial Operations Office continued its efforts to improve the Agency's Defense Working Capital Fund financial reporting, so that the Enterprise can achieve the strategic goal of managing DLA's resources for the best customer value. As a result of these efforts a standard process for reviewing the variances between financial statement comparative periods was developed and implemented. This is a DLA headquarters led process that: 1) determines which financial statement lines require review and analysis; 2) provides guidance to the operational field offices for the preparation of the variance analysis; 3) reviews the analysis from field offices; 4) analyzes and consolidates the input from the field offices for submission to Office of the Under Secretary of Defense (Comptroller) (OUSD(C)); and 5) answers OUSD(C) questions regarding either the financial data, or the analysis.

Improvements to the Management Internal Control (MIC) Program coverage related to financial management included: assigning additional personnel to resolve problems, thereby improving the internal control coverage; training personnel to efficiently use system applications, such as Wide Area Work Flow, Electronic Contract File, Electronic Data Access, and Enterprise Business System; and improving the visibility of the documentation that supports the business transactions and resulting financial data.

To stay current with regard to the latest management control challenges, the Financial Operations Office MIC Program coordinator, as well as the DLA field office points of contact, routinely reviewed Government Accountability Office and DoD Audit Reports to: 1) identify weaknesses and the corresponding corrective actions for DLA-related functions and operations; 2) disseminate the information to the responsible DLA functional managers; and 3) facilitate a proactive approach that fosters management awareness and initiates the implementation of proper controls.

Progressing Toward Audit Readiness

In support of the business segmentation, DLA launched a new governance structure comprised of an Audit Committee, a Stewardship Committee, an Audit Readiness Working Group (ARWG), Business Cycle Teams (BCTs), and Field Champions (high ranking field-level executives). The Stewardship Committee is comprised of all Enterprise Business Cycle Owners (EBCOs) and reports to the DLA Vice Director, while the ARWG is comprised of all of the BCT Leads and Field Champions.

The ten business cycles that fall under the purview of this governance structure include: Procure to Pay, Order to Cash; Plan to Stock, Budget to Execution, Environmental Liabilities, Fund Balance With Treasury, Hire to Retire, Acquire to Retire, Technical Infrastructure and Architecture, and Record to Report. Each business cycle owner (a member of the Senior Executive Service or a General/Flag Officer) is appointed by the DLA Vice Director. Further, each BCT (led by a single responsible EBCO) is responsible for creating and implementing strategies that resolve reported audit findings; documenting the approaches to maintain and sustain auditability; and developing and executing a Detailed Work Plan (DWP) to resolve audit impediments in their areas of responsibility. As such, DWPs document DLA's approach to fix audit impediments; contain the actions required to document the processes and related internal controls; and identify the steps required to validate the outcome of the corrective actions and prepare the requisite management assertions. The DWPs also contain Financial Improvement Plans (FIPs) and Key Milestones (KMs) to measure progress of each BCT. In addition, KMs are reported to the DoD Comptroller Financial Improvement and Audit Readiness (FIAR) Directorate through its web-based tool and are included in the DoD FIAR Plan – the Department's comprehensive approach to achieve DoD-wide auditability. DLA updates the FIAR tool – on a monthly basis – with the status of its key milestones.

As DLA progresses towards audit readiness, the importance of systems - within the business processes - and the reliance on the controls in and around those systems become more and more apparent. DLA has a complex Financial Systems Architecture comprised of systems owned by several separate and autonomous organizations (DLA, Business Transformation Agency, Defense Finance and Accounting Service, and other Components). Consequently, ensuring that adequate controls are embedded in and around these systems is a significant task; and because DLA-owned systems are undergoing revolutionary changes (legacy systems were replaced and its enterprise resource planning system, Enterprise Business System, is undergoing a significant software upgrade), control issues are even more difficult to manage. However, the DLA governance structure is working to ensure that management can assert that no material control weaknesses exist in its systems and that data extractions and system documentation are readily available to audit. The complexity of the DLA Financial Systems Architecture, the revolutionary nature of the on-going changes to the DLA enterprise resource planning system, and the recent automated control corrective action plans - resulting from the Office of Management and Budget's (OMB) Circular A-123, Appendix A testing - are a few of the key challenges that DLA will need to overcome before its management can assert that the Agency is ready for audit.

As of the 3rd Quarter, FY 2008, DLA reported 286 KMs in the FIAR plan; none of the 14 KMs that were scheduled for completion by the end of June 2008 were finished. These "slippages" were due to a mid-year Department-approved course change in the audit readiness strategy. It was a change that shifted management's audit readiness focus from a balance sheet/line item approach to a segmentation/business cycle approach. This new approach both adds to and expands the scope in addressing the KMs and the related deficiencies. KMs that previously addressed a smaller segmented issue (related strictly to financials) now address the impact and ramifications relative to end-to-end business cycle processes.

Financial Improvement and Audit Readiness (FIAR) Initiative

In 2007, DLA led the Department to refine the FIAR Plan's audit strategy for validating and sustaining financial improvement and audit readiness across segments of the business environment, rather than individual financial statement line items. A segment is an essential part of the financial improvement that can be individually assessed, validated, and asserted on for audit readiness. The resulting comprehensive end-to-end business process framework contains five essential elements for financial management improvement and requires a review and evaluation of:

- **Policies** - to ensure that DLA policies, regulations, procedures, and other guidance are consistent with applicable Federal and DoD business and financial management laws, regulations, and policies;

- **Processes** (manual, automated, or both) - to ensure that business and financial processes produce accurate and timely financial information;

- **Controls** - to ensure that proper controls are in place to achieve:
    - o Effectiveness and efficiency of operation,
    - o Reliability of financial reporting, and
    - o Compliance with applicable laws and regulations;

- **Systems** - to ensure that system capabilities and functionalities reliably produce the financial information or data needed to record financial transactions in a timely manner, and confirm that system documentation is up-to-date, properly maintained, and readily available for auditors; and

- **Human Capital** - to ensure that DLA has the right number of people with the right skills, knowledge, and experience to accomplish financial management improvement goals.

During the Discovery and Correction phases, DLA reviews and evaluates every business process step and develops corrective actions for each of the five essential elements of financial management improvement. Corrective actions for each element are captured as milestones in the FIPs and KM plans. Corrective actions and progress are tracked across DLA from an end-to-end business process level, the business process step level, or the element level.

DLA has engaged the services of a commercial firm to assist with the implementation of corrective actions and the preparation of process documentation required by both the DoD Comptroller's Business Rules and OMB Circular A-123. DLA's plan to achieve auditable financial statements is continually updated as progress is made toward these goals.

OTHER ACCOMPANYING INFORMATION

DoD Executive Agent (EA): An Executive Agent is defined as *"The Head of a DoD Component to whom the Secretary of Defense or the Deputy Secretary of Defense has assigned specific responsibilities, functions, and authorities to provide defined levels of support for operational missions, or administrative or other designated activities that involve two or more of the DoD Components."* The Deputy Secretary of Defense designated the Director of DLA as the DoD EA for Subsistence (Class I), Bulk Petroleum (Class III B), Construction and Barrier Materiel (Class IV), and Medical Materiel (Class VIII). The following are key activities and accomplishments of DLA in fulfilling DoD EA roles and responsibilities:

- **For Class I (Subsistence):** 1) Continued engagement of the Combatant Commands to optimize sustainment supportability analyses and planning; 2) coordinated with the Industrial Base Planning office to conduct surge tests in accordance with time phased force deployment data, and the U.S. Pacific Command's (USPACOM) Concept of Operations feeding plan, which resulted in a more thorough and comprehensive logistics sustainability analysis; 3) consolidated 76 gaps and seams jointly identified during the USPACOM and the U.S. Southern Command (USSOUTHCOM) Review of Concept (ROC) exercise into 21, and obtained Joint Subsistence Policy Board approval to close 12 of them; 4) accomplished a War Reserve Performance-Based Agreement (PBA) with the U.S. Marine Corps and the U.S. Air Force, and are coordinating the establishment of PBAs with the U.S. Army and the U.S. Navy; 5) initiated supply chain mapping of the First Strike Ration utilizing the Supply Chain Operations Reference model and Lean Six Sigma improvement processes; and 6) accomplished a Memorandum of Understanding with the Federal Emergency Management Agency (FEMA) which outlines responsibilities and procedures for the purchase, storage, and rotation of Meals Ready to Eat (MRE) in order to ensure effective support of future disaster relief efforts.

- **For Class III (B) (Bulk Petroleum):** 1) Provided funding to assist in the development and implementation of a web-based Reporting Emergency Petroleum, Oils, and Lubricants (REPOL) report capability that also supports the Defense Information Systems Agency's Joint Supply Management Module (JSMM) data requirements; 2) developed an Automated Information Technology Concept of Operations to support asset visibility and in-transit tracking of petroleum product; 3) captured the petroleum Common Operating Picture requirements to support strategic, operational, and tactical level visibility over the bulk petroleum supply chain; and 4) implemented a web-based Joint Petroleum Officer Training module that provides training to newly assigned fuels officers.

- **For Class IV (Construction and Barrier Materiel):** 1) Continued work on 42 supply chain gaps and seams identified during the USPACOM and USSOUTHCOM Humanitarian Assistance/Disaster Relief and Migrant Operation ROC drill – 15 gaps are scheduled for closure at the March 2009 Class IV Council meeting; 2) developed a requirements forecasting and management planning concept to improve DLA Depot stockage levels; 3) deployed 6 of the 14 EA team members to the U.S. Central Command (USCENTCOM) area of responsibility to gain knowledge and insights and to improve support for the Combatant Commander; 4) initiated a Lean/Six Sigma study to analyze internal and external business practices that will result in improved customer support; and 5) initiated work with the DLA Support Team-Iraq/ Multi-National Coalition to obtain materiel visibility and to establish stockage objectives for inventory in the Theater Class IV engineering yards.

- **For Class VIII (Medical Materiel):** 1) Developed a Joint Strategic Vision and Goals with the Office of the Assistant Secretary of Defense for Health Affairs (OASD(HA)) to transform the global medical supply chain and improve responsiveness for Joint Force Health Protection; 2) developed a draft DoD Instruction in coordination with the OSD, Joint Staff, Services, and Combatant Commands (COCOMs) that clarifies organizational responsibilities and procedures, and implements a more integrated end-to-end supply chain to support the COCOMs; 3) developed an enterprise architecture for medical materiel standardization and life-cycle management of medical assemblages in coordination with the Military Services and OASD(HA); 4) completed an Executive Agreement with the U.S. Army Medical Command to strengthen the DLA-Army partnership for improved management and production of medical assemblages; 5) developed a recommendation for Chairman, Joint Chief of Staff approval to designate a Theater Lead Agent for Medical Materiel (TLAMM) for the U.S. Africa Command; 6) developed a product data utility in coordination with the

OASD(HA), Department of Veterans Affairs, and major industry groups that provides major benefits in terms of product price reductions and transitioning purchase order items to more efficient e-commerce purchases thereby improving medical supply chain support for the Medical Heath Service and USCENTCOM; 7) currently developing a Plan of Actions and Milestones that supports the priorities for implementing the Joint Strategic Vision and that incorporates Class VIII Medical Materiel Readiness Assessment II Recommendations; and 8) currently engaged in joint discussions with the Military Services to plan and implement a second TLAMM in the Pacific Region to extend EA capabilities beyond the Korean Peninsula to the rest of the USPACOM area of responsibility.

Base Realignment and Closure (BRAC) 2005 Supply and Storage Implementation: The Office of the Secretary of Defense (OSD) designated DLA as the business manager responsible for implementing, in coordination with the Military Services, the three BRAC 2005 Supply and Storage recommendations: 1) Depot-Level Reparable (DLR) Procurement Management Consolidation (including Consumable Item Transfer (CIT)); 2) Supply, Storage, and Distribution (SS&D) Management Reconfiguration; and 3) Commodity Management Privatization. The three recommendations will be fully implemented by September 15, 2011, enforced by law under the United States Congressional legislation.

With the BRAC 2005 Supply and Storage implementation, the Military Services and DLA are creating an integrated end-to-end supply chain operation for DoD that will optimize warfighter support and readiness. The BRAC Supply and Storage recommendations, along with supporting systems and process changes, will: increase buying power with suppliers, create smoother materiel flow, reduce customer wait time for parts, achieve inventory investment savings, and reduce redundancy in processes for the Department, all of which enable logistics economies and efficiencies that better support joint operational and expeditionary forces.

Following are descriptions and a summary of accomplishments for the three Supply and Storage recommendations:

- **Depot-Level Reparable (DLR) Procurement Management Consolidation (including Consumable Item Transfer):**

  - **DLR Procurement Management Consolidation:** This recommendation creates a single, integrated new depot-level reparable procurement management provider supporting all Military Services' requirements by realigning the procurement management and related support functions for the procurement of new DLRs from the Military Services to DLA. In June 2008, over 100 full-time equivalent (FTE) positions transferred in place from the Air Force to DLA when DLA activated its first DLR detachments at Air Force Air Logistics Centers (ALCs) Ogden and Oklahoma City. DLA DLR detachments are scheduled for activation at two Naval Inventory Control Points, as well as one remaining Air Force ALC, in November 2008. DLA DLR detachments at three Army sites are scheduled to stand up beginning in FY 2009 and continue through FY 2011, while the DLA DLR detachment for Marine Corps is slated for activation in FY 2011.

  - **Consumable Item Transfer (CIT):** This recommendation also includes Consumable Item Transfer, which further consolidates consumable item management with one provider by transferring work related to the management of the remaining consumable items (except exempted items) from the Military Services to DLA. Over the course of implementing the CIT directive, which began in March 2007 and is slated for completion in September 2011, management responsibilities for more than 50,000 National Stock Numbers (NSNs) are projected to transfer. From March 2007 through September 2008, the Military Services have transferred over 22,000 NSNs to DLA.

- **Supply, Storage, and Distribution (SS&D) Management Reconfiguration:** This recommendation consolidates the supply, storage, and distribution functions and associated inventories at the current DLA Defense Distribution depots with the Military Services' maintenance activities to support operations, maintenance, and production. It involves the transfer of SS&D functions from the Military Services to DLA at 13 Service industrial sites to create an integrated supply operation and reconfigures the distribution network.

  - **Functional Transfer for Integrated Supply Operations:** For the transfer of SS&D functions and related personnel, implementation is progressing incrementally by Military Service, beginning with the Air Force:

    - ◆ Air Force – From October 2007 to July 2008, SS&D functions and over 850 FTEs at three ALCs transferred in place to DLA with the activation of DLA Warner Robins, DLA Oklahoma City, and DLA Ogden. At these three sites, support to Air Force production lines continues without disruption.

- Navy – In August 2008, Fleet and Industrial Supply Center (FISC) Jacksonville's Cherry Point Detachment supporting Fleet Readiness Center (FRC) East transferred SS&D functions and 150 FTEs to DLA. Additional FISC SS&D operations and associated personnel in support of two FRCs and two Naval Shipyards are scheduled to transfer in FY 2009.

- Marine Corps - Two Maintenance Centers are slated to transfer SS&D functions and related personnel, one each in FY 2009 and FY 2010.

- Army – Three Maintenance Depots are scheduled to transfer SS&D functions and related personnel to DLA, one in FY 2010 and two in FY 2011.

o **Strategic Distribution Platform (SDP)/Forward Distribution Point (FDP) Network:** The recommendation regarding SS&D Management Reconfiguration calls for the creation of four continental United States support regions, each having one SDP and one or more FDPs. The current SDPs in San Joaquin, CA, and Susquehanna, PA, will be joined by new SDPs in Warner Robins, GA, and Oklahoma City, OK. The remaining 11 collocated distribution depots and one non-collocated depot will be reconfigured as FDPs. Their mission will be to provide storage and distribution support to collocated and non-collocated industrial customers and select local customers and to provide support for reimbursable work, end items, hard to handle items, and hazardous items. The entire Distribution Network will support global, regional, on-base, and industrial maintenance activities and is intended to create an efficient materiel flow for customers within a region, achieve inventory investment savings for DoD, and reduce customer wait time for parts.

o **Defense Distribution Depot Disestablishemnt:** Defense Distribution Depot Columbus, OH was officially disestablished on September 30, 2008.

- **Commodity Management Privatization:** This recommendation charges DLA with the responsibility for privatizing DoD's entire logistics process for three commodity lines: tires; packaged petroleum, oils, and lubricants; and compressed gasses. Commodity Management Privatization requires DoD to disestablish the supply, storage, and distribution functions previously performed by DLA and the Military Services for these commodities and rely completely on private industry vendors to perform them. The privatization recommendation also transfers the supply contracting functions for these items from the Military Services to DLA. In executing this mandate, DLA assumed responsibility for these commodities from the Military Services and awarded four privatization contracts for land tires, aviation tires, chemicals and packaged petroleum products, and compressed and liquefied gasses and cylinders. Full implementation of all contracts was completed in August 2008, with vendors responsible for 100% of the supply support for the commodities covered under the privatization contracts.

Enterprise Business System (EBS): DLA's EBS capabilities will continue to be leveraged as a major transformation initiative. It will expand capabilities and benefits introduced under the Business Systems Modernization (BSM) Program by delivering additional standard systems and business processes through the integration of a family of software applications. The Agency will continue to leverage best practices and its commercially-based Commercial Off-the-Shelf (COTS) infrastructure to enable DLA to extend its EBS capabilities outward throughout the DoD supply chain. EBS will integrate DLA's previously program-focused IT initiatives into an enterprise capability-focused solution. Specifically, the Agency will leverage its existing core enterprise architecture components (SAP-based Enterprise Resource Planning (ERP) tool, Distribution Standard System (DSS), and Integrated Data Environment (IDE)) to enable a single, integrated, capability-based system that is accessible and of value to warfighters across the enterprise.

- **Energy Convergence:** As DLA's enterprise is extended across the DoD supply chain, a technology insertion effort is needed to enable the SAP Industry Solution Public Sector and the SAP Industry Solution Oil & Gas solutions to coexist in support of the Defense Energy Support Center (DESC) mission requirements. At the highest level DESC business processes and other DLA supply chain operations appear similar, but at a more detailed level there are significant differences. Energy Convergence will allow DLA to integrate fuels commodity management within the DLA Enterprise Architecture.

- **Enterprise Operational Accounting System (EOAS):** EOAS is a planned post-production enhancement that will add all operational accounting functions to EBS. The result will be an enterprise-wide financial system that complies with federal government accounting standards.

- **eProcurement:** eProcurement is a planned post-production enhancement that will integrate the SAP Government Procurement software into EBS, replacing remaining legacy contract writing systems. This initiative will standardize DLA procurement and contract writing capabilities and provide state-of-the-art decision planning tools. It will position the Agency to assume depot-level reparable(DLR) procurement responsibility from the Military Services as result of the latest BRAC recommendations.

- **Distribution Standard System (DSS):** DSS provides a fully integrated storage and distribution capability that optimizes transportation planning for vendor shipments and provides customers with real-time supply chain information.

- **Reutilization Business Integration (RBI):** Formerly known as the Reutilization Modernization Program (RMP), it is DLA's strategy to replace the current Defense Reutilization and Marketing Service (DRMS) Automated Information System suite of applications with a solution based on best-business practices, best-of-breed Government Off-The-Shelf and Commercial Off-The-Shelf software. RBI will integrate and leverage DLA Enterprise solutions: Distribution Standard System, Enterprise Business System, and Integrated Data Environment. This integration will incorporate DRMS information systems into the DLA Enterprise Information Technology (IT) Solution Set, with the intent of maximizing use of existing IT solutions in the execution of the DRMS business.

- **DLA Real Property and Project Systems:** This is an integrated module within the DLA EBS that will standardize the enterprise-wide management of real property assets to include: project documentation, approvals and tracking, financial improvement and audit readiness, and DoD real property inventory and environmental liabilities requirements.

Retail Integration: Retail integration is a transformational program to extend the DLA enterprise closer to the warfighter; and where DLA becomes a manager of complete supply chains – versus a manager of wholesale supplies. Instead of merely operating as a wholesaler, DLA will take supply ownership and management from the factory to the ultimate customer. By using Department-wide initiatives (such as the National Inventory Management Strategy (NIMS); Joint Regional Inventory Materiel Management (JRIMM); Joint Environmental Materiel Management Service (JEMMS); and the implementation of the BRAC supply, storage, and distribution recommendations), DLA will replace distinct wholesale and retail inventories with a national inventory that can be managed in a more integrated manner. Through FY 2008, DLA has rolled-out NIMS to six locations: the Joint Environmental Materiel Management Service Center, Okinawa (June 2002); Naval Station Ingleside, TX (July 2003); Naval Air Station Whidbey Island, WA (August 2005); Naval Air Weapons Station China Lake, CA (February 2006); Marine Corps Air Station Miramar, CA (February 2006); and Naval Auxiliary Landing Field San Clemente, CA (February 2006). In FY 2008, DLA also implemented JRIMM throughout the island of Oahu, HI. DLA's retail strategies will provide better demand visibility, increase supply availability, and reduce customer wait-time. As the strategies become more fully integrated into our business systems, benefits will include: further reductions to customer wait-times, higher levels of supply readiness, more tailored logistics support solutions, improved inventory and customer demand visibility, greater optimization of the supply chain, better use of available resources (including lower overall DoD inventory and inventory management costs), and a reduction in the Military Services' inventory investments without reducing support.

Forward Logistics: Forward Logistics is the net sum of the DLA Enterprise efforts to perform end-to-end supply chain management on the eight DLA supply chains - Aviation, Maritime, Land, Construction & Equipment, Subsistence, Clothing & Textiles, Medical, and Energy. In managing these supply chains, DLA's efforts in FY 2008 focused on supporting two of DLA's Strategic Goals: extending the Enterprise and continuing to improve performance. The Enterprise accomplishments include those outlined in the discussion of Retail Integration, as well as building on/expanding the Customer Demand Collaboration initiative begun under the BSM/EBS program. Looking forward, we see these efforts (retail integration and customer demand collaboration) coalescing into a collaboratively extended supply chain with close involvement of customer requirements generators and ultimate consumers of DLA's goods and services.

Reverse Logistics: Reverse Logistics in DLA consists primarily of two components: the Materiel Returns Program, which equates to the 'Return' process of the Supply Chain Operations Reference Model of supply chain management, and the reutilization services performed by the Defense Reutilization and Marketing Service (DRMS). Under the Materiel Returns Program, customers return materiel that they no longer need to the wholesale supply chain to support a future customer's requirements. These assets, in turn, preclude the need to initiate procurement actions to acquire assets to meet projected requirements, thus improving both the efficiency and effectiveness of supply chain management. The DRMS reutilization mission, which is described in detail separately, primarily involves receiving materiel that is no longer needed by a component of the DoD and making it available to all of the components of the DoD. These efforts optimize the use of materiel that is available for use by the DoD and help minimize the investment in inventory.

Strategic Communications: As a newly formed focus area, DLA is developing an agency-wide strategic communications plan to proactively and effectively communicate with both internal and external audiences. For example, Strategic Visual Communications designs visual communication campaigns that highlight the use of video in various formats to reach global audiences. The underlying services will include: video productions, podcasts, video news releases, live broadcasts, and media training programs. Customer outreach consulting is also offered.

Enterprise Organizational Alignment (EOA) provides a standardized means for determining the optimal structure of an organization, the timing for the restructuring, whether a particular organizational change will have an enterprise-wide impact, and all of the supporting actions necessary to implement an EOA.

Continuous Process Improvement (CPI) provides an ongoing method for analyzing how work is accomplished and how processes can be operated more efficiently and effectively. It is an enterprise-wide approach to develop a culture of continuous improvement in the areas of reliability, process cycle times, costs, quality, and productivity. CPI applies and employs a broad range of tools and methods, such as Lean (to eliminate all types of waste), Six Sigma (to optimize process variation), and Theory of Constraints (to alleviate process bottlenecks).

Reservists: Among the manpower available to DLA were 735 reservists - authorized and funded by the Military Services. The reservists are utilized by DLA in a variety of capacities in support of peacetime operations, contingencies, and wartime surges. Since September 11, 2001, the wartime surges were supported with the mobilization of 510 reservists who served a total of 694 tours of duty in support of Operations Enduring Freedom and Iraqi Freedom in the Global War on Terrorism. During FY 2008, 55 reservists mobilized and provided support to DLA's three Support Teams (DSTs) in Kuwait, Iraq, and Afghanistan, while 5 reservists staffed the Sustainment Division of the U.S. Central Command's Deployment and Distribution Operations Center. Collectively, activated reservists logged more than 23,000 man-days of support to DSTs, field activities, and headquarters missions. In addition, to those deployed overseas, reservists provided more than 8,000 man-days of operational support to the various stateside DLA activities during their statutory annual training.

DEFENSE LOGISTICS AGENCY

WORKING CAPITAL FUND

Consolidated and Combined Financial Statements

As of and for the Years Ended September 30, 2008 and 2007

UNAUDITED

DEPARTMENT OF DEFENSE
DEFENSE LOGISTICS AGENCY WORKING CAPITAL FUND

Consolidated Balance Sheets
As of September 30, 2008 and 2007
(In Thousands)

	2008	2007
ASSETS (Note 2)		
Intragovernmental:		
Accounts Receivable (Note 5)	$ 632,209	$ 932,515
Other Assets (Note 6)	124,980	124,925
Total Intragovernmental Assets	757,189	1,057,440
Cash and Other Monetary Assets (Note 7)	9,775	7,421
Accounts Receivable, Net (Note 5)	781,421	489,224
Inventory and Related Property, Net (Note 9)	21,620,021	17,516,903
General Property, Plant, and Equipment, Net (Note 10)	1,888,857	1,938,422
Other Assets (Note 6)	25,685	43,629
TOTAL ASSETS	25,082,948	21,053,039
LIABILITIES (Note 11)		
Intragovernmental:		
Accounts Payable (Note 12)	114,351	90,388
Other Liabilities (Notes 15 & 16)	68,429	64,757
Total Intragovernmental Liabilities	182,780	155,145
Accounts Payable (Note 12)	3,050,001	2,751,119
Military Retirement and Other Federal Employment Benefits (Note 17)	236,426	235,596
Environmental and Disposal Liabilities (Note 14)	91,494	72,644
Other Liabilities (Notes 15 & 16)	227,807	149,449
TOTAL LIABILITIES	3,788,508	3,363,953
NET POSITION		
Cumulative Results of Operations – Other Funds	21,294,440	17,689,086
TOTAL NET POSITION	21,294,440	17,689,086
TOTAL LIABILITIES AND NET POSITION	$ 25,082,948	$ 21,053,039

The accompanying notes are an integral part of these statements.

UNAUDITED

DEPARTMENT OF DEFENSE
DEFENSE LOGISTICS AGENCY WORKING CAPITAL FUND

Consolidated Statements of Net Cost
For the Years Ended September 30, 2008 and 2007
(In Thousands) (See Note 18)

	2008	2007
PROGRAM COSTS		
Gross Costs	$ 41,020,264	$ 35,587,003
Less: Earned Revenue	(42,788,025)	(36,148,078)
Net Program Costs	(1,767,761)	(561,075)
NET COST OF OPERATIONS	$ (1,767,761)	$ (561,075)

The accompanying notes are an integral part of these statements.

UNAUDITED

DEPARTMENT OF DEFENSE
DEFENSE LOGISTICS AGENCY WORKING CAPITAL FUND

Consolidated Statements of Changes in Net Position
For the Years Ended September 30, 2008 and 2007
(In Thousands) (See Note 19)

	2008	2007
CUMULATIVE RESULTS OF OPERATIONS		
Beginning Balances	$ 17,689,086	$ 17,641,781
Budgetary Financing Sources:		
Appropriations used	317,771	489,316
Transfers-in/out without reimbursement (+/-)	(40,000)	(374,904)
Other Financing Sources:		
Donations and forefeitures of property	-	2,710
Transfers-in/out without reimbursement (+/-)	1,417,932	(782,613)
Imputed financing from costs absorbed by others	141,890	151,721
Total Financing Sources	1,837,593	(513,770)
Net Cost of Operations (+/-)	(1,767,761)	(561,075)
Net Change	3,605,354	47,305
Cumulative Results of Operations	21,294,440	17,689,086
UNEXPENDED APPROPRIATIONS		
Budgetary Financing Sources:		
Appropriations received	342,975	489,385
Appropriations transferred-in/out (+/-)	-	-
Other adjustments (rescissions, etc.) (+/-)	(25,204)	(69)
Appropriations used	(317,771)	(489,316)
Ending Balances	-	-
NET POSITION	$ 21,294,440	$ 17,689,086

The accompanying notes are an integral part of these statements.

UNAUDITED

DEPARTMENT OF DEFENSE
DEFENSE LOGISTICS AGENCY WORKING CAPITAL FUND

Combined Statements of Budgetary Resources
For the Years Ended September 30, 2008 and 2007
(In Thousands) (See Note 20)

	2008	2007
BUDGETARY FINANCING ACCOUNTS		
Budgetary Resources:		
Unobligated balance, brought forward, October 1	$ (23,848)	$ (30,820)
Recoveries of prior year unpaid obligations	1,295,519	438,636
Budget authority		
Appropriation	342,975	489,385
Contract authority	47,867,268	36,589,729
Spending authority from offsetting collections:		
Earned		
Collected	41,634,578	34,015,324
Change in receivables from Federal sources	30,257	47,316
Change in unfilled customer orders		
Advance received	1,997	(95,521)
Without advance from Federal sources	714,883	1,893,299
Subtotal	90,591,958	72,939,532
Nonexpenditure transfers, net, anticipated and actual	(40,000)	(374,904)
Permanently not available	(43,595,741)	(36,059,827)
Total Budgetary Resources	$ 48,227,888	$ 36,912,617

UNAUDITED

DEPARTMENT OF DEFENSE
DEFENSE LOGISTICS AGENCY WORKING CAPITAL FUND

Combined Statements of Budgetary Resources (Continued)
For the Years Ended September 30, 2008 and 2007
(In Thousands) (See Note 20)

	2008	2007
Status Of Budgetary Resources:		
Obligations incurred:		
Reimbursable	$ 48,205,128	$ 36,936,465
Subtotal	48,205,128	36,936,465
Unobligated balance:		
Apportioned	22,761	(23,848)
Subtotal	22,761	(23,848)
Unobligated balance not available	(1)	-
Total Status of Budgetary Resources	48,227,888	36,912,617
Change in Obligated Balance:		
Obligated balance, net		
Unpaid obligations, brought forward, October 1	16,960,614	13,840,700
Less: Uncollected customer payments		
from Federal sources, brought forward, October 1	(7,234,730)	(5,294,115)
Total unpaid obligated balance, net	9,725,884	8,546,585
Obligations incurred, net	48,205,128	36,936,465
Less: Gross outlays	(42,905,975)	(33,377,915)
Less: Recoveries of prior year unpaid obligations, actual	(1,295,519)	(438,636)
Change in uncollected customer payments		
from Federal sources (+/-)	(745,139)	(1,940,616)
Obligated balance, net, end of period		
Unpaid obligations	20,964,247	16,960,614
Less: Uncollected customer payments		
from Federal sources (+/-)	(7,979,870)	(7,234,730)
Total unpaid obligated balance, net, end of period	12,984,377	9,725,884
Net Outlays:		
Gross outlays	42,905,975	33,377,915
Less: Offsetting collections	(41,636,576)	(33,919,803)
Net Outlays	$ 1,269,399	$ (541,888)

The accompanying notes are an integral part of these statements.

DEFENSE LOGISTICS AGENCY
WORKING CAPITAL FUND

Notes to the Consolidated and Combined Financial Statements

For the Fiscal Years Ended September 30, 2008 and 2007

Note 1. Significant Accounting Policies

A. Basis of Presentation

These financial statements have been prepared to report the financial position and results of operations of the Defense Logistics Agency (DLA) Working Capital Fund (WCF), 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 DLA in accordance with the Department of Defense (DoD) Financial Management Regulation (FMR), the Office of Management and Budget (OMB) Circular A-136, Financial Reporting Requirements, and to the extent possible generally accepted accounting principles (GAAP). The accompanying financial statements account for all resources for which DLA is responsible unless otherwise noted.

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

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

The DoD currently has several auditor identified financial statement material weaknesses. Of these, DLA has the following: (1) Financial Management Systems, (2) Intragovernmental Eliminations, (3) Unsupported Accounting Entries, (4) Fund Balance with Treasury, (5) General Property, Plant, and Equipment, (6) Inventory, (7) Accounts Payable, and (8) Accounts Receivable.

B. Mission of the Reporting Entity

The DLA's primary mission is to provide best value logistics integrated solutions to meet the needs of America's Armed Forces and other designated customers around the clock, around the world in time of peace, national emergency, and war. Support begins with joint planning for parts used in new weapons systems, extends through production and contract support, distribution and warehousing, and concludes with the disposal of materiel that is obsolete, worn out, or no longer needed.

The DLA provides supply support, technical/logistics services and quality support to all branches of the Military and other nonDoD customers. The services provided fall into the following activity groups: Supply Management, Defense Distribution Center (DDC), Defense Reutilization and Marketing Service (DRMS), and Document Automation and Production Service (DAPS). Supply Management is comprised of NonEnergy and Energy. NonEnergy Supply is further divided into the following supply chains: Clothing and Textiles, Medical, Subsistence, Construction and Equipment, Aviation, Land, and Maritime.

The DLA continues to leverage its operational efficiencies to implement the Base Realignment and Closure 2005 Supply and Storage recommendations. The DLA has engaged in the following transformational initiatives with the Military Departments: (1) The Commodity Management Privatization to privatize the supply and storage of selected commodities (i.e., tires, compressed gases and petroleum, oil, lubricant packages), (2) Depot - Level Reparable (Procurement Management/Consumable Item Transfer) to realign procurement management of repair parts from the Military Services to DLA at selected sites and to transfer supply management of selected consumable items to DLA, and (3) Supply, Storage and Distribution Reconfiguration to realign supply, storage and distribution functions through consolidation and management reconfiguration at 13 sites.

C. Appropriations and Funds

The DLA WCF receives its appropriations and funds as working capital funds. The DLA uses these appropriations and funds to execute its missions and subsequently report on resource usage.

The DLA WCF received its initial working capital 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, the Congress provides additional appropriations to supplement the WCF as an infusion of cash when revenues are inadequate to cover costs within the corpus.

The DLA WCF is provided two forms of budgetary authority: contract authority and anticipated reimbursement authority. The DLA's Supply Management, DDC, and DRMS activity groups are provided contract authority for both operations and capital programs. The DAPS activity is provided anticipated reimbursement authority for its operations and contract authority for its capital programs. Contract authority allows for the incurring of obligations prior to receipt of customer orders. In contrast, anticipated reimbursement authority requires the receipt of customer orders prior to incurring obligations. Contract authority must subsequently be liquidated through the receipt of customer orders, appropriations or transfers.

D. Basis of Accounting

For FY 2008, DLA's financial management systems are unable to meet all of the requirements for full accrual accounting. Many of DLA's financial and nonfinancial feeder systems and processes were designed and implemented prior to the issuance of GAAP for federal agencies. These systems were not designed to collect and record financial information on the full accrual accounting basis as required by GAAP. Most of DLA's (financial and nonfinancial) legacy systems were designed to record information on a budgetary basis.

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

E. Revenues and Other Financing Sources

The DLA WCF activities recognize revenue from the sale of inventory items and services.

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

F. Recognition of Expenses

For financial reporting purposes, the DoD policy requires the recognition of operating expenses in the period incurred. However, because DLA's financial and nonfinancial feeder systems were not designed to collect and record financial information on the full accrual accounting basis, accruals are made for major items such as payroll expenses, accounts payable, environmental liabilities, and unbilled revenue.

G. Accounting for Intragovernmental Activities

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

The U.S. Treasury Financial Management Service is responsible for eliminating transactions between DoD and other federal agencies. The Treasury Financial Manual Part 2 – Chapter 4700, "Agency Reporting Requirements for the Financial Report of the United States Government," and U.S. Treasury's "Federal Intragovernmental Transactions Accounting Policy Guide" provide guidance for reporting and reconciling intragovernmental balances. While DLA is unable to fully reconcile intragovernmental transactions with all federal partners, DLA 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, therefore, do not report any portion of the public debt or interest thereon, nor do the statements report the source of public financing whether from issuance of debt or tax revenues.

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

H. Transactions with Foreign Governments and International Organizations

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

The DLA's fuel transactions with foreign governments are made under fuel exchange agreements (FEAs). The FEAs, also known as replacement in kind agreements, are international acquisition and cross-servicing agreements established between DLA and the military departments of other nations. The DLA utilizes FEAs to account for fuel provided by foreign militaries to the U.S. Military as well as fuel provided by DLA to other nations. Settlement can be made either in fuel or cash. For cash settlements, the agreements typically call for reciprocal pricing (i.e. prices cannot be more than the participants charge their own military). The DLA charges DoD standard prices to foreign militaries.

I. Funds with the U.S. Treasury

The DLA's monetary financial resources are maintained in U.S. Treasury accounts. The disbursing offices of the 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 DLA's cash collections, disbursements, and adjustments worldwide. Each disbursing station prepares monthly reports to the U.S. Treasury on check issues, electronic fund transfers, interagency transfers, and deposits.

In addition, DFAS sites and USACE Finance Center submit reports to the U.S. Treasury by appropriation on interagency transfers, collections received, and disbursements issued. The U.S. Treasury records these transactions to the applicable Fund Balance with Treasury (FBWT) account. Appropriations are suballocated to DLA by DoD. Differences between U. S. Treasury and the DoD balances are reconciled at the Departmental level.

The U.S. Treasury maintains and reports the Defense Working Capital Fund (DWCF) fund balances at the Treasury Index (TI) appropriation sub-numbered level. Defense Agencies, to include DLA, are included in the Defense-Wide Working Capital Fund (DWWCF), a TI 97 DWCF appropriation sub-numbered account. This account is maintained at an aggregate level that does not provide identification of the separate Defense Agencies. Additionally, while DLA maintains collection and disbursement clearing accounts, those cash balances are transferred to the DWWCF cash account on an annual basis. As a result, DLA does not report FBWT separately. The DLA's balance in the DWWCF cash account as of 4th Quarter, FY 2008 is $568.1 million.

J. Foreign Currency

Not Applicable to DLA WCF.

K. Accounts Receivable

As presented in the Balance Sheet, accounts receivable includes three categories: accounts, claims, and refunds receivable from other federal entities or from the public. Allowances for uncollectible accounts due from the public are based upon Analysis of Receivables by Age Group method except for the Energy business area, which uses the General Reserve method based on bad debt experience. 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.

Exchange transactions such as FEAs must be settled through the issuance or receipt of replacement supplies or services within 12 months of the original transaction according to current DoD policy. As the settlement of the exchange transactions is authorized to take up to 12 months, the analysis of the nonfederal accounts receivable balances greater than 180 days old could be distorted. To assist in the analysis, Note 5, Accounts Receivable, separates FEA transaction balances from the remainder of the nonfederal accounts receivable. Currently, upon reconciliation the purchases of fuel from foreign governments are netted against their accounts receivable balances. This methodology is currently being reviewed for conformance with GAAP.

L. Direct Loans and Loan Guarantees

Not Applicable to DLA WCF.

M. Inventories and Related Property

The DLA values approximately 60% of its resale inventory using the moving average cost method. An additional 40% (fuel inventory) is reported using the first-in-first-out method. The DLA reports less than 0.5 % 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 (P.L. 104-208). By utilizing new systems development processes, DLA is continuing to transition the balance of the inventories to the moving average cost method. However, since the on-hand balances which were transitioned were not, for the most part, baselined to auditable historical cost, the reported values remain noncompliant with SFFAS No. 3 and GAAP.

The DLA manages only military or government specific materiel under normal conditions. Materiel is a unique term that relates to military force management, and includes all items (including ships, tanks, self-propelled weapons, aircraft, etc., and related spares, repair parts, and support equipment, but excluding real property, installations, and utilities) necessary to equip, operate, maintain, and support military activities without distinction as to its application for administrative or combat purposes. Items commonly used in and available from the commercial sector are not managed in DLA materiel management activities. Operational cycles are irregular, and the military risks associated with stock-out positions have no commercial parallel. The DLA holds materiel based on military need and support for contingencies. The DoD does not attempt to account separately for "inventory held for sale" and "inventory held in reserve for future sale" based on SFFAS No. 3 definitions, unless otherwise noted.

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

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

N. Investments in U.S. Treasury Securities

Not Applicable to DLA WCF.

O. General Property, Plant and Equipment

The DLA's General Property Plant & Equipment (General PP&E) capitalization threshold is $100 thousand except for real property which is $20 thousand. The DLA has not implemented the threshold for real property. The DLA is currently using the capitalization threshold of $100 thousand for all General PP&E.

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 capitalization threshold. The DoD also requires the capitalization of improvements to existing General PP&E assets if the improvements equal or exceed DoD 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.

The WCF capitalizes all General PP&E used in the performance of their mission. These capitalized assets are categorized as General PP&E, whether or not it meets the definition of any other General PP&E categories.

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

The DoD is developing new policies and a contractor reporting process for Government Furnished Equipment that will provide appropriate General PP&E information for future financial statement reporting purposes. Accordingly, DLA reports only government property in the possession of contractors that is maintained in DLA's property systems. The DoD has issued new property accountability and reporting requirements that require DLA to maintain, in their property systems, information on all property furnished to contractors. This action and other DoD proposed actions are structured to capture and report the information necessary for compliance with federal accounting standards. The DLA has not fully complied with these revised reporting requirements due to system and process limitations.

P. Advances and Prepayments

When advances are permitted by law, legislative action, or presidential authorization, the DoD's policy is to record advances or prepayments in accordance with GAAP. 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 DLA has implemented this policy.

Q. Leases

Lease payments for the rental of operating assets are classified as either capital or operating leases. When a lease is essentially equivalent to an installment purchase of property (a capital lease), DLA records the applicable asset and liability if the value equals or exceeds the current capitalization threshold. The DLA records the amounts as the lesser of the present value of the rental and other lease payments during the lease term (excluding portions representing executory costs paid to the lessor) or the asset's fair market value. The discount rate for the present value calculation is either the lessor's implicit interest rate or the government's incremental borrowing rate at the inception of the lease. The DLA initiated a process in 4th Quarter, FY 2007, to phase in the reporting of assets acquired through capital lease agreements. However, the majority of DLA's leases are for copiers, multi-functional devices and vehicles that do not meet the capitalization threshold.

R. Other Assets

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

The DLA 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, DLA may provide financing payments. Contract financing payments are defined in the Federal Acquisition Regulations, Part 32, as authorized disbursements of monies to a contractor prior to acceptance of supplies or services by the Government. Contract financing payments clauses are incorporated in the contract terms and conditions and may include advance payments, performance-based payments, commercial advance and interim payments, progress payments based on cost, and interim payments under certain cost-reimbursement contracts.

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

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 DLA recognizes contingent liabilities when past events or exchange transactions occur, a future loss is probable, and the loss amount can be reasonably estimated.

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

Other liabilities arise as a result of anticipated disposal costs for DLA's assets. This type of liability has two components: nonenvironmental and environmental. Consistent with SFFAS No. 6, "Accounting for Property, Plant, and Equipment," recognition of an anticipated environmental disposal liability begins when the asset is placed into service. Nonenvironmental disposal liabilities are recognized for assets when management decides to dispose of an asset based upon DoD's policy, which is consistent with SFFAS No. 5, "Accounting for Liabilities of Federal Government". The DLA has not fully implemented these policies due to system and process limitations.

T. Accrued Leave

The DLA reports as liabilities civilian earned leave, except sick leave, that has been accrued and not used as of the Balance Sheet date. As a WCF activity, DLA is required to fund civilian accrued annual leave earned but not taken. Sick leave and travel compensatory time are expensed as taken. The liability reported at the end of the accounting period reflects the current pay rates.

U. Net Position

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

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

Cumulative Results of Operations represent the net difference, since inception of an activity, between expenses and losses and financing sources (including appropriations, revenue, and gains). Beginning with FY 1998, the cumulative results also include donations and transfers in and out of assets that were not reimbursed.

V. Treaties for Use of Foreign Bases

Not Applicable to DLA WCF.

W. Comparative Data

The DLA's financial statements and notes are presented on a comparative basis.

X. Unexpended Obligations

The DLA obligates funds to provide goods and services for outstanding orders not yet delivered. Unless the title has passed, the financial statements do not reflect a liability for payment for goods and services not yet delivered. Unexpended obligations includes both obligations for which goods and services have been delivered (title passed) and a liability recognized, and obligations for which no delivery has occurred and no liability recognized. The balance of unexpended obligations appears immediately before net outlays in the Statement of Budgetary Resources, and is referred to as "Total, unpaid obligated balances, net, end of period."

Y. Undistributed Disbursements and Collections

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

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

Z. Significant Events

Not Applicable to DLA WCF.

Note 2. Nonentity Assets

As of September 30	2008		2007	
(Amounts in thousands)				
Nonfederal Assets				
Cash and Other Monetary Assets	$	9,775	$	7,421
Accounts Receivable		2,745		3,077
Total Nonfederal Assets	$	12,520	$	10,498
Total Nonentity Assets	$	12,520	$	10,498
Total Entity Assets	$	25,070,428	$	21,042,541
Total Assets	$	25,082,948	$	21,053,039

Nonentity Assets are assets for which DLA maintains stewardship accountability and responsibility to report, but are not available for DLA's operations.

Cash and Other Monetary Assets consists of cash collected by the Defense Reutilization and Marketing Service (DRMS) that will be paid to other entities. When DRMS enters into a long-term contract with a buyer purchasing excess/surplus government property or scrap, DRMS requires a prepayment. After contract closeout, any remaining balance is refunded to the sales contractor. Also included are credit card collections that are payable to DRMS' commercial sales partner and the portion of sales proceeds from certain types of property that DRMS is required to return to the Military Services or Defense Agencies that originally owned the property.

The Nonfederal Accounts Receivable consists of interest, penalties, and administrative fees that are related to the Nonfederal accounts receivable that have been referred to Defense Finance and Accounting Service debt management for collection. This accounts receivable is nonentity because upon collection the amounts will be transferred to the U.S. Treasury.

Note 3. Fund Balance with Treasury

Status of Fund Balance with Treasury

As of September 30	2008		2007	
(Amounts in thousands)				
Unobligated Balance Available	$	22,761	$	(23,848)
Obligated Balance not yet Disbursed		20,964,247		16,960,614
NonFBWT Budgetary Accounts		(20,418,937)		(15,377,069)
Total	$	568,071	$	1,559,697

The Status of Fund Balance with Treasury reflects the budgetary resources to support the FBWT.

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

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

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

NonFBWT Budgetary Accounts represents adjustments to budgetary accounts that do not affect FBWT. DLA's NonFBWT Budgetary Accounts consists of contract authority, accounts receivable and unfilled orders without advance from customers. This category reduces the Status of FBWT.

Unobligated balances are segregated to show available and unavailable amounts in the note schedule. There are no restrictions on DLA's unobligated balances.

The DLA's FBWT is zero as the net of DLA's current year disbursements, collections, cash transfers, and appropriations received are transferred to the DWCF cash account. The Total Status of Funds represents what DLA's FBWT would have been if the transfers to the cash account had not taken place.

The U.S. Treasury maintains and reports the Defense Working Capital Fund (DWCF) fund balances at the Treasury Index (TI) appropriation sub-numbered level. Defense Agencies, to include DLA, are included in the Defense-Wide Working Capital Fund (DWWCF), a TI 97 DWCF appropriation sub-numbered account. This account is maintained at an aggregate level that does not provide identification of the separate Defense Agencies. Additionally, while DLA maintains collections and disbursement clearing accounts, those cash balances are transferred to the DWWCF cash account on an annual basis. As a result, DLA does not report Fund Balance with Treasury (FBWT) separately. The DLA balance in the DWWCF cash account as of the 4th Quarter, FY 2008 is $568.1 million.

Note 4. Investments and Related Interest

Not Applicable to DLA Working Capital Fund.

Note 5. Accounts Receivable

As of September 30	2008			2007
	Gross Amount Due	Allowance For Estimated Uncollectibles	Accounts Receivable, Net	Accounts Receivable, Net
(Amounts in thousands)				
Intragovernmental Receivables	$ 632,209	N/A	$ 632,209	$ 932,515
Nonfederal Receivables (From the Public)	$ 839,483	$ (58,062)	$ 781,421	$ 489,224
Total Accounts Receivable	$ 1,471,692	$ (58,062)	$ 1,413,630	$ 1,421,739

Note 6. Other Assets

As of September 30	2008	2007
(Amounts in thousands)		
Intragovernmental Other Assets		
Advances and Prepayments	$ 55	$ 0
Other Assets	124,925	124,925
Total Intragovernmental Other Assets	$ 124,980	$ 124,925
Nonfederal Other Assets		
Outstanding Contract Financing Payments	23,590	41,597
Advances and Prepayments	2,095	2,031
Other Assets (With the Public)	0	1
Total Nonfederal Other Assets	$ 25,685	$ 43,629
Total Other Assets	$ 150,665	$ 168,554

Composition of Other Lines

Intragovernmental Other Assets consist of crude oil held by the Department of Energy (DoE) on behalf of the Department of Defense (DoD). The DLA has the right to approximately 6.4 million barrels of crude oil held by DoE on behalf of DoD. Public Law 102-396, Section 9149 enacted in November 1992 established the requirement for DoE to acquire and maintain a strategic petroleum reserve for national defense purposes. Section 9149 provided appropriations for the acquisition, storage, and drawdown of such reserve. Proceeds from sales of this reserve will be deposited to DoD's accounts and remain available until expended. The DoE reports this crude oil in inventory in their financial statements, with an offsetting custodial liability to DoD. By law, the reserve cannot be drawn down or released to DoD without a Presidential Order along with the advice from the Secretary of Defense. To date none of the reserve has been drawn upon, thus the full inventory remains on hand with DoE. See the Energy Policy and Conservation Act (42 USC 6241(d)), Section 161(d) for further details.

Contract Financing Payments

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

The Contract Financing Payment balance of $23.6 million is comprised of $20.0 million in contract financing payments and an additional $3.6 million in estimated future payments that will be paid to the contractor upon future delivery and Government acceptance of a satisfactory product. (See additional discussion in Note 15, Other Liabilities).

Note 7. Cash and Other Monetary Assets

As of September 30	2008	2007
(Amounts in thousands)		
Cash	$ 9,775	$ 7,421
Total Cash, Foreign Currency, & Other Monetary Assets	$ 9,775	$ 7,421

The entire Cash balance is restricted because it consists of prepayments, credit card collections, and sales proceeds that will be paid to other entities. Refer to Note 2, Nonentity Assets for details.

Note 8. Direct Loan and Loan Guarantees

Not Applicable to DLA Working Capital Fund.

Note 9. Inventory and Related Property

As of September 30	2008	2007
(Amounts in thousands)		
Inventory, Net	$ 21,620,021	$ 17,516,903
Total	$ 21,620,021	$ 17,516,903

Inventory, Net

As of September 30	2008			2007	
	Inventory, Gross Value	Revaluation Allowance	Inventory, Net	Inventory, Net	Valuation Method
(Amounts in thousands)					
Inventory Categories					
Available and Purchased for Resale	$ 21,609,418	$ (11)	$ 21,609,407	$ 17,511,032	LAC,MAC
Held for Repair	17,689	(7,075)	10,614	5,871	LAC,MAC
Excess, Obsolete, and Unserviceable	5,811,994	(5,811,994)	0	0	NRV
Total	$ 27,439,101	$ (5,819,080)	$ 21,620,021	$ 17,516,903	

Legend for Valuation Methods:
Adjusted LAC = Latest Acquisition Cost, adjusted for holding gains and losses; NRV = Net Realizable Value; MAC = Moving Average Cost

Restrictions

The DLA has restrictions of $5.4 million related to inventory in litigation. Inventory in litigation (condition code L) is materiel held pending litigation or negotiation with contractors or common carriers, and remains in condition code L until negotiated or settled.

General Composition of Inventory

The DLA inventory is comprised of NonEnergy Supply and Energy Supply. The NonEnergy Supply inventory consists of commodity based supply chains and is reported in the Enterprise Business System (EBS). Energy Supply is reported in Business System Modernization - Energy (BSM-E).

NonEnergy Supply consists of Troop and Weapon Systems Support supply chains. Troop Support supply chains include Clothing and Textiles; Construction and Equipment; Medical; and Subsistence. Weapon Systems inventory includes repair parts for the Aviation and the Land and Maritime supply chains.

Energy Supply inventory consists of jet fuels, aviation gasoline, automotive gasoline, heating oils, power generation, naval propulsion fuels, lubricants, and missile propellants.

Table 1: Total Gross Value of Purchased and Available Materiel for Resale by System

Table 1 ($ millions)

Systems	Inventory Gross Value	Valuation Method
EBS	$ 12,949	Moving Average Cost (MAC)
BSM-E	$ 8,665	Transactional First-In, First-Out (FIFO)
Legacy	$ 5	Moving Average Cost (MAC)
Legacy	$ 1	Latest Acquisition Cost (LAC)
Total	$ 21,620	

Decision Criteria for Identifying the Category to which Inventory is assigned:

The Office of the Under Secretary of Defense (Comptroller) (OUSD(C)) established a condition code crosswalk as stated in the memorandum, "Accounting for Excess, Unserviceable, and Obsolete Inventory and Operating Materials and Supplies" in order to standardize DoD reporting of the categories. The categories and condition codes are:

Inventory Category	Condition Code
Serviceable	A, B, C, D
Unserviceable	E, F, G, H, J, K, L, M, N, R
Excess, Obsolete, Unserviceable	H, P, S

Minimum Inventory Levels

The DLA maintains congressionally mandated minimum levels of specific inventory items. These items are not necessarily restricted on use, rather these are mandated minimum levels for DLA, which drive fluctuations in the DLA inventory levels. The Meals Ready to Eat (MRE) has a congressionally mandated level of 5.1 million cases. In addition, MRE have a disaster reserve level of 230 thousand cases for use by the Federal Emergency Management Agency, Department of Homeland Security.

Petroleum inventories are comprised mostly of products with military specification and are stocked primarily to meet wartime operation plans and to ensure that DLA has sufficient stocks in place to minimize any risk to the warfighter. Wartime petroleum requirements are calculated by Military Services and coordinated with Combatant

Commanders. The DLA's Energy Supply then works with the Combatant Commanders to position those stocks where space permits and within the funded volumes. The current wartime stockage objective is 34.5 million barrels (mbbls). Peacetime bulk petroleum inventory requirements are calculated by Energy Supply in accordance with guidelines provided by OUSD(C), and are positioned by Energy Supply prior to placing war reserve inventories. The peacetime objective is 25.7 mbbls. These inventories are not physically segregated in tankage, meaning that wartime (appropriated funded) stocks can be used to meet peacetime (working capital funded) requirements.

Note 10. General PP&E, Net

As of September 30	2008					2007
	Depreciation / Amortization Method	Service Life	Acquisition Value	(Accumulated Depreciation / Amortization)	Net Book Value	Prior FY Net Book Value
(Amounts in thousands)						
Major Asset Classes						
Buildings, Structures, and Facilities	S/L	20 or 40	$ 1,907,449	$ (1,253,979)	$ 653,470	$ 697,357
Software	S/L	2-5 or 10	1,352,953	(523,504)	829,449	862,123
General Equipment	S/L	5 or 10	650,015	(399,640)	250,375	246,035
Construction-in-Progress	N/A	N/A	155,563	N/A	155,563	132,907
Total General PP&E			$ 4,065,980	$ (2,177,123)	$ 1,888,857	$ 1,938,422

Legend for Valuation Methods:
S/L = Straight Line N/A = Not Applicable

Restrictions

There are no restrictions on the use or convertibility of General Property, Plant and Equipment (General PP&E) except for heritage assets.

Heritage Assets and Stewardship Land

Statement of Federal Financial Accounting Standards No. 29, Heritage Assets and Stewardship Land, requires note disclosures for PP&E that are unique because of historical or natural significance; cultural, educational, or artistic (e.g. aesthetic) importance; or significant architectural characteristics. The DLA's policy is to preserve and account for its heritage assets. The DLA's heritage assets consist of a building, a monument, and cemeteries. The DLA has no stewardship land. The DLA's heritage assets are resources that are managed to provide multiple use activities for the public benefit to include compliance with required federal laws, executive orders, Department of Defense policies, final governing standards and other binding agreements.

The DLA heritage assets include: (1) an early nineteenth century plantation house which the Defense Supply Center Richmond (DSCR) operates and serves as the DSCR Officer's Club and is listed in the National Register, (2) a Native American monument which was jointly established by DSCR and a local Native American organization to honor Native American culture, and (3) two cemeteries located at DSCR which DLA has administrative and curatorial responsibilities.

Assets Under Capital Lease

As of 4th Quarter, FY 2008, DLA did not have any leases that met the capitalization threshold. Refer to Note 1Q, General Property, Plant and Equipment, for further details.

Note 11. Liabilities Not Covered by Budgetary Resources

As of September 30	2008	2007
(Amounts in thousands)		
Intragovernmental Liabilities		
Other	$ 25,596	$ 10,120
Total Intragovernmental Liabilities	$ 25,596	$ 10,120
Nonfederal Liabilities		
Military Retirement and Other Federal Employment Benefits	236,427	235,596
Environmental Liabilities	25,102	22,249
Other Liabilities	13,234	17,690
Total Nonfederal Liabilities	$ 274,763	$ 275,535
Total Liabilities Not Covered by Budgetary Resources	$ 300,359	$ 285,655
Total Liabilities Covered by Budgetary Resources	$ 3,488,149	$ 3,078,297
Total Liabilities	$ 3,788,508	$ 3,363,952

Liabilities Not Covered by Budgetary Resources are liabilities for which congressional action is needed before budgetary resources can be provided. The DLA Working Capital Fund current year liabilities not covered by budgetary resources are primarily comprised of actuarial Federal Employees Compensation Act (FECA) benefits. The FECA liability is for actuarial cost projections, and therefore is unfunded. The environmental liabilities are estimates related to future events and therefore are unfunded.

Composition of Other Lines

Intragovernmental Liabilities Other primarily consists of accruals for current year estimated FECA liability and interest on overdue nonfederal accounts receivable that must be remitted to the U.S. Treasury upon receipt.

Nonfederal Liabilities Other includes accruals for unfunded leave and contingent liabilities for contract financing payments.

Military Retirement and Other Federal Employment Benefits

Military Retirement and Other Federal Employment Benefits not covered by budgetary resources are comprised of various employee actuarial liabilities not due and payable during the current fiscal year. These liabilities are comprised of $236.4 million for FECA. Refer to Note 17, Military Retirement and Other Federal Employment Benefits, for additional details and disclosures.

Note 12. Accounts Payable

As of September 30	2008			2007
	Accounts Payable	Interest, Penalties, and Administrative Fees	Total	Total
(Amounts in thousands)				
Intragovernmental Payables	$ 114,351	$ N/A	$ 114,351	$ 90,387
Nonfederal Payables (to the Public)	3,049,438	563	3,050,001	2,751,119
Total	$ 3,163,789	$ 563	$ 3,164,352	$ 2,841,506

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

In FY 2007, the Department recognized accounts payable balances of the Mechanization of Contract Administration Services (MOCAS) system at gross value without reductions for partial, progress payments, and non-accounts payable records overstating accounts payable and expenses. The overstated balances for FY 2007 were undeterminable due to system limitations: therefore no corrections have been made. Balances at FY 2008 are properly reported net of non-accounts payable records, partial and progress payments of $68.8 million.

Note 13. Debt

Not Applicable to DLA Working Capital Fund.

Note 14. Environmental Liabilities and Disposal Liabilities

As of September 30	2008			2007
	Current Liability	Noncurrent Liability	Total	Total
(Amounts in thousands)				
Environmental Corrective Action	$ 23,822	$ 67,672	$ 91,494	$ 72,644
Total Environmental Liabilities	$ 23,822	$ 67,672	$ 91,494	$ 72,644

Environmental Disclosures

The DLA's environmental liabilities (EL) are from current and out-year Remedial Action Cost Engineering and Requirements (RACER) estimates related to DLA's Defense Energy Support Center for 245 sites; 214 sites associated with closure costs, and the remaining 31 are corrected action costs. In August 2007, DLA executed the RACER model and it generated the FY 2008 Cost to Complete (CTC) estimates which are an estimation of anticipated costs necessary to complete environmental restoration requirements. The CTC estimates for the first year plus the unliquidated obligations as of year end equal the current liability. All remaining CTC estimates are categorized as noncurrent liabilities.

The DLA has developed a plan for collecting and reporting EL for NonDefense Environmental Restoration Program (NonDERP) contamination at DLA managed installations including government-owned contractor-operated (GOCO) fuel points and for Service-owned and operated fuel terminals where DLA stores fuel. To obtain the Service-owned fuel terminals data, DLA developed an environmental template that will be provided to the Military Services after the Office of the Under Secretary of Defense (Comptroller) resolves real property record inconsistencies between the Military Services and DLA. This template will be used to populate the Environmental Disclosures table and for the reporting of overseas base EL in the 1st Quarter, FY 2010 financial statement.

Applicable Laws and Regulations for Cleanup Requirements

The DLA is required to clean up contamination resulting from past waste disposal practices, leaks, spills and other prior activities which may have created a public health or environmental risk. The DLA is required to follow the Comprehensive Environmental Response, Compensation, and Liability Act; Resource Conservation and Recovery Act; and the Superfund Amendments and Reauthorization Act to clean up contamination on installations managed by DLA in coordination with regulatory agencies. This cleanup may at times extend beyond installation boundaries onto privately owned property and to sites where DLA is named as a potentially responsible party by a regulatory agency.

Types of Environmental Liabilities and Disposal Liabilities

The DLA has cleanup requirements for NonDERP installations. All cleanup is done in coordination with regulatory agencies, other responsible parties, and current property owners.

Methods for Assigning Estimated Total Cleanup Costs to Current Operating Periods

The DLA uses the RACER model, an independently validated model, to estimate environmental costs. The DLA validates the model in accordance with Department of Defense (DoD) Instruction 5000.61 and primarily uses the model to estimate the liabilities based on data received during a preliminary assessment and initial site investigation.

The DLA provides RACER estimated NonDERP costs associated with General Property, Plant, and Equipment (General PP&E). Initial data on the environmental cost linked to General PP&E was gathered during FY 2006 and is the basis for the development, implementation, and reporting.

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

The DLA had changes in estimates resulting from changes in site conditions, changes in recent groundwater modeling data, better site characterization and improved analysis by program managers. The EL are expected to fluctuate due to changes in agreements with regulatory agencies, deflation, inflation, and technology. The FY 2008 CTC has incorporated the DoD inflation factors into the NonDERP closure estimates. The latest version of RACER (2008 version 10.0.2) was used to rebaseline estimates.

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

The EL for DLA are based on accounting estimates and assumptions that are believed to be reasonable based upon information available at the time of the RACER calculation. The actual results may materially vary from the accounting estimates if agreements with the regulatory agencies require different remediation than anticipated at the time of the calculation. The liabilities can be further impacted if further investigation of the environmental sites discloses contamination different than known at the time of the estimate.

Although DLA has instituted extensive controls to ensure that these estimates are accurate and reproducible, they are generally considered accurate at +/- 20%. This percentage is supported by a 2004 RACER validation. RACER is currently undergoing another validation that will provide updated supporting statistical analysis. The stated noncurrent liability is an estimate of future liabilities, as the majority of DLA sites will require cleanup for up to 30 years. Estimates for work that are more than 1 to 2 years in the future may be subject to significant change.

Liability for Overseas Bases

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

Note 15. Other Liabilities

As of September 30	2008			2007
	Current Liability	Noncurrent Liability	Total	Total
(Amounts in thousands)				
Intragovernmental				
Advances from Others	$ 24,642	$ 0	$ 24,642	$ 21,932
FECA Reimbursement to the Department of Labor	7,030	22,997	30,027	30,823
Custodial Liabilities	2,580	0	2,580	3,099
Employer Contribution and Payroll Taxes Payable	11,180	0	11,180	8,903
Total Intragovernmental Other Liabilities	$ 45,432	$ 22,997	$ 68,429	$ 64,757
Nonfederal				
Accrued Funded Payroll and Benefits	$ 183,675	$ 0	$ 183,675	$ 161,665
Advances from Others	17,052	0	17,052	17,578
Deposit Funds and Suspense Accounts	9,929	0	9,929	(55,809)
Accrued Unfunded Annual Leave	8,208	0	8,208	7,064
Contract Holdbacks	53	225	278	1,730
Employer Contribution and Payroll Taxes Payable	13	0	13	619
Contingent Liabilities	5,026	3,626	8,652	16,601
Total Nonfederal Other Liabilities	$ 223,956	$ 3,851	$ 227,807	$ 149,449
Total Other Liabilities	$ 269,388	$ 26,848	$ 296,236	$ 214,206

Abnormal Balance

In 4th Quarter, FY 2007, Document Automation and Production Service (DAPS) had a long standing abnormal balance in Deposit Funds and Suspense Accounts that was created when the Navy Printing Service (now DAPS) transferred to DLA from the Navy. In November 2007, the Office of the Under Secretary of Defense (Comptroller) (OUSD(C)) authorized a net adjustment of $45.0 million to clear the abnormal balance.

Contingent Liabilities

Contingent Liabilities include $3.6 million in estimated future contract financing payments that will be paid to the contractors upon delivery and Government acceptance. In accordance with contract terms, specific rights to the contractor's work vests with the Government when a specific type of contract financing payment is made. This action protects taxpayer funds in the event of contract nonperformance. These rights should not be misconstrued as the rights of ownership. The DLA is under no obligation to pay the contractor for amounts greater than the amounts authorized in the contract until delivery and Government acceptance. Because it is probable that the contractor will complete its efforts and deliver a satisfactory product to DLA and the amount of potential future payments is estimable; DLA has recognized a contingent liability for estimated future payments, which are conditional pending delivery and Government acceptance.

Note 16. Commitments and Contingencies

The DLA is a party in various administrative proceedings and legal actions, with claims including environmental damage claims, equal opportunity matters, and contractual bid protests.

The DLA has accrued contingent liabilities for legal actions where our Office of General Counsel (OGC) considers an adverse decision probable and the amount of loss is measurable. In the event of an adverse judgment against the Government, some of the liabilities may be payable from the Judgment Fund. The DLA records Judgment Fund liabilities in Note 12, "Accounts Payable," and Note 15, "Other Liabilities."

The DLA has a reasonably possible loss contingency of $673.0 thousand. This contingency is from six cases in which the OGC is the party. The DLA's Case Management System (CMS) is used by OGC to project the outcome and value of open cases. The CMS projects a minimum liability of approximately $673.0 thousand and a maximum liability of approximately $11.0 million.

The DLA Working Capital Fund does not have undelivered orders related to cancelled appropriations for contractual commitments.

Environmental Contingencies

The DLA has developed a process to identify and record contingent environmental liabilities. Where DLA is aware of any pending environmental claims, the appropriate program category will be reported in Note 14, Environmental Liabilities. If the Judgment Fund is responsible for a portion of claims for settlement, an imputed financing amount (i.e. paid on the agency's behalf) will be reflected only for the amount to be paid by the Judgment Fund on behalf of DLA.

Potential Loss Related to Economic Price Clause Contracts

The DLA is involved in litigation in the U.S. Court of Federal Claims regarding the use of economic price adjustment clauses in fuels contracts awarded from 1982 through 1999. The DLA continues to believe that the use of such clauses was proper and in accordance with law. In previous financial statements, DLA reported 27 cases challenging economic price adjustment clauses. The value of these cases was approximately $3 billion, and DLA disclosed the potential liability in the footnotes to the financial statements. Since that time, DLA's OGC has determined an outflow of cash associated with these cases is remote.

In April 2005, the U.S. Court of Appeals ruled in the Tesoro Hawaii and Hermes cases that the Defense Energy Support Center's economic price adjustment clauses are authorized by the Federal Acquisition Regulation. The court's decision is precedent and applies to the remaining 25 cases pending in the U.S. Court of Federal Claims. However, plaintiffs in many of these cases pursued alternative theories, meaning that the cases were not yet finished. In September 2007, the U.S. Court of Appeals upheld the August - September 2006 dismissal of a number of these alternative theories by three U.S. Court of Federal Claims judges. The U.S. Court of Appeals decision is precedent for other cases and all but one of the plaintiffs has abandoned these cases. That one plaintiff has not yet determined whether it intends to proceed despite the precedent now against it.

Contingencies that are considered both measurable and probable have been recognized as liabilities. Refer to Note 15, Other Liabilities, for further details.

Note 17. Military Retirement and Other Federal Employment Benefits

As of September 30	2008				2007
	Liabilities	Assumed Interest Rate (%)	(Less: Assets Available to Pay Benefits)	Unfunded Liabilities	Liabilities
(Amounts in thousands)					
FECA	$ 236,426		$ 0	$ 236,426	$ 235,596
Total Other Actuarial Benefits	$ 236,426		$ 0	$ 236,426	$ 235,596
Total Military Retirement and Other Federal Employment Benefits:	$ 236,426		$ 0	$ 236,426	$ 235,596

Actuarial Calculations

The DLA actuarial liability for workers' compensation benefits is developed by the Department of Labor's (DOL) Employment Standards Administration and provided to DLA at the end of each fiscal year. The liability includes the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases. The liability is determined using a method that utilizes historical benefit payment patterns to predict the ultimate payments. The projected annual benefit payments are then discounted to the present value using the Office of Management and Budget's (OMB) economic assumptions for 10-year U.S. Treasury notes and bonds. Cost of living adjustments (COLAs) and medical inflation factors are also applied to the calculation of projected future benefits.

Actuarial Cost Method and Assumptions

The liability for future workers' compensation benefits includes the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases, plus a component for incurred but not reported claims. The liability is determined using a method that utilizes historical benefit payment patterns related to a specific incurred period to predict the ultimate payments related to that period. Consistent with past practice, these projected annual benefit payments have been discounted to present value using OMB's economic assumptions for 10-year U.S. Treasury notes and bonds. Interest rate assumptions utilized for discounting are as follows:

4.368% in Year 1
4.770% 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 (COLAs) and medical inflation factors (Consumer Price Index Medical (CPIMs)) were applied to the calculation of projected future benefits. These factors were also used to adjust the methodology's historical payments to current year constant dollars. The compensation COLAs and CPIMs used in the projections for various charge back years (CBY) were as follows:

CBY	COLA	CPIM
2008	3.03%	4.71%
2009	3.87%	4.01%
2010	2.73%	3.86%
2011	2.20%	3.87%
2012	2.23%	3.93%
2013+	2.30%	3.93% 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 loses per case (a measure of case-severity) in CBY 2008 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 2008 projection to the average pattern for the projections for the most recent three years.

Programs Upon Which Actuarial Calculation are Based (Retirement Systems)

The DLA interacts with, and is dependent upon the financial activities of the Federal Government as a whole. The DLA's civilian employees participate in the Civil Service Retirement System (CSRS) and the Federal Employees Retirement System (FERS) while the Military Retirement System (MRS) covers military personnel. Additionally, personnel covered by FERS and MRS also have varying coverage under Social Security. The DLA finances only a portion of the civilian pensions. While reporting and funding civilian pensions under CSRS and FERS is the responsibility of Office of Personnel Management, DLA recognizes an imputed expense for the portion of civilian employee pension's benefit on the Statement of Net Cost. The DLA also recognizes corresponding imputed revenue from the civilian employee pension's benefit on the Statement of Changes in Net Position.

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

As of September 30	2008	2007
(Amounts in thousands)		
Intragovernmental Costs	$ 1,603,792	$ 1,285,443
Public Costs	39,416,472	34,301,560
Total Costs	$ 41,020,264	$ 35,587,003
Intragovernmental Earned Revenue	$ (36,331,341)	$ (30,251,340)
Public Earned Revenue	(6,456,684)	(5,896,738)
Total Earned Revenue	$ (42,788,025)	$ (36,148,078)
Net Cost of Operations	$ (1,767,761)	$ (561,075)

Intragovernmental costs and revenue are related to transactions made between two reporting entities within the Federal Government. Public costs and earned revenues are exchange transactions made between the reporting entity and a nonfederal entity.

The DLA's systems do not track all intragovernmental transactions by customer at the transaction level. Therefore, internal Department of Defense buyer-side balances are adjusted to agree with internal seller-side balances for revenue. Expenses were adjusted by reclassifying amounts between federal and nonfederal expenses.

The Statement of Net Cost (SNC) represents the net cost of programs and organizations of the Federal Government 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 Department'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 Department 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".

The amounts presented in this statement do not meet accounting standards and are based on budgetary obligations, disbursement 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 DLA accounting systems do not capture information relative to heritage assets separately and distinctly from normal operations. Where it was able to separately identify the cost of acquiring, constructing, improving, reconstructing, or renovating heritage assets, DLA has identified $26.9 thousand for the fiscal year.

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

Composition of Other Lines

Unexpended Appropriations: Other Adjustments (Rescissions, etc) consists of a specified reduction (rescission) directed in Section 8003 of the Supplemental Appropriations Act of 2008, Public Law 110-252.

Note 20. Disclosures Related to the Statement of Budgetary Resources

As of September 30	2008	2007
(Amounts in thousands)		
Net Amount of Budgetary Resources Obligated for Undelivered Orders at the End of the Period	$ 17,330,117	$ 13,743,356
Total	$ 17,330,117	$ 13,743,356

Abnormal Balance

Unobligated balance brought forward, October 1, 2007, shows an abnormal balance of $23.8 million. This abnormal balance exists because prior to 4th Quarter, FY 2003, Document Automation and Production Service (DAPS) processed its budgetary reports as if contract authority was used for operating authority. The use of contract authority accounting was determined to be incorrect and an adjustment was made at year end in FY 2003, resulting in an abnormal balance in Unobligated Balance. The remaining abnormal balance of $23.8 million was resolved in 4th Quarter, FY 2008, by a cash transfer from NonEnergy Supply to DAPS.

Apportionment Categories for Obligations

The DLA had apportionment category B reimbursable obligations totaling $48.2 billion.

Other Disclosures

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

The DLA received direct appropriations totaling $343 million during FY 2008. These amounts are comprised of $303 million in the DESC area for increased fuel costs, $23 million in the Non-Energy area to finance the Reutilization, Transfer, and Disposal program and a share of the Defense Finance and Accounting Service systems costs, $12 million in the DDC area for GWOT Theatre Distribution shipping point costs, and $5 million in the DRMS area for GWOT operations.

Note 21. Reconciliation of Net Cost of Operations to Budget

As of September 30	2008	2007
(Amounts in thousands)		
Resources Used to Finance Activities:		
Budgetary Resources Obligated:		
Obligations incurred	$ 48,205,128	$ 36,936,465
Less: Spending authority from offsetting collections and recoveries (-)	(43,677,234)	(36,299,054)
Obligations net of offsetting collections and recoveries	4,527,894	637,411
Net Obligations	$ 4,527,894	$ 637,411
Other Resources:		
Donations and forfeitures of property	0	2,710
Transfers in/out without reimbursement (+/-)	1,417,932	(782,613)
Imputed financing from costs absorbed by others	141,890	151,721
Net Other Resources Used to Finance Activities	$ 1,559,822	$ (628,182)
Total Resources Used to Finance Activities	$ 6,087,716	$ 9,229
Resources Used to Finance Items not Part of the Net Cost of Operations:		
Undelivered Orders (-)	(3,586,762)	(3,231,660)
Unfilled Customer Orders	716,880	1,797,778
Resources that fund expenses recognized in prior Periods (-)	(9,363)	(76,984)
Resources that finance the acquisition of assets (-)	(36,406,594)	(26,984,654)
Other (+/-)	(1,417,931)	779,903
Total Resources Used to Finance Items not Part of the Net Cost of Operations	$ (40,703,770)	$ (27,715,617)
Total Resources used to Finance the Net Cost of Operations	$ (34,616,054)	$ (27,706,388)

Reconciliation of Net Cost of Operations to Budget (Continued):

As of September 30	2008	2007
(Amounts in thousands)		
Components of Net Cost of Operations that will not Require or Generate Resources in the Current Period:		
Components Requiring or Generating Resources in Future Periods:		
Increase in annual leave liability	$ 1,230	$ 314
Increase in environmental and disposal Liability	18,850	0
Other (+/-)	20,504	0
Total Components of Net Cost of Operations that will Require or Generate Resources in future periods	$ 40,584	$ 314
Components not Requiring or Generating Resources:		
Depreciation and amortization	$ 197,221	$ 175,395
Revaluation of assets or liabilities (+/-)	(200,007)	(1,246,091)
Cost of Goods Sold	32,784,825	28,237,383
Other	25,670	(21,688)
Total Components of Net Cost of Operations that will not Require or Generate Resources	$ 32,807,709	$ 27,144,999
Total Components of Net Cost of Operations that will not Require or Generate Resources in the Current Period	$ 32,848,293	$ 27,145,313
Net Cost of Operations	$ (1,767,761)	$ (561,075)

The Reconciliation of Net Cost of Operations to Budget provides information on the total resources used by DLA - both those received through the budget and those received by other means. It reconciles the budgetary obligations incurred to the net cost of operation for a given reporting period. It articulates and details the relationship between net obligations from budgetary accounting and net cost of operations from proprietary accounting.

Due to DLA's financial system limitations, budgetary data is not in agreement with proprietary expenses and assets capitalized. The difference between budgetary and proprietary data is a previously identified deficiency.

The reconciliation requires that adjustments be processed because of imbalances between the budgetary and proprietary amounts recorded in DLA's accounting systems. The balancing entries for DLA include adjustments of $307 thousand to Other Components Not Requiring or Generating Resources. These adjustments were required in order to bring the reconciliation into agreement with the Statement of Net Cost (SoNC).

The following note schedule 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

Composition of Other Lines

Resources Used to Finance Items Not Part of Net Cost of Operations: Other consists of the end of quarter Fund Balance with Treasury (FBWT) that is transferred to or from Defense-Wide Working Capital Fund (DWWCF) component level, where the DWWCF FBWT is managed. Refer to Note 1.I., Significant Accounting Policies, Funds with the U.S. Treasury, for further details and disclosures.

Components Requiring or Generating Resources in Future Period: Other consists of contingent legal liabilities and future funded FECA liability and expense.

Components Not Requiring or Generating Resources: Other is comprised of changes in the allowance for bad debt, miscellaneous expenses that did not require budgetary resources and to record the note schedule to SoNC budgetary adjustment.

Note 22. Disclosures Related to Incidental Custodial Collections

Not Applicable to DLA Working Capital Fund.

Note 23. Earmarked Funds

Not Applicable to DLA Working Capital Fund.

Note 24. Other Disclosures

Not Applicable to DLA Working Capital Fund.

Note 25. Restatements

Not Applicable to DLA Working Capital Fund.

DEFENSE LOGISTICS AGENCY

WORKING CAPITAL FUND

Required Supplementary Information

For the Fiscal Year Ended September 30, 2008

HERITAGE ASSETS

For Fiscal Year Ended September 30, 2008

Heritage Asset Categories	Measurement Quantity	As of 10/01/07	Additions	Deletions	As of 09/30/08
Buildings and Structures	Each	4			4
Archeological Sites	Each	NA			NA
Museum Collection Items (Objects, Not Including Fine Art)	Each	NA			NA
Museum Collection Items (Fine Art)	Each	NA			NA

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

The Defense Supply Center–Richmond (DSCR) operated and maintained four distinct heritage assets during the year: the Bellwood Home, an early nineteenth century plantation house that is listed in the National Register and served as the Officer's Club; a monument to honor the Native American culture; and two cemeteries (one containing the remains of African Americans and the other was used by the Gregory family, a family that owned the property prior to its acquisition by the U. S. Government).

The fiscal year 2008 categories are defined as follows:

Buildings and Structures

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

Archeological Sites

Sites that have been identified, evaluated, and determined to be eligible for or are listed on the National Register of Historic Places.

Museum Collection Items

Items which are unique for one or more of the following reasons: historical or natural significance; cultural, educational or artistic importance; or significant technical or architectural characteristics. Museum collection items are divided into two subcategories: fine art and objects. Fine art includes paintings, sculptures and other three dimensional art. Objects are current use, excess, obsolete, or condemned material; war trophies; personal property such as uniforms, medals, or diaries, and military equipment.

REAL PROPERTY DEFERRED MAINTENANCE

For Fiscal Year Ended September 30, 2008 (In Millions)

Property Type	**Current Fiscal Year (CFY)**		
Buildings, Structures, and Utilities	Plant Replacement Value	Required Work (Deferred Maintenance)	Percentage
Enduring Facilities	$12,822	$135	1.05 %
Excess Facilities or Planned for Replacement	NA	NA	NA
Heritage assets	NA	NA	NA

Deferred maintenance is maintenance that was not performed when it should have been or was scheduled to be and which, therefore, is delayed for a future period. The amount of real property deferred maintenance is based upon facility Q-ratings found in DLA's real property inventory that represents the cumulative deferred amount for facility restoration and modernization.

Plant Replacement Value (PRV) is the cost of replacing the existing constructed asset at today's standards (adjusted by a local area cost factor). PRV includes overhead costs such as planning and design, supervision and inspection.

The Q-ratings represent work needed to bring a facility to a fully serviceable condition with no repair needs. Reported deferred maintenance is the difference between the facility Q rating and the target Q rating, representing the acceptable operating condition. The low value is the mid-point of the Q-2 rating band, representing deferred work valued at 15% of the facility's replacement value. This point equates to DOD's minimum goal for average facility condition. The high value is fully serviceable condition, representing a facility with no deferred requirements.

The DLA employs various methodologies to assess facility conditions, from detailed building inspections by engineers and technicians, to occupant surveys, to computer systems that model estimated condition. The DLA conducts periodic, on-site facility inspections by qualified engineering staff for a sufficient sample of facilities to gain "benchmark" data to validate the condition assessment methodology as being consistent, repeatable and accurate within the Q-Rating bands.

Q-Rating Bands: Bands that allow DLA to group facilities by condition for the purposes of developing investment strategies.

Band	Calculated Rating	Descriptions of the Bands
"Q-1"	100% to 90%	Good condition
"Q-2"	89% to 80%	Fair condition
"Q-3"	79% to 60%	Poor condition
"Q-4"	59% to 0%	Failing condition

Facility Categories are as follows:

- Category 1 Facilities: enduring facilities required to support an ongoing mission including multi-use Heritage Assets.
- Category 2 Facilities: facilities excess to requirements, or planned for replacement or disposal including multi-use Heritage Assets.
- Category 3 Facilities: heritage assets (building and structure).

DEFENSE LOGISTICS AGENCY

WORKING CAPITAL FUND

Supply Management Activity Group Overview

For the Fiscal Year Ended September 30, 2008

SUPPLY MANAGEMENT ACTIVITY GROUP

The Supply Management Activity Group consists of three supply centers, one support center, two service centers, and several support organizations. The supply centers are located at the Defense Supply Center Columbus (DSCC) in Columbus, OH; the Defense Supply Center Richmond (DSCR) in Richmond, VA; and the Defense Supply Center Philadelphia (DSCP) in Philadelphia, PA. DLA supports its Military Service customers by managing supply chain business processes that ensure worldwide logistics support is provided at the right time, to the right place, and consistently at the best value in peacetime, emergency, and wartime scenarios. Each supply center acts as a supply chain lead for one or more commodity groups. Each commodity group contains common suppliers, similar items, and to some extent, similar customers. They are formed to improve alignment with industry and customers. The seven supply chains at these three centers include: aviation, land, and maritime (associated with weapon system spare parts and related consumable materiel), construction and equipment, food, clothing and textiles, and medical. The Defense Energy Support Center (DESC), which is located at Fort Belvoir, VA, purchases, manages, positions, and sells fuel to the Military Services and provides centralized energy supply chain support to meet the energy needs of the military installations. The service centers are: the Defense Logistics Information Service, located in Battle Creek, MI, which manages the Federal Supply Catalog System and provides logistics information products and services for all military and civilian activities; and the Defense Automatic Addressing System Center, located in Dayton, OH, which provides support to DLA's logistics mission by editing and routing electronic logistics transactions (including maintaining the addresses of customers and suppliers), maintaining network interoperability for the logistics community, and conducting special services and reports.

During FY 2008, DLA supported more than 1,500 different weapon systems and managed fuel that generated sales of 132.5 million barrels. By year's end, there were 7,995 civilian, 221 active duty military, and 205 military reserve personnel that supported this business area. The Supply Management Activity Group generated revenue which totaled about $40.7 billion during FY 2008. This was an increase of $7.0 billion from the previous year.

MISSION

The Supply Management Activity Group's mission is to provide materiel and logistics services that support peacetime and combat operations, combat preparedness, emergency support, and humanitarian aid. These services include the integrated materiel management of more than 5.2 million items that support the eight separate supply chains. The support requirements are dynamic, and DLA continues to adjust its approach in response to evolving changes in national priorities, requirements of the Military Services, technology, and the commercial marketplace.

The primary logistics functions include:

- **Supply-chain integration and inventory management;**
- **Transportation management (shared with the Distribution Activity Group);**
- **Technical management, which guarantees product quality and proper pricing of materiel;**
- **Procurement management, ensuring DoD gets the best value;**
- **Logistics data and information collection, management, and distribution and providing for the integration and availability of this information; and**
- **Logistics management process and processing of logistics and standard Military Logistics Systems transactions.**

STRATEGIC GOALS

The long-term goals of the Supply Management Activity Group are consistent with those in the DLA Strategic Plan. By achieving these goals, DLA will ensure that the supplies and services required by its customers are procured and delivered in the most effective and efficient manner and that these services reflect the customers' concerns for timeliness, quality, and cost. These goals will be achieved through a series of supporting strategies and executed primarily by the supply centers.

PROGRAM INITIATIVES AND ACCOMPLISHMENTS

Supplier Relationship Management (SRM): SRM is a major transformation effort, which encompasses all of the Agency's supplier facing initiatives. The focus of SRM is to forge new relationships and enhance the quality of existing business relationships. These enhanced relationships between DLA and its suppliers will allow the Agency to achieve the underlying goal of having "the right item, right service, right place, right time…every time." Consequently, SRM will affirm DLA as an integral partner in the end-to-end supply chain that links our suppliers to our customers. Detailed below are some of the key initiatives within SRM including Strategic Materiel Sourcing (SMS), Warstopper Program, Strategic Supplier Alliances (SSAs), Supply Chain Alliances (SCAs), and Performance-Based Logistics (PBL):

- **Strategic Materiel Sourcing (SMS):** SMS focuses on stratifying and satisfying customer driven high demand and readiness hardware items – 335,715 of the more than 3 million hardware items managed by DLA - through long-term agreements. While the targeted SMS items make up only about 8% of the DLA managed hardware items, they account for 88% of its hardware procurement actions and 87% of sales. The primary performance measurement of the SMS program is inventory savings. Since the inception of this program, DLA has realized over $231.8 million in one-time inventory savings. DLA currently has 118,839 items under SMS long-term agreements. These agreements include Prime Vendor Agreements, Corporate Contracts, and standard Long-Term Contracts.

- **Warstopper Program:** This program recognizes that peacetime demand for certain items is inadequate to sustain an industrial base sufficient for readiness and mobilization. Consequently, extra preparedness measures are required for those items, and that critical industrial capabilities must be preserved to support the Department's readiness and sustainment requirements. In most cases, the Warstopper Program preserves essential production capability by investing in industry responsiveness to a projected surge requirement in lieu of procuring the materiel or items without purchasing, storing, and managing a finished goods inventory. This concept applies to items such as chemical protective suits, nerve agent antidote auto-injectors, meals-ready-to-eat, and tray pack assemblies. The most recent return on investment (ROI) analysis for the program indicates that from 1993 through 2008 the Warstopper program has offset over $3.9 billion in War Reserve Materiel inventory purchases - a return on investment of more than 7:1.

- **Strategic Supplier Alliances (SSAs):** SSAs are long-term partnerships - formed with DLA's key suppliers - that allow the Agency and the supplier to work together by sharing information and jointly working problem areas. The result is added value for both parties and improved support to the warfighters. There are currently 28 SSAs and each is assigned to a Supplier Relationship Manager, whose primary responsibility is the maintenance and success of the partnership.

- **Supply Chain Alliances (SCAs):** An outgrowth of the SSA initiative, SCAs are alliances with key suppliers who provide competitive items. SCAs further the goals of the SRM transformation effort by adding value to both DLA and the supplier. To date, DLA has formed SCAs with 22 suppliers. To assist these suppliers with their operational planning, DLA provided them with a tool, the Supplier Requirements Visibility Application (SRVA), which forecasts 24 months of requirements for both competitive and sole source items. This initiative is essential in achieving the DLA objective of linking supply with demand.

- **Performance-Based Logistics (PBL):** PBLs are: 1) the preferred contract method to support weapon systems; 2) mandatory for all new major systems and for fielded Acquisition Category (ACAT) I and II systems; and 3) expected to increase support to warfighters through increased materiel availability, improved reliability, and enhanced obsolescence management. The strategy is to increase partnering with PBL Product Support Integrators (PSI) as a Product Support Provider; expand DLA capability to be the selected PSI in support of Military Services PBL initiatives; and to leverage DoD buying power through existing Strategic Supplier Alliances, Supply Chain Alliances, and other related DLA initiatives. DLA sold almost $187.3 million worth of materiel in FY 2008 through its 17 active PBL partnerships where the majority of those sales were obtained from commercial vendors (who were awarded Military Service PBL contracts and then utilized DLA as a source of supply for consumable items). DLA expects to fully execute 14 more PBL arrangements by FY 2011.

Chemical Management Services (CMS): Championed by the Assistant Deputy Under Secretary of Defense for Supply Chain Integration - CMS is a DoD enterprise-wide and cradle-to-grave initiative designed specifically to manage hazardous materiel (hazmat), reduce associated hazmat management and disposal costs, and enable DLA to get closer to its customers. It is a strategic, long-term relationship where either the service provider or supplier manages a customer's chemical-related services. While initially developed to meet the needs of Military Service industrial complexes, CMS is fully capable of managing hazmat down to the tactical retail levels, and will incorporate the best business practices of DLA's Tailored Prime Vendor initiatives. These best business practices will also include many of those developed and used to execute the National Inventory Management Strategy (NIMS), Joint Environmental Materiel Management Service (JEMMS), and the Base Realignment and Closure supply, storage, and distribution concepts. DLA is collaborating with the Navy to transition the JEMMS Center in Okinawa to CMS and extend this service to Guam by late FY 2009. DLA will award and mange the contract for this initiative and - as the strategy becomes more fully integrated into DLA's business models – achieve benefits to include reduced wait times for customers, higher levels of DLA supply readiness, more effective and efficient tailored logistics support solutions, better inventory visibility, a more optimized supply chain, and reduced waste/disposal cost. Consequently, these benefits will produce significant cost savings and better utilization of resources.

EBS Customer Support Management (CSM): DLA uses SAP Customer Support Management tools and processes to more deliberately understand warfighter needs and meet customer expectations. DLA began using these standard Enterprise-wide tools and processes for account management, opportunity management, and customer outreach in March 2006. In the following month, analytics and service modules were configured and deployed. System enhancements were periodically deployed during the remainder of 2006 and into 2007. These enhancements improved program reporting, customer outreach, account management, opportunity management, and various other service capabilities. The EBS CSM reached full operational capability in July 2007. Approximately 1,800 DLA employees now use the system and processes to perform customer outreach, manage accounts and customer support opportunities, provide customer service, as well as take advantage of the integrated analytics capability that provides reports for each process.

Client-level Survey: The client-level survey was conducted in 2007 from October to December to evaluate the warfighters' assessment of DLA goods and services and provide feedback for the continued improvement in the delivery of those goods and services. The survey focused on the opinions of strategic-level warfighters (clients) – within the officer/civilian grade of O-6/GS-15 and above – by evaluating enterprise partnerships, reputation, and brand name. The client-level survey was modified slightly based on lessons learned from the 2006 pilot study. Changes included making it slightly shorter by removing duplicity amongst questions, and making it web-enabled to afford respondents added flexibility and time to provide their critical feedback. Specifically, the survey revealed that the overall client-level satisfaction was at 82%, which is consistent with results for similar respondents in the larger overall customer satisfaction survey – conducted from April to July 2007. Additionally, 63% of respondents indicated they would recommend DLA to another unit or colleague. Warfighters cited that the Agency strengths were: delivering well on its commitments; maintaining a relatively good reputation; and providing valuable support. However, this updated client-level survey also revealed a number of customer concerns that require additional in-depth analysis and research. We are assessing these concerns to determine how DLA can best respond to them.

PROGRAM PERFORMANCE INDICATORS

In December 2006, DLA finalized the transition of data from its legacy system (Standard Automated Materiel Management System - SAMMS) to the Enterprise Business System (EBS). This transition enables DLA management greater access to more timely, complete, accurate, and reliable performance and financial data. Consequently, the following metrics are or will soon be available for management decision-making:

- **Perfect Order Fulfillment (POF)** is undergoing development with interim results being displayed internally to DLA via the Fusion Center. Customer-oriented weapon system data is being piloted in coordination with the Marine Corps. POF is the Supply Chain Operations Reference (SCOR) reliability metric; it shows the percentage of orders that are "perfect" in the eyes of the customer – the warfighter. Performance indicators aligned to POF include: Timeliness (materiel and data are delivered to the correct place and on time), Quantity (correct item and quantity are delivered), Quality (materiel is delivered in the correct condition and packaging), and Documentation (correct shipping, compliance and payment documents support the order). The POF metric is expected to be fully developed and deployed during FY 2009.

- **Demand Planning Accuracy (DPA)** measures the degree of accuracy of a demand forecast compared to the actual demand. It is first calculated at the lowest level of detail, the Demand Forecasting Unit (DFU), comprised of a customer and an item of supply. The DFU can be rolled up to compute the DPA for the various and significantly larger customer groups (such as an Enterprise, a Demand Chain, a Customer, etc.). DPA is measured in "lags" or forecasted ahead for set periods of time: Lag 0 (Current Month), Lag 1, 2, 3, 6, 12 & 24 months. Increased demand planning accuracy should result in better customer support and lower inventory investments and holding costs. To this end, DLA is pursuing both top down and bottom up approaches.

- **Procurement Productivity** measures the Supply Chains' response to Purchase Requests (PRs) by awarding either contracts or Purchase Orders and maintaining an acceptable level of backlog, PRs in process. It includes manual awards, automated awards, Long Term Contract (LTC) delivery orders, and cancellations, as measured against the number of PRs in process. The Supply Chains significantly reduce the number of PRs in process from a high of nearly 240,000 in October 2007 to slightly more than 201,000 by the end of FY 2008.

- **Administrative Lead Time (ALT)** is the total time between receipt of a customer order or planned requirement and contract award date. ALT is evaluated by comparing the actual lead time to the historical lead time of record. The actual ALT fluctuated between 31 to 40 days during FY 2008, and as of September 2008 was 35 days. However, by year-end the historical ALT records were still being populated with data and the analysis model was undergoing refinement for use as a decision-making tool.

- **Production Lead Time (PLT)** is the total time between the receipt of award by the vendor and the receipt of 51% of the contract quantity. PLT is evaluated by comparing actual lead time to the historical lead time of record. Actual PLT fluctuated between 56 to 67 days during FY 2008, and as of September 2008 was 67 days. However, by year-end the historical PLT records were still being populated with data and the analysis model was undergoing refinement for use as a decision-making tool.

- **Long Term Contracts (LTCs) Administration:** LTCs are flexible vehicles that remove workload from buyers' desks and provide documented, reduced administrative and production lead times. These reduced lead times allow DLA to reduce inventory investments. The three metrics used for FY 2008 were:

  - **Strategic Materiel Sourcing (SMS) Net National Stock Number (NSN) Growth:** Measured the change in net number of SMS NSNs on LTCs with the goal to increase the overall population on LTCs by 4,705 NSNs. The Supply Chains were able to attain a total of 6,514 NSNs.

  - **SMS LTC Renewals/Lapses:** Measured the timeliness of planned renewals for expiring SMS Hardware NSNs on LTC. The DLA goal was to renew 5,853 NSNs identified on expiring LTCs. DLA achieved 7,524 renewals with 27% unplanned lapses.

  - **LTC Obligation Rate:** Measured the overall success at maintaining coverage and selecting the correct items - and in the right quantities - to be placed on LTC as a percent of total obligations made against items on LTCs during the fiscal year. Because of unplanned lapses, DLA achieved a rate of 59.2% versus a 63.6% goal.

For 2009, the metrics were redefined to improve management and attainment of the goals:

- **Attainment to Plan (ATP):** Identifies the percentage of Purchase Requests and Stock Transport Orders (DLA-owned stock redistribution orders) generated through the supply planning process which meet criteria for quantity, quality, and timeliness. A failure of one or more of these criteria indicates that a problem exists within the supply chain. An increase in ATP demonstrates that supply plans are more reliable and lower safety stock levels (smaller inventory investments) may be possible. Performance objectives will be established once training is taken, trend data elements are determined, and metric testing is completed.

- **LTC Maintenance for Hardware NSNs:** Measures the timely renewals of planned LTCs (expirations and options). This will be a new measure for FY 2009. The goal will be to complete renewals for 26,749 SMS NSNs and 354 Troop Support contracts by the end of FY 2009.

- **SMS Growth:** Measures the increase in total Annual Demand Value (ADV) and Annual Demand Frequency (ADF) of SMS items on LTC. This starts from the FY 2009 baseline of total ADV and ADF for all SMS NSNs on LTC and measures absolute growth or shrinkage from the baseline. Supply Chains will need to target new LTCs to counter shrinkage from planned drops and to grow these values to meet the goals. The Enterprise FY 2009 goals are to increase the ADV baseline (the LTC Obligations) by slightly more than $605 million and decrease the ADF baseline (the manual procurement workload and the investment in inventory) on more than 1.4 million SMS NSNs.

- **Outcome/Selection:** Measures the LTC obligation rate as a percent of total obligations made against items on LTCs (during the fiscal year) as an indicator of the overall success of maintaining LTC coverage for the right items and in the right quantities. The FY 2009 goal for the LTC Obligation rate is 63.3%.

FINANCIAL PERFORMANCE MEASURES

DLA establishes its prices predicated on three primary factors: 1) its current financial position, as determined by the Accumulated Operating Result (AOR); 2) its projected cash position relative to the stated objective; and 3) the estimated expenses that will be incurred to generate the estimated revenue. It is Agency policy to set prices that achieve an AOR of zero over the long-term and maintain cash balances that preclude an Anti-Deficiency Act violation. In addition, not all costs attributed to the business are recovered by the business - imputed costs, depreciation expenses applied to investments funded from General Fund accounts, and the recording of revenue that is for non-expense items (peacetime inventory augmentation, mobilization inventories, and adjustments to the cash position). The Financial Results section below more fully describes DLA achievement during FY 2008.

DLA measures the effectiveness of program budgeting and execution with unit cost performance measures.

The following table depicts the Supply Management unit cost results for the Energy supply chain:

Unit Cost Results	FY 08 Goal	FY 08 Actual
Cost Per Barrel of Fuel	$127.02	$159.10

The total cost per barrel of fuel is comprised of the composite product cost (the acquisition cost of a barrel of petroleum product sold) and the non-product cost (operations costs for fuel services, transportation, storage, and overhead). Even though total non-product costs were lower than planned (primarily facility maintenance and terminal operations costs), this unit cost sill exceeded its goal by $32.08 (a 25% increase). While this increase was slightly affected by an increase in customer demand (sold 132.5 million barrels versus the 130.0 million barrels planned), the more significant impact was the market driven product cost (the composite cost of the refined product, $132.80, was $22.18 per barrel higher than the planned cost, $110.62).

The following table depicts the Supply Management unit cost result for the Non-energy supply chains:

Unit Cost Results	FY 08 Goal	FY 08 Actual
Non-Energy	$.98	$1.02

The Non-Energy unit cost was $1.02, which exceeded the goal by $.04. The actual unit cost was higher than the goal primarily due to concentrated efforts to support the warfighter by improving the availability of the inventory. Other factors that contributed to a higher unit cost were increases to the storage and distribution cost and unplanned credit returns from our customers.

DLA also measured and monitored financial performance of its Non-Energy business segment by comparing the Cost Recovery Rate (CRR) approved in the budget to that which was executed. The CRR is a composite rate that is calculated by dividing its related operating costs by the cost of goods sold; and is used as an aggregate measurement of the costs that DLA incurred to generate a level of sales. The long-term financial goal is to achieve a break-even budget-related accumulated operating result. DLA's composite FY 2008 CRR goal was 14.2%. The actual CRR was 12.3%, which was 1.9% lower than the FY 2008 President's Budget and is attributed to greater than expected Net Sales at the end of the fiscal year and focused efforts to reduce operating costs.

FINANCIAL RESULTS

The Supply Management Net Cost of Operations, which includes costs (military construction depreciation, imputed expenses, and accounting adjustments) not recovered by the Defense-wide Working Capital Fund, reflects a gain of about $2.2 billion. The increase is primarily attributable to the Energy business segment where both sales price and sales quantity increased. Additionally, revenue grew in the Non-Energy area due to greater demand by the Military Services.

DEFENSE LOGISTICS AGENCY
WORKING CAPITAL FUND

Supply Management Consolidated and Combined Financial Statements

As of and for the Years Ended September 30, 2008 and 2007

UNAUDITED

DEFENSE LOGISTICS AGENCY WORKING CAPITAL FUND

Supply Management

Consolidated Balance Sheets
As of September 30, 2008 and 2007
(In Thousands)

	2008	2007
ASSETS (Note 2)		
Intragovernmental:		
Accounts Receivable (Note 5)	$ 566,195	$ 876,414
Other Assets (Note 6)	124,980	124,925
Total Intragovernmental Assets	691,175	1,001,339
Accounts Receivable, net (Note 5)	775,620	482,581
Inventory and Related Property, net (Note 9)	21,614,472	17,511,771
General Property, Plant and Equipment, net (Note 10)	1,241,016	1,265,784
Other Assets (Note 6)	24,124	41,838
TOTAL ASSETS	24,346,407	20,303,313
LIABILITIES (Note 11)		
Intragovernmental:		
Accounts Payable (Note 12)	(13,081)	10,087
Other Liabilities (Note 15 & Note 16)	22,002	13,148
Total Intragovernmental Liabilities	8,921	23,235
Accounts Payable (Note 12)	2,926,476	2,595,024
Military Retirement and Other Federal Employment Benefits (Note 17)	36,737	36,608
Environmental and Disposal Liabilities (Note 14)	91,494	72,645
Other Liabilities (Note 15 & Note 16)	151,240	134,070
TOTAL LIABILITIES	3,214,868	2,861,582
NET POSITION		
Cumulative Results of Operations - Other Funds	21,131,539	17,441,731
TOTAL NET POSITION	21,131,539	17,441,731
TOTAL LIABILITIES AND NET POSITION	$ 24,346,407	$ 20,303,313

The accompanying notes are an integral part of these statements.

UNAUDITED

DEFENSE LOGISTICS AGENCY WORKING CAPITAL FUND

Supply Management

Consolidated Statements of Net Cost
For the Years Ended September 30, 2008 and 2007
(In Thousands) (See Note 18)

	2008	2007
PROGRAM COSTS		
Gross Costs	$ 38,521,641	$ 32,842,943
Less: Earned Revenue	(40,688,814)	(33,674,612)
Net Program Costs	(2,167,173)	(831,669)
NET COST OF OPERATIONS	$ (2,167,173)	$ (831,669)

The accompanying notes are an integral part of these statements.

UNAUDITED

DEFENSE LOGISTICS AGENCY WORKING CAPITAL FUND
Supply Management

Consolidated Statements of Changes in Net Position
For the Years Ended September 30, 2008 and 2007
(In Thousands) (See Note 19)

	2008	2007
CUMULATIVE RESULTS OF OPERATIONS		
Beginning Balances	$ 17,441,731	$ 17,349,180
Budgetary Financing Sources:		
Appropriations used	300,930	470,050
Transfers-in/out without reimbursement (+/-)	(70,000)	(374,904)
Other Financing Sources:		
Donations and forfeitures of property	-	2,710
Transfers-in/out without reimbursement (+/-)	1,208,624	(923,586)
Imputed financing from costs absorbed by others	83,082	86,612
Total Financing Sources	1,522,636	(739,118)
Net Cost of Operations (+/-)	(2,167,173)	(831,669)
Net Change	3,689,808	92,551
Cumulative Results of Operations	21,131,539	17,441,731
UNEXPENDED APROPRIATIONS		
Budgetary Financing Sources:		
Appropriations received	324,700	470,119
Appropriations transferred-in/out (+/-)	-	-
Other adjustments (rescissions, etc.) (+/-)	(23,770)	(69)
Appropriations used	(300,930)	(470,050)
Ending Balances	-	-
NET POSITION	$ 21,131,539	$ 17,441,731

The accompanying notes are an integral part of these statements.

UNAUDITED

DEFENSE LOGISTICS AGENCY WORKING CAPITAL FUND
Supply Management

Combined Statements of Budgetary Resources
For the Years Ended September 30, 2008 and 2007
(In Thousands) (See Note 20)

	2008	2007
BUDGETARY FINANCING ACCOUNTS		
Budgetary Resources:		
Recoveries of prior year unpaid obligations	$ 1,295,464	$ 438,475
Budget Authority		
Appropriation	324,700	470,119
Contract authority	45,853,147	34,623,573
Spending authority from offsetting collections:		
Earned		
Collected	39,484,244	31,967,505
Change in receivables from Federal sources	83,882	147,012
Change in unfilled customer orders		
Advance received	6,039	(98,363)
Without advance from Federal sources	700,733	1,917,961
Subtotal	86,452,745	69,027,807
Nonexpenditure transfer, net, anticipated and actual	(70,000)	(374,904)
Permanently not available	(41,825,063)	(34,467,805)
Total Budgetary Resources	45,853,146	34,623,573
Status Of Budgetary Resources:		
Obligations incurred:		
Reimbursable	45,853,146	34,623,573
Total Status of Budgetary Resources	45,853,146	34,623,573
Change in Obligated Balance:		
Obligated balance, net		
Unpaid obligations, brought forward, October 1	16,141,354	13,127,305
Less: Uncollected customer payments from Federal sources, brought forward, October 1	(7,009,909)	(4,944,936)
Total unpaid obligated balance, net	9,131,445	8,182,369
Obligations incurred, net	45,853,147	34,623,573
Less: Gross outlays	(40,503,152)	(31,171,049)
Less: Recoveries of prior year unpaid obligations, actual	(1,295,464)	(438,475)
Change in uncollected customer payments from Federal sources (+/-)	(784,614)	(2,064,973)
Obligated balance, net end of period		
Unpaid obligations	20,195,884	16,141,354
Less: Uncollected customer payments from Federal sources (+/-)	(7,794,523)	(7,009,909)
Total unpaid obligated balance, net, end of period	12,401,361	9,131,445
Net Outlays:		
Gross outlays	40,503,152	31,171,049
Less: Offsetting collections	(39,490,282)	(31,869,142)
Net Outlays	$ 1,012,870	$ (698,093)

The accompanying notes are an integral part of these statements.

DEFENSE LOGISTICS AGENCY
WORKING CAPITAL FUND

Distribution Activity Group Overview

For the Fiscal Year Ended September 30, 2008

DISTRIBUTION ACTIVITY GROUP

The Distribution Activity Group operates through the Defense Distribution Center (DDC) in New Cumberland, PA, and 26 subordinate distribution centers located throughout the United States, Europe, Pacific, and Southwest Asia. The group's mission is to manage the receipt, storage, and issuance of DoD materiel. It delivers that materiel to customers collocated on a base or to far-off ships, posts, and repair facilities. The activity group uses contracts with commercial sources to transport items from DLA-owned warehouses directly to customers worldwide. Some distribution centers are highly automated facilities that were specifically designed to provide global support for general commodities; while others fill customer requirements on a regional basis or may provide global support for materiel that requires special equipment, facilities, or training. For example, one distribution center - with eleven subordinate satellite operations - provides global support for all map distribution requirements. The distribution centers maintain the accountable inventory records and are responsible for preserving about $99.7 billion (at selling price) in DoD materiel, representing over 3.6 million items. In addition, they processed 22.3 million receipt and issue transactions during FY 2008 and their business services generated more than $1.4 billion in revenue. By year's end this activity group employed 6,718 civilian, 123 active duty, and 180 reserve military personnel.

MISSION

The mission of the Distribution Activity Group is to provide the full range of distribution services and information enabling a seamless, tailored worldwide DoD distribution network that delivers effective, efficient and innovative support to the Combatant Commands, the Military Services and other Agencies during peace and war. The distribution network ensures that America's Warfighters receive competitively priced and best value distribution services by providing "around the clock - around the world," world-class service. The Distribution Activity Group is also responsible for the DLA transportation management functions which support all shipments both the first and second destination points.

STRATEGIC GOALS

The strategic goals established by the Distribution Activity Group are consistent with those contained in the DLA Strategic Plan. These goals are achieved through a series of supporting strategies that will:

- Increase our reliability and value coupled with a faster response time to our customers by continuously improving and reengineering business practices;
- Provide best-value solutions to our customers by continuously evaluating our activities and implementing changes, as necessary, to ensure efficient and effective distribution operations; and
- Reduce under-utilized infrastructure by eliminating unnecessary storage capacity.

PROGRAM INITIATIVES AND ACCOMPLISHMENTS

Infrastructure Cost Reduction through A-76 Cost Comparisons: In FY 1998, DDC began the process of competing DLA depots with private industry. The goal of these competitions is to reduce operating costs either by reengineering existing depot business processes or by inserting the market forces of competition into the distribution functions. As of the end of FY 2008, fifteen competitions have been completed, with the government retaining depot and installation support operations at seven sites, while the other eight were contracted with private industry. One depot completed its second A-76 competition, which was awarded to a contractor. The estimated long-term (FY 1998 - FY 2015) net savings from these 15 competitions is $585 million.

Domestic Disaster Support: As part of the DLA Domestic Disaster Plan to support the Federal Emergency Management Agency (FEMA), the DDC developed distribution initiatives to maintain 100% in-transit visibility of DLA shipped supplies using satellite tracking capability. The DDC established a Defense Transportation Tracking System account to track DDC booked DLA shipments from the commercial vendor and/or distribution center to the FEMA drop-off destination. The DDC also established a Deployable Distribution Depot, with positions battle-rostered and available to respond to domestic disaster situations in the Continental United States (CONUS). This response will be in concert with the coordinated requirements and capabilities of both FEMA and the U.S. Northern Command (USNORTHCOM).

Foreign Disaster Support: Working with the Combatant Commanders' planning staffs, the development of a fully deployable Outside Continental United States (OCONUS) strategic distribution capability is being pursued with the goal of providing: a) wholesale distribution depot capability during contingency operations, b) wholesale support services and in-theater distribution expertise, and c) materiel visibility in a manner similar to existing fixed based forward stocking locations. Conceptually, this would provide a combination of functions and capabilities of both a Theater Consolidation and Shipping Point and a fixed base forward stocking site to meet contingency needs and priorities. Those needs and priorities would include wholesale support services, as well as materiel visibility.

Theater Consolidation and Shipping Points (TCSP) - Kuwait, Europe, Korea, and Sigonella: In FY 2006, DLA accepted the transfer of the Army Theater Distribution Center (TDC) in Kuwait at Camp Arifjan and established the TCSP-Kuwait. The TCSP-Kuwait is the primary conduit for sustaining theater operations by rapidly consolidating or segregating shipments from multiple sources and then preparing and forwarding those shipments directly to the customer. Key features of TCSP-Kuwait include the capability to maintain visibility of the transportation control numbers and asset control. Collectively, these features will allow for the movement of palletized materiel directly from the receiving dock to the shipping dock. The ability to "cross-dock" eliminates the need for any storage or staging and facilitates an efficient transition from inbound to outbound operations. At the request of the Army, DLA established TCSP-Europe (located at Defense Distribution Depot Europe) in September 2006. TCSP-Europe's mission is to rapidly segregate, sort, and consolidate multiple consignee shipments from a range of sources and then deliver those supplies to the customer. These efforts provide both effective and efficient support to the warfighters throughout Europe, Africa, and the Middle East. Thus far, this mission has reduced cost by 20% with a 40% reduction in redundant hub and spoke distribution systems. Based on the successes achieved by both the Kuwaiti and European operations, a TCSP in Korea was established with U.S. Pacific Command (USPACOM) in October 2007; and a TCSP will be established in Sigonella (Rota), Spain. The expansion of the TCSP services in Rota extends the enterprise and delivers supply chain excellence by providing real time capability to enhance warfighter support. This postures the Sigonella Distribution Center to execute the mission as requirements emerge in U.S. Africa Command (USAFRICOM).

Deployment Distribution Operations Center: DLA partnered with the U.S. Transportation Command (USTRANSCOM), the Joint Munitions Command, and the United States Central Command to establish the Deployment Distribution Operations Center (DDOC). Subsequently, USTRANSCOM codified the DDOC concept with the Joint Staffs and DDOCs were established in the USPACOM and U.S. European Command (USEUCOM). The DDOC is a cross-Command, cross-Service team that focuses on integrating movement of DLA and Military Service sustainment cargo, deploying forces and equipment, and managing in-theater stocks. The goal is to optimize the use of personnel and equipment (such as aircraft and materiel handling equipment) by improving asset visibility and sustaining pipeline velocity, using DoD transportation assets.

Enterprise-wide Transportation System: Completed near the end of FY 2007, this system established a single point of contact for vendors, supply chain representatives, and the carriers (excluding Energy, which has transportation requirements unique to its supply chain). It improved the reliability and predictability of transportation delivery time and other related services by standardizing business practices and driving down transportation lead times. Consequently, DLA achieved an estimated 65% cost avoidance in transportation and improved the visibility of shipments by consolidating and centralizing the management and services for seven of its eight supply chains.

Customer Relationship (Outreach) Management: The Customer Supplier Engagement (CSE) staff provides customer support to the warfighter and federal civilian agencies to improve the efficiency and effectiveness of operations in the global distribution network. The CSE team is functionally responsible for all customer outreach programs, related service support, and analytics. CSE agents use standardized, Enterprise-wide processes and systems that provide the DDC with near real-time visibility of warfighter issues spanning customer and distribution operations. The CSE team performs in-depth analyses of customer outreach metrics, especially in the critical area of resolving customer concerns. This allows the CSE leadership to evaluate the DDC's operational response times to customer issues and provide actionable intelligence to reallocate resources to meet demands. The analyses of daily operational reports identify potential issues and allow managers to avoid problems that may adversely impact responsiveness to their customers' needs. In addition to this in-house capability, CSE engages contractors to fulfill its business process analyst (BPA) roles. The BPAs develop systemic and process improvements, as well as provide sustainment and training support to resolve operational issues for DDC end-users. To further enhance warfighter support, the BPAs identify system requirements; then create and employ processes and tools for continuous process improvement.

Defense Transportation Coordination Initiative (DTCI): DTCI is a CONUS freight initiative to reduce costs and improve customer satisfaction; it will achieve these objectives by decreasing shipment cycle time and improving shipment predictability. By systematically coordinating its efforts DTCI provides DoD, DLA, and the

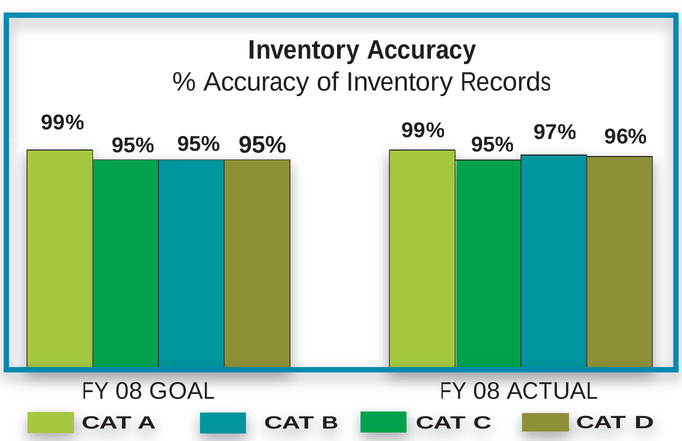
DDC with greater insight on shipment consolidation and transportation cost reduction opportunities throughout the DoD transportation enterprise. Consequently, this initiative contributes to the DoD goal to integrate the Department's logistics to make it more responsive to warfighter readiness while achieving greater efficiencies. The DTCI contract - awarded in August 2007 - provides for a full range of transportation management services to include arranging, coordinating, monitoring and controlling DoD freight shipments from shipment receipt through delivery. Six DLA distribution centers implemented DTCI during the second half of FY 2008 and savings will begin to accrue in FY 2009.

PROGRAM PERFORMANCE INDICATORS

Inventory Record Accuracy: This performance metric measures the accuracy of inventory records using statistical sampling techniques, which are performed semi-annually. Starting in FY 1999, DLA incorporated established DoD stratification and tolerance levels into the inventory sampling methodology. The DoD plan takes into consideration item characteristics such as dollar value and provides a means to focus resources commensurate with the significance of the errors found.

The FY 2008 goals for inventory accuracy were: 99% for items in the high dollar strata (Category A) and 95% for the remaining three strata.

Category A: Unit Price > $1,000
Category B: Unit of Issue Not Equal to Each **OR** On-Hand Balance > 50 **AND** Extended Dollar Value < $50,000 **OR** Activity > 50 per year
Category C: On-Hand Balance < 50 **AND** Date of Last Inventory > 24 Months
Category D: All Others



The FY 2008 performance sample inventory shows that the goals were met or exceeded in all inventory accuracy categories. In FY 2008 DDC continued an aggressive schedule for the conduct of sample inventories for all categories of materiel at each of its Distribution Centers. DDC is also providing continuous training in the related distribution responsibilities and processes, as well.

Maintaining Process Performance: Increased inspections to verify accurate documentation and materiel marking and preclude incidents of incorrect shipping (specifically sensitive, classified or items going outside the DoD network) were instituted in April 2008. As a result, the processing of High Priority Requisitions, New Procurement Receipts and Customer Returns each fell below the standard. To mitigate process performance streamlined standard operating procedures (SOPs) were developed and will be implemented by November 2008. The DDC continuously monitors the impact of these inspections requirements and will take steps to improve performance as opportunities present themselves.

	FY 08 Goal	FY 08 Actual
High Priority Requisitions (Shipped in)	1 Day	1.1 Days
Routine Requisitions (Shipped in)	3 Days	2.6 Days
New Procurement Receipts (Stored in)	1 Day	1.6 Days
Customer Returns (Stored in)	3 Days	5.1 Days
Denial Rate (Ordered Materiel Unavailable)	0.05%	0.46%
Location Accuracy (Materiel locations verified)	99.5%	99.7%

FINANCIAL PERFORMANCE MEASURES

We measure the effectiveness of program budgeting and execution with unit cost performance measures. The following table depicts the distribution unit cost results for processing and storage cost rates.

Unit Cost Results	FY 08 Goal	FY 08 Actual
Unit Cost-Total Composite Processing Rate	$24.28	$28.88
Unit Cost-Covered Storage	$3.973	$4.03

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The Unit Cost-Total Composite Processing Rate measures processing costs (direct, indirect, and applied overhead) relative to the number of line items (receipts and issues) processed.

The Unit Cost-Covered Storage measures the costs (direct, indirect, and applied overhead) to provide covered storage to the cubic footage used.

Actual processing unit cost exceeded the goal by $2.60. Actual processing workload was 22.8 million lines or 0.5 million lines less than our original FY 2008 estimate. Actual processing cost (without Second Destination Transportation) was $612 million, or $70 million more than planned.

Actual covered storage unit cost was $.06 greater than the goal. While the covered storage workload (67.4 million cubic feet) met the goal, the storage costs ($271.6 million) were $3.8 million more than the budgeted amount ($267.8 million). This increase was attributed to higher facility maintenance costs than planned.

FINANCIAL RESULTS

The Net Cost of Operations, which includes costs not recovered by the Defense-wide Working Capital Fund (military construction depreciation, imputed expenses, and accounting adjustments), reflects an excess of expenses over revenue of approximately $344 million.

DEFENSE LOGISTICS AGENCY
WORKING CAPITAL FUND

Distribution Consolidated and Combined Financial Statements

As of and for the Years Ended September 30, 2008 and 2007

UNAUDITED

DEFENSE LOGISTICS AGENCY WORKING CAPITAL FUND
Distribution

Consolidated Balance Sheets
As of September 30, 2008 and 2007
(In Thousands)

	2008	2007
ASSETS (Note 2)		
Intragovernmental:		
Accounts Receivable (Note 5)	$ 57,837	$ 50,813
Total Intragovernmental Assets	57,837	50,813
Accounts Receivable, Net (Note 5)	1,301	1,409
General Property, Plant, and Equipment, Net (Note 10)	572,072	600,165
Other Assets (Note 6)	358	131
TOTAL ASSETS	631,568	652,518
LIABILITIES (Note 11)		
Intragovernmental:		
Accounts Payable (Note 12)	114,520	62,854
Other Liabilities (Notes 15 & 16)	23,749	25,092
Total Intragovernmental Liabilities	138,269	87,946
Accounts Payable (Note 12)	46,430	53,475
Military Retirement and Other Federal Employment Benefits (Note 17)	172,685	172,078
Other Liabilities (Notes 15 & 16)	46,921	49,506
TOTAL LIABILITIES	404,305	363,005
NET POSITION		
Cumulative Results of Operations – Other Funds	227,263	289,513
TOTAL NET POSITION	227,263	289,513
TOTAL LIABILITIES AND NET POSITION	$ 631,568	$ 652,518

The accompanying notes are an integral part of these statements.

UNAUDITED

DEFENSE LOGISTICS AGENCY WORKING CAPITAL FUND
Distribution

Consolidated Statements of Net Cost
For the Years Ended September 30, 2008 and 2007
(In Thousands) (See Note 18)

	2008	2007
PROGRAM COSTS		
Gross Costs	$ 1,772,899	$ 1,599,309
Less: Earned Revenue	(1,428,607)	(1,395,873)
Net Program Costs	344,292	203,436
NET COST OF OPERATIONS	$ 344,292	$ 203,436

The accompanying notes are an integral part of these statements.

UNAUDITED

DEFENSE LOGISTICS AGENCY WORKING CAPITAL FUND
Distribution

Consolidated Statements of Changes in Net Position
For the Years Ended September 30, 2008 and 2007
(In Thousands) (See Note 19)

	2008	2007
CUMULATIVE RESULTS OF OPERATIONS		
Beginning Balances	$ 289,512	$ 338,380
Budgetary Financing Sources:		
Appropriations used	11,981	15,500
Transfers-in/out without reimbursement	-	341,500
Other Financing Sources:		
Transfers-in/out without reimbursement (+/-)	225,340	(251,961)
Imputed financing from costs absorbed by others	44,722	49,529
Total Financing Sources	282,043	154,568
Net Cost of Operations (+/-)	344,292	203,436
Net Change	(62,249)	(48,868)
Cumulative Results of Operations	227,263	289,512
UNEXPENDED APPROPRIATIONS		
Budgetary Financing Sources:		
Appropriations received	13,000	15,500
Other adjustments (rescissions, etc.) (+/-)	(1,020)	-
Appropriations used	(11,980)	(15,500)
Ending Balances	-	-
NET POSITION	$ 227,263	$ 289,512

The accompanying notes are an integral part of these statements.

UNAUDITED

DEFENSE LOGISTICS AGENCY WORKING CAPITAL FUND
Distribution

Combined Statements of Budgetary Resources
For the Years Ended September 30, 2008 and 2007
(In Thousands) (See Note 20)

	2008	2007
BUDGETARY FINANCING ACCOUNTS		
Budgetary Resources:		
Budget authority		
Appropriation	$ 13,000	$ 15,500
Contract authority	1,636,655	1,622,228
Spending authority from offsetting collections:		
Earned		
Collected	1,419,695	1,447,433
Change in receivables from Federal sources	7,057	(104,934)
Change in unfilled customer orders		
Without advance from Federal sources	12,107	(28,977)
Subtotal	3,088,514	2,951,250
Nonexpenditure transfers, net, anticipated and actual	-	341,500
Permanently not available	(1,451,859)	(1,670,522)
Total Budgetary Resources	$ 1,636,655	$ 1,622,228

UNAUDITED

DEFENSE LOGISTICS AGENCY WORKING CAPITAL FUND
Distribution

Combined Statements of Budgetary Resources (Continued)
For the Years Ended September 30, 2008 and 2007
(In Thousands) (See Note 20)

	2008	2007
Status Of Budgetary Resources:		
Obligations incurred:		
Reimbursable	$ 1,636,655	$ 1,622,228
Total Status of Budgetary Resources	1,636,655	1,622,228
Change in Obligated Balance:		
Obligated balance, net		
Unpaid obligations, brought forward, October 1	546,986	473,195
Less: Uncollected customer payments from Federal sources, brought forward, October 1	(130,235)	(264,147)
Total unpaid obligated balance, net	416,751	209,048
Obligations incurred, net	1,636,655	1,622,228
Less: Gross outlays	(1,657,186)	(1,548,435)
Change in uncollected customer payments from Federal sources (+/-)	(19,164)	133,910
Obligated balance, net, end of period		
Unpaid obligations	526,457	546,987
Less: Uncollected customer payments from Federal sources (+/-)	(149,400)	(130,236)
Total unpaid obligated balance, net, end of period	377,057	416,751
Net Outlays:		
Gross outlays	1,657,186	1,548,436
Less: Offsetting collections	(1,419,696)	(1,447,433)
Net Outlays	$ 237,490	$ 101,003

The accompanying notes are an integral part of these statements.

DEFENSE LOGISTICS AGENCY
WORKING CAPITAL FUND

Defense Reutilization and Marketing Activity Group Overview

For the Fiscal Year Ended September 30, 2008

DEFENSE REUTILIZATION AND MARKETING ACTIVITY GROUP

The Defense Reutilization and Marketing Activity Group operates through the Defense Reutilization and Marketing Service (DRMS), headquartered in Battle Creek, MI, and 104 Defense Reutilization and Marketing Offices (DRMOs) located on military installations throughout the world. The group's mission is to coordinate the reuse of excess and surplus DoD property. DRMOs receive, classify, segregate, demilitarize, account for, and dispose of excess materiel in accordance with all applicable laws and regulations. The reutilization of excess materiel by DoD customers reduces their need to purchase new materiel. In FY 2008, materiel with an acquisition value of $27.6 billion was turned in to DRMS, and $1.5 billion was reutilized within DoD. DRMS also oversees the demilitarization and disposal of the remaining property through transfers, donations, and sales, or its ultimate disposal - as in the case with hazardous waste. The business services provided by this activity group generated revenues of approximately $312 million in FY 2008. By year's end, this activity group employed 1,234 civilian, 10 active duty, and 228 reserve military personnel.

MISSION

DRMS manages the reutilization, transfer, donation, and sale of military personal property as well as the disposal of hazardous waste items no longer needed for national defense. The DRMS mission is to safeguard national security in a cost efficient and operationally effective manner, conserve valuable natural resources, and protect the environment.

STRATEGIC GOALS

The long-term goals established by the Reutilization and Marketing Activity Group are consistent with the goals contained in the DLA Strategic Plan. These goals are achieved through a series of supporting objectives and initiatives designed to improve and reengineer business practices to ensure efficient, effective, and best-value operational support.

The DoD disposal business model calls for a balance between maximizing the use of property with an absolute requirement to prevent it from getting into the hands of unauthorized recipients. Accordingly, DRMS' goals are to continue to provide quality support to the warfighter, mitigate risks to national security by strengthening the disposal process and inventory accountability, and ensure taxpayer dollars are spent appropriately. DRMS is committed to eliminating the release of potentially harmful property to the public. DRMS continues to balance the maximum reutilization of property with controls over potential vulnerabilities, even if it results in reduced revenues and increased costs.

In short, DRMS "PR0VES" it is the provider of choice for disposal solutions by:

P reventing unauthorized releases;

R eutilizing as much as possible DRMS adds value to the American taxpayer. By ensuring

0 defects;

V erifying everything;

E xecuting its operations flawlessly; and

S elling only what should be sold, it protects National Security.

PROGRAM INITIATIVES AND ACCOMPLISHMENTS

Reduced Concurrent Procurement: Numerous actions were taken to reduce the frequency of DoD organizations procuring the same items they are disposing as excess but which are still in serviceable condition. Specific actions included:

- Conducted on-going education, training, and working group sessions with senior Military Service representatives to increase reutilization and determine how existing systems can interface with DLA's systems;

- Updated systems to allow DLA activities to automatically match DRMS excess property assets against DLA inventory retention levels;

- Provided electronic notifications to past customers of available property;

- Featured scrolling photographs of high dollar and/or unique good condition items on the DRMS R/T/D website; and

- Worked with training ranges so that the Military Services could reutilize property for live fire training.

This resulted in an increase of $348 million from FY 2007 to FY 2008 in the acquisition value of excess property reutilized/recouped. Overall the monthly average reutilization for the best quality property was 4,900 lines in FY 2008.

Safeguarding Controlled Property: Several offices were established and processes were implemented to enhance oversight and security:

- **Controlled Property Centers (CPCs):** DRMS operated five CPCs; four are in the United States, one in Europe, and a sixth center is being established in the Pacific Region. Because all batch lot and Local Stock Number properties are sent to a CPC to verify the properties' availability for release for sale, these CPCs provide better accountability for the items entering the DRMS disposal accounting system. The CPCs received 7,203 batch lots in FY 2008; 10,299 batch lots were verified for proper content; 602,965 lines were inspected; and 260,907 lines of property were determined inappropriate for release, resulting in the removal of 3,360,042 pieces of property for sale to the public.

- **Controlled Property Verification Office (CPVO):** The CPVO is responsible for reviewing DRMS property before it enters the sales cycle with the objective of preventing government-sensitive or controlled property from being released to the public. This includes property earmarked for our Commercial Venture (CV) business sales partner and the Pacific and Europe sales programs. Part of the process includes conducting an automated system pre-sale review of property that is received by the CV, and will be posted on the CV's web-site for sale to the public. This pre-sale review is effectively a 3-day quarantine period to determine whether controlled property will be offered for sale. Historically, problematic sales are also periodically reviewed manually as part of an on-going quality assurance process. The CPVO will perform reviews for various special programs and conduct special projects as required. Taken as a whole, the processes implemented by the CPVO resulted in the review of 1,286,643 units of property and removal of 2,943,026 items from various sales processes. The CPVO also focuses on analyzing the accuracy of the assigned demilitarization (DEMIL) code assigned to each National Stock Number (NSN) in the federal inventory which results in a substantial improvement to the security of the United States. In an instance where the CPVO believes that a DEMIL code was incorrectly assigned a challenge is forwarded to the DEMIL Coding Management Office for evaluation and action if necessary.

- **Scrap Venture (SV):** The SV contract was modified to require the contractor to physically witness, attest to the mutilation process, and complete the certificates of destruction for controlled property received by the contractor and required to be scrapped. These contract requirements reduce the risk that controlled property will be made available to the public. The modification also allows DRMS to conduct random physical inspections of the mutilation process.

- **Commercial Venture (CV) Contract Changes:** DRMS awarded a new usable property sales contract in July 2008. Unlike the previous CV sales contract, where DRMS shared expenses and revenue with the contractor, the usable property sales contract is more like a term contract. The contract requires the contractor to pay DRMS a set price – a price based on the acquisition value of the property - for property issued to the contractor; and an additional payment for the property is due 120 days after the property is issued. This second payment is based on a percent of the acquisition value of the property delivered. It allows prospective buyers to re-sell the property and use those sales proceeds to meet the second payment requirement. This minimizes the requirement for the contractor to have significant upfront capital to meet the terms and conditions. The contract also includes property assurance requirements - related to national security - to ensure that the items issued to contractors remain safe to sell; to allow the government to retrieve property, when necessary; and to provide DRMS with monthly asset tracking reports. Disincentives will be levied against the contractor should any item be offered for resale that has been identified by DRMS as ineligible for sale. The contractor is also obligated to participate in the Government's Federal Asset Sales (eFAS) Program whereby the contractor agrees to integrate all of its property re-sales on the GovSales.gov website. The contractor must also submit quarterly sales performance reports to DRMS for submittal to the GSA GovSales Planning Office.

Safeguarding Excess/Surplus Property: The list of security-related facility projects continues to grow in both visibility and numbers. Each fiscal year DRMS prioritizes and funds multiple projects; for FY 2008 DRMS invested approximately $251,000 in non-Controlled Property Centers (non-CPC) and $728,000 in CPC-related security-related facilities projects. There are 70 additional projects - costing more than $4 million - identified for funding by FY 2014. In addition to the investment in facilities, significant changes were also implemented activity group-wide to tighten the walk-in procedures for property removal. Consequently, DRMS ensures that authorization letters and potential screeners are independently verified before property is released; and conducts weekly site inspections of contractor facilities where security risks exist.

Vulnerability Integrated Process Team (IPT): The Vulnerability IPT consists of nine sub-teams that examine

DRMS' receiving, warehousing, knowledge management, demilitarization, sales, scrap, environmental, reutilization/transfer/donation (RTD), and recycling control point operations. Since the inception of the Vulnerability IPT in 2006, a total of 236 potential corrective actions were identified. Of those, 86 were completed; 38 are works in progress; 7 are on hold (pending completion of other activities); 36 were either transferred or consolidated with other actions; and 69 were deleted due to feasibility concerns or overtaken by other corrective actions/events. Initially, many of the potential corrective actions focused on warehousing and property security issues identified during targeted brainstorming sessions. Examples of the completed corrective actions include: the establishment of the DRMS Controlled Property Centers; contracts for scrap, sales, and de-manufacturing increased DRMS operational oversight; tighter DRMO visitor controls (sign-in log, color-coded badges) were instituted; and an RTD centralized Letter of Authorization File to assist in verifying appropriate release of property to RTD customers was established. The collective efforts of these sub-teams have evolved beyond corrective actions for vulnerabilities and expanded into process improvement, property identification enhancements, and follow-on efforts targeted at developing the workforce.

Continuous Process Improvement (CPI): DRMS established a Lean Six Sigma/Continuous Process Improvement office to further the benefits of proven methodologies that improve quality and reduce waste. CPI encompasses any effective combination of continuous improvement tools and techniques. DRMS is focusing on applying the Lean Six Sigma and Theory of Constraints methodologies. Application of these techniques will eliminate waste from DRMS' processes, reduce variation in processes, and eliminate bottlenecks that impact prompt disposal service.

- DRMS has accomplished a Lean event at 11 of its 21 hub sites. After undergoing a thorough analysis of its receipt process, each site eliminated non-value added steps; streamlined the remaining receipt process; and generated savings associated with reduced overtime and travel costs.

- The Lean Six Sigma/Continuous Process Improvement office will also promote the institutionalization of CPI into the DRMS culture so that every employee will identify waste, reduce variation, and identify process constraints into their daily work routine.

Targeted Program Oversight: This is an effort to assess the effectiveness and compliance of operations and assist DRMS in achieving its strategic goals. Areas targeted for oversight are periodically updated to reflect both risk and relevancy, such as the implementation of revised or new processes. As part of the oversight program, all DRMS field activities performed quarterly self-assessments focusing on receiving, warehousing, demilitarization, RTD, sales, scrap, safety/security, and environmental processes. In addition, the DRMS headquarters conducted 32 Operational Effectiveness Reviews, 28 Environmental Effectiveness Reviews and 6 Environmental Management System audits in FY 2008, which included the effectiveness review of DRMO Arifjan.

Military Service Customer Training: DRMS developed a two-day course designed to give the Military Services a basic knowledge of the DLA/DRMS mission, the importance of property condition codes, demilitarization codes, national stock numbers, local stock numbers, and how to maximize the reutilization of DoD excess property. The course also teaches students how to maneuver through the DRMS website for regulations, formatted reports, and special processing guidance; how to build a reutilization want list; and how to prepare and submit a requisition. Students are provided course materials and work aids to better assist them in either preparing property for turn-in or utilizing DRMO inventory as a valued source of supply. A pilot course was held in Richmond, VA with students from all four Military Services. As a result of the students' evaluations and recommendations, the decision was made to offer training throughout the Military Services. The course material was finalized, and the conduct of the course began in the summer of 2008. The following locations received the training: Army at Tobyhanna, PA; Marine Corps at Albany, GA; Army Reserve Command at Ft. Gillem, GA; Navy at Patuxent River, MD; Air Force at Lackland, TX; and Marine Corps at Lejeune, NC.

Developing Waste Disposal Standards and Executing Waste Disposal Operations for Iraq: Iraq's environmental standards, which include DRMS' waste disposal and treatment standards, were drafted by Multi-National Force Iraq (MNF-I). DRMS expects approval of these standards by early FY 2009. DRMS, in conjunction with Multi-National Corps Iraq (MNC-I), is striving to achieve the Department's goal of reducing hazardous waste (HW) exports and increasing opportunities for in-country treatment and disposal. Consequently, DRMS - in collaboration with MNC-I - awarded a contract in September 2008 for in-country HW disposal.

Supporting Operations in Iraq and Afghanistan: The DRMOs are fully functional in receiving and reutilizing property, performing or assisting in the performance of demilitarization, disposing of scrap and hazardous material/waste and, where possible, the redistribution and disposal of useable property. DRMS is continually striving to expand disposal services throughout these theaters and to make redistribution and disposal a vital part of supply chain management. The six DRMOs were fully operational during the course of the year and have expanded their capabilities to support the Forward Operating Bases, such as Taqaddum and Fallujah where more than 7.2 million pounds of scrap were removed.

Disposal Remediation Teams (DRTs): The DRT Program is a joint Military Reserve force comprised of Navy, Army and Air Force personnel that is instrumental in meeting the customer requirements in a very fluid operational environment. In FY 2008, DRMS deployed six DRTs comprised of 32 members to locations spread throughout three countries: Iraq, Afghanistan, and Kuwait. These members serve as Disposal Service Representatives and operate in an expeditionary manner by going to Forward Operating Bases to support the customer in their environment and location. This initial effort has laid the foundation for future DRT joint Military Reserve force operations in the Central Command area of operational responsibility; has extended the DLA enterprise to the outermost tip of the spear; and has connected and integrated DRMS' disposal operations with the customer to allow for responsive expedient support.

Enhanced DRMS Intern Program: Faced with an aging workforce, DRMS utilizes an Intern Training Program to ensure that the knowledge base is transferred to a trained employee prior to an individual's retirement. The program includes completion of mandatory formal training courses, on-the-job training, cross training, and rotational training within a 2-year period. Each intern is assigned to one of three disciplines (Property Disposal, Environmental, or Contracting) with specific program development requirements: the various training courses, prerequisites, and learning objectives. Each intern is also assigned to a targeted position with established progression criteria that must be met prior to assigning the intern to a permanent position. DRMS employed 24 interns (15 in Property Disposal, 7 in Environmental, and 2 in Contracting).

PROGRAM PERFORMANCE INDICATOR

Reutilization/Transfer/Donation (R/T/D) rate: This indicator represents the aggregate number of line items of the property reutilized, transferred, and donated expressed as a percentage of the total line items disposed. The indicator applies to the available assets that are economically reused. It addresses disposal via reutilization by another defense customer, transfer to another Federal Agency, or donation to an eligible state or local government or to a non-profit organization. R/T/D dispositions, as a percentage of total dispositions, indicate support provided to DoD, Federal government, and state and local agencies. Customer utilization of these programs increases troop readiness, avoids new procurement costs, and provides needed items to agencies at no cost. In FY 2008, DRMS successfully reutilized, transferred, or donated over 182,396 line items of excess property for an R/T/D rate of about 15.5%.

- Operations Enduring Freedom and Iraqi Freedom Reutilization: Total reutilization supporting these two contingencies surpassed 36,000 line items with a value of $491 million. Examples of the types of items issued in support of these operations include vehicles, tanks, trucks, and body armor.

- Computers for Learning: DRMS is responsible for overseeing the transfer of computers to schools in support of the DoD's Computers for Learning Program. In FY 2008, 4,631 schools participated in the program, and computers worth over $20 million in acquisition value were transferred.

R/T/D will continue to increase as a percentage of total dispositions by:

- Marketing high dollar, good condition items through scrolling photographs on the R/T/D website. In FY 2008, DRMS received 341 requisitions for property with an original acquisition value of $21.5 million.

- Pushing (to past customers) inventory alerts of the availability of same/similar items that they previously purchased. In FY 2008, DRMS received over 4,000 requisitions for property with an original acquisition value of $174 million.

- Implementing changes that will improve the information on available property. This includes providing more photographs on the web and writing better descriptions of the property.

- Working closely with DLA and DoD supply centers to fill backorders and new purchase requests.

- Establishing and implementing automated tools that will provide priority screening for item managers.

- Promoting the additional 2-day screening opportunity for Local Stock Number items and batch lots that were previously screened and cleared for sale. In FY 2008, DRMS received 1,169 requisitions for property with an original acquisition value of $2.7 million, resulting in an increase of $2.5 million in acquisition value of excess property from FY 2007 to FY 2008.

FINANCIAL PERFORMANCE MEASURES

DLA measures the effectiveness of program budgeting and execution with unit cost performance measures. Cost is defined as obligations incurred in support of or attributed to the service performed. DRMS is measured on five unit cost goals:

- Receiving
- Reutilization/Transfer/Donation (R/T/D)
- Useable Sales
- Hazardous Waste (HW) Disposal
- Recycling/Disposal

These measures recognize that all property received incurs processing costs; that certain types of excess property require costly special handling, such as demilitarization, without generating any economic return to DoD; and that partnerships with the private sector incur cost to the government. The DRMS unit cost structure is flexible to remain viable during periods of significant process changes. The table below depicts the unit cost results for each category.

Financial Performance Measures	FY 08 Goal	FY 08 Actual
Cost incurred per line item of useable property received – Receiving	$30.40	$32.53
Cost incurred per line item – Reutilization/Transfer/ Donation (R/T/D)	$183.287	$291.342
Cost incurred per line item – Useable Sales	$21.756	$25.161
Cost incurred per pound – Hazardous Waste Disposal	$.234	$.219
Cost incurred per pound – Recycling/Disposal	$.0614	$.05

The Receiving unit cost goal is based on the total cost associated with the stock, store, and issue (logistics) of usable property divided by the number of line items of usable property received. The FY 2008 Useable Property Received unit cost was higher than the plan by 7%. There were 3.5 million line items actually received versus 3.8 million line items planned (an 8% decrease). The receipt of inactive – but useable - stock (anticipated based on the BRAC recommendations) did not materialize in FY 2008.

The R/T/D unit cost goal is calculated from the total cost associated with reutilizing, transferring, and donating excess personal property divided by the line items of property disposed via R/T/D. The unit cost for R/T/D was 59% higher than planned. There were 41% fewer line items (153,000 versus 216,000) disposed by R/T/D than planned. The decrease in line items was primarily the result of tighter security controls and additional screening requirements which decreased the amount of property available to process through the R/T/D programs.

Useable Sales unit cost goal is calculated by dividing the costs associated with the public sales of surplus useable personal property (sold primarily through a Commercial Venture partnership) by the number of line items of property sold. The unit cost for Useable Sales was about 16% above the goal in FY 2008. The increase to the unit cost occurred because there were about 126,000 fewer lines items sold (394,492 versus the number of line items planned for sale 520,000).

The Hazardous Waste (HW) Disposal unit cost goal is calculated from the non-contract costs associated with environmentally regulated disposal of HW divided by the number of pounds of HW disposed. The increased HW disposal workload (3% greater than the plan due to the purging of expiring Nuclear, Biological, and Chemical Over-garments) was the most significant contributing factor to the unit cost variance.

The Recycling/Disposal (R/D) unit cost goal is calculated by dividing both the costs of storing property in a demilitarization and scrap zone and the costs of all recycling processes by the number of pounds of property disposed. The actual R/D unit cost for FY 2008 was 19% lower than planned. Because DRMS extended support to the Warfighter in Iraq and implemented stricter property control measures (to ensure that property was not improperly sold to the public), R/D workload was greater than planned.

FINANCIAL RESULTS

The Net Cost of Operations, which includes costs not recovered by the Defense-wide Working Capital Fund (military construction depreciation, imputed expenses, and accounting adjustments), reflects an excess of expenses over revenue of approximately $67.5 million.

DEFENSE LOGISTICS AGENCY
WORKING CAPITAL FUND

Defense Reutilization and Marketing Consolidated and Combined Financial Statements

As of and for the Years Ended September 30, 2008 and 2007

UNAUDITED

DEFENSE LOGISTICS AGENCY WORKING CAPITAL FUND
Reutilization & Marketing

Consolidated Balance Sheets
As of September 30, 2008 and 2007
(In Thousands)

	2008	2007
ASSETS (Note 2)		
Intragovernmental:		
Accounts Receivable (Note 5)	$ 764	$ 417
Total Intragovernmental Assets	764	417
Cash and Other Monetary Assets (Note 7)	9,775	7,421
Accounts Receivable, Net (Note 5)	3,849	5,075
General Property, Plant, and Equipment, Net (Note 10)	64,976	62,217
Other Assets (Note 6)	338	164
TOTAL ASSETS	79,702	75,294
LIABILITIES (Note 11)		
Intragovernmental:		
Accounts Payable (Note 12)	9,957	12,401
Other Liabilities (Notes 15 & 16)	21,248	24,918
Total Intragovernmental Liabilities	31,205	37,319
Accounts Payable (Note 12)	32,301	31,189
Military Retirement and Other Federal Employment Benefits (Note 17)	17,222	17,162
Other Liabilities (Notes 15 & 16)	23,056	21,242
TOTAL LIABILITIES	103,784	106,912
NET POSITION		
Cumulative Results of Operations – Other Funds	(24,082)	(31,618)
TOTAL NET POSITION	(24,082)	(31,618)
TOTAL LIABILITIES AND NET POSITION	$ 79,702	$ 75,294

The accompanying notes are an integral part of these statements.

UNAUDITED

DEFENSE LOGISTICS AGENCY WORKING CAPITAL FUND
Reutilization & Marketing

Consolidated Statements of Net Cost
For the Years Ended September 30, 2008 and 2007
(In Thousands) (See Note 18)

	2008	2007
PROGRAM COSTS		
Gross Costs	$ 380,037	$ 319,970
Less: Earned Revenue	(312,522)	(252,889)
Net Program Costs	67,515	67,081
NET COST OF OPERATIONS	$ 67,515	$ 67,081

The accompanying notes are an integral part of these statements.

UNAUDITED

DEFENSE LOGISTICS AGENCY WORKING CAPITAL FUND

Reutilization & Marketing

Consolidated Statements of Changes in Net Position
For the Years Ended September 30, 2008 and 2007
(In Thousands) (See Note 19)

	2008	2007
CUMULATIVE RESULTS OF OPERATIONS		
Beginning Balances	$ (31,618)	$ (40,637)
Budgetary Financing Sources:		
Appropriations used	4,861	3,766
Transfers-in/out without reimbursement (+/-)	-	(341,500)
Other Financing Sources:		
Transfers-in/out without reimbursement (+/-)	60,861	403,453
Imputed financing from costs absorbed by others	9,329	10,380
Total Financing Sources	75,051	76,099
Net Cost of Operations (+/-)	67,515	67,080
Net Change	7,536	9,019
Cumulative Results of Operations	(24,082)	(31,618)
UNEXPENDED APPROPRIATIONS		
Budgetary Financing Sources:		
Appropriations received	5,275	3,766
Other adjustments (rescissions, etc.) (+/-)	(414)	-
Appropriations used	(4,861)	(3,766)
Ending Balances	-	-
NET POSITION	$ (24,082)	$ (31,618)

The accompanying notes are an integral part of these statements.

UNAUDITED

DEFENSE LOGISTICS AGENCY WORKING CAPITAL FUND
Reutilization & Marketing

Combined Statements of Budgetary Resources
For the Years Ended September 30, 2008 and 2007
(In Thousands) (See Note 20)

	2008	2007
BUDGETARY FINANCING ACCOUNTS		
Budgetary Resources:		
Unobligated balance, brought forward, October 1	$ -	$ -
Budget authority		
Appropriation	5,275	3,766
Contract authority	377,057	341,104
Spending authority from offsetting collections:		
Earned		
Collected	311,808	249,060
Change in receivables from Federal sources	732	3,825
Change in unfilled customer orders		
Advance received	(4,043)	3,701
Without advance from Federal sources	56	41
Subtotal	690,885	601,497
Nonexpenditure transfers, net, anticipated and actual	-	(341,500)
Permanently not available	(313,828)	81,107
Total Budgetary Resources	$ 377,057	$ 341,104

UNAUDITED

DEFENSE LOGISTICS AGENCY WORKING CAPITAL FUND
Reutilization & Marketing

Combined Statements of Budgetary Resources (Continued)
For the Years Ended September 30, 2008 and 2007
(In Thousands) (See Note 20)

	2008	2007
Status Of Budgetary Resources:		
Obligations incurred:		
Reimbursable	$ 377,057	$ 341,104
Total Status of Budgetary Resources	377,057	341,104
Change in Obligated Balance:		
Obligated balance, net		
Unpaid obligations, brought forward, October 1	146,032	123,408
Less: Uncollected customer payments		
from Federal sources, brought forward, October 1	(6,085)	(2,219)
Total unpaid obligated balance, net	139,947	121,189
Obligations incurred, net	377,057	341,104
Less: Gross outlays	(373,488)	(318,480)
Change in uncollected customer payments		
from Federal sources (+/-)	(788)	(3,866)
Obligated balance, net, end of period		
Unpaid obligations	149,600	146,032
Less: Uncollected customer payments		
from Federal sources (+/-)	(6,873)	(6,085)
Total unpaid obligated balance, net, end of period	142,727	139,947
Net Outlays:		
Gross outlays	373,488	318,480
Less: Offsetting collections	(307,766)	(252,761)
Net Outlays	$ 65,722	$ 65,719

The accompanying notes are an integral part of these statements.

DEFENSE LOGISTICS AGENCY
WORKING CAPITAL FUND

Document Automation & Production Service Activity Group Overview

For the Fiscal Year Ended September 30, 2008

DOCUMENT AUTOMATION & PRODUCTION SERVICE

The Document Automation & Production Service (DAPS) is responsible for printing, duplicating, and document automation programs. This responsibility encompasses the full range of automated services to include: document workflow, conversion, electronic storage and output, and distribution of hard copy and digital information. DAPS provides time sensitive, competitively priced, high quality products and services that are either produced in-house or procured commercially. DAPS manages its mission through a headquarters, located in Mechanicsburg, PA, and a worldwide network of 185 production facilities. During FY 2008, DAPS earned approximately $358 million in revenue and employed 758 civilians at year-end. Major customers were: Air Force (21%), Navy (30%), Army (22%), Defense Agencies (23%), and non-DoD customers (4%).

MISSION

The mission of DAPS is to provide best value document automation and management services in support of America's Armed Forces and Federal Agencies. DAPS' value to DoD is characterized by two elements. First, DAPS provides a full portfolio of best value document services ranging from traditional offset printing, through on-demand output, to online document services and workflow. Second, DAPS actively functions as a transformation agent moving DoD towards the use of online documents and services. These services include building libraries of digital documents to permit online access, providing multifunctional devices (that print from networks, copy, fax and scan) in customer workspaces, and converting paper documents to target digital formats.

STRATEGIC GOALS

DAPS is committed to the following goals:

- Serving as a major catalyst in transforming business by revolutionizing document automation services;
- Rapidly utilizing technology for agile and responsive internal business solutions;
- Aggressively pursuing partnerships with government, industry, and suppliers;
- Ensuring the DAPS workforce is enabled to deliver and sustain world-class performance;
- Striving to reduce costs, simplify organizational structure, eliminate unnecessary facilities, and ensure that equipment and personnel are commensurate with the workload; and
- Aligning processes to focus on improving the quality of products and services while meeting or exceeding customers' delivery requirements.

PROGRAM INITIATIVES AND ACCOMPLISHMENTS

Most Efficient Organization (MEO) of DAPS was highlighted for achieving performance milestones (high on-time delivery and customer satisfaction rates) in the Report on Competitive Sourcing Results published in May 2008 by the Office of Management and Budget. DAPS was DoD's only MEO - among more than 1,200 in the federal government - singled out for achieving its milestones. The report also indicated the DAPS MEO accounted for 11.7 percent of the total federal savings accrued from the results of the A-76 competitive sourcing process ($112 million of the $958 million saved) between FY 2003 and FY 2005. Through FY 2008 the DAPS MEO has saved more than $320 million.

High Performing Organization (HPO) designation was received by DAPS in a letter signed by the Deputy Under Secretary of Defense for Installations and Environment. The HPO designation is effective October 2009 and extends the operation of the MEO for three fiscal years.

Comprehensive Equipment Strategy for replacing its aging equipment throughout the organization was initiated during FY 2008. DAPS equipment inventory of over 1,600 items was reviewed and placed on a standard replacement cycle. The equipment included black and white, color, and wide format production printers, as well as hardcopy output production equipment such as paper cutters, hole punchers, CD ROM duplicators, and binding devices. The total investment from FY 2008 through FY 2012 is expected to be about $43 million.

PROGRAM PERFORMANCE INDICATORS

Product Rework: In-house rework percentage is used to measure the quality of delivered products. This performance metric is calculated by dividing revenue lost from orders not accepted by the total in-house production revenue. During FY 2008, DAPS achieved a rework percentage of 0.19, exceeding its goal of 0.25%.

Customer Satisfaction: This performance metric measures satisfied customers as the percentage of customers ranking DAPS performance as "satisfied" or "very satisfied." DAPS uses a survey professionally prepared and administered by an independent commercial entity to determine an overall customer satisfaction rating. DAPS achieved a customer satisfaction rating of 97% for FY 2008, exceeding its goal of 90%.

On-Time Delivery (In-house Production): This performance metric measures the timeliness of customer order completion. The performance metric is calculated by dividing the total number of orders filled on time by a DAPS owned and operated production facility (in-house) by the total number of orders filled by these facilities. DAPS achieved an on-time delivery rate of 98.59%, exceeding its goal of 98%.

FINANCIAL PERFORMANCE MEASURES

In addition to program performance measures, DAPS measures the effectiveness of program budgeting and execution with a unit cost performance measure. It measures the total units produced relative to the total cost to produce those items.

Unit Cost Results	FY 08 Actual	FY 08 Goal
Unit Cost per In-House Production Unit	.0553	.0481

DAPS produced 1% fewer in-house units than planned (2,741 million actual versus 2,773 million planned); and actual in-house costs were almost 14% lower than planned ($132.0 million actual versus $153.0 million planned). By incurring significantly less cost, while producing slightly fewer units, DAPS was able to better its unit cost goal by more than 13%.

FINANCIAL RESULTS

The Net Cost of Operations, which includes costs not recovered by the Defense-wide Working Capital Fund (military construction depreciation, imputed expenses, and accounting adjustments), reflects an excess of revenue over expenses of approximately $12.4 million.

DEFENSE LOGISTICS AGENCY
WORKING CAPITAL FUND

Document Automation & Production Service Consolidated and Combined Financial Statements

As of and for the Years Ended September 30, 2008 and 2007

UNAUDITED

DEFENSE LOGISTICS AGENCY WORKING CAPITAL FUND
Document Automation & Production Service

Consolidated Balance Sheets
As of September 30, 2008 and 2007
(In Thousands)

	2008	2007
ASSETS (Note 2)		
Intragovernmental:		
Accounts Receivable (Note 5)	$ 7,413	$ 4,871
Total Intragovernmental Assets	7,413	4,871
Cash and Other Monetary Assets (Note 7)	-	-
Accounts Receivable, Net (Note 5)	651	159
Inventory and Related Property, Net (Note 9)	5,549	5,132
General Property, Plant, and Equipment, Net (Note 10)	10,793	10,258
Other Assets (Note 6)	865	1,495
TOTAL ASSETS	25,271	21,915
LIABILITIES (Note 11)		
Intragovernmental:		
Accounts Payable (Note 12)	2,955	5,048
Other Liabilities (Notes 15 & 16)	1,430	1,598
Total Intragovernmental Liabilities	4,385	6,646
Accounts Payable (Note 12)	44,795	71,429
Military Retirement and Other Federal Employment Benefits (Note 17)	9,782	9,748
Other Liabilities (Notes 15 & 16)	6,590	(55,369)
TOTAL LIABILITIES	65,552	32,454
NET POSITION		
Cumulative Results of Operations – Other Funds	(40,281)	(10,539)
TOTAL NET POSITION	(40,281)	(10,539)
TOTAL LIABILITIES AND NET POSITION	$ 25,271	$ 21,915

The accompanying notes are an integral part of these statements.

UNAUDITED

DEFENSE LOGISTICS AGENCY WORKING CAPITAL FUND
Document Automation & Production Service

Consolidated Statements of Net Cost
For the Years Ended September 30, 2008 and 2007
(In Thousands) (See Note 18)

	2008	2007
PROGRAM COSTS		
Gross Costs	$ 345,688	$ 824,783
Less: Earned Revenue	(358,082)	(824,706)
Net Program Costs	(12,394)	77
NET COST OF OPERATIONS	$ (12,394)	$ 77

The accompanying notes are an integral part of these statements.

UNAUDITED

DEFENSE LOGISTICS AGENCY WORKING CAPITAL FUND

Document Automation & Production Service

Consolidated Statements of Changes in Net Position
For the Years Ended September 30, 2008 and 2007
(In Thousands) (See Note 19)

	2008	2007
CUMULATIVE RESULTS OF OPERATIONS		
Beginning Balances	$ (10,539)	$ (5,143)
Budgetary Financing Sources:		
Transfers-in/out without reimbursement (+/-)	30,000	-
Other Financing Sources:		
Transfers-in/out without reimbursement (+/-)	(76,895)	(10,518)
Imputed financing from costs absorbed by others	4,759	5,199
Total Financing Sources	(42,136)	(5,319)
Net Cost of Operations (+/-)	(12,394)	77
Net Change	(29,742)	(5,396)
Cumulative Results of Operations	$ (40,281)	$ (10,539)

The accompanying notes are an integral part of these statements.

UNAUDITED

DEFENSE LOGISTICS AGENCY WORKING CAPITAL FUND
Document Automation & Production Service

Combined Statements of Budgetary Resources
For the Years Ended September 30, 2008 and 2007
(In Thousands) (See Note 20)

	2008	2007
BUDGETARY FINANCING ACCOUNTS		
Budgetary Resources:		
Unobligated balance, brought forward, October 1	$ (23,848)	$ (30,820)
Recoveries of prior year unpaid obligations	55	161
Budget authority		
Contract authority	409	2,824
Spending authority from offsetting collections:		
Earned		
Collected	418,831	351,327
Change in receivables from Federal sources	(61,414)	1,413
Change in unfilled customer orders		
Advance received	1	(859)
Without advance from Federal sources	1,987	4,274
Subtotal	359,814	358,979
Nonexpenditure transfers, net, anticipated and actual	30,000	-
Permanently not available	(4,991)	(2,607)
Total Budgetary Resources	$ 361,030	$ 325,713

UNAUDITED

DEFENSE LOGISTICS AGENCY WORKING CAPITAL FUND
Document Automation & Production Service

Combined Statements of Budgetary Resources (Continued)
For the Years Ended September 30, 2008 and 2007
(In Thousands) (See Note 20)

	2008	2007
Status Of Budgetary Resources:		
Obligations incurred:		
Reimbursable	$ 338,269	$ 349,561
Subtotal	338,269	349,561
Unobligated balance:		
Apportioned	22,761	(23,848)
Subtotal	22,761	(23,848)
Total Status of Budgetary Resources	361,030	325,713
Change in Obligated Balance:		
Obligated balance, net		
Unpaid obligations, brought forward, October 1	126,242	116,792
Less: Uncollected customer payments		
from Federal sources, brought forward, October 1	(88,501)	(82,813)
Total unpaid obligated balance, net	37,741	33,979
Obligations incurred, net	338,269	349,561
Less: Gross outlays	(372,149)	(339,950)
Less: Recoveries of prior year obligations, actual	(55)	(161)
Change in uncollected customer payments		
from Federal sources (+/-)	59,427	(5,687)
Obligated balance, net, end of period		
Unpaid obligations	92,306	126,242
Less: Uncollected customer payments		
from Federal sources (+/-)	(29,074)	(88,501)
Total unpaid obligated balance, net, end of period	63,232	37,741
Net Outlays:		
Gross outlays	372,149	339,950
Less: Offsetting collections	(418,832)	(350,468)
Net Outlays	$ (46,683)	$ (10,518)

The accompanying notes are an integral part of these statements.

DEFENSE LOGISTICS AGENCY
GENERAL FUND

Consolidated and Combined Financial Statements

As of and for the Years Ended September 30, 2008 and 2007

UNAUDITED

DEPARTMENT OF DEFENSE
DEFENSE LOGISTICS AGENCY GENERAL FUND

Consolidated Balance Sheets
As of September 30, 2008 and 2007
(In Thousands)

	2008	2007
ASSETS (Note 2)		
Intragovernmental:		
Fund Balance with Treasury (Note 3)	$ 757,876	$ 725,689
Accounts Receivable (Note 5)	11,990	17,933
Total Intragovernmental Assets	769,866	743,622
Accounts Receivable, Net (Note 5)	120	268
General Property, Plant, and Equipment, Net (Note 10)	277,546	394,730
TOTAL ASSETS	1,047,532	1,138,620
LIABILITIES (Note 11)		
Intragovernmental:		
Accounts Payable (Note 12)	11,131	9,173
Other Liabilities (Note 15 & 16)	6,004	5,694
Total Intragovernmental Liabilities	17,135	14,867
Accounts Payable (Note 12)	23,448	8,024
Military Retirement and Other Federal Employment Benefits (Note 17)	6,245	6,223
Environmental and Disposal Liabilities (Note 14)	257,415	263,625
Other Liabilities (Note 15 & 16)	3,094	3,682
TOTAL LIABILITIES	307,337	296,421
NET POSITION		
Unexpended Appropriations – Other Funds	733,951	689,926
Cumulative Results of Operations – Other Funds	6,244	152,273
TOTAL NET POSITION	740,195	842,199
TOTAL LIABILITIES AND NET POSITION	$ 1,047,532	$ 1,138,620

The accompanying notes are an integral part of these statements.

UNAUDITED

DEPARTMENT OF DEFENSE
DEFENSE LOGISTICS AGENCY GENERAL FUND

Consolidated Statements of Net Cost
For the Years Ended September 30, 2008 and 2007
(In Thousands) (See Note 18)

		2008		2007
PROGRAM COSTS				
Gross Costs	$	713,504	$	704,110
Less: Earned Revenue		(40,082)		(54,132)
Net Program Costs		673,422		649,978
NET COST OF OPERATIONS	$	673,422	$	649,978

The accompanying notes are an integral part of these statements.

UNAUDITED

DEPARTMENT OF DEFENSE
DEFENSE LOGISTICS AGENCY GENERAL FUND

Consolidated Statements of Changes in Net Position
For the Years Ended September 30, 2008 and 2007
(In Thousands) (See Note 19)

	2008	2007
CUMULATIVE RESULTS OF OPERATIONS		
Beginning Balances	$ 152,273	$ 160,824
Budgetary Financing Sources:		
Appropriations used	661,835	737,875
Other Financing Sources:		
Transfers-in/out without reimbursement (+/-)	(136,544)	(98,526)
Imputed financing from costs absorbed by others	1,906	2,078
Other (+/-)	196	-
Total Financing Sources	527,393	641,427
Net Cost of Operations (+/-)	673,422	649,978
Net Change	(146,029)	(8,551)
Cumulative Results of Operations	6,244	152,273
UNEXPENDED APPROPRIATIONS		
Beginning Balances	689,926	780,802
Budgetary Financing Sources:		
Appropriations received	686,267	646,322
Appropriations transferred-in/out (+/-)	28,581	11,012
Other adjustments (rescissions, etc.) (+/-)	(8,988)	(10,335)
Appropriations used	(661,835)	(737,875)
Total Financing Sources	44,025	(90,876)
Net Change	44,025	(90,876)
Ending Balances	733,951	689,926
NET POSITION	$ 740,195	$ 842,199

The accompanying notes are an integral part of these statements.

UNAUDITED

DEPARTMENT OF DEFENSE
DEFENSE LOGISTICS AGENCY GENERAL FUND

Combined Statements of Budgetary Resources
For the Years Ended September 30, 2008 and 2007
(In Thousands) (See Note 20)

		2008		2007
BUDGETARY FINANCING ACCOUNTS				
Budgetary Resources:				
Unobligated balance, brought forward, October 1	$	219,985	$	192,244
Recoveries of prior year unpaid obligations		35,990		15,209
Budget authority				
Appropriation		686,267		646,322
Spending authority from offsetting collections:				
Earned				
Collected		45,014		13,297
Change in receivables from Federal sources		(6,075)		9,807
Change in unfilled customer orders				
Without advance from Federal sources		830		3,813
Subtotal		726,036		673,239
Nonexpenditure transfers, net, anticipated and actual		28,581		11,012
Permanently not available		(8,987)		(10,336)
Total Budgetary Resources	$	1,001,605	$	881,368

UNAUDITED

DEPARTMENT OF DEFENSE
DEFENSE LOGISTICS AGENCY GENERAL FUND

Combined Statements of Budgetary Resources (Continued)
For the Years Ended September 30, 2008 and 2007
(In Thousands) (See Note 20)

	2008	2007
Status Of Budgetary Resources:		
Obligations incurred:		
Direct	$ 801,740	$ 634,841
Reimbursable	41,404	26,541
Subtotal	843,144	661,382
Unobligated balance:		
Apportioned	123,539	185,686
Subtotal	123,539	185,686
Unobligated balance not available	34,922	34,300
Total Status of Budgetary Resources	1,001,605	881,368
Change in Obligated Balance:		
Obligated balance, net		
Unpaid obligations, brought forward, October 1	527,619	599,813
Less: Uncollected customer payments from Federal sources, brought forward, October 1	(21,916)	(8,296)
Total unpaid obligated balance, net	505,703	591,517
Obligations incurred, net	843,144	661,382
Less: Gross outlays	(718,686)	(718,368)
Less: Recoveries of prior year unpaid obligations, actual	(35,990)	(15,209)
Change in uncollected customer payments from Federal sources (+/-)	5,245	(13,620)
Obligated balance, net, end of period		
Unpaid obligations	616,087	527,619
Less: Uncollected customer payments from Federal sources (+/-)	(16,671)	(21,916)
Total unpaid obligated balance, net, end of period	599,416	505,703
Net Outlays:		
Gross outlays	718,686	718,368
Less: Offsetting collections	(45,014)	(13,295)
Net Outlays	$ 673,672	$ 705,073

The accompanying notes are an integral part of these statements.

DEFENSE LOGISTICS AGENCY
GENERAL FUND

Notes to the Consolidated and Combined Financial Statements

For the Fiscal Years Ended September 30, 2008 and 2007

Note 1. Significant Accounting Policies

A. Basis of Presentation

These financial statements have been prepared to report the financial position and results of operations of the Defense Logistics Agency (DLA) General Fund (GF), 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 DLA in accordance with the Department of Defense (DoD) Financial Management Regulation (FMR), the Office of Management and Budget (OMB) Circular A-136, Financial Reporting Requirements, and to the extent possible generally accepted accounting principles (GAAP). The accompanying financial statements account for all resources for which DLA is responsible unless otherwise noted.

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

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

The DoD currently has several auditor identified financial statement material weaknesses. Of these, DLA has the following: (1) Financial Management Systems, (2) Intragovernmental Eliminations, (3) Unsupported Accounting Entries, (4) Fund Balance with Treasury, (5) General Property, Plant, and Equipment, and (6) Accounts Payable.

B. Mission of the Reporting Entity

The DLA's primary mission is to provide best value logistics integrated solutions to meet the needs of America's Armed Forces and other designated customers around the clock, around the world in time of peace, national emergency, and war. Support begins with joint planning for parts used in new weapons systems, extends through production and contract support, distribution and warehousing, and concludes with the disposal of materiel that is obsolete, worn out, or no longer needed.

The DLA provides supply support, technical/logistics services and quality support to all branches of the Military and other nonDoD customers. The services provided fall into the following activity groups: Supply Management, Defense Distribution Center (DDC), Defense Reutilization and Marketing Service (DRMS), and Document Automation and Production Service (DAPS). Supply Management is comprised of NonEnergy and Energy. NonEnergy supply is further divided into the following supply chains: Clothing and Textiles, Medical, Subsistence, Construction and Equipment, Aviation, Land, and Maritime.

The DLA continues to leverage its operational efficiencies to implement the Base Realignment and Closure 2005 Supply and Storage recommendations. The DLA has engaged in the following transformational initiatives with the Military Departments: (1) The Commodity Management Privatization to privatize the supply and storage of selected commodities (i.e., tires, compressed gases and petroleum, oil, lubricant packages), (2) Depot - Level Reparable (Procurement Management/Consumable Item Transfer) to realign procurement management of repair parts from the Military Services to DLA at selected sites and to transfer supply management of selected consumable items to DLA, and (3) Supply, Storage and Distribution Reconfiguration to realign supply, storage and distribution functions through consolidation and management reconfiguration at 13 sites.

C. Appropriations and Funds

The DLA receives its appropriations and funds as general funds. The DLA 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 accounts.

The Operation and Maintenance appropriation finances Other Logistics Services, Other Logistics Programs, and environmental programs.

The Research, Development, Test, and Evaluation (RDT&E) appropriation finances the development of major upgrades that increase the performance of existing systems, the purchase of test articles, and the developmental testing and/or initial operational test and evaluation prior to system acceptance.

The Procurement Defense-Wide appropriation finances mission essential equipment, including automated data processing, telecommunications equipment and passenger carrying vehicles that afford a high degree of efficiency, effectiveness, and productivity in the accomplishment of DLA's logistics mission.

The Military Construction (MILCON) appropriation finances the construction of facilities to support DLA's logistic support mission to include DoD fuel infrastructure projects (strategic refueling mission, environmental concerns, and fuel operations). The DLA suballots MILCON funds to certain entities such as the Air Force, Navy and U.S. Army Corps of Engineers (USACE) for the execution of specific authorized programs.

The Family Housing appropriation finances the routine operations, maintenance, and construction improvements of 201 military family housing units. Routine operation and maintenance includes management costs, utility costs and cyclical maintenance such as painting and renovations.

D. Basis of Accounting

For FY 2008, DLA's financial management systems are unable to meet all of the requirements for full accrual accounting. Many of DLA's financial and nonfinancial feeder systems and processes were designed and implemented prior to the issuance of GAAP for federal agencies. These systems were not designed to collect and record financial information on the full accrual accounting basis as required by GAAP. Most of DLA's (financial and nonfinancial) legacy systems were designed to record information on a budgetary basis.

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

E. Revenues and Other Financing Sources

The DLA receives congressional appropriations as financing sources for general funds on either an annual or multi-year basis. When authorized by legislation, these appropriations are supplemented by revenues generated by sales of goods or services. The DLA recognizes revenue as a result of costs incurred for goods or services provided to other federal agencies and the public. Full cost pricing is DLA's standard policy for services provided as required by OMB Circular A-25, Transmittal Memorandum #1, User Charges. The DLA recognizes revenue when earned within the constraints of current system capabilities. In some instances, revenue is recognized when bills are issued.

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

F. Recognition of Expenses

For financial reporting purposes, DoD policy requires the recognition of operating expenses in the period incurred. However, because DLA's financial and nonfinancial feeder systems were not designed to collect and record financial information on the full accrual accounting basis, accruals are made for major items such as payroll expenses, accounts payable, environmental liabilities, and unbilled revenue.

G. Accounting for Intragovernmental Activities

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

The U.S. Treasury Financial Management Service is responsible for eliminating transactions between DoD and other federal agencies. The Treasury Financial Manual Part 2 – Chapter 4700, "Agency Reporting Requirements for the Financial Report of the United States Government," and the U.S. Treasury's "Federal Intragovernmental Transactions Accounting Policy Guide" provide guidance for reporting and reconciling intragovernmental balances. While DLA is unable to fully reconcile intragovernmental transactions with all federal partners, DLA 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, therefore, do not report any portion of the public debt or interest thereon, nor do the statements report the source of public financing whether from issuance of debt or tax revenues.

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

H. Transactions with Foreign Governments and International Organizations

Not Applicable to DLA GF.

I. Funds with the U.S. Treasury

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

In addition, DFAS sites and USACE Finance Center submit reports to the U.S. Treasury by appropriation on interagency transfers, collections received, and disbursements issued. The U.S. Treasury records these transactions to the applicable FBWT account. The DLA's recorded balance in FBWT accounts and U.S. Treasury's FBWT accounts must balance monthly.

J. Foreign Currency

Not Applicable to DLA GF.

K. Accounts Receivable

As presented in the Balance Sheet, accounts receivable includes three categories: accounts, claims, and refunds receivable from other federal entities or from the public. Allowances for uncollectible accounts due from the public are based upon Analysis of Receivables by Age Group method. 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.

L. Direct Loans and Loan Guarantees

Not Applicable to DLA GF.

M. Inventories and Related Property

Not Applicable to DLA GF.

N. Investments in U.S. Treasury Securities

Not Applicable to DLA GF.

O. General Property, Plant and Equipment

The DLA's General Property Plant & Equipment (General PP&E) capitalization threshold is $100 thousand except for real property which is $20 thousand. The DLA has not implemented the threshold for real property. The DLA is currently using the capitalization threshold of $100 thousand for all General PP&E.

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 capitalization threshold. The DoD also requires the capitalization of improvements to existing General PP&E assets if the improvements equal or exceed DoD 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.

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

P. Advances and Prepayments

When advances are permitted by law, legislative action, or presidential authorization, the DoD's policy is to record advances or prepayments in accordance with GAAP. 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 DLA has implemented this policy.

Q. Leases

Not Applicable to DLA GF.

R. Other Assets

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

The DLA 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, DLA may provide financing payments. Contract financing payments are defined in the Federal Acquisition Regulations, Part 32, as authorized disbursements of monies to a contractor prior to acceptance of supplies or services by the Government. Contract financing payments clauses are incorporated in the contract terms and conditions and may include advance payments, performance-based payments, commercial advance and interim payments, progress payments based on cost, and interim payments under certain cost-reimbursement contracts.

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

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 DLA recognizes contingent liabilities when past events or exchange transactions occur, a future loss is probable, and the loss amount can be reasonably estimated.

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

Other liabilities arise as a result of anticipated disposal costs for DLA's assets. This type of liability has two components: nonenvironmental and environmental. Consistent with SFFAS No. 6, "Accounting for Property, Plant and Equipment," recognition of an anticipated environmental disposal liability begins when the asset is placed into service. Nonenvironmental disposal liabilities are recognized for assets when management decides to dispose of an asset based upon DoD's policy, which is consistent with SFFAS No. 5, "Accounting for Liabilities of Federal Government." The DLA has not fully implemented these policies due to system and process limitations.

T. Accrued Leave

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

U. Net Position

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

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

Cumulative Results of Operations represent the net difference, since inception of an activity, between expenses and losses and financing sources (including appropriations, revenue, and gains). Beginning with FY 1998, the cumulative results also include donations and transfers in and out of assets that were not reimbursed.

V. Treaties for Use of Foreign Bases

Not Applicable to DLA GF.

W. Comparative Data

The DLA's financial statements and notes are presented on a comparative basis.

X. Unexpended Obligations

The DLA obligates funds to provide goods and services for outstanding orders not yet delivered. Unless the title has passed, the financial statements do not reflect a liability for payment for goods and services not yet delivered. Unexpended obligations include both obligations for which goods and services have been delivered (title passed) and a liability recognized. The balance of unexpended obligations appears immediately before net outlays in the Statement of Budgetary Resources, and is referred to as "Total, unpaid obligated balances, net of period."

Y. Undistributed Disbursements and Collections

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

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

Z. Significant Events

Not Applicable to DLA GF.

Note 2. Nonentity Assets

As of September 30	2008		2007	
(Amounts in thousands)				
Total Entity Assets	$	1,047,532	$	1,138,620
Total Assets	$	1,047,532	$	1,138,620

Nonentity Assets are assets for which DLA maintains stewardship accountability and responsibility to report, but are not available for DLA's operations.

Note 3. Fund Balance with Treasury

As of September 30	2008		2007	
(Amounts in thousands)				
Fund Balances				
Appropriated Funds	$	757,876	$	725,689
Total Fund Balances	$	757,876	$	725,689
Fund Balances Per Treasury Versus Agency				
Fund Balance per DLA		757,876		725,689
Reconciling Amount	$	(757,876)	$	(725,689)

The DLA shows a $757.9 million reconciling net difference with U.S. Treasury. The U.S. Treasury maintains and reports fund balances at the Treasury Index appropriation level. Defense Agencies, to include DLA, are included at the Treasury Index 97 appropriation level, an aggregate level that does not provide identification of the separate Defense Agencies. As a result, the U.S. Treasury does not separately report an amount for DLA and, therefore, the entire DLA Fund Balance with Treasury (FBWT) amount is reflected as a reconciling amount.

Status of Fund Balance with Treasury

As of September 30	2008		2007	
(Amounts in thousands)				
Unobligated Balance				
Available	$	123,540	$	185,686
Unavailable		34,921		34,300
Obligated Balance not yet Disbursed		616,086		527,619
NonFBWT Budgetary Accounts		(16,671)		(21,916)
Total	$	757,876	$	725,689

The Status of Fund Balance with Treasury reflects the budgetary resources to support the FBWT.

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

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

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

NonFBWT Budgetary Accounts represents adjustments to budgetary accounts that do not affect FBWT. DLA's NonFBWT Budgetary Accounts consists of unfilled customer orders without advance and accounts receivable. This category reduces the Status of FBWT.

Unobligated balances are segregated to show available and unavailable amounts in the note schedule. There are no restrictions on DLA's unobligated balances.

Note 4. Investments and Related Interest

Not Applicable to DLA General Fund.

Note 5. Accounts Receivable

As of September 30	2008			2007
	Gross Amount Due	Allowance For Estimated Uncollectibles	Accounts Receivable, Net	Accounts Receivable, Net
(Amounts in thousands)				
Intragovernmental Receivables	$ 11,990	N/A	$ 11,990	$ 17,933
Nonfederal Receivables (From the Public)	$ 120	$ 0	$ 120	$ 268
Total Accounts Receivable	$ 12,110	$ 0	$ 12,110	$ 18,201

Note 6. Other Assets

Not Applicable to DLA General Fund.

Note 7. Cash and Other Monetary Assets

Not Applicable to DLA General Fund.

Note 8. Direct Loan and Loan Guarantees

Not Applicable to DLA General Fund.

Note 9. Inventory and Related Property

Not Applicable to DLA General Fund.

Note 10. General PP&E, Net

As of September 30	2008					2007
	Depreciation / Amortization Method	Service Life	Acquisition Value	(Accumulated Depreciation / Amortization)	Net Book Value	Prior FY Net Book Value
(Amounts in thousands)						
Major Asset Classes						
Construction-in-Progress	N/A	N/A	$ 277,546	$ N/A	$ 277,546	$ 394,730
Total General PP&E			$ 277,546	$ 0	$ 277,546	$ 394,730

Legend for Valuation Methods:
N/A = Not Applicable

The DLA General Fund (GF) General Property, Plant and Equipment (General PP&E) consists of only construction in progress (CIP). The CIP is funded by the Military Construction (MILCON) and Family Housing appropriations. The CIP account is used to accumulate the costs of real property assets under construction until the construction is completed and the assets are available for use. These costs include direct labor, direct material and overhead, as well as engineering and design costs. When construction is completed and the constructed asset is available for use, the asset is transferred from the DLA GF CIP account to the appropriate Service's General PP&E account.

The DLA transfers resources to the U.S. Army Corps of Engineers, Navy Facilities Engineering Command, and the Air Force to manage and execute construction projects. These agencies maintain CIP accounts for each construction project they are managing and are responsible for facilitating the transfer of completed assets to the applicable real property account.

Note 11. Liabilities Not Covered by Budgetary Resources

As of September 30	2008	2007
(Amounts in thousands)		
Intragovernmental Liabilities		
Other	$ 5,095	$ 4,967
Total Intragovernmental Liabilities	$ 5,095	$ 4,967
Nonfederal Liabilities		
Accounts Payable	5,505	2,256
Military Retirement and Other Federal Employment Benefits	6,245	6,223
Environmental Liabilities	221,482	243,664
Other Liabilities	2,582	2,217
Total Nonfederal Liabilities	$ 235,814	$ 254,360
Total Liabilities Not Covered by Budgetary Resources	$ 240,909	$ 259,327
Total Liabilities Covered by Budgetary Resources	$ 66,428	$ 37,094
Total Liabilities	$ 307,337	$ 296,421

Liabilities Not Covered by Budgetary Resources are liabilities for which congressional action is needed before budgetary resources can be provided. The DLA General Fund current year liabilities not covered by budgetary resources are primarily comprised of environmental liabilities. These environmental liabilities are estimates related to future events and therefore are unfunded.

Accounts Payable consists of undelivered orders for open contracts citing cancelled appropriations which remain unfulfilled or unreconciled and for which DLA may incur a contractual commitment for payment.

Composition of Other Lines

Intragovernmental Liabilities Other primarily consists of estimated unemployment compensation.

Nonfederal Liabilities Other consists of accruals recorded for unfunded leave owed to civilian employees. It also includes the unpaid portion of compensatory time and credit hours not taken but earned by employees who are entitled to compensation.

Military Retirement and Other Federal Employment Benefits

Military Retirement and Other Federal Employment Benefits not covered by budgetary resources are comprised of various employee actuarial liabilities not due and payable during the current fiscal year. These liabilities are comprised of Federal Employees Compensation Act benefits for $6.2 million. Refer to Note 17, Military Retirement and Other Federal Employment Benefits, for additional details and disclosures.

Note 12. Accounts Payable

As of September 30	2008			2007
	Accounts Payable	Interest, Penalties, and Administrative Fees	Total	Total
(Amounts in thousands)				
Intragovernmental Payables	$ 11,131	$ N/A	$ 11,131	$ 9,173
Nonfederal Payables (to the Public)	23,448	0	23,448	8,024
Total	$ 34,579	$ 0	$ 34,579	$ 17,197

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

In FY 2007, the Department recognized accounts payable balances of the Mechanization of Contract Administration Services (MOCAS) system at gross value without reductions for partial, progress payments, and non-accounts payable records overstating accounts payable and expenses. The overstated balances for FY 2007 were undeterminable due to system limitations: therefore no corrections have been made. Balances at FY 2008 are properly reported net of non-accounts payable records, partial and progress payments of $5.1 million.

Note 13. Debt

Not Applicable to DLA General Fund.

Note 14. Environmental Liabilities and Disposal Liabilities

As of September 30	2008			2007
	Current Liability	Noncurrent Liability	Total	Total
(Amounts in thousands)				
Environmental Liabilities-- Nonfederal				
Active Installations— Installation Restoration Program (IRP) and Building Demolition and Debris Removal (BD/DR)	$ 28,161	$ 178,958	$ 207,119	$ 216,446
Environmental Corrective Action	105	9,807	9,912	11,534
Environmental Closure Requirements	0	2,613	2,613	0
Installation Restoration Program	17,134	20,637	37,771	35,645
Total Environmental Liabilities	$ 45,400	$ 212,015	$ 257,415	$ 263,625

The DLA environmental liabilities (EL) are from current and out-year Remedial Action Cost Engineering & Requirements (RACER) estimates generated for 39 Defense Environmental Restoration Program (DERP), 175 Non Defense Environmental Restoration Program (NonDERP) sites, and 28 Base Realignment and Closure (BRAC) sites. In August 2007, DLA executed the RACER model and it generated the FY 2008 Cost to Complete (CTC) estimates which are an estimation of anticipated costs necessary to complete environmental restoration requirements. The CTC estimates for the first year plus the unliquidated obligations as of year end equal the current liability. All remaining CTC estimates are categorized as noncurrent liabilities.

The DLA has developed a plan for collecting and reporting EL for NonDERP contamination at DLA managed installations including government-owned contractor-operated (GOCO) fuel points and for Service-owned and operated fuel terminals where DLA stores fuel. To obtain the Service-owned fuel terminals data, DLA developed an environmental template that will be provided to the Military Services after the Office of the Under Secretary of Defense (Comptroller) resolves real property record inconsistencies between the Military Services and DLA. This template will be used to populate the Environmental Disclosures table and for the reporting of overseas base EL in the 1st Quarter, FY 2010 financial statement.

Applicable Laws and Regulations for Cleanup Requirements

The DLA is required to clean up contamination resulting from past waste disposal practices, leaks, spills and other prior activities, which may have created a public health or environmental risk. The DLA is required to follow the Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA); Resource Conservation and Recovery Act (RCRA); and the Superfund Amendments and Reauthorization Act to clean up contamination on installations managed by DLA in coordination with regulatory agencies. This cleanup may at times extend beyond installation boundaries onto privately owned property and to sites where DLA is named as a potentially responsible party by a regulatory agency.

Types of Environmental Liabilities and Disposal Liabilities

The DLA has cleanup requirements for DERP sites at active installations, BRAC installations, and sites at active installations that are not covered by DERP. All cleanup is done in coordination with regulatory agencies, other responsible parties, and current property owners.

Methods for Assigning Estimated Total Cleanup Costs to Current Operating Periods

The DLA uses the RACER model, an independently validated model, to estimate environmental costs. The DLA validates the model in accordance with Department of Defense (DoD) Instruction 5000.61 and primarily uses the model to estimate the liabilities based on data received during a preliminary assessment and initial site investigation.

The DLA provides RACER estimated NonDERP costs associated with General Property, Plant, and Equipment (General PP&E). Initial Data on the environmental cost linked to General PP&E was gathered during FY 2006 and is the basis for the development, implementation, and reporting.

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

The DLA had changes in estimates for FY 2008 resulting from changes in site conditions, recent groundwater modeling data, better site characterization, and improved analysis by program managers. The DLA's EL are expected to fluctuate due to changes in agreements with regulatory agencies, deflation, inflation, and technology. The FY 2008 CTC has incorporated the DoD inflation factors into the NonDERP closure estimates. The latest version of RACER (2008 version 10.0.2) was used to rebaseline estimates.

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

The EL for DLA are based on accounting estimates and assumptions that are believed to be reasonable based upon information available at the time of the RACER calculation. The actual results may materially vary from the accounting estimates if agreements with the regulatory agencies require different remediation than anticipated at the time of the calculation. The liabilities can be further impacted if further investigation of the environmental sites discloses contamination different than known at the time of the estimate.

Although DLA has instituted extensive controls to ensure that these estimates are accurate and reproducible, they are generally considered accurate at +/- 20%. This percentage is supported by a 2004 RACER validation. RACER is currently undergoing another validation that will provide updated supporting statistical analysis. The stated noncurrent liability is an estimate of future liabilities, as the majority of DLA sites will require cleanup for up to 30 years. Estimates for work that are more than 1 to 2 years in the future may be subject to significant change.

Liability for Overseas Bases

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

Note 15. Other Liabilities

As of September 30	2008			2007
	Current Liability	Noncurrent Liability	Total	Total
(Amounts in thousands)				
Intragovernmental				
FECA Reimbursement to the Department of Labor	$ 719	$ 0	$ 719	$ 753
Employer Contribution and Payroll Taxes Payable	189	0	189	146
Other Liabilities	5,096	0	5,096	4,795
Total Intragovernmental Other Liabilities	$ 6,004	$ 0	$ 6,004	$ 5,694
Nonfederal				
Accrued Funded Payroll and Benefits	$ 0	$ 0	$ 0	$ 390
Accrued Unfunded Annual Leave	2,582	0	2,582	2,218
Contract Holdbacks	512	0	512	1,074
Total Nonfederal Other Liabilities	$ 3,094	$ 0	$ 3,094	$ 3,682
Total Other Liabilities	$ 9,098	$ 0	$ 9,098	$ 9,376

Composition of Other Lines

Intragovernmental Other Liabilities consists primarily of amounts for unfunded unemployment compensation not covered by the current year's budget authority.

Note 16. Commitments and Contingencies

The DLA is not aware of any contingent liabilities for legal actions for General Fund.

The DLA has an estimated $5.5 million of undelivered orders for open contracts citing cancelled appropriations which remain unfulfilled or unreconciled and for which DLA may incur a contractual commitment for payment.

Note 17. Military Retirement and Other Federal Employment Benefits

As of September 30	2008				2007
	Liabilities	Assumed Interest Rate (%)	(Less: Assets Available to Pay Benefits)	Unfunded Liabilities	Liabilities
(Amounts in thousands)					
FECA	$ 6,245		$ 0	$ 6,245	$ 6,223
Total Other Actuarial Benefits	$ 6,245		$ 0	$ 6,245	$ 6,223
Total Military Retirement and Other Federal Employment Benefits:	$ 6,245		$ 0	$ 6,245	$ 6,223

Actuarial Calculations

The DLA actuarial liability for workers' compensation benefits is developed by the Department of Labor's (DOL) Employment Standards Administration and provided to DLA at the end of each fiscal year. The liability includes the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases. The liability is determined using a method that utilizes historical benefit payment patterns to predict the ultimate payments. The projected annual benefit payments are then discounted to the present value using the Office of Management and Budget's (OMB) economic assumptions for 10-year U.S. Treasury notes and bonds. Cost of living adjustments (COLAs) and medical inflation factors are also applied to the calculation of projected future benefits.

Actuarial Cost Method and Assumptions

The liability for future workers' compensation benefits includes the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases, plus a component for incurred but not reported claims. The liability is determined using a method that utilizes historical benefit payment patterns related to a specific incurred period to predict the ultimate payments related to that period. Consistent with past practice, these projected annual benefit payments have been discounted to present value using OMB's economic assumptions for 10-year U.S. Treasury notes and bonds. Interest rate assumptions utilized for discounting are as follows:

4.368% in Year 1
4.770% 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 (COLAs) and medical inflation factors (Consumer Price Index Medical (CPIMs)) were applied to the calculation of projected future benefits. These factors were also used to adjust the methodology's historical payments to current year constant dollars. The compensation COLAs and CPIMs used in the projections for various charge back years (CBY) were as follows:

CBY	COLA	CPIM
2008	3.03%	4.71%
2009	3.87%	4.01%
2010	2.73%	3.86%
2011	2.20%	3.87%
2012	2.23%	3.93%
2013+	2.30%	3.93% 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 loses per case (a measure of case-severity) in CBY 2008 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 2008 projection to the average pattern for the projections for the most recent three years.

Programs Upon Which Actuarial Calculation are Based (Retirement Systems)

The DLA interacts with, and is dependent upon the financial activities of the Federal Government as a whole. The DLA's civilian employees participate in the Civil Service Retirement System (CSRS) and the Federal Employees Retirement System (FERS) while the Military Retirement System (MRS) covers military personnel. Additionally, personnel covered by FERS and MRS also have varying coverage under Social Security. The DLA finances only a portion of the civilian pensions. While reporting and funding civilian pensions under CSRS and FERS is the responsibility of Office of Personnel Management, DLA recognizes an imputed expense for the portion of civilian employee pension's benefit on the Statement of Net Cost. The DLA also recognizes corresponding imputed revenue from the civilian employee pension's benefit on the Statement of Changes in Net Position.

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

Intragovernmental Costs and Exchange Revenue

As of September 30	2008	2007
(Amounts in thousands)		
Intragovernmental Costs	$ 107,564	$ 130,994
Public Costs	605,940	573,116
Total Costs	$ 713,504	$ 704,110
Intragovernmental Earned Revenue	$ (36,831)	$ (22,323)
Public Earned Revenue	(3,251)	(31,809)
Total Earned Revenue	$ (40,082)	$ (54,132)
Net Cost of Operations	$ 673,422	$ 649,978

Intragovernmental costs and revenue are related to transactions made between two reporting entities within the Federal Government. Public costs and revenues are exchange transactions made between the reporting entity and a nonfederal entity.

The DLA's systems do not track all intragovernmental transactions by customer at the transaction level. Therefore, internal Department of Defense buyer-side balances are adjusted to agree with internal seller-side balances for revenue. Expenses were adjusted by reclassifying amounts between federal and nonfederal expenses.

The Statement of Net Cost (SNC) represents the net cost of programs and organizations of the Federal Government 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 Department'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 Department 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".

The amounts presented in this statement do not meet accounting standards and are based on budgetary obligations, disbursement 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.

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

Composition of Other Lines

Other Financing Sources: Other (+/-) consists of transaction correcting funds transfer.

Unexpended Appropriations: Other Adjustments (Rescissions, etc) consists of a permanent reduction to unexpended appropriations.

Note 20. Disclosures Related to the Statement of Budgetary Resources

As of September 30	2008	2007
(Amounts in thousands)		
Net Amount of Budgetary Resources Obligated for Undelivered Orders at the End of the Period	$ 585,592	$ 510,628
Total	$ 585,592	$ 510,628

The DLA apportionment categories for obligations incurred are Category A direct and reimbursable obligations and Category B direct obligations. The table below summarizes the apportionment categories.

($ millions)	Category A	Category B	Totals
Direct Obligations Incurred	406.2	395.5	801.7
Reimbursable Obligations Incurred	41.4	0.0	41.4
Total	447.6	395.5	843.1

Other Disclosures

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

Note 21. Reconciliation of Net Cost of Operations to Budget

As of September 30		2008		2007
(Amounts in thousands)				
Resources Used to Finance Activities:				
Budgetary Resources Obligated:				
Obligations incurred	$	843,144	$	661,382
Less: Spending authority from offsetting collections and recoveries (-)		(75,759)		(42,126)
Obligations net of offsetting collections and recoveries		767,385		619,256
Net Obligations	$	767,385	$	619,256
Other Resources:				
Transfers in/out without reimbursement (+/-)		(136,544)		(98,526)
Imputed financing from costs absorbed by others		1,906		2,078
Other (+/-)		196		0
Net Other Resources Used to Finance Activities	$	(134,442)	$	(96,448)
Total Resources Used to Finance Activities	$	632,943	$	522,808
Resources Used to Finance Items not Part of the Net Cost of Operations:				
Undelivered Orders (-)		(74,964)		74,642
Unfilled Customer Orders		830		3,815
Resources that fund expenses recognized in prior Periods (-)		(6,209)		(924)
Resources that finance the acquisition of assets (-)		0		(158)
Other (+/-)		136,349		98,526
Total Resources Used to Finance Items not Part of the Net Cost of Operations	$	56,006	$	175,901
Total Resources used to Finance the Net Cost of Operations	$	688,949	$	698,709

Reconciliation of Net Cost of Operations to Budget (Continued):

As of September 30	2008	2007
(Amounts in thousands)		
Components of Net Cost of Operations that will not Require or Generate Resources in the Current Period:		
Components Requiring or Generating Resources in Future Periods:		
Increase in annual leave liability	$ 364	$ 0
Increase in environmental and disposal Liability	0	17,537
Other (+/-)	3,400	166
Total Components of Net Cost of Operations that will Require or Generate Resources in future periods	$ 3,764	$ 17,703
Components not Requiring or Generating Resources:		
Revaluation of assets or liabilities (+/-)	20,477	7,492
Other	(39,768)	(73,926)
Total Components of Net Cost of Operations that will not Require or Generate Resources	$ (19,291)	$ (66,434)
Total components of Net Cost of Operations that will not Require or Generate Resources in the current period	$ (15,527)	$ (48,731)
Net Cost of Operations	$ 673,422	$ 649,978

The Reconciliation of Net Cost of Operations to Budget provides information on the total resources used by DLA - both those received through the budget and those received by other means. It reconciles the budgetary obligations incurred to the net cost of operation for a given reporting period. It articulates and details the relationship between net obligations from budgetary accounting and net cost of operations from proprietary accounting.

Due to DLA's financial system limitations, budgetary data is not in agreement with proprietary expenses and assets capitalized. The difference between budgetary and proprietary data is a previously identified deficiency.

The following note schedule 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

Composition of Other Lines

Resources Used to Finance Activities: Other consists of a gain from various transactions which have no budgetary impact.

Resources Used to Finance Items Not Part of Net Cost of Operations: Other consists of transfers out of Construction in Progress (CIP) to the appropriate Services upon completion.

Components Requiring or Generating Resources in Future Period: Other consists primarily future funded expense for reestablished accounts payable for a cancelled appropriation.

Components Not Requiring or Generating Resources: Other consists primarily of operating expenses that were reclassified as CIP.

Note 22. Disclosures Related to Incidental Custodial Collections

Not Applicable to DLA General Fund.

Note 23. Earmarked Funds

Not Applicable to DLA General Fund.

Note 24. Other Disclosures

Not Applicable to DLA General Fund.

Note 25. Restatements

Not Applicable to DLA General Fund.

THE WARFIGHTER'S LOGISTICS COMBAT SUPPORT AGENCY